HOUSE OF LORDS

SELECT COMMITTEE ON THE EUROPEAN UNION

The Multiannual Financial Framework 2014-2020

Oral evidence with associated written evidence

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Professor Robert Ackrill, Professor of European Economics and Policy, and Jean Monnet, Chair in European Economic Studies Division of Economics, Nottingham Trent University – Written Evidence

Introduction
1. This evidence is submitted in addition to my previous evidence of January 2011. In so doing, I am affirming the evidence submitted at that time.

Expenditures
2. National governments are having to pursue fiscal consolidation because of domestic fiscal imbalances. In some cases these have existed for several years, whilst the global economic crisis has impacted on all countries. This issue does not affect the EU Budget insofar as it is subject to an annual balanced budget rule. Nor has the EU Budget been a factor in the development of those imbalances at national level. As I made clear in January, I believe the strict enforcement of the balanced budget rule has been of vital importance to the EU Budget. It must therefore be retained, with no other budget decisions undermining it.

3. The key questions, therefore, concern the overall size of the budget, the items of expenditure and sources of revenue. In the absence of a systematic economic analysis of the appropriate size of the EU Budget the current MFF proposal, which sees annual fluctuations, but little change overall, in real-terms payment appropriations, seems a reasonable political compromise.

4. Within that, whether seen in terms of recovery from recession or more broadly as a necessary policy response to an increasingly competitive multi-polar world economy, the rise in spending on 'smart and inclusive growth' is not just appropriate, but necessary. Under that spending heading, the rising share of money targeted on policies other than cohesion is also, I believe, appropriate. This, it should be remembered, is rising spending in the context of a budget that is small in size compared to national government budgets; and which is subject to a balanced budget rule. Thus such a rise in spending does not represent fiscal profligacy.

5. I believe establishing some expenditure elements outside of the MFF framework is appropriate, insofar as they represent 'known unknowns' regarding possible future EU expenditure; they are agreed in advance within defined parameters; and insofar as the terms and conditions of activation and scale are very carefully laid out. Their presence in the MFF could compromise the robustness of the balanced budget rule, but they must be subject to equally robust constraints, albeit different in design.

The EU Budget, Expenditures, and the CAP Reform Proposals
6. Whilst not strictly part of the MFF proposal, the CAP reform proposals have profound implications for the MFF, given the scale of CAP spending. For the MFF to deliver on the goals desired of it, all spending elements, including the CAP, must be designed in a consistent and mutually-reinforcing manner.

7. There is a concern over spending on the CAP: in the context of EU spending promoting the Europe 2020 targets, this would be better done via Pillar II instruments. Most CAP spending, however, will continue to be channelled through Pillar I. As a result, the greater financial resources (from this part of the EU Budget) for Europe 2020 are being channelled through the less suitable policy instruments. To that extent, this element of the MFF can, at best, also make only a truncated contribution to the aims of the "Budget for Europe 2020" document.

8. In addition to this internal contradiction, other problems arise in relation to the hugely important part of the EU Budget. Reverse modulation, the movement of some money from Pillar II budgets into Pillar I direct payments, was allowed in the new member states as a temporary measure, to mitigate the effects of phasing-in of Pillar I payments over 10 years. The CAP reform proposals, rather than ending reverse modulation, are looking to give all countries this policy option. In the context of a MFF which is seeking to promote a wider range of objectives under Europe 2020 – and given the point in the preceding paragraph – this element works against the broad policy thrust sought for the new MFF.

9. Another element of the CAP reform proposals which also runs counter to the broad (and positive) goals for the MFF – again in the context of the point made in paragraph 7 – is the attempt to address wider policy concerns by building-in environmental and other dimensions to the Pillar I payments. As such, rather than contributing to the simplification of EU spending, this is likely to increase complexity – significantly.

Revenues
10. I remain unconvinced by arguments about the benefits of new revenues, as expanded upon in detail in previous submissions to the Committee (HL 125, 2010-11; HL 64, 1006-07). Piggybacking an EU VAT element on top of national VAT is, I think, inappropriate economically and dangerous politically. Economic concerns over the regressive nature of VAT have long resulted in constraints and adjustments being imposed on that own-resource and are, I am sure, one reason for the steady reduction in the percentage of the VAT base drawn upon in determining a country's VAT-based own-resources contribution. By the same token, this has been replaced by the 'fourth resource', based on GNP, then GNI; a better representation of ability to pay. Expanding the VAT-based contribution as a 'true' own-resource, presumably at the expense of the GNI-based contribution, would be a backwards step in terms of contributions being based on ability to pay. Furthermore, rightly or wrongly, for the new VAT contribution to make a significant contribution to EU budget revenues, the amount piggy-backed would have to be significant. This would run the very real risk of increasing citizens' negative feelings towards the EU, rather than the desired goal of reducing them by bringing the EU and it citizens closer together.

11. I also think a Financial Transactions Tax (FTT) is inappropriate as an EU own-resource, for two reasons. First, with financial assets mobile globally, the use of an FTT regionally could potentially have a very distorting effect and damaging impact on the EU financial services industry, within the EU and globally. Second, I think an EU revenue based on a single sector is, of itself, inappropriate. VAT and GNI are economy-wide. Even a carbon tax, another possible revenue source discussed from time to time, would be horizontal in nature. The FTT, however, is sector specific and, thus, would represent a reversal of the trend towards horizontal measures seen in other policy areas. An FTT discussed in the context of

a global response to the Global Economic Crisis is one thing – but as a regional source of revenue-raising I think it is inappropriate and potentially very damaging to the EU economy.

12. I believe the arguments in paragraph 11 are a sufficient counter to an FTT of themselves, without having to play the 'City of London' card, which has its own dangers in the politics of the EU.

13. I do not believe the introduction of any new 'true' own-resource would have any impact on member states and their focus on net national budget transfers.

Other Observations
14. In my submission of January 2011, I argued against aligning the MFF cycle with that of the Commission and/or European Parliament. I wish to add one further point here. It takes time for a new Commission to bed-in and establish its own policy agenda. With the European Parliament this applies *a fortiori*, given the time needed first to establish the membership of Committees, before they can begin work. I therefore see no practical, simple, way of bringing something as substantial and as demanding to agree as the MFF within such a cycle.

15. I believe the eurozone crisis – and the range of possible fiscal responses – should have no fundamental impact on the EU budget at all. Referring to the fiscal functions of allocation, distribution and stabilisation, from the literature on fiscal federalism, for reasons I have explained in previous submissions there is a fundamental difference between stabilisation and the others. I therefore believe that whatever fiscal response to the crisis is eventually agreed upon, it must operate totally separately from the EU Budget as we understand it. This should apply even if, in the distant future, every EU country adopted the euro. This is because of the nature of the fiscal transactions that the stabilisation function represents, and their incompatibility with the core functions and values of the EU Budget.

15 December 2011

Mrs Marta Andreasen MEP – Written Evidence

In replying to the questions below, I would also refer the Noble Lords to my earlier written submission to the meeting of 10th November, which I was sadly unable to attend.

1. Are the Commission's proposed expenditure ceilings appropriate, taking into account the pressures on so many Member States to pursue fiscal consolidation?

By looking for 972 billion euros in payments, an increase over the 2007 to 2013 MFF of a nominal 5% in the face of uncertain growth and shrinking public budgets for years to come the Commission is demonstrating that it thinks it is business as usual. The nations of Europe are unable to support such demands. The MFF should at the very most be held to a zero percent increase but a 10% reduction would be a more realistic position to take.

6. What is your assessment of the Commission's proposals for expenditure outside the MFF framework?

I am not sure whether the question is meant to refer to the effectiveness of those items outside the MFF, or to the principle of moving some items outside the MFF, or both.

The principle of moving items which were previously within the MFF to outside it minimises any apparent increase in the MFF. It also removes comparability between programmes, and transparency.

I attach some work which I have done, which attempts to compare the proposed 2013-20 MFF with the previous one on like-for-like terms. I have not offered this up to the Commission, and must stress that it is fairly rough and ready, but it does seem to indicate that the headline increase in the MFF understates the reality.

Regarding the overall effectiveness of measures taken by the EU, both within and outside the MFF, my views are well-known - that it is generally less effective than measures taken by member states.

7. What is your assessment of the Commission's proposals to grant the EU more 'own resources' and of the choices advocated (a new VAT resource and/or a financial transactions tax)?

The Commission, under pressure from the European Parliament wants to avoid budget negotiations such as those that have taken place in the last two years. In these negotiations the Council held firm to the funding it was offering the EU in the face of much larger demands from the European Parliament.

In the 2011 negotiation this resulted in brinksmanship where the European Parliament rejected the Council's position out of hand only to receive no counter offer. Parliament had to then accept the increase on offer from the Council or go back to one twelfth of the previous year's budget per month.

In the 2012 negotiation the Parliament on its guard from the previous year attempted to negotiate an increase beyond that proposed by Council and bargained as hard as it could in the details while accepting Council's payment increase.

As a result of these negotiations the Commission under Parliament's influence is proposing new own resources to bypass the annual budget negotiation.

The Commission has made several suggestions including EU-wide VAT, carbon tax, a financial activity tax and a financial transaction tax. All have met significant opposition from the Member States. However, the financial transaction tax (FTT), the last suggestion has the support of the large continental nations.

A recent report by PriceWaterhouseCoopers showed that the financial services industry provides tax revenue of £56 billion to Her Majesty's Government. The opinion of the financial services industry is that the FTT will decimate the City of London. If applied unilaterally by the EU it will cause wholesale flight of financial services from the EU to other parts of the world.

The new VAT resource proposed by the Commission is for a 1% to 2% own resource rate of VAT to be applied across the EU. In other words the Commission wants the EU to take 1% to 2% out of VAT before the national government gets its share. At present the EU contribution is based on 0.3% of the VAT tax base and yields about 14 billion euros a year. The new VAT would yield about 37 billion.

Theoretically these taxes could add up to 80 billion Euros leaving the EU to negotiate 45 billion Euros from the Member States annually, a much smaller negotiation than at present.

In conclusion, we are opposed to these new resources as they will give the Commission the power to operate independently of the Member States. Additionally, regardless of what any protocol says, the costs will be passed on to end users, not only of financial services but also in the energy and other sectors.

9. What is your assessment of the innovative financing instruments proposed by the Commission?

From a budget perspective leveraging grants with innovative financial instruments may seem a way to get a "bigger bang for the buck" by involving private financing in European projects.

In fact in my opinion it will suffer from the same disadvantage that all private public partnerships suffer from, the uneven distribution of risk and reward to the benefit of the private party. In other words the private partners will ensure that they benefit from distributing the risk disproportionately to the public partner while at the same time maximising the reward for themselves.

A second disadvantage that I see is the reduction in transparency that ensues from such co-operations. Inherently greater accounting control will have to be written into the system to provide the same accounting assurances that exist in a public project.

Comparison of 2007 – 13 and 2014 – 20 Multiannual Financial Frameworks

€ million at 2011 prices

MFF 2007 - 2013		MFF 2014 - 2020				COMPARISON	
COMMITMENT APPROPRIATIONS		**COMMITMENT APPROPRIATIONS**	**2014-2020**	**Adjustments**	**Adjusted**	**Incr./(Decr.)**	**% Incr./(Decr.)**
1) Sustainable Growth	**438,618**	1) Smart & Inclusive Growth	**490,908**	13,214	**504,122**	**65,504**	14.93%
1a Competitiveness for Growth & Employment	90,203	Of which Economic, social & territorial cohesion	376,020				
1b Cohesion for Growth & Employment	348,415						
2) Preservation & Management of Natural Resourc	**412,411**	2) Sustainable Growth: Natural Resources	**382,926**	4,808	**387,734**	**(24,677)**	-5.98%
Of which: market related expenditure & direct payment	330,085	Of which: market related expenditure & direct payment	281,825				
3) Citizenship, freedom, security & justice	**12,216**	3) Security & Citizenship	**18,536**	6,890	**25,426**	**13,210**	108.14%
3a Freedom, Security & Justice	7,549						
3b Citizenship	4,667						
4) Europe as a global player	**55,935**	4) Global Europe	**70,000**	2,862	**72,862**	**16,927**	30.26%
5) Administration	**55,735**	5) Administration	**62,629**	214	**62,843**	**7,108**	12.75%
6) Compensations	**862**					**(862)**	-100.00%
TOTAL COMMITMENT APPROPRIATIO	**975,777**	**TOTAL COMMITMENT APPROPRIATIO**	**1,024,999**	**27,988**	**1,052,987**	**77,210**	**7.91%**
As percentage of GNI	1.12%	As percentage of GNI	1.05%		1.08%		
TOTAL PAYMENT APPROPRIATIONS	**925,576**	**TOTAL PAYMENT APPROPRIATIONS**	**972,198**	**27,988**	**1,000,186**	**74,610**	**8.06%**
As percentage of GNI	1.06%	As percentage of GNI	1.00%		1.03%		
		OUTSIDE THE MFF					
		Emergency aid reserve	2,450	(2,450)	0		
		European globalisation fund	3,000	(3,000)	0		
		Solidarity fund	7,000	(7,000)	0		
		Flexibility instrument	3,500	(3,500)	0		
		Reserve for crises in the agricultural sector	3,500	(3,500)	0		
		ITER	2,700	(2,700)	0		
		GMES	5,838	(5,838)	0		
		EDF ACP	29,999		29,999		
		EDF OCT	322		322		
		Global Climate and Biodiversity Fund	0		0		
		TOTAL OUTSIDE THE MFF	**58,309**	**(27,988)**	**30,321**		
		TOTAL MFF & OUTSIDE THE MFF	**1,083,308**	**0**	**1,083,308**		
		As percentage of GNI	1.11%		1.11%		

Professor John Bachtler – Oral evidence (QQ38-49)

COHESION POLICY AFTER 2013

Evidence Session No. 2. *Heard in Public.* *Questions 38 - 49*

COHESION POLICY AFTER 2012

TUESDAY 20 DECEMBER 2011

Members present

Lord Harrison (The Chairman)
Lord Hamilton of Epsom
Lord Haskins
Baroness Hooper
Lord Jordan
Lord Kerr of Kinlochard
Baroness Maddock
Lord Moser
Lord Woolmer of Leeds

Examination of Witness

John Bachtler, Professor of European Policy Studies and Director, European Policies Research Centre, University of Strathclyde.

Q38 The Chairman: Professor Bachtler, welcome to the first witness session of our contribution to the Select Committee's report on the multi-annual financial framework for 2014-20. I remind Members to declare any interests as this is our first session of a fresh investigation. We are extremely grateful to you for coming. I apologise for the delay in beginning but we had a very interesting private session with our BIS colleagues, which has helped us to understand the matter better. However, we are looking to you to improve our knowledge of quite a complicated and changing scene. As you know, we keep a record of House of Lords reports and will send you the transcript. We would be grateful if you could check that to see that it is correct. Indeed, since we will be writing this up for the Select Committee report over the next month or so, we would be very grateful for your post-Christmas thoughts if, suddenly in the middle of your Christmas pudding, you think, "I didn't tell them that". That would be helpful to us.

Thanks very much for coming. Did you want to make an opening statement? My first question is just to try to get a better understanding of the original 2007-13 proposals, which we are coming to the end of, and the new proposals for 2014-20. The Committee would like to understand what the broad outlines and changes are and might be.
Professor Bachtler: Thank you very much for that introduction and the invitation to contribute to the work of the Committee. What is notable about the changes is that, first, the proposals that were put forward for the current period of 2007-13 essentially represented a sort of tactical repositioning of cohesion policy, designed to ensure the continuity of the policy with a substantial amount of funding, whereas the proposals for the next period are more strategic. Clearly, there is a tactical element. The Commission is keen to retain cohesion policy as a well-funded policy area. However, there has been a process of evaluation and assessment of the performance of the policy, which is more extensive than has taken place in the run-up to any reform of the structural funds. Secondly, there has been a process of consultation with member states and other stakeholders, which has been more extensive than for any other reform. Obviously, the backdrop to the proposals has been particularly difficult.

Looking at the proposals from the perspective of a researcher or an academic, one can see that a real effort is being made to address head-on major criticisms that have been made of the policy. Hence, in the draft legislative package, you can see important changes to the process of programming, particularly in the strategic context—the degree to which an integrated approach should be pursued, co-ordination between institutions at the European and national levels, and the emphasis on performance and results. There are also changes to the architecture with the creation of a transition regions category, which one can justify on the grounds of economic development, although there is clearly a strong political aspect to it. I am happy to develop each of those points. What is remarkable about the set of proposals for the next period is that they have been conceived in a more strategic way than has been the case in the past.

Q39 The Chairman: That is very helpful. We will indeed tackle the various matters under their separate headings. Broadly speaking, the Commission has responded to the criticisms of the last septennat. Do you think it is more or less on the right track, or is it pointing in the right direction with some of its solutions being wrong? Could you take a broad-brush approach to that?

Professor Bachtler: There are questions about a number of the proposals, particularly those to do with the architecture of the transition regions. However, if we look at the principle of more concentration, more co-ordination and greater results orientation, they are on the right track. Of course, the devil is in the detail, which is clearly what is exercising a lot of people's minds. However, the principles underlying the approach are on the right track.

Q40 Lord Hamilton of Epsom: Cohesion policy makes up a substantial amount of the EU budget—35.7%, the equivalent of €352 billion in 2011 prices. The 2020 budget proposes to allocate €336 billion to the cohesion policy, which represents a decrease of just under 5%. Bearing in mind the economic problems that the EU is facing, should spending on EU funds be encouraged to help develop economic growth? To what extent have they been an instrument for enhancing reform and increasing growth?

Professor Bachtler: How much is spent is ultimately a political decision. However, my view is that, at a time of economic strain and austerity, we can see across many member states that budgets for economic development are under pressure. During the first years of the financial crisis, and subsequently in reactions to changed economic conditions, we have seen that spending on a variety of economic development priorities has been cut back in many member states. That is perhaps understandable because they are often not particularly visible and are easier to cut back without public reaction. The value of cohesion policies is that they guarantee a certain level of spending on economic development—a certain priority and profile. They provide predictability because funding is allocated for a seven-year period and they guarantee a certain minimum of national co-financing. From that economic development point of view, having a significant budget allocated to cohesion policy is positive.

On the second part of your question, about whether such policies are growth enhancing, I would say two things. First, they have the potential to enhance growth because of the nature of how the policy is managed and delivered. You can tailor spending to places—regions, cities and localities—with a policy mix of investment support, human resources support, infrastructure, innovation and so on, in a way that suits regional and local circumstances. So it has the potential to be growth enhancing. The degree to which it has in fact been growth enhancing is subject to a lot of debate. There has been an enormous amount of research. Essentially, if you were to try to sum up the results of evaluation studies and other research, you could say that the performance has been very variable and there are reasons for that. Effectiveness is dependent, first, on the degree of strategic coherence—the degree to which decisions on the allocation of resources are based on a sound analysis of what the development needs and challenges are—and, secondly, on whether the capacity is in place in the form of administrative institutions, structures, procedures, human resources and so on to be able to select the best projects and ensure that they are implemented in the right way.

Q41 Lord Hamilton of Epsom: Following that, would you identify any difference between the effectiveness of the European Regional Development Fund and that of the European Social Fund and the value that they add?

Professor Bachtler: They are extremely difficult to compare because they have different objectives and are administered in quite different ways in different countries. There are often national ESF programmes, whereas ERDF programmes are regional. The Commission has a logic in its proposals to increase the proportion of ESF spending, by having guaranteed percentages that will be allocated to ESF relative to ERDF. This is justified on the basis that there has been a decline in the proportion of structural funds spent on ESF over the past couple of programme periods. Given that, at European level, the Commission has put a lot of emphasis on what it calls social cohesion, particularly at a time of rising unemployment—especially youth unemployment—it wants predictability in what will be committed to the ESF.

There is also some evidence of a potentially greater longer-term impact from spending more money on ESF—on human resources, employment, training and so on—compared to investing in infrastructure or business support, although the impacts vary depending on whether one is looking at the short or the long term. Therefore, it is very difficult to say that one adds more value than the other. I would say that the territorial dimension of ERDF is a particularly important aspect of its ability to generate added value.

Q42 Lord Moser: I think that you referred in your introductory remarks to the general positioning of cohesion policy. As we understand it, the Commission sees the cohesion policy as being absolutely key in reaching Europe 2020 objectives. One can see the point of that. I gather that discussions between the Commission and individual member states will be the means of working out what individual member states have to do to achieve all that. The counter view to, or possible criticism of, that approach, which we have become conscious of in looking at the budget side of things, is to look at cohesion policy as an overall way of achieving all kinds of unrelated objectives. We should like to hear from you whether that is a sensible criticism or not.

Professor Bachtler: That is a good question. Certainly, one of the difficulties in identifying what cohesion policy has achieved over successive programme periods relates to the fragmentation of support across a range of objectives or priorities. There is a strong case for greater focus. As far as Europe 2020 is concerned, it is undeniable that there is a tension between the Commission's proposals for cohesion policy to be a delivery agent, or arm, of Europe 2020 and the traditional mission of the policy of reducing regional disparities. However, the political context is one where, as a number of Commission officials in DG Regio have said, Europe 2020 is the only game in town as far as the Commission is concerned. Therefore, to guarantee the future of cohesion policy, it needed to be linked very closely to Europe 2020 objectives but, at the same time, to address some of the key criticisms of the policy, which are either that it has not delivered or that the visibility of what it claims to have achieved has been very low.

The current Commissioner for Regional Policy, Johannes Hahn, and the previous one, Danuta Hübner, have played the negotiations within the Commission adeptly to ensure that cohesion policy survives. However, the focus on Europe 2020 could mean that the cohesion policy loses some important characteristics, which, to my mind, have been significant contributors to its performance. In particular, some member states, which are in receipt of significantly less funding, may decide to sectoralise the way that that funding is spent. In other words, increased funding may be allocated to sectoral or thematic programmes that are very good at delivering the Europe 2020 objectives and which can ensure that results are achieved and that they are visible. The problem is that that way of spending the money may not be in the best interests of the broader regional development objectives within a country in terms of development needs and challenges and the disparities between regions. It may also lose an aspect of the territorial approach to implementing the funding.

Q43 Lord Moser: Overall, when you talk about the results, do you mean the differences between regions?

Professor Bachtler: That is one of the key objectives at a European level—to reduce regional disparities as well as those between countries.

Lord Moser: On the whole, has it been a success story?

Professor Bachtler: On the whole, I would say that it has been a success story but there are big differences in effectiveness. In some countries and regions the money has not been effective for some of the reasons that I mentioned earlier.

Lord Moser: I would be interested to know how you now see the basic success or otherwise in reducing disparities between countries and regions, and whether, on the whole, the Commission's plans, which I referred to, look more hopeful from now to 2020 in terms of reducing disparities.

Professor Bachtler: It is important to differentiate between levels when talking about regional disparities. There has been significant success over the past 20 years and, in the case of the new member states, over the past seven years in reducing disparities between the poorer countries and regions and the rest of the EU. There is an argument among economists about the degree to which cohesion policy has contributed to that, but there is significant evidence that EU funding has been an important contributory factor. However, if one looks at disparities within countries, these have been increasing. We see this particularly in the new member states, where there has been a process of what one could call metropolitanisation. The big cities such as Warsaw, Prague, Budapest and so on are motoring ahead but social and economic disparities are widening within those countries. The contribution to reducing regional disparities varies depending on the spatial scale you are dealing with.

Lord Moser: Absolutely. Thank you for that.

Q44 Lord Haskins: You could add that the United Kingdom is another example of a country where disparities have risen. Therefore, the implication would be that there is some flaw. The single market is a much bigger factor than all this in its effect on economies. You could argue that the balance towards urbanisation, whether it is in Warsaw or London, is accelerating, which is almost what the Commission is trying to stop. You could argue that it has totally failed.

Professor Bachtler: The difficulty is that the Commission has, certainly over the past two programme periods, had relatively limited influence on how money is spent within countries. These have been very much member state decisions. One has to look at the differences between countries. In countries such as Sweden, the Netherlands, Finland, the UK and a few others, structural funds represent a very small proportion of economic development spending, let alone as a proportion of economic activity in any country or region. Therefore, if one is trying to do a thorough evaluation, it is inordinately difficult to pick up evidence for what structural funds have contributed to, for example, jobs, GDP or the reduction of disparities between regions. At the micro level, if one is looking at individual projects or, to a certain extent, individual programmes, one can find indicators of successful outcomes or the results of spending, but the broader impacts are very difficult to pick up.
That is easier in the case of countries where structural funds account for 3% or 4% of national GDP and a significant proportion of government investment. Some quite positive evaluation evidence of what structural funds have done is coming through from the countries that joined in 2004. I could talk at length on this because a variety of messages are coming through on the effectiveness of spending. However, the main point is that it is important to differentiate between countries or groups of countries when thinking about effectiveness.

Q45 Lord Jordan: The new package of legislation underpinning the cohesion policy suggests the EU funding a limited number of priorities, calling it a thematic concentration to be defined at EU level and agreed with each member state. Do the Commission's proposals ensure that there is sufficient flexibility or power for regions and local communities to focus on investment in line with their own development needs? Can a top-down approach be reconciled with a bottom-up approach, and could the introduction of this thematic concentration for structural funds become counterproductive?

Professor Bachtler: That is a very interesting question. This is a classic example of where the principle underlying what the Commission wants to do, in this case with respect to thematic concentration, is widely, if not universally, supported. There is general agreement that the EU needs to be more focused in its spending, for the reasons that I have just mentioned, but the question is how. Personally, I have great difficulty with top-down, prescriptive, relatively crude percentages of the kind that are being proposed. The Commission clearly feels that setting these kinds of percentages in the way that has been trialled in the current period sends a powerful signal. Such percentages are easily understood and are relatively straightforward to negotiate with member states. They also represent a message that is easy for the Commission to communicate to wider audiences: "This is what we are doing in the area of renewables, or competitiveness, or innovation, or social funding—we are spending these percentages or amounts of money." The Commission would argue that these percentages apply at the member state level and that the member state can then create programmes with different percentages of funding as long as overall it meets the requirements.

My main objection—and that of others as well—is that, as your question implied, member states differ so much, not just in their development needs and challenges but in what they are already doing in different policy areas. To take just one example, Germany invests massively more than the UK in renewables. Does it make sense to have the same percentage and the same approach for Germany as for the UK in the way that structural funds are spent on renewables? Arguably it would be preferable to take a more sophisticated approach where the Commission negotiates with each member state on what it spends on different target priorities, based on a sound analysis of the problems and development needs, as well as the existing policy response. The problem with that is that it creates all kinds of difficulties for the Commission in negotiating with member states.

This is the kind of approach that was adopted in the 1990s, when the Commission engaged much more with member states on the policy content of its programmes. Member states did not always like that but it required a certain level of capacity and understanding on the part of the Commission to be able to engage with member states. One can understand where the Commission is coming from with its proposals. One way around this, a sort of compromise, might be to provide ranges of the proportions of expenditure that the Commission would like to see allocated to specific investment priorities. That would provide a bit more flexibility and scope for negotiation, but within certain parameters. The Commission would still get a degree of predictability and visibility about how the money is going to be spent. There would be clear progress in thematic concentration but there would be more flexibility to adapt the percentages to the needs of individual member states.

Q46 Lord Kerr of Kinlochard: Professor, perhaps you can help us on the issue of conditionality. First, on the macro, this Committee has argued in the past for a geographical concentration on the poorest regions in particular difficulty at times of national austerity programmes. Am I right in thinking that the Commission is going in exactly the opposite direction? In particular, if a country was under the excessive deficits procedure, the plan would be to reduce the amount of money made available. That presumably does not apply to countries like the UK that are not in the eurozone. What do you think about the economics of this difficulty—that those who are struggling are made to struggle more? What is the balance?

Professor Bachtler: My view is that having macroeconomic conditionality would be counterproductive from an economic development point of view. That is quite clear. Essentially, this is a political stick that, ideally, would never be used but nevertheless it is a stick to incentivise compliance with the economic and fiscal policies of member states. In practice, what would happen is that, as you say, you would be taking money away from countries when they could least afford it. You would also be penalising those involved in economic development for policy conditions which are not under their control and are not their responsibility. That then cascades all the way down to beneficiaries. It also runs counter to what we know about the exercise of conditionalities. There is a lot of experience—not so much in cohesion policy, although we have some conditionalities, such as the decommitment rule—in relation to the World Bank and other international financial institutions that use conditionalities as part of development spending that can give us lessons in terms of the criteria that you should use to implement conditionalities. One of them is ownership; you do not impose conditionalities from the top down. You ensure that they are critical or relevant to the policy to which they are being applied, that they are controllable or under the influence of those responsible for the policy, that they are transparent and that there is predictability on when they might come into play. These kinds of criteria come through from all the studies and experience of using conditionalities. Macroeconomic conditionalities fail a number of those tests. There are other conditionalities that the Commission proposes - ex ante conditionalities - which fit or meet more of those criteria, but not the macroeconomic ones.

Q47 Lord Kerr of Kinlochard: Of course, you could argue that thanks to the cumbrous procedure and the lags in the system, to try to make cyclical use of the cohesion money would be quite difficult—you would tend on the whole to be a little bit behind the game. Is that right?

Professor Bachtler: Yes, that is definitely the case, particularly if one is looking at countries where the allocations of the cohesion policy budget are of sufficient size to make a difference, such as money being spent on major projects, large-scale infrastructure and so on. There is already a lag in the planning time of one or two years. Then you have the expenditure, which again will run over another one or two years. Then you have the effects of that spending on the major projects. There are real problems of lags with such spending. On the other hand, we have seen that cohesion policy has been used very positively in the current crisis because money has been reallocated to—to use Obama's expression—"shovel-ready" projects, such as business support, employment support and so on. Here, the lags are much shorter but there are limits on the amount of spending that you can accommodate within those kinds of spending areas.

Q48 Lord Kerr of Kinlochard: Thank you very much. Can I also ask you about performance-related conditionality and this idea of the reserve—the 5% in the back pocket? What is your feeling about that? The idea is that it could be counterproductive—and I get the impression that Whitehall is not thrilled about the idea—in that it could encourage people to spend fast, and not necessarily to spend best, to make sure that they do not lose the money. Also, programming late in the period, the reserve moneys being held back might not be optional. Are we right about that?

Professor Bachtler: Yes, I think so. There is progress in the sense that rather than having an EU-wide performance reserve it would be implemented at member state level. We have some experience from the 2000-06 period and elsewhere of how these kinds of schemes work. Again, as with the ring-fencing and the allocation to cities and so on, there is a somewhat arbitrary figure or percentage. Nevertheless, this kind of performance scheme potentially has value because it focuses minds on achievements. As you implied in your question, it is important that the expectations, or the milestones against which performance is judged, are appropriate to what the funding is trying to achieve, so that money is not just committed and absorbed but is related to the targets. We have seen with the decommitment rule—the N+2 rule—how you get unexpected behavioural consequences of these kinds of measures.

If we look at lessons from the past, we can see that in the 2000-06 period many countries did everything they could to minimise the impact of a performance reserve scheme that became just another minor administrative hurdle, and there was minimal competition between programmes. But some countries such as Italy and Portugal went a step further. They combined the EU performance reserve with their own national performance reserve, but framed very much as part of a wider drive to increase performance. Therefore, it was not just a single, crude indicator but part of a broader approach of using evaluation evidence and so on to force local, regional and national politicians, as well as those responsible for the implementing of the funds, to pay attention to the way in which they were spending the money, not just the amounts that they were spending. As I said in respect of conditionality, if a performance reserve is imposed from the top down and there is no ownership on the part of those responsible for implementing the funds in the member states or in the regions, it is not going to be effective. If there is some process whereby a scheme is used as part of a broader approach to raise performance, then I think it has merit.

Lord Kerr of Kinlochard: Thank you. That is very helpful.

The Chairman: Colleagues, we are running a bit over time, which is my fault for delaying the start. Perhaps I could ask Lord Haskins and Lady Maddock to table their questions in succession and we will see how we do. If everyone will forgive me, perhaps we will run five minutes over time, if that is okay with you, Professor Bachtler.

Professor Bachtler: Yes, of course.

The Chairman: Thank you very much.

Q49 Lord Haskins: Professor, when looking at these schemes before, it has been said to us that there have been great concerns about the ability of countries to deliver. There are three obstacles: co-financing, where some countries, including this one, have sometimes been reluctant to co-finance and therefore schemes have not developed; project management, where particularly developing countries have not been able to manage the schemes as they have come through, and that has been a real concern; and the leakage, the skulduggery, which there has been no mention of. These are the great classic areas where procurement money gets into the wrong hands. Do these proposals address any of those situations constructively?

Baroness Maddock: I wanted to ask you about innovative financial instruments. New forms of finance for investment have been developed during the current programming period, moving away from grant-based financing towards more innovative ways of combining grants and loans. I wondered what your view was of that. A follow-up question that I would have asked after you had answered that is: do you think that the EU budget should be used more systematically to leverage financing of strategic private sector investments, with support from the European Investment Bank, given the current fiscal constraints?

Professor Bachtler: On the first question from Lord Haskins, there has been a concerted effort to improve institutional administrative capacity. Certainly, the countries that joined the EU in 2004 have made a better fist of spending EU funds than many expected. If one looks at error rates, absorption and other, more qualitative, indicators, their performance in managing the Funds is not out of line—with exceptions— to member states with longer experience. However, the Commission is increasingly aware of capacity issues and is putting more resources into institutional capacity; it is placing more emphasis on this and its ex ante conditionalities are partly designed to ensure that capacity as well as a supportive policy framework is in place.

On co-financing, during the financial and economic crisis the Commission has done its best to take steps to help member states overcome problems with co-financing, particularly the extra 10% that has been made available to a number of member states. In future, co-financing will be a serious problem for the UK, for example, but also for other countries that have major public expenditure constraints. On the other hand, I would be in favour of limiting these very favourable high co-financing rates from the EU side to as short a period as possible, because they create disincentives for optimal decisions on project selection.
In terms of leakage, the error rate for cohesion policy has been a red flag issue for the Commission for many years. However, if one looks behind the figures, a relatively small proportion is related to fraud. A lot of these "irregularities" relate to inadequate procedures for keeping invoices or maintaining a sufficient payment trail, for example. Those are not unimportant issues, but it involves relatively minor mismanagement as opposed to fraudulent expenditure. In a shared management system, which is highly complex, with a hierarchy of organisations involved in spending the money, it is inordinately difficult to take further steps to reduce the error rate—desirable though that would be—without imposing counterproductive administrative obligations on beneficiaries. We are already seeing organisations not bidding for structural funds because of the administrative burden.
On the innovative financial instruments, I think this is a positive direction. We have seen a very significant increase in the use of innovative financial instruments over successive programme periods. They have important advantages: clearly, they fill a funding gap; they lever in private sector resources; they encourage a move away from grants; and they create some recycling. It is interesting that in some countries, such as Germany or Austria, they are still reusing Marshall Plan funding for small loan schemes and so on, because of the recycling of funding. However, we have also learnt, particularly in the current period, that there are some significant administrative problems associated with the use of the funding, in particular because if you are administering these kinds of instruments you have to have detailed knowledge of structural fund regulations, of state aid compliance and investment principles. Partners tend to have expertise in one of those areas rather than all three. There has been a series of problems, particularly associated with state aid. Also, it is not easy trying to pull together public and private partners; in particular, their attitude towards risk or innovative projects may differ quite significantly. While I think it is desirable to use the budget to increase the usage of these kinds of instruments, there are some quite important lessons to be learnt from the current period for the future.

Baroness Maddock: Do you see any indication that that is happening?

Professor Bachtler: Yes, I think that the Commission is very aware of these kinds of experiences, particularly within the Directorate General for Competition as well as the Directorate General for Regional Policy. There is a lot of work going on to create implementation regulations that are more supportive. We will find out in the spring when those regulations come out whether all this work is in fact going to make life easier.

The Chairman: Professor Bachtler, we will conclude there. I thank you for what you have told us today, including reminding us that the Marshall Plan is still in operation. Thank you very much for the questions that you have answered. Two that we were not able to tackle were on the Common Strategic Framework and the ERDF. Perhaps you would be kind enough to write to us as a Committee, and add to that anything that you think you may have wanted to have said to us in the course of the questioning which would be useful for our deliberations in the new year.

This has been webcast, as you know, and we will send a transcript of what has been said today. Perhaps you could look at that and correct it, and add any other additional points that come to your mind over the year's change. In the meantime, I thank you on behalf of the Committee. You have concluded a very useful session for the Committee in thinking about what is a very important area but one that sometimes needs demystifying, if I may say so. You have enormously helped the Committee in that task today. Thank you very much indeed.

Professor Bachtler: Not at all. Thank you very much, and I am happy to provide further information.

Professor John Bachtler – Supplementary written evidence

Common Strategic Framework (CSF)

12. The preparation of the new generation of programmes will be based on a Common Strategic Framework (CSF) at EU level, Partnership Contracts with each Member State and Operational Programmes at the national or regional level. Will the Common Strategic Framework, Partnership Contracts and Operational Programmes be an improvement on the experience of alignment between the Funds during the 2007-2013 period? Is there time to negotiate and prepare all necessary plans including to the operational level by the beginning of the new period?

The proposed system of CSF, Partnership Contracts and OPs has the potential to deliver what the Commission wants, but it depends on a number of factors. First, if the CSF is to provide a strategic framework, it will be necessary for the different Directorates-General to work together in a much more integrated way than before, so that there clearly common objectives and priorities governing each of the policy areas and instruments. Harmonisation of rules wherever possible is welcome/ Second, Member States will need to adopt a more strategic approach at national level – which will not be straightforward in many countries – and accept greater accountability; several Member States have already voiced doubts about the value of the Contract. It is also unclear how much national governments will be required to involve local and regional actors and other stakeholders in drawing up the Contracts.

Regarding the calendar for negotiating and preparing the plans, this will be tight, but I believe that the Commission is expecting the Contacts and OPs to be drawn up and submitted together (rather than sequentially) so that they can be negotiated together. Much depends on the progress made with the negotiations on the regulations, as well as the financial framework, and whether the Danish and Cypriot EU Presidencies can broker agreement on the main Commission proposals in good enough time. At regional and local levels, most programme managers are aware, based on previous experience, that programmes may not be ready to go on 1 January 2014, and special arrangements may need to be made (at EU or national levels) to enable continuity of spending.

European Regional Development Fund (ERDF): Sustainable urban development

13. The Commission proposes that a minimum of 5% ERDF funding at Member State level should be allocated to sustainable urban development - delegated to cities for management through Integrated Territorial Investment. What is your assessment of this proposal?

An increased focused on cities is positive. It encourages countries to consider using functional areas rather than administrative regions for determining how money is spent. The Commission’s proposals on sustainable urban development encourage integrated and joint management of different interventions; and they provide flexibility on management and implementation arrangements. However, as on other aspects of the Commission's proposals, I am not in favour of prescription based on set percentages of expenditure: for some Member States, cities may not be in regions where money needs to be spent, and domestic strategic priorities may not accord with an urban focus. My preference would be for Member States to be given the option – and for them to have to justify, during the negotiations with the Commission, why or why not they are taking up the 5% option.

22 December 2011

Ann Branch, DG - Education and Culture, European Commission, Agnieszka Moody, MEDIA Desk UK, and Yvette Vaughan-Jones, Visiting Arts – Oral Evidence (QQ28-48)

Transcript to be found under Agnieszka Moody, MEDIA Desk UK – Creative Europe

Business for New Europe – Written evidence

Business for New Europe (BNE) welcomes the opportunity to make a submission as part of the consideration by the House of Lords Select Committee on the European Union for their follow-up Inquiry into the EU Financial Framework. This evidence outlines what BNE views as the key priorities for the Multiannual Financial Framework 2014-2020.

1. Executive Summary

- Significantly **reform and reduce the Common Agricultural Policy** alongside increasing agricultural support for the poorest EU member states.
- **Overhaul eligibility criteria for EU cohesion funds** so that wealthier EU member states are responsible for their own "pockets of poverty."
- Increase investment in areas most conducive to Europe's long-term growth: **boost spending on research, infrastructure and SME's** access to finance.
- Think outside the box – **explore alternative budget options** to the multiannual financial framework.

2. Introductory Comments

2.1 BNE is an independent coalition of business leaders advocating a positive case for reform in Europe. We are an independent not-for-profit organisation funded by donations from the private sector with offices in London and Brussels.

2.2 Our Advisory Council consists of Chairmen and CEOs of FTSE 100 companies and our Executive consists of experts in foreign and economic policy.

2.3 We are involved in a wide range of advocacy activities to provide a platform for debate on European issues to business leaders and policy makers. We publish research, hold seminars and conferences, and contribute in the media. We seek to ensure that a reasoned, pro-European voice is heard in the UK.

2.4 On 10 October 2011, we released a publication entitled *"Rethinking the EU Budget: An alternative financial perspective for the Multiannual Financial Framework 2014-2020"*. The publication advocates considerable reform for the next Multiannual Financial Framework (MFF) based around the belief that spending which goes against the philosophy of the EU single market should be limited and funds should be reallocated to areas most conducive to competitiveness and long-term growth.

2.5 The author of the aforementioned publication, Ariane Poulain, specialises in quantitative and qualitative analysis, EU and UK affairs, immigration, development and economics. The editor, Phillip Souta, is an expert on the eurozone, regulatory affairs, international trade, and Britain's relationship with the EU, European foreign affairs, and comments on these issues regularly in the media.

2.6 BNE appreciates the opportunity to put forward evidence on the MFF and will focus on explaining why there should be: (a) a reduction or increase in certain policy areas and (b) rethinking of the overall size and shape of the long-term financial package.

3. Recommendations

3.1 The MFF amount allocated to Common Agricultural Policy (CAP) should be reduced. Reform is required to ensure that CAP spending is conducive to long-term growth and provides European Added Value to the EU's agricultural sectors. The main issues surrounding negative CAP spending are:

3.1.1 The allocation of direct payments are highly unequal: (a) over 50% of CAP goes to the top 16% of farmers (b) direct payments per hectare vary significantly across EU member states, from €462 to €190; this primarily disadvantages the Central and East European (CEE) member states and the CEEs are most in need of support to strengthen their agricultural sectors.

3.1.2 Subsidising the EU agricultural sector goes against the values of the single market: it is (a) highly protectionist and (b) distorts regional and global markets.

3.1.3 CAP is currently allocated over 40% of total MFF spending and of this amount, only 25% goes towards rural development. Rural development spending is more sustainable and effective than direct payments in the long-term.

3.2 We consider that the above issues should be addressed in the next MFF and as a result, an 8% reduction would be made to overall CAP spending but alongside efficiency gains and an increase in positive spending. The following reforms should be considered:

3.2.1 Introduction of means testing for individual beneficiaries of CAP.

3.2.2 A 50% reduction in direct payments to the top eleven EU member states with a GDP above the EU average, with the aim to phase out post-2020.

3.2.3 Increase direct payments by 26% to the four EU member states with the lowest GDP below the EU average.

3.2.4 An increase in rural development spending by over €4 billion.

3.3 Cohesion policy should also be reformed to ensure that funds are allocated to the regions in member states that are most in need of financial assistance to address their social, territorial and economic inequalities. In short, the richer EU member states should be responsible – from their national budgets – for their own regions that fall below the EU average. To address this, reforms to the eligibility criteria should be considered. We recommend the following:

3.3.1 Reform the convergence programme. At present, regions are eligible if they have a GDP less than 75% of the EU average. The next MFF should retain this ceiling but only apply to member states not regions; therefore, regions in member states with a GDP that is not less than 75% of the EU average would be excluded.

3.3.2 Reform the regional competitiveness and employment programme. At present, regions are eligible if their GDP per inhabitant falls between 1-25%. The next MFF should retain this ceiling but only apply to member states not regions.

3.3.3 Increase investment in the "European Territorial Objective", this cohesion programme is under-funded in the current MFF despite making a significant contribution to the improvement of cross-country transport links.

3.4 Increasing Europe's competitiveness must be a priority for the next seven year spending plan; the EU single market must not be undermined by a lack of smart investment, this requires investment towards areas that have the greatest potential to promote long-term competitiveness in Europe. Thus, the following recommendations are viewed as vital to boosting the EU's productivity, jobs and growth:

3.4.1 The EU should consider increasing investment in the European Research Council (ERC). The ERC is the best vehicle to accelerate EU innovation and would make a significant contribution to improving Europe's research and development arm. Doubling funding to the ERC is recommended. The European Commission proposals for the next MFF appear to boost spending for the Eighth Framework Programme (FP8), however, the inclusion of programmes that were previously outside of the scheme combined with overall cutbacks would lead to FP8 being reduced overall compared to the current Seventh Framework Programme (FP7).

3.4.2 Research investment needs to be better supported at the implementation level, namely for SMEs. SMEs provide approximately 90 million jobs and make up 99% of the EU's total enterprises. Access to finance for SME should be increased and any extra investment here should go towards the key frameworks SME Guarantee Facility (SMEG) and the High Growth and Innovative SME Facility (GIF) which would enlarge venture capital funds and loan guarantee schemes at the EU-level.

3.4.3 Member states should support the European Commission's proposal to create the new "Connecting Europe Facility" to significantly strengthen energy, transport and ICT infrastructure. Due to national budget pressures, EU-level financing is most effective for cross-border infrastructure projects.

4. Alternative options for reform

4.1 We strongly recommend the reforms detailed in Point 2 [Recommendations] but also advocate considering alternative approaches to the EU's next financial perspective package. The current challenges surrounding the EU and the eurozone may demand an approach to the long-term budgetary system that has not been previously explored.

4.1.1 Factor the amount of commitment appropriations that were not spent in MFF 2007-2013 into the negotiations for MFF 2014-2020. These unspent funds indicate that a reduction in certain policy areas is not directly correlated to unfulfilling programme targets. Therefore, significant reductions and reallocations could be achieved in the next MFF alongside an improvement in economic growth – less money but better spent.

4.1.2 Reforms to certain policy areas – such as those mentioned in Point 2 [Recommendations] – could be achieved outside of the financial package. The commitment appropriations for MFF 2014-2020 could be tightly limited at the most basic necessary ceiling and reforms could be made on a more annual-focused timeframe.

4.1.3 A single policy area in need of reform most could be prioritised within MFF 2014-2020. For example, CAP requires radical changes which would have a significant impact on MFF funds, whereas, infrastructure requires greater investment but not significant reform.

4.1.4 Reconsider the viability of 5-7 year financial perspectives. The concept of MFFs originates from 1986 when the SEA was signed and the EU decided to overhaul its annual budgetary procedure by creating long-term perspectives to link projects to finances. Unsurprisingly, all MFFs (since Delors Package 1) reflect the economic and political climate of their times; thus, in the light of the eurozone crisis and uncertainty surrounding future development, the EU may wish to consider shorter term budgets.

15 December 2012

Convention of Scottish Local Authorities (COSLA) – Written evidence

- The **Convention of Scottish Local Authorities (COSLA)** is the representative voice of all Scottish Local Authorities both nationally and internationally and it has long being advocating strong, consistent EU budgets in which local communities are given the means to prosper and where the partnership principle, whereby Local Authorities are fully involved in the design and implementation of the programmes, is fully applied.

- COSLA welcomes the opportunity to provide a follow up contribution to this public consultation on the future of the EU Budget. Since the proposal was tabled last June and the main draft regulations concerning the key funds have already been tabled since we have been able to discuss them in detail with our Councils, national and EU officials and MEPs in several occasions. Therefore we hope that the gathered evidence below is found useful for the Committee's inquiry.

1. Are the Commission's proposed expenditure ceilings appropriate, taking into account the pressures on so many Member States to pursue fiscal consolidation?

a) This is of course a political choice, one that needs based on financial and budgetary grounds, but inevitably it comes down to a political decision on whether the EU budget is the best place in which to allocate up to 154 billion euro of public money per year. As expressed in our earlier contribution this can be of course defined in terms of additionality (EU funds being able to deliver on outcomes that 27 domestic budgets cannot do separately).However this concept is wide enough, and as it is not articulated in the EU Law, so a decision would ultimately come down to a political judgment.
b) In terms of affordability, it is worth outlining that this year the UK Budget roughly amounted to 847 billion euro (thousand million) and its contribution to the EU, after the rebate, is around 12, 9 billion euro. This is a significant figure amounting, for sake of comparison, close to the total budget of Scottish councils. Conversely, the UK budget has many bigger headings than those. Also it is forecasted that Scotland will receive beyond one billion euro in regional and rural spend over the next EU Budgetary period and significantly larger amounts if counting CAP farm payments and other non-territorially earmarked spend from the EU thematic funds. All this to say that the figures, once put into perspective, it ultimately it comes down to whether the EU budget allocations do actually respond to EU-wide political and policy needs that the UK is prepared to support.
c) Concerning the ceilings, the Commission has introduced in its proposals a bit of political signposting. As the ceiling level is seen both by political actors and the media as one of the more visible and symbolic elements of the budget proposal, care was exercised for the existing maximum ceiling of 1.24% GNI to be respected while the actual budget in commitments are set as slightly lower level than the current one, even if the actual amount in absolute terms is larger.
d) In other words the current budget is, over seven years, €975bn, in commitment appropriations, (1.12% of EU GNI) the next Multi Annual Financial Framework asks for €1083bn (1.11%) over seven years. As a political signal to the group of net contributing Member States the actual expenditure to be paid per year (payment appropriations) is budgeted to be below the symbolic 1% of EU GNI or 972bn over seven years, which is actually slightly less than payments at the moment.

e) However to achieve these politically symbolic markers, the Commission now proposes that €58bn are placed outside the main budget headings and the above GNI thresholds. Irrespective of the technical reasons that might justify some of these amounts being moved outside the main budget, we are of the view it is necessary to look at all the funds that are put in and how it compares, in 2011 prices with the existing budget. The above figures point towards a slight increase (if €111bn euro can be considered a small amount) divided over seven years than the current total. At the same time the EU is much larger than it was in 2004 and the needs in many headings have all but diminished. So, again, it comes down to a political judgement.

f) Finally, the above question 1 draws a direct relation between the budget ceilings and the domestic fiscal consolidation. For a direct correlation to exist in the future, this would imply that the current system where the lion's share of the EU budget comes from Member State (MS) contribution is continued.

g) By contrast, the Commission is proposing to reduce by a quarter the current levels of MS contribution and these be replaced by EU wide own resources sources. This is aimed at moving from the existing "fair return" logic. Obviously the funds would still come from the same citizens and businesses in each Member State (MS). Whether the UK and other MS prepared to allow the EU institutions to raise in a significant way their own sources of income is wholly a political decision, one that it very much remains to be seen whether it has any chances to be agreed.

2. What is the most appropriate basis for comparing the Commission's proposals with current expenditure?

a) The Commission tries to make the best case possible for its proposal. However it is not possible, only by reading the Communication, to compare like for like. To simplify our own assessment we went to the rather painstaking exercise of comparing each budget heading of the current budget, in commitment appropriations and at 2011 prices in euro, with their successor in each heading of the new proposal. It is perhaps a rough estimate but we believe sufficiently accurate to broadly show the direction of travel of the changes per item of expenditure, as it can be seen below:

b)

COMPARISON 2007-13 Budget and 2014-20 budgets (commitment allocations, 2011 prices)			
Heading	**Now**	**Post 2014**	**Comment**
CAP Pillar I farm payments	€300bn	€281bn	Decrease €19bn
CAP rural development	€96bn	€89bn	Decrease €7bn
Cohesion "Convergence" Objective	€283bn	€230bn	Decrease €53bn Includes Cohesion fund. Partly transferred to Transition objective below
Cohesion "Competitiveness" Objective	€55bn	€53bn	Decrease €2bn. Includes Lowlands and Uplands of Scotland.
Cohesion "Transition" Objective	n/a	€39bn	New. currently is phasing in and phasing out, but these are accountable as part of existing Objectives 1 and 2 Includes Highlands and Islands

Cohesion "Territorial Cooperation"	€9bn	€11bn	Increase €2bn
Maritime and Fisheries Fund	€6.2bn	€6.7bn	Increase €500m
Innovation	€2.1bn innovation (CIP)	€80bn	Increase €30m (approx). New Merged Fund Research and Innovation (€60bn more to be earmarked in cohesion funding)
Research	€50.5 research (FP7)		
SME support	n/a	2.3bn	was part of CIP, now separate programme
Transport	€8bn	€21bn	Increase €13bn Part of Connecting Europe (without counting 10bn Cohesion)
Energy	€0.73	€9.1bn	Increase €8bn. Part of Connecting Europe (without counting cohesion earmarking) Includes Supergrid, possible funds for local energy efficiency
ICT	€0.72	€9.1bn	Increase €8bn Part of Connecting Europe (without counting cohesion earmarking)
Environment LIFE	€2.1bn	€2.6bn	€500m increase (without counting the CAP and Cohesion ringfencing)
Climate Change	n/a	€800	New fund, part of the new LIFE programme
European Solidarity Fund	€0.5bn	€7bn	Increase 7.5bn outside the budget
Globalisation Adjustment Fund	€2.3bn	€3bn	Increase 700m outside the budget, current figures is counting unspent funds as of 211
PROGRESS programme	€0.63bn	€0.8bn	Increase €200m New joint Education Youth Sport Programme
Education	€6.9bn	€15bn	
Youth	€0.8bn		
Training	n/a		
Sport			
Citizenship	€0.2bn	€0.2bn	
Culture	€0.4bn	€1.2bn (part of Creative Europe)	Creative Europe. €900m increase
Media	€0.75		
Justice and Home Affairs	€5.8bn	€8bn	Increase €2.2bn
External issues	€55bn	70bn	Increase €15bn
EU Civil Service	€54bn	€62bn	Increase €8bn (includes schools and pensions)
Proportion of budget funded by Member States	*75%*	*50%*	*Currently only VAT and CAP duties are own resources of the EU budge, the rest comes from the MS budget on a GNI basis*
TOTAL	**€972bn**	**€1083bn**	**(€111m increase)**

Please note that not all programmes are included in the above budget chart, only the more important are highlighted, around €30bn is spent in smaller programmes on nuclear energy, criminal justice, etc. All figures are in 2011 prices.

c) The short reading of the above is that 111 extra billion of the overall size over the new period is proposed and an additional €138bn has been made available to fund new priorities on innovation, transport, external aid, etc. which are seen as more universally supported than other budget headings, particularly the two largest, cohesion and CAP. These two headings will see their budget size cut €24bn and €11bn respectively. The rest of the 111bn budget increase would come from the new own resources that is proposed. In other words this draft budget is a difficult balancing act aiming to address the concerns of all key constituencies involved in this discussion. In typical EU consensus-building fashion it tries to enable the progress of the core agenda of each main player while avoiding endangering their respective core values. However this difficult balancing act rests in the assumption that Member States would agree their contributions to the budget decrease by a quarter in exchange for the EU to have enhanced revenue raising mechanisms (own resources) that would cover the 11% increase foreseen over seven years.

3. What benefits, both financial and practical, will be derived from the Commission's proposals for simplification, particularly through the use of common strategic frameworks in research policy (Horizon 2020) and regional policy? Is the Commission's approach strategically justified, or is it a mere merging of funds? How can the approach be made to work in practice?

a) The Commission proposals towards integration and simplification through a Common Strategic Framework (CSF) are widely supported by everyone involved in this discussion, including COSLA.
b) In particular, it is to be strongly welcome the creation of the Common Strategic Framework covering Rural Development, Regional Policy and Fisheries funds it will ensure that funds are delivered in an integrated fashion locally. Indeed we have been working with the Commission on Integrated Local Development partnerships, including the Scottish Community Planning Partnerships, which we would be keen to see as a main driver of the future Scottish programmes.
c) However, it needs to be questioned the rationale of having TWO Common Strategic Frameworks, one for cohesion and another for Innovation when the Budget proposal also say that they expect the Cohesion funding still provide at least €60bn to innovation. At the very least there is a clear and as yet unresolved demarcation issue. However it could also bear the question on in spite of the stated aim of funding consolidation (and acknowledging the EU wide tendering of the new research H2020 programmes), why there are two very sizeable but separate EU funds (80bn and 60bn) dealing with innovation.
d) Thirdly, while the Cohesion Budget will spend a sizeable amount of resources on transport and energy, the little effort has been made for new Connecting Europe facility to be linked or even part of the above mentioned CSF. There is a fourth Common Strategic Framework dealing with Education, training, youth and sport: €15bn (a 68% increase).
e) This disconnect between these four Strategic Frameworks reflect not only practical reasons but crucially, inter-departmental arrangements rather than a policy rationale on the ground.
f) Even in the Cohesion-Rural-Maritime CSF the ringfencing of the European Social Fund (52% of allocations to prosperous regions) or the earmarking of up to 30% of CAP and

cohesion to environmental purposes respond again more to balancing acts between Commission Directorates than a strict and cold assessment of spending needs.

g) Even delineation between the priorities of each fund, crucial to avoid overlapping and gaps in expenditure, remains sketchy. This was supposed to be resolved through the draft General Regulation tabled last October 6. However the "menu" of priorities for all funds proposed in its Art. 9 does not allow to relate this global menu with each of the eligible spending activities foreseen in the four fund-specific draft regulations (ERDF, ESF, EMFF, EAFRD), so further polishing is needed in the Common Strategic Framework proposal that will be launched end this year and subject to two months consultation, to which COSLA will participate.
h) In terms of implementation on the Regional-Rural-Maritime CSF, which is the one of more direct interest for local government, it is to be extremely welcome that the new Partnership Contract between the Commission and each Member State covers the above four funds, thus inciting each relevant government department to work with its peers from the outset. Furthermore the draft General Regulation's Article 5 clearly foresees that Local Government from across the UK should be involved also from the outset in these preparations, something we are waiting for central government to indicate the process.
i) However, the biggest breakthrough from Local Government, something COSLA has been actively campaigning for is the very detailed proposals in the Gen. Reg. over <u>local development</u>. An entire chapter (Ch. II) is outlined to foresee how all these EU rural, regional and maritime funds can be targeted to, and eventually directly managed by local communities for the design implementation of multi-dimensional and cross-sectoral EU funded strategies and programmes. This coupled with other instruments such as the Integrated Territorial Instruments and the Joint Action Plans, would allow, if Governments allow for it, for these EU funds put together in an integrated way by local communities to respond to local needs on the ground.

4. Is the proposed distribution of funds between and within the five main expenditure headings right? In particular, do the proposals offer enough to fulfil the aims of the Europe 2020 strategy? If you call for more spending in one area, please say whether you would expect a net increase or an offsetting saving elsewhere.

a) We have already outlined in the chart of Question 2 the main shifts between the existing and proposed EU budget headings. As outlined above the proposal is the result of the Commission trying to address a wide variety of constituencies and inter-departmental balances. Equally as outlined in the above question, the existence of four Common Strategic Frameworks does amount to an unfinished work in progress to achieve proper consistence, clear delineation and effectiveness of the several streams of EU funding.

b) As asking for further reallocations between funds could prove technically and politically difficult given that we only have a year to get the overall Budget approved before starting the specific spending plans per country, region and per programme rather than a attempting a radical overhaul at this stage, which could be impractical if the main goal is to have the funds up and running on 1 January 2014, what can and should be attempted is a clear delineation and demarcation on the funds. For instance, if both the new Horizon2020 research programme (€80bn) funds basic research, then the about 20% that is estimated to be used for innovation-related purposes of the total €183bn that would be available through European Regional Development Fund (ERDF) should be used for different purposes in our outside the innovation chain. For instance, linking the innovation coming up from the local research community to generate wider economic return to the surrounding local economy. The same can be said from similar areas of potential overlap on energy and transport (between ERDF and Connecting Europe), social inclusion (ESF, ERDF, CSF Education), SME support (EAFRD, ERDF, H2020), not to speak on climate and environment (CAP Pillar I, EAFRD, ERDF, LIFE). Finally the Common Strategic Framework on Rural, Regional and Maritime Funding clearly needs the priorities better demarcated than what the General Regulation menu is proposing.

c) This can be undertaken through the coordinated amending of the respective draft Regulations as they go through the legislative pipeline and, as regards to the Regional and rural funding, through the actual Common Strategic Framework proposal to be tabled, and open for public consultation in the next few weeks.

d) Finally, as it could not be otherwise COSLA strongly request the UK to support the transition regions category foreseen in the EU budget as this will enable at least a dozen of the poorest UK regions, including the Highlands and Islands of Scotland, to cope with the tough economic situation that they face at the moment.

5. Do the proposals live up to the aims set out in the Commission's *Budget for Europe 2020* of: focus on delivering key policy priorities; focus on EU added value; focus on impacts and results; and delivering mutual benefits across the EU?

a) As outlined in the two previous questions, the proposals move in the right direction, but they are only halfway there, particularly as regards to delivering integrated and consistent approaches on the ground.

b) Equally additionality is still a wide concept that can only be partially measured at this stage. Nevertheless the move towards outcomes does clearly signify progress towards proving additionality of EU funds, which as we said it is the clear criteria to justify specific investments being made at EU level.

c) There has been some good progress in terms of moving from an output based policy, where the priority was to ensure that the money was spent according to the rules, towards an outcome based policy delivery, where the ultimate purpose of the funds is to achieve tangible results on the ground. This is most particularly the case of Cohesion Policy than other areas where the move is still more tentative. However even in Cohesion Policy the approach is more open ended in the draft legislation than in the original drafts. The General Regulation and those governing the four funds do contain annexes where a performance framework is introduced. Member States and the Commission need to agree to a series of results to be achieved and measured at several stages of the programming period, with a performance reserve awarded to the more performing ones. The approach is however tentative and less detailed than the Commission original plans simply because very few governments operate domestically using outcomes. There is an issue here as the outcomes to be achieved to deliver Europe2020 will be defined, negotiated and assessed at UK level in the Partnership Contract with the Commission. In spite of assurances from the Commission that the UK Partnership Contract will in effect be a collection of national chapters for each of the home nations, the need for the UK to report and deliver Europe2020 objective through the EU funds might bring to a more centralistic dynamic that would be perhaps desirable. This is why COSLA would be keen to see article 5 of the General Regulation provisions for partnership negotiations between the central the devolved and the four local government administrations to be fully exploited so that whatever outcomes the UK signs up to, they would have been agreed and understood by all concerned governance levels rather than be imposed from the top down.

d) There are also internal constraints to how far the Commission can move towards outcomes. For instance it is extremely interesting their proposal to create Joint Action Plans to deliver part of the Structural Funds, such Plans would keep audit and reporting bureaucracy to a minimum as they would be measured mainly on whether they have delivered over a given period previously agreed. However, the extensive use of this and other new schemes will very much depend on whether the EU Court of Auditors would be comfortable with this new, and in their eyes, potentially more unreliable delivery method. The Court's views on these proposals are not know yet adding an element of incertitude.

e) Finally, COSLA is keen to assist the UK Government in defining an outcome based system to report and measure the use of EU funds throughout the UK. Scotland is rather unique in Europe in having developed Single Outcome Agreements (SOAs) between national and local authorities for the delivery of domestic policies. There is ample scope for the EU fund, both in Scotland and elsewhere in the UK to draw from the lessons learnt in developing the SOAs in Scotland.

6. What is your assessment of the Commission's proposals for expenditure outside the MFF framework?

a) We already outlined in the above answer 1.d that while there might be technical reasons to put part of the proposed expend outside the main headings we believe that any assessment of the budget needs to take into account the whole amounts as we have attempted ourselves.

7. What is your assessment of the Commission's proposals to grant the EU more 'own resources' and of the choices advocated (a new VAT resource and/or a financial transactions tax)?

a) As indicated in answer 2.c, this is a crucial element of the proposals as if MS do not agree for a significant expansion of the own resources system the whole carefully crafted budget proposal unravels, forcing unwelcome cuts in some areas dear to local government such as Cohesion and possibly across all headings, including those that have been proposed drastic increases. Ultimately is a political decision and a long term policy consideration up for each MS government to consider.

8. What is your assessment of the likely impacts of the Commission's proposed restructuring of abatement mechanisms on the UK or other net contributors?

a) This is a question that as local government we will defer to consider to the appropriate instances.

9. What is your assessment of the innovative financing instruments proposed by the Commission?

a) On paper, they mean progress. Creating a uniform and standard legal basis for all purposes of financial engineering would remove the tentative and quite slow implementation of the existing tools. A proof of this is that only in mid-December 2011, four years after the official start of the programmes the first financial engineering tool worth €50m was unveiled in Scotland, with many other countries further behind.

10. What effects could the development of the Eurozone, in response to the Euro area crisis, have on the future EU budget?

a) While agreeing to an EU budget is never easy, this time adds an unprecedented variable of the uncertainty. However as we are aware that detailed negotiations among Member States and MEPs on all these programmes are taking place irrespective of this wider considerations, it is the intention of COSLA to continue actively engaging and making the case for solid provisions that will deliver efficient EU-funded local development policies in Scotland.

December 2011

Department for Culture, Media and Sport – Oral Evidence (QQ1-37)

Transcript to be found under HM Treasury – Connecting Europe

Department for Energy and Climate Change – Oral Evidence (QQ1-37)

Transcript to be found under HM Treasury – Connecting Europe

Department for Transport – Oral Evidence (QQ1-37)

Transcript to be found under HM Treasury – Connecting Europe

European Economic and Social Committee, Section for Economic and Monetary Union, Economic and Social Cohesion – Written evidence

1. Preamble

1.1. Being a body of the European Union, the European Economic and Social Committee (EESC) has just started the process of elaborating its position following the initiation of the respective procedures by the European Commission with the adoption of its Communication on the Budget for EU 2020, COM(2011) 500 final.

1.2. One opinion of the European Economic and Social Committee will deal with the Budget 2014-2020, a second one will deal with the system of own resources, and there will equally be an opinion on the related proposal on a financial transaction tax. The EESC opinions on this matter will, according to current planning, be adopted in March 2011. During the drafting of the opinions a hearing with Commissioner Lewandowski (tbc), Members of the European Parliament and various stakeholders will be held at the EESC's premises in Brussels.

1.3. The principles for a future financial framework outlined below have been agreed in earlier work, and have been put together by my secretariat, based on the EESC opinion "*The EU Budget Review* "[1] of 16 June 2011.

1.4. This opinion is attached for further reference

1.5. The EESC is at the disposal of the Select Committee on the European Union of the House of Lords for further cooperation, especially in view of a the public hearing you announce for January 2012 at which our Rapporteur would be available to present the updated views of the European Economic and Social Committee on that matter.

2. Agreed principles for the new multiannual financial framework 2014-2020

2.1. The EU budget review is a tool serving a political project. Today the European Union does not have the budgetary means to implement either its political strategy or the commitments deriving from the new Lisbon Treaty.

2.2. The economic and financial crisis has severely affected Europe and caused a cascade of growing deficits in most Member States. This situation inevitably has repercussions for the next multiannual financial framework but the European Union must not be the victim of this.

2.3. We therefore have to have the imagination to draw up a "smart" European budget which will provide the EU with the means to achieve its objectives without increasing the overall tax burden on the public and on businesses.

[1] OJ C 248 of 25.08.2011, p. 75.

2.4. The "juste retour" principle must be abandoned as it is contrary to the values of solidarity and mutual benefit which underpin European integration. Rather, the subsidiarity principle needs to be applied by transferring to European level that which has lost its meaning and effectiveness at national level. The EESC congratulates the European Commission on proposing a return to the principle of own resources which can be newly created or substituted for national taxes.

2.5. The European budget must be strengthened and have a leverage effect. The EESC maintains that national and European budgets should complement each other, which will make it possible to achieve economies of scale with a view to meeting the EU's major political objectives. The effectiveness of EU action will also be strengthened by more systematic recourse to EIB loans, public-private partnerships and the creation of Eurobonds for investment.

2.6. In order to show that a euro can be better at used at European level, the EU must embark on a real revolution in procedures, which today are much too cumbersome, and concentrate its action on projects with a high public profile.

2.7. The only way to make a success of an ambitious budget is to win the battle of public opinion. That is why the EESC would like studies to be carried out and published on the cost of non-Europe, highlighting duplication in national budgets. In this way the EESC is supporting the European Parliament's initiative.

2.8. In order to be credible vis-à-vis European citizens, the EU budget must be a model of governance, effectiveness, transparency and control of administrative expenditure.

European Economic and Social Committee

ECO/290
The EU Budget Review

Brussels, 30 November 2011

Brussels, 7 June 2011

OPINION
of the
Section for Economic and Monetary Union and Economic and Social Cohesion
on the
Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee, the Committee of the Regions and the national parliaments: The EU Budget Review
COM(2010) 700 final

Rapporteur: **Mr Malosse**
Co-rapporteur: **Mr Dantin**

Administrator: Gerald Klec

European Economic and Social Committee, Section for Economic and Monetary Union, Economic and Social Cohesion – Written evidence

On 19 October 2010, the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the

> *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee, the Committee of the Regions and the national parliaments - The EU Budget Review*
> COM(2010) 700 final.

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 31 May 2011.

At its ... plenary session, held on … (meeting of ...), the European Economic and Social Committee adopted the following opinion by … votes to…, with… abstentions:

*

*   *

Conclusions and recommendations

1. **The EU budget review is not a question of figures but rather a tool serving a political project. Today the European Union does not have the budgetary means to implement either its political strategy or the commitments deriving from the new Lisbon Treaty.**

1.1 The economic and financial crisis, which began in the United States, has severely affected Europe and caused a cascade of growing deficits in most Member States. This situation inevitably has repercussions for the preparation of the 2014/2020 financial perspective but the European Union must not be the victim of this.

1.2 We therefore have to have the imagination to draw up a "smart" European budget which will provide the EU with the means to achieve its objectives without increasing the overall tax burden on the public and on businesses**.**

1.3 The "juste retour" principle must be abandoned as it is contrary to the values of solidarity and mutual benefit which underpin European integration. Rather, the subsidiarity principle needs to be applied by transferring to European level that which has lost its meaning and effectiveness at national level. The EESC congratulates the European Commission on proposing a return to the principle of own resources which can be newly created or substituted for national taxes.

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1.5 In order to show that a euro can be better at used at European level, the EU must embark on a real revolution in procedures, which today are much too cumbersome, and concentrate its action on projects with a high public profile.

1.6 The only way to make a success of an ambitious budget is to win the battle of public opinion. That is why the EESC would like studies to be carried out and published on the cost of non-Europe, highlighting duplication in national budgets. In this way the EESC is supporting the European Parliament's initiative, to which it will make its contribution.

1.7 In order to be credible vis-à-vis European citizens, the EU budget must be a model of governance, effectiveness, transparency and control of administrative expenditure.

2. In search of a **new** objective

2.1 In its communication, the Commission does not hide its desire to set out an ambitious approach for establishing the EU's post-2013 financial perspective. The EESC welcomes this since the Treaty of Lisbon has opened the way towards a strong political identity for the European Union.

2.2 The EESC agrees with the Commission that the concept of "juste retour" is even less appropriate today than it was at the start of the European venture. This concept, which has too often distorted European integration and derailed debates, is in large measure responsible for the shortcomings, delays and failures of the integration process. It runs counter to the spirit of a union of states and peoples and defies rational economic argument. The advantages and added value of an economic, monetary and political union should, by their very nature, be of benefit to everyone. The progress made by the European Union is all based on the multiplier effect of joint efforts, the polar opposite of the "juste retour".

2.3 On the basis of these considerations, the Committee was of the view as early as 2008 that "There is a fundamental choice to be made when shaping budget policy: federalism or an intergovernmental system. Clearly, the arrangements for financing the budget are one measure of the level of advancement of European integration[2]".

2.4 In this connection, the Committee would also like all lessons to be drawn from an objective analysis of the way in which the budget currently functions. The Commission rightly points the finger at delays in the launch of programmes, the complexities inherent in the system and decentralised implementation, which has not yielded positive results. These shortcomings must be analysed in depth with the participation of all stakeholders in order to learn the necessary lessons to correct them.

2.5 The EESC supports the four core principles set out by the Commission: delivering key policy priorities, strengthening added value, the obligation to ensure results and

[2] EESC opinion, EU budget reform and future financing, OJ C 204, 9.8.2008, p. 113.

maximising the mutual benefits of solidarity. The EESC wishes to add one further requirement, visibility:

2.5.1 The current impact of the EU's budgetary measures is not satisfactory from this point of view. This shortcoming is an obstacle to European integration since it makes it more difficult to achieve genuine public support and provides Member States with arguments to curb the growth of the European budget. This should be rectified from the point of view both of the budgetary procedure, which seems very opaque to the public, and of operational expenditure, which too often is confidential, scattered over minuscule projects or concealed within the framework of complex co-financing**.**

2.6 For the EESC, such changes to the EU's budget policy should contribute directly to the objective of renewing the Community method, which the Committee explicitly called for in its opinion of October 2010, adopted by a very large majority[3]**.**

3. In search of greater complementarity between the national and European levels

3.1 The EESC cannot accept the process of European integration, which depends on the budgetary resources it is granted, being taken hostage by the question of reducing public deficits. This would jeopardise the political ambitions of the European Union stemming from the Lisbon Treaty and the Europe 2020 strategy.

3.2 The EESC proposes complementarity between national budgets and the European budget on common objectives, for example via partnership contracts for the 2020 strategy's development and investment. It would also involve the "smart" aggregation of national and European resources in order to achieve economies of scale and a leverage effect and reduce national budget deficits as a result of the positive effects of pooling of resources.

3.3 To this end, the Committee calls on the Commission to provide the necessary funds to update without any further delay the evaluation of the cost of non-Europe, which has not been calculated since the Cecchini report4 23 years ago. The Committee welcomes the intention expressed by the European Parliament to undertake an initiative in this area. The Committee itself intends to participate fully in work in this area and to make an active contribution**.**

3.3.1 European citizens and taxpayers should be aware of the size of the bill they are now forced to pay as a result of the unnecessary duplicate costs of persistent barriers in both administrative and economic areas. They should be informed of the "economies of scale" from which European public policies could benefit through further integration. For example, the public pays every day for the absence of a European transport system, although enshrined in the Treaty of Rome, in terms of delays and disruptions and a certain lack of productivity for businesses. The same applies to the inadequate opening up of public procurement, although the Cecchini report estimated that opening up European public procurement could generate two million new jobs.

[3] EESC opinion, Renewal of the Community method (guidelines), OJ C 51, 17.2.2011, p. 29.
[4] Cecchini report on The Cost of Non-Europe, Paolo Cecchini, 1988.

3.4 The EESC stresses in particular the knock-on economic effect that one would rightly expect from an increase in the European budget based on such economies of scale. By offsetting the negative impact of severe corrective measures in national public finances through productivity gains, the need for budgetary discipline to deal with deficits could be reconciled with economic and social recovery to help Europe emerge from the crisis and "weak" growth**.**

3.5 This kind of support for the economy would in turn have a positive impact on tax revenues and thus on balancing public accounts. A smart increase in the European budget should make it possible to initiate and sustain a virtuous economic and budgetary circle by exploiting areas of mutual complementarity. Sustainable consolidation of growth and employment in Europe requires that these complementaries between the national and European levels be exploited**.**

4. Seeking greater budgetary autonomy

4.1 The EESC believes that increasing the European budget is not only desirable but necessary, given the scale of the new challenges requiring a joint response**.**

4,2 To this end, it supports the European Commission's proposal concerning the primacy of a system based on own resources, with revenues going directly into the EU budget without passing via the national level. The EESC considers that there will be no effective reform of the European budget without restoring well targeted, sustainable and autonomous own resources, in place of national contributions which were introduced from 1980 with a special rebate for the United Kingdom, and which were made permanent by the 1984 Fontainebleau Agreement, perpetuating the erroneous concept of the "juste retour"**.**

4.3 The Committee appreciates the diversity of the proposals for new resources put forward by the Commission in its communication, particularly those regarding financial transactions and CO2. Without wishing to comment at this stage on the nature of the new own resources, the EESC stresses the need to submit all proposals in this area to an impact analysis, which will permit a more effective assessment. The Committee would also like the possibility to be explored of transferring taxes or a proportion of existing national-level taxes to the European level, using VAT as a model. One possibility here would be to transfer a proportion of corporation tax if there were a common base, as proposed by the European Commission**.**

4.4 The EESC expects that such a reform would potentially remove national corrective mechanisms over the long term which would no longer be justified in a reformed European budget providing extra added value for all Member States.

4.5 The EESC also stresses three principles which it believes are key to the success of any reform of the European budget's resources**:**

4.5.1 The tax burden in Europe must not rise as a result of the reform of own resources**.**

4.5.2 The possible new European levies must not have an excessive discriminatory impact on certain countries on grounds of their specific national features or hamper the activities of businesses established in the European Union. Nor should they have an excessive impact on citizens, especially the most disadvantaged, as is the case with VAT.

4.5.3 The reorganisation should contribute to rationalisation and better balancing of the overall tax burden, in line with the Union's competitiveness and employment objectives. European expenditure should also be focused more on the EU's priorities and areas where economies of scale can be achieved. For the EESC this is a necessary precondition for any significant increase in the European budget**.**

4.6 Finally, the EESC believes that it could be possible, pending further EU integration, to adopt innovative approaches bringing together, through specialised agencies or some other route, national budgets and the European budget in areas such as research and development, innovation, development aid, and financing of major infrastructure. Such an approach would make it possible to achieve real integration of priorities and means, while ensuring monitoring capacity at each political level of responsibility, both national and European.

5. In favour of measures geared more towards European added value

5.1 The Committee stresses the need to ensure that the European budget matches the objectives and commitments of the Europe 2020 strategy. Apart from the corresponding budgetary resources, this also requires visible links between the budgetary activities planned and the various pillars of the Europe 2020 strategy.

5.2 The Committee particularly stresses the need for effective use of the budget in areas where the European Union has direct responsibility: first and foremost consolidating economic and monetary union, strengthening solidarity among EU Member States and implementing new policies stemming from the Lisbon Treaty: energy and climate, justice and home affairs and external policy**.**

5.3 The recent crises in the euro area have underscored the need to promote solidarity within the framework of economic and monetary union in particular. The means available under the European budget have themselves provided useful, urgently needed support, anticipating the creation of the stabilisation fund. The decision to incorporate this stabilisation mechanism into the Treaty is a new stage in European solidarity and in meeting the objective of political and economic integration, with a view to sustainable consolidation of the economic and monetary union which has been a key element of progress in the European venture and the economic and social cohesion of the single market. It is for example urgent to relaunch the economic union which has lagged behind monetary union, thus weakening it. The Europe 2020 strategy will have little prospect of success unless this gap is closed. This prospect should have been examined in greater depth in the Commission document**.**

5.4 The other major priority for the European budget is, as rightly stressed by the Commission, strengthening the policies of the "magic triangle" of research, innovation and education, which are at the heart of the challenge of globalisation**.**

5.4.1 However, with a budget representing just 4% of that of public research in Europe, it will not be possible to change the situation fundamentally in the face of global challenges. The means must be found, especially financial means, to transform

European programmes into useful tools to make European industry more competitive.

5.4.2 Integrating national programmes and the European research framework programme in one way or another is vital in order to achieve economies of scale and critical mass. It will also be essential to ensure that the focus is on key sectors, to take account of specific national points of departure and to correct any shortcomings identified, especially administrative practices which weigh or slow down proceedings.

5.4.3 The European innovation policy should form a fundamental basis at the heart of research in Europe, whereas to date it has been treated by the Commission merely as a by-product of research measures. The European Commission was due to propose a major change and this is what it did in its recent communication Europe 2020 Flagship Initiative – Innovation Union (COM(2010) 546 final).

5.4.4 The EESC reiterates in particular its calls for a far more ambitious policy linking support for entrepreneurship, the removal of barriers between national networks supporting and promoting innovation and a European "clusters" policy, in order to allow "European champions" to emerge in place of "national champions". The Committee welcomes the decision taken to introduce reinforced coordination with a view to creating a Community patent. This should be put into effect as soon as possible in order to end a situation which has been a serious handicap to EU competitiveness for decades.

5.4.5 In the area of education, the EESC has called for more ambitious initiatives and in particular the launch of new "European schools", open to all, as a tangible sign of a stronger European identity, the emergence of genuine European universities5 as well as a European policy of new skills for new jobs[6]**.**

5.4.6 The European Commission should pay greater attention to objective analyses of the effects of EU policies and to ensuring precise correlation between the information included in the annexes and the main document.

5.5 The economic, social and territorial cohesion policy also contributes directly to development of European solidarity. The EESC will oppose any dismantling of this policy, which is the symbol of a union of peoples. However, the EESC calls for it to be overhauled to make it more effective, especially by simplifying the way it is managed, focussing more on flagship projects linked to European priorities and ensuring that economic and social stakeholders are involved more closely. With this in mind, the EU must tackle the exclusion of the most vulnerable sections of the population and support the countries and regions which are the most remote and disadvantaged on account of their specific characteristics in order to allow them to participate fully in economic and social progress. From this point of view, and with regard to the employment situation, the European Social Fund should be the preferred instrument, particularly in view of its financing, for the implementation of the European Employment Strategy. This should be at the centre of the "inclusive growth" strategy of Europe 2020.

[5] EESC opinion, Universities for Europe, OJ C 128, 18.5.2010, p. 48.
[6] EESC opinion, New skills for new jobs, OJ C 128, 18.5.2010, p. 74.

5.6 A major priority of the Community budget, which is directly linked to the objective of a more effective and cohesive EU, which is closer to the grass roots, should be to invest more in European public goods. This priority is rightly mentioned by the Commission. However, it should be spelt out and stated in practical terms. For its part, the EESC intends to explore the matter in greater depth in conjunction with economic and social stakeholders with a view to clarifying needs and objectives. The EESC would stress a number of requirements in this connection:

5.6.1 The EESC stresses first and foremost the need to develop genuine services of general interest at European level, complementing national administrations and in partnership with European users, in order to ensure the sound organisation and security of the EU in areas coming under its collective responsibility.

5.6.1.1 This concerns in particular the organisation of the internal market and customs, but also new areas where the Member States have decided to transfer powers: immigration and asylum policy, justice and home affairs, the establishment of the European diplomatic and external action service as well as guarding external borders.

5.6.2 The EESC also stresses the need to increase trans-European infrastructure investment, *inter alia*, in order to support these European services of general interest and to ensure that they function correctly. There have been too many delays since Jacques Delors presented the Commission's White Paper in 1993, whose proposals and methodology have hardly been followed up by action. A large area of Europe, especially in the countries which have recently joined the EU, remains excluded from major trade patterns on account of these shortcomings. Among the infrastructure priorities to be met, the EESC stresses structural projects, such as the specifications of the Single European Sky[7], high-speed train lines and networks of navigable canals. Large-scale investment with a European dimension is also required in the field of energy policy in order to ensure greater independence of supply and in order to invest in security, efficiency and renewable energies.

5.6.3 There is also a need for common innovative investment to deal with the new challenges of competitiveness and security in the area of telecommunications, the environment and civil protection.

5.7 As regards the common agricultural policy (CAP), the EESC reiterates its support[8] for an overhaul of the policy. It is a question of reform in order to adapt to the new challenges without renationalising or abandoning the principles which are its strengths: internal and external solidarity, quality of food production, Community preference, territorial cohesion to promote rural areas, especially upland and island areas. Indeed, one of the CAP's main tasks is to upgrade the role of farmers. It is also required to contribute to the sustainable management of natural resources, making it possible to respond in specific ways to the major challenges of combating climate change, protecting the environment and biodiversity[9].

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[7] EESC opinion, Single European Sky, OJ C 182, 4.8.2009, p. 50.
[8] EESC opinion, Strengthening the European agri-food model, OJ C 18, 19.1.2011, p. 1.
[9] EESC opinion, The future of the CAP , OJ C 132, 3.5.2011, p. 63.

5.8 In respect of external policy and development aid for third countries, the EESC reiterates its support for streamlining the representations of the EU and Members States, as well as making European aid more effective, complementing national aid and in closer partnership with the economic and social stakeholders directly concerned.

5.9 With regard to development aid, where traceability of use has to be ensured, the EESC considers that it would be appropriate to combine the national and European programmes, both in the interests of effectiveness and coherence and in order to make European support more visible. In this connection, the EESC points out that the clause in the Cotonou agreements reserving 15% of EDF aid for activities by non-state actors was introduced on its initiative. It proposes that this principle be applied and extended to all development programmes.

6. In search of effectiveness

6.1 At this difficult time for European public finances, the European budget should set an example of good governance. Without resorting to facile demagogy about the administrative costs of the European institutions, which are proportionately much less expensive than national administrations (for example, the European Commission employs no more staff than the city of Paris!), the EESC recommends that measures be taken to highlight the participation of the European institutions in the administrative economies being undertaken by the Member States. At the same time, the institutions, including the EESC, should be mindful of the principles of equal opportunities and non-discrimination enshrined in the Treaty during recruitment and promotion procedures. The EESC stresses, however, that good governance also requires giving European civil society the means to participate fully in the European debate.

6.2 The support provided through the European budget to Member States should itself be subject to greater conditionality; in particular beneficiaries should respect Community rules and ECJ rulings and it should be ensured that Community support is compatible with competition rules.

6.3 Faced with the challenges of converging economic policies within the framework of EMU, support should be geared more towards ensuring conformity with the requirements of the Euro Plus Pact.

6.4 The financial support granted to third countries should be dependent on the traceability of its use, respect for their commitments, especially as regards economic and social reforms geared towards openness, mutual partnerships, and participation of socio-occupational stakeholders from civil society.

6.5 The development of the euro and the need to consolidate the cohesion of the euro area vis à vis the markets also provides untapped possibilities for innovative borrowing and lending policies at European level, multiplying the impact of support from the European budget. First of all, the EESC calls for greater coordination between the ECB, the Eurogroup and the EIB. It welcomes the encouraging results of the first Eurobonds and is keen for them to be extended to the areas of training, research, industry and European infrastructure. At the same time, provided that strict conditions and requirements are met, the establishment of this "European treasury" could be used to pool a significant proportion of the Member States' debts. These instruments would be further evidence of the European Union's internal solidarity, and its political commitment to the irreversibility of the euro.

6.6 The EESC advocates better identification of projects supported by the European Union with a view to focusing on that which offers the greatest European added value. The EESC therefore calls for greater flexibility in the "additionality" rule, which should no longer be judged on a project-by-project basis but rather in a global manner in the framework of strategic partnerships with Member States.

6.7 Accelerating the procedures for defining priorities and allocating funds may also make it possible to respond to certain needs. The EESC has already recommended exploring more widespread use of either specialised agencies or global subsidies to grassroots bodies, such as regions or civil society organisations. The latter technique, which the EESC prefers, has worked well for regional policy and could be extended to all the EU's financial measures.

6.8 For major investment projects the use of EIB loans and private financing must also be encouraged, with a legal framework such as the one formulated in a recent EESC opinion[10]. Developing this on a new scale would make it possible to make up the European delays in infrastructure construction and to finance the major technological projects which will determine our competitiveness against a background of globalisation.

6.9 Furthermore, the EESC believes that more flexibility and better adapted mechanisms may be required for emergency situations, following the example of the Globalisation Adjustment Fund[11].

Brussels, 31 May 2011

The President
of the
Section for Economic and Monetary Union
and Economic and Social Cohesion

Michael Smyth

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[10] EESC opinion, Private and public investment, OJ C 51, 17.2.2011, p. 59.
[11] EESC opinion, EU budget reform and future financing, OJ C 204, 9.8.2008, p. 113.

HM Treasury – Oral evidence (QQ 1-37)

CONNECTING EUROPE

Evidence Session No. 1. *Heard in Public.* *Questions 1 - 37*

MONDAY 19 DECEMBER 2011

Members present

Baroness O'Cathain (Chairman)
Lord Bradshaw
Lord Brooke of Alverthorpe
Lord Clinton-Davis
Lord James of Blackheath
Lord Plumb
Lord Rowe-Beddoe
Lord Ryder of Wensum
Baroness Valentine
Lord Walpole

Examination of Witnesses

Mike Glycopantis, Deputy Director, International and European Group, HM Treasury, **Simon Towler**, Deputy Director, Head of Spectrum, Broadband and International ICT, Department for Culture, Media and Sport, **Katrina McLeay**, Head, EU Low-Carbon and Climate Change Policy, International Energy and Technology Directorate, Department of Energy and Climate Change, and **Verna Cruickshank**, DfT Lead on TEN-T Policy Review, Department for Transport

Q1 The Chairman: Ladies and gentlemen, thank you very much indeed for coming here at fairly short notice. A couple of weeks ago we would not even have thought about this sort of session, but it has been thrown at us, in a way. Before we start, could you give us just a quick view of the future you see for this, or how you see this all getting connected in terms of the Multi-annual Financial Framework? I will start with the Treasury, as we always seem to start with the Treasury. You are very welcome, Mr Glycopantis. Perhaps you could give us a two-minute—or thereabouts—introduction as to how you see this.

Mike Glycopantis: We are at a very early stage of the negotiation. We had the Commission's overall proposal, as you know, at the end of June, and we are getting all the different regulations that make up the financial framework during the six months up to Christmas. A couple might come out in January. In terms of the Connecting Europe facility, the Government believes that a greater share of the EU budget should go towards growth-enhancing infrastructure. We, and all the departments here think the same, believe that this is an area where conceptually there is a strong case for EU value added and certainly a much stronger case than in other parts of the EU budget. We are certainly well disposed towards some of the thinking behind this proposal and elements of this proposal, and of course you will hear from the departments about the detail.

The other thing I should say to introduce this is that I speak to the other member states all the time and there is a degree of scepticism about the instrument. Some member states see the EU value-added aspect of it, but there is a degree of scepticism that comes from the net-contributor member states in particular. This brings me on to my main point for the Treasury, which is that this proposal for extra money for Connecting Europe is part of a proposal that the Government has deemed far too big for the next financial framework. We calculated on our chosen measure—the payments that will flow out of the EU budget—that the proposal from the Commission was over €100 billion bigger than the ceiling set out by the Prime Minister, President Sarkozy and Chancellor Merkel.

Q2 Lord Ryder of Wensum: Sorry, did you say, "Only €100 million"?

Mike Glycopantis: Over €100 billion.

Lord Ryder of Wensum: Only €100 billion?

Mike Glycopantis: Over €100 billion.

The Chairman: Over the original.

Lord Ryder of Wensum: I just wanted that repeated so there was no doubt about it, thank you.

Mike Glycopantis: Over €100 billion. The Prime Minister wrote last December, almost exactly a year ago, with four other heads of state, including President Sarkozy and Chancellor Merkel, setting out his desired path for the future EU budget. The basic idea is that the budget should be at a maximum frozen in real terms. That allows for growth at 2% less. That is the real-term inflator, but the Prime Minister and the other heads of state said that should be the maximum: the budget should not grow in payments by more than inflation. They set out a path right through to 2020. The proposal the Commission subsequently came out with is over £100 billion higher than that.

Q3 The Chairman: What is that in percentage terms? Could you just remind us?
Mike Glycopantis: It is about 11%.

The Chairman: I see. Does that mean it is just a stalemate, and the Commission is going to just fight and insist that it gets its way, or are the governments going to say, "Enough is enough"? They have been waiting 12 months to do something about it. What are they going to do about it?

Mike Glycopantis: Last time, in the negotiations that spanned 2004 to 2005, the Commission's proposal was cut by over 10% by the member states. Formally the two arms of the budgetary authority are the Council and the European Parliament. The European Parliament is very, very close to the Commission's position. The SURE Committee brought out a report, which is extremely close, just before the Commission's proposal, which essentially asked for, in overall terms—

The Chairman: Spend, spend, spend.

Mike Glycopantis: Yes.

The Chairman: Continue, if you have more to say.

Mike Glycopantis: That is all for introduction.

Q4 The Chairman: Then can we hear next from Mr Towler? Mr Towler is going to be afterwards, is he not? You are DCMS.

Simon Towler: I am DCMS.

The Chairman: And you are broadband—Mr Broadband?

Simon Towler: Yes.

The Chairman: We have a lot of firm supporters of broadband: more and more and better and better, and not costing anything.

Simon Towler: I do not have a great deal to add to Mike's introduction. The proposal in the area of telecommunication services—it is not entirely restricted to broadband—is for a fund of €9 billion. In percentage terms, this is just vast, because in contrast with transport and energy, there were no existing projects and proposals.

Q5 The Chairman: You are starting from nowhere.

Simon Towler: Exactly so. We are very broadly supportive of the aims of the Commission: they broadly mirror the policy that we are undertaking in the United Kingdom. We are providing direct support for broadband through a series of programmes in the United Kingdom in areas the market will not serve. We support their broad analysis that there is a gap between the funding that the market will provide and the amount required to provide the level of connectivity and broadband that will meet the European targets, which are broadly good ones. But in common with colleagues—we follow the concerns of the Treasury—and as the explanatory memorandum has said, we are concerned about the overall budgetary discipline and the overall level. There is a point that has been raised with us about the scale: the point here is that you could construct programmes and projects of any size, from a few million euros, to have any sort of scale, up to the number they propose and way beyond. We are at a very early stage there—new programme, new proposals—and we need to see what happens during the Danish presidency.

Q6 The Chairman: Thank you very much. Katrina McLeay, could you give us an opening statement, please? Thank you. You are Department of Energy and Climate Change.

Katrina McLeay: Yes. We will be discussing the energy infrastructure side. Mike has already covered the main position on the budget and its size. That said, from the Government's perspective there is a need to look at increasing expenditure on low carbon, but only within the context of the smaller budget that Mike has outlined as our objective. The Connecting Europe facility offers us a possible way of doing this, but I have to be honest and say we are not entirely comfortable that the amount that has been proposed is the right amount. We want to further interrogate the analysis of the Commission on this. We think the proposal they have made has a lot of merits, but as others have said we are still at a very early stage. It is essential to make sure that any spend in this area does give real EU added value, and we need to look into that more closely.

Q7 The Chairman: Thank you very much. Now finally Miss Cruickshank—I do not know whether you are Miss, Mrs or Ms, but Miss Cruickshank.

Verna Cruickshank: Miss or Ms: it does not matter.

The Chairman: You are Department for Transport.

Verna Cruickshank: That is right, yes. From the transport side, as my colleagues have said, we are at the very early stages of discussions with the Commission and member states on the proposal for transport. In terms of the budget that was proposed, transport was marked as having the largest amount. We could not see any real justification for that in the current climate. In the UK we have had to look at prioritising and making cutbacks on transport, even though it is recognised as something that supports growth. But there are tough decisions by all member states, not just the UK. We were quite comfortable with the position that has been put forward by the Treasury: we have agreed that with both the EAC and the explanatory memoranda that have gone around.

Q8 The Chairman: Thank you very much. Before I ask the questions, or the Committee asks their individual questions, members of the Committee with relevant interests will declare them. The session is on the record; it is being webcast live and will be subsequently accessible via the parliamentary website. The witnesses will receive a transcript of the session to check and correct, and this will be put on the public record in printed form and on the parliamentary website.

Now we start with the questions, and I am asking the first question, which you have notice of. You state that you support the reprioritisation of resources in the next multi-annual financial framework towards engines for growth and job creation, and at the same time note that the infrastructure development needs more focus in order to deliver Europe 2020 goals on smart, sustainable growth. However, you state that you cannot support the expenditure proposed for the Connecting Europe facility. What budgetary provision would you be comfortable with and how would you achieve the same goals with less?

Mike Glycopantis: We are comfortable with the situation where growth-enhancing infrastructure, like Connecting Europe, takes a greater share of the EU budget. We are very comfortable with that position. We are not in a position to say exactly how much we think should go to Connecting Europe, and other member states are in exactly the same position. It is very early in the negotiation. It is also the case that, in order to deliver the overall real freeze in the budget size, we need to be extremely careful in how we negotiate individual elements of the budget. Therefore, we are not advocating increases from the current level provision at the moment, in any area of the budget. If we reach a point much further on in the negotiation where we have achieved a consensus around the overall budget size that we are comfortable with and that meets the Prime Minister's objectives, we can look at the individual elements.

The Chairman: Allocation within it.

Mike Glycopantis: Yes.

Q9 The Chairman: Can I just ask, for the avoidance of doubt, how long are these negotiations going to last? Give us some idea of what we are in for, so to speak. Secondly, you said that the people who are so determined about this are the Commission—and obviously you are negotiating with the Commission—but also the European Parliament. Do you in your position manage to negotiate with the European Parliament?

Mike Glycopantis: The formal process is that the European Council has to reach a conclusion that is then put to the European Parliament for its approval right at the end. In terms of the how long the negotiations will take, there is a lot of uncertainty over that. The reference point is that the next financial framework begins in January 2014. For good process, we would expect an annual budget proposal for the year 2014 to come from the Commission in April 2013. That is the ordinary process that we follow. Last time round the deal was done under the UK presidency in December 2005. The equivalent point in the cycle this time round would be December 2012, which would then allow—

The Chairman: Four months.

Mike Glycopantis: It would allow a few months to then prepare the annual budget. We have the Danish presidency now, and then we have the Cypriot presidency from July to December. We also have a new role now, which is the role of the President of the Council, Herman Van Rompuy, who we expect will take obviously a bigger role than—

The Chairman: A lively interest.

Mike Glycopantis: Yes. I am not saying that the deal will be done in December; I really do not know when the deal will be done, and it is about 27 member states—it is unanimity. But those are the reference points I can give you.

The Chairman: Thank you, Mr Glycopantis. That gives us some sort of framework within which we can act. Now, do any members want to come in on that particular question?

Q10 Lord Clinton-Davis: Does the view that you have additionally expressed go right across the political parties here?

Mike Glycopantis: Yes: the view that we would not be arguing for more than a real increase and that should be the maximum, and ideally we should go below. Yes, that is right.

Lord Clinton-Davis: That is shared by the political parties.

Mike Glycopantis: Yes.

The Chairman: That is a very good question, and thank you for the answer.

Q11 Lord Brooke of Alverthorpe: I was just trying to work out the sequencing of this: so it could be December 2012, do you think, when we are getting towards the end?

The Chairman: Best guess. No, it is the Cypriots.

Mike Glycopantis: It is definitely a European Council negotiation. Last time there was one failed negotiation in June 2005, which would be the equivalent of the coming June, and then the deal was done in December. The Danish presidency is working very intensively: they have not started yet, but they have a very intensive work programme. They will be doing as much as they can to try to narrow the deal down, but they are very open. They feel that they are a little bit stymied by the timing of the French elections. You have two rounds of presidential elections in April and May, and then you have the parliamentary election in June. They feel that makes things extremely difficult.

Lord Brooke of Alverthorpe: And it has to be unanimous.

Mike Glycopantis: It is unanimity, yes.

Lord Brooke of Alverthorpe: So there could be another veto here.

Mike Glycopantis: It is unanimity.

The Chairman: It is a forbidden word—a *verboten* word. But it would not be in the hands of the Danes, would it, to meet the December 2012 date? That would be the Cypriots.

Mike Glycopantis: That is right. The Cypriots will take over in July.

The Chairman: We need to get as much done possible.

Q12 Lord Rowe-Beddoe: Can I just ask a quick supplementary? I am little confused in reading these explanatory memoranda. What sort of period of time are we dealing with here? I see 2030; I see other dates thrown around. I added up the €3 trillion, and I arrived at 2030.

Mike Glycopantis: I am not the expert on that, and Simon has asked me to make another point about the regulation, but my understanding is that, in the transport proposal, they want to complete the Core Network by 2030, and the Comprehensive Network, the more detailed network, by 2050. That is where that distinction comes from.

The Chairman: Thank you. Are there any more supplementaries on that first question?

Q13 Lord Bradshaw: Just to follow this up, if decisions have to be made—and it would seem to me that it is most likely decisions would be made that fewer projects will be, as it were, passported through—is the system of appraisal of those projects one that you are very comfortable with, and would you explain it a little?

Mike Glycopantis: I should probably bring the departments in, but at the moment we have quite a lot of uncertainty about what the first set of projects would be, which makes it a little bit difficult to talk about some of the flexibility issues, which we will come on to. I do not know if the other departments would like to talk about what information we have on appraisal.

Verna Cruickshank: On the transport side, the project list that has been attached to the Connecting Europe facility is just an initial list of projects that member states have put forward. The UK was not able to put much forward because we were not in the right stage of our comprehensive spending review, so we did not have ministerial approval. The criteria and what the project should be, they are both being discussed at the moment, so it is a bit difficult to say right now if they are going to be the right criteria. What we are broadly trying to address is bottlenecks, gaps and cross-border projects, where it is seen that there would be better EU value for them. The criteria should support those very broad aims. That is what it has tried to do in the past and hopefully that is what it will continue to do in the future. That is certainly what we would be looking to make it do. That is in transport.

Q14 Lord Bradshaw: I am certainly very interested to learn that we have not got a firm list of projects that we want to put forward and that such projects are supported by a rigorous analysis, because it seems to me that the way this works is that people put down their favourites without much justification.

Verna Cruickshank: That has been a problem in the past, and that is what they have tried to move away from. In putting a project forward, it is meant to be something that fits the criteria, and the criteria should hopefully come from the EU regulation. It should try to avoid politically supported projects or favourite projects; it should be something that is seen to form part of the new TEN-T Network. The focus, from what the Commission has said, would be on the Core Network. It is, if you like, a subset of the detailed network.

Lord Bradshaw: I would expect that the ones that were most attractive to the United Kingdom were the schemes that promoted growth and jobs, not vanity projects building roads in remote places.

The Chairman: Exactly; we will keep that front of mind.

Q15 Lord Brooke of Alverthorpe: Two of you said that the Prime Minister and other influential leaders are unhappy with the resource of the budget itself, but could you say, in coming now to deal with whatever is the final money that has to be allocated, whether you are content with the rules that have been put in place for the assignment of funding to the individual projects? Are you happy with the mechanism that has been set up for that? Secondly, and to a degree you have been answering this already about the projects, are the guidelines seeking to direct funding to the right projects?

Mike Glycopantis: Shall we start with the Department for Transport?

Verna Cruickshank: I thought you might. Again, there is a difference between where we are and where we are going to. In the past there might have been some projects that possibly were not in a position to go ahead properly, needed a bit more work or were favoured. I am not going to name any; unfortunately I was not around when they were done. But in moving forward it is very much to identify what projects should be on what is called the Core Network, the higher level network, which we are agreeing and discussing the criteria for. Any future projects should be meeting the new criteria, and they should be delivering EU added value. The concerns that are being raised about it should not be about small projects just improving a very remote road somewhere.

Sorry, I am not sure if something is whistling; I am not sure if you can all hear properly.

The Chairman: I think Lord Clinton-Davis has problems with his ears.
Verna Cruickshank: It is trying to identify what the major projects are. That is what the Commission is also trying to do when it calls to look at cross-border projects. Some cross-border ones do not necessarily have to go across just one boarder; it could be going across several if you are looking at road or rail links.

Q16 Lord Bradshaw: Perhaps I might just follow that. When you are appraising projects, are you absolutely certain that money needs spending on concrete and steel, rather than sorting out pettifogging regulations that are restricting flow through the area?

The Chairman: Before you answer that, can we ask if you seen our latest report, *Tunnel Vision? Completing the European Rail Market*, which is about the Channel Tunnel? If you have read it, you will know exactly what Lord Bradshaw is talking about. Pettifogging regulations is really right up there. Can I recommend you to read it?

Verna Cruickshank: I will certainly read it. What I would say is that I take advice from all of my transport policy lead colleagues as well as the Devolved Administrations, because this is obviously a wide-reaching policy; it covers all transport modes and it covers all parts of the UK. I would not confess to be an expert on all of them by any stretch. I would definitely ask all my colleagues. I know whom you would be dealing with when talking about this report, even though I have not seen the report. One thing I would say is not all the money would go into hard infrastructure; some would look at studies as to whether certain projects should go ahead in the first place. What is initially proposed in the Commission's proposal is percentages. It is not paying for the full projects; the percentages differ depending on what you would be doing. Member states or private sector companies would still be expected to put their own money into the work.

The Chairman: That is accepted as a given.

Q17 Lord Plumb: It is a pleasure to note that the Government supports the concept of simplification, and it really follows the theme of some of the things that have already been said in terms of moving forward and using the money available for the best possible purpose. But you argue that Connecting Europe is not the right one, and you say that it risks increasing bureaucracy, and to that extent, therefore, claim that it is unclear. What evidence needs to be clarified, as you see it? What alternative structures would you prefer? You also raise the specific concerns as to how the Cohesion Fund expenditure and the Connecting Europe fund will work together, and it is very much related to the general situation. Do you think that the two regimes will conflict in any detrimental manner?

Mike Glycopantis: We do not have a lot of information at this point about how the central management will work. It is clear that the Commission is asking member states to hand over a great deal of control. Alongside the money, they want more powers over setting regulations and they want to be able to choose projects. Member states would be handing over control over regulations and choice of projects. We need far more information about all of that.

The interaction with the Cohesion Fund is not clear. We have a Cohesion Fund that is shared management, which gives the Commission some responsibilities and gives member states some control, and fixed-country allocations. Obviously the cohesion countries and a lot of the rich member states cherish their fixed allocations. This is a methodology that is much more about bidding for projects. We have this situation where the net contributors are concerned about much more cost and you also have a situation where some of the net recipients are also going to be concerned, because they may be very big supporters of EU value added, but they are also very keen to make sure that they have their own national revenue stream. So it is not a straightforward situation.

Q18 Lord Plumb: Early days, as you said. But you also said you were in regular contact with your colleagues in all the other countries. How do you read them? Would they be generally favouring simplification? Would they generally be favouring the sort of growth rate that we have been talking about?

Mike Glycopantis: Maybe colleagues could answer on the simplification element. In terms of the funding, the other large net contributors whom I talked to who are looking for savings against the Commission's proposal of the order of the savings as I set out earlier are certainly looking at Connecting Europe as an area where essentially the Commission has bid for an extra €30 billion, and there is not a lot of clarity about what it is going to deliver. They are all looking very much at this as a big threat to their budget discipline objectives and therefore an area where they are looking for savings.

Q19 Lord Plumb: Bearing in mind that at the moment we are not the most favoured member of the club, how do you think those countries are going to react?

Mike Glycopantis: I was asked this question at an internal seminar last week: what impact might it have on the budget negotiations? To be honest I do not think there is any impact at all, because people argue their national interests in the budget negotiations—

The Chairman: Throughout?

Mike Glycopantis: Yes.

The Chairman: Of course; quite rightly too.

Lord Bradshaw: That is why the appraisal has to be important, because people have to be using the same facts.

The Chairman: Exactly right. Does anybody else want to come in on Lord Plumb's question?

Q20 Lord Walpole: The Government submitted during the previous Committee inquiry into the multi-annual financial framework that transport infrastructure projects were the highest priority for the TEN-T programmes. I assume this still is the case in a cash point of view, is it? What should the balance be between spending on transport, energy and telecoms? You are concerned by the mechanisms by which the funding should be moved between sectors within the Connecting Europe instrument. What are your specific concerns and how would you prefer to approach shifting funds between sectors? May I just ask you a question that everyone is going to ask you later on? You are not going to be able to answer it, but we would like you to in the long run; perhaps you could write to us. Is the Treaty of Canterbury out of date?

The Chairman: Please; I was going to send—

Lord Walpole: I thought you were going to say that.

The Chairman: I was going to send a copy of our report to Miss Cruickshank and ask her if the Treaty of Canterbury was out of date, but for the moment let us park the Treaty of Canterbury.

Lord Walpole: Let us forget that.

Verna Cruickshank: I will start on this one. First of all, at least I know what the Treaty of Canterbury has to do with Channel Tunnel rail. Again, I would defer to my rail colleagues on that one as to whether it is out of date or not. I believe they have just been to see you recently anyway, so I am sure you have probably asked that question. What did they say?

Lord Walpole: Sorry?

Verna Cruickshank: Did they say it was out of date?

Lord Walpole: The answer is that you will have to read the report.

The Chairman: Miss Cruickshank, you should really just forget what Lord Walpole said. He is a trainspotter. We are all train nerds after being stuck in the Channel Tunnel for about seven months, so as a result everything is clouded. But come on: get up for air and get on with your question.

Lord Walpole: I thought I was getting on with it.

Verna Cruickshank: I will stop stirring things up for you then. As for the balance between the different areas, I did read the report where it says this, and I am not sure where it has come from. We normally look at transport and the projects, and the fact that it does deliver growth. Recently our Secretary of State has announced that money is going to be put into transport. There has been a bit of a shuffling round of funds. We recognise the importance from a UK perspective, but equally I know the Government has strong interests in energy, climate change and innovation, and more broadly in innovation and research. It is something we support in the budget as well. But I feel I am getting into other people's territory on this. As for transport, we think it is important in terms of the TEN-T regulation as well and the wider EU joined-up network. It is important that we can get our business all around Europe.

Simon Towler: Perhaps I may add that it is extremely difficult for individual departments to do anything other than give you a view of the utility or otherwise of proposals in our own areas. There is a certain amount of seeking interdependency between different areas and seeing whether you can make use of different infrastructures, and of course that is something that in telecommunications—the ability to run telecom fibres along network rail infrastructure, and indeed energy infrastructure—is well-known and well documented. What you need to look for in each of the cases, as you said earlier on, is the potential to underpin growth and productivity. There is strong and ever greater emerging evidence that communications infrastructure underpins growth and productivity. The underpinning for our own national, governmental approach is absolutely what we are seeing here mirrored at the European level. It is fairly similar to what other people do. But the difference here is that we have no proposals at all from anywhere to work with, so we have no idea whether 10 pence or €10 billion is the right amount of money until you start to see the proposals coming through.

The Chairman: I think we all accept that, but thank you for the additional clarification. Have you finished, Lord Walpole?

Q21 Lord Walpole: In the energy field—again, if you look up, I asked a question about the Orkneys the other day—I think there is a lot of very cheap energy about the place if we make a big effort. It is mainly in Scotland, I am afraid, but there are things called tides, and they come in other places like Bristol, and that sort of thing. We could get a lot of free energy very cheaply on the whole. Perhaps I am wrong; perhaps it is going to be far too expensive. I am keen on turbines in the sea, in rivers and all that sort of thing.

The Chairman: And broadband.

Lord Walpole: And broadband, of course, yes.

The Chairman: And railways in Norfolk.

Lord Walpole: They will realise I come from Norfolk, which is the most deprived area of the country, with the possible exception of Cornwall.

The Chairman: That is enough. Your question was: what are your specific concerns and how you would prefer to approach shifting funds between sectors? That really is full square at the Treasury. Would you like to piggyback on Lord Walpole's question, please?

Mike Glycopantis: We do not know how the funds would be shifted, but we also do not know the starting point either. If we knew the starting point and had the list of projects, and then we had some clear rules about how funds might be shifted around, depending on the pace at which projects in the different sectors were progressing, we could look at that and reach some kind of assessment. But there is a lot of uncertainty even about the starting point, and therefore we are not in a position to comment on the flexibility. We start in a situation where member states have their national allocations, and we are talking about moving to a situation where essentially the Commission would like free hand to just say, "We are going to take this money from energy and we are going to move it to transport," or "We are going to take it from transport and move it to broadband". We are anxious about that, and the overall affordability situation of the Commission's proposals do not help.

Q22 The Chairman: Yes, but can I also ask you—I do not want to nail you down on this one—what you think the balance of spending should be between transport, energy and telecoms?

Mike Glycopantis: We need to look at the projects. The situation has shifted, because in the current financial framework, which runs to 2013, this is principally a transport instrument. The response that we gave in the past was pretty much a statement of fact. This is principally a transport instrument; now it is being presented as an instrument that is much more about energy and broadband as well.

Q23 The Chairman: Can I just press you a little further? Surely there must be ongoing studies in the Treasury about where the big gaps are in bringing us up to a position where we can get growth going and increase employment. I am not nailing you on this one, but how do you get the feeling that this is something that is probably just a smidgen more important than that?

Mike Glycopantis: We have our national infrastructure plan, but the situation here is that we are talking about where EU value added can really—

The Chairman: Yes, of course.

Mike Glycopantis: It is much more about how you can capture the externalities across borders. Therefore, it is much more difficult to even start with the—

The Chairman: That is a very valid point, thank you.

Lord Bradshaw: You may have to, because you mention the private sector, and they may be interested in one or two things, but basically the infrastructure that will interconnect our energy supplies with those on the continent, and much of the transport infrastructure—I do not know much about broadband—is something that we should have a strategy for dealing with. We should have a reasoned strategy based on strong appraisal methods, so that when the opportunity comes we can put these things forward. I am trying to get the UK ahead of the game, not trailing along behind, moaning.

The Chairman: Exactly.

Verna Cruickshank: I am sure my DECC colleague would be able to say something more on that.

Katrina McLeay: The situation is slightly different on the energy side from the one on the transport side, in that the specific projects themselves are projects of common interest that have not yet been identified, but all the processes that have been proposed build on existing processes and mechanisms by which projects that are of genuine interest and genuine added value can be identified, and can be identified with involvement from national regulators, from TSOs and from member states. Concerns have been expressed about the extent to which the Commission may have control over the decisions that are being made. It is certainly the case that they may have the final say, but they will not have the say up until that point because all of our entities will have been feeding in and will have been part of regional discussions that seek to identify where these kind of projects can best add value to create an integrated energy picture across the regions within Europe. For example, in the case of the North Seas Countries' Offshore Grid Initiative, that is an existing group. I understand that the Commission would look to keep that as an existing regional group to look at offshore renewable energy. All the countries around that group—of which we are a participant—will be looking to identify which are the most suitable projects. Our situation is slightly different.

It is hard for us to assess how much money would be appropriate to fund some of these projects because not all of them require public funding. We fully expect to see the absolute majority funded through the market and we expect that projects that are funded as a result of direct funding from the EU budget would be a very small proportion and meet specific criteria. Given that we are still at a very early stage of negotiations, there is a lot in the way that the proposal is set up that we like and that builds on things that have already gone forward in the third package on having 10-year plans for what energy corridors we should be looking at and so on.

Q24 The Chairman: How confident are you that the Commission, when you give them all the work you are doing at the sub level, will not say, "Go away, because we are already doing such-and-such and such-and-such"?

Katrina McLeay: There are some elements of the proposal that we still need to work through with the Commission, which we covered in a previous question. But we are broadly happy that the balance is right, given that right up to that very final choice our own entities will have been involved, and obviously our colleagues are also speaking with the devolved Administrations as well to make sure that there are not any—

The Chairman: It is in all our interests that you maintain that momentum and just insist. Too often a lot of work is done and then it is just said "Cheerio" to.

Katrina McLeay: Yes, and we recognise that there is this risk, but at the same time there could potentially be advantages to having somebody take an overall view to make sure that people are not independently doing things—provided that they are projects that we have had an input into.

The Chairman: Yes, exactly. And provided that you are confident that they are competent.

Katrina McLeay: Yes.

Q25 Lord Clinton-Davis: In your paper you are seriously concerned about the level of prescription involved in the idea of Core Corridors. On the other hand, some parliaments see that as inevitable; it is a method of overriding national competence in project planning. How do you reconcile those two points of view? Do you anticipate that corridors would work? How would they work in practice? The Commission claims that there is a great deal of insufficient co-operation by member states as far as this is concerned. How do you see that?

Verna Cruickshank: The first thing we need to say about the Core Corridors at the moment is it is something the Commission introduced quite late on in developing the guidelines that finally got published. There has not been much of an opportunity to discuss them or the thinking behind them. We are currently seeking to get clarity from the Commission as to what it is looking to do with them and what criteria they look to apply. From what we have seen in the regulation, they are proposing a lot more monitoring and reporting. The impression we have is that they would be taking control of what projects member states should be bringing forward on a transport basis and deciding where the money should be spent—not just EU money, but also UK money—because members states put a lot of money into all the projects going forward. If you are successful in a bid to get EU money it is a percentage, and it has been quite a small percentage. It is good to have, but we would not want to see additional bureaucracy or financial burdens put on the member states. It would be wider than the member states. Because it is a regulation, it applies to the private sector as well. At the moment we are trying to clarify what they mean by Core Corridors, what they mean by the corridors in which they put the UK and what they are seen to achieve there. What we have been told is that the corridors should try to address the bottlenecks, the gaps and the cross-border projects. We are not clear where that is meant to lie on the corridors that they have put forward for us. First and foremost we need to get more information from them.

Q26 Lord Clinton-Davis: From your discussions so far, is there any light at the end of the tunnel?

Verna Cruickshank: I hope so. The Commission has obviously set out what its ambition is and what it would like to see. We would not be very good negotiators if we came out with what we would be prepared to accept. There is a long way to go yet. In terms of times, we have tried to get a feel from other member states—do they think this is something we could be looking for a quick decision on? We know the Polish presidency had TEN-T as one of the top priorities and has held a lot of work groups on it. We understand that Denmark's presidency is very keen on it as well, and sees it as one of its priorities. It is certainly going to get a lot of discussion, but at the moment there are such different views and concerns from member states on the financial side of things, on the projects, on the criteria, that at the moment it is very much, "What is written and what does it mean, and are we talking about something prescriptive or a framework?" A lot of people are much more comfortable when we talk about frameworks rather than set timescales and standards.

Q27 Lord Clinton-Davis: Is there any similarity between the views expressed by Her Majesty's Government and other states?

Verna Cruickshank: Yes. We are not isolated on this.

The Chairman: You do not have to tell us who.

Verna Cruickshank: Some view the standards as very ambitious. There are some things that some member states might like to see, but at the back of a lot of member states' minds is the fact that these standards bring costs with them, and the costs are not funded by the EU budget. They are funded by member states or the private sector. First and foremost we need to understand what they are trying to achieve and see what things are already being done. We are already implementing some things, but maybe at a slower timescale on the rail side. We are looking to bring in some of the proposals they have made, but alongside signal and equipment replacement. If 2030 is a bit ahead of that, we would like it to slow down a bit.

Lord Bradshaw: I just wish to agree with the last sentence.

The Chairman: Quite. Pushing at an open door.

Q28 Lord James of Blackheath: In your impact assessment you express quite strong anxieties about the resource implications resulting from any mandating of the Core and Comprehensive Network infrastructures. Are these concerns of yours based on an inherent opposition to the idea of the mandating of standards, or are you concerned simply with the scope and scale of the proposal as drafted?

Verna Cruickshank: With some of it, it is the scope and scale. Some of the proposals are already being discussed in other transport forums. We do not want to duplicate discussions that are already happening or decisions that have been taken only fairly recently and work is under way to implement them. For example, there are discussions on the railway side. We do not want to see the same proposals discussed at the same time as they are being discussed somewhere else. It does not seem to be a good use of time. We would like to see a reference to the other expert working groups in the TEN-T regulation. There are some suggestions that are going forward to say that we agree and we support; it is just that the timing of them is different from the timing where we would do it. We want to make best use of the assets we have just built, developed and are rolling out. We do not want abortive costs. I could say more about some of the standards, but I think you get the idea.

The Chairman: I think we have the idea, yes, absolutely.

Q29 Lord James of Blackheath: What avenues are you able to advance those anxieties through, and what positive benefits might you get?

Verna Cruickshank: The UK is definitely not isolated. A lot of other member states are very supportive of that view if there are other working groups. One example was on something called ITS—intelligent transport systems—for roads. The proposals for taking it forward are supported, but it was agreed by all member states that it should not be mandatory. It was something that the Polish chair spoke about in one of our working groups. She had been part of the working group that had looked at it and did not want it to suddenly becoming mandated under TEN-T when that is not what member states had supported. Working with member states continuously on the whole regulation to make sure that we are not isolated, we obviously build our relationships with the countries that share similar views, and we work with the Commission and the presidency. It is not at a position where we do not talk to anybody. We will engage, and we are seeing the Commission tomorrow again to get some clarification and to see where there are areas of compromise.

Q30 The Chairman: Well done and good luck. Can I just ask a simple question: have we got to learn another acronym? ITS, or intelligent transport systems—what on earth does it mean?

Verna Cruickshank: Broadly it is the technology systems that come in—

The Chairman: Electronics and things?

Verna Cruickshank: Yes. There are different ones for different modes. ITS tends to be the road one. There is one for shipping, there are different ones for—

The Chairman: I am very sorry that I have asked.

Lord Bradshaw: Very simply it is things like road price.

Verna Cruickshank: I would have said it is more the information systems.

The Chairman: It is computers—iPads on lorries or something. I am really sorry that I asked that question, because I have taken time away from Lord Rowe-Beddoe.
Q31 Lord Rowe-Beddoe: Underlying all the guidelines of TEN-T are the two elephants in the room, as it were—subsidiarity and proportionality. What do we think about that? Are we concerned and, if we are, what are we going to do about it?

Verna Cruickshank: It is the Core Corridors and the governance associated with it that we have most concerns about. From what the Commission has said, it seems to be proposing a lot more by way of reporting and monitoring structures being set up. That is something about which we are definitely asking a lot of question—I say "we", but other members states as well—to understand what it is and what are the benefits and the risks. We understand the Commission has had problems in the past where there have been cross-border projects and where maybe one member state has delivered and another has not. But we do not necessarily think that means that you need to have it for all the Core Corridors. It is getting a better idea of what they are trying to achieve here, but what we said in our last reply when the Commission did their consultation was that ultimately we thought it should be member states that should retain the final decision on what transport planning happens on the networks and when it happens on the networks.

Lord Rowe-Beddoe: Yes. And do you think that will occur at the end?

Verna Cruickshank: That is my aim.

Lord Rowe-Beddoe: Well, I wish you well in your aim, because it is clearly a fundamental problem in both those issues.

The Chairman: Does anybody else want to ask a supplementary on that? Now you will be glad to know you are let off the hook for a moment or two. Thank you very much indeed, you have been most helpful; you have all been most helpful. Right, it is now the turn of energy.

Q32 Lord James of Blackheath: Permit granting is set out to be rather prescriptive. If the regulatory system that you are calling for is taken into account, would you support that element of the proposal, or would you want to see it changed?

Katrina McLeay: As we have said, we are still in quite an early stage of the negotiations, so we are still finalising positions. But the UK so far is one of the only member states that has made constructive drafting suggestions to the Commission, and some of this has been around the pragmatic flexibilities to ensure that the regulation does work for the UK, and that it does recognise the high standards that we already have. We would like to see permitting processes improved. We do think that the complications that can occur in cross-border projects on energy infrastructure with permitting can be detrimental to attracting investment, but obviously we want to have the flexibility to protect our own national interests on that, and those of the devolved Administrations as well. We are still working through some of those proposals, is the short answer. In principle, yes, it is a good idea, but only as long as it takes account of our national circumstances.

Q33 The Chairman: There is quite a pragmatic feeling going through all of this evidence today. We seem to be looking at the efficiency side and then thinking what is possible and whether we can achieve it.

Katrina McLeay: On the energy side there is quite a lot that we like, where we see that this proposal can add value at the European level, not necessarily just in terms of the financing but in terms of dealing with some of the regulatory and permitting issues that are currently a block to the market investment that we would prefer to see. We are in a position of being able to welcome it cautiously and then work through a lot of these details to make sure that we retain the right flexibilities to protect the very good standards we already have.

The Chairman: That is excellent, thank you. Lord James, are you satisfied with that?

Lord James of Blackheath: Yes.

Q34 Lord Ryder of Wensum: Thank you all very much indeed for coming. It is very reassuring to find so many people of sanity in the midst of this Orwellian nightmare—

The Chairman: Exactly, and feet on the ground.

Lord Ryder of Wensum: I am sure that your knowledge of Pliny—indeed, both Plinys—will come in very valuable in the next few months. The Commission, rather characteristically, has presented us with an overcomplicated, rather unrealistic methodology for cost and benefits. I wonder whether you could tell us if this is likely to bear fruit, as far as we are concerned, in terms of the results that we are likely to get from the negotiations and outcome.

Katrina McLeay: Again, I am afraid that this is a slightly similar answer to the one I have already given. The working group on this has only met twice so far. We are still at an early stage, and my colleagues rightly would not necessarily put all our negotiating strategy in the public domain. Again, it is an issue of, yes, this is something that needs to be addressed, for the reasons I have explained in relation to permitting, but we need to make sure it allows our national regulatory authorities the right flexibility to behave as they currently are doing. I am afraid that is as much as I can say at this stage.

Lord Ryder of Wensum: I fully understand, thank you.

Katrina McLeay: I take a stoic position on it.

Q35 Lord Bradshaw: I will have one go again at this, although not to the representative of the Department for Transport. It is about the complex methodology for cost and benefit allocation. As far as I know the cost-benefit allocations are mostly done on the values of time. They are also done on the adding together or aggregation of very small values of time, which themselves are not economically productive, but it is the method that is used. I hope that you think in terms of projects that add real value to the economy, not ones that save very small amounts of time and add them together. If somebody gets home 30 seconds earlier and puts their slippers on, I cannot see what economic value it has. But if you can enable a business to do better, that is much more important.

The Chairman: You have set our imaginations going now, Lord Bradshaw.

Lord Bradshaw: You could have a glass of sherry.

The Chairman: Exactly. I was just thinking that it depends where the bottle is.

Katrina McLeay: Perhaps on the energy side, the cost-benefit analysis takes account of slightly different elements.

Lord Bradshaw: It is a different way of thinking.

The Chairman: Provided he does not put on his electric fire.

Katrina McLeay: Yes, which is being adequately distributed through the new smart grids—intermittent, new renewable sources.

Lord Bradshaw: I support that.

The Chairman: In the season we are in, we could do quite a pantomime about all of this, but no.

Q36 Lord Plumb: Supporting what Lord Bradshaw has just said, there must be an awful lot of projects in the pipeline. We have so many different systems of producing energy from all sorts of sources. Wave power has been mentioned as one of the best. I think it is one of the worse, but that is a matter of opinion.

Katrina McLeay: I take a technology-neutral approach.

Lord Plumb: A lot of them are held up because of planning and all these applications are in. I have some experience of this over the last three years: it has taken over three years to get one particular system through, which is absolutely ridiculous. How do we compare with other countries at the moment for projects coming in, knowing of course that Germany is way at the top?

Katrina McLeay: As far as I am aware of the list of projects, we are not in a comparable position to that of transport. If this regulation is agreed, subject to the negotiating amendments that we might seek, we would be in a position to start looking at specific projects. The Commission has identified priority energy corridors—the North Sea offshore renewables grid is one of those areas—and smart grids, which would allow us to control these new renewable sources better. Then there are ones designed to enhance energy security and to eliminate energy islands within Europe. But until the regional groupings get together and start discussing what their specific priorities are, which is one of the strengths of the way the energy side has done it, we will not have a list of the specific projects, but the member states are all represented in those groups. We will be responsible for identifying in our region which energy projects we think are the most beneficial to enhancing the region's energy security and meeting its low-carbon objectives.

Lord Plumb: I would like the list as soon as we can get it. I understand, of course, that it will take a long time to get those through, but as and when if you could note—

Katrina McLeay: It may be some time, but yes.

Lord Plumb: We would like to know the difference between countries; it would be helpful.

The Chairman: Absolutely, it is a very good point, Lord Plumb.

Q37 Baroness Valentine: The proposals lay down extensive powers for the Commission to launch calls for tenders on delayed projects, to offer the option for other promoters to invest in projects and to appoint European co-ordinators in case of delays. Are these proposals acceptable? Do they, in your view, respect the principles of subsidiarity or proportionality?

Katrina McLeay: I mentioned in one of my earlier answers that there was one outstanding issue in terms of where we needed to get a much clearer idea of what exactly has been proposed. It is obviously necessary to consider very carefully any possible extension of EU competence, and particularly where it is relating to some of these more prescriptive parts of the regulation. We are still seeking some clarification from the Commission on this, because we need to understand better what exactly is meant by the proposal before we can go to Ministers and explain what is being required of them. In terms of the role of the EU co-ordinator, that is slightly different in that it already exists under the TEN-T guidelines and they have proved to be effective.

The Chairman: Really?

Katrina McLeay: Yes. We would welcome them, but provided that the process for their selection is transparent and that there is scope for member state input into that and involvement in the selection, because obviously we want to have a say on who has been chosen. So far they have proved to be beneficial in terms of creating momentum and driving things forward.

The Chairman: Thank you very much indeed. I think, Committee, we have been very honoured to have such a great team to be witnesses, and it has been a terrific session, so thank you. It has restored a lot of my faith in things that were getting slightly wobbly. Before you go, are there any questions that you think we should have asked but did not, and if you have any further thoughts about clarifying our minds, do you think, if you could, would you write to us, and probably to Mark Davies, as that would be very helpful? Finally, thank you, each one of you, for an excellent session, and may I wish you, on behalf of the whole Committee, a very happy, relaxed, fun and blessed Christmas, and a healthy and prosperous 2012. Thank you.

HM Treasury – Oral evidence (QQ 66-105)

Evidence Session No. 4. *Heard in Public.* *Questions 66 - 105*

TUESDAY 6 MARCH 2012

Members present

Lord Harrison (Chairman)
Lord Bowness
Lord Dear
Lord Dykes
Lord Foulkes of Cumnock
Lord Hannay of Chiswick
Lord Jopling
Baroness Howarth of Breckland
Lord Maclennan of Rogart
Lord Plumb
Lord Richard
Lord Roper
Earl of Sandwich
Lord Teverson
Lord Tomlinson
Lord Trimble
Baroness Young of Hornsey

Examination of Witnesses

Mike Glycopantis, Deputy Director, International and European Group, HM Treasury; **Alex Skinner**, Head of European Union Institutions and Policy Team, HM Treasury; and **Brendan Bayley**, Head of Agriculture and Regional Policy Branch of EUIP Team, HM Treasury.

Q66 The Chairman: Colleagues, welcome from the Treasury. Mike Glycopantis, perhaps you would be kind enough to introduce your colleagues at an appropriate stage, but I think you will be aware that we are replete with votes. We have had a taster of a vote before we started this session, and there will be others at various interludes, but we are very grateful for you coming. We will be making a transcript of this session and we will send it on. It will get published in the usual way, uncorrected, but if you could correct it or, indeed, if you need to correct yourselves or supply further information which would be useful to the Select Committee, I would be most grateful. Unless you wanted to make an opening statement—did you want to do that?

Mike Glycopantis: A very short opening statement, if that is okay, and to introduce my colleagues. First, the Financial Secretary sends his apologies. He is engaged in the debate. As you know, he wrote with evidence—

Baroness Howarth of Breckland: Chairman, before we move forward—

The Chairman: Yes, I do not know whether you are obscured by the mic there, but if you could speak up it would be very helpful.

Mike Glycopantis: The Financial Secretary is very sorry that he could not be here today. He is engaged in another debate. He wrote with written evidence last week, as you are all aware, so I am joined by Alex Skinner, who is head of EU institutions and policy and an expert on EU growth—he was also involved with structural funds in the previous negotiation on the financial framework seven years ago—and by Brendan Bayley, who is our expert on the common agricultural policy.

I have a very brief opening statement. As you know, the Government's view is that the next multiannual financial framework must reflect the consolidation efforts being made by the member states to bring deficit and debt on to a more sustainable path. The Prime Minister and key allies have set out a real freeze in payments as the path that should be followed, as a maximum, and therefore the Government do not support the European Commission's proposal, which we see as being far above a real freeze. It also includes €18 billion of new off-budget items, which I know that the Committee has picked up on. The Government also believe very strongly that the proposals on the financing side are not acceptable, because they disadvantage the UK. We also believe that they are an unnecessary distraction to the debate at the moment over on the spending side, so the focus should be on making real reform underneath the ceiling of the real freeze. I think that is enough.

Q67 The Chairman: Thanks very much. Let me start by asking this: the Commission has argued that setting out the MFF in terms of commitment appropriations offers certainty to end-users of the EU funds and programmes. Does an MFF negotiated in this way indeed offer advantages for beneficiaries, in your view? Or would an MFF negotiated in terms of payments, using the 2011 figures, be too restrictive or a better basis for the approach and the benefit of everyone involved?

Mike Glycopantis: The Government believe that payments are a better way to manage the budget. We believe that the negotiations should be conducted in payments as well as commitments, with an emphasis on payments. The letter that the Prime Minister wrote in December 2010 gave payments a primacy over commitments in controlling the budget. We believe that the system of commitments has created some problems. At the moment, we have a very big build-up of unspent commitments, which is creating a huge overhang on the budget and lots of uncertainty both for net contributors and for net recipients. We believe that this system of commitments has actually created uncertainty for everybody in the system.
We believe that thinking in terms of payments can give just as much certainty to recipients. The key point here is that the UK budget is negotiated in cash payments, and that provides certainty to recipients in the UK. We understand why commitments were introduced, but we think that the time is right to focus absolutely on payments—and we believe that payments can provide recipients with the certainty that they require.

Q68 The Chairman: But does the UK have any support for that view?

Mike Glycopantis: Some key member states, mainly on the contributor side, are really focused on the issue of payments because they have targets to meet on their deficit reduction plans and they have to control spending, and therefore have to control payments. There are member states out there who are traditionally big supporters of the budget, like France, who are very focused on controlling payments and their contributions. It is absolutely explicit in, for example, France's response to the Commission's proposal that the proposal is far too high and that the French objective for the negotiations is to stabilise their contributions.

Q69 The Chairman: But is there a sufficient number of those who would perhaps like to change the basis?

Mike Glycopantis: There are the four other member states who signed the Prime Minister's letter which gave payments primacy: France, Germany, the Netherlands and Finland. The other budget disciplinarians such as Austria, Sweden and Denmark are very sympathetic to controlling payments as well.

The Chairman: Good. I think other colleagues will come in, if they might. Lord Hannay?

Q70 Lord Hannay of Chiswick: Yes, if I could follow up on this point, which you alluded to yourself when you talked about a "real freeze". Does a "real freeze" mean a real-terms freeze, or what on earth does it mean if it does not mean that? If it means a real-terms freeze, why do we not say so? In fact, in the Financial Secretary's letter, I think three different formulations were used at different points in the answers and it is all rather confusing. I assume that the line that the French, the Germans and others signed up to was a real-terms freeze. If that is so, would you not think it was better to use that phrase rather than a rather misleading phrase, where nobody knows what it means? A "real freeze" could be interpreted as meaning a nominal-terms freeze.

Mike Glycopantis: For the sake of clarity today, we mean that the budget should rise by no more than inflation, year-on-year.

Q71 Lord Hannay of Chiswick: You would agree that that is correctly, in Treasury-speak, a real-terms freeze?

Mike Glycopantis: Yes.
Q72 Lord Hannay of Chiswick: Right. So the phrase "real freeze" in these answers from the Financial Secretary means a real-terms freeze.

Mike Glycopantis: Precisely.

Lord Hannay of Chiswick: I see. Thank you. Well, that is very helpful.
Q73 Lord Trimble: The Commission has told us that the MFF structure is ill-suited to more flexible funds, such as the European Globalisation Fund, and that including projects such as ITER within the MFF could prejudice the funding of other projects, such as university research labs. How could the MFF be adapted to remedy these problems, so that all funds are kept "on-budget"?

Mike Glycopantis: First, the Government are very concerned by the lack of transparency in the Commission proposal and the very substantial increase in expenditure that has been taken off budget. The UK wants to see all these items taken back on to the budget, to ensure proper clarity and sound financial management. It is absolutely the case that the member states would still foot the bill; whether these items are off-budget or on-budget, we would still foot the bill. We do not believe that there is a particular risk to projects such as ITER, if they are on-budget and managed effectively, and we believe that keeping them on-budget will promote the kind of sound financial management that we want from the Commission to manage the whole budget effectively. There are underspends in areas every year, and which are available. There is a degree of flexibility in the budget and there are some instruments available. We believe that taking something such as ITER, which has overspent very significantly, and putting it off-budget would just be an easy way out and one that member states would end up footing the bill for, so we are not at all in favour.

Q74 Lord Trimble: So you see the benefits of keeping spending on-budget as clarity and greater financial discipline?

Mike Glycopantis: Yes. That discipline would be lost if you took ITER off-budget, and said, "Well, the member states will just pay for any overspends".

Q75 The Chairman: Do you have a view on flexibility in intra-budget headings and inter-budget headings?

Mike Glycopantis: If we can achieve the real-terms freeze that the Prime Minister has set out, we will look kindly on ideas to improve flexibility within the budget. What we cannot do is to have a situation where you have lots of flexibility instruments that can be added on to each other, and can increase the overall size of the budget. But if we are confident that the overall budget ceiling is protected, we can certainly look at elements of flexibility.

Q76 Lord Tomlinson: When you talk about areas of flexibility, it all sounds very seductive and then you give an answer which is much less clear. What about flexibility within an area of the budget where you increase one line of expenditure at the expense of another? At the moment, the sort of Treasury mantra that has been issued to all departments is seeming to us to wind up as a budget which is going to be treated on every budget line identically. That means the most conservative budget that we will ever create, with no capacity for changing it.

Mike Glycopantis: Actually, we have some ideas around policy flexibility which Brendan was about to introduce—

Lord Tomlinson: Perhaps you would share them with us, because we do not see them at the moment.

Brendan Bayley: So, for example, in the draft regulation for direct payments under the CAP it is envisaged that there would be flexibility to transfer, at member-state discretion, funds from Pillar 1 into Pillar 2 of the CAP. That is a very good idea; in fact we think that the percentage, which currently stands at 10% in the draft regulation, should go higher. That would be an example of member state flexibility which would be a very good thing.

Lord Tomlinson: Having seen the "Panorama" programme last night, I would have hoped that the idea of flexibility went a damn sight further than that, but that is another question.

The Chairman: Lord Hannay, do you want to pursue another point.

Q77 Lord Hannay of Chiswick: Yes, could I just ask you: has any consideration been given by the Government to the possible advantages, if this negotiation gets very stuck—as it probably will—to a settlement that will cover only five years, not seven? It seems to me, at any rate, that a seven-year period, given the present state of affairs, is a pretty ambitious thing to suggest.

Mike Glycopantis: Yes. The Lisbon treaty talks about a financial framework of a minimum of five years, so everybody has always contemplated five years as being a sensible length. We can see some attractions to five years: we live in uncertain times, and the idea of setting out commitments to 2020 in this period of uncertainty is something that makes you pause. We have been fairly relaxed about a shorter financial framework. The consensus around the Council is that people would generally prefer seven years, so we have said that we will have the seven-year deal as long as we can have a budget discipline deal. But if things moved towards a five-year deal, we would be relaxed about that.

Lord Hannay of Chiswick: Thank you.

The Chairman: Mike, perhaps I could encourage you just to speak up a little bit.

Q78 Lord Richard: I would like to quote this to you, and then put a question at the end of it. When he gave evidence to our Sub-Committee on Economic and Financial Affairs, Professor Bachtler said, "There is a strong case for greater focus". I am sure we all agree with that. He said, "As far as Europe 2020 is concerned, it is undeniable"—a strong word—"that there is a tension between the Commission's proposals for cohesion policy to be a delivery agent, or arm, of Europe 2020 and the traditional mission of the policy of reducing regional disparities". If that is correct, and I am bound to say that looking at the document it seems as if it is, and since the Commission has told us that more than 80% of the proposed MFF targets Europe 2020 objectives, do the Government support the Commission in their efforts to tailor the MFF to the Europe 2020 strategy? What about the tension that Professor Bachtler sees, and how do you fit that into it?

Mike Glycopantis: I will defer to Alex Skinner on structural funds.

Alex Skinner: Thank you very much, and it is a pleasure to be here today. If I can answer your latter question first, I will then come back to the structural funds question. The Government recognise that the crisis has affected all member states, and that there are two very important elements to any solution: one around fiscal consolidation and the other around growth. The Government are also clear that growth comes across the whole range of policy action taken at EU level, so that can include regulation, the single market or trade, and spending items as well. As you mentioned, I think that the Government welcome the fact that the Commission is focusing the budget on growth and employment, which are very important. However, the Europe 2020 strategy itself encompasses seven broad areas, and sitting underneath that are something like 500 different actions. The Government would welcome a greater focus and prioritisation by the Commission, because while many of those actions are worth-while, it is clear that some will have a greater—and quicker—impact on growth than others.

Q79 Lord Richard: So the answer to the simple question "Do the Government support the Commission's efforts to tailor the MFF to the Europe 2020 strategy?" is yes, the Government do support that.

Alex Skinner: To the extent that Europe 2020 has an impact on jobs and growth, that is absolutely right. My only reservation is that it encompasses a lot of other areas as well, some of which have much less impact on this.

Q80 Lord Richard: I do not want to leave the structural funds, because they are terribly important. Again, it seems that we really have a conflict here: that countries or the Commission may want to prioritise spending in certain areas, which are not necessarily the same areas that regional funds and the social cohesion fund would actually like to get their money put into. There is a conflict there too, is there not?

Alex Skinner: To some extent, the Commission has thought about the conflict. When they have looked at the design and regulations for the structural funds this time round they have attempted to give member states flexibility, such that they can pursue those areas which are most important for growth in their domestic circumstances.

Q81 Lord Richard: Is that a good thing?

Alex Skinner: Yes. We are supportive of the idea of member states having more flexibility to tailor their structural fund expenditure in support of growth and employment, so in our response to the cohesion report the Government made that very clear.

Q82 Lord Richard: Can I give you one more quote from Professor Bachtler? Then I will shut up. He also said: "In particular, some member states, which are in receipt of significantly less funding, may decide to sectoralise the way that that funding is spent. In other words, increased funding may be allocated to sectoral or thematic programmes that are very good at delivering the Europe 2020 objectives and which can ensure that results are achieved and that they are visible. The problem is that that way of spending the money may not be in the best interests of the broader regional development objectives within a country in terms of development needs and challenges". Do you accept that dichotomy?

Alex Skinner: There is an element of truth in that. You have a series of programmes which are essentially within heading 1a, where the way that those are allocated allows you less flexibility. Then you have the structural funds which are under heading 1b, where there is considerably more flexibility. I could see a tension where a particular member state may feel that a centralised spending item under heading 1a may not be perfectly suited to their circumstances. However, we have been very clear. In the negotiations in Brussels, we are pressing very hard for member states to have flexibility—constrained flexibility—in order to be able to focus on those areas that are most important for growth, but we are clear that structural funds should be in support of growth and employment. We are trying to limit countries going beyond that and spending in other areas, because we think the primary focus should be on growth and employment.

Q83 The Chairman: But does the traditional mission of the cohesion policy, of reducing regional disparities, get threatened or overturned by the focus on Europe 2020?

Alex Skinner: I do not think it does. The treaty obligation is to reduce disparities between the least favoured parts of the European Union. To the extent that you can promote growth, that should be supported, and the opportunities for promoting growth are greatest in the least developed regions. What I could not answer for you is exactly how quickly we will reduce that disparity, because if all regions took maximum opportunity, not just with European spending but with their domestic expenditure and opportunities, I could not tell you exactly how quickly they would all grow. However, certainly at a European level, more funds—and indeed, we want more funds to be focused on the poorest, as those are the areas where there is the greatest scope for catching up—would lead you to see a reduction in the disparities.

Q84 Lord Plumb: You will be aware that the agriculture committee produced an excellent report. I am not on the agriculture committee, but nevertheless I speak from that report to a large extent. The report was on the reform of the CAP as a whole, but much of the comment in it was obviously related to the budget. Are you satisfied or confident that the Government's wish to substantially cut spending on the CAP can be achieved and if so, how—recognising, of course, that many other countries may not see it in the same way? There is another part to that, which is continually raised, on whether you see any future in co-financing at national level and not just relying on one budget.

The Chairman: Who is going to take that?

Brendan Bayley: I will if I may, my Lord, thank you very much. I think it is helpful to set the context again by recognising that the key priority, as Mike Glycopantis has emphasised already, is ensuring that the overall EU budget does not grow. Clearly, there is a range of ways of doing that. Our view is very much that the best way is to focus on those areas of the budget where value for money is demonstrably lowest, and that would be on the CAP. That would seem a very logical approach to us. Now, how realistic is it? We are realistic about the power of the agricultural lobby across the EU but, at the same time, given the constraints on budget size other member states will increasingly focus on how far they want to see their receipts coming through as structural funds, say, or as CAP. There is a choice to be made.

On top of that, the case for reform of the CAP is not just about fiscal arguments. I think that the agricultural policy case for reform of the CAP is very strong, and the agricultural policy and fiscal policy cases are mutually reinforcing. As the proposals stand, there is indeed a risk that we will see just over €280 billion spent over seven years on measures which, if anything, will undermine the competitiveness of European agriculture. In the context of budgetary restraint, that feels like a big lost opportunity. We are hopeful that we can secure very substantial cuts to the CAP but, as Lord Plumb has recognised, there is clearly a very complicated political dynamic.

In respect of co-financing, I must be honest: I have not heard too much debate recently about the possibility of co-financing of Pillar 1, which I assume is what you were alluding to.

Lord Plumb: Absolutely.

Brendan Bayley: The difficulty there is the uncertain interaction with overall EU budget size. For example, if you have a situation where, for argument's sake, you introduce €20 billion a year of national co-financing, if the overall EU budget were to fall by €20 billion and you introduce that co-financing, that would give you one fiscal outcome. But if you introduced that national co-financing element and the budget did not fall by the related amount, what would have happened is that you would have had an expansion in public spending at the behest of the EU budget. Personally, I find it difficult to see that Pillar 1 co-financing will come on to the table, because of those uncertainties. It is also the case that the newer member states are very suspicious of suggestions around national contributions to agricultural subsidy, because they feel that their budgets will not be able to compete with the budgets of certain other member states on that. That is not to say it is necessarily a bad idea, but there are those complications.

Q85 Lord Maclennan of Rogart: I wonder if you, Mr Bayley, could expand a little on what you said about value for money from CAP funding. Have the Government given any indication of what are the possible comparators vis-à-vis other objects of funding—innovation, employment, regional policy, structural policy or whatever—and how is this statement made? Secondly, if I may ask another question, what sort of timeframe do you have in mind for achieving the Government's financial goals in respect of making savings on CAP funding?

Brendan Bayley: On the value-for-money question, we understand what the origins are of direct payments, which are the bulk of Pillar 1. They were compensation for past reforms of market price support that stretch back to the early 1990s, so we know where those payments come from. Over time, the case for compensation has fallen away and the question has then been: what are these payments for? I must confess that we take every opportunity to ask in European fora, "What is the purpose of these direct payments? What are their objectives?" I am not sure we have ever had a particularly satisfactory response. Some people feel that they are income support; some feel that they are environmental. Other arguments are also made, but once you dig a little deeper one can critique those arguments.

Q86 Lord Maclennan of Rogart: I am sorry to interrupt, but you said that it was the Government's view and now you are talking about asking questions of others. Do the Government have a spelled-out position on value for money, and what are the particular comparators that they make with other programmes? Would our position not be a great deal stronger in arguing these cases if we were more explicit and clear about what is behind our generality of argument?

Brendan Bayley: The Government have put material into the public domain. For example, just thinking back, there was the UK response to the Commission consultation on the CAP communication. The UK Government put in a response there; I could not quote it chapter and verse, but I am confident that in it the point was made about the value for money of Pillar 1.

Just to finish the point, the problem with the subsidies is that they undermine processes whereby European agriculture could become more efficient. On top of that, you have market price support which distorts prices in a static sense, so we are confident in an absolute sense that the value for money is very poor. There are questions to be asked about all parts of the EU budget but the possibility of investment in infrastructure, for example, in contributing to growth and having positive value for money, is much greater than on these Pillar 1 subsidies.

The Chairman: Your replies have engendered a number of subsequent questions. Let us have Lord Sandwich followed by Lord Hannay, then Lord Tomlinson and Lord Dykes—and please keep them quite short, because I want to get on to Lady Howarth.

Q87 Earl of Sandwich: We are in danger of getting into a big debate here. I declare an interest in coming from the West Country, and I can say that the Government ought to consult some of the marginal farmers. They may be historic payments and we can call them environmental or direct payments, but whatever we call them they are very serious in terms of those households. My question is more to do with the Government's attitude to the Pillar 1/Pillar 2 swap, which you mentioned earlier. What do you feel is up-and-coming if we use the words greening or environmental? How is it impacting on your world at the moment in forecasting?

Brendan Bayley: On greening, the Government are very clear that they support the idea that the CAP should have a much more positive environmental impact. The question is then: how does one go about achieving that? Again, the Government are very clear that Pillar 2 of the CAP is the appropriate route. The concern about the so-called greening of Pillar 1 is that if one is looking at efficient policy instruments for getting environmental outcomes, they tend to be targeted. For example, agri-environment schemes will be relatively targeted at what they are trying to achieve. If you look at the proposals under Pillar 1 in respect of greening, they are very general and not targeted. The concern is that it will make the administration of the payments much more complicated, both from the farmers' perspective and the Government's, without achieving any particular environmental improvement. Indeed, the suspicion is that this is about making Pillar 1 direct payments more acceptable to the European population, as much as about any environmental objectives.

Q88 Lord Hannay of Chiswick: I was a little disappointed by your lack of enthusiasm for co-financing, because it seems to me that we ought to plug away at this in the longer term if we are to try and get the CAP under continuing control. Have you given any thought to making it easier for the new member states to accept by modulating the degree of co-financing in proportion to their GNP per capita, so that the more prosperous countries would have to pay a higher degree of co-financing on their national budgets, and the less prosperous would pay a lower level on theirs? Would it not be sensible to at least keep this idea in play for a certain time? Your reservations about the effect on the overall fiscal stance of member states seem slightly odd, since presumably the countries in the eurozone will have that on their minds anyway without you reminding them of it.

Brendan Bayley: I agree with you that one can have differential rates of co-financing. I guess it comes back to prioritisation and taking a view as to what the key priority is. If it is to bring the overall level of spending through Pillar 1 down, the question would be whether a debate about co-financing would necessarily reinforce that or whether it might serve as a distraction to it. I perfectly recognise that there is a debate to be had about that, but the feeling is probably that it might well be a distraction, and that we need to focus on getting overall national envelopes under Pillar 1 down rather than redistributing the burden.

The Chairman: Let us press on. Lord Tomlinson, would you table your question?

Q89 Lord Tomlinson: Briefly, I was beginning to get excited with one of your responses, Mr Bayley, when you said that the Government had replied to the consultation document and that we had asked for value for money on Pillar 1. Now that is a surprise, is it not? What I want to know, and what I think Lord Maclennan was trying to find out, is: how will we recognise value for money when we get it? What specifically are you asking for in terms of value for money? Perhaps we can reflect on that while we have a vote.

The Chairman: While you are considering that awkward question, we will retire to vote but we will return. Thank you very much.
[Meeting suspended for a Division in the House.]

Q90 The Chairman: Colleagues, I am going to make a start. We have time if we reconvene for Brendan to assuage the disappointment of Lord Tomlinson on value for money.

Brendan Bayley: What would one want in terms of value for money? If one had a hierarchy, one would start by phasing out market price support, which is the most damaging and has the most negative effect in value-for-money terms, then move on to coupled direct payments, which are not as bad as market price support but worse than decoupled direct payments, which would be the next on one's list. That is the negative agenda. In terms of a positive agenda, what sort of thing would one spend on? On the environmental side of the equation, one would look at agri-environment schemes targeted at biodiversity outcomes and climate change mitigation. That would generate positive value for money. On the competitiveness side, one would look at research and development, depending on the location, infrastructure and advice. Those are the sorts of things that improve productivity. That would be a value-for-money agenda within the CAP. Defra would share this analysis. If you draw from the OECD's work, one sees that there have been several declarations by European professors of agriculture and economics which are succinct summaries of the sorts of things that one would like to see in reform of the CAP. All of that is consistent with what I have referred to. One can construct both a positive and a negative agenda around value for money. I do not know whether that answers the question.

Lord Tomlinson: And you have done that in reply to the consultative document.

Brendan Bayley: From memory, I could not tell you how much of that detail is in there, but that logic informs our response.

The Chairman: I think that there have been a couple of points this afternoon where you may need write to us, just to verify what has been said.

Lord Tomlinson: It would be helpful to know what you said.

Q91 Baroness Howarth of Breckland: I listened with great interest to all that. Before I move on to my question, I want to pursue your optimism that you might get change. Our Sub-Committee on Agriculture has spent some time looking at innovation in agriculture and talking with a number of colleagues across Europe. It is now moving into water policy and looking at what is happening there. On both of these, because water obviously has a relationship with the environment and Pillar 2—on Pillar 1, we have looked at that in some detail in terms of innovation—what became incredibly clear was the inertia in the system. We know that on 15 February the Agriculture Ministers of France and Spain issued a joint statement saying that they "will not accept" any budgetary overhaul. In the face of that negative gateway, how do you see the Government's agenda being pressed forward? That is what everyone really wants to ask. What levers do the Government have into the biggest part of the EU budget that could prise so much more forward to make change?

Brendan Bayley: First, I hope that I do not come across as overly optimistic, because—

Baroness Howarth of Breckland: You are a civil servant

Brendan Bayley: I recognise the point that you are making about the politics. There is an incredibly strong logic there for arguing, "No change, please. We're very happy with our direct payments". So it is undoubtedly a challenge. There are a lot of processes going on in parallel. There are debates in the Agriculture Council and other Council formations about individual regulations. Around Europe, Agriculture Ministers will be very clear about what they might want out of the EU budget negotiations. At the same time, you will be as aware as we are of the broader fiscal situation across Europe. At some point, those two realities come together and it is impossible to be precise about the outcome. The fiscal pressure is a very important lever and should not be underestimated. That comes through in terms not just of the amount of money available but of prioritisation. For example, it is quite interesting that certain new member states are very clear that they want a competitive agricultural sector. That is not say that they want less funding, but they see how Pillar 1 might have a negative impact on their farming sector. Then there is the debate about structural funds versus Pillar 1 of the CAP and how far one promotes growth better than the other. There are all sorts of debates along those lines going on in capitals as well as in European fora. To come to the second part of your question, on what the UK Government can do, I think that it is to engage with others around Europe to put the reasoned-evidence case, both around the specifics of CAP and the broader budget and broader economic environment, and to see what comes through. There is likely to be a better reception for that argument in the current climate than there might have been if the economy was doing better.

Q92 Baroness Howarth of Breckland: On rationalisation, the CAP proposals include a range of measures to support risk management in the agriculture sector, including the risk management toolkit within Pillar 2 and the global agricultural risk management fund, currently placed outside the MFF. Are these measures necessary? Could they be rationalised? What possible consolidation might there be to allow the budget in this area to be reduced without damaging the efficacy of the risk management measures offered?

Q93 ***Brendan Bayley***: On risk management, if one takes a step back from the EU budget, we have seen price spikes in international markets, and there are debates about the extent to which volatility will increase. At the very least, one would conclude that risk management is exceedingly important and may well be even more so depending on what happens against the backdrop of climate change. That is true both in terms of price and of the impact of weather and disease on crops and livestock. Risk management is absolutely central to the sector, but it is also important that farmers take the initiative to manage their own risks, which they can do in a range of ways. The extent to which the EU budget can assist in that process is very much up for debate. The risk with having a pot of money off-budget which people might expect the Agriculture Council or others to draw on is that it perhaps sends the wrong signals. In any event, the fact that this money is off-budget is very unhelpful; it does not sit well with our broader approach to the EU budget in terms of transparency and better fiscal management. Certainly, the agricultural element of the globalisation fund and the globalisation fund as a whole need to come on-budget. To make room for the agricultural element on-budget, one would simply see a reduction in Pillar 1. If one is going to have this fund, one would make space for it.

Q94 Baroness Howarth of Breckland: What you are describing is flexibility, which we discussed earlier in terms of the budget. How do you get the transparency which ensures that you are on budget?

Brendan Bayley: There needs to be an agreement in the context of the broader MFF negotiations that this money is not an off-budget item, and that, if it exists, it is on-budget and is subject to the normal disciplines of the EU budget.

The Chairman: What about Lady Howarth's point about consolidating the risk management elements?

Brendan Bayley: We do not think that there is a good case for an agricultural component to a globalisation fund, but, in any event, the globalisation fund does different things to the toolkit under Pillar 2. The toolkit under Pillar 2 is about access to risk management measures in advance of the fact, whereas the fund is directed not at farmers but at a sector, almost as compensation for policy reform elsewhere. They are distinct. I agree that there are very serious questions to be asked of both from a value-for-money perspective, but, in any event, they should be on-budget.

Q95 Lord Dykes: I want to get on to Horizon 2020, but, before that, can I ask a quick preliminary question on the evidence given by Mr Glycopantis on 19 December? Replying to a question on Connecting Europe moneys, he said: "We are comfortable with the situation where growth-enhancing infrastructure, like Connecting Europe, takes a greater share of the EU budget. We are very comfortable with that position. We are not in a position to say exactly how much we think should go to Connecting Europe, and other member states are in exactly the same position. It is very early in the negotiation". It is early days, I agree, so my question is slightly unfair, but are figures beginning to emerge? Is it getting slightly clearer? After all, the schedule is quite tight when one thinks about it.

Mike Glycopantis: It is quite tight, but actually I was in a discussion this morning with another member state and there is no desire to move quickly to the numbers. The discussions are around the quality of spending; they remain at that level. We have no expectation that there will be numbers on the table even in June. We think that we will still be discussing issues around quality and type of spending, but not numbers. That is the current approach.

Lord Dykes: So maybe putative indications in the autumn, for example?

Mike Glycopantis: I would expect there to be some numbers in the autumn.

Q96 Lord Dykes: As you know, Horizon 2020 is the main financial instrument for bringing in the Innovation Union Europe 2020 flagship initiative. The funds earmarked for innovation are also included in other budget lines. What are the advantages and disadvantages of having "mainstreamed" innovation funding elsewhere in the budget, versus consolidating all such funds in a single instrument? That is slightly akin to the previous question.

Alex Skinner: It is akin to the previous question and it is also relevant to the common strategic framework. Horizon 2020 takes a whole series of policies but introduces, as you say, some simplification and rationalisation, particularly around the mechanics, to reduce bureaucracy. In that sense, the big advantage of the consolidation is, first, that we minimise duplication; secondly, we allow greater focus; thirdly, we get more scale; and, fourthly, bureaucracy is reduced. The issue is then where the line is drawn. In the Innovation Union, the clearest distinction is between spending on excellence, which is mainly in heading 1a, and spending on regional development, which is mainly in heading 1b. There would be an issue about trying to consolidate those, because the nature of the objective, the nature of the participants and the nature of the mechanics of how the money would be allocated are very different. We are supportive of moving to this consolidation in Horizon 2020 because of the advantages that I have just spoken about. If you were to think about extending it to structural funds, that would become more difficult. There are some communalities between structural funds and other parts of the budget. It might be natural to bring those together in one group, with this in another, but not to mix the two.

Q97 Lord Dykes: What will the Government and perhaps other like-minded governments, and maybe some of the others on the list of people who wrote with the Prime Minister to the Commission, try to do if inertia in the system means that farm spending ends up being somewhat higher than some ambitious member governments would like—one talks about 20% to 25% of the budget—to preserve and protect innovation funding? This must be one of the keys to the growth syndrome that we were talking about.

Alex Skinner: My colleagues might want to come in on this in a minute. The impact on the ground is about two things: first, the amount of money; and, secondly, how well that money is spent. There is considerable scope in all areas of the EU budget to improve the quality of expenditure. One could improve outcomes under Innovation Union without necessarily increasing the money. In the worst-case scenario, we could improve outcomes by doing that. Horizon 2020 is the big element in heading 1a and structural funds are the big element in heading 1b. The Government have been clear that they think there should be a significant reduction in the amount of structural fund spending that goes to richer member states because of recycling. There is scope for looking at those elements. However, my first answer would be that you could achieve a significant impact by improving the quality of expenditure. Indeed, the Commission has gone some way towards attempting to do that, but I think that more could be done.

Q98 Lord Hannay of Chiswick: Could we go back to where the discussion started, in the reference both to the real-terms freeze and the point that Lord Tomlinson raised about a perceived lack of flexibility and ability to move some areas of the budget towards an increase on the basis of cutting down others and rearranging priorities? On justice and home affairs, I think that the Government are taking the position that any increase in programme funding has to be found within the justice and home affairs budget. Frankly, it is difficult to see how that is going to work, because the budget has been going up rather a lot in recent years because of the increase in the number of agencies that have been set up—for example, Frontex—and not just because the Commission has been spending wastefully. From the documents that are filtering through to us from the Home Office and elsewhere, we get the impression that that the idea of resisting any increase within existing budgets is being applied with unbelievable rigidity. For example, the Government, like this Committee, support the idea that Europol needs a cybercrime centre to deal with the increasing amount of cybercrime. However, the Home Office is now taking the position that that has to be funded within Europol's budget, not just within the JHA budget. So this is basically a complete freeze. I do not know whether your satraps around Whitehall are applying this somewhat overzealous approach, in which case you could perhaps suggest that a little more flexibility is desirable. It is a little difficult to see the British Government spending £650 million more to provide for cybersecurity, but you cannot really hope that Europol will do it for nothing. If it is expected to do it for nothing, we are driven to ask the Home Office, "Which parts of Europol would you cut in order to fund cybercrime?" I know that the answer to that is that it does not want to cut any of them because it thinks that they are valuable. So you see the problem. Might there not be some slight excess of zeal around the place?

The Chairman: Lord Bowness, do you want to come in with your supplementary?

Q99 Lord Bowness: Thank you. I am also interested in justice and home affairs, particularly from the justice side. The Court of Justice is funded, as you will know, from the administration budget, which I have no doubt is top of the Government's list because people always believe that you can save the world with cuts in the administrative budget. But I think that the Government now recognise that the Court of Justice needs more resources—a second point that we as a Committee have made is that it needs more judges. So there has to be an increase in real terms so far as the court is concerned. Flexibility between one budget and another, or within the administrative budget, is extremely important, so I hope that it is recognised that the Court of Justice needs more money.

Mike Glycopantis: Let us look at heading 3. Border security, asylum and migration are all important issues that the Government care about. The budget has risen by a lot during the current seven-year framework and it is underspending by a large amount. The provision for 2011 was €1.9 billion; the provision for 2012 was €2.1 billion; and the actual payments are €1.5 million in 2011 and 2012, so you have a 25% underspend against what was provided. We believe that there should be a real-terms freeze at the 2011 level—that is the reference point for the Prime Minister's letter. The basic answer to your question is that these areas are currently underspending. We see the pressure, and it is in areas that we care about such as migration, but these programmes are currently underspending by an average of 25%. Therefore, we do not think that we need to give more money to the budget to cope with these areas. It is a tough position that we are taking: that no heading or significant sub-heading should have more than a real-terms freeze. It is an incredibly difficult negotiation where the Commission has come forward with a budget that is more than 10% bigger than the real-terms freeze; it is a negotiation where the Commission has come forward with proposals to end the UK's permanent abatement—we can come on to that—and proposed a temporary and much smaller abatement; and it is a negotiation where it has come forward with proposals for a financial transaction tax, which, on most calculations, would be funded mostly from the UK, the UK being not just the biggest contributor but contributing more than 50%. So this is a difficult negotiation. The Prime Minister is absolutely resolved not to allow the budget to rise by more than inflation over the coming years, which means that we have taken a very tough approach on the components of the budget.

Lord Hannay of Chiswick: I do not think that you would find anybody in this Committee of whom I know who does not recognise that the Commission's proposals on the abatement and the financial transaction tax are unacceptable, and they are not going to pass. However, to counter that by a manoeuvre which involves a complete freeze right across the budget at every single level, at every point, is to negate a policy that successive British Governments have had over the years for rebalancing the budget and trying to move the priorities to areas which are of greater value for the European Union and for Britain. It seems to me, therefore, that your retaliation is a singularly damaging way of dealing with a matter which we will probably be able to deal with anyway, because it requires unanimity both to change the abatement and introduce the financial transaction tax. Are you not damaging our objectives in the individual fields quite a lot by applying this retaliatory measure in such a rigorous style?

Mike Glycopantis: I would not call it a retaliatory measure for the abatement proposal.

Lord Hannay of Chiswick: You made it sound retaliatory.

Mike Glycopantis: The proposed budget size for the Commission is far too high, and it looks like other member states are saying that. We have also said that we believe that a greater share of the budget should go towards certain areas such as tackling climate change, delivering growth and external action. We are not silent on how the budget should be spent, but we are saying that we should reprioritise away from the lower-value CAP and administrative expenditure towards those areas. So we are not silent on the shape of the budget; we just feel that, in a situation where there are so many advocates for higher spending across the piece, we need to keep firm and keep reminding people that the EU budget is large—€126 billion in 2011 prices; that there is scope for reprioritising across the budget; and that individual headings are large and are being underspent at the moment. The underspending is the other key point. It is happening across most of the budget, not in the direct payments but in most other areas of the budget. We want to keep reminding people of that fact. Underneath the headings, people should keep to the real-terms freeze, while at significant-programme level they should look constantly for offsetting savings.

Q100 The Chairman: Colleagues, we have three more questions. I wondered, Mike, whether you would consider what was being said by Lord Hannay. Would you also think about the point made by Lord Bowness on administration, which all too frequently figures in these discussions without much evidence? I would like to complete this session by inviting questions from Baroness Young, Lord Sandwich and Lord Dear.

Q101 Baroness Young of Hornsey: Mr Skinner, you have already referred to the common strategic framework and the consolidation of structural funds within that programme. Can you tell us from your analysis of the proposals what savings have been achieved as a result of these rationalisations? Do you think that there are any hidden increases in the financial envelope for these funds?

Alex Skinner: As you will know, the Commission has published the draft regulations but has not published some of the more detailed documents that it will do on the common strategic framework. We are therefore at the beginning of what is likely to be a long and difficult negotiation. At this point, we have not attempted to assess what the benefits of a rationalisation through the common strategic framework could be, because we do not really have the level of detail that we need to be able to do it. As a result of the common strategic framework, some efficiencies are likely to be realised, either because of the way that the planning is done, the way that the performance framework is managed or the way that member states, and indeed the Commission, have to produce the documents required. The question on whether there are hidden increases comes back to the question of the overall budget, which has not yet been settled. If we were in a negotiation where the budget was fixed and there was some objective way of assessing exactly how much should be spent, that might be the case. The Commission has proposed changing the nature of structural funds, which has affected the budget. There have then been changes in how rich different member states are, which has affected the budget. And then we have these new proposals. My sense is that there will not be some hidden efficiency, because by the end of the negotiation there will have been difficult discussions about the size of the budget and, at a political level, what the objectives of structural and cohesion funds should be. Therefore, the administrative budget of the structural cohesion funds, which will be affected by this at least at the Commission level, will end up being reduced in line with what Mike was saying about the administration budget. Therefore, the bulk would be in support of the activities of the structural and cohesion funds.

Q102 Baroness Young of Hornsey: You spoke earlier about looking at improvement in the quality of expenditure. Would you apply that to this case as well, and how do you assess it?

Alex Skinner: Yes, I think that it would be, because it is part of the ambition of the common strategic framework. For example, if you are in receipt of all five funds, you should produce one document that says what you are going to do with them. At the moment, five different organisations in a member state might be producing five different documents with different sets of objectives in five different areas. There are probably some other dimensions to that as well. The idea is that you would have just one document which would be co-ordinated. In terms of quality of expenditure, at the very least you would expect more thought to have gone into, "What do we want to use this money for and where best could it have an effect?" So we would certainly look at quality of expenditure. How we will know whether that has been achieved will come through the negotiation between the member state and the Commission right at the beginning of the partnership programme process. The Commission then has a series of evaluations which will run through the next financial perspective. That would give you the answer to your question.

Q103 Earl of Sandwich: Would you also say a word about conditionalities and their impact on the structural funds? What are the risks and benefits? For example, macroeconomic conditionality, including compliance with the fiscal compact, could be unfair on some organisations which lie outside that compact. There must be other examples of how conditionalities affect the way in which the structural funds are working.

Alex Skinner: You are absolutely right. The regulations and common strategic framework include a series of conditionalities. There are ex ante conditionalites, ex post conditionalities and then, as you said, macroeconomic conditionality. Ex ante conditionalities, framed in the right way, could be very sensible. The Government are supportive in the sense that we are all very keen for this money to be spent appropriately and on things that will promote growth and development. To the extent that ex ante conditionality helped in that process, it would be useful. For example, there is already a list of the areas where you can spend structural funds, and having a sensible list would be useful. The Government do not support a performance reserve, whereby a certain proportion of the structural funds would be held back, because of the perverse incentives that it may have and because the assessment of the performance reserve means that only very late in the proposal would you know how much money you were going to get, and you would have then to make decisions about how to allocate. On macroeconomic conditionality, the proposal is that it will affect member states. The UK is in a different position from other member states; first, as a result of our protocol to the treaty, which means that, under the stability and growth pact, we do not have the same obligations as others; and, secondly, because the Van Rompuy report on economic governance is very clear that wider macroeconomic conditionality should be applied to euro area member states only, and that was supported by euro area member states. So you are right about conditionality. At the moment, we have something with differential effects, because only the cohesion fund is subject to macroeconomic conditionality under the stability and growth pact. The proposal is that it would be not just that but the other funds as well. As I have said, other member states may be happy with that, but, in terms of what happens to the UK, we cannot have conditionalities apply to us under the stability and growth pact. The Van Rompuy taskforce report is very clear that it should not apply to us on the excessive imbalance procedure.

Earl of Sandwich: So you have quite a lot of anxieties on that one.

The Chairman: We conclude with Lord Dear. Would Lord Hannay also table his supplementary question?

Q104 Lord Dear: Can I wind up by looking at VAT and abatement—I know that, essentially, you have already covered the same sort of ground. We all know that the Government have opposed the new VAT-based own resources and previously told us that they would be happy to see the current VAT-based resource phased out. However, the VAT-based resource is currently used in the calculations of the UK's abatement. If this resource is phased out, but the UK abatement remains in place in its current form, what alternative calculation methods are available to us? If there are any, how would these methods impact on the quantum of the abatement?

Mike Glycopantis: It is a difficult situation.

Lord Dear: It is Catch-22.

Mike Glycopantis: It is a bit. We might be prepared to look at some reform of the financing system and VAT is a candidate for reform. However, the Government are clear that they want to protect the rebate in its entirety. Since the abatement is calculated with respect to VAT as part of the VAT system, we cannot make any changes to the VAT system that would disadvantage the abatement. Some changes might be able to be made to the way that we collect the VAT or other elements of the system which are quite complicated, but we are wedded to the calculation of the abatement, which is in the VAT regulations. The Government have been very clear that they will not accept any change to the financing side that disadvantages the UK and prejudices the abatement. As you say, it is a bit of a Catch-22.

Q105 Lord Hannay of Chiswick: On this question of the abatement, I fear from the evidence that we received from Monsieur Jouanjean and his written evidence that we are slipping back some 30 years into a bizarre debate about something called the juste retour, which seems to ignore the fact that the British abated net contribution has gone up substantially in recent years. It is an absurd suggestion, in my view, that you should move to a lump-sum payment which has no possibility of being scientifically calculated because it is going to be calculated several years—seven years in some cases—before the actual expenditure. I suggest that you need to do a bit more to explain these two propositions—which are pretty aberrant—than you are doing at the moment, because it does not seem to me that the facts are getting out. I would think that it was really important for the report that we are going to write that you should provide us with, for example, an explanation as to why the lump-sum payments from 1980 to 1984 were thoroughly unsatisfactory for all concerned, because, in the first two years, we got back more than we should have got back and virtually had a nil contribution and in the last three years we got back far too little. So the lump-sum payment system is proven bad, but you would not guess that from reading the Commission's proposals. They presumably are all too young to have been around when that was started, but it would nevertheless be helpful if you could set out some of this argumentation rather than simply saying, "We're not going to agree to it". Although that is our ultimate option, we will also have to be a bit more convincing. Frankly, the arguments that the Commission is adducing on the abatement are unconvincing in the extreme if they are subjected to careful, calm analysis.

Q106 The Chairman: Let us conclude there, because I think that you can respond to that as I have asked you to do to other points. I would also be grateful if you could respond to three other points. First, would the Government ever consider an alternative source of own resources? Secondly, on my opening question about having payments rather than commitments, is that just a way of lowering the budget? Finally, what comes over very strongly is that the Government are very resistant to the idea of changing juste retour. You seem to be very supportive of that, whereas some of us would like to see some more fundamental changes in the budget to direct it to modern times. Would you respond to those questions, consult our Second Clerk if there is any doubt or ambiguity about some of the questions that have been put and be kind enough to write to us? Indeed, if there is anything that you wish to add, we would be grateful for your further thoughts.

You know that the meeting is being recorded; we would be grateful for any corrections to the transcript. In the mean time, we are extremely grateful for having the three of you before us in a much punctuated session. We will think very hard about what you have had to say. I conclude by thanking Brendan, Alex and you, Mike, for coming this afternoon. I conclude the session and put us back into the hands of our Chairman.

HM Treasury – Supplementary written evidence

1. Brendan provided a very helpful explanation of the thinking that has informed the Government's view on value for money within the CAP, but members would be grateful to know at what stages and in what form this point of view has been articulated to the Commission and other Member States as part of the MFF negotiations.

The UK response to the Commission's CAP Communication (attached for ease of reference) in January 2011, refers to the Government's concern about the poor value for money of the CAP. Ministers and officials meet frequently with counterparts in other Member States, in the Commission, and in the European Parliament, and emphasise, amongst other things, the need for overall budgetary restraint, and the scope that exists for securing savings in those parts of the budget (such as Pillar 1 of the CAP) that represent poor value for money.

2. What the Government's view is of the similarity between the Commission's abatement proposals and the system in place in 1980-84. I have attached a copy of Director-General Jouanjean's supplementary evidence to the Committee, which addressed this question (at Q11), for information.

The main similarity between the Commission's latest proposals and the 1980-4 system is that both involve lump sum payments on a temporary basis. Amounts were –and in the case of the new proposals, would be - determined by opaque systems, unlike the current analytically-justified system. The system in place in 1980-1984 consisted of ad hoc arrangements which can be seen as a precursor to the current permanent system based on actual budgetary imbalances.

The Council conclusions of 30 May 1980 stated;

> "*For 1982, the Community is pledged to resolve the problem by means of structural changes (Commission mandate, to be fulfilled by the end of June 1981: the examination will concern the development of Community policies, without calling into question the common financial responsibility for these policies which are financed from the Community s own resources, or the basic principles of the common agricultural policy. Taking account of the situations and interests of all Member States, this examination will aim to prevent the recurrence of unacceptable situations for any of them). If this is not achieved, the Commission will make proposals along the lines of the 1980 to 1981 solution and the Council will act accordingly.*"

As the structural changes pledged to "resolve the problem" did not happen, the Commission made similar proposals in the following years, until the current system – which automatically corrects excessive budgetary burden and imbalance that the UK faces under the current expenditure policies – was negotiated in 1984 and established through changes in successive Own Resources Decisions.

3. Whether the Government would ever consider an alternative source of own resources that could underpin the UK abatement in place of the current VAT-based calculation method.

For the UK to consider any change to the current system, alternatives must not (i) increase the UK's gross contributions compared to the current system; (ii) pose a threat to UK's position in the long term; and (iii) involve any EU taxes. Unfortunately the Commission's draft proposals do not meet any of these criteria. The UK's position is a principled and fair one given the UK's continued excessive budgetary burden and imbalances.

4. Whether the Government's preference for negotiating in terms of payments and not commitments is, at root, simply a method to reduce the overall envelope of the budget

Clearly the overriding priority for the UK in MFF negotiations is to deliver restraint in the EU budget, limiting the budget to a maximum real-terms freeze from a baseline of 2013 payments. However, payments-based budgeting is primarily an issue of clarity and sound planning.

In the simplest terms, working in payments is good budgeting. Payments represent actual expenditure (and actual *need*), rather than notional expenditure plans which are rarely delivered. The UK works in the equivalent of payments domestically, so this is clearly a realistic system. But importantly, it is payments which directly affect domestic budgets. It is payments which drive contributions from Member States and therefore it is payments which impact on UK taxpayers.

The Government has also been clear that action must be taken to address the mounting liability of unspent commitments in the EU budget. Delays in 'spending' commitments during the current MFF have led to important delays and have caused the RAL to reach unprecedented levels at the end of the current programming period. It is likely that the actual stock at the end of 2013 will exceed €245bn – almost two full years' worth of budget payments. Budgeting primarily in payments, rather than in commitments, is one step towards tackling that liability.

Ultimately, working in payments gives greater certainty to contributors, recipients and taxpayers alike.

5. Whether the Government is in support of a *juste retour* approach being taken in negotiations.

The UK has never taken a *juste retour* approach in negotiations. We make a net contribution to the EU budget and do not demand that our receipts match our contributions. However, continuing distortions in EU expenditure mean that without the abatement the UK would sustain a budgetary burden that would be excessive in relation to the UK's relative prosperity. The abatement reduces the distortion which the UK experiences under the current expenditure policies.

6. Whether the Government is in support of an increased budget for the Court of Justice within the Administration Heading, and how they see that can be achieved.

The Government is aware of the large backlog of cases facing the ECJ and supports reforms that would enable the ECJ to operate more effectively. At a time of ongoing economic consolidation at home, the Government seeks to impose real budgetary restraint at EU level and aims for significant savings to EU administrative expenditure over the next Multi-annual Financial Framework. Therefore, the Government hopes that the ECJs capacity may increase as a result of cost-effective reforms, which would ideally be met within the ECJs existing budget or at least offset by administrative savings in other areas.

7. Whether the Government will reconsider its position on the JHA budget (particularly in regard to Europol and a Cybercrime Centre).

The UK's position is that no heading of the next MFF should receive above a real-terms freeze, including Heading 3. This applies even to areas such as research and innovation and external funding, which are relatively higher priorities for the UK in the EU Budget than JHA.

If our opening position were to recommend explicit increases in certain areas of the budget before we achieved any corresponding decreases, there would be a risk that we would ultimately become committed to a higher budget overall, undermining the Government's top priority in the negotiation of achieving budgetary restraint. As negotiations progress we will retain flexibility in how we allocate spending once a restrained budget is achieved.

Mark Hoban MP, Financial Secretary, HM Treasury – Written evidence

12475/11, Communication from the Commission, A budget for 2020 and associated documents

Thank you for your letter of 15 February regarding providing evidence for the Committee's follow-up inquiry into the 2014-2020 EU Multiannual Financial Framework.

As you note, I will not be able to give oral evidence to the committee. However I am, as ever, pleased to provide written evidence in response to the questions you set out in your letter of 15 February. Officials from the International and European Union Group of HM Treasury will give oral evidence on 6 March, led by Mike Glycopantis (Deputy Director, Head of the EU Finance team).

As written evidence alongside the oral evidence my officials will provide later, I have set out responses to your questions in turn below.

Negotiations

1. ***What concrete agreements have taken place thus far in the Council working groups considering the specific MFF proposals?***

No concrete agreements have taken place thus far in the Council working groups considering MFF proposals. Council working groups and MFF formations have been primarily focussed on understanding Member States' positions in advance of attempting agreements. The UK Government has been clear that, while the MFF breaks down into many individual elements of legislation, no concrete agreements on these are possible until there is agreement on the overarching question of budget size.

However, the UK Government has been clear that at a time of ongoing economic fragility in Europe and tight constraints on domestic public spending, the Commission's proposal for very substantial spending increases compared with current spend is unacceptable, unrealistic, too large and incompatible with the tough decisions being taken across the EU.

2. ***Where does the Government anticipate finding the biggest disagreements between Member States in Council negotiations? How does the Government intend to bridge divides between Member States in the Council on the big questions, such as the overall envelope or own resources?***

The UK Government is aware that there are diverse views on budget size and own resources across Member States. The Prime Minister has been clear, however, that the maximum acceptable increase is a real freeze in payments, year on year from actual payments in 2013. Four other Member States: France, the Netherlands, Finland and Germany, signed up to that message. Furthermore, a group of eight like-minded Member States made clear ahead of the General Affairs Council of September 2011 and again in January 2012 that the Commission proposal was too large.

Given the need for unanimity in Council to agree the overall envelope or to amend the existing own resources arrangements, this substantial coalition represents significant collective pressure in favour of budgetary restraint. Any effort to introduce new own resources to fund the budget, or to target the UK abatement, however, would require UK support to advance. The UK has made it clear that both changes to the abatement and new taxes to fund the EU Budget are unacceptable.

General principles

3. ***A recent paper on the EU budget as a tool for growth, published by the Centre for European Policy Studies begins: "Once again, the Member States are locked in an unrelenting and sterile battle about the size of the EU budget. They are barking up the wrong tree…When it comes to EU spending, quality matters far more than quantity". To what extent does the Government's focus on the overall size of the budget risk reducing the quality of the budget, particularly its ability to contribute to long-term growth?***

The UK Government has been clear that the overriding priority for the next MFF is budgetary restraint, thereby ensuring that the EU budget contributes to domestic fiscal consolidation.

However, while the UK Government's overall objective is to reduce budget size, we consider that spending on growth and competitiveness, on external funding and on climate change should have a proportionately larger share of a budget that at most increases by no more than inflation. Furthermore, in order to align the budget towards higher-value areas of expenditure, the UK Government is seeking very substantial reductions from the CAP, focussed on direct payments and from administration expenditure across the budget.

4. ***How much weight is given to European Added Value (EAV) by Member States during budget negotiations, as compared to questions of net contributions and receipts? How does EAV relate to Value for Money (VFM), and which of these does the Government think should take priority in the EU budget?***

Considerations of EAV and the importance of net contributions and receipts vary by Member State. However, the UK Government recognises that some Member States value receipts from the budget particularly highly, regardless of relative value. That is a major reason behind the continued dominance of the budget by Structural Funds and CAP. The Government clearly places great importance on understanding, and restraining, the UK net contribution in the next MFF, in order that the EU budget contributes towards domestic fiscal consolidation.

However, the Government has also been clear that the budget should be directed towards what the UK Government considers to be higher-value areas, as set out above. This shift in spending aims to focus on areas of European Added Value, and therefore towards deriving greater Value For Money from the EU Budget as a whole.

5. ***Is the Government satisfied with the administrative processes being proposed for managing MFF programmes and funds, such as humanitarian aid, ITER and Connecting Europe?***

The UK Government believes that EU institutions should not be immune from savings and is targeting very substantial savings in administration expenditure across the budget. Any suggestion of waste in the budget damages the standing of the institutions and of the EU as a whole.

We are also concerned by errors. According to the latest report by the European Court of Auditors on EU financial management, the error rate in the 2010 EU budget actually increased to 3.7%, up from 3.2% for 2009 and above the 2% level needed to for a positive statement of assurance. The UK recently voted against the discharge of the 2010 EU Budget, owing to the slippage on progress made in previous years, and has called for urgent improvements.

The DFID Multilateral Aid Review found that the European Commission Humanitarian Office (ECHO) is cost effective, with low administration costs and joint-working with the rest of the EU to ensure efficiency. Within ECHO, however, Value for Money is not yet an overarching narrative and some current financial management procedures can push partners towards greater bureaucracy. The Commission has not yet released a draft regulation on the Humanitarian Aid Instrument, but in negotiations on humanitarian aid in the next MFF, the UK will continue to argue for greater effectiveness and efficiency in ECHO.

On ITER, recent measures following a 2009 assessment have produced improvements in the management of the project. The UK opposes the movement of significant funding (including ITER and GMES), 'outside the MFF'.

On Connecting Europe, we are concerned by the Commission's proposal that they should be able to move money between the three sectors covered without consulting Member States and do not yet have a clear sense of to what extent the Facility will be centrally managed.

Specific programmes and budget lines

6. ***The Government has called for "a higher proportion of a restrained EU budget" to be "spent to promote sustainable growth" (HC Deb 909). What concrete counter-proposals does the Government have for programmes such as Connecting Europe and Horizon 2020 to show how this might be achieved? Where would the Government focus investment?***

The UK Government's top priority is restraining the size of the EU Budget to, at most, a real freeze in payments compared to 2011 levels. We are not advocating increases in any heading of the budget.
However, within this context growth and competitiveness, external relations and the climate change components of these headings are priority areas. In Heading 1 we have made it clear that Horizon 2020 is a priority area, although we do not advocate the spending levels for it proposed by the Commission. We also oppose the huge 400% increase for transport, energy and infrastructure spending in the Connecting Europe proposal. These programmes can be scaled according to affordability.

Our counter-proposal therefore centres firstly on making reductions to the levels of spending proposed by the Commission and secondly focussing the spending that remains on these UK Government priorities. When targeting how the final agreed level of funding should be spent, we will aim to focus on those areas of the proposal that offer the best EU-added value and the best return to the UK taxpayer. Work is ongoing to assess which elements of the individual proposals best support these aims.

In parallel, we are also pursuing a series of administrative reforms at EU level which can make a genuine contribution to growth at minimal cost, such as completing the Single Market (particularly in services and the digital single market), reducing administrative burdens on business, and ensuring that the EU can be the driver of world trade. The joint pre-Spring Council letter also called for a well-functioning Financial Services sector which supports growth and helps business to access finance.

7. ***Does the Government see a role for cohesion policy and funds in supporting EU growth by addressing structural weaknesses and competitiveness challenges? How does this relate to the Government's call for a budgetary freeze?***

As highlighted by the Prime Minister's recent joint letter "A plan for growth in Europe" with eleven other Heads of Government, the key to long term sustainable growth in the EU is structural reform. For example, amongst other things, the letter highlighted the importance of implementing previously agreed single market legislation, establishing the European Research Area and the swift conclusion of free trade agreements with India and Canada.

The UK Government sees that, when designed well, cohesion funds and policy can compliment structural reform, but they are not, by themselves, the central mechanism for achieving EU growth. And as a result of the 2011 Annual Growth Survey, the Commission calls for three growth levers to be fully deployed as part of EU-wide action: EU digital single market; internal market for services; and tapping into the potential of external trade.

The UK Government supports the aim of cohesion policy in reducing disparities in development between the different regions of the EU, so that every part of the EU is able to develop to its full potential. As well as raising living standards in poorer Member States, this compliments the growth and integration of the Single Market, of direct benefit to all parts of the EU, including the UK.

Growth and competitiveness are priority areas for the UK Government and should have a proportionately larger share of an EU budget that, at most, increases by inflation compared to payment levels in 2011 The UK Government message is clear that fiscal responsibility and restoring economic stability is vital for growth. As the Chancellor remarked in the Autumn Statement "If left unaddressed, high levels of public borrowing and debt risk undermining growth and economic stability in the UK Government".

8. ***The staff regulations are currently being revised (18638/11), and the Commission is operating a zero growth policy in relation to staff numbers, among other initiatives. Does the Government think that enough is being done to restrain administrative costs? What specific actions could the Commission take to further reduce administrative costs, and what are the barriers to further reductions?***

The Staff Regulations are indeed currently under revision, and the Commission is proposing a 5% staff reduction over the next Multiannual Financial Framework, among other initiatives, although the UK and other Member States have yet to see sound a financial analysis of these proposals and the savings they are estimated to make.

The UK Government believes that considerably more can be done to restrain the administrative costs of the EU Institutions. The proposals currently under discussion do not go anywhere near far enough in finding financial savings. The UK Government has committed to deliver savings of 33% on its own administrative domestic departments and would like to see a similar level of ambition from the European Institutions.

There are many areas where the UK Government believes the Commission could further reduce administrative costs, most notably in the automatic annual salary adjustment method, the pension scheme and the allowances offered to EU Institutions staff through the Staff Regulations. The UK has broad the support of other Member States on this issue, but does anticipate obvious reluctance from the EU Institutions themselves.

Own resources and the rebate

9. ***During the previous inquiry, the Government said that it would resist EU taxes and was in favour of the current VAT-system being axed (written evidence from Justine Greening MP). Would the Government therefore wish to see the EU budget financed solely through levies and the GNI-based resource? What is the Government's current assessment of the proposed new VAT-based own resource?***

In response to the Committee's question of 18 January 2011 on the Government's position on the VAT-based resource, the then Economic Secretary to the Treasury Justine Greening MP made it clear that the Government is in favour of simplifying the financing of the EU budget, for which the current VAT-based contribution is one candidate. The answer also highlighted the fact that there are a number of complications for the UK, including the explicit link between the abatement formula and VAT-based contributions. To be perfectly clear, the Government is not in favour of any change to the current Own Resources system that would jeopardize the UK abatement.

The UK Government opposes any new EU Own Resources, and in particular any new EU taxes or changes to the existing Own Resources system, that increase UK contributions or pose a threat to our position in the long term. The Commission's current proposals on the Own Resources system would remove the permanency of the UK abatement. This means that we oppose the new VAT resource whether you consider it a new tax or not.

10. ***Does reliance on the GNI-based resource encourage a 'juste retour' approach from Member States? What is the Government's assessment of the Commission's suggestion that the current system of financing the budget results in a "tension which poisons" debate about the budget (p.1, 12478/11)?***

A *juste retour* approach from Member States does not arise from reliance on GNI-based resource alone. The main drivers of such an approach likely include the perceived unfairness and imbalances in EU expenditures and increasing reliance on net contributors to finance higher spending.

The UK Government does not agree that the current system is the sole reason for the "tension which poisons" debate. The current system of allocating expenditures across budget headings is as much a reason for tension as the way these expenditures are financed, as exemplified by annual budget negotiations. Such references to tensions experienced in previous negotiations act as a distraction from more pressing issues, including for example questions of fairness and expenditure reform.

11. ***Do you agree with the Commission that the UK rebate results in "perverse" disincentives, such as discouraging applications for structural funds that require co-financing, or for EU aid following natural catastrophes (p.7, 124781/11)? How can such disincentives be avoided, either in the MFF or by the UK Government?***

The abatement calculation mechanism is set in a way to reduce the imbalance between the UK's share in overall EU expenditure and the UK's share in contributions. In areas that require co-financing from national budgets, we of course do not get an abatement on the domestic financing that match EU funds.

Nonetheless, in strict financial terms, the UK derives a net benefit from EU expenditure in the UK. As such, the UK Government does not consider the abatement a disincentive for implementation of EU funds and the UK Government intends to fully draw down its Structural Funds allocation from the 2007-13 programming period.

12. ***The Government has taken a strong position on the UK rebate. How does the Government propose to renegotiate the Commission's proposals for a new system of corrections? What is the Government's response to the Commission's consultation that found that there is "very heavy opposition among all categories of contributors against any kind of corrections, exceptions or compensations" (p.17, 12478/11 ADD 1)?***

The temporary lump sum corrections proposed by the Commission would remove the permanency of the UK's current abatement and threaten our long-term outcomes. It would mean giving up our permanent correction for a temporary one. As such, the proposal is not acceptable to the UK Government in its current form.

It is important to remember that the UK abatement is not the only budgetary correction. Germany, the Netherlands, Austria and Sweden pay a reduced share of the abatement and have a VAT correction. The Netherlands and Sweden also receive GNI corrections.

The UK abatement remains fully justified due to continuing expenditure distortions in EU budget. However, given its profile and visibility, the UK abatement seems to be used as an easy target by a number of people, often to deflect attention from more serious issues such as expenditure distortions.

Inequities in EU expenditure is common knowledge and an increasing number of Member States are not opposed to the principle of corrections in cases of *excessive budgetary burdens in relation to Member States' relative prosperity* (i.e. the Fontainebleau principle), as the Commission suggests. Notwithstanding, the UK Government will continue to make a strong case and defence for the UK abatement to other Member States and remind them that there is an automatic mechanism to reduce the UK abatement, namely comprehensive expenditure reform that will remove distortions in the budget.

I hope that these responses provide all that you need, but remain happy to provide further evidence should Committee require it.

I am copying this letter to William Cash MP, Chairman of the House of Commons European Scrutiny Committee; Alistair Doherty, Clerk to the Commons Committee; Jake Vaughan, Clerk to the Lords Committee; Stuart Stoner, Clerk to Lords Sub-Committee A; Les Saunders, Cabinet Office; Jay Amarasena, Dominique Lam, Mike Glycopantis, Brendan Bayley, Philip Dixon, HM Treasury.

1 March 2012

Anne E. Jensen MEP – Written evidence

The Committee seeks evidence on any aspect of this topic, and particularly on the following questions. We would welcome submissions that focus on only some of these questions.

1. Are the Commission's proposed expenditure ceilings appropriate, taking into account the pressures on so many Member States to pursue fiscal consolidation?

Members states' current consolidation efforts are necessary due to excessive spending between 2000 and 2010. In those 10 years national budgets rose by 62 % while the EU budget rose by 37 %.

Also, from 2010 to 2011 only five member states actually cut government spending (Portugal, Spain, Greece, Ireland and Germany). UK expenditure rose by 2.02 % [1][1].

Furthermore, EU spending is intended (and should be seen as such) to reduce national spending.

The level proposed by the Commission is based on the policies adopted by national ministers and the European Parliament. I do not agree to all policies and could see spending decreased on agriculture and structural funds. However, reducing expenditure should only be done, if it is accompanied by policy reforms within the relevant policy areas. If cuts are made on for instance agriculture, agricultural ministers should together with the European Parliament identify which programs should receive less funding.

2. What is the most appropriate basis for comparing the Commission's proposals with current expenditure?

The Europe 2020 plan. Europe 2020 was adopted by the European Council, and if the European Council can agree to scrap priorities from that plan, this should be the basis for lowering expenditure. Sectoral policy goals should determine expenditure.

3. What benefits, both financial and practical, will be derived from the Commission's proposals for simplification, particularly through the use of common strategic frameworks in research policy (Horizon 2020) and regional policy? Is the Commission's approach strategically justified, or is it a mere merging of funds? How can the approach be made to work in practice?

Simplification is highly necessary in research programs.

4. Is the proposed distribution of funds between and within the five main expenditure headings right? In particular, do the proposals offer enough to fulfil the aims of the Europe 2020 strategy? If you call for more spending in one area, please say whether you would expect a net increase or an offsetting saving elsewhere.

I believe the Commission has struck a very good balance. Personally I would like to see even more money for research, innovation, energy and infrastructure. Savings could be found on agriculture and structural funds (especially programs with low absorption rates).

5. Do the proposals live up to the aims set out in the Commission's *Budget for Europe 2020* of: focus on delivering key policy priorities; focus on EU added value; focus on impacts and results; and delivering mutual benefits across the EU?

I believe EU added value is most visible in relation to infrastructure, energy, research, education and innovation. However, agricultural spending can only be significantly reduced through a WTO agreement, and that is not on the cards. Also, having agricultural subsidies at EU level is far more desirable than having them at national level. The latter would lead to competition among member states on who would subsidise their agricultural sector more.

6. What is your assessment of the Commission's proposals for expenditure outside the MFF framework?

I prefer spending to remain inside the budget. This allows for better scrutiny of spending and adds to transparency on the general expenditure level. However, as the ITER project has in recent years been subsidised by funds originally allocated to FP7, I understand the necessity to leave it outside the MFF.

7. What is your assessment of the Commission's proposals to grant the EU more 'own resources' and of the choices advocated (a new VAT resource and/or a financial transactions tax)?

I believe that a new and more simple VAT would add to transparency and fairness. The current system of horse trading for rebates and derogations is a disgrace on member states. A simple system where member states contribute according to their relative wealth is the only dignified way to finance the EU budget.

8. What is your assessment of the likely impacts of the Commission's proposed restructuring of abatement mechanisms on the UK or other net contributors?

I believe abatement mechanisms have no place in a common international community.

9. What is your assessment of the innovative financing instruments proposed by the Commission?

Project bonds are an obvious solution to overcome financial challenges in large scale projects particularly relating to infrastructure.

10. What effects could the development of the Eurozone, in response to the Euro area crisis, have on the future EU budget?

December 2011

Hervé Jouanjean, Director-Generale, DG Budget – Oral evidence QQ 50-65

Evidence Session No. 3. *Heard in Public.* *Questions 50 -65*

TUESDAY 14 FEBRUARY 2012

Members present

Lord Roper (Chairman)
Lord Bowness
Lord Carter of Coles
Lord Dear
Lord Dykes
Lord Foulkes of Cumnock
Lord Hannay of Chiswick
Lord Harrison
Baroness Howarth of Breckland
Lord Maclennan of Rogart
Baroness O'Cathain
Lord Plumb
Lord Richard
Earl of Sandwich
Lord Teverson
Lord Tomlinson
Lord Trimble
Baroness Young of Hornsey

Examination of Witnesses

Mr Hervé Jouanjean, Director-General, and **Mr Johan Ureel**, of DG-Budget, European Commission

Q50 The Chairman: Perhaps I could begin by reminding my colleagues that when they first speak today during the public evidence session they should declare any interest that they consider relevant to the subject of the day's hearings. Mr Jouanjean, we are delighted that you have come from Brussels to be with us, accompanied by your colleague Mr Ureel, who is head of the unit in the DG-Budget that is dealing with the multiannual financial framework. There is a risk that we may have some votes during the course of the afternoon, in which case we will have to break for about 10 minutes while people go and vote and come back.

This session is being taken in public; it will be televised, and a transcript is being taken. A copy of the transcript will be sent to you and you will have the opportunity to make minor amendments to it, although it will be published online in an uncorrected form first. Given the

very large number of proposals related to the multiannual financial framework and the time constraints of the session, the Committee may wish to write to you following this meeting with further questions, which we would be very grateful if you could reply to in writing. I think that you would like to make a short opening statement.
Mr Jouanjean: Thank you, Lord Chairman and my Lords. First, let me say that it is an honour for me to be able to address the Select Committee on the European Union and to share with you some insights into the Commission proposals for the next multiannual financial framework.

At the moment, Europe is going through some particularly challenging times, and we all know about it. The economic situation and the uncertainties have led us to give particular attention to the medium-term future of the EU budget and to the investments that are required to help Europe to recover from this crisis as well as to meet the challenges of the future. When the Commission made its proposals for the future EU budget, it sought to strike the right balance between responding to the current economic crisis and the longer-term ambition of the EU budget to increase investment in a number of priority areas. Therefore, we have taken the overall ceilings of the financial framework of 2013 and limited ourselves to overall adjusting them for inflation. This means that the overall ceilings for the next multiannual financial framework will be constant in real terms. Further, we propose to keep the two major spending blocks, agriculture and cohesion, nominally constant—that is, not to adjust them for inflation. By freezing 70% of the budget, we create substantial savings, which can be used for increases in other policy areas and new activities. Among these are: the important increase for research and innovation; the creation of the new Connecting Europe facility; and increases for cross-border mobility in education and for strengthening external policies.

The share of the EU budget in payments, expressed as a percentage of EU GNI, is likely to decrease significantly over the next period to reach 0.94% of EU GNI by 2020. Its proposed average share as a percentage of EU GNI over 2014-2020 is 1%. In that context, I would like to recall that this share was 1.18% of EU GNI on average between 1993 and1999 and 1.06% of EU GNI as an average between 2000 and 2007 and between 2007 and 2013. This means that, whether we like it or not, the average share of the EU budget, as a share of the size of the overall EU economy, has gone down, and will continue to go down, by around 20% between 1993 and 2020. Looking at the evolution of the EU budget in comparison to that of national budgets, we can see that most member states have not decreased their spending; on the contrary, they have been increasing it. If we look at the figures between 2000 and 2011, we can see that national budgets in the EU increased by 62%, while the EU budget payments increased by slightly less than 42%.

An important distinction to bear in mind concerns the long-term nature of the goals of the EU budget when compared to those of national budgets. When we construct the architecture of the next multiannual financial framework, we are making choices reflecting a long-term vision of the EU economy that goes beyond the current difficult economic environment. Recent economic developments and, in particular, appraisals of the national economic situations in some member states show the necessity of making a link between the budgetary consolidation of national budgets and investments to foster future economic growth. This is exactly what the Commission proposals strive to do: stabilising the EU budget, on the one hand, so that national contributions are kept at a very moderate level, while on the other hand focusing on investments and expenditure geared towards the implementation of the Europe 2020 strategy for smart, inclusive and sustainable growth.

I would like to stress that when the Commission proposes to stabilise the EU budget on average at the 2013 level, it has made all efforts to strike the right balance between fully taking account of the pressure on national budgets and securing a distinct role for the EU budget in supporting investments which will condition the success of the Europe 2020 strategy.
It is true that those member states that are most affected by the crisis need to undertake serious structural reforms. But they also need public investments, which may be difficult to make given the precarious state of their public finances. Investments at the EU level, in particular, if coupled with the newly proposed macroeconomic conditionalities, can be an important way of bringing these countries back on track for growth. I invite you as well to look beyond the traditional headings and focus on how, throughout the budget, we will deliver the Europe 2020 goals. It is clear that we will need measures to bring back growth in the European periphery. Structural measures are not enough. We need a stable investment horizon.

It is also true that the EU financing system could play a significant role in the Union-wide budgetary consolidation efforts. With the progressive introduction of new resources, the need for member states' transfers from national budgets to the EU budget would diminish and member states would gain an additional degree of freedom in managing scarce national resources.

The time has also come to reform the system of rebates and corrections. In the new EU financing system that we propose, the logic of the so-called juste retour would be diminished. At the same time, in a spirit of fairness, one should avoid national contributions becoming disproportionate in relation to relative prosperity. That is why the Commission, following the Fontainebleau principle, proposes to contain the contributions of certain member states that would otherwise face a budgetary burden "excessive in relation to their relative prosperity".
Finally, the Commission proposal constitutes a middle ground—a proposal that seeks to finance EU priorities but in a fiscally responsible way. It is a reasonable proposal that takes the fiscal consolidation efforts of member states fully into account. Thank you very much for your attention.

Q51 The Chairman: Director-General, thank you very much indeed for giving us such a clear overview of the proposals of the Commission. Could I ask you one question which is to some extent related? As you said, the totals in the MFF are expressed as a percentage of GNI. I wonder what assumptions were made about future GNI growth in determining the spending aggregates.

Mr Jouanjean: We have made evaluations regarding the GNI growth on the basis of the last available evaluations at our disposal, which were 1.7% for that period[12]. This is what we have as a reference. Of course, we will have to revisit those assumptions in future, having in mind the evolution of the economic situation.

Q52 The Earl of Sandwich: Can we deal with the amounts that are off-budget? The Committee heard from Commissioner Lewandowski that he was in favour of the integration of the EU budget in future. However, the expenditure currently off-budget comes to 5.7% of

[12] Note by witness: 1.9% represents the consumption for real GNI growth for the period 2014 - 2020.

the MFF total. Could you remind us of the arguments for keeping these amounts outside the budget? How long will it take to make the transition?

Mr Jouanjean: A lot of emphasis has been put on something which, by and large, is just a repetition of what we had in the past. If I may say so, the price for the MFF, which is to a certain extent very rigid, is the need to have elements of flexibility, which we have had in the past. Those elements of flexibility have been maintained in the current proposal. They have been traditionally outside the multiannual financial framework. That is the first point. Here you find the instrument of flexibility, the solidarity fund and a few other instruments. We have added to that—and this is the only new element—the instrument to fight agriculture crises. The rationale for those instruments is the fact that they are there to face unexpected situations. They may be used; they may not be used. Therefore, they are not the same kind of expenditure as the expenditure within the MFF. So that is the first category.

The second category that is outside is the European Development Fund, which has always been outside the MFF, for historical reasons—one being that some member states were more involved in the development issue than others, due to their past. There has been a long-standing request from the European Parliament to bring the European Development Fund inside the multiannual financial framework, which would suit certain member states to the extent that it could reduce their contributions. But for a number of reasons, the Commission has considered that the situation is not right at this time to bring the EDF within that framework. But at the same time we have proposed to reduce again the difference between the contribution of member states according to the GNI key and the contribution of member states according to the current EDF, reducing the difference by 50%. That is what we have proposed.

The third category is ITER and the GMES, which is a novelty. Why have we put those two big projects outside the financial framework? For a very simple reason—because of the lessons of the past, the lessons of Galileo and the current lessons of ITER. The lesson of Galileo: following the failure of the public-private partnership, which the EU budget has been obliged to finance, at the expense of other research projects which matter as well for the future of economic growth and jobs in Europe. It has been very difficult for the Commission to find a balanced way out, while at the level of the Council of Ministers many member states wanted to impose a full redeployment of the resources. The second lesson of the past is the ITER project. We have been faced with terrible over-costs with that project. It is not a surprise for such a project, since we are in an area where everything is new—there are totally new technologies. Some elements are more costly, some less, and it is very difficult to maintain the cost. But the €1.3 billion that has recently been agreed on by the Council and the European Parliament will be financed to a large extent by redeployment within Heading 1a, i.e. at the expense of other projects of research. Therefore the message that the Commission wanted to pass to member states is the following: we are favourable to the big projects, which are necessary for the future of Europe and the European dimension is the right dimension for them. But at the same time, given the size of the European budget, you cannot impose on the European budget burdens which exceed by far our possibilities of flexibility within a structure that is extremely rigid. That is why we have made this proposal covering both ITER and GMES.

The last one concerns climate change, and here we have put a P.M. Here again it is because on one side we wanted to launch a signal to our partners in the world that we are willing to take action at EU level, both in the European Union and in the member states, and that we are ready to pool our money together. That needs an instrument that is outside the MFF. So this is the explanation, which I hope will satisfy the noble Lord.

Q53 Baroness O'Cathain: I am very glad that you mentioned ITER in the same breath as Galileo. We are deeply concerned that ITER is now outside the budget, because there is no problem in comparing Galileo and ITER in terms of the new science and technology. Galileo went horribly wrong; it was brought back in under the budget in order that governance—and that is the big thing, after the analysis—should be improved, and it was thought to be better in there. Why, we ask, can ITER not follow that and avoid having to learn the same lessons outside as Galileo did? Why can we not shove it into the budget so that the crossover in terms of governance, and even the ability to organise both projects under one certain head, would more or less guarantee that ITER would not go the way that Galileo went outside? That is the problem that we have in our Committee.

Mr Jouanjean: ITER in many respects is very different from Galileo, I agree. The problem for ITER is a governance problem as well, but the governance for ITER is different from the governance for Galileo, because for Galileo we have control: it is an asset of the EU and is taken as such in our accounts. In ITER, we are a very strong party to the international agreement. As you know, the governance issue was not directly in our hands; it was in the hands of the international body, and appropriate measures were taken to reform the ITER governance and change the staff, which needed to be moved. There have been very strong commitments from ITER to control costs, but the fact remains there is still a lot of uncertainty regarding the future costs of this project. We believe that we cannot take commitments regarding ITER which may have in future negative consequences on our objectives in the field of research and development. If ITER is paid for, that will mean less money for research laboratories in universities or other big projects, that would matter for our economy as well.
The Chairman: We may want to write to you with a supplementary question on that. It is certainly something that concerns us.

Q54 Lord Harrison: I, too, want to talk about budgetary flexibility—this time not on off-budget items but on intra-budget items. Could you explain to us the new landscape in terms of the flexibility that might operate for transfer of funds between headings, within headings and between programmes? In order to lead into that, could you explain what the current situation is? Has flexibility been exercised to the benefit of the budget in the current seven-year period? It would be very helpful to us to understand what is proposed for 2014-20.

Mr Jouanjean: Well, I will try to give you a few elements on that. As I said earlier, we have flexibilities that exist outside the financial framework. I will not come back to that except to say that in past years we have used in particular the instrument of flexibility to finance needs in the field of so-called Heading 4, and to some extent last year Heading 1a—Heading 4 to finance actions abroad when we have had crises that needed more action from our side, when there was not enough money available under that heading. That is one example. We have used the globalisation fund to finance actions with companies who have been victims of delocalisations. We have used the solidarity fund to finance actions to support certain European governments: in the case of L'Aquila, for instance, more than €500 million has been given; another instance is help with the consequences of weather conditions in the Czech Republic—that is another case that I have in mind. Those are almost normal management flexibilities.

You have also the classical flexibilities, via transfers within headings, which follow the rules of the Financial Regulation and, depending on the amount, have to be subject to the approval of the budgetary authority—that is, the Council and the European Parliament—as do the use of all the flexibilities that I mentioned before.

Then—and this is an instrument that we have had to use for Galileo and ITER—it is possible to move amounts between headings. There you touch on the distribution of the amounts between headings. Therefore, this implies that we change the basic elements of the balance of the MFF. Therefore, we need to have a special procedure for that, depending on whether it is a modification that is above 0.03% of GNI, or below. If it is below, under the previous rules of the agreement between the European Parliament and the Council, the decision could be taken on the qualified majority basis. Now we are in a kind of no man's land, in-between the previous system and the Lisbon Treaty system, which for a number of reasons has not been implemented in this area, and we need the unanimity of member states. We have used this for ITER to increase the ceiling for Heading 1a, drawing 1a funds from Heading 2—from agriculture in particular. Thank God, we have had a lot of money available, due to the underspending on agriculture; it has been available for Galileo and ITER. But also we have taken money from Heading 5 and administration, where we have made a lot of savings, which has helped us to find the resources for that. Here we have modified the ceilings. For the new MFF, we have tried to maintain those elements. We have reduced the number of headings, which will, we hope, help us to have a little more flexibility. We have also proposed to increase the amount of transfers that can be done by the budgetary authority within certain co-decided programmes. We have a possibility to move 5% and we have proposed to move to 10% for this. These are the elements that I can mention—to try to maintain what we have, to improve their functioning. We have proposed to increase the availability of the Emergency Aid Reserve, which is very much used to finance humanitarian aid. We have a line for ECHO, which in our proposals we have limited to a certain amount, which is an improvement compared with the past. But there are fluctuations, if I may say so, in the number of catastrophes in the world, and it may be that in certain years we will have to intervene more than in others.

Q55 Lord Harrison: Is there a rigid percentage limit to be applied in future against such a virement? Will you be asked to restrain any such virement of the budget?
Mr Jouanjean: The instruments per se have a limit, which is in the agreement for the European Globalisation Fund. Under the current situation, we have €500 million, if my recollection is correct. So once we have reached €500 million, it is over—we cannot use it. These are the amounts which are added to our proposal to show that there is a base figure. But in the globalisation fund, for instance, we are far from having used the totality of the funds made available. We have used a lot under the Emergency Aid Reserve, because we have had a number of catastrophes, such as in Ethiopia in recent months, when we have had to intervene and provide food aid, which has to be financed. If there is no more money available on the appropriate lines, we need to find this. The big limitation is that applicable to the transfer between headings, where we have the 0.03% limit. This is really the limitation that matters. Going above 0.03% in the previous system meant unanimity; we hope that in the future system we can come back to a flexible system below 0.03%, but above that we enter untested waters, and I have my doubts that under the present circumstances member states would be willing to go above 0.03%.

Q56 Baroness Howarth of Breckland: We wondered how much the problem is compounded by the basic framework of the budget not matching the planning for programmes towards 2020 and whether you are going to be able to manage those changes in the budget as time goes on, so that the problems about moving between headings may not be as great if the basic budget is strengthened. I know there are all sorts of political issues around that, but I wondered if there was any movement towards it.

Mr Jouanjean: I am not so sure that I have understood your question well.

Baroness Howarth of Breckland: If we are moving towards a programme for 2020 that corresponds more to the Europe 2020 strategy and is somewhat different from the existing programme in nature, the budget therefore needs to move towards matching that programme. I wondered how that transition was going to take place, because clearly you are not going to go for baseline budgeting. You will be moving forward on the budgets because of the political implication of some of the lines. Is that one of the problems that compounds the issue in terms of flexibility of the budget?

Mr Jouanjean: Yes. From a legal point of view, in the European Union—and, in many cases, in member states as well—there cannot be expenditure without legal basis so, under the current financial framework, we have a specific legal basis for each and every programme. What have we tried to do under the so-called Horizon 2020 programme? We have tried, as we have done for the CSF as well, to revisit the architecture. Why? Because, as a matter of fact, many programmes these days are the result of a kind of piling-up of initiatives and there was a need to revisit all that and reorganise, to make it simpler and more attractive for beneficiaries. This is what we have tried to do for Horizon 2020.

We have, as you must have seen, basic legislation where we have the various dimensions which are proposed. But this will be a different legal base as compared with the previous programmes, so there will be no overlap. The contracts signed under Framework Programme 7 will continue under Framework Programme 7. The contracts which will be signed under Horizon 2020 will be under this legislation and will, in particular, benefit from the possible action in conjunction with certain funds. I do not know whether this is the question you wanted to ask, but I think that this is the beginning of the explanation. I can maybe give you more details if you wish in writing.

Q57 Baroness Young of Hornsey: Director-General, European Added Value is an important criterion for evaluating spending at EU level, but often it can be quite difficult to quantify. Can you tell us what the specific criteria are for determining whether the EU is actually adding value in its spending, and how these criteria have been applied to the MFF proposals?

Mr Jouanjean: Yes. As a very well known French politician, who lived in London for a while, said: "C'est un vaste sujet." Well, there are various angles to look at the question of added value. Of course, first there is a political dimension and there is, I would say, an economic dimension. I will not talk here about the political dimension, but it is key because in certain areas the very fact that the European Union intervenes as such is of enormous added value.

If we turn to the added value from an economic point of view, if I can give a definition, I would say that the European Added Value is the value resulting from EU intervention, which is additional to the value that would have been otherwise created by member state action alone. That is what guides us. How do we translate this into our daily life as bureaucrats in Brussels? How do we give an answer to that? We have introduced a number of criteria, which are established mainly through the impact assessment which we present to the Council and to the European Parliament together with our proposals. We have asked the Commission's services to answer this kind of question. For instance, would action by member states alone, or the lack of EU action, significantly damage the interest of member states, or would action at EU level produce clear benefits as compared with action at the level of member states?
As we mentioned in the previous question, in the case of ITER it is clear that there is justification for action at EU level. We have a financing problem, but the objective as such is clear. It is the same for Galileo. For instance, if you take our proposal on the European infrastructures, clearly here we are talking about the missing links in between member states. We are not talking about internal investment; we are talking about those investments which, under the current market conditions, will not be financed because there is not enough interest on one side of the border or the other. But there is a joint interest to do it, so these are criteria which we use to assess whether there is European added value.

Q58 Baroness Young of Hornsey: Some of those criteria that you have mentioned can be more flexibly interpreted than others. Could you tell us: have any items of EU expenditure from previous MFFs been, as it were, failed on the basis that they have not lived up to that European Added Value test?

Mr Jouanjean: I would say that the evolution of our policies shows where we believe that the European Added Value test has brought some necessary changes. As a matter of fact, if I might try to summarise, I would say that we have tried to improve the efficiency. Therefore on actions where we have decided to maintain our activity, which I believe is most of our actions—because these actions have been decided by the Council of Ministers and the European Parliament—what we have tried to do is to make sure that the action is focused and effective. For instance, in what we have proposed for the cohesion policy, you have the possibility to spread the money all over. While you can have doubts as to the efficiency and effectiveness of those instruments, if you create a link between our objectives for 2020 and the use of money, then you can really improve the added value of the European funds. That is why we have tried to limit the intervention of the EU to a number of thematic issues, which are very limited when we talk about the richer regions but wider when we talk about the less rich or the poorest regions. Therefore the evolution has not been necessarily in eliminating this expenditure, because it responds to a need—as expressed by the Council of Ministers and which we have proposed to it and to the European Parliament—to better spend this money, having in mind our objectives of jobs and growth.

Q59 Lord Dykes: Director-General, thank you very much for your explanations. I think we were told a number of times last year by Commissioner Lewandowski that evolution is better than revolution in these matters. It was of course at a time of considerable tensions being imposed, sometimes rather unfairly, on the idea of the European budget by the national member states while dealing with their very painful austerity programmes of varying degrees, as we know. There are arguments about the percentage increase in the overall EU budget being perhaps excessive against that background, although I think there were some extra projects built into those calculations which justified certain real-terms expenditure increases. How do you feel about the proposition, at a time of particular national austerity, which is very fierce in member states, including here, France and other countries, and with the calls that you get in the national press from member states for a freeze on MFF spending, that the EU would be better served by a zero-based budgeting approach?

Mr Jouanjean: I would say that there are two dimensions to your question. First, at the EU level, are we in a position to implement such an approach? My answer would be negative, to the extent that the way we have to take decisions in the Council—that is, by unanimity—has a lot of impact on the kind of policy that we have to develop. Secondly, this does not mean that this kind of question cannot be at the centre for those who conceive the policy—that is, in the Commission. From that angle, I would say that we do our best to follow the kind of questioning that is behind the zero budgeting approach.

I come back to the point that I mentioned earlier about the impact assessments which we produce. At the end of the day, the question that we have to address is: do we do it or not? On zero budgeting, say, if we were to start from scratch, what would we do? It is a bit different in our context, but we still have the question with us in the impact assessment: do we do it or not? Is it better to do it at EU level or not? That is the answer I would give on that.
My colleague Johan Ureel advises me that this is what we have applied in the fisheries sector, where we have come to the conclusion that the scrapping of vessels does not bring any added value for the EU as such, and therefore had to be discontinued. This is an example which I can imagine.

Q60 Lord Dykes: The European Union budget is unique in the whole of the EU system because its receipts equal its payments and sometimes the expenditure is below the actual appropriation originally decided, unlike the member states, which tend to have very substantial deficits of one kind or another. Do you feel that officials like you are being unfairly criticised by outsiders in the national press in different countries because the EU budget system has a resultant effect, rather than a new creation effect, throughout the member states' budgets, decided by national Parliaments, and therefore you are being unfairly criticised for it and the system as well? Maybe you do not mind.

Mr Jouanjean: I mind a lot. Yes, the EU budget is a very unique budget, as you rightly say. It is a budget which is mostly about investment, with extremely limited administrative expenditure, a little more than 5%. In other words, 94.5%, let us say, goes back to member states. Very often, public opinion does not know that what goes to Brussels comes back. The EU budget is constructed on the basis of some form of contract between member states, called the multiannual financial framework. Why do we have this contract? We have it because it appeared in the past that the yearly budget negotiations were so difficult that the stability needed for investment was at stake and was endangered. Therefore, the idea was, "Let's have a multiannual financial framework", and the period of seven years was chosen. The decision was to have commitment appropriations on the one side, and payment appropriations on the other. Commitment appropriations are very important because they give certainty to beneficiaries, whether they are member states or private beneficiaries, that there will be something for them at the end of the day. Secondly, it helps to ensure a fair balance among member states because we have the problem of the so-called juste retour. The fact that you have balance as a negotiation on the commitment of appropriations brings a lot to member states in terms of their own public finance. That is established through the ceiling for commitment appropriations—the global ceiling, the ceiling by headings and the

global ceiling for the payments. It is true that for Treasuries, whether in the UK, in my own country, France, or in other countries, what matters is what goes out of the budget—the payments.
During the previous financial frameworks, we noticed, and we notice these days, that the profile of payments is, in a sense, disconnected from the profile of commitments because we are mostly talking about investments. Therefore, when you agree to finance an airport, a highway or telecommunications equipment, there is a period of time needed between the moment when you start the project, when you get the green light, and when the project is finalised. Therefore, there is a kind of back-loading of the payments. Very often we read in the press that those funds are not used. Recently, at the time of the European Council, we could read in the newspapers that in cohesion 30% was available, but it is not true. In the beginning, for instance with cohesion, the financing decision is taken and then member states have a number of tranches which correspond to the duration of the MFF. Of course, they sign progressively with contractors when the programmes are being finalised. Therefore, we have this differentiation.

The problem that we have today—this is where I come to your question about our frustration—is that, in a sense, yes, we are frustrated because it is very easy to put on the back of the European Commission and European institutions the fact that payments are increasing at a time when our national budgets have to face austerity. I am the first to understand this very well, but the fact is that that is the result of commitments undertaken six years ago. Therefore, the question is: can we say today to those around the table in Brussels—the member states, the heads of states and of Governments—"Look, what we signed in 2005 is not valid any more"? It is a big political problem. It is the view of the Commission that *pacta sunt servanda*, so we have got to have the money. The payment appropriations that have been put in the EU budget in 2011 or 2012 may be a serious problem because we may run out of money, not because there is a wrong policy from our side, but because there is some kind of mechanism that leads us there. In this context, let me repeat that we are financing mostly investments for the future.

Q61 Lord Foulkes of Cumnock: Director-General, you are very eloquent in your plea, but decisions by national governments made six years ago have been overturned completely. They have long-term investment programmes, infrastructure programmes, which are not going ahead. Their budgets are not zero, but they are being reduced, and you are asking for an increase. You are also asking for a total reform of your own resource structure at a time when we have riots on the streets of Athens and 50% youth unemployment in Spain. Do you not think that it is provocative of the Commission to continue in the way that it has been going for the past six years, increasing its expenditure, reforming its structure and getting more money through own resources when these things are happening on the streets of some of the countries of Europe?

Mr Jouanjean: I understand your question perfectly. I have to give you an answer. The duty of the Commission is to implement the instructions the member states have given it. The instructions of the member states have been to implement the multiannual financial framework. The Commission, as I said earlier, proposes to the Council the consequences of what the member states have decided. The Commission makes its proposals within the ceilings that have been decided by the member states. This is part of a contract between the member states.

I totally agree with you. First, on expenditure and own resources, our proposal was to stabilise expenditure at the 2013 level until 2020. Not a single national government has undertaken such a commitment for its own public finance. We have made that proposal. We stabilised expenditure until 2020 on the basis of 2013. Secondly, it is true that we have proposed to reform the own resources system, because this system does not work. We have not proposed to reform the own resources system to bring more money into the EU budget. We have stabilised the budget.

Q62 Lord Foulkes of Cumnock: But our Government have said, and we agree with this, that to reform your own resources at this time is a distraction. Would it not be better to wait until the economies of the countries of Europe have stabilised?

Mr Jouanjean: That is a view; others have other views. We believe in particular that bringing new own resources for the EU budget which, like the customs duties, would not necessarily go through national budgets, would be an immense help in reducing national deficits. We can have different views of the same issue. I understand your viewpoint, but we have made a different analysis. We believe that the system of financing the EU budget as it now stands is poison for the European Union because governments, as we witness today, do not think in terms of what Europe can bring to them, and I understand that. They just think in terms of how they can reduce their contribution to the EU budget because they need that money at home. Here we come back to the question of European Added Value. We believe that what we propose brings something to the whole EU. This is the dilemma we are in. It is very difficult for politicians to sort out. I believe that it needs vision. What do we want to do together? Do we believe that what we are putting on the table is good in the medium term for employment and growth? That is what we have tried to achieve through the Commission's proposals, having in mind that, at EU level, in terms of the structure of the budget, there are certain constraints, which we all know. They are part of our family problems, if I may say so.

Q63 Lord Teverson: I think the EU should get on with changing the way that own resources work. It seems an utterly opaque system that none of our citizens understand. There is always an excuse not to get on with it. I would rather be critical from the other end in that the proposals are not a lot more understandable to citizens, let alone parliamentarians and member states, than the present system.

I would like to return to the new VAT system of own resources. What progress has been made on this proposal? How will it overcome the differences in national VAT arrangements that have led to complex adjustments in the current system?

May I just ask one supplementary question now? The nearest thing that we have to an EU tax will be the EU emissions trading system when we auction the majority of those permits. That could have been an own resource. It is like a carbon tax in many ways. Can you confirm to us that all that income will be redistributed to national governments, given the fact that, I think, national quotas will disappear during that period as well?

Mr Jouanjean: The system as it stands is extremely complicated, very difficult and very opaque. We consider that what we are currently tabling is a major simplification and is a fair way of doing things because we will eliminate all the specific arrangements that have progressively been introduced. There are extremely complex statistical corrections. What we propose is to take the products that are subject to the standard VAT rate in each member state. For instance, in the UK, children's clothing, which is subject to the zero rate, would not be considered. We would take as the basis for calculation products that are subject to the standard VAT rate throughout the member states of the EU—a totally fair treatment. We have proposed that a certain amount—1%—could be used as an own resource for the EU budget. It is very simple. You just take the products. You can do it easily, and we would have a system that is far more transparent and easy to calculate. We also believe that this would help in further developing the internal market.

On CO_2, decisions have been taken by the European Council. There is no question of the Commission coming back to this. At one stage, we thought that it would be a good candidate for being an own resource for the EU. There have been divergent views within the European Council on this issue, and the consequences are those that we know.

Q64 Lord Carter of Coles: Director-General, the question that I would like to ask is on the common agricultural policy. Before doing that I declare an interest as a farmer in receipt of CAP payments. The planned expenditure on direct payments to farmers and to market expenditure is forecast to be £281 billion, which I think is 27% of the total envelope. Yet we feel that that does not seem to be consistent with the Europe 2020 agenda, which concentrates its spending on smart, sustainable and inclusive growth. We feel that we would like to be pluralists. There is a sort of lack of ambition in the CAP and we are curious as to how that can be justified, particularly given the economic conditions and climate throughout the EU.

Mr Jouanjean: Let me make a few points on this. First, you will allow me to disagree with you when you say that what we have proposed—the reform of the CAP—is not in line with the 2020 objectives. As a matter of fact, we have introduced in the reform a number of elements to ensure a more sustainable management of natural resources. In particular, I would like to draw your attention to what we have decided on the green issue. I would also like to draw your attention to the research element, which has been increased as well. Clearly, we all know that there are divergent views around the table in Brussels on what the CAP is about. For the Commission, the CAP remains a strategic policy, and it is the only policy that finances 70% of the EU expenditure in the field of agriculture. We believe that it helps to produce products that are safe and healthy. We know that from the amount of inquiries from our fellow citizens. Having said that, I would also like to underline the fact that we have proposed a freezing of the expenditure on the CAP. As a matter of fact, this means that agriculture expenditure will have been frozen for a period of 14 years, from 2007 to 2020. Bear in mind the fact that, during this period, we have had a very important enlargement and that the new member states have benefited from the direct payments—this is in our proposal for 2014-2020—at the expense of the so-called full member states. It is also a very important element and the result of all this is the fact that the share of agriculture will decrease during the period in a relatively substantive way by more than 5 points down to about 33% or 34% from 39% or 40%. That is quite an important point. This is the situation on the table today. I would like again to insist on the fact that we are a union of 27 countries with different views on agriculture and we need to find a balanced solution in this area.

Q65 Lord Plumb: I also declare my interest as a farmer in receipt of funding under both Pillar 1 and Pillar 2. I say that deliberately because they are very different funding for different interests. It is perfectly obvious, and I accept fully, that the proposals that we have at the moment are fairly radical. I doubt very much whether the finished product is going to

be as it is now tabled. There will be changes but, nevertheless, I think the framework for possible agreement has already been made. As a farmer, I make the point straightaway that farmers prefer a market price rather than subsidies. The difficulty with that, of course, is if you rely on market prices you are going to have instability in the price mechanism, going up and down depending on the volume of the product at any one particular time. We have seen radical changes in the past—the fact that we took 10% of the land out of production. Now, of course, we are proposing taking 7% out of production. That was a measure that was effective, but it was very expensive. A radical change also was the implementation of quotas. That, again, I think was expensive. Then, of course, we moved to the direct payment, as well as the Pillar 2 payments for environmental purposes. That has been successful, but, as far as we are concerned in this country, a lot of the money there has gone not to farmers but to consultants or to other purposes—improving village life and so on. I am totally with that. I think that is the sort of thing that can happen—and money coming in from Pillar 2.
The changes are there but, having seen the growth of the food industry in this country, it is not always understood that 14% of the workforce is in the largest food manufacturing industry in this country. It is 14% of the total workforce so it is big business. We are in a situation where we want to see growth, in the difficulties we are facing—growth of a product that can be produced more and will be produced more, I am quite sure, with techniques and so on. That opportunity, therefore, has to be there. Really the question I think we pose is how we put in security—security of supply and security for the nations of Europe—and also, recognising the world situation at the moment, how we can achieve stability in price without a safety net to provide support, or at least put some stability in the base of the market, hopefully facing a market which is going to provide a return. That, of course, means higher food prices and, in the present circumstances, that is not very commendable to the consumers of any one of our countries.

Mr Jouanjean: It is a difficult equation.

Lord Plumb: It always has been.

Mr Jouanjean: On the one side, citizens want cheap products; on the other side, they want security of supply and they want quality. Bearing in mind the future trend for demand of food products in the world, we believe that it is absolutely key to maintain production in Europe which is capable of feeding people. This does not mean that we do not import. We are the largest importer of food products. I remember when I was a trade negotiator in Geneva, at the time of a trade policy review mechanism, being attacked very violently by my fellow ambassador from Argentina. My answer was: "Look, when you have a good customer, and we are your first client, in business we treat those clients very well." We have at this stage, and if we look at the recent food crisis, which has very severely touched a number of developing countries, we must learn lessons from that. We need to have a strong agriculture in Europe but, and this is the objective of the proposal that we make, we must continue taking steps towards a more competitive agriculture vis-à-vis its competitors in the world.
The Chairman: Does Lord Dykes have a final question?

Lord Dykes: It has been covered.

The Chairman: Director-General, I would like to thank you very much indeed on behalf of my colleagues, for the very full answers you have given us on a range of questions. The evidence we have taken today will certainly be of great use when we come to consider and prepare our report. As you know, there are other topics which, if we had had time, we would have liked to discuss. But we will, if we may, write to you about those and about one or two other matters. Again, we are extremely grateful to you, and to Mr Ureel for coming from Brussels, in order to give us such detailed replies to such an important range of questions. Thank you again.

Hervé Jouanjean, Director-Generale, DG Budget – Supplementary written Evidence

European Financial Framework from 2014

1. Since 2011, estimates of future economic growth have been reduced significantly. Based on your most recent calculations, what percentage of EU GNI would the total envelope of €1,083 billion amount to?

Any recalculation on the basis of the currently available data would be obsolete by the time of the June 2012 European Council, since these data would be superseded by the upcoming Spring 2012 macro-economic forecast this May. In order not to unnecessarily complicate the discussions, the Commission has therefore decided not to release any intermediate updated figures before the publication of this new Commission Spring 2012 forecast.

2. Could the governance of ITER not be improved by including it in the MFF, alongside Galileo, rather than retaining it 'off-budget'? Is it impossible to find the necessary level of flexibility within Heading I?

The governance of ITER should not be negatively affected by the fact that its financing is being placed outside the MFF. The legal framework and implementation structures remain unchanged:

- The ITER project is conducted under the terms of the international Agreement on the Establishment of the ITER International Fusion Energy Organization for the Joint Implementation of the ITER Project (the "ITER Agreement")[13] between the European Atomic Energy Community (EURATOM) and 6 other Parties: China, India, Japan, Korea, Russia, and the USA. This legally binding agreement established the ITER Organization with full international legal personality, as the body responsible for the joint implementation of the ITER project. The Commission represents EURATOM in the different ITER instances, in particular the ITER Council, the project's major governing body.

- The EU contribution to the ITER project is managed through the European Joint Undertaking for ITER and the Development of Fusion Energy ("Fusion for Energy", or "F4E"), established by Council Decision on 27 March 2007[14]. The Members of Fusion for Energy (Euratom, the 27 Member States and Switzerland) are all represented in its Governing Board.

- The Commission proposal for a Council Decision on the adoption of a Supplementary Research Programme for the ITER project (2014-2018)[15] is based on Article 7 of the Euratom Treaty. The Euratom Treaty limits the duration of Research Programmes to a maximum of five years. According to the ITER Agreement, the ITER project will have an

[13] OJ L 358, 16.12.2006, p.62
[14] OJ L 90, 30.03.2007, p.58
[15] COM(2011) 931 final of 21.12.2011.

initial duration of 35 years (i.e. until 2041); thus, subsequent Council decisions will be needed to continue to fund the EU contribution to this project, as is the case for all the activities financed under the Euratom Treaty.

- Euratom will continue to participate in the governance, management and staffing of the ITER Organization and Fusion for Energy, in accordance with the provisions of the agreement establishing the ITER Organization and the Council Decision establishing Fusion for Energy.

- The proposed Supplementary Research Programme provides that it will be implemented by the European Commission, which can delegate tasks to the "Fusion for Energy" Joint Undertaking, in accordance with the Financial Regulation based on Article 322 of the Treaty on the Functioning of the European Union.

As to whether it is possible to find the necessary level of flexibility within Heading I, the Commission has taken its decision to propose that the ITER project be financed outside the MFF on the basis of the experience made under the current MFF: despite all efforts by the partners to the ITER agreement to keep costs under control, the implementation of the project resulted in a financing gap of 1.3 billion euro in commitment appropriations for the years 2012 and 2013. A Commission proposal to provide for this additional financing by a mix of redeployments within Heading 1a and a revision of the MFF[16] led to protracted discussions between Parliament and Council, which definitively failed at the beginning of 2011. A new Commission proposal made in April 2011[17] again led to protracted discussions which resulted in a partial agreement at the end of 2011, including a revision of the MFF[18] but leaving a gap of EUR 360 million in commitment appropriations to "be made available in the 2013 budget procedure within the MFF commitment appropriations ceilings making full use of the provisions laid down in the Financial Regulation and in the IIA of 17 May 2006, excluding any further ITER-related revision of the MFF"[19].

Experience clearly shows that the strict financial discipline imposed on the financial framework, and its lack of flexibility, does not provide enough responsiveness for such projects. In the case of ITER, it risks undermining the Union's commitments towards the project and vis-à-vis its international partners.

The proposal to place ITER and GMES outside the MFF is therefore intended to ensure that the Union can continue fully to meet its international commitments whilst taking account of the additional pressures that this type of large scale projects place on the EU budget, given the limited size of the latter. The time span needed for realising such projects exceeds by far the duration of a financial framework. They involve a strong commitment from Governments from both within and outside the Union. They cannot be planned and implemented in the same way as other EU spending programmes which fit the strict rules and limitations applying to the financial framework.

The Commission feels comforted in its choice by the resistance many Member States have been showing to any proposed increase of the level of flexibility of the MFF whilst at the same time exerting strong pressure to bring expenditure ceilings further down.

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[16] COM(2010) 403 final of 20.7.2010.
[17] COM(2011) 226 final of 20.4.2011.
[18] OJ L 4, 7.1.2012, p. 12.
[19] Joint conclusions on financing of ITER of the budgetary trilogue meeting of 1.12.2011.

3. The Committee has previously recommended that the Climate Action Commissioner should have overall responsibility for the success of the 'mainstreamed' approach to climate change policies within the MFF. Can you clarify how these policies will be overseen under the Commission's current proposals?

Based on a thorough impact assessment, the Commission proposed the mainstreaming approach to climate action which is an important dimension of the Europe 2020 strategy. As elaborated in the Multiannual Financial Framework (MFF) Communication "A budget for Europe 2020", climate concerns will be reflected across policies and instruments in view of a low-carbon, resource efficient and climate resilient economy that will enhance Europe's competitiveness, create more and greener jobs, strengthen energy security and bring health benefits.

Regarding the question of political responsibilty in the Commission, the principle of collegiality obviously applies. It means that all Commissioners can contribute to decisions, and all share collective responsibility once initiatives are adopted. The Commission is a team working together effectively to ensure the coherence and consistency of Commission policies.

Mainstreaming implies that all Commissioners and Commission services in their policy making and implementation will have to take climate aspects into consideration. This is already largely reflected in the sectoral legislative proposals and it will remain a horizontal challenge for the next Multiannual Financial Framework period. On the level of implementing climate-related expenditures within the sectors, the so-called Authorizing Officer by delegation – as a rule the competent Director General - is responsible for sound financial management and signs legally binding contracts with recipients of funds.

Beyond these general remarks, let me try to respond to the core of your question which also alludes to the risk that "where everybody is responsible – no one is responsible". This is indeed the background against which the Commissioner for Climate Action has a particular role to fulfil. The present Commissioner for Climate Action has been tasked by the Commission President with a cross cutting responsibility for developing, in particular, adaptation to climate change inside the EU and for working with other Commissioners to ensure that an appropriate climate dimension is present in all Community policies. To help her fulfil these responsibilities, she has under her authority a DG for Climate Action.

And indeed, in the preparations of the MFF proposals the Climate Action Commissioner and her services have paid special attention that climate change issues are properly reflected in the policy proposals and the ensuing draft legislation. Besides being closely involved in the policy formulation stage, she will also follow up on how the policies will be translated into concrete action throughout the multiannual expenditure programmes. Tracking climate related expenditure across the EU budget is part and parcel of this task. Without prejudice to the role and portfolio that the next Commission president will assign to the next "climate action commissioner", the horizontal task of overseeing the follow-up and respect of the mainstreaming will remain a quintessential element of his/her job.

Finally, I would like to take the occasion to recall that the continuous commitment and dedication of many actors are necessary to make the "challenge of mainstreaming" a success "in the field". In the realm of shared management, the Member States and the final beneficiaries have a particularly important role to play as well.

4. In particular with regard to cohesion policy, is there a risk that realigning current policies to fit the Europe 2020 framework will divert programmes from their traditional mission? Will orientating cohesion policy towards Europe 2020 result in all Member States receiving sizeable amounts from this budget line, and does it make sense for richer Member States to receive such funds?

There is indeed a strong link in the proposal between cohesion policy and the Europe 2020 Strategy, but the specific aims of cohesion policy are maintained. Cohesion policy thus provides essential EU public goods that enable EU countries and regions to concentrate resources on improving economic, social and territorial cohesion and meeting Europe 2020 targets.

In the proposal, provisions are introduced for the ring-fencing of funds with a view to enhancing the thematic concentration of the funds. Nonetheless, this streamlining is focused principally on more developed and transition regions. For the ERDF, for example, in these regions at least 80% of the funds would be dedicated to research and innovation, SME competitiveness and the shift to the low carbon economy. For the less developed regions, the percentage for the focus of the funds is set at only 50%.

The thematic concentration on the EU 2020 strategy does not have an impact on the calculation of the regional and national allocations. Under the Commission proposal EU cohesion policy funding will remain concentrated on the regions and Member States lagging behind, to more than 70 % of the total of the resources available for the Investment for growth and jobs goal (which makes up 95.52 % of the total resources available for cohesion policy, the remaining being allocated to territorial (cross-border, transnational and interregional) cooperation. About 16 % of the resources shall be available to more developed regions and 12 % to the proposed new category of intermediate regions (whose GDP per capita ranges between 75 % and 90 % of the average GDP of the EU-27).

As demonstrated by evaluations, cohesion policy has had a considerable impact also in regions other than those lagging behind as an incentive to mobilise each region's potential and reorient spending towards investments, strengthening their potential for growth and jobs. The added value of the partnership principle and of medium-term programming has been widely recognised, notably in the context of the public consultation carried out under the Budget Review, which has shown overwhelming support for the continuation of EU-wide assistance from the funds whilst fully respecting the principle of concentration.

5. How will the new Common Strategic Framework for structural funds allow flexibility for regional and local objectives to be set?

Each region has its territorial specificities and its distinct needs, which will determine its response and contribution to the achievement of Europe 2020 objectives, through the process of selection of thematic objectives and investment priorities to be supported by the different Funds.

Integrated solutions will be encouraged, bringing together different EU Funds to address challenges such as demographic imbalances, increased exposure to globalisation, climate change and environmental degradation (including pollution, loss of biodiversity) and energy security. Specificities of territorial areas should thus be taken into account in the programming of the Funds, translating Europe 2020 into specific territorial contexts.

In accordance with a multi-level governance approach (involving *inter alia* competent regional, local, urban and other public authorities), the partners will be involved by Member States in the preparation of Partnership Contracts.

6. Is there a danger that macro-conditionality within cohesion funds might unfairly impact organisations that are not themselves responsible for national fiscal policies?

The achievement of the growth and jobs related objectives of cohesion policy depends on sound fiscal and economic policies. In their absence, investments co-funded by cohesion policy will not provide the expected impact. This is the reason why the Commission has proposed to align cohesion policy with the economic governance of the EU. Against this background, the proposal of the Commission provides the possibility to redirect EU funds with a view to address economic problems of a Member State. This process will be gradual starting with amendments to the Partnership Contract and to the programmes in support of Council recommendations.

Where, despite the enhanced use of EU funds, a Member State fails to take effective action in the context of the economic governance process, the Commission will have the right to suspend payments and commitments. It needs to be underlined that the trigger for suspension is not that a Member State faces macroeconomic difficulties, but that the Council decides that a Member State has failed to take the necessary corrective actions. All decisions on suspension must also be proportionate. The Commission will take into account the economic and social situation of the Member State concerned and the impact of the suspension on its economy. The suspension will be lifted and the funds made available again as soon as the Member State takes the necessary actions. These provisions will limit the risk that macroeconomic conditionality will negatively impact on organizations that are not themselves responsible for national fiscal policies.

7. The budget of the Connecting Europe facility, taking into account the €10 billion earmarked elsewhere in the MFF, has increased by 400%. If, in negotiations, the Connecting Europe facility has its budget pared down, what do you see as the most important elements to preserve? If the MFF is to boost growth, does one of the three limbs (energy, transport or telecommunications) offer greater scope for this than others?

– The Commission does not intend to be drawn in a discussion on which of the proposed priorities should be scaled down. Our proposals have been examined in details during the preparatory process with national authorities. Therefore they are not the result of bureaucratic dreams but the result of in depth analysis. We consider that we have made a serious proposal which fully takes into account the context of budgetary austerity. We want to make the substantial savings obtained by effectively freezing the major traditional spending blocks in nominal terms available for investments at Union level which we consider are indispensable for realising the Europe 2020 strategy and a more forceful role of the Union on the international stage.

– The three areas covered by the Connecting Europe Facility – transport, energy and telecommunications – all belong to those top priorities. The fact that the proposed budget would be six times higher than in the current period should be assessed in the context that there has been almost nothing available for investments in energy networks until recently and with a view to the huge investment needs in all these three areas:

- 1.5 trillion euro for sustainable transport networks by 2030, amongst which 250 million euro by 2020 for the highest priority corridors ("core network");

- 1 trillion euro of investment needs by 2020, amongst which € 200 billion of investment into gas pipelines and power grids and storage facilities of EU relevance;

- up to €270 billion to bring ultra-fast broadband to all households by 2020.

– Whilst most of these investments are to be shouldered by the private sector and Member States, the Union budget is crucial in triggering investments needed for realising modern, cross-border networks at EU level.

– For example, without the stimulating effect of the CEF, market plans to invest no more than €50 billion by 2020 in ultra-fast broadband.

– And €100 billion of investments into the mentioned energy investments of EU relevance are at risk of not being delivered due to obstacles linked to permitting and financing difficulties.

– Such networks are not only needed for strengthening the internal market and its competitiveness, meeting our climate targets, and securing energy supply throughout Europe. They can generate growth in the geographic environment, and substantial savings by rationalising transport, energy and telecommunications networks which are artificially constrained by national boundaries.

– € 10 billion are proposed to be earmarked from the Cohesion Fund for transport projects under the CEF. This aims at making sure that Cohesion Fund spending is effectively directed towards the transnational and cross-border priority corridors. Without taking these € 10 bn into account, which are taken from the cohesion budget, the increase is less than four times what is available in 2013. Again, this should be assessed in comparison of the estimated needs.

– As an example, private and public partners in the UK are investing about £ 15 billion in one major transport infrastructure alone (with a contribution of £ 7.1 bn from the

Mayor of London and of £ 4.7 bn from the Government's Department for Transport, and a € 1 billion loan from the EIB): Crossrail, the new East-West railway link which will run through and under central London and is to be completed by 2018. This is the scale of ambition we should have throughout Europe!

8. The Horizon 2020 instrument has also seen a substantial budget increase. Given that funding for innovation is included in other budget lines, is there further scope to consolidate spending and avoid duplication of administrative costs and efforts? For instance, could the €60 billion of funding earmarked for innovation within cohesion funding be consolidated within Horizon 2020 and offer savings in the overall budget?

The Commission's proposal has responded to many of the issues raised in your report of April 2011. However, your question shows that we need to better explain our approach to the funding for innovation in our proposals. Indeed, it is one of the main objectives of the Horizon 2020 proposal to bring the previously dispersed funding mechanisms in support of innovation under a common roof. Horizon 2020 brings together all existing Union research and innovation funding, including the Framework Programme for Research, the innovation related activities of the current Competitiveness and Innovation Framework Programme and the European Institute of Innovation and Technology (EIT).

It is certainly not our intention to duplicate costs and efforts – quite the reverse. This framework programme will be implemented through one specific programme (the current FP7 covers five different specific programmes), thus bringing more flexibility, increasing transparency and facilitating implementation of cross-cutting actions. In addition, we propose a single set of rules applicable to the funding of all actions undertaken by participants under Horizon 2020, including Euratom, regardless of the body (Commission, agency, joint undertaking, EIT or other) granting financial assistance.

Finally, we have also proposed major simplification measures in favour of beneficiaries of Union funds, notably in the areas of cost eligibility rules, where we have proposed simplified cost methods, and grants, where we encourage the recourse to lump sums, unit costs and flat rates, as well as the broader acceptance of the beneficiaries' cost accounting practices. This should in turn lead to a simplified control system that is designed to take account of the minimised risks of errors resulting in particular from the simplification measures in the field of grants.

9. The Heading V Administration budget incorporates funding for EU institutions, such as the External Action Service and the Court of Justice. Are there separate ring-fenced budgets within Heading V for these institutions?

The annual budget of the European Union clearly identifies in 10 separate budget sections a ring-fenced budget for each European Institution[20] or body[21]. The amounts concerned are adopted each year by the budgetary authority (the European Parliament and the Council).

[20] European Parliament (Section 1), European Council and Council (Section 2), European Commission (Section 3), European Court of Justice(Section 4), European Court of Auditors (Section 5)
[21] Economic and Social Committee (Section 6), Committee of the Regions (Section 7), European Ombudsman (Section 8), European data-protection Supervisor (Section 9), European External Action Service (Section 10)

The Commission section of the budget is specific, as it includes all the operational appropriations of the Budget, as well as the administrative expenditure concerning the Commission of course, but also the European Schools and the budget related to pensions for staff from all European Institutions and bodies. The nine other sections of the budget exclusively concern administrative appropriations related to the concerned institution or body.

Heading V of the financial framework represents the maximum amount foreseen for all administrative appropriations.

10. Do the administrative procedures for 'off-budget' programmes and funds differ from the procedures that apply to 'on-budget' ones? If so, how and why?

A distinction needs to be made between three different cases:

- The instruments for flexibility
- ITER and GMES
- EDF

The instruments for flexibility

The four existing instruments for flexibility (Flexibility Instrument, Emergency Aid Reserve, Solidarity fund, EGF) and the proposed new instrument (Reserve for crises in the agricultural sector) are not off-budget instruments. They have always been placed outside the MFF because of their very purpose, which is to keep the EU budget responsive to emergency situations and unforeseen circumstances. *They are mobilised in case of need and then entered into the EU budget "over and above the ceilings" (i.e. without altering the MFF).*

The procedures for their mobilisation and entering into the budget are well described in the draft proposal for a new IIA[22].

ITER-GMES

As regards ITER, according to the Commission proposal, the contributions to the programme will be made to the EU budget (in proportion to their GNI) as 'assigned revenue', managed by the Commission. The project would continue to be managed on the EU side by the European Commission and "Fusion For Energy" (F4E), the European Union's Joint Undertaking for ITER and the Development of Fusion Energy. The current financial and staff rules would continue to apply and the Commission would continue to represent the EU in the different ITER bodies.
The functioning of F4E, its management and staffing as well as the general technical and administrative support are also covered by the Supplementary Research Programme for the ITER project.

As regards GMES, as far as funding is concerned, the Commission proposes to opt for the creation of a specific GMES fund, similar to the model chosen for the European Development Fund, with financial contributions from all Member States, based on their

[22] COM(2011) 403 final, points 10-14

Gross National Income (GNI). The management of the fund would be delegated to the European Commission.

As far as governance is concerned, the European Commission proposes to remain responsible for the political supervision and the overall coordination of the GMES, on behalf of the Union. The Commission proposes to delegate certain management tasks (e.g. evaluation, negotiation and follow-up of contracts) to the European GNSS Agency (GSA). These tasks would however not include operations.

For operations, the European Commission proposes that the technical coordination of service is entrusted to several European entities, depending on their knowledge and expertise (e.g. the technical coordination of the land monitoring service could be entrusted to the European Environment Agency, the technical coordination of the atmosphere monitoring service could be entrusted to the European Centre for Medium-range Weather Forecasting, the technical coordination of the emergency management service could be entrusted to the European Emergency Response Centre, etc.).

European Development Fund

The European Development Fund (EDF) is the main geographic instrument for financial and technical instrument that is funding agreements between EU on one side and ACP (African, Caribbean and Pacific)-countries as well as overseas countries and territories (OCTs) on the other side based on the Cotonou agreement. The EDF is financed outside the framework of the EU Budget by financial contributions by the Member States, with different cost-sharing formula or contribution keys from those used to determine the expenditure of the general budget.

Due to this background the administrative procedures differ from those applicable to the general budget in the following ways:

- The Member States retain a direct influence on the financial measures through the Council of Ministers and Committee of Ambassadors, set up by the Cotonou Agreement, and through the EDF Committee in the Council, which issues an opinion prior to any Commission decision on country or regional strategy papers and on annual action programmes prepared jointly with the ACP partners..

- The European Development Fund, unlike the other European funds (EAGGF, ESF, ERDF, Cohesion Fund, etc), is a true financial instrument separate from the general budget. However it has neither a legal personality nor management autonomy since its administrators are the European External Action Service (EEAS), responsible for programming, and the Directorate-General Development and Cooperation (DEVCO), responsible for implementation.

- Unlike the management of the general budget, the principle of annuality is not applicable to the implementation of the EDF. After commitment, expenditure may be executed over several calendar years.

- A large proportion of the EDF expenditure is implemented at the local level through the decentralised management method; by a national authorising officer designated by each ACP country and under the supervision of a Commission delegation. Given the specificities of the EDF rules, the EDF accounts are not consolidated with those stemming from the use of the general budget. Nevertheless, the financial statements are drawn up in conformity with International Accounting Standards (IPSAS/IAS) and Generally Accepted Accounting Principles (GAAPs).

- The implementing rules for revenue and expenditure under each EDF are the subject of a specific Financial Regulation, as far as possible aligned with the Financial Regulation applicable to the Union general budget. The EDF's revenue and expenditure, like operations under the general budget, are subject to Commission's internal controls and examined by the European Court of Auditors which regularly devotes a special chapter of its annual report to the management of the EDF. Both the EU Council and the European Parliament exercise their supervisory role through the discharge procedure.

11. How similar is the proposed corrections system to that which existed for the UK between 1980 and 1984? Is there a risk that this new system will encounter the same difficulties and result in an inequitable outcome that is inconsistent with the Fontainebleau conclusions?

At the time, the issue of corrections was limited to the United Kingdom (although Germany started to highlight its position as the main contributor to the Community budget from 1981 onwards).

The correction system that existed for the UK between 1980 and 1984 could hardly be called a 'system'. It consisted of a series of ad-hoc Council conclusions[23] which:

- were not based on any particular underlying logic;

- did not provide any medium or long term predictability for treasury planning purposes;

- and above all: required a renegotiation on a more or less annual basis.

Whether this system resulted in an inequitable outcome is a political appreciation which is difficult to substantiate with figures more than 30 years later. However, the main disadvantage would appear to have been the ad-hoc nature of the yearly negotiation and the resulting uncertainty in terms of medium-term treasury planning. Moreover, since these corrections were not incorporated in the own resources decision (as is the case for the corrections existing today) they were not submitted to the procedure of adoption by unanimity and ratification by national parliaments, a procedure which provides a much higher degree of reliability for beneficiaries of corrections.

In stark contrast, the lump sum approach proposed by the Commission provides:

- a coherent approach across all Member States, providing equal treatment in the light

[23] Council conclusions of 30 May 1980 – Council conclusions of 25-26 October 1982 – European Council conclusions of 21-22 March 1983 – Council Reg. 2744/80 of 27 October 1980 – Council Reg. 624/83 of 15 March 1983 – Council Reg. 625/83 of 15 March 1983

of both the relative prosperity of each Member State (which is clearly not the case today) and the expenditure structure agreed for the next MFF;

- is fixed for the entire period of the MFF and is embedded in the ORD, providing perfect predictability and assurance to all Member States.

The risk of producing an inequitable outcome inconsistent with the Fontainebleau conclusions remains very limited, since the lump sums proposed by the Commission are consistent with the maximum expenditure ceilings included in that same proposal. The risk of inequity, if any, is therefore mainly on the side of those Member states who have to finance the lump sums: a possible under-execution of the budget as compared to the maximum ceilings would results in lump sums which de facto 'overshoot'.

Whether the lump sums proposed are sufficient is a matter of political appreciation and negotiation. Recipients of lump sums will try to maximize the amounts while those who have to finance them will seek to minimize their financing contribution. This issue will only be settled in the final stage of the negotiations.

The Commission has recognized that under the current circumstances corrections are inevitable in order to avoid an inequitable outcome for a number of Member States. These corrections should provide transparency, simplicity, predictability and equal treatment. Finally their global financing cost should remain reasonable.

Janusz Lewandowski, Commissioner for Financial Planning and Budget, European Commission – Written evidence

Replies to call of evidence:

1. Are the Commission's proposed expenditure ceilings appropriate, taking into account the pressures on so many Member States to pursue fiscal consolidation?

The Commission proposals impose a strict budgetary discipline for a long period of time: until 2020. In commitment appropriations, the proposed amount of € 1025 billion expressed in 2011 prices corresponds to the agreed ceiling for the year 2013 (€ 146.4 billion in 2011 prices) multiplied by seven. The ceiling for payment appropriations (€ 972.2 billion), which is mainly a consequence of decisions on the level of commitments taken in previous years, is slightly higher than the corresponding 2013 ceiling (€ 137.8 billion in 2011 prices) times seven.

For a period of seven years the EU's multiannual financial framework would thus be restricted to a nominal increase of 2% per year. The 2% fixed deflator is much lower than the current average inflation in the EU. The ceilings proposed by the Commission therefore not only offer stability but also predictability, which is a crucial element for both potential recipients of multiannual programmes as well as national treasuries.

The stabilisation of the MFF in real terms will mean that the economic growth of the EU for the period 2014-2020 will not even partially be translated into additional public expenditure at EU level. Consequently, the share of the MFF in commitment appropriations, expressed as a percentage of EU GNI, is likely to decrease significantly over the period under consideration to reach the equivalent of 1.03% of EU GNI by the year 2020 compared to 1.16% in 2011 and 1.12% in 2013. As for payment appropriations, the situation is even more modest: as a share of GNI, payments go down to 0,94 % by 2020.

It would be difficult to find any examples of a similar budget discipline being imposed ex ante on a national budget until the year 2020. More importantly, the EU budget is fundamentally different to national budgets insofar as it to a large extent supports investments. Budgetary consolidation of national budgets will be impossible without investments which help implementing the Europe 2020 strategy for smart, inclusive and sustainable growth. The Commission has sought to strike the right balance between fully taking account the pressure on national budgets and securing a credible role for the EU budget in supporting the Europe 2020 strategy.

Finally, an agreement on the multiannual financial framework for 2014-2020 not only requires reaching a unanimous Council agreement, it is also necessary to obtain the consent of the European Parliament under Art 312 of the Lisbon Treaty. In this respect, it is important to remember that the European Parliament in its vote on the report of the "Special committee on the policy challenges and budgetary resources for a sustainable European Union after 2013 (SURE)" called for a MFF of 1.11% of GNI.

2. What is the most appropriate basis for comparing the Commission's proposals with current expenditure?

The current multiannual financial framework 2007-2013 was agreed on 17 May 2006, after Member States reached a unanimous agreement at the December 2005 European Council under the UK Presidency. That agreement was reached after long and difficult negotiations. The 2013 ceiling is an integral part of it. As the endpoint of the current MFF the Commission considers that the 2013 ceiling represents the benchmark against which to measure the size of the next MFF. As explained above, the Commission proposes to keep this level unchanged in real terms for the average of the years 2014-2020.

The Commission insists on the importance of respecting the MFF agreements, which are enshrined in a different logic than the annual budget cycle. The value added provided by the stability and the predictability of the ceilings cannot be overestimated. The alternative would be to fall back on the logic of the annual budget approach, with expansive budgets possible during the years of economic upturn and restrictive budgets imposed during recession years. This system was in place at the EU level until 1988 with negative results, in particular with Council and European Parliament frequently failing to agree on the budget. The complexities of the EU budgetary decision making process coupled with the specific multiannual nature of the majority of EU budgetary expenditure have made everyone understand the value of the MFF; nobody should want to return to the situation prior to 1988.

3. What benefits, both financial and practical, will be derived from the Commission's proposals for simplification, particularly through the use of common strategic frameworks in research policy (Horizon 2020) and regional policy? Is the Commission's approach strategically justified, or is it a mere merging of funds? How can the approach be made to work in practice?

The Commission proposes to bring together the three main existing research and innovation programmes (FP7, CIP, EIT) into a single Common Strategic Framework for Research and Innovation (CSF), Horizon 2020, and in the case of regional policy to bring together the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund (CF), the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF) under a Common Strategic Framework. This will eliminate fragmentation and ensure more coherence among different instruments, including with national programmes. As regards research and innovation, the Common Strategic Framework will be closely linked to key sectoral policy priorities such a health, food security and the bio-economy, energy and climate change. The European Institute for Technology will be part of the Common Strategic Framework.

The Commission considers that the CSF-approach ensures greater coherence between the sources of funding and a much sharper and targeted focus on the priorities of the Europe 2020 Strategy. Enhanced coherence and streamlined funding schemes with harmonised rules and procedures should increase the impact and added value of EU funding and make access to funding easier and more attractive for beneficiaries.

Meaningful simplification of the use of EU funding will require the combined efforts of all the institutions in reviewing both the general rules in the Financial Regulation and the sector-specific rules now proposed by the Commission. The simplification efforts at EU level will not produce their full effect if they are not accompanied by parallel efforts at national level, for instance in the area of shared management.

4. Is the proposed distribution of funds between and within the five main expenditure headings right? In particular, do the proposals offer enough to fulfil the aims of the Europe 2020 strategy? If you call for more spending in one area, please say whether you would expect a net increase or an offsetting saving elsewhere.

The long-term growth priorities have been taken up in the Commission's proposals for the next MFF 2014-2020. A large part of the budget will be aimed at getting people into work and the economy growing, tied in with the Europe 2020 strategy for smart, sustainable and inclusive growth. In the current times of fiscal austerity it is obvious, that when the Commission calls for more investments in some policy areas, savings need to be made elsewhere, which is why it has proposed to operate a nominal freeze on both the Common Agriculture Policy and the Structural Funds for the period 2014-2020. The Commission has proposed in a realistic and responsible way to stabilize the EU budget at 2013 level in real terms.

The Commission proposes fairly limited changes to the structure of the current MFF, aimed in particular at giving more emphasis to the priorities of the Europe 2020 Strategy. In that respect, the main changes proposed relate to: the merger of the current sub-headings 1a and 1b into a single heading 1 ("Smart and Inclusive Growth"); and the creation of a sub-ceiling under the new heading 1 for economic, social and territorial cohesion, including the "Connecting Europe Facility".

The following examples covering more than 80% of the proposed MFF funding gives an overview, how the Commission's proposals contribute the aims of the Europe 2020 strategy:

The Commission proposes a CAP reform, which would make it more modern, greener policy, equipped to contribute actively to the goals of the Europe 2020 strategy by unlocking economic potential in rural areas, developing local markets and jobs, accompanying the restructuring of agriculture and supporting farmers' income to maintain a sustainable agriculture sector throughout Europe. In financial terms, the Commission proposed to allocate €281.8 billion for Pillar I and €89.9 billion for rural development (in 2011 prices).

The Commission proposes to allocate €376 billion for economic, social and territorial cohesion and link them more closely to Europe 2020 objectives particularly through a Common Strategic Framework and thematic concentration. The Commission also proposes the creation of a Connecting Europe Facility to accelerate the infrastructure development that EU needs. It will have a dedicated budget of €40 billion, supplemented by an additional €10 billion ring-fenced for related transport investments from the Cohesion Fund.

As concerns investments in research and innovation, the Commission proposes to increase funding (from €55 billion in 2007-2013) to €80 billion (+46%) for the new Common Strategic Framework for Research and Innovation – with a further significant amount of spending on research and innovation, around €60 billion in line with the 2007-13 period, will come from the Structural Funds. Moreover, education and vocational training should be strengthened with a proposed budget allocation of €15.2 billion (+68%).

Finally, the Commission proposes significant further effort to respond to the "20/20/20" climate/energy headline target set in the Europe 2020 strategy. With regard to climate-related expenditure the Commission proposed to increase its proportion of the total EU budget to at least 20%. Furthermore, the LIFE programme should be continued as a dedicated instrument for the environment and climate action, with a proposed budget allocation of €3.2 billion for 2014-2020.

5. Do the proposals live up to the aims set out in the Commission's Budget for Europe 2020 of: focus on delivering key policy priorities; focus on EU added value; focus on impacts and results; and delivering mutual benefits across the EU?

The programmes and instruments in the MFF proposals have been redesigned to ensure that the EU budget will implement the principles mentioned above. The programmes and instruments must be clearly linked to the commonly agreed goals and priorities of the Europe 2020 Strategy.

The EU budget brings added value through initiatives with a pan-European dimension that cannot be implemented without a European perspective. The Commission staff working paper on EU added value which accompanies the Commission's proposals for the next MFF the added value of the interventions under the EU budget and presents many examples of how this works in practice in the Member States (please see details SEC(2011) 867 final).

The Commission has proposed to introduce stronger conditionalities for the next MFF. Conditionalities will be introduced into programmes and instruments in order to sharpen the focus on policy outcomes rather than on inputs. A very good example in this respect is the Cohesion policy where the Commission proposes to conclude a Partnership Contract with each Member State. These contracts will set out the commitment of partners at national and regional level to use the allocated funds to implement the Europe 2020 strategy, a performance framework against which progress on commitments can be assessed. The Contract will set out clear objectives and indicators and establish a limited number of conditionalities (both *ex ante* and linked to the achievement of results so that they can be monitored), and include a commitment to give yearly account of progress in the annual reports on cohesion policy. In order to strengthen the focus on results and the achievement of the Europe 2020 objectives, 5% of the cohesion budget will be set aside and allocated, during a mid-term review, to the programmes have met their milestones in relation to the achievement of the programme's objectives related to Europe 2020 targets and objectives.

The MFF proposals also encourage more use of innovative financial instruments as they can provide an important financial stream for strategic investments. By leveraging investments and working with the private sector it is possible to magnify the impact of the EU budget, enabling a greater number of strategic investments to be made, thus enhancing the EU's growth potential.

6. What is your assessment of the Commission's proposals for expenditure outside the MFF framework?

In presenting a second table regrouping the elements put outside the MFF the Commission wanted to be fully transparent in giving a complete overview of the potential financial impact of all EU budgetary expenditure. This has generated some concerns and possible misunderstandings.

In reality, almost all of the elements included in the additional table exist already today, mostly outside the MFF.

Nothing changes for the European Development Fund, which the Commission proposes to remain outside the EU budget (as it is today) until the expiration of the Cotonou agreement.

No change as well for the four existing "flexibility instruments": the Emergency Aid Reserve, the European Globalisation Adjustment Fund, the European Union Solidarity fund and the Flexibility instrument. They have always been placed outside the MFF because of their very purpose, which is to keep the EU budget responsive to emergency situations and unforeseen circumstances. The only new instrument proposed here is a Reserve for crises in the agricultural sector. The need for the CAP to rely in future even more on the market than is the case today should be coupled with the development of new risk tools able to respond to emergency situations; this is why the Commission is proposing to set up outside the MFF a reserve for crises in the agriculture sector.

All flexibility instruments can only be activated with the agreement of the Council and the European parliament.

Finally ITER and GMES are indeed two elements which today are financed within the MFF and which the Commission has proposed to finance outside the EU budget. The proposal to place ITER and GMES outside the MFF is intended to ensure that the Union can continue fully to meet its international commitments whilst taking account of the additional pressures that this type of large scale projects place on a EU budget which is very small compared with the growing financial needs of many EU policies. The time span needed for realising such projects exceeds by far the duration of a financial framework. They involve a strong commitment from Governments from both within and outside the Union. They cannot be planned and implemented in the same way as other EU spending programmes which fit the strict rules and limitations applying to the financial framework.

7. What is your assessment of the Commission's proposals to grant the EU more 'own resources' and of the choices advocated (a new VAT resource and/or a financial transactions tax)?

The proposal to modify the mix of own resources to finance the EU budget is underpinned by a series of considerations. During the intensive consultation process in preparation of the EU Budget Review in 2010, it became obvious that the current financing system suffers from a number of weaknesses:

First, the financing system is extremely opaque and very complex. This raises issues in terms of public and parliamentary scrutiny of the EU financing.

Second, except for the traditional own resources (customs duties and agricultural levies), EU resources have no link to the EU policy objectives. Own resources to finance the EU budget should support commonly agreed EU policy objectives, in the same way as the customs duties accruing to the EU budget derive from to the EU customs union and policy.

Third, national budgets and the EU budget compete for the same tax revenues. The way the EU budget is financed (mainly with contributions of the Member States to the EU being seen as mere expenditures in the national balance sheets) inevitably creates tensions. This, in turn, leads to the progressive development of increasingly complex correction mechanisms and increases the pressure to pre-determine where certain categories of expenditures will be made.

Last, the recent financial crisis creates a new context which needs to be taken into account when designing the future architecture of the EU budget. The EU financing system could play a significant role in the Union-wide budgetary consolidation efforts. With the progressive introduction of new resources the need for Member States transfers to the EU budget would diminish and Member States would have an additional degree of freedom in managing scarce national resources.

It is therefore reasonable to envisage well-grounded alternatives to the existing system, noting that the introduction of new own resources is not an argument about the size of the budget; it is a debate about the right mix of resources. As a matter of fact, it is proposed in parallel with a stabilisation of the EU budget in real terms.

The analysis of the various potential candidates identified in the EU Budget Review as potential new own resources gave rise to a substantial technical work. It highlighted the following key elements:

Financial transaction taxation would constitute a new revenue stream, therefore potentially reducing the existing contributions from Member States, giving an extra room for manoeuvre to national governments and contributing to general budgetary consolidation efforts. Action at EU level could prove more effective and efficient than action at the Member States level, and it could play a role in reducing the existing fragmentation of the Single Market. Considering the complex cross-border interactions at play in the financial sector, the national incidence of the FTT would be particularly difficult to establish, thus justifying a supra-national approach. An EU initiative in this area would constitute a first step towards the application of a FTT at global level. As shown by the example of the UK stamp duty, an FTT with a limited geographical scope is feasible without leading to massive re-location of economic activity.

The development of a new VAT resource creating a genuine link between national VAT revenues and the EU budget would be desirable. While revenue collection would rely exclusively on Member States administrations, such a system could provide significant and stable revenues to the EU with limited administrative costs for national administrations. This resource would not create a new VAT system parallel to the national ones, nor would it impose new charges on businesses or citizens. The introduction of a new VAT resource could form part of a broader reform initiated by the Commission's Green Paper on the future of VAT. Broadening the tax base, reducing the scope for fraud, improving the administration of the tax and reducing compliance costs in the context of a broad reform of VAT, could deliver important results and generate new revenue streams for the Member States. A fraction of the gains derived from this initiative could be attributed to the EU level, and these could be further increased as the VAT system improves its performance.

8. What is your assessment of the likely impacts of the Commission's proposed restructuring of abatement mechanisms on the UK or other net contributors?

The currently existing correction mechanisms consist of a mixture of elements with no foreseen end-date (the UK abatement and the rebates on the rebate for DE, NL, SE and AT; the 25% collection cost on traditional own resources) as well as some corrections limited to the period 2007-2013 (reduced VAT rates of call for DE, NL, SE and AT; a lump-sum reduction of the GNI contribution for NL and SE).

These corrections have grown over time as the result of successive negotiations, which have resulted in ever increasing complexity and reduced transparency. In the absence of a coherent approach to this issue, more Member States can be expected to demand some form of correction or compensation during the upcoming negotiations. It is the Commission's assessment that this ad hoc approach to budgetary corrections has reached its limits and should be replaced by a new, coherent system.

The Commission proposes to return strictly to the 1984 Fontainebleau European Council conclusions which state that 'any Member State sustaining a budgetary burden which is excessive in relation to its relative prosperity may benefit from a correction at the appropriate time.' This means that the concept of an 'excessive budgetary burden' is recognised under two conditions:

(a) <u>in relation to relative prosperity</u>, which means that the notion of 'excessiveness' of the budgetary burden of any Member State will depend on that Member State's affluence (measured as GNI per capita in PPP). Richer Member States should be expected to bear a somewhat higher budgetary burden than less affluent ones.

<u>(b) at the appropriate time,</u> which means that the correction is subject to the specific nature and structure of EU budgetary expenditure. In practice, the correction should be linked to a specific MFF, to be reviewed and renegotiated for each subsequent MFF which could potentially present a fundamentally modified expenditure structure.

This approach would ensure transparency and simplification. Contrary to the current system, the proposed lump-sums would be very easy to understand and explain. Better democratic scrutiny would be the result.

More importantly, the Commission proposal assures fair and equal treatment across all Member States since a horizontal methodology for calculating the lump-sums would be applied.

In short, the proposed new system of lump sums is considerably more simple and transparent than the current mechanisms. Contrary to the current mix of corrections it also ensures transparency, fairness and equal treatment of Member States.

9. What is your assessment of the innovative financing instruments proposed by the Commission?

The Commission has recently adopted on 19 October 2011 a Communication on "A new framework for the next generation of innovative financial instruments – the EU equity and debt platforms" (COM(2011)622 final), which presents the Commission's view on the future of innovative financial instruments in EU budget spending.

The innovative financial instruments proposed by the Commission include instruments which provide equity/risk capital, or debt instruments (such as loans or guarantees to intermediaries that provide financing to a large number of final recipients who have difficulties in accessing finance, or risk sharing with financial institutions in order to increase the volume of finance and hence the impact resulting from the EU budget intervention).

The Commission assesses that innovative financial instruments have the potential to play an important role in achieving the Europe 2020 Strategy's objectives of smart, sustainable and inclusive growth, as well as the capacity to attract funding from other public or private investors in areas of EU strong interest but which are perceived as risky by investors (e.g. high growth and innovative business activity). In the current MFF 2007-2013, EU spending through innovative financial instruments represents less than 1% of the overall EU budget. The Commission considers that this percentage could be increased in the next MFF 2014-2020 and innovative financial instruments could provide an important new financing stream for strategic investments, supporting long-term, sustainable investment at a time of fiscal constraint.

The Commission has proposed a specific chapter on financial instruments in the Financial Regulation, setting out the overall principles for the budgetary management of such instruments. In parallel, the Commission will work on the more detailed rules and guidance in order to have this in place when the Financial Regulation has been agreed by the co-legislator.

10. What effects could the development of the Euro zone, in response to the Euro area crisis, have on the future EU budget?

The EU budget is a budget for all Member States, embedded in a MFF unanimously agreed by Council and subject to the consent of the European Parliament, and financed by own resources, laid down in a unanimously agreed own resources decision subject to ratification by all national parliaments. This leaves absolutely no room for the emergence of a 'budget-within-the-budget' exclusively for the Euro zone. Under the Lisbon Treaty the EU budget must and will remain a budget for all Member States.

However, the financial and economic crisis followed by the emerging sovereign debt crisis has had a significant impact on the EU budget, in particular on its role as loan guarantor. This role, which up till now had been relatively limited and mainly restricted to external lending (Macro Financial Assistance, EIB external lending mandate), has been significantly modified and expanded with the extension of the Balance of Payment Facility for non-euro zone Member States to € 50 billion and the creation of the European Financial Stability Mechanism of € 60 billion.

13 December 2011

London Government Association – Written evidence

1. The Local Government Association (LGA) is a voluntary membership body and our 422 member authorities cover every part of England and Wales. Together representing over 50 million people and spending around £113 billion a year on key public services that deliver local ambitions for people and places.

Local Government's role in the EU budget

2. The LGA recognises that the EU's spending plans, totalling over €1 trillion, can make an important contribution to help councils to achieve their goals. We see EU programmes as particularly valuable when they directly support councils' 'place shaping' activities in the local area. This includes economic development in both urban and rural contexts; support for education, training and skills programmes; support for SME development; support for research and innovation; the protection of the environment; and helping to combat poverty and social exclusion.

3. Equally, local government is pivotal in helping the EU achieve its development objectives. Councils deliver EU projects, shape EU investment priorities, and manage parts of EU programmes. The Government's commitment to giving local communities a greater say over spending in their areas must be made a reality by allowing local government to play a greater role in delivering the EU spending proposed for 2014-2020.

4. The LGA has been particularly active in engaging with Government, the Committee of the Regions and the European Institutions to ensure that the voice of local government in England and Wales is reflected as the budget negotiations progress.

5. LGA would be willing to submit any oral evidence to the Inquiry as required to elaborate on the views expressed in this response.

Are the Commission's proposed expenditure ceilings appropriate, taking into account the pressures on so many Member States to pursue fiscal consolidation?

6. The European Commission has a number of key priorities it wants to focus on as part of the EU 2020 strategy, and a number of interests to balance in proposing an EU Budget to deliver them.

7. Leaving aside the debate on the overall EU Budget ceilings, the LGA is concerned that - whatever the level – communities across the UK benefit suitably from EU spending. We are therefore pleased that the UK will continue to benefit from the major European programmes in the future, although express some reservations that Cohesion Policy, which councils use to deliver invaluable growth and skills projects, will receive less as a share of the overall EU Budget than it does currently.

8. Furthermore, given the fiscal consolidation and tightening of public budgets around Europe, the EU needs to think hard about simplifying the process for spending various programmes across all expenditure lines. Similarly, many of its programmes must be

matched by some level of co-finance, this will be more difficult to achieve across expenditure lines and across all places of Europe in the next programming round. To combat this, the EU should consider approaching programme co-financing in a more flexible way.

What is the most appropriate basis for comparing the Commission's proposals with current expenditure?

9. Expenditure comparisons between 2007-13 and 2014-2020 must take account of 'real terms' change brought about due to inflation. We note that the Commission has suggested a budget frozen in real terms at current levels.

10. The Inquiry should be particularly alert to the creative presentation of the new €40bn Connecting Europe Facility as boosting the cohesion budget available for regional development. By adding in this facility in its presentation of the funds available for cohesion policy the Commission is attempting to mask a budget cut for structural funds (ERDF and ESF) of 3%: €347bn currently, being reduced to €336bn for 2014-20.

11. The use of a Common Strategic Framework (CSF) in regional policy is the first step towards better aligning and integrating all EU funds with a territorial dimension. It is to be welcomed, although it is not clear how the administrative proposals for each fund makes better coordinated spending on the ground a reality.

What benefits, both financial and practical, will be derived from the Commission's proposals for simplification, particularly through the use of common strategic frameworks in research policy (Horizon 2020) and regional policy? Is the Commission's approach strategically justified, or is it a mere merging of funds? How can the approach be made to work in practice?

12. LGA survey work during 2011 suggests a better integration of different EU programmes could make funds simpler to understand and easier to access for councils and other beneficiaries. This should help to ensure a greater use of the funds in the UK: it may lead to concrete financial benefits in terms of improved absorption.

13. We particularly welcome the integration of rural development funds (EAFRD) into the CSF, as rural development spending under the Common Agricultural Policy (CAP) is not currently always well coordinated with structural fund (ERDF,ESF) spending in rural areas. Government should explore what benefits may be gained by moving rural development funds out of agricultural expenditure (heading 2) and into the regional development budget heading (heading 1).

14. To make the approach work in practice the CSF must however go beyond aligning funds at the strategic level and actually ensure common implementation practices and procedures between the funds during implementation.

15. A CSF approach for the various research and innovation programmes is also welcomed for the same reasons as outlined above.

Is the proposed distribution of funds between and within the five main expenditure headings right? In particular, do the proposals offer enough to fulfil

the aims of the Europe 2020 strategy? If you call for more spending in one area, please say whether you would expect a net increase or an offsetting saving elsewhere.

16. The LGA welcomes the fact that the budget headings have been renamed to more closely reflect the Europe 2020 priorities. We believe the Europe 2020 approach is helpful in ensuring the EU focuses its budget on key priorities.

17. It is important however that Europe 2020 sets a flexible framework within which interventions can be tailored to the specific needs of places, and that local partners are fully engaged in the process for negotiating and delivering those objectives.

18. LGA regrets that the opportunity has not been taken to place all EU funds promoting territorial development under a single heading. In particular placing rural development and fisheries funding under heading one would result in a more coherent budget structure.

19. The LGA notes that the Common Agricultural Policy at €372bn remains the largest single area of proposed spend compared with the €336bn allocated to the structural funds for regional development. Greater parity between these two areas of spend to ensure a robust settlement for cohesion policy would be of greater benefit to councils and UK beneficiaries as a whole.

20. The EU's proposals to ensure a 'greening' of the CAP, so that it better contributes to Europe 2020 objectives of environmental protection and climate change should be fully supported.

21. *Europe 2020 & key policy priorities.* It is questionable whether the scale of funding proposed can truly match the political aims and ambitious set out in 'A Budget for Europe 2020'.

22. *Focus on impact & results*. The LGA notes the proposed introduction of 'conditionalities' which could lead to a greater focus on achieving results and better communication of those results to the public.

23. We support the introduction of only those conditions into the approval of EU programmes which would assess actual technical and administrative capacity. We do not therefore support conditions which require the implementation of EU legislation in other fields.

24. The requirement to draw up given strategies, plans or measures must not mean that the EU funds are conditional upon the subsequent implementation of such plans, particularly those which are not co-financed by EU funds. Such an approach would infringe upon the rights of local self-governance.

25. The LGA underlines that outcomes and targets must be agreed in conjunction with local authorities and any new monitoring and reporting burdens should be kept to a minimum.

26. The suspension of funds should be a last resort. It should only apply under certain

clearly-specified measurable conditions and only if the expected results are seriously underachieved.

27. The move towards measuring *outcomes* should see the current system of measuring detailed inputs and *outputs* reformed accordingly. This would avoid a doubling of the administrative burden.

28. We underline the strong opposition of the LGA to any form of 'macroeconomic conditionality' that would see a discontinuation of EU funding to local projects due to economic decisions taken by national governments.

29. The whole approach relating to the new performance framework in EU funds requires clearer and better explanation to delivery bodies and stakeholders as to how it will operate in practice.

What is your assessment of the Commission's proposals for expenditure outside the MFF framework?

30. The LGA does not believe as a principle that major areas of EU spend such as the European Globalisation Adjustment Fund (EGF) the Global Monitoring for Environment and Security (GMES) programme, and the Agricultural Reserve, together with other instruments accounting for €58bn of Union expenditure, should be financed outside the scope of the MFF. This is a device used increasingly by the Commission to make the EU budget appear smaller than it really is. It limits the involvement of Parliamentary democracy and harms transparency.

31. Greater budgetary flexibilities should therefore be used to tackle crises rather than creating an increasing array of different reserves, funds, and emergency instruments outside the scope of the budget.

32. As a principle, all items of EU expenditure, even those projected for a longer term, or which may not be deployed, should be subject to a transparent debate on equivalent terms to the financing proposed within the scope of the budget.

What is your assessment of the Commission's proposals to grant the EU more 'own resources' and of the choices advocated (a new VAT resource and/or a financial transactions tax)?

33. The LGA is not currently seeking to agree a position on the issues of a new EU VAT resource or a Financial Transaction Tax, which would allow the UK to reduce its direct annual contributions to the EU budget.

34. A thorough impact and feasibility assessment needs to be carried out in a UK context before any new 'own resources' mechanisms can be agreed upon. More importantly a fuller debate should be launched within the UK including the close involvement of local authorities.

35. Any new systems to finance the Union's budget should guarantee the principles of fairness, economic stability, transparency and simplicity.

What is your assessment of the likely impacts of the Commission's proposed restructuring of abatement mechanisms on the UK or other net contributors?

36. It appears that the UK rebate is not in immediate jeopardy under the reform of the correction mechanisms proposed, so the impact may be minimal. As a principle, the UK rebate must remain so long as the reason for the rebate persists: a disproportionate allocation of EU funds to the Common Agricultural Policy. In particular, the UK rebate should not be given an expiration date.

What is your assessment of the innovative financing instruments proposed by the Commission?

37. The EIB loan instruments should act as a valuable addition to, but not a replacement for, EU grant funding.

38. There is a need for greater awareness amongst councils of the possibilities offered by such instruments, and government should do more to promote them, especially given their increasing prominence in EU programmes.

What effects could the development of the Eurozone, in response to the Euro area crisis, have on the future EU budget?

39. The serious nature of the economic difficulties currently faced by several Eurozone States underlines that the EU's budget, the Europe 2020 Strategy, and European economic governance, should act together in a coordinated fashion to promote stability, sustainable economic growth and territorial cohesion.

40. The crisis has highlighted that greater flexibility needs to be achieved within the EU budget. A greater ability to transfer funds to different tasks within the same budget heading should be allowed. A full mid-term review of the budget should also be undertaken in 2017 to reallocate funds to emerging policy priorities, subject to certain limits.

Links
LGA position papers, publications, and supporting evidence on EU issues:
www.local.gov.uk/eu

December 2011

Jean Monnet, Chair in European Economic Studies, Division of Economics and Professor Robert Ackrill, Professor of European Economics and Policy, Nottingham Business School, Nottingham Trent University – Written evidence

Submission to be found under Professor Robert Ackrill, Professor of European Economics and Policy, Nottingham Business School, Nottingham Trent University

Agnieszka Moody, Director, MEDIA Desk UK, Ann Branch, European Commission, DG Education and Culture, and Yvette Vaughan Jones, Executive Director, Visiting Arts – Oral evidence (QQ28-48)

CREATIVE EUROPE

Evidence Session No. 2. *Heard in Public.* *Questions 28 - 48*

THURSDAY 22 MARCH 2012

Members present

Baroness Young of Hornsey (Chairman)
Viscount Bridgeman
Earl of Courtown
Lord Foulkes of Cumnock
Baroness Henig
Baroness Prosser
Baroness Scott of Needham Market

Examination of Witnesses

Ann Branch, European Commission, DG Education and Culture; **Agnieszka Moody**, Director, MEDIA Desk UK; and **Yvette Vaughan Jones**, Executive Director, Visiting Arts

Q28 The Chairman: Good morning everyone. Thank you for coming along today to give evidence to what is not actually a full-blown inquiry into Creative Europe but what we call "enhanced scrutiny". That means that it is a relatively short piece of work at the moment. As a result of what we find from the witnesses that come along and the written submissions, we will be writing to the Minister with our response to the proposals for Creative Europe.

I have just a couple of housekeeping notes before we start. Members' Interests are recorded in the Register of Lords' Interests, and the list of declared interests is on the witness table. The session is on the record, is being webcast live and will be subsequently accessible via the parliamentary website. You will receive a copy of the transcript of the session to check and correct, and this will be put on the record on the parliamentary website.

If you could, please begin by stating, for the record, your name and your official title. If you want to, you can make a brief opening statement, but you do not have to; that is entirely up to you.

Yvette Vaughan Jones: My name is Yvette Vaughan Jones. I am the executive director of Visiting Arts which is the cultural contact point for the EU in the UK. We welcome the opportunity to talk about the good stories of culture that is being supported by the EU.

Ann Branch: My name is Ann Branch. My function is head of unit of the Culture programme and actions unit in the European Commission's DG Education and Culture. I am very happy to be here on behalf of the European Commission to answer your questions on Creative Europe, which we think is an important programme for really enhancing jobs and growth in the cultural and creative sectors in the coming years.

Agnieszka Moody: My name is Agnieszka Moody. I am the director of MEDIA Desk UK, based at and co-funded by the British Film Institute. It is the information office for the MEDIA programme, which looks after the audio-visual industry. I have been in this post for over 10 years now, so this is the second time that I have observed or contributed to the negotiations on the new generation of EU support. I am grateful for this opportunity.

Q29 The Chairman: Thank you very much indeed. I am going to start by asking what can sometimes be a bit of a vexed question, about added value. Feel free to participate as you will. Do you believe that the EU has added, and can continue to add, value to the UK's cultural and creative sectors?

Agnieszka Moody: Obviously, in absolute financial terms, there is extra money flowing in, which is not the money from this Government's budget or any resources at home but coming from the European Union. I can speak for the MEDIA programme, to say that in the current generation of just over five years €36.5 million has been directly paid to British companies, with a further €30 million supporting UK films that travel across the continent with that same support from Brussels. What is important in terms of added value is that the money is given to the companies for slightly different reasons than it would be at home. When producers, distributors and cinema exhibitors come to us, they all have to put an international hat on. They always have to think about the benefits from operating in the European market, to reap benefits beyond their domestic market. So if producers come to us for support, they will be presenting projects that they hope will actually be exploited not only in the UK but further beyond, in other European countries and so forth. That is one aspect. We are thinking beyond the confines of a rather small domestic market.

The second element of added value would be transnational distribution. MEDIA will always help to shift a cultural or audio-visual product across borders. We have a problem with that across Europe. The moment that cultural products, including film, that are quite successful at home, cross the border they really need support. We are not that good at consuming our neighbours' cultural fare. This is where the MEDIA programme comes in, and also the cultural programme, to help so that we open up other countries' product to other people in each country.

Finally—this is a little bit more technical—for the MEDIA programme's added value in particular there is a lot of public support in every member state for the audio-visual and film industries. However, a lot of that concentrates on the production phase, on producers making more films. That, if you like, is the middle of the process. There is a lot of work that needs to be done before we are ready to make films. A lot of work is needed after the production is completed to distribute them widely, to promote them and to help them exist in the market. Those two extremes of the value chain are less catered for at home, across the Member States. That is where the MEDIA programme complements what is available in every participating country. We do not put money into production at all. We help audio-visual product before production and after, which is exactly where there is less support at member state level.

Yvette Vaughan Jones: I am not going to talk very much about the economic impact at this stage because we will talk about that later. Clearly, however, the amount of money going into the programme increases employment and the leverage of the money elsewhere. That is extremely important added value. I will concentrate my remarks at this stage on the impact on this sector of transnational working. In order to receive grants from the EU, most of the projects have to have at least three or four European partners. This kind of transnational working is extremely important not only for the inspiration that cross-border artists can bring to the artists in the UK, but also for the cultural offer to the audiences of the UK. Agnieszka Moody pointed to the fact that we are not traditionally very good at understanding our neighbours.

However, much more important is the capacity building in the sector. In order to work transnationally, as you can imagine, a lot of work needs to be done on cultural understanding, logistics and very complex and sophisticated, multi-layered budgeting and accountability. So we are building the capacity of the UK sector. This is unique in funding in the UK, and it is the kind of funding that is very difficult for national Governments to provide because it is very much about sharing and international work. In the UK, money for international work has been very much on the decline. It is not easy to get. As budgets get smaller, people tend to focus on domestic and local work.

Ann Branch: I can only agree with what my colleagues have said. I do not want to repeat everything, but with the programmes we are designing with Creative Europe the idea is to focus only on areas where there is a European added value; there is a section on that. The transnational aspect is incredibly important. These are areas that are not covered by national funding. They include, for example, helping the transnational mobility of artists and cultural professionals, the transnational circulation of cultural and audio-visual works and international peer learning and capacity building. Tremendous accelerated learning can take place through collaborating across borders with peers from other countries.

The Chairman: Thank you for that. We will follow it up in a slightly different format later.

Q30 Baroness Henig: Building on part of what we have already heard, can you tell us more about the proportion of funds that United Kingdom organisations receive, including leverage funding and existing programmes? What kind of economic benefit does the funding provide, particularly in terms of helping to generate growth and create jobs?

Agnieszka Moody: I feel quite comfortable answering that question. In the mix of cultural and creative industries, film and audio-visual are quite serious about the business side of their activities. Film is a strange creature in that it is both commercial and cultural. That is a debate that has been going on in different fora for a long time, but it is both. The companies that we help are doing their very best to run their businesses effectively. The vast majority of them are micro or SMEs, undercapitalised and under-resourced. They need help. The MEDIA programme support definitely contributes to that. To have one headline figure, it has been worked out at the Commission that every €1 of support generates €6 from other sources. That is the final, neat result of putting a few sums together. It comes down to intensity of support. Our most intense grant could be up to 50% of a project, no more. So there is definitely at least another 50% coming primarily from the private sector or from public sources available in Member States. I like to use the example of specific aid for cinemas. We help cinemas across Europe. There are several hundred of them, nearly 1,000, which, in return for a subsidy—usually very small grants that are a small proportion of their operation—programme significantly more European films than multiplexes at the edge of town. There, intensity of aid is 1:14. Very little money goes a very long way. Altogether, it is 1:6. In different operators there will be different ratios, but it is quite effective. Removing that €1 would have quite serious effects on other sources of finance.

Yvette Vaughan Jones: The European Council's conclusions on the contribution of culture to the implementation of the Europe 2020 strategy pointed out that employment in the cultural sector grew at three times the average of other sectors across the EU in the past decade. Investment in the sector will have a high proportion of jobs created. The Culture programme itself contributes €400 million over the period, which is roughly €50 million per year. The UK averages €4 million to €5 million as its share, which is a good share. We have performed rather well in what we get, with a 35% to 48% success rate, which compares well with the average of 27% across the EU.

However, you are really asking about employment and economic impacts. We have done a survey of the UK beneficiaries and calculate that there is an increase of 58 employment weeks per project. For every project that is funded by the EU, it guarantees a full year's salary plus. That does not take into account the economic impact of the work itself, which may be toured or sold. Literary translation increases markets. We, too, have a multiplier effect; it is not quite as big as the MEDIA programme, but it is 1:4. For every €1 that comes in, it levers €4.

European funding itself finances 50% of the projects, or up to 60% for cultural festivals. That levers in money from other sectors. A number of the projects are about culture in health, education and the environment, so we are bringing in money from outwith the cultural sector. We are also bringing in money from overseas, which is useful. There are a lot of economic impact assessments that show the impact of programmes such as Lumiere in Durham, which had 150,000 people come to see it in a city of something like 30,000. The impact on hotels rooms, ancillary services and restaurants is enormous. There is also good evidence of a supply chain. When work is created in a locality, there is increased spend on—if you are set building, for example—timber yards and local suppliers. That contributes greatly to local economic development.

Many of the programmes are aimed at inner-city disadvantaged youth. There is a cost benefit where there is diversionary activity that will counteract anti-social behaviour. So there is an economic impact at the very local level, too.

Q31 The Chairman: Related to that, you talk of growth in jobs and in the sector in general. What about the sustainability of those jobs? Obviously, by its very nature, the sector is kind of temporary. People might have a succession of temporary jobs. Is there any way of making an argument for the sustainability of those jobs? You talk about the growth of the sector, which is what has been happening. What is the prediction for growth in the sector, or the different sectors, over the next five-year period or so? Is it set to grow at the same rate? I do not wish to pile too many questions on. Some of these you may not be able to answer today, and you can write in to us. How even is that growth across the EU, if you have any sense of that? Will it be growing higher in some Member States than others? I am sorry if this is a big bundle of questions, but I am interested to know. We have to consider this in the context of the budget allocations for the next five or so years.

Agnieszka Moody: I will come back on sustainability. This is our turn to say that we have also had a survey done. It is a good time to carry out surveys because it is good to cross-check certain assumptions that we might make—those we think that the programme should be delivering—against reality. It is a very fresh report. It is not presentable yet, but I would be grateful for the opportunity to forward it to the Committee at a later date. We have surveyed companies across the UK, all the beneficiaries of the MEDIA programme across the past decade, so it is quite a good reading for sustainability. Just over 400 companies were asked because there were supported. We received 199 responses, which is a very encouraging rate of response. Of those companies which had had MEDIA money more than once, 93% said that the programme has been effective or very effective in contributing to the sustainability of their business. Of certain categories of funded companies, the recurring rate of coming back for grants was 48%. For some people working in the audio-visual business, it is definitely part of their business model. They have committed to these more challenging areas of the market, such as foreign language films. But they rely a great deal on the European subsidy for that. The whole network of independent cinemas that I mentioned before undertakes to programme more specialist films, such as foreign language films coming from different European countries. They get MEDIA money every year. That is part of their business, and that definitely contributes to their sustainability.

Similarly, for some distributors, part of the package is that they have found a niche in the market and will be leading on what we call specialist film. These are not blockbuster titles that make a lot of money, but there is still room in the market for them. I like to cite the example of Artificial Eye, which is definitely a market leader. If you add up all the grants it has had since 2007, it comes down to €2 million. That would definitely make a big dent in a company's operation, and thus it contributes to the sustainability of the business.

Yvette Vaughan Jones: I will mention three things. The survey that we have done looked at what happens after the programme and projects that they have been involved in. The three areas are, first, the increase in the ability to penetrate new markets. These relationships open up a whole series of further relationships. Artists and cultural organisations become more familiar with different markets. They may also have more commissions to do more work, and more opportunities to work in fields like education and workshops. They are also increasing their sales. Thirdly, the capacity-building element that I spoke of really makes you work in a much more entrepreneurial way, seeing opportunities, forging new partnerships and working in a multilateral way. Those skills are very transferable. The programme helps organisations become more sustainable by increasing their ability to work entrepreneurially.

Ann Branch: I have two elements of response, one on the sustainability of projects, and the other on the sector more broadly, which I also understood you to be interested in. Obviously I agree with what my colleagues have said on the projects. I reinforce that by saying that one of the added values of international co-operation is the sustainability aspect to these organisations whereby they become more professional through working internationally. They establish longer-term collaborations which may go beyond the period of grant funding that they have. They may apply for other grants, but often they continue collaborating even without them. It presents them with new professional and market opportunities. Definitely at the level of projects, we see that the funding helps these organisations to achieve sustainability.

On the general sustainability of the sectors, our intention with the programme is of course to try to put in place some of the right enablers to help these sectors. We have seen that they have been very strong sectors of growth in recent years with higher than average growth rates in many countries. We also think that they are sectors for the future. Of course, there are many causal factors that can impact on these sectors in addition to what will be quite a small funding programme in absolute terms. There are regulatory issues and things like that, many issues at national level and national policy choices which are beyond our control.

In response to your question about variation between countries, yes of course there are differences between countries and that is partly because of national policies and national funding choices. However, our impression is that there is a growing awareness across the board of these sectors for jobs and growth, even in countries where they are perhaps not as advanced as the UK in this area, and a growing recognition of their importance.

Q32 Baroness Scott of Needham Market: I am still struggling a bit with this "added value" question. The case for the creative industries is made, particularly in this country, in terms of generation of jobs and that sort of less tangible sense of being something that we are good at, which is something that we in Britain are very proud of. But it seems odd to me that decisions get made to spend taxpayers' money subsidising some things at a European level, as opposed to it being done at member state level. For example, to take the case of film with the preparation and post-production, one wonders why that is not done at Member State level if it is so self-evidently valuable. I am still struggling to understand why some decisions are made at Member State level and some at EU level. Particularly with regard to that, there are clearly huge differences between Member States in how advanced and profitable these different sectors are. Is this programme about attempting to level the playing field—in which case the UK would have something to be afraid of, because it is not in our interests for that to happen—or is it something different?

Agnieszka Moody: It is much more about the benefit of the Single Market. We all work in small compartments, at least in the audio-visual industry. Film is an international business, so closing yourself into small, domestic markets is not to our advantage. We should be thinking beyond borders. We should be thinking about co-producing with one another. We should be thinking about distribution opportunities in terms of exports for domestic product.

Baroness Scott of Needham Market: When you say "we should", are you saying that because it is financially beneficial?

Agnieszka Moody: Absolutely.

Baroness Scott of Needham Market: In that case, why does it not just happen? Why does the market not do it?

Agnieszka Moody: Because the intervention is most effective on a European level. Everybody is told that they have to put attention into shifting product across borders. This point may be made more weakly everywhere at a national level, but if it is a joint action that we will all try to shift it more vigorously, then there is European value to it. For example, in the area of training, we need skills. To be competitive, we need to have a professional, skilled workforce. We should be very proud of how we train our audio-visual professionals in the UK. There is a lot of expertise here, and we do it well. Why do we need money for training from Europe? Because if we send our professionals on a MEDIA-funded training course, not only will they get knowledge, as they do, but they will also be mixed with their peers from other countries. There is a networking value to this. They will get an insight into how other markets operate. That is not necessarily a priority for our training agencies here, and nor should it be. There is a different aspect to it. It could be turned into a benefit that we can have it both ways: we are supporting those industries at home for a certain set of priorities, and there is an enhancing a set of priorities from Europe that work for all of the countries.

The Chairman: We have spent some time on these first couple of questions, so we are running a little behind. Please do not apologise, because it was an important question. After all, we really have to dig into this and see what case is being made. If colleagues spot that part of their question has already been asked, please feel free not to re-ask it. If I could ask the witnesses to have quite succinct responses so that we can cover all the ground, if anything occurs to you afterwards that you were not able to say, please feel free to write later; we would welcome that.

Q33 Baroness Prosser: We have sort of been alluding to this, but you have told a very heartening story thus far of economic success and, interestingly, the things that are learnt by the greater mix of people, cultures, et cetera. As well as the economic benefit, what about the social and cultural benefits that we may get from being part of the wider European Union family?

Yvette Vaughan Jones: The Culture programme has as one of its key criteria the importance of enhancing intercultural dialogue and European citizenship. In the UK, the arts and cultural organisations have translated this into a very specific approach, which is to work in a socio-economic way, particularly in inner cities. I can give you quick examples of a number of projects. Brouhaha in Liverpool is just in phase 2 of its projects. Do not forget, going back to Lady Scott's point, you only get the money if you have three or four partners across Europe; that is why it has added value. At this stage, an audience of 10,000 has attended the performance work and 222 young, local and international performers worked together with 11 international artists. This sort of experience for young people cannot be had elsewhere. The target groups for direct beneficiaries were the low-income neighbourhoods in Liverpool, the black and racial minorities, refugees and asylum seekers, and social housing organisations. The targets for those target groups were met and exceeded. Projects which have at their heart the need to be intercultural have taken a very specific approach in the UK which has enormous cultural and social impacts. There are also projects that are specifically to do with disability, inclusion and health. Other examples include the Bristol COAST project, which looks at migration, and creativity and culture education in Newcastle, which looks specifically at working in primary schools with a particular focus in disadvantaged areas. The interpretation of the Culture programme in the UK very much looks at social benefits.

Q34 Lord Foulkes of Cumnock: Are the projects that you just mentioned the ones that get the money sent directly? Do they get euros sent to them? Cheques?

Yvette Vaughan Jones: Yes, but do not forget that it is part of a consortium, so they need to work with their other cultural partners across the UK. But these are the lead partners, yes.

Q35 Lord Foulkes of Cumnock: I am a bit down to earth. I am not like Lady Scott and all these artistic types. Give me a few more examples of who gets the money sent to them. What would be the effect if they did not get it from Europe?

Yvette Vaughan Jones: Well, there is a very broad range of organisations. I could mention a number of arts organisations, from mainstream ones like the Tate and Liverpool Biennial, to very small organisations and local groups like SeaChange in Norwich and Acta in Bristol. It is a wide range. Higher education institutions also get money.

Lord Foulkes of Cumnock: I saw that Napier University in Edinburgh was one of them.

Yvette Vaughan Jones: Wales and Scotland do particularly well out of this programme because they are very well networked in Europe. So the range and approach are very broad.

Q36 Lord Foulkes of Cumnock: If they lost it, would they have to stop some of their programmes?

Yvette Vaughan Jones: There is a very different answer from my sector and from the MEDIA sector, so I want Agnieszka to answer that question. The loss to the cultural sector would be enormous in terms of its inspiration from Europe, its ability to network and its ability to involve young people. There would be a very strong lack of skills development through this specific and interesting way of working which is transferable to other sectors.

Q37 Lord Foulkes of Cumnock: Is it different in the media sector?

Agnieszka Moody: In film, it is more acute. The Members of the Committee need to be aware that we have one extremely powerful, wealthy, well resourced and well organised competitor in film, which is called Hollywood. With its power being above European creative outputs, we are struggling and fighting for, at best, 30% of the market. Removing support would mean that we no longer have a right to tell our own stories at all, but would be increasingly consuming what is conceived and created by our colleagues on the other side of the Atlantic.

It is quite an acute issue for the film industry, and it has been like this from inception. The studios have been powerful throughout the history of cinema. There were some cases in the 1920 and 1960s against the monopoly of the studios in this country. So it is also a way of strengthening our own industry and creativity. There is an illuminating report by the UK Film Council, now the BFI, *Stories we tell ourselves*, which absolutely makes a strong case for the cultural impact of film on our identity and citizenship.

There is no time to talk about film in schools. Film is a very useful educational tool for developing the younger generation, which is now gaining more and more persuasion within the education sector. We teach our young drama, we teach them other art forms, and film should be getting there. It is mature enough.

Lord Foulkes of Cumnock: Thank you. You have made it seem much more real now. That is very helpful.

Agnieszka Moody: It is real. The digital shift does not help. Everybody looked at the digital revolution thinking, "Right, it is our turn now. There will be space for us because there will be more space for everybody". But that is exactly what the studios thought, too. They are definitely well equipped to take the benefits of the digital revolution as well.

Ann Branch: I will complement that with a couple of statistics on the MEDIA side: 50% of European films released outside their national territories cross borders thanks to MEDIA. A lot of distribution companies would probably go bust without it. From 1989 to 2009, over a 20-year period, the proportion of European film among all first-time releases in European cinemas rose from 36% to 54% thanks to the MEDIA programme. Without it, that would not have happened. In the same period, the share of US films fell from 47% to 44% despite a high increase in marketing spending. I think those are useful statistics.

Q38 Earl of Courtown: The Minister last week told us that the Government were opposed to the proposed increase in funding for Creative Europe, which obviously must concern you. If the increase is agreed, would United Kingdom organisations stand to gain significant additional funds as well?

Yvette Vaughan Jones: Our evidence is that we do rather well in applications, better than the EU average. I do not see that that is going to change. As we said earlier, the ratio of leverage is 1:4, so it must be good news for the jobs, employment and the economy of the UK, with more money coming into this sector.

Q39 Earl of Courtown: But if it is set at the same level, as opposed to getting an increase, is it going to be a disaster for you?

Yvette Vaughan Jones: It will. We will not be able to trade so well.

Earl of Courtown: But you are succeeding at doing it quite well at the moment, from what you are saying.

Agnieszka Moody: But there are still a great number of high-quality projects that end up below the thick line because there were insufficient funds. My favourite example is Stephen Woolly, a very respected film producer, who is now making another adaptation of "Great Expectations" which will export well out of this country. That was a MEDIA-supported project in the early stages of development, but it had to sit for several months on the reserve list because it was just about good enough. If that is not enough, it just means that there is not enough money. Or, for example, we have those 50 cinemas that programme European films, but we could have 150 if there were more resources made available. Is it disastrous that we have 50? I think so. Especially if we go outside London, the availability of films other than those produced by Hollywood studios is very limited, so that support is really needed quite desperately.

Q40 The Chairman: Would that be prioritised, do you think?

Agnieszka Moody: That is a question. Altogether in the MEDIA programme, I think that what is going across to the new generation is that the focus is on distribution and exhibition. The Europa Cinemas supported network of cinemas is a great success story with a big potential, which has recently been boosted by MEDIA Mundus money. So we now have Europa Cinemas in Jordan and places like that. There is definitely potential for growth there.

Ann Branch: I add that, as we have proposed this financial facility for the small and medium-sized enterprises in the cultural and creative sectors, we estimate that there is a funding gap of something like €2.8 billion to €4.8 billion. In other words, if we were able to fill part of that gap—we estimate that if we were to make an investment of €211 million—the leverage mechanism could leverage €1 billion of private lending. It would not fill the entire gap, but you can just imagine how many opportunities for jobs and growth are being missed out on, plus the cultural benefits of what those organisations would be producing. We think that, although a great deal has been achieved, that funding gap demonstrates that we could do even more. We need to find growth sectors at a time of crisis. These are sectors for the future, with sustainable jobs, many of which cannot be relocated by their nature. We should be more ambitious and we could achieve a great deal more.

Q41 Baroness Scott of Needham Market: I was wondering, because we have not got time to go into it now, whether you might be able to send figures if you have them on the overall level of support for these sectors. We are talking about support coming from the EU, but most Member States have local programmes. For example, here, there is tax relief, which is pretty significant, and it was announced yesterday that it is to be expanded to high-end television programmes, "Wallace and Gromit" and so on. All I am getting at is that what one might call subsidies or grants from the EU are certainly not the whole picture. It might be quite useful to know what the whole picture is.

Ann Branch: I can give one quick example to give an idea of scale. Under the Culture programme at the moment, our annual budget is roughly the equivalent of the operating costs of one national opera house, but that money helps us to reach over 1,000 organisations each year. That is another type of leverage effect. Even if it is a small amount of money, it can go a long way.

Q42 Viscount Bridgeman: You have given us a very impressive account of the MEDIA activities. I was particularly impressed by the multiplier figures that you cited. These are fairly standard questions when any sort of amalgamation is proposed; we are talking about the combination of the culture and MEDIA programmes into Creative Europe. For instance, does the new proposal structure represent a significant improvement to the operation of the current programmes? Have the right objectives been set for the culture and MEDIA strands?

Yvette Vaughan Jones: We welcome the new approach with Creative Europe. Combining the two programmes will not take away the autonomy of the two ways of working. They are very different supply chains. There is some synergy with the overlap, particularly in new technologies. It can certainly have some cost savings in administration, delivery and marketing. That must be a good thing. We are looking forward very much to exploring the synergies in the content. Policy-makers should be ahead of the curve, and that is a way of saying that we are looking ahead to those synergies. In terms of the objectives, we all swim in the same sea. We are very aware of the economic realities going forward and the Europe 2020 agenda. There is no problem at all in looking at how we can focus the programme to create a more sustainable, effective and efficient sector. We are looking at smart, sustainable and inclusive growth. The sector as a whole is pretty supportive of the way that this is moving.

Agnieszka Moody: On the new objectives for the MEDIA programme going forward, it is not set to change dramatically because it has been delivering well for the audio-visual sector. The one significant improvement is the greater focus on audience development. For 20 years, we were feeding the industry, intervening on the supply side of things. For the new programme, the new focus is to look more significantly at the demand side, growing audiences and supporting educational activities that will help develop a taste for European and domestic film early on among young people and then throughout their lives as citizens. That is a very exciting development for the MEDIA programme, that it is going out further into the community.

Q43 The Chairman: We have got the Commission's view on this, obviously, but is there anything you quickly wanted to add?

Ann Branch: Of course I support our proposal. To our knowledge, we have had no one disagree with the problems that we have identified that need resolving through this programme. There is virtually no opposition, as far as we can see, to the idea of merging these programmes together within this framework structure so that they keep their autonomy to respect the different value chains. From what we can see, there seems to be broad overall support for the aims at this stage.

Yvette Vaughan Jones: Briefly, I did not mention that the new programme for the cultural sector is slightly different. It is very much more focused on capacity building. We think that that is a useful move.

Q44 The Chairman: The Minister told us last week that the Government are opposed to the proposed financial guarantee facility. We wondered what you thought about that. Is there much support for such a facility among the other stakeholders?

Yvette Vaughan Jones: There are surveys; there is one coming out called "Banking on culture" for the cultural sector, which reports that it is true that small cultural businesses find it very difficult to get access to finance. The guarantee facility, we feel, would be a very good thing. It is not traditional for arts organisations to look in terms of investment and equity share; they tend to look in terms of grants. We have looked at this shift carefully, and at comparators. In certain places like Quebec it has been working extremely well for certain kinds of programmes. These can be infrastructure, new technology and certain large-scale performance programmes that can begin to recoup their investment over time and then go into profit and feed profit back into these organisations. It is not going to be suitable for all kinds of organisations. It will require a different mindset but, as part of the toolkit, it is an extremely effective and important part. It can help organisations change their business model and look at recycling money, taking the pressure off the public purse. This surely must be a good direction for the economy.

Agnieszka Moody: Similarly, in the audio-visual sector, it is a mix. It is a part of the mix that some businesses will not be quite ready to shift to this system of loans; they will be relying on grants. But some will welcome the opportunity. An example could be cinemas again. There was an initiative by the UK Film Council some eight years ago to equip a large amount of screens with digital projectors. Some 240 screens were paid for with public money. The reasoning behind this initiative was to provide audiences with access to films. This equipment is now eight years old, and it will definitely need updating soon. But it is not a rescue situation anymore. Those cinemas are there. They have transferred to digital. They would be quite reasonable contenders for perhaps even teaming up as a group and going for a loan on preferential terms that would be supported by this facility. Another obvious sector would be games, which are on the commercial edge of audio-visual. There it is less about plugging the gap in finances with a grant than about plugging the temporary gap in financial projections of profitability with an injection of cash—again, on better terms than are commercially available. The demand will be there from the sector, for sure.

Ann Branch: From the European perspective, on the stakeholder aspect, there has been a lot of research and consultation. A 2009 study on the role of banking in European film highlighted the need for such an instrument, and a study published in 2011 on the entrepreneurial dimension of the cultural and creative industries indentified this as a key issue for these sectors. In 2010 we published a green paper—a consultation document—on how to unlock the full potential of the cultural and creative sectors; it emerged there as an issue. It was also called for strongly by a member state expert group comprising national experts appointed by Governments on the cultural and creative industries. It made recommendations for such an instrument to address the access to finance issue. There is also a stakeholder platform at European level - representing over 40 European representative organisations - on the cultural and creative industries, and it has also called strongly for such an instrument. The European Parliament, in a resolution last year, also called on Member States and the Commission to consider the setting up of such an instrument. In the public consultation on the MEDIA programme, 54% strongly agreed with setting up something like this. We have had various meetings with financial institutions in 2009 and two meetings in 2011. Finally, it is important to mention that the European Investment Fund—the idea would be that it would run it for us—has AAA status and previous experience of running such generic schemes. It agrees that there is a specific need for these sectors that is not currently being addressed and tackled through generic instruments.

The Chairman: Thank you, that is very helpful indeed. If you send us some of that material, that would aid us greatly in writing our letter once we have finished the inquiry.

Q45 Baroness Scott of Needham Market: The Government opened a public consultation on the Creative Europe proposal in December. When we spoke to the Minister last week, only about half a dozen responses had been received but—perhaps as a result of the millions of people who watch our Committee proceedings—the number of responses has now surged to something like 43. Given the benefits that you have outlined, it is interesting that the response rate was so poor. Therefore, I would appreciate hearing your take on why that is. Is the UK particularly bad in responding to such consultations, or is that pretty standard across Member States? If so, what is happening here, given how important you have said this programme is?

Agnieszka Moody: There are several points to make here. First, it is important who responds, rather than how many responses are made. It would be quite ambitious to expect the end-user to have the knowledge that we have of the detail of what is proposed. To be frank, end-users see that there is going to be more money, but that is probably the depth of their response. For example, to understand fully the details of the financing facility requires a bit of homework, and I am not sure that many people would have done that for the purposes of the consultation. From my own inquiries, I know that all major public agencies responded, including the BFI on the audio-visual aspect. That matters a lot because these are policy-makers who have expertise in this area, and their view on the proposal should be considered very seriously. All of those are in the mix: the producers association and the exhibitors association—all the people that I would hope would respond—have responded to the consultation. On the issue of measuring the engagement of industry, we organised a briefing in the British Library in order to educate users about the Creative Europe proposal and we filled the 255-seat auditorium—we were turning people away. So there is interest.

The consultation had 24 questions, including on things that sounded perhaps more future and less familiar, but the beginning of the consultation was all about asking people about the impact of the programmes. I am hoping that the DCMS will look at our survey, because we have 200 responses with a great deal of detail on what this money has actually done to the audio-visual industry.

However, I hope that this consultation will not be the Government's only way of evaluating this proposal. In some cases, in particular on the financial facility, you really need the experts to give their views, so the banks should be consulted. Some representatives of the industry—not the industry at large, but some targeted companies—should be asked for their views, which should be listened to. I hope that that happens as well as the public consultation.

Yvette Vaughan Jones: From the cultural sector's point of view, the consultation was never something that the public would respond to—

Baroness Scott of Needham Market: I was not suggesting that the public should respond, but perhaps the sector should respond.

Yvette Vaughan Jones: Within the sector, we have had meetings with the UK beneficiaries, who are very familiar with the new programme and have strong views. We find that the small businesses in the sector are part of membership organisations, which represent them. For example, the IETM[24]—which is based in Brussels but has a very high proportion of UK performing arts organisations—sent round its response to all its members, and I assume that people in the sector will feel that, if their views are well covered there, the IETM submission represents their response. I think that you will find that there is high awareness in the sector of the issues and a lot of debate, but when it comes to the more detailed analysis, as Agnieszka Moody said, they rely on their umbrella bodies to do that for them.

Q46 Baroness Scott of Needham Market: I was not for a moment suggesting that the general public would engage with the consultation, but there are many hundreds, if not thousands, of cultural organisations. Given that the Commission is proposing a 37% uplift in the budget, you need all the justification and support that you can get if you are to get that through. That was my point.

Ann Branch: Perhaps I can add some European context. First, I agree entirely that most responses will come from the representative organisations, which is a phenomenon that is true in any sector—I have worked in the business sector before, where companies do not

[24] International Network for Contemporary Performing Arts

have time to look at policy documents so they rely on the process within their representative organisations to feed into such consultations.

It may be interesting for you to know that, in our public consultation at the beginning of this process on the Creative Europe proposal, on the culture side we had 1,000 responses in total, of which 47 came from the UK—that seems to be approaching the figure for the Government's consultation. On the MEDIA programme, we received a total of 2,586 respondents, of which 259 came from the UK, so some of these organisations have already responded before. Another important point to add about engagement is that, if you are trying to understand the impact on operators, you need to look at how many people actually apply under the programme. Those figures are of course much higher, but not all of those people will respond.

An additional point on engagement that is worth mentioning is that there is a process at European level of structured dialogue with the cultural sector through three thematic platforms, which represent all the key sectors across Europe, including many UK organisations. That has produced a lot of work and recommendations, which have fed into our proposal upstream. That is just another dimension of the consultation and engagement that is taking place, but you would not see that from this UK exercise.

Q47 Baroness Henig: When the Committee took evidence from the Government's Minister for Culture, Communications and the Creative Industries last week, he was pretty frank in admitting that his contact with his European counterparts over the past two years has been pretty sporadic, if I may put it in those terms. Obviously, he was using his time in other ways. Do you think that United Kingdom Ministers could engage more fully with their counterparts in Europe? In a way, this is all about adding value and effectiveness, so is there anything specific that that would achieve? I would really like to get your perspective on this issue of direct engagement at ministerial level.

Agnieszka Moody: There is definitely room for improvement, as I think the Minister himself said, which would definitely be of benefit. The European Union is one big negotiating table. Obviously, we are all in it together for a reason—together we are stronger, and the bigger countries help smaller countries—but national interests are not to be overlooked there, and certain countries that are more engaged may secure their own part of the offer more intensively. We can see that at the level of how Member States contribute to the work of the committee that oversees the MEDIA programme, and there either you are part of the conversation or you abstain from the discussion. That can be applied to the higher ministerial level: when you are in dialogue with your colleagues, there will be benefits at home.

Q48 Baroness Henig: I hear what you say, but at the beginning of this session we accepted that the UK does very well out of these programmes. That is why I qualified my question, because there may well be other ways of securing the benefits. That was the point of the question, really.

Yvette Vaughan Jones: Culture is inherently international, so I would have thought that the importance for the Culture Minister to talk internationally is self-evident. You can also learn about and share some of these intractable problems across Europe by talking with your partners. You see how the role of culture can be strengthened and how its role in developing the European economy can be strengthened. Sharing with other countries that do things differently—and perhaps see culture differently and fund it in different ways—is surely a good thing.

Ann Branch: From our perspective, the more engagement in Europe from Ministers in general, the more welcome it is—from every single country. Just as cultural operators can learn from one another, Ministers can learn from each other as well, and the debates do concern them. There are also regular occasions for them to meet. In addition to the two formal Council meetings each year for Culture and Audio-visual Ministers, which take place in May and November, there are sometimes informal ministerial meetings—there will be one in October under the Cypriot presidency, where they will meet with their education counterparts. These informal ministerial meetings are a good opportunity to meet with other counterparts, so I think that could be a very interesting opportunity, too.

The Chairman: Thank you very much indeed, especially for your thoroughness in addressing some of the quite difficult questions that we put to you. I think that virtually all of you have agreed to send us quite a lot of different kinds of information, and we would be grateful if we could receive that as soon as possible. On behalf of my colleagues, I thank you very much for giving up your time this morning.

National Council for Voluntary Organisations (NCVO) – Written evidence

Introduction
TSEN has now merged with NCVO from where we continue to provide ESF Technical Assistance support to the sector and represent its interests on the ESF Programme Monitoring Committee in England. TSEN former members provide their expert input to NCVO through the European Funding Network Advisory Group. TSEN previously responded the House of Lords Select Committee Inquiry into the 'EU Financial Framework from 2014' and to a large extent we wish to reaffirm our previous contribution. For the purpose of the follow up we concentrate a selected number of questions which we feel are relevant to the work of the voluntary, community and social enterprise sector.

Issues
Q3 what benefits both financial and practical will be derived from the Commission's proposals for simplification, particularly through the use of common strategic frameworks in research policy (Horizon 2020) and regional policy? Is the Commission's proposal strategically justified or is it a mere merging of funds? How can this approach made to work in practice?

We welcome the simplification that a common strategic framework might bring to the future implementation of the funds: common rules for all the funds should bring about the ability for single projects to use resources from all funds (ESF, ERDF and the EARDF) for the benefit of local communities.
For example, Housing, including social housing, is eligible under ERDF proposals, to benefit from energy efficiency and renewable investment paving the road potentially to Housing Associations accessing both ERDF funding to improve their housing stock whilst at the same time training the unemployed in green jobs with ESF funding. Similarly there Social Innovation is citied as an investment priority in ERDF which could well complement work undertaken under the Social Inclusion Thematic Objective in ESF. This in our view constitutes a strategic approach to the use of the funds in a way that it has not been possible in the current programme: at present some ERDF local management committees in England have banned the use of ERDF for social housing retrofit projects.

All funds will be governed by the same eligibility rules which should make it easier either to access them from separate managing authorities or from a unique managing authority managing both funding streams. At present there is no opportunity for projects funding under ESF and since the departure of Regional Monitoring Committees accountability for how the funds are utilised is all down to the national Co-financing Organisations and their prime providers. ERDF on the other hand seem to enjoy still of local management committees perhaps in the future these can become joint committees to oversee both funds or perhaps the LEPs will play a more strategic role, but whatever mechanism is utilised it will be important that the principles of transparency and involvement of all relevant actors, including the Voluntary, Community and Social Enterprise Sector, are upheld.

In order for the funds to work in a more strategic manner in the next Programme we believe that there is a need to allow for an implementation system which is much closer to the localities, the so-called bottom up approach, and would support mini-programmes at the regional or local level led by democratically-accountable bodies such as Local Authorities or groupings of local authorities. Similarly, we would not oppose the creation of multi-funds as the unique contribution of each CF fund is guaranteed through specific regulations in addition to the Common Provision Regulation.

We are very supportive of the proposed delivery mechanisms that would allow all the funds to be used in an integrated manner such as the *Community-led Development* and the *Integrated Territorial Investment.* There are also opportunities to appoint Intermediary Bodies from the NGO sector who could for instance be leading on programmes sections around Social Inclusion and Poverty. We would also support mechanisms which sit outside co-finance, such as direct bidding allowing for greater flexibility at the local level and use of match funding in kind including volunteer time. Whilst co-finance is an approached favoured by Government as it is cheaper to run and whilst the primary contracting model allows Government to outsource risk onto providers, we believe that in order for the next programme to be more strategic and innovative, a 'space' for the sector to engage through small projects and grants is needed. Much discontent has been voiced by the sector in engaging as mere sub-contractors to large private prime providers not only because terms and conditions are not always fair but also because the talent of the sector in working with the most vulnerable and those furthest from the labour market are either under utilised or not utilised at all as often VCS organisations are not involved strategically in the design of interventions. We see the proposals on the new Structural Funds programme as an opportunity to allow for the direct access to the funds. We often cite examples from the Welsh Programme where the sector seems to be better recognised for the value it can bring to the Structural Funds. This can be seen for example by the support given to a large strategic project 'Engagement Gateway' led by WCVA and supported by some investment by the Welsh Assembly.

It will be important to recognise in the context of Horizon 2020 that innovation is a characteristic of the NGO sector both in content of service delivery and organisational form. That the NGO sector comprises 4-5% of most member states economies thus it will be important to develop mechanisms in that part of the programme to facilitate the involvement of NGOs in delivering Innovation in the EU.

Q4 Is the proposed distribution of funds between and within the main expenditure headings right? In particular do the proposals offer enough o fulfils the aims of Europe 2020?

In our previous submission we maintained that the EU budget should be based on the principles of solidarity not only with poor regions but also with poor people. We therefore welcome the increased budget for ESF to €84 billion and setting minim shares of ESF as this is a direct expression of European Solidarity and makes an important contribution to Europe 2020 and its headline targets.

Q5 Do the proposals live up to the aims set out in the Commission's Budget for Europe 2020 of focus on delivery key policy priorities; focus on EU added value; focus on impact and results?

As a sector we do welcome the proposals which link into Europe 2020 themes and key policy priorities which of course places strong emphasis on Inclusive Growth. This should give us ample room to devise results that are appropriate to the most vulnerable such as soft outcomes focussing on the empowerment of the individual as well as wider social impact of NGOs. We feel this is a budget that unequivocally commits to the achievement of EU Social Policy objective.

Q9 what is your assessment of the innovative financing instruments proposed by the Commission?

We welcome the extension of their use but sadly we have very little experience as they have not been taken up particularly in the ESF programme. As explained at the House of Lords seminar these would include marrying grant finance (ESF) with loan finance (from banks or other financial institutions) to provide micro-credit to social enterprises. It seems to be widely used outside the UK and we should explore its potential particularly if the new programme is going to allow access outside the primary contracting model. However, this should not be seen as a panacea for all civil society organisations funding challenges and not all organisations are income-generating. We continue to maintain that a balance between contracts, loans and grants in introduced and maintained. Grants can be a viable option for strategic involvement of local organisations in the design and implementation of services that it is not allowed by inflexible national commissioning and procurement processes; they can promote social value and community engagement as well as quickly respond to changing circumstances in an innovative manner.

December 14, 2011

Jorge Núñez Ferrer PhD, Independent Consultant and Associate Research Fellow of the Centre for European Policy Studies, and Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University – Written evidence

Submission to be found under Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University

Professor Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University; Chairman of the Board of the Bank of Sweden Tercentenary Foundation, and Jorge Núñez Ferrer PhD, Independent Consultant and Associate Research Fellow of the Centre for European Policy Studies – Written evidence

Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University; Chairman of the Board of the Bank of Sweden Tercentenary Foundation

Jorge Núñez Ferrer PhD, Independent Consultant and Associate Research Fellow of the Centre for European Policy Studies

The opinions expressed are inspired by the results of a Task Force meeting at Centre for European Policy on the future financial perspectives and their focus on long- term growth. They closely reflect the consensus of the group composing the Task Force. The report "Investing where it matters, an EU budget for long-term Growth" will be published at the start of 2012. Nevertheless, this evidence commits only the authors and is not necessarily endorsed by the members or the organisations they work with.

The evidence submitted here concentrates solely on the expenditure side of the budget, with a focus on Europe's competitiveness.

The size of the budget

The first question presented by the enquiry concerns the size of the budget and the link to national fiscal consolidation movements. While there is of course a need to ensure efficiency by the EU budget, it is far from evident that the fiscal consolidation in member states should be reflected in a reduction of expenditures of the EU budget. The nature, composition and focus of this budget are very different from those of national budgets.

The Commission has nevertheless understood the need to keep the budget under tight control and proposals go a long way towards finding a compromise between member states wanting to rein in EU finances, and those member states and the European Parliament that demand an increase in funding.

The proposal has managed to maintain expenditure constant at the level of 2013, while increasing expenditures in areas recognised by most member states (including the UK) as essential for Europe's future competitiveness, namely research and innovation and the infrastructure that is essential to the single market and Europe's energy security.

There are areas where undoubtedly cuts in expenditures can still be undertaken. These are areas where the European value-aAdded is low and where the subsidiarity principle would better allocate the competences to the national level. Unfortunately, those areas are the most difficult to cut, namely, the Common Agricultural Policy (CAP) and structural policies in the wealthier regions of the EU.

Professor Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University; Chairman of the Board of the Bank of Sweden Tercentenary Foundation, and Jorge Núñez Ferrer PhD, Independent Consultant and Associate Resear
On balance, and given the number of important new objectives of the EU in the area of growth, innovation, energy and climate change, the Commission's proposal is as sober as it can be. Pushing for cuts alone would most likely affect new areas with high European value added and would run counter to the interests of the UK.

Key changes in the Commission's proposals compared to the present budget

Probably weary of the backlash in 2005 from the member states against the Commission's proposals in the negotiations for the present budget, the European Commission has also largely retained the structure of the budget. Reforms are 'under the bonnet', i.e. in the strategy and implementation stages. The most important reforms are to be found in for the Cohesion Policy, where – first of all – the *first* priority of the funds has now been changed to promote research and innovation in the regions. The Commission also demands improvements in structural fund strategies including the drafting of a smart specialisation strategy for innovation, which most interestingly would be peer reviewed, a first for EU regional policy.

The proposals also place a lot of weight on and reinforce the successor programme for the FP7, called Horizon 2020. This policy will now focus, in addition to basic research, also on the whole life cycle of innovations from concept through demonstration down to deployment. Grants and financial instruments are to be combined to find the right equilibrium between the public and private intervention. Thus the proposal reinforces the innovative financial instrument for research, the Risk-Sharing Financial Facility (RSFF), a move that is to be commended.

Finally, as a major change, the Commission aims to invest heavily in the development of cross-border key trans-European infrastructures with the Connecting Europe Facility (CEF), with a larger budget (€40 billion) and the earmarking for trans-European transport of €10 billion from the Cohesion Funds. While earmarking Cohesion Funds for the CEF is a positive idea, the restrictive focus exclusively on transport is illogical and should be deleted. In the Cohesion countries, the needs in the energy sector and ICT are vast. These countries have on average a much higher green-house gas emissions intensity per unit of output than in old member states.

The Commission also proposes to create the Project Bonds to support the CEF, using a variation of existing proven risk finance instruments, combining those with bonds in order to attract new private investment from e.g. pension funds and/or sovereign funds. The Commission has just launched a proposal to start a pilot phase for the Project Bonds for 2012-13.

The expansion of innovative financial instruments across the different areas of the EU budget (including the project bonds) is to be encouraged. With the right rules, the risk and debt capital the budget provides can be kept self-contained, thus avoiding unexpected budgetary repercussions if specific projects assisted by those instruments fail. The innovative instruments are based on well-known and tested practices, which are innovative in the sense of being new to the EU budget, not the financial sector. They ensure a better balance of investment between the EU budget and the private sector, ensuring an increase in the quality and financial viability of projects. While those instruments cannot replace grants in a number of areas, there is ample scope to increase their size and reach. Some of the financial instruments can be made revolving, i.e. recoverable and thus possible to redeploy.

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Those are generally speaking the most important and most laudable proposals, which should be defended by member states seeking to promote a budget investing in long-term growth and key European objectives. Under the policy constraints in which the European Commission operates, the integration of the Europe 2020 objectives into policies is remarkably forward-looking.

All is not well and reforms in other policies, such as those for the Common Agricultural Policy (CAP) fall short of being sufficiently ambitious. Those are still largely driven by considerations unrelated to the real problems facing the sector.

Financial envelopes of the Budget

On the size of the financial allocations, the balance between the expenditure items is politically charged, rather than economically optimal. There are key areas where there should be more financial support, which is the case for energy for research (Strategic Energy Technology (SET) Plan) and energy infrastructures for the CEF. For the SET-Plan, grant funding should be increased as well as funding earmarked to energy from the RSFF, approximately to up to two billion yearly in grants and €2 billion risk guarantee over the 2014-20 period.[25] This represents an increase of well over double today's allocation, but necessary if the investment objectives in new technologies are to be achieved in time. Changing the energy sector has major implications on growth for the long-term. Funding for the SET-Plan can be redeployed using the resources from within the Horizon 2020 project. For the CEF, an increase could be financed from the CAP.

Another funding area, which is highly neglected, is INTERREG. Cross-border collaboration is a key function of the EU, but there has been a preference to allocate funding in more inward-looking financial instruments. The very small envelope for INTERREG should be reinforced by multiplying the funding three-fold, mainly transferring the funding coming from the structural funds allocated to regions with a per capita income over 90% of EU GDP.

Knowledge-based governance and the case of administration

A weakness of the proposals is the cut in administrative expenditure, while very visible and popular it runs counter to the needs and changes on the ground. Europe´s future must be based on a knowledge-based economy. This was set out clearly in the Lisbon agenda and is once again confirmed in the Europe 2020 programme and the communication on the Innovation Union. In an ever more competitive world economy, constantly evolving cutting-edge technologies and supreme skills in a variety of services are needed to secure high levels of employment and living standards in our continent.

An important precondition for this is excellence in policy formulation and policy implementation. A knowledge-based economy requires knowledge-based governance, both at national and regional levels and within the European Union. With the constantly increasing impact of our regulatory sphere, the quality of the EU machinery will achieve ever-greater importance. European legislation is already decisive for our economic development and is bound to become even more so in the future.

[25] The rational for these figures is explained in the CEPS report: J. Núñez Ferrer, C. Egenhofer and M. Alessi, (2011), "SET-Plan: From Concept to Successful Implementation", CEPS Task Force Report, CEPS, Brussels, May..

Professor Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University; Chairman of the Board of the Bank of Sweden Tercentenary Foundation, and Jorge Núñez Ferrer PhD, Independent Consultant and Associate Resear
Growth is more dependent on EU rules than on EU expenditures. But some EU expenditures are decisive for the formulation and implementation of EU rules. These deserve particular attention in the elaboration of the new MFF.

The cognitive inputs required to provide momentum and sound direction for EU policy-making reach the EU institutions from many different sources. Research institutes, think tanks, interest groups, NGOs, national governments and regional bodies all make important contributions. It is vital that the EU institutions are well equipped to assemble, systematise and digest all these insights, proposals and criticisms. Much has been done in recent years to improve this process, particularly since the 2001 governance report. New methods for impact assessment are evolving and the practice of consultations has reached impressive proportions.

But this is hardly reflected in the Commission's budget proposal. Its chapter on "administration" boasts about cuts already undertaken and promises a further 5% reduction in the next period. The administrative programme put forward is based on such concepts as simplification, rationalisation and the introduction of single frameworks. An 'equal pains' approach suggests that EU institutions should be reduced in response to similar cuts in the member states.

This is simplistic and at odds with other elements in the budget proposal. The idea of increased conditionality, for instance, is bound to fail unless the Commission obtains more resources to conduct its dialogue with national and regional governments and perform its own analysis of their initiatives. Today, several DGs and parts of DGs are already clearly under-equipped for this task. With the new proposals, this capacity deficit will inevitably widen.

EU legislation plays an increasing role in setting the framework conditions for European enterprises and private individuals. External policy analysis and diplomacy are vital to formulate European lines of action and to assert European interests in the world. Cramming all these high-brow, highly qualified activities into the grey category of 'administration' is to misrepresent and underestimate the crucial intellectual infrastructure of the European Union.

The traditional label 'administration' is in fact singularly ill-chosen for the multitude of qualified tasks carried out by the various segments and sections of the EU institutions. Under present conditions, however, it serves as a conceptual umbrella for a whole range of indispensable functions: analysis, forecasting, statistics, implementation, auditing, monitoring, evaluation, impact assessment, deliberation, adjudication, stakeholder communication and the ramified activities of 40+ independent agencies. In addition, the potential savings of replacing member states' administrative units by central bodies is ignored, a fact that is clear for external representation of member states, but also for common agencies such as Eurocontrol, which reduces the need of uncoordinated and duplicated work over 27 countries.

A further mistake is to make 'simplification' the principal avenue for the development of EU governance. Pushes in this direction may play some role but must always be balanced against conflicting interests. Accountability to the taxpayers requires regulatory safeguards. Sophisticated policy-making often relies on differentiation and avoidance of the one-size-fits-all recipe. 'Red tape' has a bad name, but the formal requirements linked to obtaining EU

Professor Daniel Tarschys, Professor Emeritus in Political Science and Public Administration, Stockholm University; Chairman of the Board of the Bank of Sweden Tercentenary Foundation, and Jorge Núñez Ferrer PhD, Independent Consultant and Associate Resear funds have also many positive effects in administrative cultures traditionally characterised by favouritism, clientelism and cosy informality.

In conclusion, both the name and the size of the fifth chapter of the Commission's proposed budget ("administration") deserve reconsideration. EU decision-making must be embedded in a constant pursuit of better knowledge about policy costs, outputs and outcomes. High-quality governance mechanisms and a strong support to the institutional infrastructure of the European Union are indispensable to strengthen the quality and impact of EU rules, not least those connected with the internal market.

Other considerations

This text is based on the compromise positions of a Task Force, which did not deliberate on own resources or other aspects on the EU. What the members of the Task Force all agreed is that the member states should concentrate first and foremost on the expenditures in the key areas for long-term growth and on the quality of delivery mechanisms. Issues on net balances and resources should not overshadow this important discussion. Decisions on Own resources based on 'excessive net balance' considerations can be taken once the distributional implications of an efficient EU budget implementation are understood.

Summary recommendations

The European Commission's proposal is a cleverly devised and carefully balanced budget retaining the structure and limiting EU's expenditure items. The proposals, however, introduce strong governance requirements which should be defended.

The proposals are bringing the budget more in line with the Europe 2020 objectives. The EU budget should be focusing on long-term growth and economies of scale. Many of the proposals should be supported and it is important that any cuts in the budget are not done in growth-oriented expenditures. The negotiations should be on policy quality and content, not on quantities.

15 December 2011

Ed Vaizey MP, Minister for Culture, Communications and Creative Industries, Department for Culture, Media and Sport – Oral evidence (QQ1-27)

CREATIVE EUROPE

Evidence Session No. 1. *Heard in Public.* *Questions 1 - 27*

THURSDAY 15 MARCH 2012

Members present

Baroness Young of Hornsey (Chairman)
Viscount Bridgeman
Lord Foulkes of Cumnock
Lord Skidelsky
Baroness Scott of Needham Market

Examination of Witness

Ed Vaizey MP, Minister for Culture, Communications and Creative Industries, Department for Culture, Media and Sport.

Q1 The Chairman: Good morning, Minister. Thank you for coming to this relatively brief condensed inquiry into the creative industries and the Creative Europe proposal. I remind you, as I am sure you already know, that Members' interests are recorded in the register of Lords' interests and the list of declared interests is on the Witness Table. The session is on the record; it is being webcast live and will subsequently be accessible via the parliamentary website. You will receive a transcript of the session to check and correct, and this will be put on the record on the parliamentary website. Please begin by stating for the record your name and official title. If you would like to make a brief opening statement, please feel free to do so.

Ed Vaizey: I am Ed Vaizey and I am Minister for Culture, Communications and the Creative Industries. I welcome the opportunity to talk to the Committee about the Creative Europe proposal.

Q2 The Chairman: Thank you. Do you think that the EU has brought in the past, and continues to bring, some element of added value to the UK's cultural and creative sector? Do you agree that existing EU funds provide a significant source of capital for UK stakeholders, helping to create jobs, growth and benefits for the public?

Ed Vaizey: As Minister for Culture with responsibility for the creative industries, which includes film, video games, broadcasting and the like, I am very alive to the fact that the creative industries in the UK provide a strong source of potential economic growth. I hope that all the Committee Members will agree that we in the UK are very successful in those industries. We are known around the world for our creativity. The UK box office has been topped by UK films, whether those funded by US studios such as the Harry Potter series or independent films like "The King's Speech", we have topped the charts in America—for the first time in 25 years we have had numbers one, two and three—and we have successful fashion and games industries. I am supportive of anything that can support those industries. It is fair to say that we welcome the Commission's focus on the economic and growth potential of the cultural and creative sectors, particularly in the context of the Europe 2020 strategy, and its emphasis on ensuring added value and achieving clear measurable objectives and outcomes from the proposed programme. It is also fair to say that we have benefited from this EU programme. The current proposals build on an existing programme where UK participants have received something like £100 million in the four-year period 2006-10. To pick a few random examples, in 2010 UK production companies received grants for the early stages of production work, including a new adaptation of *Great Expectations*; the British Library received funding to support its work in China; and the Chamber Orchestra of Europe also received funding support for its work in China. My understanding is that the new proposal for 2014-20 is designed to strengthen competitiveness in the cultural and creative sectors. It will focus on building capacity and expertise in organisations, and will support the circulation of cultural works across Europe. Those are objectives that we support.

Q3 The Chairman: It might be difficult for you to put your finger on this but I am interested in the extent to which that funding and support has value over and above the money that goes in and whether it has an extended reach. Are we talking about small and medium-sized enterprises as well as the larger, more headline-grabbing organisations?

Ed Vaizey: I think we are talking about SMEs. For example, the adaptation of *Great Expectations* will be by a relatively small independent production company. One could describe the Chamber Orchestra of Europe as a small and medium-sized enterprise while, as you know, the British Library is a very large enterprise worth £100 million a year in funding and support. The very nature of the creative industries means that they tend to be made up of SMEs, and by definition the programme benefits them. We in this country are very good—and I pay tribute to the officials behind this—at securing this grant funding. We have had a focus on this fund, and we have people who understand how it works and are able to access the funds appropriately.

Q4 The Chairman: On the question of added value, if there were a fund of money that gave out similar amounts of funding, is there something extra that would happen because it came from Europe? Would it have a stamp on it, as it were?

Ed Vaizey: If the fund was solely a UK fund as opposed to a European one, you could debate whether or not one was recycling money in the sense that the UK's contribution to the EU was then coming back to support the creative industries, but there is probably added value in that the fund is very focused on international work and supporting cross-border cultural exchanges. By encouraging applicants who are applying for the fund to think about what they will do across Europe or internationally, it probably does add value.

Q5 Lord Skidelsky: As part of the Creative Europe proposal, I understand that the Commission would like to allocate €210 million to a new financial guarantee facility, which it is expected would be able to leverage up to €1 billion in bank loans and would be managed by the European Investment Fund. I am told that the Government are opposed to the creation of such a facility because, among other things, the sums involved would be too small. As an example of an existing facility, though, there is currently the MEDIA production guarantee fund which has a capitalisation of €2 million—that is, 100 times smaller than the proposed new financial facility. That is a leap in amount. How can the new proposal be too small if the existing proposals are 100 times smaller? What is the basis of the Government's opposition to the Commission proposal?

Ed Vaizey: Unless I am very much mistaken, my understanding is that we oppose the facility in principle. We were not sure that it would be effective. There are various schemes—UK and European—that help to support small and medium-sized enterprises in getting access to finance, which is a live issue for the creative industries. There is a debate about whether this sector is a riskier investment than mainstream businesses. I understand that we oppose the facility because we are not sure that it is right to proceed on a sector-specific basis and it would be better, if there is to be a financial instrument, for that to be on a non-sector-specific basis—although, to be slightly legalistic, I reserve the Government's right to oppose anything on a non-sector-specific basis. There is a feeling in Government that if this facility were agreed then other business sectors would come forward and say, "Well, you've agreed to a financial facility for the creative industries; why don't you agree a financial facility for X, Y and Z sectors?". There is a also a risk in creating a financial facility that we will give support where it is not needed, and that banks and businesses that are already very active in this sector and might already be lending or have access to finance will simply say, "Here's a new opportunity to get some guaranteed finance so we'll fill that space". We have seen no evidence that this would open up financial access opportunities to a new range of businesses in the creative sector which currently find that a difficult issue.

Q6 Lord Skidelsky: Two points strike me from what you have said. First, this business is risky, and a risky business always has difficulty in raising finance from banks, especially at the moment when there is a lot of risk aversion around. Secondly, the banks are shuttered. I would have thought—sorry, I am asking a question and should not be stating an opinion—that this would be a way of getting money flowing into this area, which after all is an area that to a large extent defines Europe, including the UK as a member of the EU.

Ed Vaizey: To a certain extent, your second point echoes the point that I was making earlier about where a potential disagreement might lie. If one is concerned about the level of bank lending to small and medium-sized enterprises, the Government's contention is that one should be concerned across the piece about bank lending. As you will know, the Chancellor has put forward various loan guarantee schemes and the like, as well as putting pressure on the banks to lend. His approach has been to encourage lending across all sectors.

There are two points in response to question of the creative industries being a risky business. First, there are a number of schemes in the UK such as the enterprise investment scheme, now evolving into the seed enterprise investment scheme, which are designed in effect to give investors a great deal of tax relief—rewarding them, you could argue—for investing in risky businesses. The second more general point about investing in the creative industries, from where I am sitting in terms of my engagement with the creative industries and with investors, is that there is an important education role to take with investors to introduce them more and more to those industries. I have been to quite a few seminars and conferences where investors are educated about the potential of the creative industries. Those investors who are experienced at investing in the creative industries say that they are not actually that different from mainstream businesses—there are the same problems and opportunities. In terms of taking a small enterprise and growing it, it is much more about the skill of the management and the team than necessarily an inherent risk in the product itself. The investment climate for the creative industries is a very live debate, but I am not sure that the proposed financial guarantee facility would be a panacea.

Q7 The Chairman: I take the points that you have made on that; you say that the facility is not a panacea, and I think that is right. However, it might serve as some kind of bridging mechanism while we are still in the process, as you say, of educating potential investors. I think that people do have a slightly different attitude to risk in the cultural and creative industries to that in other sectors. Could the loan fulfil that role, not as an end in itself but on the way to somewhere else? Do you have any evidence that our creative organisations have already benefited from existing financial facilities that you consider to be more appropriate for this purpose? I think that you have already mentioned one investment pot, but I wondered whether there were any others.

Ed Vaizey: It is a perfectly legitimate argument that the financial facility could potentially be a bridging mechanism while we carry out this education role. My concern would be that once it was established it would never be removed; it might become an ongoing financial burden on the European budget, and we might find three or four years down the line that the high hopes that we had had for the financial guarantee facility had somewhat dissipated and it had effectively become a pot of money for savvy investors to access when in any event they could always access money in a mainstream fashion. That would be one major concern about having it as a temporary facility for that period. The other concern, which I have already expressed, is that if you produced a financial guarantee facility for this sector, you would have various other sectors banging on the door saying, "If that's appropriate for the creative industries, what about us?".

On the question of how the creative industries have benefited from financial instruments, from my perspective in the UK I know that the Enterprise Investment Scheme (EIS) is seen by many creative industries and investment funds as a good scheme for them to use to invest in creative industries. The games industry takes advantage of the research and development tax credit, to a certain extent; to some of the bigger games companies it is probably worth on average 2% or 3% of their investment. It tends to be the bigger companies that take advantage of it because they tend to employ one or two people who are absolutely focused on jumping through the hoops to secure that tax credit. Venture capital trusts have also been used to support the creative industries. The film tax credit has been a great success, not just in supporting UK cultural films made by independent producers in the UK but in attracting inward investment.

The Chairman: Thank you. If you have any relevant statistics or written evidence that we do not already have, it would be helpful if your officials could send us some after this session.

Ed Vaizey: I will certainly do that.

Q8 Baroness Scott of Needham Market: The Commission is proposing what you could describe as an enthusiastic 37% increase in the total budget compared with the predecessor programmes, although it is fair to say that it is one-200th of 1% so it is very small in the overall pot. Is your objection part of a broader government concern about expenditure within the multiannual financial framework, or do you have specific concerns about spending money on the Creative Europe proposal?

Ed Vaizey: The adjective "enthusiastic" should enter the political lexicon to describe any controversial proposal; that might get you past some objections. From my perspective, I would like the entire EU budget to be devoted to the cultural and creative industries—that would be a very effective use of money. On one level it is unusual for me as a Culture Minister to oppose a proposed substantial increase in a budget designed to support the cultural and creative industries, but I do oppose it because I very much sign up to the Government's position that in times of great economic austerity, when the European Union should be focused on growth, looking hard at its budget and the money it spends and reducing it if possible, it would be terribly wrong for me, given my own particular passion, to say, "That's all very well but we'll take the increase in the culture programme". The Government's position is that the EU should be freezing its budget for the next six financial years, and that is absolutely right. We oppose the increase proposed in the culture programme because that is consistent with the position of seeking a freeze in the budget.

Q9 Baroness Scott of Needham Market: Given your responsibilities, are you not tempted by the fact that under the predecessor programmes the UK has benefited proportionately more than any of the other large states? There is no reason to imagine that that would not continue. Are you not tempted to be a bit more supportive, given that the UK does very well out of this?

Ed Vaizey: I am always tempted, but in this life one has to impose a self-denying ordinance. I feel strongly indeed that it would be a great victory for the EU, particularly in terms of public opinion, if it came forward with a budget freeze, recognised the difficulties that many EU citizens are labouring under with their own budgets and financial positions and said, "We're going to get our house in order and effectively reduce our budget with a real-terms freeze in spending".

Q10 Baroness Scott of Needham Market: If that were to be the case and this budget and others were cut back, what sort of programmes do you think should be prioritised in a Creative Europe fund if there were rather less money going into it?

Ed Vaizey: If we were successful in negotiating a budget freeze for the European Union and therefore a freeze in the culture programme, we would then say to the Commission, "In that case don't go ahead with the financial guarantee scheme". The cross-sectoral strand is another strand where we might see scope for saving.

Q11 The Chairman: I just want to clarify—when you say "freeze", do you mean a real-terms freeze linked to inflation?

Ed Vaizey: A real-terms freeze, yes.

Q12 Lord Foulkes of Cumnock: I am slightly perplexed. In reply to Baroness Scott you say that you do not want any increase—you want a freeze—because the focus should be on growth. In replying to the Chairman earlier, though, you said that the cultural sector was particularly good at economic growth and job creation. Surely spending more money would provide economic growth and job creation in the cultural sector. Is there not a bit of a contradiction?

Ed Vaizey: This is where you and I will probably disagree, Lord Foulkes. You probably would not have to, but I must defer to the economic expertise of Lord Skidelsky in this regard: in my view you create growth not necessarily by government or Commission spending but by getting out of the way of business and allowing the private sector to grow. I do not see a direct link between increased spending in Commission budgets and growth in particular sectors.

Q13 Lord Foulkes of Cumnock: With regard to the cuts that you have had in the domestic budget—Arts Council England by 30%, English Heritage by 32%—is any of the loss there likely to be made up if European money is forthcoming?

Ed Vaizey: We have never seen European money as filling a gap where government money has been reduced. In this country we are lucky that we have the lottery supporting the arts and heritage. As you know, we have substantially increased the proportion of lottery funding that goes to the arts and heritage to 20% for each of them. There is an interesting socioeconomic phenomenon that more people are now playing the lottery, and we have worked out that overall the Arts Council's budget will probably be reduced by less than 5% over the next five years because of the increase in the proportion of the lottery going to it as well as in the number of people playing it.

Q14 Lord Foulkes of Cumnock: Why do you think that lottery money in that sector is good but any more money from Europe by increasing the MFF is not?

Ed Vaizey: Traditionally, over the past 20 years, the lottery has been seen as one of the elements that support funding for the arts and heritage. It is not there to support statutory provision, of course—the core grants given by the Arts Council to what are now known as national portfolio organisations come out of grant in aid. When we reached our settlement with the Arts Council, we were careful to ensure that we targeted our savings at—I am afraid it is a terrible phrase—the "back office" as opposed to the front line, so the Arts Council has reduced its grants to national portfolio organisations by just under 15% and will find savings elsewhere. For example, certain programmes that perhaps will have had support in this Committee and elsewhere, such as Creative England, have had to be cancelled.

Lottery money supports the arts, and has done for many years, through grants for the arts and similar schemes. It is used to support touring work by arts organisations, and for the past 20 years it has been part of the mix of arts funding in this country. However, we have never regarded European money as being a banked sum of money that we can factor in as part of our perception of the overall support for UK cultural industries.

The Chairman: I apologise, by the way, as I should have declared my numerous interests in the arts, which I think you are aware of.
Ed Vaizey: There is a whole page of interests here, Chairman, showing your passion for the cultural and creative industries.

Q15 The Chairman: It was the mention of English Heritage that made me remember that.

My next question is about the consultation exercise, which I think closes at the end of this week. Have you had a chance to look at the responses? Have they expressed support? What kinds of views have they expressed in relation to the Creative Europe proposal, including the proposed loan facility and funding increase?

Ed Vaizey: I have not looked personally at each response but I have had a report from my officials about them. I am told that we have received about half a dozen responses, generally supportive of the proposal. They might all come at once at the end of the consultation. Apparently they have expressed caution about the proposed loan facility and how it would work in practice. I do not know whether the small amount of responses indicates the level of interest across the sector in the proposal or whether there will be a sudden rush of responses. I have a couple of examples in front of me. The British Screen Advisory Council has expressed concerns about the proposed financial facility, and has said that it wants investors to have a look at it to assess how effective it is. I suspect that that body is coming from a different perspective, not simply opposing it in the manner that I am but asking whether it is a workable proposal from an investor's point of view. The Electric Shadow Company has expressed a view in support of these programmes, particularly seeing them as supporting indigenous UK film production as opposed to inward investment in UK film production.

Q16 The Chairman: If the number of responses were to remain at around half a dozen, how would you feel about that? Would you feel that it was a self-selecting group, and would it be an adequate sample from which to draw conclusions? How would you work with that relatively small number?

Ed Vaizey: That is a very good point. If it stuck at half a dozen responses, I would be concerned. Given the level of benefit that there has been in the 2006-10 period, particularly for some of the very well known organisations like the British Library, if the consultation closed and that had been the level of response, I would want to have a discussion with my officials about whether we felt that we had adequately publicised this proposal, and possibly a discussion with the Arts Council and English Heritage to see whether they felt that it had not been flagged up enough. At the close of the consultation I would like to write to the Committee with some reflection about what the level of response says about our perception of the engagement with the consultation or support for the proposal.

The Chairman: We have three witnesses next week: Ann Branch, head of unit in the European Commission's DG Education and Culture; someone from Visiting Arts and someone from the British Film Institute representing MEDIA Desk UK. Doubtless they will give some fairly robust answers to these questions which, hopefully, will be useful for you as well.

Q17 Viscount Bridgeman: Mr Vaizey, you remarked briefly on the UK film industry. Lord Smith's committee laid great emphasis on the involvement with Europe. The financial benefits of the MEDIA programme were €66 million 2007-11, half of which was directed to UK companies and the other to non-UK European distributors. These funds have very much helped to boost British films in other European countries—140 films to the level of $30 million in that period, including "The Iron Lady", "Slumdog Millionaire" and "The King's Speech", which had remarkably low budgets in comparison with the usual cost of these films. They show the sort of return on investment that these films can make. Following the publication of Lord Smith's review of the UK film industry, how do the Government intend to implement the recommendations that engage the European dimension?

Ed Vaizey: My understanding from my engagement with the UK film industry is that it takes this programme seriously. As I referred to when I was speaking earlier in response to the Chairman, this is one of the areas where I have been impressed by how the UK Film Council and now the BFI have had officials who know the programme inside out and are able to use it to benefit UK film-makers. We want to continue to engage with European colleagues through the current MEDIA programme via the British Film Institute, which is now responsible for all UK film policy. The programme has three main objectives: first, to preserve and enhance European cultural diversity; secondly, to increase the circulation of what they call "audiovisual works" but you and I would call "films", which it has been successful in doing; and, thirdly, to strengthen the competitiveness of the film industry. We support those objectives and I understand that we will continue to support the MEDIA programme and the BFI in working to ensure that it benefits UK film-makers as much as possible.

Q18 Lord Foulkes of Cumnock: Do you meet your fellow Culture Ministers from the other countries of Europe and discuss the development of the European dimension of the film industry?

Ed Vaizey: I have rarely met my fellow Culture Ministers. There has been only one Culture Council—I shall have to look at the records and, if necessary, write to correct the record—which I was not able to make. There is a great opportunity during the Olympics and Paralympics: the Scottish Government are going to host a cultural summit between the end of the Olympic and the beginning of the Paralympics, during the Edinburgh International Festival. That will be an important occasion on which to engage with European Culture Ministers, as well as engaging with Culture Ministers from outside Europe, on all these issues.

Q19 Lord Foulkes of Cumnock: I am very encouraged that it is the Scottish Government that are taking the initiative in bringing your counterparts together. Do you ever meet on a bilateral basis with the French or Greek Culture Ministers?

Ed Vaizey: I met the French Culture Minister at the Venice architecture biennale, in a brief meeting at the French pavilion. I am trying to recall if I have met others. I met the Russian Culture Minister, although obviously Russia is not technically part of the European Union, and I think that was also in Venice, which tends to be where I bump into my fellow Culture Ministers.

Q20 Lord Foulkes of Cumnock: I am not clear how you can follow up the European dimension that Lord Smith's committee recommends if you do not meet regularly with your counterparts and talk about what the European Commission is suggesting.

Ed Vaizey: You make a very good point, Lord Foulkes, particularly given the Commission's recent communication on the future of the film tax credit. I think that I have met the Hungarian Culture Minister as well, come to think of it. It is all coming back to me—it is repressed memory syndrome. I will take advice from an experienced politician that I should engage more with my counterparts, particularly on these issues.

Lord Foulkes of Cumnock: I look forward to seeing you at the Edinburgh festival as well.

Ed Vaizey: I am never one to pass up an opportunity to get someone else to do the work, so when the Scottish Government suggested holding this cultural summit I was only too glad to agree. I am sure that somewhere in there some complicated Scottish politics are going on.

Q21 The Chairman: So, to your knowledge, there are no specific structures or mechanisms that regularly bring Culture Ministers together?

Ed Vaizey: There is a European Culture Ministers Council. I go to Brussels a lot for the telecommunications summit council, and there are occasions when telecoms Ministers have a cultural overlap, but as far as I am aware—I will double-check this, and I will write to correct this if I am wrong—there has been only one Culture Ministers Council and I was not able to make it.

Q22 Lord Foulkes of Cumnock: It occurs to me, as an aside, that with a French film doing so well at the Oscars and the awards for British films as well, there is more that we could do now with the French film industry to take advantage of that.

Ed Vaizey: That is right. Across the piece there are successful German and Spanish films and so on, and you have given me some food for thought. For example, I should be more proactive in thinking about how we could use, for example, the BAFTAs, although it is an independent charity that is not there to do the Government's bidding, or the London film festival to invite my fellow culture Ministers to come and immerse themselves in UK culture.

Q23 Lord Foulkes of Cumnock: That is a very helpful response. I turn to the publishing industry, one of the largest creative industries in the United Kingdom with a turnover of £19 billion. Creative Europe suggests that we should use resources to translate 5,500 books into some of the 23 languages of the countries of Europe. How could we take advantage of that to support British publishers, particularly those outside London?

Ed Vaizey: That is a very important point. It is worth making clear, as I think you did in your question, how important the publishing industry is to the UK. It is not often front of mind when it comes to political discussions because it is one of those industries that do not often come to Government demanding a tax credit or a subsidy; it is extraordinarily successful in its own right. Publishing has every right to say that it should have a higher profile in political circles, so I am particularly looking forward to participating in the London Book Fair, where China is this year's official guest nation, to highlight not only the success of UK publishing but its international success as well. I was pleased to see it proposed in the proposal that more than 5,500 books and other literary works should be translated. This would benefit smaller publishers that specialise in publishing translated works as well as publishers that publish original works in English, which will have the opportunity to have their work translated into a wider range of languages. The Commission is keen to encourage the translation of works into English, as they are then more likely to be translated into other languages. That also helps British writers who happen to write in Gaelic or Welsh. We want to work with the Publishers Association, a very effective trade body ably led by Richard Mollet, to ensure that these opportunities are appreciated. To pick up on what Lord Foulkes said, when we work with the Publishers Association the focus is not just on engaging with the major publishing houses, which will probably be fully aware of this facility, but on ensuring that that smaller publishers are aware of this opportunity, particularly those outside London.

Q24 Lord Foulkes of Cumnock: That is very helpful. In our House we are very conscious of the importance of publishing when we have Baroness Rendell and Lord Dobbs among us, not to mention Lord Fellowes.

Ed Vaizey: We should not forget Baroness James.

The Chairman: Yes, we have many writers.

Ed Vaizey: And Lord Mandelson, whose autobiography was a bestseller.

The Chairman: Are we talking about works of fiction? I have no comment.

Q25 Baroness Scott of Needham Market: I was going to say that, Chairman, but I thought it would be quite unseemly.

I want to ask about film distribution. A few years ago, when I was on the House of Lords Communications Committee, we undertook an inquiry into the British film industry. One of the issues highlighted was the question of distribution and what I could fairly describe as the stranglehold by a very few American distributors. Do you have any thoughts about whether there is a role for Government either here or in a European context—either European states or the EU—in helping the distribution industry? There is a real link here to independent production and moving away from big blockbuster movies.

Ed Vaizey: That is a massive issue. It is the logjam in the future success of the British film industry. As you know, what tends to happen is that after a film is green-lit, if you like, a lot of people then need development money, so the film policy review emphasised a clear focus on development assistance. Then you make the film but afterwards you do your distribution deal, and that is when you give up a lot of your IP. So what we regard as huge successes in independent British film production tend also to be enormous financial successes for the distributors—"Slumdog Millionaire" being a very good example where very little money came back to the UK because they had to rely on an American film distributor. That is a big problem. One of the recommendations from Lord Smith's film policy review was to ensure that proposals that come to the BFI for funding come with a distribution deal, so the hope is that independent productions can tie up with a distributor earlier before giving away the IP, so that when the funding is put in place the IP can be more fairly distributed between the producer and the distributor. We are also looking at whether we can use a network of what are known as cross-art venues—what you or I might call art-house cinemas—to support distribution within the UK, so that independent British films can be seen by audiences across the country without necessarily relying on the big distributors.

The big question in trying to predict the future is how distribution will change. It is not just about getting films out into cinemas or on television but more and more about getting them out through what are known as over-the-top services such as Netflix and LOVEFiLM. I know that there is concern among the British film community, although this is vigorously resisted, that distributors do not give enough of the cut to films and that companies like Sky do not pay enough for British films. Those are all live issues that the film policy review addressed, and we hope in response that the BFI will take them a stage further.

Q26 The Chairman: There are some proposals in Creative Europe that are extraordinarily hands-on, such as funding for individual cinemas to show certain films. Do you think that is going too far in terms of intervention at a European level? Do you think it is better left to member states? Should we be quite so hands-on?

Ed Vaizey: My instinct is not to be too hands-on. I am always wary if you get into a position where you are effectively directly subsidising a particular facility or exhibition. My instinct would be to be cautious on that. If there is a way that we can use the public money that finances film production in the UK to ensure better distribution deals with a better cut of the profits for independent film-makers, that would be a more sustainable way forward.

Q27 The Chairman: There is the issue of the cut, as you say, but there is also the issue of the range of material that is deemed to be popular or indeed accessible to audiences. You mentioned art-house; film-makers say to me that it is really hard to get a distributor to see beyond quite a narrow view of what an audience will want to watch, and then it becomes a self-fulfilling prophecy.

Ed Vaizey: That is weird, is it not? I know that it is a deeply dull and boring cliché, but I will say it anyway: the point has been made on every programme about film that if I came to you as an exhibitor and said, "I've got this great film—it's a silent movie shot in black and white and made by the French", you would say, "Get out of my house". It is odd that they seek to focus only on blockbusters or quite homogenous films when year after year the films that sweep the board are the difficult, awkward, non-mainstream ones that not just critics but audiences end up loving. I think that people love quality, and they love movies with heart—"The Descendants" and "The Help" are also good examples of films that are not smash-and-grab action movies but that audiences love.

The Chairman: Minister, thank you for your most helpful responses. If anything else should occur to you or your officials, we would welcome any further written evidence.

Yvette Vaughan Jones, Executive Director, Visiting Arts; Ann Branch, European Commission, DG Education and Culture and Agnieszka Moody, Director, MEDIA Desk UK – Oral Evidence (QQ28-48)

Transcript to be found under Agnieszka Moody, Director, MEDIA Desk UK – Creative Europe

Yvette Vaughan Jones, Executive Director, Visiting Arts; Ann Branch, European Commission, DG Education and Culture and Agnieszka Moody, Director, MEDIA Desk UK – Oral Evidence (QQ28-48)

David Willets MP, Minister of State for Universities and Science Department for Business, Innovation and Skills — Oral Evidence (QQ70-91)

MODERNISATION OF HIGHER EDUCATION IN EUROPE: THE EU CONTRIBUTION

Evidence Session No. 4. *Heard in Public.* *Questions 70 - 91*

THURSDAY 12 JANUARY 2012

Members present

Baroness Young of Hornsey (Chairman)
Lord Cotter
Lord Eames
Lord Foulkes of Cumnock
Baroness Henig
Lord Lexden
Baroness Prosser
Lord Skidelsky

Examination of Witness

David Willetts MP, Minister of State for Universities and Science, Department for Business, Innovation and Skills

Q70 The Chairman: Good morning, Minister. Thank you very much for coming along this morning and sparing us a significant chunk of time. I know that you know the score, but I have to give the housekeeping notes to start with. Members' interests are recorded in the Register of Lords' Interests and a list of declared interests is on the witness table. The session is on the record. It is being webcast live and will subsequently be available through the Parliamentary website. You will receive a transcript of the session to check and correct and this will be put on the record on the Parliamentary website. Perhaps you could begin by stating for the record your name—I see that you are not accompanied by any officials. If you want to make an opening statement, please feel free to do so, otherwise we will go straight into questions.

Yvette Vaughan Jones, Executive Director, Visiting Arts; Ann Branch, European Commission, DG Education and Culture and Agnieszka Moody, Director, MEDIA Desk UK – Oral Evidence (QQ28-48)

David Willetts: I am David Willetts, Minister for Universities and Science. Obviously, I am very keen to answer the Committee's questions. I think that this is a really valuable inquiry, as we are coming up to the ministerial meeting on Bologna in April. I very much look forward to the Committee's report, which we will draw on in our preparation of our proposals for that ministerial discussion.

Q71 The Chairman: Thank you. In fact, that leads nicely into my first question, which is about how beneficial the Bologna Process has been for the UK. You mentioned the upcoming ministerial conference and I wonder whether you anticipate any significant outcomes from that. Perhaps you could also tell us a little more about the Government's desire for the proposed revision of the professional qualifications directive, taking account of the Bologna dimension. Perhaps we could start off with that.

David Willetts: I think that Bologna is overall a good thing. It is of course an intergovernmental agreement. We believe that it has increased the coherence, transparency and comparability of qualifications and credits in Europe. Although one must not be complacent, I think that it is true to say that Britain has had a big influence in shaping the Bologna agenda. It very much ties in with the structure of higher education in Britain, which is a good thing. I notice whenever I am at international meetings that our higher education system is well regarded and well respected. Bologna is also a mechanism for improving exchange of students and researchers through greater mutual recognition and mutual trust. That is a good thing, because increasingly research is an international activity. To be frank, we are just beginning our process of preparing for the April meeting—we are going to have meetings with key stakeholders and, as I said, we will study this Committee's report—and at the moment it is too early to say exactly what will emerge from that. I suspect that there will be commitments to do more to implement Bologna. Although we have done very well in implementing Bologna, other members of Bologna still have more to do, so I suspect that implementation will be an important part of the discussions. On the revision of the Professional Qualifications Directive, our aim is to try to ensure that the levels of education outlined in the Directive are aligned with the Bologna cycles so that training courses towards regulated professions do not have to work to two different benchmarks.

Q72 The Chairman: Thank you very much. How engaged do you think higher education institutions here are with the process? Do you have a view on that?

David Willetts: I think that it is mixed. I would say that in general they are engaged. Perhaps later in the questioning we will focus on areas where we need to do better. In KICs, for example, I was rather disappointed with the outcome of the first round and I hope that we can do better there, but I think that in general we are engaged. We know the structural issues that we face. When we look at the flow of students and researchers into Britain, it is clear that we attract many more in. I personally think that it would be a very good thing if rather more British students had the experience of doing some study or research abroad, so I think that we could do more there. Because our most prestigious universities are genuinely global, they tend to look around the world, rather than simply thinking of connections to the continent of Europe. But I think that, net, there are good levels of engagement, although I am sure that this Committee will have ideas about how we can do even better.

Q73 The Chairman: Some of the points that you have raised will be raised later on during this session. Obviously, the economic situation is a huge challenge for everybody everywhere, but, leaving that aside for the moment at least, what other major challenges do you see for the Bologna Process in the coming years?

David Willetts: There is still more to be done on the frameworks for qualifications. We expect the Bologna follow-up group to focus on their priorities of transparency, mobility and qualifications frameworks, so that is an area where there is more to be done. We in the coalition attach a lot of importance to transparency and the release of data that, for example, prospective students can look at and I think that there is more that can be done across Europe on that type of agenda. One of our strengths in Britain is the autonomy of our universities. I notice in discussions that my European colleagues are looking at reforms that strengthen the autonomy of their institutions. For all of us, when money is tight and times are tight, there is the question of strengthening links with business and the extent to which, without sacrificing their core mission, universities can secure more funding through more engagement with business.

Q74 Baroness Prosser: Good morning. I wanted to ask you something about the Innovation Union within the context of the 2020 strategy and all that stuff. What role do you think the EU can play in stimulating closer collaboration between higher education institutions and business? Would you be concerned within that context about duplication between European Innovation Partnerships and Knowledge and Innovation Communities?

David Willetts: First, I am broadly in favour of what the Commission is trying to do. We are still at an early stage. It made its proposals for Horizon 2020 just before Christmas and we had our first exploratory discussion in Brussels in December. We broadly welcome the Commission's proposals. They have tried to reflect our belief that, for example, excellence is the crucial criterion for funding. If you want to achieve regional policy objectives, you do it through the structural funds; you do not compromise on the function of Horizon 2020. There have been problems with the bureaucracy of, for example, securing individual grant funding, which the Commission says it will tackle. For the future, I confess to the Committee that sometimes I find it rather hard to distinguish between a host of different EU initiatives; the exact difference between them is not something on which I would like to be answering on "Mastermind". It can be tricky, which is why part of the agenda in the EU is sometimes to simplify these things and bring them all together. Sometimes the subtle differences between them escape me.

Q75 Baroness Prosser: Do you think that these programmes give the possibility for greater collaboration between British institutions and universities and the institutions and universities of other European countries?

David Willetts: Yes, they do. It is a very fair criterion. If you are looking for research funding, they do not want to fund just a single institution; they want to fund an institution that has at least one partnership with another institution in another country. I think that that is an admirable way of proceeding. It is a very useful incentive to getting universities to look outside their national boundaries, which is a good thing.

Q76 Lord Skidelsky: I see that the national curriculum is being reviewed for the umpteenth time. Are you confident that modern languages will emerge in a stronger position, especially at the secondary level, from that review? Is that not key to getting our students on to the continent?

David Willetts: Lord Skidelsky is right that our weakness in foreign languages is a big problem. I know that my colleague Michael Gove, the Secretary of State for Education, is absolutely committed to this. It is very much his departmental responsibility and not mine. The fact that modern languages are included in his EBacc measure of GCSE performance appears already to be having an effect on the number of people submitted to GCSEs. The DfE tells me that, from September 2011, 52% of year 9 pupils in schools responding to its survey were due to study a foreign language, which is up nine percentage points from GCSE entries in 2010. We hope that the EBacc measure will help. For the review of the national curriculum, the expert panel has recommended that a language should be statutory at key stages 2 to 4. I know that the Secretary of State for Education is considering that recommendation at the moment.

Q77 Lord Skidelsky: What is your view about how tuition fees may result in fewer European students undertaking Erasmus programmes in this country? Do you fear that they may be a deterrent? In addition, English language teaching on the continent has become a lot cheaper and students may take courses there rather than in the UK.

David Willetts: We have not yet had the final results from UCAS. The very provisional evidence so far is interesting. In total, the number of non-EU prospective students applying to universities through UCAS seems to be holding up, but there appears so far to have been a modest decline in applications from EU students. One could speculate about lots of reasons for that. I accept that our universities face an increasingly competitive challenge from elsewhere in the EU. My view is that globalisation—to use that cliché—is still at its very early stages in HE. One of the competitive challenges that our universities have to face is not just that English language schools on the continent are becoming better but that university courses are being taught in English in continental universities. To be able to do engineering at a German university taught in English is a strong competitive challenge for us. I do not think that we should hide from it. It is a separate and controversial debate but one of the reasons for our reforms is precisely to get a focus back on the quality of the teaching experience. Yes, we should not be complacent, because there are these types of competitive pressure.

Q78 Baroness Henig: Good morning. In a former life, I headed up a university humanities department as dean of arts and humanities and I had a fair amount of involvement with the Erasmus programme. Apart from language issues, on which you have already touched, there were enormous difficulties in getting students on to Erasmus programmes, partly because of financial issues and, as you have mentioned, the teaching experience, which on the continent looked very different for students who were used to a tutorial system, for example. There are also all sorts of issues about assessment. What can be done to encourage a more diverse body of students to engage with the Erasmus programme? The research is all showing very narrow bands of students—for example, language students and a lot of female students—but we really need to broaden the number going on to Erasmus programmes.

David Willetts: I completely agree with you. I am sorry to push the question back to you, but this would be a really useful area on which to get advice from this Committee. It is a bit tricky and one is always wary of a kind of "Auf Wiedersehen, Pet" caricature where we say, "Oh go and study abroad". It is clearly an enriching experience for individuals personally. Our businesspeople say that one of the problems is around British graduates being monocultural—not having another language or not having lived in another country. There is more that we can do to communicate the value to graduates, including employability, which is one of the things that they increasingly think about. The evidence is that that element of the international experience significantly increases employment prospects. Of course, financial support is available. I think that at the moment you collect several hundred euros a month as a kind of maintenance payment as part of Erasmus. There is obviously a set of issues around fees and fee waivers. I have just received a letter from Colin Riordan, the Vice-Chancellor of the University of Essex, who has been doing some work on that. As you would expect of Colin, he has come up with ingenious ideas for whether the loan scheme could be extended or could be on some special terms. It is very early days, but the issues are, I am afraid, frankly financial ones about what we can afford. As we have more time, we certainly will consider those types of recommendations as well.

Baroness Henig: Would it be possible to forward to the Committee further information on the breakdown of participants in Erasmus by ethnicity, age, disabilities and so on? That would be quite helpful to us.

David Willetts: Yes. Whatever information we have I am very happy to share with the Committee.

The Chairman: Thank you very much. That would be very helpful.

Q79 Lord Eames: Minister, in a sense you have touched on this already, but I am interested in the Masters level loan facility. The obvious conclusion is that it is a good idea if it increases mobility. It would make that easier, particularly at the present time. Is that too simple a conclusion and would you welcome it?

David Willetts: It certainly has that appeal. There are eloquent advocates of a Masters loan scheme, including, I think, even the NUS in its oral evidence to you. I was encouraged to see the NUS coming here and recommending a student loan scheme. That was very good. So there are arguments in favour. Of course, again, I am afraid that we are operating within financial pressure and, although you would get some of the money back, you could not work on the basis that you would get all the money back. You would certainly have to make a realistic estimate of the funding that you might not get back, which would give rise to a set of public expenditure issues. I cannot in any way commit us to doing it, but it is an interesting idea and we will consider it. But it would cost money.

Q80 Lord Eames: If it comes to pass that you can say eventually that it would definitely increase mobility at the Masters level, would the temptation be to say that such success could lead us into another field or other levels? Is that too simple?

David Willetts: Sorry. What do you mean when you refer to leading to other fields?

Lord Eames: We have succeeded at the Masters level, so to speak, and it has increased mobility. If the thinking that has gone into it at a Masters level has been a success, would the Government be tempted to say, "Well, let's increase the area we are looking at"?

David Willetts: Are you thinking of doctorates or something?

Lord Eames: I am thinking about PhDs and so on. I recognise your reservations about finance—of course I do—but should it turn out in the future to be a success and mobility has obviously increased at that level, is a temptation likely to be put to you to move into the doctorate level?

David Willetts: I am obviously very wary, especially when someone of your background starts talking to me about leading me into the paths of temptation.

Lord Eames: I deserved that.

David Willetts: You are inviting me to cross several hurdles. I cannot even commit on the loan scheme for Masters courses, let alone going further. All I would say is that I take heart from the fact that by and large these are worthwhile experiences and worthwhile in their own right. But they also have a financial value and therefore you can loan people money and expect a repayment subsequently after they are in employment. The fact that this is now widely recognised as a way of financing study at this level is a sign of progress—people are not as scared of loans as perhaps they would have been a few years ago. But we will have to take it stage by stage.

Lord Eames: I understand. Thank you.

Q81 Lord Cotter: You spoke in your opening remarks about the importance of mobility and we have talked a lot about that. How do the Government intend to boost the mobility of students and academics, particularly in light of the concerns about new immigration rules not deterring international talent from coming to the UK? On a slightly different subject, a lot of concerns have been expressed to me and others about the difficulty of getting people to come to this country under the business portfolio. You have expressed support for the mobility of students. The Academic Exchange Service encourages mobility in Germany in particular ways, so could you delineate how we could encourage it in this country, as there are concerns that the public sometimes do not understand these issues?

David Willetts: Obviously, the Government as a whole work within the framework of the coalition agreement, which commits us to the control of immigration. On the other hand, we absolutely recognise that higher education is an international activity and we welcome the brightest and the best from around the world. That is essential for the flourishing of our universities and the success of British business. For scientists and researchers, as you know, Tier 1 now has a new category for exceptional talent, which is about achievement in science and the arts. We have also made progress in conversations with the Home Office about Tier 5 to make it easier for temporary visiting academics and researchers. There is certainly no limit on students from the rest of the EU but even internationally there is no numerical limit on the number of students coming to Britain, provided that they are properly qualified and things are done legitimately. So I think that we have tried to strike that balance. The German Academic Exchange Service is well respected and I know that this Committee has been interested in it. It has a lot of funding, but I think that in our way in Britain, through the work of the British Council, through the reputation of our universities and through our open system of attracting researchers and students, we have done pretty well. The net figures are striking. We have approximately 400,000 students from outside the UK coming to study in Britain and we have about 30,000 British-born, UK citizens going to study outside the UK. The figure of 400,000 should be a source of great national pride, but the challenge is the

30,000 the other way—you wonder whether some people are missing out on the opportunity of studying abroad to enrich their background and experiences.

Lord Cotter: It would be very welcome if the Minister could commit himself to keeping an eye on this issue, as it is an ongoing concern.

David Willetts: Yes, and it is regularly raised with me and the Secretary of State—we are very aware of it. The Government as a whole are aware that being open to students, researchers and academics and their being able to come here to research, study or give a guest lecture is very important. It is the lifeblood of an open university system and it is very important that that system is kept open.

Q82 The Chairman: Just before Lord Foulkes comes in, could you say how engaged you think we are in the development of the European Research Area?

David Willetts: I think that we are engaged with it. It is sometimes a bit hard to pin down exactly what it means in practice, but I take it to mean researchers moving around, research projects being shared by researchers in more than one country, mutual recognition of qualifications and all that. We are wholehearted supporters of that. Perhaps I should have said this earlier, but we think that a lot of this can be done through co-operation and intergovernmental action. I take this to be an example of where there are successful EU initiatives but by and large they are not driven by the EU claiming a competence and instructing us to do things, so that we have to wade through a set of directives with an instruction from Brussels. What this shows is that, if you approach it in a constructive spirit and try to work together, you do not need an EU legal competence to make these things happen.

Q83 Lord Foulkes of Cumnock: I wanted to go back to the control of migration and the figure that the Minister mentioned of 400,000. Of course, that is before the new rules have any effect. I agree, as I am sure we all would, on the clampdown on bogus colleges, which is very welcome, but we have read of lots of examples of academics and students having difficulties coming into the United Kingdom. I just wonder what influence your department has not just on the Home Office but on the UK Border Agency, which seems to be almost an autonomous body making its own decisions and not really taking account of the areas that you have been dealing with about getting academics to come in as freely as possible.

David Willetts: Often at my meetings with the Home Secretary and Home Office Ministers the UK Border Agency is also represented. There are two levels of discussion. The first is agreeing the overall policy framework and the second is implementation. I think that the UK Border Agency would accept that, in the early days of the tier system, there were, shall we say, some rather eccentric decisions. The last thing that you want is stories going round the world of a visiting academic from the US coming to give a guest lecture, for which he is paid £50 and a sack of port or something in some ancient college endowment, and being asked where his work permit is. There were problems, but, to be fair to the UK Border Agency, it recognised that there were issues. There has been a lot of exchange, including working-level exchanges between Universities UK and the Border Agency, and it has been trying to provide clear guidance and to tackle some of these things, which do cause embarrassment and awkwardness. I personally think that, even in the past 12 months, the situation with that kind of stuff has got better.

Lord Foulkes of Cumnock: I think that we respect your judgment on this. If you say that you are sure that these eccentricities have been ironed out now, we would go along with it. Are you quite confident about it?

David Willetts: I cannot give you a guarantee that they have 100% gone, but I would say that, especially with the Tier 5 arrangements for visiting academics, the situation is getting better. The conversations are not just the ones that I have had with Home Office Ministers, who, to be fair to them, want the system to work properly—we work together on this—but also, as I say, at working level. I think that we are making progress.

Lord Foulkes of Cumnock: And you will keep an eye on it for us?

David Willetts: Certainly, I assure you.

Q84 The Chairman: I just want to talk about league tables and data. As you know, there is the proposed U-Multirank tool, to which the Government have already expressed their opposition on a number of logical bases. Is there anything that would change your mind on that? Do you think that there is potential use in a ranking tool that is perhaps a little different from those which already exist?

David Willetts: We are very sceptical about it, to put it very crudely, if it is an attempt by the EU Commission to fix a set of rankings in which we do better than we appear to do in the conventional rankings, of which there are three main ones. It is a dangerous parallel, but I am slightly reminded of some of the attempts with the financial rating agencies to say, "Well, we will come up with our own ratings that will ignore the uncomfortable evidence from Standard & Poor's" or whatever. So that will not work. We are in favour of more information. If you just put out the raw material for independent groups to do their own rankings, and if they command consent and respect and are trusted, there is no reason why the three main systems at the moment should not face some alternative challenge. There is an argument that they are very heavily weighted to research and that the teaching experience, which is important, perhaps does not get enough weighting in some of the current systems. I would not rule that out, but we do not think that it is a good use of limited EU resource and we do not want to impose unnecessary burdens on our higher education institutions that would compel them to collect data that they perhaps do not already have to collect. They already complain to me about the burden of data collection.

The Chairman: We have asked a number of people this and we are still waiting for some illumination on the proposed European Tertiary Education Register. We wondered whether you might be able to add anything further. I see your officials shaking their heads behind you.

David Willetts: Fine, well let me shake my head then. The Commission has not released any detailed information, so we have not been able to get a handle on it ourselves.

Q85 The Chairman: No doubt, if you do, in time you will let us know. In its evidence, the NUS expressed doubt about the quality of student mobility data and called for the creation of a data collection and standardisation agency at the EU level to improve the situation. Do you have any views on that subject?

David Willetts: I think that the NUS is right about this—it is nice to be able to say that. We accept that the data are imperfect and that it would be worthwhile to improve them. Again, we have to be a bit careful about the burdens of data collection and cost. But if there are cost-effective ways in which it can be improved, that would be worthwhile.

Q86 Lord Lexden: The European Commission is suggesting that it might involve itself in the promotion of European higher education on the wider world stage. Do you support this proposed internationalisation? If so, how should it be done?

David Willetts: There is always that issue of competence creep, to which I referred earlier. I am not against things being done through European co-operation but it should be when universities and governments think that it is worthwhile. I would not completely rule it out but, in reality, as we have heard with the example of the German arrangements and what is done by the British Council, quite a lot is done nationally. We have rather different national systems: if you are sitting in India or China, you will probably want information about how German, French or British universities work, rather than be thinking generically about European universities. But we would be open-minded if someone could persuade us that this is worthwhile. I suspect that Lord Lexden is not going to be the person to make that case.

Lord Lexden: The Commission talks about developing a strategy. You have probably covered that already, but you might like to say a little more about the validity and possible content of any such strategy.

David Willetts: We would be very wary if it involved any expenditure, because money is tight. We would be very wary if it involved any attempt to establish some EU authority and to impose obligations. I guess that, in general, as I said earlier, the Bologna Process works rather well. I am not convinced that we need a second strand when Bologna is a basis for intergovernmental co-operation. We are very cautious about all this, but we will look at it when it is produced with a degree of wariness as to whether it really will add value.

Q87 Baroness Prosser: This is the penultimate question, as I am sure you will be pleased to hear. Erasmus for All is a proposal to bring together a number of different programmes. Do you think that that is likely to achieve the aim of simplification and greater flexibility? I know that those are not words that normally go with discussion about the European Union, but I would be interested in your view. Do you think that they would be able to move forward and make headway without any further significant increase in funding?

David Willetts: There are two points. The first point is that, in general, as you suggest, it is a good idea to simplify and streamline the process. There should be savings by eliminating the excessive number of different schemes and programmes. That is a good idea, which we would support as improving efficiency. However, the proposal is that the budget for EU mobility programmes for 2014-20 should increase by around 70%, which is completely unrealistic. It is not just that the British Government are committed to saving money and holding down the EU budget; in my meetings in Councils of Ministers at Brussels it is clear that many other member states are also facing budgetary pressures. So that proposal for increased spending is simply impossible.

Q88 Baroness Prosser: How about the role of other funding streams in supporting HE, such as the European Social Fund? Do you see any relationship there?

David Willetts: Yes. The universities of some of the newer Member States in central and eastern Europe sadly suffered terribly through the Second World War and after, but they are now emerging into freedom. When we discuss this, I turn up as a British representative and say that what crucially matters in the funding in the research area is excellence. They come back and say, "That looks awfully like a policy for looking after those who have rather than those who have not". They are on a route to excellence and we want them to be on that route. It would be great if some of these historic European universities came back as leading universities again. That is something we all want to see. We say, "Look, that is where the structural funds can help". These Member States are free to choose how to spend their structural funds. It does not need to all go on new motorways. It is perfectly possible to spend structural fund money on investment in research facilities and in university facilities. As they increase their performance, they can then become eligible for research funding under the criterion of excellence. Yes, I want to see that support. But, as I say, we should not confuse instruments and objectives. It is Tinbergen, isn't it? We allocate instruments to objectives. We have the research funding on the criterion of excellence and we have structural funds to help them develop.

Baroness Prosser: Do you see the relationship between those two, and the background that you have just explained, as relating to this country as well as to Eastern European countries?

David Willetts: Yes, and of course our universities are eligible as well. We think that, in general, this is best in our less affluent regions. We think that there scope there as well.

Q89 The Chairman: This is the last question, which continues the theme of the funds available and Horizon 2020, the new framework programme for research and innovation. It appears that the Government are keen to endorse the Horizon 2020 proposals. We also understand that industry has been less successful than higher education in accessing funds. How do you intend to encourage and facilitate industry to access more funds under this programme heading?

David Willetts: Overall, we have done well out of FP7. We estimate that we are getting about the second largest share of funding. But the Committee is absolutely correct. It appears to be driven by a very strong performance on higher education, which accounts for 69% of all UK FP7 funding to date, whereas British industry gets 17.4% of the FP7 funding coming to the UK. That is a different balance from that in many other member states and is below the average. The average across FP7 is that industry gets about 23.3% of FP7 funding, so there is a challenge there. Our understanding is that it is not that industry applications have a lower success rate; it is that there are fewer industrial bids in the first place. That is where the problem lies. Again, this Committee may have ideas. Certainly, one thing that industry complains about is the bureaucracy and complexity of the procedure. It is a point that I have made to the Commissioner and is one of the reasons why in the proposals for Horizon 2020 there are suggestions for significant simplification of procedures.

The Chairman: Is there general knowledge and awareness in industry about the possibility of accessing these funds? Is that an issue?

David Willetts: I think that that is another area where we could do better. There are national contact points but they are probably not as well known as they should be. Again, working with the Technology Strategy Board, we are looking at this as an area where we should improve our performance.

Q90 The Chairman: In the negotiations on the Multiannual Financial Framework, will the Government be supporting a greater proportion of funds being allocated to this heading?

David Willetts: The Government's overall position on this is that the EU budget needs to be held down. We do not just believe in fiscal restraint domestically; we think that we have to practise it in Europe. I guess that in our ideal world we would see research as a higher proportion of a smaller total budget. That will obviously be a crucial area for negotiation. The Prime Minister has said that the maximum acceptable expenditure increase through the next MFF is a real freeze in payments. That is our position.

Q91 The Chairman: The last question, which I meant to ask you earlier, is on the European Credit Transfer System. Do you have any particular views on that, given that some critical comment has been made about its not being fit for purpose and so on? Do you think that it could be improved or whether it is worth putting effort into?

David Willetts: Yes, I think that there is still more that we can do, because it needs to be improved. Progress is already being made but, again, I would be interested in this Committee's ideas. I accept that it is not yet fully fit for purpose.

The Chairman: Any other questions from colleagues? If not, thank you very much indeed for your fulsome and open responses. No doubt you are looking forward to receiving our report.

David Willetts: Thank you very much.