#IKEMClimateFinanceWeek

Lessons learned from EU funds

International level

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The target audience of this brief is development finance institutions and global climate funds as well as multilateral and bilateral development agencies that provide international climate finance in developing and emerging countries. The brief draws on lessons learned from the programming and implementation of climate finance disbursed by the European Structural and Investment Funds in EU Member States from 2000–2020. Lessons learned from European countries provide insight into how a stable long-term climate policy framework can be formed and financed. These lessons suggest that the programming and implementation of international climate policy could benefit from the following: strengthening partnership aspects throughout the negotiation and implementation processes; aligning better climate programmes with national priorities other than the climate; orienting these programmes towards long-term development finance; promoting national ownership of programme implementation; and providing comprehensive technical assistance, not only to manage the disbursement of funds, but also to increase the supply of quality projects.[1]

The European Structural and Investment Funds (ESIF) are a part of the EU budget. These funds accounted for 43% of the EU budget from 2014–2020; the total EU budget scaled to approximately 1% of EU's gross national income in 2019. Each Member State contributes to the EU budget based on its gross national income. The EU budget is implemented through a range of EU funds and programmes that disburse finance to beneficiaries located in the EU Member States. The beneficiaries include regional and local authorities, small and medium-sized enterprises (SMEs), large enterprises, farmers, non-governmental organisations and academic and research institutions. These entities obtain finances disbursed by the ESIF through grants and other financial instruments. In some EU Member States, the cumulative support that beneficiaries receive from the EU budget exceeds the amount that the respective Member States contribute to the budget; other Member States are net contributors to the EU budget.

Lessons learned from European countries provide insight into how a stable long-term climate policy framework can be formed and financed. Many challenges that arise in Europe, especially in Central and Eastern European countries, are also relevant to emerging countries. The flow of ESIF financing from the EU budget to beneficiaries in the EU Member States bears certain resemblances to the structure of international climate finance that is provided by developed countries to developing economies via development finance institutions (DFIs) and global climate funds.

This brief analyses two ESIF: the European Regional Development Fund (ERDF) and the Cohesion Fund (CF). We studied the changes to and impacts of these funds in EU Member States from 2000–2020 and examined factors contributing to and limiting success, with examples provided from Lithuania and Slovakia. Viewed through the prism of international climate finance policy, these conclusions and lessons learned could be useful for donors and recipients. We narrowed our focus to the analysis of energy efficiency as a component of mitigation action.

It is important to note that not all lessons from the EU are easily transferrable or applicable to the international climate finance regime due to the differences between the legal nature of the ESIF and that of international climate policy. The ESIF is a solidarity mechanism among the EU Member States and a means to reach common EU objectives, defined as economic and social cohesion.[2] Global climate finance architecture is largely governed by the United Nations Framework Convention on Climate Change (UNFCCC), which obliged developed countries to provide new and additional financial resources for climate actions in developing countries.

LESSON 1: Strengthen partnership aspects throughout the negotiation and implementation process

The focus on partnership-building throughout the negotiation process was identified as a success factor in the formulation of programming objectives and priorities in a mutually acceptable way. In this context, negotiations between the European Commission and Member States on the programming of EU funds are perceived as occurring between equal parties, with both sides having an equal impact on the outcome. In contrast, the programming of international donor support for climate finance more closely resembles a stakeholder consultation than a negotiation.

> Negotiation between the European Commission and their countries as equal parties was identified by Latvian and Lithuanian interviewees as a success factor in the formulation of programming objectives and priorities that were acceptable to and politically feasible for both sides. Inevitably, however, consensus-building of this kind requires more time and effort than does the top-down approach, in which priorities are dominated by the donor. Even the language of the key documents reflects this difference: 'Partnership Agreements' are signed between the European Commission and the EU Member States, while the prevailing practice in international

climate finance is to enter into 'Grant Agreements' or 'Funding Agreements'. Whereas 'partnership' suggests collaboration towards common goals, 'grant' implies a more unequal, top-down relationship between parties. Although we cannot draw an exact parallel between EU and international climate finance, the EU's partnership-based approach does offer useful lessons for the architecture of global climate finance and the achievement of global climate goals.

LESSON 2: Involve stakeholders to ensure an alignment with national priorities and a maximisation of non-climate benefits, such as new jobs, poverty reduction and economic recovery

ESIF negotiation and programming involves extensive analytical and consultation processes, which were identified as another success factor. The most important level is negotiation among individual ministries and central government bodies. This is followed by several rounds of negotiations with the European Commission. Member State negotiators are required to include national stakeholders – including ministries, business representatives, social partners, and civil society representatives – in the consultation process. Such extensive preparatory processes with stakeholders at various levels support the design of a programme that responds best to national and local priorities and is well received by stakeholders. A maximum alignment of climate actions with national socio-economic and environmental priorities is critical to ensure buy-in, wider uptake, acceptance and demand from national stakeholders, which is especially important in times of economic crisis.

We found that the most successful measures were those which were aligned with national priorities. Lithuania's experience offers a powerful example in this respect: when a national renovation programme for energy efficiency in buildings was launched with ESIF support following the 2008 crisis, it generated significant positive co-benefits for the local economy in the form of jobs, support to small and medium enterprises (SMEs), and improved bank liquidity in addition to a substantial reduction in CO_2 emissions. Similarly, in Slovakia, some of the most successful interventions implemented with ESIF support were those with strong benefits for local communities; for example, a project to modernise technology at a steel factory led to a significant improvement in air quality in the city of Košice.

LESSON 3: Promote national ownership of programme implementation, including the involvement of national institutions, financial organisations and civil society in programme delivery to ensure sustainability and replication

The definition of programming and funding directions at country, regional- and/or country-wide theme - levels for the ESIF (as opposed to the project-based programming typical of multilateral donors) has also contributed to success. This approach, which leaves the detailed design of operational programmes and modalities of their implementation to Member States, has been identified as particularly instrumental. The ESIF are managed by EU Member States themselves based on Partnership Agreements: even though the European Commission is formally responsible for the implementation of the EU funds, the actual implementation is outsourced to Member States (the principle of 'shared management'). This principle enables countries to take full account of domestic circumstances, constraints and opportunities while remaining within the general direction and framework determined by the Partnership Agreement.

The principle of shared management entails various benefits. It fosters a broad participation of social organisations in promoting economic growth. Involvement at various policy levels also results in the design of well-suited programmes and projects. In addition, the principle promotes the use of new public management practices and positive spill overs to domestic policy, as Lithuanian representatives indicated during interviews.

LESSON 4: Design climate finance as long-term development finance to enable market transformation

The overall design of the ESIF as a 'development finance' instrument, as opposed to only a 'climate finance' instrument, has enabled countries to move beyond direct and immediate climate actions. On the one hand, such a broad design cannot always be directly translated into immediate emission reductions; on the other hand, it has enabled the implementation of broader social and economic reform processes, which are essential for achieving longer-term decarbonisation goals. As a result, the ESIF have been used across the board to mitigate negative socio-economic impacts of decarbonisation policies, making it possible for many difficult policy decisions to take an effect. In all countries where interviews were conducted, the ESIF's long-term budget planning horizon was said to be instrumental in removing numerous barriers, facilitating necessary reforms, making instruments more mature and bringing the private sector on board. It could send long-term signals to the market about funding availability, which would not be possible within the framework of annual national budgets.

> In Lithuania, the massive ESIF-financed investment programme for the energy-efficient modernisation of residential buildings has laid the groundwork and prepared tenants for a gradual removal of subsidies and a liberalisation of heat tariffs. This 'difficult' policy has in turn created a lasting incentive for consumer energy efficiency while simultaneously saving a substantial amount of public money on subsidies and improving the overall performance and competitiveness of the heat supply sector. To achieve the impact at scale, Lithuania worked for over 15 years to gradually improve the share of private finance in programme funds, which has risen from zero to over 50%. It was also necessary to prepare the local technology and labour markets to address demand. Similarly, in Czechia and the Slovak Republic, the ESIF have been used to support a painful, but essential transition process related to the economic transformation of coal.

LESSON 5:
Provide comprehensive technical assistance to support the supply of and demand for projects, and ensure that technical assistance and financial instruments are aligned within one funding framework

Technical assistance is extremely important for the self-empowerment of less developed countries. It enables these countries to continue projects without e support in the medium to long term, as many lack strong institutions and extensive experience in managing complex policies. Workable implementation arrangements and the provision of additional technical support throughout the project preparation and implementation process have been critical to success, i.e., timely disbursement of ESIF funds and the achievement of intended results. Experiences of Member States offer numerous examples of successful and not-so-successful practices that either contributed to or jeopardised implementation.

> Lithuania provides one example of an effective, well-coordinated and dedicated institutional system that offers technical assistance for renovation programmes in multi-apartment buildings with the involvement of local governments. A dedicated public agency, the Housing Energy Efficiency Agency (BETA), has been set up to administer and coordinate the provision of technical support to various stakeholders – including local governments, housing administrators and energy services companies – throughout the design and implementation of projects in multi-apartment buildings. This provides assistance not only on the supply side of projects, but also in the creation of demand for them.

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[1] For details, please see: Novikova, A., Olshanskaya, M., Dunkel, M. 2020. Lessons learned for international climate policy from the programming, implementation, and monitoring of the European Structural and Investment Funds in EU Member States. Berlin: Institute for Climate Protection, Energy and Mobility (IKEM).

[2] The EU cohesion policy is guided by the EU 2020 strategy for 2010-2020 and the Green Deal Agreement for 2020 - 2050. This policy, with its binding targets and indicators provide the framework for defining priorities and steering processes at national level. The EU climate policy setting or requesting its Member States to set national targets for energy efficiency, renewable energy, and greenhouse gas (GHG) emission reduction is an important part of the EU policy.

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