

Global Europe: vision for a 21st century budget

June 2008



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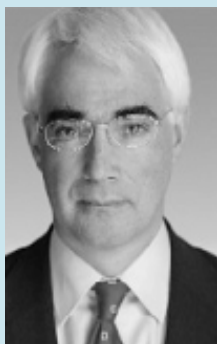
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CONTENTS

	Page
Foreword by the Chancellor of the Exchequer	3
Executive Summary	5
Chapter 1 Introduction	7
Chapter 2 The context: new challenges and opportunities	9
Chapter 3 Budgetary principles	11
Chapter 4 A 21st century budget for a global Europe	13
Chapter 5 Conclusion	19

FOREWORD BY THE CHANCELLOR OF THE EXCHEQUER



The challenge for the European Union is to decide what its priorities will be in a rapidly globalising world.

Last year, the UK Government set out its view on these priorities, in *Global Europe: Meeting the Economic and Security Challenges*. The EU must focus on the issues that matter to our citizens – jobs, the environment and security. And a key part of this should be reforming the EU budget to better equip the EU to meet the challenges of the 21st century.

I strongly welcome the European Commission's launch of the fundamental review of the EU budget. It is the opportunity to consider how the EU uses its budgetary resources and how we can achieve outcomes from the money available which genuinely benefit the Union and its citizens. Collectively, the EU must set a new direction for the budget.

This *Vision for a 21st Century Budget* is a contribution to the budget review debate. It describes the UK Government's priorities for a future EU budget, consistent with our budgetary principles. We are calling for a re-orientation of the budget towards three areas: building a prosperous Europe within a strong global economy, addressing the challenges of climate change and ensuring security, stability and poverty reduction. This re-orientation must be in the context of a shift away from agricultural support. And Structural and Cohesion Funds must be better focused on the less prosperous Member States.

The EU needs a radically reformed budget. The budget review must be a genuinely fundamental, strategic and ambitious exercise to achieve proper and effective reform. The UK looks forward to taking an active part in the debate.

A handwritten signature in black ink that reads "Alistair Darling". The signature is written in a cursive, flowing style.

**THE RT HON ALISTAIR DARLING MP,
CHANCELLOR OF THE EXCHEQUER**

EXECUTIVE SUMMARY

In the UK's view, the European Union (EU) budget needs fundamental reform to address the key challenges that matter to citizens in the 21st century. Resources should be re-oriented towards EU action in three priority areas; spending on agricultural support should be reduced.

1. Building a prosperous Europe within a strong global economy

- Supporting EU Member States' efforts to make the transition to high value added economies, with resources focused on those with the greatest transition to make, thereby helping to create jobs and prosperity.
- Making future enlargements a success by helping candidate countries to prepare for accession and further supporting their economic transition following accession.
- Complementing Member States' efforts to strengthen knowledge, research and innovation, to ensure the EU has the skills and expertise to compete in a low carbon, global economy.
- Building the capacity of developing countries to respond to new market opportunities.

2. Addressing the challenges of climate change

- Supporting well-targeted research, development, demonstration and deployment of low carbon technologies, adding value to national programmes to help enable the EU to lead in the technologies of the future, maximising the opportunities for jobs and growth and avoiding the worst impacts of climate change in a cost-effective way.
- Supporting EU Member States in honouring their commitments on climate change.
- Supporting investment in research and monitoring, to help EU Member States to adapt to the unavoidable impacts of climate change.
- Helping developing countries to reduce their greenhouse gas emissions and assisting the most vulnerable communities to adapt to the unavoidable impacts of climate change.

3. Ensuring security, stability and poverty reduction

- Supporting the building of strong, effective relations with all neighbouring countries and promoting reform, stability and growth in those countries.
- Enabling the EU to develop greater capability to deliver civilian assistance to conflict zones at every stage, ranging from the threat of instability, to potential conflict itself, through to post-conflict stabilisation, recovery and reconstruction.

- Helping to ensure that EU borders are safe and effective and that migration flows are managed efficiently and fairly both within the EU and beyond.
- Supporting joint working to confront terrorism and cross-border crime.
- Facilitating ever-greater dialogue and cooperation between Member States on common challenges.
- Showing global leadership in efforts to reduce poverty across the world, in particular in low-income countries, and with a renewed focus on realising the Millennium Development Goals, tackling climate change and protecting natural resources.

Spending on Pillar 1 of the Common Agricultural Policy (CAP) should be phased out. And against the backdrop of climate change, payments under a reshaped Pillar 2 of the CAP should be focused on delivering environmental benefits to society that would not otherwise be secured from the market.

Structural and Cohesion Funds will continue to be an important mechanism for targeted redistribution towards less prosperous Member States. Consequently Structural Funds in the richer Member States should be phased out. Given that aim, the priority should be that standard 'competitiveness and employment' funding is no longer available to richer Member States.

Consistent with the budgetary principles, EU policies in the fields of transport, natural resource protection, civil justice and citizenship should continue to receive targeted EU budget support.

Improvements to the design and administration of spending programmes should be considered to ensure that outcomes are achieved effectively and efficiently. The highest standards of financial control and independent audit are necessary, alongside continuing budget discipline.



INTRODUCTION

1.1 This document sets out a vision for a reshaped European Union (EU) budget that would better equip the EU to meet the challenges of the 21st century. It is a contribution to the budget review debate launched by the European Commission in September 2007 with its publication *Reforming the Budget, Changing Europe*¹.

1.2 Over the last 50 years the EU has played a vital role in delivering prosperity and security to our continent. In that time the EU has evolved considerably to become a larger and more integral part of the global economy. Global change has led to the emergence of challenges and opportunities that require new responses.

1.3 The EU must focus on the issues that matter to our citizens: prosperity and jobs, security and crime, tackling climate change, creating a sustainable environment and helping ensure stability. A commitment to free trade and openness is needed to deliver continued growth and employment and to ensure food security in the EU and beyond. Liberalisation of key network industries must continue, including of EU gas and electricity markets.

1.4 The full range of tools available to the EU must be focused on achieving the best long-term outcomes for its citizens and allowing the EU to demonstrate global leadership. The EU budget is one of the tools that the EU has at its disposal, alongside coordination, sharing best practice, well-targeted legislation, proactive use of competition policy and instruments such as emissions trading.

1.5 Just as the EU has evolved, so its budget needs to evolve to reflect changing priorities. It needs fundamental re-orientation so that it delivers outcomes with genuine EU benefit, consistent with 21st century priorities. Budget spending must be delivered in a way that gives EU citizens the confidence that funds are well managed.

1.6 The commitment by the European Commission and Member States to a fundamental review of the budget in 2008-09 is an important first step on the path to reform. This review is an important opportunity for European leaders to commit to modernisation of the EU budget, so that the EU is better able to deliver for the benefit of its citizens.

¹ *Reforming the Budget, Changing Europe*, European Commission, 2007.

2.1 It is striking how much the context for the budget has changed over recent decades. Europe in the 21st century looks very different to Europe in the 1950s.

2.2 In the decades immediately after 1945, Europe's focus was internal. The emphasis was on how best to deploy the primary resources of coal, steel and agricultural products and how to strengthen internal integration. In 1952, the European Coal and Steel Community (ECSC) was established, creating a free trade area and a common market in basic materials required for industrial production. The six-country ECSC focused on increasing trade within its borders, underpinned by tariffs and subsidies. A European budget was agreed in 1958 to support the establishment of the common market, reflecting this focus on internal economic integration. Early budgets were largely composed of Common Agricultural Policy (CAP) expenditure. Regional development aid was added later, the aim of which was to help the poorest regions catch up economically.

2.3 Today, the context for the European Union (EU) budget looks very different. The EU is a much larger group of countries, with 27 Member States and further accessions likely. Whilst the economies of EU Member States are at different stages of development, the EU as a whole is a high value-added economy, with services accounting for a much larger share of output and employment than goods. In 2006, services in the EU-27 economies accounted for 74 per cent of total gross value added; agriculture and manufacturing 2 per cent and 17 per cent respectively. This compares to the EU-15 in 1970 where services accounted for 53 per cent of total gross value added, agriculture 5 per cent and manufacturing 22 per cent.

2.4 Globalisation is increasingly shaping our lives, bringing with it new challenges and opportunities for citizens and businesses. The balance of global economic activity is shifting with the rise of rapidly growing emerging economies such as China and India; flows of goods and capital are becoming increasingly global. Growth in trade between the EU and other parts of the world is increasing, supporting European and global prosperity by driving up productivity and real income growth.

2.5 The aim should be to shape globalisation in the interests of all EU citizens, working together as a Union and engaging international partners. Today's global challenges will require new approaches by all nations and by those international and regional organisations which frame the way nations work together.

2.6 There needs to be a renewed commitment to high levels of sustainable, low carbon growth and employment through a new, more flexible approach to Single Market policies that focuses on promoting competition, reducing the burden of regulation, and encouraging innovation. This must be accompanied by modern social policies that combine labour market flexibility with fairness in line with Europe's social values and economic goals.

2.7 A commitment to free trade and openness is needed to deliver continued growth and employment in the EU and beyond. It is also crucial for food security. Europe produces most of the food it consumes, but like other parts of the world it is sometimes affected by animal disease outbreaks, drought and floods. Looking ahead, climate change is very likely to increase the volatility of agricultural production, both in the EU and internationally. The way for the EU and others to safeguard access to food, including in times of shortage, is to maintain access to well-functioning

efficient and integrated world markets. This is best encouraged by reducing barriers to international trade.

2.8 On climate change, the EU is at the forefront of the global effort to reduce greenhouse gas emissions, avoid the worst impacts of climate change and adapt to those which are now inevitable. In 2007, EU leaders made a commitment to ambitious emissions reductions, increased energy efficiency and an increased use of renewable and low carbon energy technologies. The successful transition to low carbon is an imperative for the prosperity and security of all Europeans. EU Member States now need to agree how to achieve these targets through the 2020 Climate Change and Energy package and put their economies on the fast-track to low carbon growth. The EU also has a crucial leadership role in securing a comprehensive international post-2012 agreement that will bring about global emissions reductions, while supporting sustainable development and poverty reduction. Actions to reduce energy demand and increase low carbon generation capacity must be complemented by measures to improve the functioning of energy markets within the EU and internationally so that the correct incentives are in place to encourage a more diverse range of producers and suppliers; to encourage innovation and investment in infrastructure; and to enhance the operation of market mechanisms for tackling climate change. The EU's policies also have a key role in delivering a collective commitment to protecting and enhancing our natural environment, including through the efficient and sustainable use of natural resources.

2.9 The EU also has an important role in promoting security and stability in neighbouring countries and beyond. EU enlargement, capacity-building, peace-keeping and peace-building, and support for an effective multilateral system can all help to further this aim. Tackling global poverty will require renewed efforts to deliver the Millennium Development Goals.

2.10 The increasingly global nature of terrorism and organised crime means that EU Member States need to work collaboratively, for instance to improve the exchange of information within the EU and to strengthen the capacity of countries outside the EU to fight crime. And migration must be managed well so that it benefits both the EU and third countries.

2.11 Overall, Europe looks very different now to how it looked in the decades immediately after 1945. The EU budget must reflect this changing context to help equip the EU to thrive in an era of globalisation. In today's budget, there is significant spending on agricultural subsidies that lack a credible policy rationale and on regional aid to parts of the EU that are no longer poor. Far-reaching reforms will be required to reorient the budget so that it is fit for the 21st century.

3.1 The European Union (EU) budget has an important role in supporting a number of collective EU priorities, but it is essential that resources are used more effectively. Public spending – whether at local, national or EU-level – must be targeted and delivered to achieve maximum benefits, giving citizens the confidence that money is being well spent. Choices must be made about how to focus resources and the UK agrees with the European Commission on the need for a principled approach that can help to ensure that choices are made with rigour and consistency.

3.2 The three principles below provide a framework for designing a future EU budget.

- First, the EU should only act where there are clear additional benefits from collective efforts or ‘**EU added value**’, compared with action by Member States, either individually or in co-operation.
- Second, where EU-level action is appropriate, it should be **proportionate and flexible**. We must recognise the limits to EU budgetary intervention. Expenditure is just one of a number of policy levers, alongside coordination, sharing best practice, and legislation or regulation. In addition, the full range of financing options should be considered, including both grant and loan finance.
- Third, there must be **sound financial management** at all times, including the highest standards of financial control and independent audit, and greater focus on delivery of outcomes in programme design and evaluation. It will be important to maintain budget discipline.

3.3 To ensure that benefits from spending are maximised, EU budget funding should only be provided where all three principles are met. Any existing spending that fails the first or second principle should be discontinued; where the third principle is not fully met, reform will be necessary.

4.1 According to the budgetary principles set out above, the European Union (EU) budget needs fundamental reform to address the key challenges that matter to citizens in the 21st century. Resources should be re-oriented towards EU action in three priority areas; spending on agricultural support should be reduced.

- Building a prosperous Europe within a strong global economy.
- Addressing the challenges of climate change.
- Ensuring security, stability and poverty reduction.

4.2 Spending on Pillar 1 of the Common Agricultural Policy (CAP) should be phased out. And, against the backdrop of climate change, payments under a reshaped Pillar 2 of the CAP should be focused on delivering environmental benefits to society that would not otherwise be secured from the market.

4.3 Structural and Cohesion Funds will continue to be an important mechanism for targeted redistribution towards less prosperous Member States. Consequently, Structural Funds in the richer Member States should be phased out. Given that aim, the priority should be that standard ‘competitiveness and employment’ funding is no longer available to richer Member States.

4.4 Consistent with the budgetary principles, EU policies in the fields of transport, natural resource protection, civil justice and citizenship should continue to receive targeted EU budget support.

4.5 Improvements to the design and administration of spending programmes should be considered to ensure that outcomes are achieved effectively and efficiently. The highest standards of financial control and independent audit are necessary, alongside continuing budget discipline.

BUILDING A PROSPEROUS EUROPE WITHIN A STRONG GLOBAL ECONOMY

4.6 Europe must ensure that globalisation works for its citizens - by delivering sustained and sustainable prosperity, in an inclusive and cohesive way, so that prosperity is shared by all. An important part of this is boosting growth and providing more and better jobs. To achieve that, Member States must continue internal reforms to promote investment in skills, research and innovation, and improve the flexibility of their economies so that they can respond to globalisation, based on a commitment to the Lisbon Strategy.

4.7 In addition, Community-wide aspects of the Lisbon Strategy form an important pillar of the approach to reach the Lisbon goals. A new approach to the Single Market is needed, that prioritises action to where the economic benefits are greatest, for instance through liberalisation of network industries. Prompt, effective action to address climate change will help the EU and the wider world avoid the worst impacts and excessive costs. It will create business opportunities as new markets are created and we move to a low carbon economy. Overall, it will be important to ensure that citizens benefit from globalisation.

Role for the EU budget

- Supporting Member States' efforts to make the transition to high value added economies, with resources focused on those with the greatest transition to make, thereby helping to create jobs and prosperity.
- Making future enlargements a success by helping candidate countries to prepare for accession and further supporting their economic transition following accession.
- Complementing Member States' efforts to strengthen knowledge, research and innovation, to ensure the EU has the skills and expertise to compete in a low carbon, global economy.
- Building the capacity of developing countries to respond to new market opportunities.

ADDRESSING THE CHALLENGES OF CLIMATE CHANGE

4.8 The EU has a crucial leadership role to play in confronting the challenge of climate change and moving to a low carbon economy, in protecting natural resources and preventing environmental degradation. Climate change is an international challenge that requires countries to work together. The EU has made commitments to cut its emissions of greenhouse gases, increase the proportion of energy from renewable sources and encourage the introduction of low carbon technologies such as carbon capture and storage. It has established an emissions trading scheme and is working internationally to secure a global agreement for emissions reductions to help developing countries respond to climate change.

4.9 The 2007 Spring Council committed to a fundamental re-structuring of the European economy towards low carbon. This will require a significant and rapid transformation of energy systems to achieve the goal of avoiding dangerous climate change. It will be necessary to make full use of national and EU instruments to deliver the shift; and to ensure that the regulatory and business environment gives the private sector the confidence to invest in the development and deployment of low carbon technologies. Liberalisation of the EU's gas and electricity markets will help create the conditions for private sector investment in infrastructure across the EU, facilitating the incorporation of new energy sources; this move will be further helped by the EU's commitment to 20 per cent of its final energy consumption coming from renewable sources by 2020. EU-level financing also has a role: through the European Investment Bank in helping to encourage private sector financing of low carbon infrastructure projects; and through the EU budget, principally in supporting the accelerated development and deployment of key low carbon technologies. The possibility of the EU budget supporting investment in low carbon infrastructure should be explored as part of the budget review.

Role for the EU budget

- Supporting well-targeted research, development, demonstration and deployment of low carbon technologies, adding value to national programmes to help enable the EU to lead in the technologies of the future, maximising the opportunities for jobs and growth and avoiding the worst impacts of climate change in a cost effective way.
- Supporting Member States in honouring their commitments on climate change.
- Supporting investment in research and monitoring, to help Member States to adapt to the unavoidable impacts of climate change.
- Helping developing countries to reduce their greenhouse gas emissions and assisting the most vulnerable communities to adapt to the unavoidable impacts of climate change.

ENSURING SECURITY, STABILITY AND POVERTY REDUCTION

4.10 The EU has an important role in promoting security and stability in neighbouring countries and beyond. Collaborative action is needed to tackle today's globalised threats to security: international crime and terrorism, illegal migration and human trafficking, and the impacts of climate change. The EU is working with countries around its borders, with other strategic partners and with countries in crisis to respond to these threats, to make the EU and beyond a safer place to be. A further key priority for the EU is to embed democracy and economic development in neighbouring countries, both prospective EU members and others.

4.11 The EU has a leading role to play in the fight against global poverty, and the promotion of growth and development internationally. EU development policy must be better focused on the immense task of eradicating global poverty, including by meeting the commitments under the Millennium Development Goals and promoting environmental sustainability. To achieve this, fundamental reform of the European Commission's overall management of aid is needed. The better-focused European Development Fund should remain outside the budget until then.

Role for the EU budget

- Supporting the building of strong, effective relations with all neighbouring countries and promoting reform, stability and growth in those countries.
- Enabling the EU to develop greater capability to deliver civilian assistance to conflict zones at every stage, ranging from the threat of instability, to potential conflict itself, through to post-conflict stabilisation, recovery and reconstruction.
- Helping to ensure that EU borders are safe and effective and that migration flows are managed efficiently and fairly both within the EU and beyond.
- Supporting joint working to confront terrorism and cross-border crime.
- Facilitating ever-greater dialogue and cooperation between Member States on common challenges.
- Showing global leadership in efforts to reduce poverty across the world, in particular in low-income countries, and with a renewed focus on realising the Millennium Development Goals, tackling climate change and protecting natural resources.

FAIR AND TARGETED SPENDING

4.12 Reorientation of the budget towards new challenges also requires a principles-based assessment of how funds are targeted. Redistribution to less prosperous Member States has been and should continue to be a function of the EU budget. Income disparities between Member States have widened since recent accessions and the recent entrants to the EU are still in the process of developing their economies as part of the convergence process. Future environmental policies and the new climate change targets will also place costs on the continued development of all Member States in the short term. The EU must view Structural and Cohesion Funds as its primary tool for targeted redistribution; any move to widen the mechanisms of redistribution beyond the EU budget could call into question their rationale.

4.13 For the UK, European budgetary solidarity is about helping those Member States that have the greatest economic transition to make and the least financial capacity to make it. According to the UK's budgetary principles, Structural and Cohesion Funds should be targeted towards the less prosperous Member States to help them invest in measures to increase their productivity and adjust to the economic challenges of globalisation, from furthering research and development capacity, to investing in skills development, to building basic institutions and infrastructure which are essential to their future growth. These investments can provide EU added value by contributing to the economic prosperity of the EU as a whole. The primary aim of Cohesion Policy should remain addressing disparities in economic development.

4.14 The EU budget is not the only, or indeed primary, tool for promoting sustainable economic growth in less prosperous Member States. Member States themselves have a crucial role to play, based on a commitment to the Lisbon Strategy, in achieving a stable macroeconomic environment, improving the underlying conditions for entrepreneurship, embedding better regulation and reforming labour markets so that employability is developed and enhanced, rather than specific jobs being protected. Community-wide aspects of the Lisbon Strategy and a renewed approach to the Single Market also help Member States to achieve sustainable growth. But the EU budget can and does have an important supplementary role to play in helping less prosperous Member States make the most of the opportunities available to them. The funding should be seen as transitional aid which helps Member States to make investments that will put them in a position to fund future investments themselves; it is not permanent subsidy. In the longer term, as Member States develop, a measure of their success will be that they no longer need these funds. Phasing out CAP Pillar 1 would also help less prosperous Member States grow their economies in line with the Lisbon Strategy, by helping economies adjust towards new, more productive, sectors.

4.15 Much of the redistribution in today's EU budget does not conform to the UK's budgetary principles. Whilst there is some distribution from richer to less prosperous Member States, there is still significant redistribution of funds between prosperous countries of similar wealth, and even within regions; some Structural Funds cycle from a region, via national governments to the EU budget, and back to the region incurring higher transaction costs. Where Member States have the institutional structures and financial strength to develop and pursue their own regional policies, they should be enabled to do so within a common EU strategic framework. Consequently, Structural Funds in the richer Member States should be phased out. Given that aim, the priority should be that standard 'competitiveness and employment' funding is no longer available to richer Member States.

4.16 Of course the EU budget is only one element of EU-level finance. Other important elements are the loans and procurement expertise provided by the European Investment Bank. In some instances, loans or blended grant/loan instruments may achieve more efficient outcomes than grants. The European Commission and European Investment Bank should work together to ensure coherence, avoid duplication and to consider where increased use of innovative financing would be appropriate.

4.17 More generally, across the rest of the EU budget, consideration should be given to how programmes can be targeted towards excellence so that the money is allocated to where it can be most effective and so that EU benefits are maximised for the amount of funding available.

IMPROVING DELIVERY

4.18 In order for the EU budget to deliver outcomes effectively and efficiently, the following five reforms should accompany re-prioritisation of expenditure:

- **Greater focus on outcomes.** All EU spending programmes need measurable - and where possible, single - objectives. Evaluations should focus on measuring outputs and outcomes from spending, with efforts made to identify the added value that accrued more widely to the EU not just to the funding recipient.
- **Consistency and complementarity** between policy areas so that EU spending programmes do not hinder the achievement of EU policy objectives, for instance in the areas of the environment, climate change or poverty reduction.
- **Changes to audit procedures** ensuring that external audit of EU budget spending focuses more on identifying the source of systemic weaknesses rather than errors in sample transactions; and that national audit institutions have an enhanced role in ensuring that Member States take adequate responsibility for funds that are managed jointly with the European Commission.
- **A more performance-orientated administration.** A wide-ranging and objective external review of all aspects of the administrative budget should be considered, building on the reforms initiated by the 2000 *Reforming the Commission*¹ White Paper. There should be annual efficiency gains in administrative expenditure.
- **More innovative financing.** Including joint working by the European Commission and European Investment Bank to ensure coherence and avoid duplication and to consider where loans or blended grant/loan instruments could generate better outcomes than pure grants.

¹ *Reforming the Commission*, European Commission, 2000

5.1 In summary, the UK Government believes that three principles should underpin the EU budget.

- First, the EU should only act where there are clear additional benefits from collective efforts or ‘**EU added value**’, compared with action by Member States, either individually or in co-operation.
- Second, where EU-level action is appropriate, it should be **proportionate and flexible**. We must recognise the limits to EU budgetary intervention. Expenditure is just one of a number of policy levers, alongside coordination, sharing best practice, and legislation or regulation. In addition, the full range of financing options should be considered, including both grant and loan finance.
- Third, there must be **sound financial management** at all times, including the highest standards of financial control and independent audit, and greater focus on delivery of outcomes in programme design and evaluation. It will be important to maintain budget discipline.

5.2 Consistent with these principles, the UK is calling for a re-orientation of the budget towards three areas.

- Building a prosperous Europe within a strong global economy.
- Addressing the challenges of climate change.
- Ensuring security, stability and poverty reduction.

This re-orientation must be in the context of a shift away from agricultural support. And Structural and Cohesion Funds must be better focused on the less prosperous Member States.

5.3 The EU budget review is an important opportunity to achieve a reformed budget better able to deliver for the benefit of all EU citizens. It must be a genuinely fundamental, strategic and ambitious exercise, conducted openly, creatively and from first principles, to achieve proper and effective reform.

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