A Primer on Developing European Public Goods

A report to Ministers Bruno Le Maire and Olaf Scholz

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1. Introduction

The EU has mostly been defined as a provider of economic integration amongst participating member states. Its cornerstones have been the removal of obstacles to cross-border flows of goods, services, labour and capital, and the development of common policies that ensure the smooth functioning of an integrated market, be it for trade, competition, infrastructures or consumer protection, to name the main ones only.[2] Even the euro was initially conceived as a natural complement to the internal market and as a trigger for further integration.

Historically, however, the EU was not created as an endeavour limited to economic integration. Early priorities – defence, until the rejection of the European Defence Community in 1954, food self-sufficiency, which was a major objective of the Common agricultural policy (CAP), and energy autonomy, with the Euratom treaty of 1957, focused more

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[2] This is sometimes referred to as 'negative' integration, as opposed to 'positive' integration meaning the joint provision of public goods and services.

on integration through the provision of European public goods. The same aim underpins some of the current policies of the EU such as research, the protection of the environment or common foreign and security policy initiatives.

The European Treaties do mandate the EU to go beyond fostering economic integration and play a role in the provision of certain public goods. Security, public health, safety and environmental protection belong to the competences the EU shares with the member states (Art 4 TFEU). But in practice the provision of public goods in Europe is primarily a task of the national governments or subnational entities. This division of labour is reflected in the distribution of public spending across government levels: excluding social transfers, public expenditures in the EU-27 amount to 16% of GDP. This is approximately 16 times more than the EU budget. In addition, a large part of that budget is spent on programmes that have a strong distributional dimension, such as the structural funds and the CAP. Very little money goes to financing pan-European public goods.

Time has come to reconsider the allocation of political impetus between the deepening of economic integration and the provision of European public goods. The former certainly deserve further efforts, not least in services sectors and in the digital field, where fragmentation along national lines tends to prevail. Another area where further efforts are called for is the internal development of the Eurozone, including as regards the banking union.[1] But the public goods must be given renewed priority in a context transformed by technology, the rise of global commons, regional challenges and geopolitical change.[2]

It is the purpose of this paper to discuss the case for enhanced provision of European public goods and to make a number of proposals for concrete steps and initiatives into that direction. Given the scope and the complexity of the issues involved, however, we

[1] These issues are of great importance, but including them here is beyond the scope of this paper. For comprehensive proposals see Bénassy-Quéré et al (2018).

[2] See Lamy and von Weizsäcker (2018) for a perspective on the EU as a provider of public goods.

do not aim at a detailed discussion of policy options in each of the potential fields for action. What this paper hopes to achieve is to contribute to and bring forward a constructive debate on the different areas where European public goods need to be provided in much greater depth and detail.

The structure of the rest of this paper is as follows. In section 2 we explain why the development of public goods is important for European citizens. Section 3 explores pros and cons of public goods provision at the European level. In section 4 we present eight promising areas for enhancing European public goods provision. In section 5 we discuss how they can be launched, organised and funded. Section 6 turns to options for France and Germany to jointly initiate European public goods provision, not as an exclusive, bilateral project, but as an open initiative where all EU member states are invited to participate. Section 7 concludes.

2. Why the development of European public goods is key for the future of European citizens

The provision of public goods is a key task of governments. Such goods are defined by two characteristics which imply that they are not provided by private markets. First, it is impossible or too costly to exclude people from the benefits generated by their provision; for this reason, consumers cannot be compelled to pay for what they consume. Secondly, there is nonrivalry in consumption; adding additional users does not increase the cost of providing the good, or only very little. It is therefore inefficient to exclude people from using public goods by charging prices, even if exclusion is possible. The standard textbook example of a public good is street lightning, but the concept is applicable to a whole range of policy areas, both nationally and internationally.

We are using the public good concept in a broad sense. The goods we have in mind do not only include pure public goods but also so-called club goods, where nonrivalry in consumption may not be perfect due to congestion effects and for which exclusion is possible, but joint provision is efficient (for instance, the Schengen Area is an example of a club). We also discuss publicly provided goods and policies which may generate significant spillovers across borders. For instance, migration policies are not classical public goods. The humane treatment of refugees may be considered as a typical public good but there are many more aspects to migration policies, some of which have properties of club goods. In the following we will refer to all of these goods as public goods or quasi-public goods.

Since the turn of the millennium, the notion of global public goods initially developed by World Bank economists (Kaul, Grunberg and Stern 1999) has been used widely and it is often referred to in policy discussions, either in a development context or as regards global commons such as the preservation of natural resources, climate change mitigation or financial stability. Strangely, the role of this concept in the European policy debate has been limited although, as developed below, its potential is significant in fields such as research, security and defence, border protection, the response to mass migrations, internal security, digital security or development aid, to name only the main ones.

The limited scope of common EU policies has been discussed for a long time. Proposals to broaden it are not new. But resistance against a stronger role of the EU in what would often amount to the provision of public goods, of club goods or the internalisation of spillovers have emphasized national sovereignty, differences in preferences and interests regarding the level and character of the public amenities provided by the EU, as well as governance issues including the so-called democratic deficit of the EU. The widespread belief that EU institutions might not be well equipped to deliver public goods because they are too far-away from the member-states and the citizens also plays a role.

Treaty provisions also contain the involvement of the EU in the provision of public goods. First, Art. 4 of the Treaty on the European Union states that “competences not conferred upon the Union in the Treaties remain with the Member States” (principle of conferral). Second, Art. 5 TUE specifies that “in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be *sufficiently* achieved by the Member States” (principle of subsidiarity, emphasis added) and that “the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties" (principle of proportionality).

Importantly, the principle of subsidiarity was made part of the EU's basic law on the occasion of the Maastricht treaty, with the intention of limiting the further extension of its role. Whereas it does not apply to exclusive EU competences, and therefore does not prevent the member states from unanimously assigning new missions to the EU, it effectively prevents mission creep. Especially, the sufficiency criterion can be used – and has been used – to prevent the EU from assuming additional responsibilities for the sole reason that this would be beneficial, or even that it would exercise them more effectively or more efficiently than the member states.

Historically, and again in recent times, thoughts have been given to extending the role of the EU in providing some public goods. This included initiatives to foster research and development, the extension of European border protection and military cooperation. Despite these initiatives the role of the EU in these policy areas remains limited, as will be explained in greater detail below.

The current division of tasks between the EU and the member states reflects complex political and economic trade-offs and compromises. However, various developments and emerging trends suggest that time has come to reconsider choices made in a different global environment. These are:

- *Increasing concerns about global commons* such as the climate, biodiversity and natural resources that call of a strengthening of global collective action. In principle, policy responsibility in such areas should be assigned to a global body, but disagreements over the severity of the issues, the distribution of efforts, and potential limitations to national sovereignty often prevent effective global governance. Initiatives can only result from coalitions built on the occasion of international negotiations where the major players have disproportionate weight. By acting jointly, the member states of the EU can contribute to tackling severe threats to the welfare of the European citizens and augment the chance that the eventual outcome will be closer to their preferences;

- *A lesser ability and lesser willingness of the US to provide global public goods.* Since World War 2, Europe has relied heavily on the US for its security, and despite occasional disagreements, for example on the occasion of the Iraq war, for major foreign policy initiatives. In the economic field, the US was widely regarded as the orchestrator of global endeavours and the guarantor of the global system. The international role of the US dollar was also often regarded as a sort of global public good that helped European companies and financial institutions to develop business on a global scale. A more nationalist stance, resources constraints and an increasing focus on the rivalry with China have contributed to changing US attitudes. The Trump administration's focus on bilateral trade balances, its open despise of multilateralism and its use of US centrality to impose unilateral preferences have led Europe to wake up to a new reality. In this context European states must redefine their own collective sovereignty;[1]
- *A more multipolar world.* The global system is being restructured by the rise of China, India and other major emerging powers. Instead of a multilateral regime orchestrated by the US and Europe it is heading towards a more transactional system dominated by a few major powers. Over a 20-years horizon the choice for Europe is to get its acts together and be one of these powers, or fall into irrelevance;
- *Regional threats and challenges.* The EU's immediate neighbourhood has been regularly affected by political instability, economic troubles, social unrest and military conflicts. From terrorism to great-power assertiveness, it portends potential security threats to the more prosperous and peaceful Europe. Instability, conflict and underdevelopment also result in significant inflows of asylum-seekers and economic migrants for whom Europe, rather than any particular country within it, acts as a magnet and a place where they hope to build a better future. These regional threats and challenges define public goods that are European by nature.

[1] See Leonard et al. (2019)

The main reason why the division of responsibilities between the national and the European level needs to be rebalanced is that, as a result of these changes, policies pursued at the national level can be increasingly limited in their effectiveness. Two examples illustrate the point:

- National sovereignty in defence policies means little for countries which are too small to defend themselves alone and therefore depend on alliances. Traditionally European defence is primarily based on NATO. We do not question its role. However the US, as the dominating military power of the alliance, understandably asks for a larger contribution coming from the nations that benefit from its security umbrella and it may be increasingly tempted to take unilateral initiatives, of which the sudden pullout from the Turkey-Syria border zone provides a foretaste. Because post-cold war US priorities are less and less centred on Europe, there is a genuine interest of the EU nations to be capable of defence initiatives that do not require the support and participation of the US. These two evolutions change the cost-benefit balance in favour of increased European cooperation in defence.
- The refugee crisis of 2015 and the developments that followed since demonstrated that in cases of massive and sudden inflows, there are limits to what EU member states can achieve acting on their own. Asylum-seekers and other migrants who happened to land in Greece, Italy or Spain did not aim to settle in these countries but in Europe. However, the EU did not have, and still does not have, a proper regime to protect borders, screen would-be immigrants, decide on their eligibility to asylum, organise their settlement and take care of them. What resulted were a messy, often inhumane processing of migration flows and increasingly bitter intra-European conflicts over the principles and the modalities of refugee protection. Even if preferences differ across the EU for historical and cultural reasons, a common policy could no doubt deliver better control over migration flows, relieve frontline member states from an excessive burden and ensure a more humanitarian treatment of refugees and migrants.

As developed in this report, similar considerations apply to a series of policy fields such as development aid, the challenges of climate change, policies towards China and others and more generally the defence of European economic and political interests as well as values in an increasingly multipolar, complex and interdependent world.

3. The pros and cons of public goods provision at the European level

What is the economic rationale behind the provision of public goods at the European level? The starting point for such debates is usually the idea of European value added. The European Commission (2011) defines it simply as "the value resulting from an EU intervention which is additional to the value that would have been otherwise created by member state action alone". This implies that competences and policies should be shifted to the European level if and only if this delivers added value relative to provision at other government levels. In the field of public spending, a study by the Bertelsmann Foundation (2013) defines European added value as follows:

"From an economic point of view, public spending at the European level ideally fulfils two criteria. For one, it should entail positive net benefits, i.e. the benefits should exceed the costs of public spending. Second, it should entail European added value (EAV) of public spending, i.e. the net benefits of public spending at the European level should be larger than those at the national level. In other words, EAV essentially compares the net benefits of spending by national governments with those that arise from spending in the same category at the European level. In this sense, added value is technically the difference between the net benefits of spending at the EU level and the national level. It is important to note that the magnitude of net benefits and EAV are not conceptually connected."[1]

This concept is compatible with the principle of subsidiarity enshrined in the EU treaty. In fact it can be regarded as one reading of it that interprets the sufficiency clause of the subsidiarity principle as requiring a positive EAV. Though initially elaborated in a public

[1] Bertelsmann Foundation (2013), p. 9

finance context, it can be extended to other policy areas like regulation or standard-setting where spending plays no or only a minor role. The same applies to allocating policy responsibilities to the national versus the regional or local levels of government.

The concept of European value added implies that positive net benefits of a policy are not enough to justify action at the European level. It needs to be demonstrated that such action yields net benefits which exceed net benefits that arise if the member states act on their own.

Various economic factors determine differences in net benefits of policies between different levels of government. These include i) economies of scale, ii) policy spillovers and iii) preference heterogeneity.

i) Economies of scale

Economies of scale are a well-known feature of many production processes. For instance, the costs of military procurement are likely to fall with size. If each European country produces its own weapon system the costs are higher compared to a joint system which is produced in much larger numbers.

Often, economies of scale are related to fixed production costs. If fixed costs are too high, individual governments may even decide not to provide a public good. The European satellite-based navigation system project GALILEO is a widely cited example. The cost of setting up this system is too large for any individual EU member state. In the absence of cooperation, it would not have been set up at all. This implies that one form of European added value may be a larger variety of public goods and services.

GALILEO illustrates the relevance of economies of scale as a criterion for public goods provision in a zero marginal cost world where fixed costs are huge, while the cost of extending the service to additional users is trivial. Such cases are increasingly frequent in the context of a digitalised economy. One should note that there may be cases where economies of scale are so significant that it is appropriate to include even non-European countries in common projects. For instance, the GALILEO project includes non-EU countries like China, South Korea, Israel and Saudi Arabia.

ii) Policy spillovers

Whoever provides it, a pure global public good benefits everyone. The concept of policy spillovers refers to less clear-cut cases where policies of one member state affect the welfare of other member states or the EU as a whole. There are many such examples. Spillovers of national migration policies played a key role in the recent refugee crisis. When Germany opened its doors to refugees in 2015 other countries were massively affected, because many migrants felt encouraged to come to Europe. Some of the refugees which came to Germany moved on to Northern European countries like Denmark and Sweden. At the same time, the German open-door policy reduced the burden on other countries (albeit not without the German government complaining that other countries were unwilling to do more). There were therefore spillovers in two opposite directions at the same time.

Spillovers occur in many areas of macroeconomic policy. If one country spends more to stimulate demand or cuts corporate taxes to attract investment, other countries will be affected through common trade and capital markets. They also arise in foreign economic policy. For instance, the decision by some EU member states to cooperate with China, within the framework of the Belt and Road Initiative, affects other member states. Along the same lines, the decision by Germany to pursue the Nordstream pipeline project has economic and political consequences for other countries that were not involved in the decision to build the pipeline.

Spillovers in public goods provision indicate that national provision fails to be efficient for Europe as a whole. If policies of one country impose costs on other countries, projects may be carried out although the net benefit to Europe as a whole is negative. If one country's policies affect partners positively, it may fail to act because benefits of national action accrue mostly to other countries.

Deep integration within the European single market gives rise to many spillovers. This is most visible to citizens as far as consumer protection is concerned: recurrent concerns over food safety illustrate the significant cross-border consequences of lousy checks by one member state. The same applies to some extent to bank safety or the security of pan-European networks. But spillovers also arise from national stances towards foreign (non-EU) investment: as the acquisition of any EU firm gives access to the entire European market, foreign investment in any member states that may raise security concerns has implications for the whole of the EU.

Policy spillovers are obviously not limited to the European level. The purest and most striking example can be found in the climate field, where action by any country (or the lack thereof) equally affects all citizens of the world, irrespective of distance or economic linkages. In principle, the corresponding collective action problem should be tackle at global level. Absent binding global governance arrangements, the provision of global public goods is however dependent on partial international agreements. By acting jointly in such fields EU countries maximise their chances of reaching a solution and upholding their joint preferences.

iii) Preference heterogeneity

Countries differ in their preferences for public goods provision. For instance, willingness of the population to spend money on defence seems to be higher in the UK and France than in Germany. If preferences for public goods provision differ, the net benefits from a common provision of these goods are smaller. Public good provision at international level therefore faces a classical trade-off between economies of scale and preference heterogeneity.[1]

In some fields, for example internet privacy or food quality, EU citizens exhibit highly homogeneous preferences, at least when compared to those of the rest of the world. In

[1] International unions can be analysed as resulting from a trade-off between economies of scale and the heterogeneity of preferences. See Alesina, Angeloni and Etro (2005).

some others, such as defence or the entry of non-Christian migrants, differences are wide.

Preferences are not set in stone, but they are the product of history. If growing economic and political integration leads to a convergence in preferences for public goods provision in the population, the scope for European policies to add value are likely to grow accordingly. But it would be an illusion to assume that integration and time will inevitably lead to convergence. Migrations again provide a telling example: in many new member states, reluctance to multiculturalism outlasted enlargement. It has perhaps even increased post-enlargement.

Of course, the concept of preferences of 'countries' is problematic. Individual people have (heterogeneous) preferences, and it is the political process that transforms individual preferences into collective decisions. Citizens accept policy to depart from their own preferences if they perceive it as the outcome of a legitimate political process. This is what happens within nations. At the European level, the political process works differently: it combines the aggregation of citizen preferences (through the parliamentary process) and that of national ones (within the Council). For this reason, for given preferences different political results will emerge at EU level than those that would emerge from the replication of standard political processes. This is especially the case in fields where decisions are taken by unanimity, but it also happens in fields governed by qualified majority. The willingness to shift more public goods provision to the European level will therefore depend not just on convergence or divergence in preferences but also on the political decision-making process at the European level, and the extent to which it is perceived as legitimate[1] and effective.

4. Promising areas for the development of European public goods

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[1] In the debate about the 'European Common Good', which is related to the notion of European public good, legitimacy also plays a key role, see Callies (2014).

The EU has for long been regarded as a market as well as a political endeavour. A first approach to European integration – historically mostly associated with the UK - put emphasis on the benefits from integrated markets for goods, services, capital and labour. A second one – initially promoted by Germany – envisaged in addition the step-by-step building of a federal Europe that would culminate in a political union. A third one – often advocated by the French, but which increasingly gained traction, especially after Germany became more and more circumspect vis-à-vis encroachments on national prerogatives – emphasised interstate cooperation under the umbrella of the European Council.

The EU as we know it combines all three approaches. All three, however, have gradually run out of steam.

- The goal of forming a single market was set 35 years ago. Although it has not been completed and remains valid, it would be an illusion to think that it can still mobilise European citizens. Throughout Europe, reservations towards the downsides of market integration have developed and concerns about distributional issues have increased. To push the envelope a little further consumes a lot of political capital;
- Political integration has reached a stalemate. If there is a consensus among European politicians, it is that this is not the time to contemplate a major treaty change. Even within the euro area, appetite for integration is hopelessly scant. The German constitutional court has expressed growing reservations to transfers of sovereignty, even within the framework of existing treaties;
- Interstate cooperation has reached its limits. Divergent perspectives, free riding incentives and widespread fondness for national sovereignty have nearly paralysed the European Council. Brexit has led to a rare display of unity, but that is not replicated about any positive project. Partly because of the nature of eurozone and migration crises, there has been a shift to an intergovernmental EU in recent years. This has led to some effective results, but the approach is nevertheless fraught with problems of free riding and strategic behaviour.

This state of deadlock is lethal for the future of the EU, especially at a time when it is confronted with so many technological, economic, climatic, security and migration challenges. If the EU is unable to build on the appointment of a new leadership team to redefine itself and if it has not achieved results by the time the term of the new Commission ends in 2024, an important opportunity will have been lost and the ability of the EU to address the key challenges of our time will be questioned.

It is time to think differently about the purpose of the EU. Not only as an economic integration project nor as a political one, not as a market or as a super-state, but as the provider of public goods that benefit the European citizens and are more efficiently and more effectively produced at European rather than at national level.

The rationale for this new approach is simple: there are nowadays reasons to believe that in a number of fields, economies of scale are more pervasive, spillovers are stronger and preferences are less heterogeneous than they used to be. At the same time, dealing with these issues on an intergovernmental basis faces the difficulty of free riding and strategic behaviour, which leads to suboptimal outcomes. As a general principle, the EU should focus on providing benefits to the citizens in fields where it has added value.

The public goods perspective can help to define how current policies should evolve. A good example is the CAP. As indicated already, it initially stemmed from well-defined objectives, some of which – such as self-sufficiency and food security – clearly qualify as common goods. Over decades however priorities have changed, the CAP has evolved, and in the process it has taken an increasingly distributional character. As apparent in global trade negotiation, food safety and food quality – including its overall environmental footprint – do have the character of European public goods, because preferences in Europe often differ from those that prevail on other continents. But the CAP nowadays is in large part a sectoral social policy, whose centralisation at EU level is a matter for discussion. Even some of the environmental services it pays for are inherently local and could be remunerated by national or subnational governments.

Focusing on the European public goods dimension of existing European policies can therefore help to map out directions for their modernisation and reform.

Potential candidates for further European public good provision can be found in fields where changes in Europe's external environment and problems of collective action call for reform, while at the same time a sufficient number of member states share common interests and perspectives. This may especially apply to the following eight areas, which we rank in ascending order of difficulty regarding political feasibility:[1]

1. Foreign economic relations
2. Climate change mitigation
3. Digital sovereignty
4. Research and development in large and risky projects
5. Development cooperation and financial assistance to third countries
6. Migration policy and the protection of refugees
7. Foreign policy and external representation
8. Military procurement and defence

i) Foreign economic relations

[1] This is admittedly a ranking based on a rather subjective assessment. For the key message of our paper the ranking plays no particular role.

The EU internal market is the largest market in the world. Controlling and granting access to this market implies huge leverage globally, which can be used to make sure that European companies have access to foreign markets, to ensure a level playing field and to assure that trade partners comply with fair competition standards.

Currently, trade policy, competition policy (above a certain merger threshold) and a large part of regulatory policy are of the responsibility of the EU. Thanks to these competences, the EU has established itself as a major global regulatory power – it has even been dubbed “the world’s regulator”.[1] Bilateral or regional trade agreements embed many European preferences as regards product safety, environmental standards and even labour standards. Competition rulings have effectively blocked mergers between non-European companies to prevent the establishment on the European markets of dominant positions that would have affected European consumers. And EU standards have had major influence worldwide, be it for car safety or internet privacy.

For long, European policies in the fields of trade, competition and regulation have been regarded as building blocks for a global rules-based multilateral regime. But the global economy has entered a new, confrontational phase characterised by trade bilateralism and increasing interference of geopolitical considerations in international economic relations. The rules and procedures of the WTO are being openly questioned by the Trump administration, which is also making use of the centrality of the US financial system and the US currency to enforce unilateral sanctions against Iran. Meanwhile, China is gradually building its own global network of bilateral trade, finance and investment agreements.

This new context has deep implications for the EU.[2] First, it will test the member states’ ability and willingness to hang together and stand by a common policy stance when confronted to direct political pressures. Disputes with the US over trade and the Iran sanctions are indicative of the risks involved. In principle, competence assignment and

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[1] Editorial Comment, Wall Street Journal, 31 March 2006.

[2] The proposals that follow draw on Leonard et al. (2009)

governance provisions give the EU the means to act unitarily, but the strength of the collective commitment to joint action will be tested.

Second, the EU still lacks competences to effectively control access to the internal market. Corresponding policies, including investment screening, are still primarily a responsibility of the member states. This is a matter for concern, both because investment gives access to the entire internal market and because politically-motivated foreign investment can serve as a channel for a foreign power to build clienteles inside the EU. In other words, economic and political spillovers from national policies are too large for investment policy to remain of the exclusive competence of the member states. A way forward would be to give the Council the right to decide by qualified majority to block a foreign investment that represents a risk to European security. The EU should also develop instruments, such as a dedicated investment fund, to offer member states alternatives when foreign investments are disallowed.

Third, the EU should reconsider its neutral stance vis-à-vis the internationalisation of the euro. During the first two decades of the European currency, it was appropriate to "neither discourage nor encourage" its use by non-resident entities, as priority was to establish the euro as a stable currency and to build the internal policy machinery. But as pointed out by the Commission (2018a) and the ECB (Coeuré, 2019), global conditions have changed: China is promoting the use of the renminbi as a first step towards turning it into an international currency, while the US is increasingly inclined to using the global role of dollar as a channel for enforcing specific geopolitical preferences. Furthermore, recent research by international economists has emphasised the adverse consequences of dollar invoicing on the sensitivity of trade flows to exchange rate changes.[1]

While structural improvements such as the development of a capital market union will certainly have a positive impact on the global demand for euro assets, the euro will not develop as an international currency and it will not emerge as a widely used vehicle for trade invoicing and financial transactions if non-residents are unsure of their access to

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[1] See Boz, Gopinath and Plagborg-Møller (2018).

euro liquidity in times of stress. For this reason, the EU should take steps towards the establishment of the euro as a major international currency, including through the granting to swap lines to partner central banks and the introduction of a common safe asset.[1]

Fourth, the EU should review its representation in international economic organisations. Nowadays European countries act as one within the WTO and in several regulatory bodies, but they participate individually in the governance of the Bretton Woods institutions. There is currently little pressure on them to change this state of affairs: they enjoy an influence out of proportion with their current economic weight and the plurality of seats leaves room for the expression of often disparate national positions. But the downside of European overrepresentation in the IMF and the World Bank is that China and other major emerging countries do not have much ownership of these institutions. The risk for Europe is to accelerate the decline of the global institutions it has most influence on. A move to a consolidated representation – perhaps first of the euro area in the IMF[2] – would make room for an enhanced representation of the developing world, while giving to the EU a strong and potentially authoritative voice.

For it to be effective, however, it would need to be preceded, or at least accompanied, by a strengthening of the internal governance of the euro area and the EU.

ii) Climate change mitigation

The incoming European Commission president, Ursula von der Leyen, wants Europe "to become the first climate-neutral continent in the world by 2050" and she has proposed to reduce EU CO_2 emissions by 50 to 55% in 2030 already. In so doing, she is responding to a growing popular demand for effective action: citizens in the EU are significantly

[1] As Bénassy et al (2018) point out this does not require joint liability of the member states for government debt, which would create severe governance and incentive problems.

[2] See also our proposal for Franco German initiatives in section 6.

more concerned by global warming than in the rest of the world, and they are increasingly alarmed.[1]

But citizens do not want pain without gain. It is important to distinguish the moral imperative put forward in media debates about climate change, which are typically dominated by middle-class educated people, and the willingness to take serious action for climate change in the wider population. As soon as voters realise that such action may require inconvenient lifestyle changes and lower real incomes, due to higher fuel prices, for instance, resistance grows. Citizens are especially reluctant to efforts if they perceive them as without reward.

As far as climate change is concerned, effectiveness cannot result from efforts conducted in isolation at national level. Most European citizens understand that none of their countries alone has sufficient leverage to have an impact in international climate policy. Therefore, they do expect the EU to be their mouthpiece and try to lead or at least influence the action for global climate change mitigation. Indeed, climate preservation is a truly *global* public good and even the EU as a whole represents less than 10% of the global emissions of greenhouse gases (International Energy Agency, 2018). It is expected that by 2030 its share will be down to 5%.[2]

While the overall economic and political weight of the EU also declines, it is still globally relevant. But using that leverage on a global scale for climate protection requires that the EU countries act jointly. The assignment of policy competence between the EU and the member states, however, remains fragmented. Art. 4 TFUE lists the environment as a shared competence and Art. 191 states that "Within their respective spheres of competence, the Union and the Member States shall cooperate with third countries and with the competent international organisations. The arrangements for Union cooperation may be the subject of agreements between the Union and the third parties concerned"

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[1] See Poushter and Huang (2019) and other Pew Research surveys. For more details on attitudes in the EU see the October-November 2018 Eurobarometer on the future of Europe.

[2] Source: www.climateactiontracker.org

before adding that “the previous subparagraph shall be without prejudice to Member States' competence to negotiate in international bodies and to conclude international agreements”.

In practice, the EU is party to the conference of the parties (COP) process and the Paris agreement of 2015. In other words, the EU member states negotiate collectively with the rest of the world. As such, the EU has committed to a certain amount of emissions reduction (the so-called *Nationally Determined Contributions - NDCs*), which is further decomposed into a series of NDCs by its constituent member states (several EU member states have specified additional goals for themselves). Climate policy instruments, however, are not all in the hands of the EU. It is in control of the Emission Trading System (EU-ETS), the cap-and-trade scheme that mostly applies to energy-intensive industries and it also has responsibility for setting regulatory standards (for example, for the performance of new vehicles). But the EU has no control of carbon taxes (still governed by the unanimity rule) nor of transportation, building or energy policies, which currently remain primarily a national responsibility. So the EU has overall international responsibility for climate policy ends but it has only partial responsibility for the means.

The governance of climate action in the EU aims at overcoming the corresponding collective action problem. The 2018 regulation on the governance of energy union and climate action sets forth precise procedures for reporting and monitoring.[1] In addition the ‘Effort Sharing Decision’ agreed in 2018 implies binding targets for the member states’ emissions reductions in sectors not covered by the ETS.[2] But it is far from clear whether this can be enforced effectively as constraints on CO2 emissions start to bite. Another open question is whether the EU will, as indicated by president-elect Ursula von der Leyen, take measures to prevent carbon leakage and preserve the competitiveness of its energy-intensive industries. A carbon border adjustment tax which that would put imports produced with high CO2 emissions on an equal footing with domestically produce goods and vice versa will be necessary if wide discrepancies in the intensity of emission

[1] See https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R1999&from=EN.
[2] See https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R0842&from=EN

reduction efforts remain or even accentuate in the years ahead. It would need to be designed in such a way that it does not contradict WTO rules.

Because climate action concerns all aspects of everyday life, it is by nature a shared competence between the Union and the member states and it would be unreasonable to transfer all powers to Union level. The EU should let countries pursue different policies in areas where conditions or preferences differ – for instance, insulation of buildings in the warm climate of Southern Europe does not need to be the same as in Northern Europe – but overall national policies should be coordinated so that the EU as a whole reaches its emission reduction targets. In other words, climate preservation is a public good at global level, but the European contribution to it is also a public good for each and every individual member state.

For the long term, the objective should be to integrate all sectors including road traffic and housing into a European carbon pricing regime based on the ETS or on an appropriate carbon tax system. In this case emissions reduction targets for individual member states would be unnecessary and even harmful because they would undermine cost-efficient emissions reduction for the EU as a whole. The EU should be given the authority to set by qualified majority binding corridors for carbon prices.[1]

Since extending the ETS to all sectors will take time, it is important that all member states introduce effective complementary systems through taxes or sector-specific emissions trading schemes during the transition. The carbon price corridor should also apply, at least after a period of adjustment. It is important that the price corridors of the different systems should converge over time, so that the full introduction of the ETS after the transition period causes no disruptions. There should also be additional mecha-

[1] Price corridors avoid excessive fluctuations in prices of emissions certificates over the business cycle and thereby reduce uncertainty which may inhibit private investments, in particular in green technologies. Nevertheless, price corridors may have to be adjusted over time to make sure that objectives for emissions reductions are met. This can be achieved through hybrid systems combining the ETS with a price corridor, see e.g. Traeger et al (2019).

nisms for sanctioning a member state that does not participate in the joint effort, for example through excluding it from targeted financing from the EU budget or by the European Investment Bank.

Additionally, it would be important to avoid replicating in the climate field the political economy set-up that has had the effect of nurturing acrimony vis-à-vis EU efficiency-promoting policies: adjustment costs should not be entirely left to the member states to cope with. A dedicated European fund would help to offset the social cost of transitioning to a decarbonised economy.

Finally, climate change mitigation is only the most important dimension of the broader global environmental agenda. The preservation of biodiversity and maritime resources raise very similar challenges and in these fields also, the EU can be much more effective if acting as one.

iii) Digital Sovereignty

In 2010 the European Commission launched the 'Digital Agenda for Europe' as part of the Europe 2020 strategy. The focus of this initiative was "to deliver sustainable economic and social benefits from a digital single market based on fast and ultra-fast internet and interoperable applications."

Developing the digital internal market remains a priority. But nearly ten years after the Digital Agenda was launched, results are disappointing. Europe is lagging behind in the global digital race and this threatens its traditional comparative advantage in a series of industries, from aerospace to motor vehicles and banking. It is at risk of losing its digital sovereignty.

The EU needs to do more. With the General Data Privacy Regulation (GDPR), implemented in 2018, it demonstrated that it is not powerless. This regulation has brought fundamental change in the protection of private data of EU citizens. It also regulates the transfer of personal data outside the EU. Internationally, the GDPR is widely seen as a leading standard for privacy protection. Thus, despite controversies about the details of the regulation, it is an example of effective policy action with global impact at the EU level. In the future the EU should strengthen its ability to determine its own digital future, including through buttressing its global influence over the setting of standards in digitization. As outlined in the digital agenda of the president-elect of the European Commission, it should especially strike a balance between stronger privacy requirements than in China or even the US, and the need to develop an adequate regulatory environment for the development of artificial intelligence

Another important area where EU involvement is key is the development and protection of digital networks. For increasingly digital economies and societies, reliable, resilient networks are of systemic importance. In this area national policies are hitting limits: cybercrime does not stop at borders and a failure to prevent it in one member state can create significant economic damage in partner countries (European Commission, 2016).

This insight is not new, and various measures have been taken by the EU. Already back in 2004, it created the European Union Agency for Cybersecurity (ENISA), located in Athens. However, the responsibilities and capabilities of this agency are limited. Its mission is primarily to support and coordinate national efforts to maintain and improve cybersecurity. In 2016, the EU directive on security of network and information systems (NIS) came into force. It requires the member states to take a number of measures to protect cybersecurity. These include the creation of a rapid response team for cybersecurity incidents and cross-border cooperation in cybersecurity matters. In 2018, the European Commission presented a concept for the digitization of its own activities (European Commission (2018b), which focuses on effective data use, privacy protection, cybersecurity and interoperability. In 2019, with the European Cybersecurity Act (Regulation 2019/881), ENISA has been given the task to prepare the 'European cybersecurity certification schemes' which will create the basis for certification of products, processes and services that aim at supporting cybersecurity in Europe and the functioning Digital Single Market.

While these are steps in the right direction, more needs to be done in view of the high degree of interdependence among member states and the collective vulnerability resulting from the weakness of common provisions. Dependence on infrastructures provided and controlled outside Europe may undermine European cybersecurity and digital sovereignty. Reliance on Chinese digital infrastructure is a case in point but strong dependence on US data storage facilities is also an example. But vulnerabilities are also internal: flaws in the security system of any member state can affect all partner countries. The EU therefore needs to pool its resources and make greater efforts to protect cybersecurity and digital sovereignty in Europe.

To assign new responsibilities to the EU level can be a response only to the extent the Union level body and the common provisions elicit sufficient trust across the member states. Clearly, this is not yet the case and mutual lack of trust is a strong driver of fragmentation. National officials in charge of cybersecurity cannot be blamed for not sharing sensitive information with partners they do not trust sufficiently. For this reason, progress can only be gradual and as in the field of defence, some form of variable geometry is inevitable. We propose to task a high-level group to assess the situation and to make proposals for raising the effectiveness of European digital sovereignty, in particular of cybersecurity. The group should propose measures that should apply to the single market as a whole, as well as avenues for closer cooperation amongst a subset of countries. It should consider, among other things, the extension of cybersecurity research both in the private sector and in public research institutions and the development of European cloud services.

iv) Research and Development in large and risky projects

Knowledge is by nature a public good and research, which aims at augmenting it, has major cross-border spillovers. For this reason, the EU has historically been involved in fostering research across the Union and beyond. The share of research and innovation spending in the EU budget has actually increased significantly, from 6% in the early 2000s to 8% in 2017, and is expected to grow further in the 2021-2027 period of the next Multiannual Financial Framework. The Commission has tabled proposals for a stepwise increase of spending on research and innovation, through the Horizon Europe (ex-Horizon 2020) programme, defence research and specific programmes such as ITER and Digital Europe. Overall, the Commission proposes spending almost €100bn over seven year on Horizon Europe, plus about €20bn on the other research programmes. Research spending would exceed 10% of the EU budget.

The value of research programmes depends heavily on the quality of the projects that are being financed. While some open science, bottom-up driven programmes like those of the European Research Council are widely recognised as promoting excellence, others, such as those financed under the Global Challenges and Industrial Competitiveness heading, combine the excellence criterion with other criteria regarding impact and the distribution of research funds across EU countries.

A recent assessment (Veugelers and Baltenspenger, 2019) has found that the overall quality of EU-funded research is satisfactory, but that it would benefit from strengthening collaboration between EU- and non-EU researchers and from highlighting excellence even more, including for targeted programmes or when aiming to support the advancement of research in catching-up member states. This highlights the importance of proper governance. In research, as well as in other fields, strong arguments for joint action through the EU budget can be quashed by a failure to administer resources efficiently.

In recent times, the financing of breakthrough innovation has become a topic of particular concern. Part of the technology and productivity handicap Europe is suffering from in the digital economy and especially artificial intelligence is attributed to a failure to finance disruptive innovation. The US DARPA programme is often mentioned as something to emulate: research and innovation funding that “reaches for transformational change instead of incremental advance”. DARPA’s mission is the financing of risky projects that have a high transformative potential but also a high probability to fail. By nature, capacity to finance such projects is related to the size and diversity of the portfolio of projects. The pooling of efforts allows to diversify risk and therefore to maximise chances of success.

This is the rationale behind Franco-German and EU initiatives for the creation of a European DARPA. Conversations have been held between Berlin and Paris. At EU level, following a pilot phase, the Commission is proposing to establish and fund a European Innovation Council devoted to the nurturing of risky projects.

Breakthrough innovation rests on a combination of bottom-up initiatives and targeted programmes that lead to the exploration of new fields. As part of a European innovation ecosystem, the potential for a DARPA-like scheme is beyond doubt. Success however requires an ability to withdraw support to fledging or insufficiently successful projects. Evidence suggests that multinational endeavours find it difficult to take such decisions, as they may have significant distributional consequences across member states. For example, innovation within the framework of European space cooperation is hampered by the rigid division of labour between states cooperating in the Ariane programme.

Whether or not a European DARPA can succeed largely depends on an exclusive focus on pathbreaking projects, without consideration for their distribution across countries and irrespective of the potentially adverse effects of radical innovation on existing industries. It also depends on an ability to terminate the insufficiently successful ones decisively and abruptly, even if this is bound to affect certain member states negatively. If agreement on these conditions can be reached at EU level or amongst a group of member states, so that an independent governance body can be put in place and implement them, the endeavour is very worth pursuing.

v) Development cooperation and financial assistance to third countries

It is the objective of development aid to fight poverty and hunger and improve health, education and general well-being of people living in developing countries. Industrialised countries have a common interest in development aid. Therefore, the support of economic development is clearly a public good for the EU member states and beyond, especially now that development assistance has been largely untied from the donors’ direct economic interests.

Together with its member states, the EU is by far the first provider of development assistance globally. The OECD reckons that its share of official development assistance reached 57% in 2017. Although the OECD figures do not include China or the Gulf countries, the EU taken as a whole devotes to development assistance twice as much as the next most important country. It also aims at addressing development issues in other policies such as trade, finance and climate change. As pointed out in the recent Wieser report (Wise persons, 2019), however, fragmentation, lack of coherence and policy inertia imply that its global influence and leverage remain limited.

The EU's main instrument for providing development aid is the European Development Fund (EDF). It was created in 1957 by the Treaty of Rome. The EDF funds cooperation activities in the fields of economic development, social and human development as well as regional cooperation and integration. It is financed by contributions from EU Member States according to a contribution key and is covered by its own financial rules. Although the 11th EDF remains outside of the EU budget, the negotiations in the Council of Ministers on its different elements have taken place in parallel with the negotiations of the external Instruments financed under the budget, to ensure consistency. The total financial resources of the 11th EDF amount to €30.5 billion for the period 2014-2020.[1] This represents a little more than 3% of the EU budget.

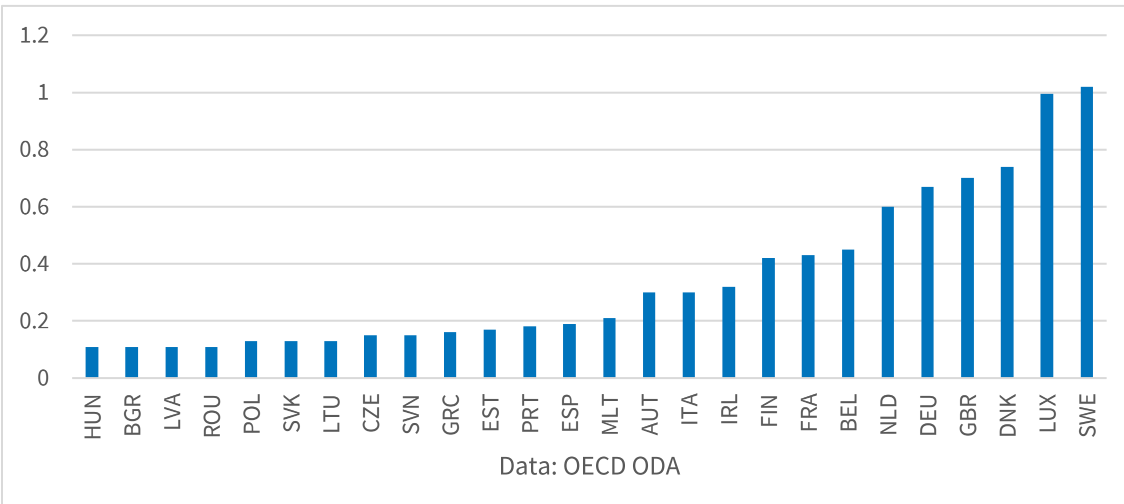
Development aid is currently a shared responsibility. Despite significant activity at the EU level, less than 20% of the total development assistance of the EU countries is channelled through the EU institutions. The largest part of development aid policy is still dominated, either by national policies and decisions, or by the multilateral development instruments.[2]

[1] See https://ec.europa.eu/europeaid/funding/funding-instruments-programming/funding-instruments/european-development-fund_en

[2] See the data compiled by the OECD's Development Assistance Committee.

Figure 1 provides an overview of the spending on development aid (official development assistance spending) of EU member states. The United Nations have agreed to set a ratio of public spending on development aid to gross national income of 0.7 per cent. Whereas Sweden and Luxembourg and UK and Denmark exceed this threshold, most EU countries fail to comply with this standard, and some are very far from approaching it (Figure 1).

Figure 1: Public Spending on Development Aid in 2017 (% of GNI)



The reason for this state of affairs is that EU members have different sectoral or geographical priorities, often as a result of historical ties with specific developing regions or countries. Traditionally, member states have been eager to maintain this division of labour, despite the fact that aid fragmentation reduces its effectiveness and may lead to an undesirable distribution of development aid, with some development countries receiving significantly more aid than others, without clear justification.

The EU also lacks an effective development arm. Responsibility for it is shared between several DGs within the Commission, and funds are allocated rigidly within the framework of the MFF. The EIB has limited development expertise and does not see itself as a policy-setting institution, while the EBRD has a limited geographical scope. National development institutions are nimbler, but smaller, and their policy agendas are only partially aligned with each-other.

Two recent evolutions however lead to question the effectiveness of current arrangements and call for a re-examination of European development policies:

- First, Europe is waking up to the renewed urgency of fostering inclusive development in Africa. Sustained demographic growth, heightened security threats and increased migration pressure combine to call for a major effort towards prosperity and stability in Africa. This is a challenge for the whole of Europe, because no EU country would lastingly avoid the consequences of poverty and instability south of the Mediterranean;
- Second, new players challenge the traditionally dominant role of Europe in development finance. Private institutions, often from the US, now contribute in a meaningful way to development assistance, and they have acquired a leadership role in their priority fields. Furthermore, China has taken a major role, especially but not exclusively through the Belt and Road Initiative. In many developing countries, it is by far the main provider of credit, investment and expertise, and its influence has dwarfed those of the former colonial powers and other partners from the EU, including the EU institutions (Horn, Reinhart and Trebesch, 2019). Institutions where the EU has a strong role, such as the Paris club of official creditors, are at risk of being pushed into irrelevance. Painfully negotiated principles, for example within the context of the debt relief to Highly Indebted Poor Countries (HIPC), are being put aside by China's collateralised lending.

To tackle these mounting challenges the EU and its member states should accept questioning the prevailing division of labour between EU institutions and the member states. They should also reassess their development priorities, instruments and procedures. This in turn raises an institutional issue: the EU currently lacks an effective development policy body able to innovate, formulate options for the future, select priorities and administer a range of development instruments. To build up one, they need to decide whether or not to bolster the out-of-area mandate of the European Investment Bank

(EIB), and whether or not to leverage their participation in the European Bank for Reconstruction and Development (EBRD). A clear, strategic choice must be made.

In these reforms it should be considered that different member states have different capacities and comparative advantages in cooperating with different countries. But these capacities should be used within the framework of a consistent EU-wide approach to development policy. There are close links to other areas of European public goods provision, in particular migration policy, the protection of external borders, climate policy and foreign policy in general.

vi) Migration policy and the protection of refugees

Migration policy is an area where spillover effects from national decisions are massive and where, at the same time, preferences differ widely. This makes common policies both particularly necessary and particularly difficult.

From foreign students to labour migrations and from the hunt for talent to the protection of refugees, migration policies have many facets, and in almost all of them policies of individual member states have consequences for others. For instance, if one member country grants residence and work permit to a national from a third country, that person has the right to live and work in the entire EU. Equally importantly, uncontrolled migration flows result from the fact that countries participating in the 26-members Schengen area practically delegate border control to their partners. Countries of entry have little incentive to limit inflows if they know that immigrants will eventually settle elsewhere.

At the same time, migration policy involves extremely strong national dimensions. National and cultural identities, the size and origin of foreign-born communities and legal conditions for acquiring nationality all vary across EU members. Where there has been remarkable convergence over recent decades (for example with the adoption of *jus soli* in Germany or the transformation of Italy or Spain from emigration countries into immigration countries), significant differences remain. Especially, most new member states are adamantly reluctant to the ethnic, cultural and religious diversity that has developed in Western Europe.

Some of the immigration spillovers are being addressed through dedicated EU programmes, for example the Blue Card programme that grants to high-skilled professionals work permits valid in 25 of the 28 EU member states (all of them but the Denmark, Ireland and the UK). Another area for potential harmonisation regards the granting of long stay visas to students from abroad. But EU policies have failed to address the most pressing issues, which concern asylum seekers and illegal migrants from third countries. The Dublin convention regime for processing asylum applications has broken down, attempts to decide by qualified majority on a quota system for relocating refugees has led nowhere, and the border-free Schengen area is on the verge of collapse.

This is not to say that progress has not been achieved. 2016 legislation has transformed Frontex from an agency for the management of cooperation amongst member states into a European Border and Cost Guard Agency equipped with monitoring, coordination and intervention abilities. But migrations issues have remained a matter for acrimonious disputes amongst member states and the threats of unravelling of European area of freedom, security and justice and the Schengen system have not dissipated.

Three objectives of migration policies are widely shared in the EU. First, it is important that member states are able to decide who is allowed to immigrate from outside the EU. Second, migrants and refugees must be treated in a civilized manner, in accordance with UN conventions. Third, legally-grounded decisions not to grant residence to an immigrant should be enforced. A fourth objective is however disputed: that refugees who are entitled to protection under the UN convention be distributed to in such a way that a certain balance is achieved across countries, considering the migrants' preferences as well as those of the member states. Whereas, if defined in broad terms, this objective is shared by a majority of member states, a minority rejects the very principle of welcoming refugees from Africa or the Middle East.

A lasting solution to the problem would require:

(1) A common border protection system combining national authorities and Frontex;
(2) A common legal framework for asylum, based on the UN convention, and a close coordination on the implementation of this framework; eventually, it should lead to a common refugees protection agency, to which the responsibility of screening applications for asylum should be given;
(3) Common principles for the allocation of persons to whom asylum rights have been granted;
(4) Common policies for the resettlement in their home country of persons to whom immigration rights have been denied, including through comprehensive negotiation with countries of origin.

"Common" provisions and policies does not imply full centralisation, but a degree of co-operation between national authorities that would ensure an even application of mutually agreed principles. Joint action would ensure a better border protection, a more uniform application of the legislation, a more balanced distribution of the inflows and, last but not least, stronger leverage in the negotiation between third countries.

It is evident that such common policies cannot be put in place between countries that do not share the same fundamental principles, which implies moving ahead with a subset of them.

Common border protection and control over migration flows is also a necessary condition for the smooth functioning of the Schengen agreements, which makes the lives of European citizens simpler by abolishing border controls. The logic of a border-free and passport-free area such as Schengen is that it implies a common migration policy. Eventually, the geometry of Schengen and that of the common migration policy area will necessarily coincide. A smaller, more coherent and resilient Schengen would be far better than the unravelling of Schengen.

There are many obstacles to common action on migration matters. But urgency also commands that these obstacles are overcome. Again, failure to act and to adopt solutions that measure up to the current and future challenges would undermine the border-free movement of persons within the Schengen area, which remains one of the major achievements of European integration.

vii) Foreign policy and external representation

In a world increasingly dominated by economic and geopolitical superpowers, foreign policy is another area where the case for a more European approach promises significant gains. As in the case of defence policy, even the large EU member states need to acknowledge that their weight in the world is diminishing and the impact of their foreign policy becomes smaller and smaller. And while the foreign policies of individual countries may support that of European partners, it may also undermine it. As a growing share of the European population shares common values and interests in foreign policy, especially vis-à-vis powers like China, Russia and the US, or global challenges like cybersecurity and climate change, there should be a lot to be gained by shifting more foreign policy competences to the European level.

A strong case can be made for better projecting European soft power. Seen from a distance, Europe often looks as a single continent as far as culture, preferences and values are concerned. Despite recent snags Europe remains a human rights harbinger, a welfare state model and a cultural magnet. It has made gender equality a priority. New and controversial issues regarding privacy, bioethics or the protection of the environment find it largely united. It has pioneered diplomatic initiatives to promote peace, democracy, self-determination, and the rule of law. It would therefore make sense for European countries to unite much more on these fronts.

In some fields, European influence globally is currently diminished by the plurality of national initiatives. At a time when powers and would-be powers strengthen their influence by speaking directly to the citizens, European media remain weak and fragmented. There is no European equivalent of the likes of Russia Today or Aljazeera – nor of CNN and Netflix – and the initiatives there have been, such as Arte or Euronews, have remained niche endeavours. A better designed, less disjointed, more entrepreneurial initiative to give Europe a voice globally would be well worth pursuing.

Going beyond soft power, the establishment of a European foreign policy would be a more challenging undertaking. The EU has taken first steps towards it. These include the creation of the position of the High Representative of the Union for Foreign Affairs and Security Policy, who is the chief co-ordinator and representative of the Common Foreign and Security Policy (CFSP) in the EU. The Union has also created the European External Affairs Service (EEAS), the EU's diplomatic service. The president-elect of the Commission, Ursula von der Leyen, has emphasised that she intends Europe to be "more assertive and more united" in the world and that its external action must become "more strategic and coherent".[1]

While these are important steps, the role of the EU in foreign policy is still limited. Member states often prefer to act independently or within the framework of ad-hoc partnerships (such as the Franco-German partnership for the "Normandy format" dialogue with Russia and the Ukraine). And even when EU countries act jointly, all key decisions are finally taken in the European Council or in the Council [of Foreign Ministers] of the EU, by the national governments of the member states and by unanimity. Proposals to move to qualified majority voting in certain areas of the CFSP have not been implemented.[2]

The creation of the High Representative position and the development of the EEAS have not resulted in delegating foreign policy to the EU level. On Iran for example, the High Representative participated in P5 +1 negotiations together with the Foreign Ministers of France, Germany and the UK. Decision to pursue a common foreign policy in a certain field or vis-à-vis a certain partner still belongs to the individual member states of the EU. For key international actors like the US, China or Russia, the large member states are

[1] See her mission letter to Vice-President Designate Josep Borrell and her note on the „Main principles oft he working method", both released on 10 September 2019.

[2] See the 2018 State of the Union address by Commission president Juncker.

perceived as the key European actors, not the EU itself. As long as that is the case, the effectiveness of European foreign policy will be limited, even in areas where there is agreement to work jointly.

The underlying rationale for this state of affairs is that national foreign policy preferences continue to differ significantly. Larger member states tend to have a more assertive view of foreign policy than smaller ones, while perceptions of security threats continue to differ markedly, as visible for example in policies towards Russia. Furthermore, governments also pursue different bilateral economic interests, with broader implications for foreign policy. Attitudes towards China are for example disparate, as indicated by distinct responses to the 16 + 1 (now 17+1, with Greece having joined) meetings or the Belt and Road initiative.

The lesson from experience is that mechanisms alone – such as the creation of a European External Action Service – are not sufficient to overcome obstacles arising from deep policy divergences. But conversely, the absence of coordination mechanisms can prevent joint action even in fields where preferences are largely common. The challenge for the years ahead is therefore to put in place cooperation mechanisms that can give effectiveness in fields where policy perspectives are widely shared. Various such mechanisms have been proposed, such as a selective move to qualified majority voting and the creation of a European Security Council. [1]

Finally, a more practical question is that considerable cost savings could be achieved if the EU member states decided to cooperate more closely at operational level. According to calculations in Bertelsmann Foundation (2013) the EU member states currently entertain 2206 embassies and 708 consulates worldwide. If their tasks were taken over by EU representations, roughly 2023 embassies and 483 consulates would be redundant and could be closed. Clearly, a merger of external representations is currently out of the picture. However, these numbers suggest that there is room for savings and effectiveness

[1] It has been proposed to strengthen EU security policy by introducing a Commissioner for defence and security and a European security council (Coelmont, 2019). However, we think that it may be counterproductive to introduce these institutions without endowing them with appropriate competences.

through much closer cooperation, for example the processing of visa applications to the Schengen zone. Currently, Schengen visas are processed and delivered independently by all the member states of the Schengen area. This is hardly a cost-effective method.

It is time for the EU to learn from experience and rethink its role in foreign policy. We propose three practical steps:

- *Well thought-out initiatives to strengthen the European soft power*. Culture, media, education and science are fields where European preferences are largely unified. The challenge is to overcome traditional fragmentation along linguistic and national lines (or their combination). As in the industrial field, this requires an entrepreneurial approach to the corresponding challenges;
- *Savings-oriented back-office cooperation.* Significant savings can be achieved by mutualising non-policy and back-office functions such as the processing of visa applications to the Schengen zone, or by organising structured cooperation amongst national foreign ministries.
- *Regular European Foreign Policy White Books.* The creation of the role of the High Representative of the Union for Foreign Affairs and Security Policy has been positive but he or she can only be effective when key member states share common objectives. This policy will only be effective if the member states have ownership of the EU's foreign policy while at the same time aligning their efforts closely. One important step towards this end would be to introduce a much more extensive common assessment and analysis of foreign policy objectives and threats. This could be achieved through the introduction of a regular (possibly yearly) report (EU Foreign Policy White Book) coordinated by the EU High Representative for Foreign Policy but prepared with strong participation of the member states.

viii) Military procurement and defence

Defence is by essence a public good, at least as far as major threats are concerned. Military procurement is also an area where potential benefits from more provision at the European level are particularly large. There are three reasons for this. First, the cost of defence programmes is escalating. Second, the response to multifaceted threats implies higher investment. Third, it has been pointed out by a number of studies[1] that the cost of military procurement and the effectiveness of the armed forces in Europe could be improved considerably through a more integrated defence industry and more coordinated or joint procurement. A reduced number of weapon systems would also increase the ability of the national armed forces to cooperate.

The European NATO members jointly spent $264bn on defence in 2018. This is 40% of the US defence budget but seven times the estimated cost to the US of defending Europe. This is also significantly more than the estimated defence budgets of China ($168bn) and Russia ($63bn).[2] However, fragmentation and inefficiency prevent Europe from being the effective defence player it could be.

As long as procurement decisions are taken at the national level, many countries will take decisions which may be rational from a national perspective but not from that of Europe as a whole. For instance, many national governments will place great weight on buying equipment from national suppliers rather than suppliers from other European countries because this will preserve an industrial capacity for defence and protect jobs. To achieve these aims, they will be ready to accept lower quality or significantly higher production costs.[3] From a European perspective, and ultimately also from a national one, this is clearly irrational.

More European coordination in procurement does not necessarily imply that defence policy is also shifted to the European level. Progress towards an integrated defence industry can be made even if defence structures remain separate and defence policies uncoordinated. But both aspects are to some extent linked, because procurement requirements reflect defence priorities. This raises the question of a European defence policy.

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[1] See e.g. Witney (2008), Bertelsmann Foundation (2013), case study 3.

[2] See International Institute for Strategic Study (2019)

[3] In some cases like Eurofighter or Tornado combat planes member states already cooperate in procurement, even if this cooperation often reflects costly and overly rigid compromises between national interests of the participating countries.

Today defence policy is a national competence. Shifting it to the European level would offer significant advantages in terms of size and leverage but clearly, preference heterogeneity is a factor which stands in the way of such a step. Views in the population of different member states about how defence policy should be conducted, under which circumstances military interventions are justified and where they should or should not take place, are divided. Defence spending levels vary widely and despite US pressure there is no sign of convergence, including between France and Germany. Since it is a key element of national sovereignty, shifting defence policy to the European level would furthermore raise difficult questions including that of democratic control.

At the same time, it should be taken into account that most EU member states increasingly face the choice between a shared sovereignty in defence policy and no sovereignty at all. Today even the larger member states have limited military power and their role is so inferior to that of the US or even Russia that their much-cherished national sovereignty faces severe limitations. Operationally, their armies are often dependent on the US for information, communications or logistics, which reduces their autonomy and gives Washington considerable leverage. This could be regarded as inconsequential as long as European and US security priorities coincided and the US was willing to take charge of protecting Europe. However, even before the Trump administration took office, growing signs of US impatience with what is perceived as European free-riding indicated that times were changing. It is by now clear that European countries cannot rely on the US the same way they have been used to.

From an efficiency standpoint, a common European defence policy would have the potential to transform the EU into a global military power, second only to the US. Whether complete autonomy from the US is ultimately necessary or even desirable is controversial amongst member states. But it is much less controversial that reducing vulnerability and dependence on the US would be desirable for Europe. This can only be achieved in the form of pooled sovereignty.

In recent years the EU member states have taken steps towards more cooperation in defence policies, but they have had limited effect at best. The EU has created the EU Global Strategy for Foreign and Security Policy (EUGS). This strategy includes the Permanent Structured Cooperation on security and defence (PESCO). Essentially PESCO is a framework for organising cooperation in defence within the EU framework. So far 25 member states have agreed to participate in PESCO. However, decisions are taken unanimously, and most of the potential advantages of a defence policy at the European level cannot be reached through PESCO, at least with its current structure.

In view of persistent differences as regards the perception of threats, decision-making procedures and the willingness to embark on overseas operations, a way forward for European defence is variable geometry – especially as the UK is a major player in that field that should remain part of the coordination of defence efforts. Smaller club-like structures such as the 10-members European Defence Initiative have emerged, but so far with limited means and ambitions.

The upshot is that progress should be made towards common procurement, shared infrastructures, common arms export policies and joint defence initiatives simultaneously. They do not need to advance at the same pace nor in the same format: cooperation on procurement can involve a wider ring of partner countries and it can also move faster than whatever has to do with the use of military force. Shared infrastructures also do not imply joint initiatives. But the development of European defence cannot be disjointed. It should be regarded as a system.

5. An action agenda

i) When: Opportunities for decision

There are not many opportunities to launch an initiative as ambitious as that of extending the provision of public goods at the European level. In principle, it could be a matter for a new Intergovernmental Conference tasked with a significant revision of the EU Treaties. But there are too little appetite for sweeping treaty change and too many divisions within the EU for this route to be considered in the short term. Furthermore, political discussions on the aim of the redefinition of the EU mandate should precede legal amendments.

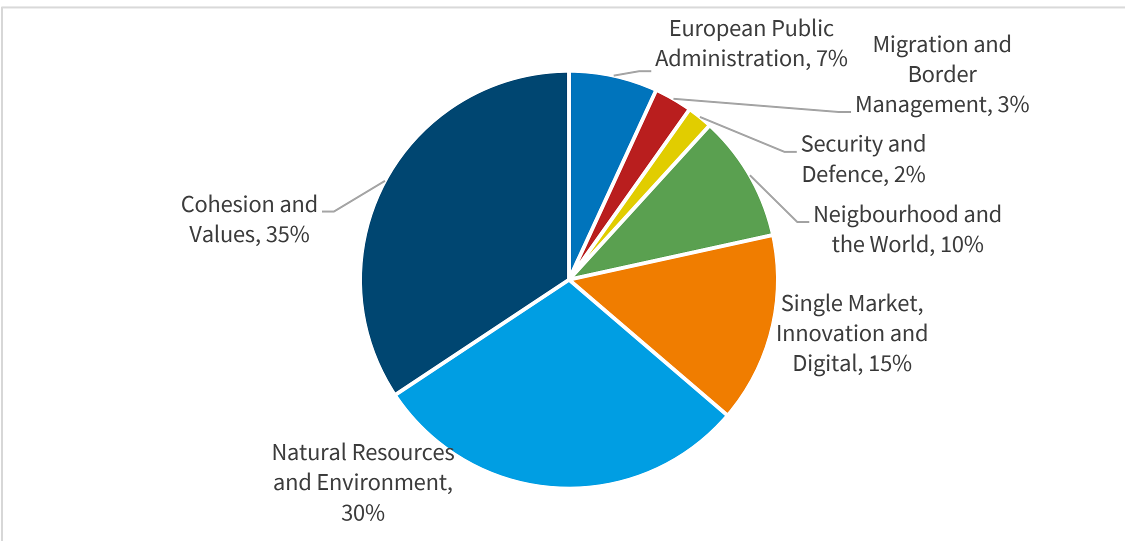
An opportunity for a political discussion has largely been missed: the European Elections. True, European added value and common policies featured in the debates between the *Spitzenkandidaten*, while the surge in voters participation and the emergence of cross-national themes such as climate change, immigration and terrorism signalled a departure from the usually (and paradoxically) very national character of European elections. However, it would be excessive to claim that the new Commission has received an unequivocal mandate to develop and implement a European public goods agenda.

Another current opportunity is the negotiation of the Multiannual Financial Framework for the years 2021-2027. The European Commission submitted its proposal last year (European Commission, 2018c). It emphasizes that it is "vital that it invests in areas where the Union can offer real European added value to public spending at national level."[1] European public goods do play a growing role in this budget. But overall spending is still dominated by spending on agriculture and regional policies. These spending items have a strong distributional character (see Figure 2) even though they include aspects of European public goods related to food security, environmental protection and EU-wide

[1] European Commission (2018), p. 3.

benefits of economic convergence. Spending on key public goods like migration and border management or security and defence is still a very small share of the budget.

Figure 2: Allocation of budgetary expenditures in the European Commission proposal for the 2021-2027 MFF



The ongoing negotiations about the MFF should be used to extend the role of public goods provision. However, in these negotiations each country generally focuses on its net contribution to the EU budget, rather than the value added of the common budget for the EU as a whole. Furthermore, the negotiations are fairly advanced, so that room for changes is probably limited, in particular because consensus would be needed among all member states. The uncertainty about Brexit further complicates the negotiations.

No time should be lost, however. The challenges Europe is confronted with are pressing, and an EU that is not able to redefine the European public goods, to set priorities, and to fund action in key area, would take the risk of being (rightly) regarded by citizens as dangerously ineffective, possibly even growingly irrelevant.

We are not offering here a new version of the "bicycle theory", according to which there is no possible European steady state until the EU reaches fully-fledged integration. What we are claiming is different: namely that external conditions have changed, that the global economic and geopolitical balance has changed, that threats to Europe's security and prosperity have changed, that policy priorities have changed, and that responses to these changes are urgently required.

An opportunity for setting the agenda could be provided by the "Conference on the future of Europe" announced by the incoming Commission president, Ursula von der Leyen, in her opening speech of 16 July to the European parliament. It would have the advantage of involving the citizens in the definition of European priorities.

The policy initiatives that this report is calling for cannot wait until the 2028-2035 financial perspectives start being discussed. They cannot even wait until the next European Parliament elections in 2024.

ii) Who: The governance of European public goods provision

Economies of scale and spillovers are strong arguments for collective action. In their presence, the full shifting of responsibilities for the provision of certain public goods to the European level has a number of advantages which are sometimes underestimated. First, free riding and other types of strategic behaviour of individual member states are avoided. Second, a greater coherence of the policies in question can be achieved. Third, cost savings through the use of economies of scale are more easily realized. But this is only true if policy responsibility is reassigned in full and if overlaps are avoided. For instance, the build-up of a common border protection system has the potential to greatly reduce the overall costs of border protection, but such gains can only be reaped if the member states reduce the resources they put into their own border police. As long as national and European activities are combined, there is a danger that costs actually increase.

An alternative to delegating policies and instruments to the European level is to coordinate them amongst states. If delegated, they can be governed through the Community method (giving the Commission and the Parliament prominent roles, as well as resorting to qualified majority voting for decisions) or through the intergovernmental method (with a prominent role for the Council, and possibly unanimity rule). But the accommodation of heterogeneous preferences has always to be weighed against the cost of duplication and overlaps.

Policies reviewed in the previous section differ considerably in this regard. Some such as foreign economic relations belong to core EU competences and can only be governed through the Community method. Some, like climate change mitigation or research and development, belong to shared competences where the EU intervenes alongside national (and possibly subnational) governments. At the other end of the spectrum some, like defence, belong to national competences, with a very limited role for the EU, if any.

In view of such current conditions, any attempt to define a unified governance regime for the provision of European public goods would be mistaken. The diversity of situations is here to stay, if only because the legal, political and operational bases for action differ.

By the same token, however, it would be wrong to assume that ad-hoc cooperation can overcome pervasive obstacles to effective collective action. In all the domains we have reviewed, attempts to coordinate national initiatives have been made. They have reached their limits for a variety of reasons ranging from bureaucratic vested interest to the free-riding temptation and from the heterogeneity of preferences to reactions to perceived encroachments to national sovereignty. Advancing the provision of European public goods requires governance reform.

iii) What geometry: The whole EU or subgroups of countries?

A key question for any initiative to extend the provision of public goods at the European level would be whether to start at the EU level or with a subgroup of countries, a 'coalition of the willing'. Starting with a subgroup of countries has significant advantages. The most important advantage is that it will be much easier to agree on objectives, on measures to develop and on ways to fund new European public goods.

But there are also drawbacks. To start with, size advantages and the internalisation of spillovers will depend on the number and size of participating countries. Moreover, and most importantly, if a subgroup of countries engages in providing European public goods of the type which generates benefits even for countries who do not participate, the likelihood that these 'outsiders' will join later may be small. If the public good is already provided for free, joining the initiative entails costs for the outsiders but few additional advantages.

This suggests that variable-geometry solutions, i.e. public goods provision by a subgroup of countries should focus on areas where few benefits to non-participating countries arise and where spillovers to or from these countries play a minor role, or where mechanisms can be put in place that limit benefits to non-participating countries. Evidently, this is very hard in certain domains such as security or climate change. But even in such fields, thoughts should be given to ways to ensure fairness and to avoid free-riding. For example, countries not participating in a defence effort can be excluded from military procurement and countries not participating on a sufficient scale in a climate change mitigation effort can be excluded from accessing certain schemes such as dedicated credits and subsidies. A "club" approach of this sort should not be seen as aiming at the exclusion of some member states, rather as a way to ensure that the benefits of joint action primarily accrue to those taking par in it.

For differentiated integration not to create roadblocks to EU solutions, it must also remain based on the EU system and be consistent both with its principles and its governance. Dedicated clubs can be the way forward if they preserve the backbone of the EU, remain open to all EU members who are willing to join and fulfil explicit criteria, and remain part of the legal and institutional system of the Union (Demertzis et al, 2018). This is the way that has been followed historically, to some avail.

EU treaties provide a mechanism - for "enhanced cooperation" amongst a subgroup of member states (Art. 20 TEU and Arts. 326-334 TFEU), but experience with it is disappointing: in part because of the safeguards that it involves, it has not provided the conduit for flexibility it was intended to be. By contrast, project-based cooperation (for industrial or innovation initiatives) or cooperation within the framework of specific treaties (as with the European Stability Mechanism) have proved more fruitful. Especially, the ESM provides an interesting template as it is both governed by a specific treaty and considered part of the EU legal framework, and as such falls within the scope of the European Court of Justice.[1]

iv) How: The funding of European public goods

If the EU takes over a more important role the question arises as to how the provision of these goods should be financed. The overall tax burden for EU citizens should not increase and it should even decline if it is true that certain public goods are more efficiently provided at European than a national level. But more resources would need to be shifted to the EU budget.

How could this be achieved? Currently the EU budget is funded by the so-called 'own resources' of the EU. De facto the most important source of revenue is made of contributions paid by the member states. These member states set a ceiling for the EU budget, and the difference between EU own resources (revenues from customs tariffs and other revenues flowing directly into the EU budget) is covered by contributions from the member states. For this purpose the contribution key is based on gross national income

[1] See the ECJ judgment of 27 November 2012 on the Pringle case.

(GNI).[1] Several corrections are finally applied to avoid to high an imbalance between contributions to, and benefits from the EU budget.

The simplest way of financing more European public goods provision would therefore be to extend the budget ceiling and to let each member state pay more in proportion of its GNI. Would this be satisfactory? It is natural to think that European public goods provision should be financed via European taxes. Accordingly, supporters of this view argue that European institutions, in particular the European Parliament, should take responsibility not only for spending but also for taxation.

For a mature EU whose role includes the provision of several public goods, such an evolution would make considerable sense. However, introducing a right to tax at Union level would require a fundamental change in the institutional architecture of the EU, essentially transforming it into a federal state with a fiscally sovereign central government. Irrespective of whether such a reform would ever find political support, it would take a lot of time. More European public goods provision is urgent and should not depend on a reform of the EU as a whole which is likely to face formidable resistance.

There is an ongoing debate about a much less radical reform of the EU's financing system. This debate focuses on a reform of the existing system of own resources which preserves its fundamental features but aims at reducing the current dependence of the EU on GNI based contributions.[2] New own resources that would still require unanimous adoption by the member states but unlike the contributions, they would not be attributable to individual member countries. Examples include the introduction of a European financial transaction tax or new environmental taxes like a tax on intra EU flights. It has also been proposed to use the profits of the ECB to fund the EU budget.[3]

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[1] GNI is the new name of GNP. Unlike GDP which is based on domestic value added, it takes into account income from factors employed abroad.

[2] See High Level Group on Own Resources (2016).

[3] ECB profits are currently distributed to the national central banks, which in turn distribute their profits to their shareholders, the national treasuries.

While it may or may not be useful to introduce new types of taxes in Europe, using them to fund the EU budget under the current institutional setup is unlikely to improve democratic accountability. This is due to the ceiling on the budget and the fact that GNI-based contributions are the residual source of finance which mechanically fill the gap between revenue from other own resources like tariffs, for instance, and the budget ceiling. As long as this setup is preserved, the introduction of new own resources would merely reduce the share of the GNI contribution in the EU budget, and vice versa. Because the marginal resource remains the GNI-based contributions, the financial consequences of any EU decision on changes in own resources would thus be borne at the national level.

We therefore propose to disconnect the provision of new European public goods from the reform of EU finances and, therefore, to fund the corresponding spending increase through higher GNI-based resources in the EU budget. This has three advantages:

- First, this approach would avoid the already complicated debate on the level and nature of European public goods being hijacked by the debate on the financing of the EU budget; while it is natural that growing policy responsibilities at the EU level raise the question of growing responsibilities on the financing side as well, it seems problematic to burden the initiative to provide more public goods at the European level, which has some urgency, with the project of introducing EU taxing rights or changing the existing financing system;
- Second, more European public goods provision will reduce the cost of providing these goods at the national level. This implies that there should be room in the national budgets to increase GNI contributions;
- Third, if European public goods provision will start with a subgroup of countries, contributions from these countries based on GNI or a similar key are the only realistic source of finance. Once these initiatives are integrated into the framework of the EU, a discussion of other funding sources may follow.

6. Flagship Franco-German projects

Joint initiatives by France and Germany have often been successful in bringing about innovative EU projects. Agreement between the two governments is often long to reach, because the policy philosophies of the two countries differ, and this is precisely why common projects have the potential to be supported by many more countries. However, even with such an initiative, finding EU-wide agreement on extending European public goods provision is likely to be difficult and take time. This raises the question of whether France and Germany could foster and complement European public goods provision through bilateral initiatives. It is important to state that these initiatives should not aim at permanent bilateral action - they would be open for other countries to join in and indeed contribute right from the start. We propose that France and Germany undertake to start the following bilateral projects:

i) A common agency and a common research institute for cybersecurity

As explained in section 4 iii) cybersecurity is an area with significant border crossing implications and economies of scale. But cooperation in this field requires considerable trust among the participants, which is an obstacle to an EU-27 initiative.

The advantages of joint action in this area are likely to be significant even if only two large countries intensify their cooperation. France and Germany should do so by creating a common agency for cybersecurity and by setting up a joint research institute for cybersecurity.

ii) A common fund for supporting breakthrough innovation

As indicated, the difficulty with the financing of breakthrough innovation is that it requires a strict selection of projects on the sole basis of their potential, and an unwavering and credible commitment to terminate projects that do not deliver enough. Such principles may entail adverse distributional consequences, both ex ante (depending on the innovativeness of national entrepreneurs) and ex post (for the firms involved and for employment). This is what makes such an endeavour hard to implement at EU level.

We therefore propose that France, Germany and other countries willing to uphold the same principles create a joint fund for breakthrough innovation. Once operational this fund could enlarge its membership.

iii) A joint defence initiative with the objective to build up joint armed forces and to introduce uniform arms systems.

For the reasons explained in section 4 vi), defence and military procurement is a key area of European public goods provision where potential efficiency gains are large. There are cooperation projects in this area between France and Germany, examples being the Franco-German Brigade and the Eurocorps, where other European countries are also involved. France and Germany should extend this cooperation in both the setting up of joint military units and military procurement. In particular there should be an ambitious objective and time schedule for the introduction of joint and uniform arms systems. Obviously, this schedule should be coherent with the gradual build-up of the German military spending effort.

iv) A joint strategy for economic development and cooperation in Africa

A joint strategy for economic development and cooperation in Africa would have a number of advantages. Although relations between France and many African countries are much closer than those to Germany, a diminishing economic weight and resource constraints have reduced its influence. Their combined weight would matter much more. Economic development and cooperation is linked to many issues including migration as well as the geopolitical implications of Chinese expansion in Africa.

In all of these areas European interests would be represented better through joint policies of France and Germany. Naturally, they should involve other member states whose history or location results in a strong interest for African matters.

v) A Franco-German chair at the IMF

France and Germany should consider merging their participation at the IMF. A joint participation of the Eurozone at the whole has been debated for some time but not been implemented. It would raise complex issues of redesign of the constituencies. If France and Germany took the initiative it is likely that other countries would join in. One may object that France and Germany often have different views on IMF matters. A merger of the French and German chairs would therefore require adequate preparation as regards both substance and governance. But there would be significant advantages in discussing policy differences between France, Germany and potentially other Eurozone member states and finding a common position which would then have significant weight at the IMF.

It should be emphasized that it is important to design these Franco-German initiatives in such a way that other member states do not perceive these as excluding others or as a claim of France and Germany to leadership, but rather as a pathbreaking initiative and as an opportunity to build a larger coalition of member states determined to bring forward European public goods provision.

7. Conclusions

In this paper we have made the case for extending the role of the EU in public goods provision. We see this as a major agenda for Europe in the years ahead. Currently the backbone of the Union consists in trade policy, the internal market, monetary integration as well as agricultural and regional policies. European public goods are part of the European policy agenda, but they are underdeveloped. The EU budget is small, and a large part of the available resources is spent on redistributive policies. This set-up is increasingly inadequate in the new European and global context where multilateralism is under pressure. By the same token, the potential for enhancing economic prosperity and security in Europe through the provision of genuinely European public goods is significant.

There are legitimate concerns about the loss of national sovereignty, and we do not question that decentralisation and subsidiarity are important. But in today's world, in several policy areas the choice is between European sovereignty and no sovereignty at all. Enhancing European public goods provision is not about an across the board extension of European policy competencies. In areas where EU involvement creates no, or little added value, renationalisation should be no taboo. European public goods provision is about developing EU policies in areas where this reduces costs and increases effectiveness.

We do not underestimate the roadblocks ahead. Beyond the overall inertia that has set in, reluctance to transferring new competences to the EU level, resource constraints and divergent priorities can easily block the transformation we are calling for. Opposition will have to be overcome, most probably through a differentiated integration process. Coalitions of the willing can unlock the potential for developing European public goods, provided they are rooted in the EU system, avoid creating incentives to free-riding and remain open to new participants.

The scope of this paper has only allowed us to sketch in a rather broad manner ways in which the role of the EU or of subgroups of member states should extend their role in the provision of public goods. Before this can be put in practice much more work will have to be done, based on deep expertise in each individual policy area. It is nevertheless urgent to start the process.

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