AN AGENDA FOR A REFORMED COHESION POLICY *

by Fabrizio Barca #

# Director General, Ministry of Economy and Finance, Italy
Today, there is a consensus that the European Union should:
- be more “people-oriented” and strengthen its “social agenda”
- “modernize” its budget and make it more “focused on results”

But the direction of change is still very open:
- the budget review has insofar failed to produce a substantive high level debate
- there are conflicting views on the rationale, results and need of cohesion policy
- a comprehensive cultural attack against any “space-aware policy” has been launched (WB Report “Reshaping Economic Geography”)
- a provisional and informal Commission document on the topic shows a strong orientation towards an alternative, sectorial approach to economic and social development
- the consultation paper “EU 2020”, in pinpointing the priorities of Knowledge, Inclusive Society and Greener Economy, does not provide any assessment of the past overall strategy, nor any idea on the specific contribution of the EU budget
PROLOGUE 2 – THE PROPOSAL FOR REFORM

➢ CONCEPT
  • A development policy for all places of the Union is indispensable for the Union’s very existence
  • Cohesion policy, if interpreted as a “place-based development policy”, is the modern and only way for the EU to perform its development task

➢ GOVERNANCE
  • Cohesion policy needs a fundamental change of direction
  • Relaunching requires a reform of the priorities and governance based on:
    – concentration
    – contracts aimed at results
    – a new metric
    – strengthening the competence of the Commission
    – public scrutiny through new political checks and balances
WHY DOES THE UNION NEED A DEVELOPMENT POLICY? (I)

- Every Union of States (with unified markets) requires a development policy:
  - The free circulation of labour, capital and goods does not produce by itself an improvement in the quality of life of the citizens of a Union. It does create new opportunities, but also new threats.
  - A development policy is needed to enable all the citizens of a Union with the chance to take the opportunities and to defy the threats: this is what the citizens of a Union expect.

- The European Union is no exception. The EU Treaty commits the Union to pursue “harmonious development” both
  - indirectly, by taking the task into account in designing any policy,
  - directly, through dedicated Funds, or “cohesion policy”.

- After successfully promoting market unification and knocking down many barriers to the mobility of citizens, goods and capital, the European Union is presently having great difficulties both in pushing down the remaining barriers and in fulfilling its citizens’ expectations to:
  - take advantage of the opportunities of market unification
  - fight its threats to their standards of living

- The very success of relaunching the Single Market depends on “harmonious development” being successfully pursued.
WHY DOES THE UNION NEED A DEVELOPMENT POLICY? (II)

1. Policy concept

➢ There are several issues where tensions are high:
  • when the EU opens the internal borders and lets its citizens to move freely and *de facto* promote inflows of migrants from outside ⇒ the EU must then provide the ways for the migrants to enjoy the same basic social rights (at least the same public services) enjoyed by the citizens of the places where they migrate and for the latter not to see a worsening of their social rights;
  • when the EU adopts a strategy for mitigating climate change ⇒ the EU must then provide the places mostly affected by this strategy with the means to innovate their economy;
  • when the EU creates an internal market and prevents any State and Region from tackling its troubles by means of State-aids or by a regional differentiation of tax rates (which would unleash beggar-they-neighbor conflicts) ⇒ the EU must then provide the means to regain comparative advantages.

➢ The EU is blamed if expectations are not met:
  • *citizens* oppose labour mobility
  • *firms* oppose market liberalization

➢ These effects are even stronger at the time of economic crisis

➢ In this context, barriers to the Single Market will not go down and possibly rise again, while national and regional ties will tend to prevail and might well undo the Union
WHAT IS THE MODEL OF DEVELOPMENT POLICY SUITABLE FOR THE EU?

- **Sectoral-federal model**: EU-wide sectoral Funds for Innovation, Transport, Climate Change, Social Inclusion, Employment, etc., allocated by the Commission to individual projects.
  MEMOS: This is the development policy addressed to specific regions by the US federal government (with funds amounting to about 2.5% of GDP every year).

- **Place-based model**: a multi-sectoral Fund allocated to Member States and Regions through “contracts” whereby their grants to projects are made conditional on a set of EU-wide principles.

1. The **place-based model** is the modern way to tackle economic and social development, because
   - it allows to take into account people’s preferences and knowledge
   - it avoids the “on-size-fits-all” syndrome and it allows public goods and institutions to be tailored to places.

2. The **place-based model** is the only model compatible with the EU’s limited democratic legitimacy (see the recent arguments by Germany’s Constitutional Court).
   - Sectoral top-down interventions would not be coherent with the role of Member States in social and economic development.
   - Place-based interventions combine EU’s responsibility for setting tasks and guidelines (conditionality) and Member States’, Regions’ and local agents’ responsibility for implementing policy according to contexts (subsidiarity).
What is the mission of “cohesion policy”? **Acting as a leverage for development for the Union as a whole.**

The mission is not redistributing funds among Regions and Member States. An unconditional transfer can compensate for a different availability of public finances, but it does not address either the issues for which the Union is - and is held to be - responsible, or the capacity of Member States and Regions to address those issues.

Limiting EU interventions to “poor” Member States (renationalisation critique) wrongly assumes that cohesion policy is a mechanism for financial redistribution.

Limiting EU interventions to “poor” NUTS2 Regions arguing that they already have access to the resources to pay for their own development is also wrong:
- even “rich” NUTS2 Regions can include “poor” places which call for exogenous interventions
- “rich” places are challenged by EU-reinforced globalisation and might fail to adjust
- strong social exclusion can exist in “rich” places.
A DEFINITION OF “PLACE-BASED DEVELOPMENT POLICY” AND “PLACE”

- A place-based development policy is:
  - a long-term development strategy aiming at reducing underutilization of resources and social exclusion of specific places, through the production of integrated bundles of public goods and services (via material and immaterial infrastructures and incentives),
  - determined by extracting and aggregating people’s knowledge and preferences in these places and turning them into projects,
  - and exogenously promoted through a system of grants whose transfer is made conditional on the implementing authorities:
    - establishing measurable objectives in terms of people’s well-being,
    - accepting and tailoring to places some agreed requirements on the economic institutions.

MEMOS: What is place in a place-based development policy?

- A place is not identified by administrative boundaries,
- Nor by any other ex-ante “functional” criteria (coincidence of residence and activity, density of population, absence of land connections, existence of water or other natural linkages, altitude, proximity to natural areas, etc.),
- Rather a place is endogenous to the policy process, it is a contiguous area within whose boundaries a set of conditions conducive to development apply more than they do across boundaries.
POLICY RATIONALE: MARKET AND GOVERNMENT FAILURES

- Why can’t one leave places to react to internal and external challenges by their own means, possibly only redistributing financial resources to poorer areas? Why both inefficiency traps and social exclusion traps can arise which call for exogenous intervention?

- Three motivations:
  1. institutions (both formal and informal) and circumstances have a strong inertia: the elites of places might lack the capacity to innovate;
  2. appropriate formal institutions can fail to be chosen by local elites due to their distributive effects;
  3. given the existence of strong returns from agglomerations (not always positive), and the indispensable role of public action in any agglomeration pattern, failures of public action can occur due to limited knowledge: an explicit and verifiable space-aware intervention is preferable to self-proclaimed space-blind policies, which prevent public scrutiny on allocation choices.

- Therefore, a place-based development policy is not a policy promoting people’s immobility – acting against “market forces” -; rather, it is a policy aimed at increasing the freedom to reasonably decide whether to move or to stay.
“Social inclusion” is here defined as: the extent to which, with reference to a set of multidimensional outcomes (health, education, housing, security, labour conditions, income, self-respect, etc.), all persons (and groups) enjoy socially acceptable standards, and disparities among them are socially acceptable, the process through which those results are achieved being participatory and fair.

The primary “ingredients” of the definition of social inclusion are:

- multidimensional aspects of people’s well-being;
  MEMOS: “income” is only one (although relevant) dimension, since it cannot be fully converted in all the other dimensions; and so is “employment”;

- both a threshold (achieving a socially acceptable standard) and an interpersonal (achieving socially acceptable disparities) concept of inclusion;

- the process through which inclusion is achieved, with reference also to the degree of democratic participation in public decision-making (i.e. the freedom of citizens and collective bodies to experiment with solutions while exercising mutual monitoring);

- an attempt to distinguish between those features effecting a person’s well-being that depend on his/her effort, and those that depend on factors beyond his/her will (circumstances).
It is often argued that equity (or social inclusion) should not be a separate policy objective since a natural correlation exists between equity and efficiency. Actually no such natural correlation exists.

**Synergies** between the equity and the efficiency objective are at work:
- social exclusion traps and inefficiency traps often share the weakness of formal and informal institutions as their common cause;
- a social exclusion trap, by causing social and political instability or preventing innovation, can negatively affect efficiency: tackling the former can help addressing the latter (market-compensating view of social policy).

**Trade-offs** can also arise between the equity and the efficiency objective:
- greater social inclusion changes the balance of negotiating power among parties (for example in favour of workers and against entrepreneurs) and it then rises the incentive, and the effort, of some, while reducing the incentive, and the effort, of others: the balance can be negative;
- policies for increasing social inclusion can reduce the incentive to make efforts.

In the short-medium term, the balance of synergies and trade-offs is an empirical matter. No ex-ante general assumption can be made on this balance ⇒ Therefore equity and efficiency objectives must be kept distinct.
Furthermore, specific interventions need to be assigned to each of the two objectives, because:

- it is often the case that the most satisfactory intervention from the point of view of tackling social inclusion is not the most satisfactory intervention from the point of view of tackling efficiency (even if both interventions have a positive impact on both objectives);

- focusing an intervention on either social inclusion or efficiency increases the verifiability of results and the forcefulness of public debate and democratic participation.

MEMOS: the opposite has taken place in recent years when the ideological concern not to stress social objectives has often resulted in social inclusion policies to be “smuggled” as competitiveness policies, with bad result for both equity and efficiency.

In summary:

- a place-based development policy must surely aim at both efficiency and social inclusion,

- but the interventions (mostly) aimed at efficiency should be kept distinct from the interventions (mostly) aimed at social inclusion,

- while an effort must be made to exploit all complementarities.
The state of the empirical evidence on the impact of cohesion policy is very unsatisfactory

- Cohesion policy enjoys high accountability in terms of financial and physical output, but not in terms of outcome:
  - Econometric studies do not offer and cannot offer conclusive general answers on policy impact,
  - There is no systematic impact evaluation of interventions,
  - The system of outcome indicators and targets is of very poor quality,
  - Methodological problems exist in the “metric of results”.

2. Lessons from cohesion policy performance
HOWEVER, THE AVAILABLE EVIDENCE LEADS TO TWO CONCLUSIONS

1. Cohesion policy provides the appropriate architecture for an EU place-based strategy, thanks to:
   - a system of multi-level governance, “contracts” and cooperation of high value,
   - a track record of achieving targets in specific contexts,
   - a contribution to institution-building in many regions,
   - an EU-wide network for cooperation and disseminating experience.

2. A comprehensive reform is needed, because:
   - the policy concept is very opaque, even inside the cohesion policy community,
   - no critical mass exists on priorities, and cohesion policy results are neither strongly perceived by citizens, nor at the centre of policy debate,
   - economic (efficiency) and social (equity) objectives are confused,
   - contracts between the Commission and Member States/Regions fail to focus on results and to create adequate incentives for the latters to use resources effectively,
   - the present strong pressure on timely spending has a negative feedback on regular and effective spending.
OUTLINE OF THE REFORM (1)

First. A “development turn” is needed, i.e. a “high political compromise” whereby cohesion policy is interpreted:
- as a policy for development,
- aimed at “people in places” (the territorial dimension)
- combining but not confusing
  ➔ the economic dimension (efficiency objective)
  ➔ the social dimension (social inclusion objective)

The social dimension: a particularly strong political return for Europe

→ The division of labour between the EU taking care of markets and MS taking care of social issues is becoming untenable, and neither the Open Method of Coordination, nor EU judiciary interventions are enough to address it.

→ President Barroso in his Agenda for the new Presidency argued that EU citizens should “make use of their rights as EU citizens in the same way as they use their rights as national citizens”.

→ The Commission’s consultation paper “EU 2020”, referring the both MS and EU actions, argues that “new policies must demonstrably contribute to social cohesion, tackling unemployment and fostering social inclusion”.

→ But how to achieve that, given the limited effectiveness of the Open Method of Coordination? Any attempt to Europeanise social policies is constrained by the diversity of national normative aspirations and by EU budgetary limits.

→ A territorialised social agenda pursued through cohesion policy in 1 or 2 priority areas can help addressing the promise of a “people’s Europe” while respecting national social contracts.
Second. Radical changes of the governance, both comprehensive and pragmatic, are needed to make the policy results-oriented and effective.

**Outline of the Reform (2)**

- **Concentration on 3-4 core priorities**
- **Results-oriented contracts**
- **Experimentalism and a new metric**
- **Improving public scrutiny through new political checks and balances**
- **Strengthening the competence of the Commission**
- **A revised negotiation system**
1. CONCENTRATION OF RESOURCES ON 3-4 CORE PRIORITIES

- Concentration of up to 2/3 of funding on 3-4 “core priorities”, selected through a high-level European strategic debate (with a relevant role of the European Parliament), on the base of three criteria:
  - relevance vis a vis the expectations of European citizens
  - place-based nature (strongly requiring local knowledge and preferences)
  - verifiability of results

- The Report puts forward six examples, that are very much in line with the three broad priorities of the “EU 2020” paper:
  - 2 options with a predominantly “economic” objective: Innovation and/or Adaptation to climate change
  - 2 options with a predominantly “social inclusion” objective: Migration and/or Children
  - and 2 options aimed at both objectives: Skills and Ageing.

While

- No substantial change (except for a 75% + X status) would be introduced in the criteria for distribution of funds between lagging and non-lagging Regions and Member States and to territorial cooperation. (A pragmatical decision given the lack of feasible alternatives)
A PLACE-BASED STRATEGY CALLS FOR A FINE BALANCE BETWEEN SUBSIDIARITY AND CONDITIONALITY

- On the one hand, a place-based strategy requires effective **subsidiarity**:  
  - policy and institutions must be tailored to contexts, by entrusting project design and implementation to the level of government which is as close as possible to the “place”

- On the other hand, a place-based strategy requires effective **conditionality**: 
  - the exogenous intervention needs enough leverage to break local institutional traps and to promote innovators, by establishing institutional principles for the implementation and ensuring that measurable objectives are set

⇒ **If subsidiarity is over-played**, a place-based policy is more likely to be captured by local rent-seekers ⇒ the very rationale of an exogenous intervention gets lost

⇒ **If conditionality is over-played**, the mobilization of local knowledge and preferences is weakened and paternalism prevails ⇒ exogenous interventions become ineffective (or even counter-productive)
THE RIGHT BALANCE BETWEEN SUBSIDIARITY AND CONDITIONALITY CAN BE ACHIEVED THROUGH A GOVERNANCE BASED ON THREE INTERCONNECTED PILLARS

1. A system of **flexible and effective contracts** between the institutions running the exogenous intervention and the “places”

2. **Experimentalism and openness**, to create incentives for actors at place level to experiment with solutions and exercise mutual monitoring

3. A **metric tailored to contexts**
2. RESULTS-ORIENTED CONTRACTS

- A National Strategic Development Contract (Contract) and Operational Programmes (presented simultaneously) commit each Member State and Regions to:
  - objectives and targets, expressed in terms of outcome indicators
  - institutional requisites, expressed in terms of broad but binding principles

- Furthermore:
  - financial additionality is simplified and linked to the Stability and Growth Pact
  - the de-commitment rule is applied at the level of whole countries, as a way to reduce the pressure on timely spending which today reduces quality of spending and increasing irregularities (both directly and via Commission’s lower incentives to suspend programs)

- The Commission can:
  - adopt the whole Contract
  - adopt some parts of the Contract “subject to condition”
  - reject some parts of the Contract

- When the contract is “subject to conditions” an Implementation Report will be later prepared by MS and, possibly, an Implementation Assessment by the Commission, as requisites for allowing transfers. This system strengthens orientation to results and differentiation among Member States

- Annual Member States’ Report on Results (after 3rd year) and Commission’s opinions and Summary Report open public debate in the European Parliament and the Council
3. EXPERIMENTALISM AND A NEW METRIC

- **Experimentalism at place level should be promoted**, i.e. stronger incentives must be created for actors at place level to reveal and exchange knowledge and to experiment with solutions while exercising mutual monitoring and being exposed to external knowledge. This result can be achieved by:
  - committing Member States and Regions to place-based (territorial) strategies
  - putting at Commission’s disposal a small share (0,1%) of all funds for *Innovative territorial actions*
  - promoting the learning process (see below)

- A new policy metric must be developed in two distinct directions:
  1. **promoting policy-makers’ focus on final policy outcomes in terms of people’s (multi-dimensional) well-being** by:
     - at the start establishing a small set of EU-wide comparable indicators (following Open Method of Coordination practice),
     - making MS and Regions to commit to the adoption of a system of indicators and targets which satisfy ordinary statistical requisites,
     - promoting community-based indicators,
     - establishing that progress towards targets will be reported and motivated;
  2. **promoting the use of “prospective counterfactual impact evaluation”** – where impact is estimated by comparing outcomes for beneficiaries of the intervention with outcomes for a *similar* population of non-beneficiaries - designed while interventions are being designed. This fundamental move can have strong disciplinary effects both in identifying objectives and in transparently selecting beneficiaries.
4. STRENGTHENING THE COMMISSION: COMPETENCE AND ORGANISATION

- **Refocusing and strengthening the role of the Commission as a centre of competence.** A more ambitious, discretionional and demanding role for the Commission calls for its Directorates in charge of cohesion policy:
  - to rebalance the internal structure towards strategic functions, by:
    - establishing core-priority task forces
    - upgrading the evaluation department
    - creating a research department
    - strengthening the links of the geographic units with those horizontal structures
  - to make a significant investment in human resources, by recruiting for those strategic functions the best junior and senior expertise that is today available in Europe
  - to achieve inter-Directorates coordination (between themselves and with sectoral Directorates) under the guidance of the Secretary general

- **Addressing financial management and control**
  - keeping the accountability of “regular policy implementation” separate from measuring progress towards outcome
  - reducing the control and audit burden for the Commission, either through the proposals being currently debated or through an appropriate implementation of the new Treaty with a transfer of responsibilities to Member States
5. PUBLIC SCRUTINY THROUGH NEW POLITICAL CHECKS AND BALANCES

- Improved information on results and greater Commission discretion make stronger public scrutiny by the two other European Institutions feasible and necessary.

- A new formal Council for Cohesion Policy would:
  - assess Contracts and Reports on Results
  - assess special decisions by the Commission:
    - approval of contracts subject to conditions
    - decision to run an Implementation Assessment and its effects
    - financial sanctions for unmotivated failure to achieve financial additionality
    - financial sanctions for unmotivated failure to achieve targets
  - issue recommendations

- The European Parliament would:
  - fully use its budgetary power as a way to demand ex-ante a clear voice in choosing among different solutions and policies
  - contribute opinions on Contracts and Reports
  - receive and debate the Commission’s Summary Report (as part of the “Evaluation Report” of the amended art. 275 of the Treaty)
A REVISED NEGOTIATION CALENDAR AND A SIMULTANEOUS AGREEMENT ON RESOURCES, GOVERNANCE AND GOALS

- **2010**: a high level political compromise on the future of cohesion policy

- **Autumn 2010-Spring 2012**: strategic dialogue between Member State and European institutions facilitated by a Policy Group and leading to a draft of a *European Strategic Development Framework*

- **Spring 2012-Spring 2013**: final negotiation on resources, governance and goals

- **Spring 2013**: simultaneous agreement on resources (Financial framework), governance (Regulation) and goals (European Strategic Development Framework)