SEIZING AN UNPARALLELED OPPORTUNITY TO MEET THE EU STRATEGIC OBJECTIVES

The Case for Cities' Increased Direct Access to EU Funding

Authors:
Zoltán Gyévai
Benedek Jávor

Edited by:
Bulcsú Hunyadi
Ioana Zamfir

June 2023

POLITICAL CAPITAL
POLICY RESEARCH & CONSULTING INSTITUTE

Political Capital is an independent, Budapest-based political research and consultancy institute founded in 2001. We are committed to the core values of the European Union, and we owe no allegiance to any government or political body. Our mission is to achieve social change by increasing the understanding of politics and promoting public discourse and policy-making based on knowledge, evidence, and critical thinking. The institute's main fields of interest include malign foreign influence and disinformation, radicalisation and extremism, the state of democracy, and EU relations. We have developed an extended network of professional partners, both domestically and internationally, all of whom have helped our institute to become one of the most influential think tanks in Central and Eastern Europe.

The current study was kindly supported by the Open Society Foundations.

The authors:

Benedek Jávor is a Hungarian environmentalist who holds a PhD in biology. From 2014 to 2019, he was a Member of the European Parliament, and since 2020, he has been the Head of the Representation of Budapest to the EU. Besides being a founding member of the Dialogue for Hungary party, he is also a founding member of the environmental NGO Védegylet (Protect the Future!). He is the author of several articles and publications on environmental threats, 'going green', and the future of the Earth.

Zoltán Gyévai is a Hungarian journalist who has been the Brussels correspondent of various Hungarian media outlets for 25 years, lately that of Radio Free Europe / Radio Liberty's Hungarian service. He is the founder and editor-in-chief of BruxInfo, a former Brussels-based EU news portal.

CONTENTS

EXECUTIVE SUMMARY AND RECOMMENDATIONS

Political Capital's novel research addresses European cities' access to financial resources under direct-management from the European Union (EU) budget and emphasizes cities' role as key actors in achieving the EU's common climate, digital, social or health objectives. The research tackles the issues of whether the EU subsidies in their current distribution system, form and amount can effectively serve the crisis management that cities face and their ability to meet the European strategic goals—notably in the context of the crises that have hit the EU in the past couple of years. The current study concludes that such is the case only to a limited extent, hence why cities deserve the EU's special attention and protection against restrictive measures by national governments in the spirit of EU principles such as subsidiarity, partnership or political non-discrimination. We argue that meeting cities' special financing needs is politically justified, legally possible, and even additional funds could be made available.

Findings

- **Cities need more support.** Cities are the strongholds of European democracy and the principle of subsidiarity. According to **a recent Eurocities survey, over half of EU mayors surveyed think that EU institutions and policies do not or not sufficiently take into account cities' specific needs and potential**. Also, mayors feel that the EU support is insufficient compared to the challenges they face. Moreover, many mayors think that EU funding schemes were more helpful in the form of direct support or if local needs were taken more into account. Cities were in the forefront to cope with recent challenges in the EU such as COVID and the inflow if Ukrainian refugees.

- **The resources available for cities are quite fragmented.** Applying for them is a serious administrative challenge for local authorities and with a few exceptions, they can provide cities with access to smaller amounts of support. The vast majority (four-fifths) of funding programs available for cities are managed under shared management (by the European Commission and national authorities jointly), and only one-fifth are handled directly by the European Commission(direct management). *(For the detailed list of funding for cities, see the Annex.)*

- **EU Cohesion Policy in need of reform.** The coronavirus pandemic and the war in Ukraine have demonstrated the limits of the EU's rapid and effective response to immediate crises. While greater centralization has occurred under the EU's Recovery and Resilience Facility (RRF), a short-term crisis management tool, its shortcomings have also appeared as inequalities within the EU have amplified. To prove its viability and avoid competition with other alternatives and budget cuts, the Cohesion Policy must undergo structural changes after 2027.

- **More direct funding is desirable – not only for cities but also for civil society organizations.** It represents a contribution to achieving the EU's ambitious strategic goals in terms of climate, digital, and social policies, to the costs of integrating refugees and legal migrants, and to strategic autonomy. Furthermore, direct funding represents an instrument to enforce the rule of law against political discrimination, especially in the context of a union-wide need for a decentralized Cohesion Policy.
- **Increasing national centralization: According to the Eurocities survey mentioned above, mayors see a worrying centralization trend in EU funds. Moreover, Eastern European mayors report that national governments use EU funds as a political weapon against opposition mayors.**
- Hand in hand with the recent crises has come a stronger desire for Member States (MSs) to centralize resources. In the political conflict between the Hungarian government and the capital, Budapest's unique position reflects the way in which European funds can be utilized as a means of political punishment to divert funds away from cities that are not politically aligned with the incumbent government. **Cities subject to restrictive government measures left out of the consulting process and recipients of minimal shares of the shared management funds run the risk of undermining common EU goals as they are financially obstructed.**
- **Legal, political and technical hurdles hamper EU direct management funding expansion.** The legal hurdle concerns the challenges pertaining to changing the legislation in favor of increasing direct-management funding from its current one fifth of the EU budget. The political hurdle encompasses the conflicts of interests that exist between MSs, between MSs and EU institutions, and between national, municipal and regional actors. Lastly, the technical hurdle regards the present lack of human and administrative resources at the EU level to commit to greater direct-management.
- **While the existing resources are quite fragmented, more sources of funding are potentially available.** Possible new avenues include: an increase in the European Regional and Development Fund (ERDF) budget for sustainable urban development from the current 8 percent to around 10 percent; an increase in the European Urban

Initiative (EUI) budget from the present EUR 500 million available now; a restructuring of the Cohesion Policy to include more direct funding; making use of the MFF as a guarantee to provide loans to cities where necessary; and returning money stuck in non-approved Recovery and Resilience Plans (RRPs) or not booked or used by MSs to an EU pool that would redistribute it on a direct management basis to final beneficiaries.

- **Flexibility as the core of the EU's resilience.** The review of the Multiannual Financial Framework (MFF) will center around the EU's ability to support Ukraine and to ensure and enhance its strategic autonomy. While no major budget increases or substantial modifications of the current financing model can be expected, greater flexibility should be given to MSs to respond more quickly and effectively to new emerging challenges difficult to predict. Moreover, placing the earmarked amount under direct or semi-direct management would prevent discrimination based on political grounds, ensure recipients are directly accountable to the Commission, involve the Commission in a way that does not cause an administrative burden, and safeguard the MSs' commitment to the EU strategic goals.
- **The mid-term MFF review remains an unmissable opportunity.** While no major revisions can be expected to ensue following the review and given the limited timeframe of the whole process, cities should emphasize the cost of receiving Ukrainian refugees and their role in industrial development as a rationalization for increased direct funding. The mid-term review further represents a key moment for cities to prepare the ground for the future Cohesion Policy after 2027.

Recommendations

In our study, we have identified several possible solutions to increase the financial resources available for cities. They are the following:

Short-term opportunities

- **Use the MFF mid-term review as an opportunity** for cities to argue for more direct funding and prepare the ground for the future Cohesion Policy after 2027.
- **Increase cities' role in the RFF and its REPowerEU-related programs** and require MSs to improve cities' inclusion in the RRF programming and implementation process, and widen cities' access to these sources.

- **Regroup Cohesion Policy funds** irrecoverably lost for the MSs' governments due to the rule of law conditionality mechanism **to projects serving sustainable urban development in a direct funding scheme**.
- **Top up the Horizon Europe '100 Climate-neutral and Smart Cities by 2030' program** by an additional €3-500 million to finance climate neutrality efforts of cities within the framework of the yearly EU budget debates.
- **Return money** stuck in non-approved Recovery and Resilience Plans (RRPs), not booked or used by MSs **to an EU pool and make it available for final beneficiaries of the respective country on a direct management basis** to boost economic and social recovery at the local level. However, this would require an amendment to the RRF rules, which is quite unlikely to happen by 2026.

Long-term opportunities

- **Increase in the European Regional and Development Fund (ERDF) budget the proportion that must be devoted to sustainable urban development** from the current 8 percent to around 10 percent. Place the earmarked amount under direct or semi-direct management to prevent discrimination on political grounds. The purpose would be for the recipients of funds to be directly accountable to the European Commission.
- **Increase the budget of the already directly managed European Urban Initiative (EUI)** from EUR 500 million available now. An enhanced EUI could become the core of a special fund to support cities in reaching their climate and other objectives related to sustainability.
- **Create multi-country projects dedicated to energy transition and decarbonization within the future Strategic Technologies for Europe Platform (STEP)**, considering cities' critical role in industrial development.
- **Include in the country-specific recommendations (CSRs)**, within the European Semester, **a golden rule for cities' long-term investment needs**. Doing so would allow cities to borrow from capital markets. Moreover, **the MFF could be utilized as a guarantee to provide loans to cities where necessary**.
- **Let NGOs distribute part of the funds** along the lines of the European Economic Area (EEA) and Norway Grants, in which part of the resources are managed not by the beneficiary state but by civil society organizations.

- **Redefine the principle of excellence** in research and innovation-related programs and **adapt it to local needs**.
- **Reconsider the support system affecting cities according to the principle of efficiency.** The extension of existing direct management financing can play a useful role in this, through the completion of existing funds or the creation of new ones focused on special needs. This can be especially useful in countries where political discrimination afflicts large cities led by the opposition thus imperiling the achievement of favorable changes at the local and EU level.

1. INTRODUCTION

Cities not only contribute to a country's wealth and gross domestic product, but also face economic, social, environmental and climate challenges cumulatively and play a key role in their management. Achieving the European Union's climate neutrality goal, for example, is impossible without a sustainable reduction of greenhouse gas emissions in metropolitan areas. The costs of integrating refugees and migrants are also borne mostly by cities, an issue that has raised in importance with the reception of millions of Ukrainians fleeing the war.

In an own-initiative report adopted by the European Parliament in 2021 on the challenges for urban areas in the post-COVID-era, the rapporteur, Katalin Cseh, member of the Renew group, stresses that the commitment from urban areas is crucial for the transition to a climate-neutral society and to a prosperous, fair, sustainable and competitive economy.[1] She further emphasizes that urban authorities must have direct access to EU funding in the future.

At the same time, the resources from the EU budget specifically intended to meet the needs of cities are dwarfed by the real needs. According to estimations of the '100 climate neutral cities mission', the decarbonization costs of a city is around EUR 10.000 /inhabitant in the EU.[2] Thus, EUR 17 billion only for Budapest.

The Cohesion Policy is the largest source of funding to support job creation, business competitiveness, economic growth, sustainable development, and improve citizens' quality of life. It does so in inverse proportion to the level of development: the more developed a statistical region is compared to the EU average, the less financial support it can expect from the EU budget. In the EU, certain resources accessible to cities have been created over time, but according to general opinion[3], their volume falls significantly short of what is desirable, and also of what is possible in reality to obtain.

There are already signs of a change in attitude, however, considering the EU's legal status quo, the territorial characteristics of the MSs and conflicts of interest, present union-wide and nationally, make it very difficult to implement any changes that would enable the restructuring of resources.

There has been a long-standing debate within the EU about the necessary and desirable degree of decentralization. The series of crises of recent years, the economic consequences

[1] https://www.europarl.europa.eu/doceo/document/A-9-2021-0352_EN.html
[2] https://op.europa.eu/en/publication-detail/-/publication/bc7e46c2-fed6-11ea-b44f-01aa75ed71a1/language-en/format-PDF/source-160480388
[3] https://monitor.eurocities.eu/wp-content/uploads/2023/06/Eurocities-Pulse-FINAL.pdf

of the coronavirus pandemic, the energy crisis and the war in Ukraine have led MSs toward even greater centralization. The corona crisis fund alias the Next Generation EU (NGEU), and within it the Recovery and Resilience Facility (RRF), which entrusted the use of the recovery funds to the governments, with only a soft condition that they consult with the lower levels, reflected the stronger monopoly of national authorities on the finances received. Several studies on the subject have confirmed that MSs have largely ignored this expectation and had hardly, or not at all, consulted with the local levels about the use of resources.[4]

The picture is even bleaker in countries where governments have used the health emergency as an excuse to excessively concentrate power and distribute EU funds according to their political interests and sympathies, often discriminating against towns and cities under opposition control. One glaring example of this is the situation in the Hungarian capital Budapest, to which this study devotes a separate subchapter.

The following chapter, based on interviews with a number of stakeholders[5], concludes that, given the challenges facing the EU, the special situation of urban and metropolitan areas and the interests of their population, expanding cities' direct access to EU funds is not only possible, but also necessary, and it is arguably a good investment from a political point of view as well. Given their size, the high concentration of the population and the numerous challenges they face, cities play an eminent role in upholding democracy and democratic values. "Talking about cities means talking about democracies" - says Catherine Fieschi, director policy and strategic outreach at Open Society Foundations.

The purpose of this study is not to examine the challenges of possible legislative amendments. However, it can be said that the transition to direct management would require, among other things, the amendment of the Multiannual Financial Framework (MFF) and the Common Provisions Regulation (CPR). Overall, in addition to listing the arguments for and against direct financing, we also outline several possible solutions. Moreover, in the Annex, we have mapped in detail the resources available from the EU budget to cities and local governments between 2021 and 2027, where possible, outlining the number of available resources and the main criteria for applications.

---

[4] https://eurocities.eu/wp-content/uploads/2021/10/Eurocities_Briefing2_NRRPs.pdf

[5] Altogether, we have conducted 14 interviews for the study with the following subjects: a political scientist focusing on the EU Cohesion Policy, three journalists dealing with EU topics, two deputy mayors of big urban centers, two high-level municipality officials, an expert of a European city network, three mid and high-level officials of the European Commission, a scientific assistant of an MEP and an MEP, all dealing with the topic in question. Moreover, we collected important feedback, which were incorporated in the final version of this study, at the closed-door roundtable discussions with invited experts, decision makers and journalists, held in June 2023 in Budapest and Brussels.

2. STATE OF PLAY: DIRECTLY AVAILABLE EU SOURCES FOR CITIES AND LOCAL GOVERNMENTS

Around 70% of the EU's budget is managed in 'shared management', with MSs distributing the funds.[6] Some 20% of the budget is still directly managed by the European Commission (EC) and its agencies. The majority of the EU budget allocated to humanitarian aid and international development (around 10% of the EU budget) is implemented under indirect management. Thus, direct funding is not something new or unprecedented in the EU.

In direct management, the EC is directly responsible for all steps in a program's implementation:

- launching the calls for proposals
- evaluating submitted proposals
- signing grant agreements
- monitoring project implementation
- assessing the results
- making payments

These tasks are carried out by the Commission's departments, at its headquarters, in the EU delegations or through EU executive agencies.

There are many programs run directly by the Commission. These include, for example, the program for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME), the European External Action Service (EEAS) Development Cooperation, and the European Urban Initiative (EUI). Around 12% (EUR 376 million) of the Asylum, Integration and Migration Fund (AMIF) is distributed for annual work programs through direct management.[7]

---

[6] https://commission.europa.eu/funding-tenders/find-funding/funding-management-mode_en#:~:text=Three%20management%20types,-All%20the%20programmes&text=direct%20management%3A%20EU%20funding%20is,inside%20or%20outside%20the%20EU

[7] Such was the case for the 2014 to 2020 period, while the 2021-2027 one builds on the previous period to support local and regional authorities, though without specifying a clear share of the fund allocated to direct management. See for the 2014-2021 period, https://home-affairs.ec.europa.eu/funding/asylum-migration-and-integration-funds/asylum-migration-and-integration-fund-2014-2020_en; see for the 2021-2027 period, https://home-affairs.ec.europa.eu/funding/asylum-migration-and-integration-funds/asylum-migration-and-integration-fund-2021-2027_en.

Former pre-accession funds (former PHARE, SAPARD, ISPA) were also run under direct or semi-direct management.[8]

Looking into the EU budget we have found at least twenty-five programs and funds funded by the EU that are 'in principle' available for cities and other local actors (see more in the Annex). Although the entire amount available from various programs cannot be calculated, we are not far from the reality if we estimate the level of EU subsidies available to cities at several billion euros. This estimate does not include funds available from Cohesion Policy sources, which are much greater, but are distributed under shared management.

According to the EC, some EUR 115 billion from the Cohesion Policy funds were invested in cities during 2014-2020.[9] Of these, EUR 17 billion were implemented locally through more than 980 sustainable urban development strategies managed directly by urban authorities.[10] In parallel with these significant urban investments, the Urban Innovative Actions (UIA) initiative provided direct support for cities to experiment with innovative solutions.

The table we prepared (see in the Annex) shows that there are already many EU programs running under the direct control of the EC and for which cities and local authorities can apply independently or as a joint project. Among these programs most notable are the European Urban Initiative (EUI) with a budget of EUR 500 million between 2021 and 2027; URBACT IV with a grant of nearly EUR 80 million; the Circular Cities and Regions Initiative (CCRI) with a budget of EUR 58 million; EU4Health with a budget of EUR 5.3 billion; and European Local Energy Assistance (ELENA), which finances energy efficiency and renewable energy investments above EUR 30 million.

---

[8] PHARE is the Poland and Hungary Assistance for the Restructuring of the Economy, SAPARD is the Special Accession Program for Agricultural and Rural Development, and ISPA is the Instrument for Structural Policies for Pre-Accession.

[9] https://cohesiondata.ec.europa.eu/stories/s/How-does-Cohesion-Policy-support-cities-and-local-/rgzr-e44d/

[10] https://www.urban-initiative.eu/what-european-urban-initiative

Also significant are LIFE, the EU's large environmental protection and climate action program, which operates in direct management form, the Connecting Europe Facility (CER), which supports energy, transport and digital investments for which cities and regions may apply for the first time in this seven-year budget period, and the Interreg plus interregional programs under shared-management aiming to reduce disparities in the levels of development, growth and quality of life in and across Europe’s regions.

It can be concluded that although there are various sources for cities, they are quite fragmented, applying for them is a serious administrative challenge for local authorities, and with few exceptions they provide cities with access to smaller amounts of support. Therefore, the question arises, as to whether it is appropriate and possible to create EU funds that meet the special needs of cities under the direct management of the EC.

3. THE EU COHESION POLICY BETWEEN STABILITY AND THE NEED TO CHANGE

Fewer EU policies than the Cohesion Policy are better suited to the well-known phrase 'in order to remain the same, they must change'. From the beginning, the catch-up policy was about a marathon instead of a sprint: a long-term, structural investment policy with stable financial frameworks. Understandably, this predictability was also reflected in its legal framework which, thanks to the n+3 rule, practically created a ten-year development cycle, giving few opportunities to deviate from the plans.[11]

"The allergy to flexibility is deeply embedded in the genes of the supporters of the Cohesion Policy," pointed out Pierluigi Boda, expert on the Committee of the Regions and the challenges to enforcing any change of the cohesion political ecosystem.

Crises as an impetus for structural reforms to meet immediate short-term needs

However, in recent years, the European Union has faced two crises that made it obvious that 'business as usual' is no longer an option in regional politics. The Covid-19 pandemic and then Russia's aggression against Ukraine prioritized short-term crisis management to ensure the survival of economic actors, while Cohesion Policy with its cumbersome, bureaucratic operating system focuses on the long term.

During the pandemic and the war, it seemed for a while that the EU's number one solidarity instrument and investment policy would become irrelevant amid short-term challenges. Healthcare, households and businesses had to be thrown a lifeline immediately as traditional methods could not effectively respond. The costs of projects financed by structural and cohesion funds were originally planned for stable energy prices and, as energy prices have skyrocketed, some of the ten-year investment plans suddenly lost their relevance.

Greater centralization under the Recovery and Resilience Facility (RRF)

The impression that the cohesion policy could lose ground could have been reinforced by the creation of the Recovery and Resilience Facility (RRF), based on joint borrowing with a total

[11] The Common Provisions Regulation (CPR) provides the main legal basis for Cohesion Policy funds and for shared management funds. It ensures the necessary means to address emerging economic and social challenges through higher flexibility in terms of transferring resources and extended capacity to address future crises. As part of the decommitment rule set for 2021-2027, the n+3 rule allows for funds to be spent by the end of the third year after their commitment to the program.

value close to EUR 750 billion.[12] In terms of its goals, it shows almost complete overlap with the Cohesion Policy. While it operates in a more centralized way, the allocation criteria are different and faster while additionally enabling a less bureaucratic use of money, thus exerting a greater incentive for structural reforms.

Aware of this, certain MSs, according to some experts interviewed for this study, froze the Cohesion Policy in the hopes of acquiring funds more easily and transferred their best projects to the RRF, resulting in a huge implementation gap in the Cohesion Policy. The fact that they had to manage three funding programs in parallel[13] presented the governments with a difficult situation from the start: firstly, the use of the seven-year framework budget resources between 2014 and 2020, which was already affected by the crisis; secondly, the development, adoption and implementation of Recovery and Resilience Plans (RRP); and finally, the launch of the Multiannual Financial Framework (MFF) and Cohesion Policy between 2021 and 2027.

Widening gaps under the short-term crisis management tools

It is by no means excluded that the forward-looking elements from the RRF, such as the simplification of rules and less bureaucracy, will be transferred to the Cohesion Policy in the new multi-annual cycle starting in 2028. At the same time, according to some experts, the implementation of the RRF so far has pointed out that the new, short-term crisis management tool is not a panacea either. Even though it is too early to come to conclusions in the short term, the RRF may have amplified existing inequalities within the EU, notably regarding the digital gap, which has been noted to have widened between children studying in urban and rural schools.

Re-evaluating Cohesion Policy for better short-term crisis response

The polycrisis had an ambivalent effect on Cohesion Policy. Inevitably, Cohesion Policy had to be redesigned to manage the crisis as efficiently as possible. The EC temporarily made the rules unprecedentedly flexible for Cohesion Policy, essentially creating the conditions for the rapid reallocation of unused funds and projects. In the meantime, taboos such as the ban on EU financing of current budget expenditures were also overturned. Cohesion Policy has become an integral part of the EU's crisis management toolkit, which can ensure its usefulness in the future.

[12] https://commission.europa.eu/business-economy-euro/economic-recovery/recovery-and-resilience-facility_en

[13] I.e., the RRF, the 2014-2020 Multiannual Financial Framework (MFF) and the 2021-2027 MFF.

According to several experts who spoke to the authors of this study, the lessons learned during the crisis management forced a re-evaluation of the Cohesion Policy, especially given that governments realized that the effective use of RRF resources required regions' and cities' involvement. "The governance model of the Cohesion Policy has become a value again," stated Pierluigi Boda, an expert from the Committee of the Regions.

Proving its viability through structural changes

In recent years, it has become clear that to avoid rendering itself irrelevant, Cohesion Policy must understand the word of the times and adapt to rapidly changing circumstances. Since its creation, it has been under constant pressure to prove itself to avoid the financial cuts demanded by the net contributors to the budget. From time to time, competing alternatives to Cohesion Policy, such as the Juncker plan (InvestEU) between 2014 and 2020 or, more recently, the RRF, have been on the agenda.

In fact, the change in Cohesion Policy started a long time ago. For the most part, MSs' strategic (sectoral and regional) investment plans had to be put at the service of the green and digital transition already in the 2014 and 2020 period, and this trend is getting stronger with each MFF. The regulation on the rule of law conditions also ultimately serves the purpose of ensuring that MSs use investments financed by European taxpayers in a corruption-free and transparent manner.

Dynamic urban growth: Promising results

According to the 8th Cohesion Report published in February 2022, metropolitan agglomerations perform better than other regions.[14] Between 2001 and 2019, GDP per capita in the capital regions grew faster than elsewhere. In the southern and eastern part of the EU, in addition to the capitals, the GDP of other metropolitan regions also grew more dynamically, which resulted in an increasing degree of economic and employment concentration. Meanwhile, the GDP of large cities and other regions in the western and northwestern part of the EU increased to a similar extent, and to a somewhat greater extent in the capitals.

[14] https://ec.europa.eu/regional_policy/sources/reports/cohesion8/8cr.pdf

4. THE CASE FOR MORE DIRECT FUNDING FOR CITIES

4.1 What European cities want?

A recent Europe-wide survey, the Eurocities Pulse Mayors Survey 2023[15], conducted by Eurocities with the participation of almost hundred EU and non-EU mayors, gives strong indications on top challenges cities are facing, their priorities and their demands to European and national decision makers.

According to respondents, the rise of energy prices is considered by the municipalities to be the most important challenge (28.57%), followed by climate (26.37%), economic recovery (23%) and migration crisis (22%), Other top challenges include Ukraine, inflation, mobility, public budget, COVID pandemic and housing. For example, Warsaw, which hosted around 300,000 Ukrainian refugees in the first three months of the war, swelled by 15% overall.

While over 92% of EU mayors surveyed feel that they contribute to EU policy priorities and processes, more than half of them (52.6%) consider that EU institutions and policies do not or not sufficiently take into account the specific needs and potential of cities.

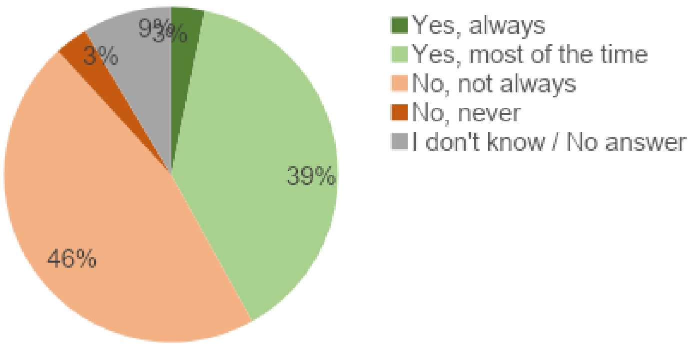


Figure 1 Do you feel that the EU institutions and policies take into account the specific needs and potential of cities effectively? (Answers of all mayors surveyed, including EU and non-EU mayors. Source: Eurocities Pulse Mayors Survey 2023)

Over 50% of EU mayors have even encountered situations where current EU rules and policies prevent them from achieving their goals. For example, EU rules for social housing are often too strict for a city to invest effectively.

Climate action is by far the top priority for mayors in 2023, with more than half of mayors selecting it as one of their top three responses, with the other two being mobility and economic recovery.

[15] https://monitor.eurocities.eu/eurocities-pulse-mayors-survey/

When it comes to their expectations of being able to fund different priorities and where the greatest gaps exist for the next five years, mayors clearly highlight (at least 80% of them) that current resources are not enough. The survey confirms that EU funding helps mayors to somewhat cover the huge financial gaps for climate and energy investments. But according to them, more investment is still needed. Mayors do not feel that they receive comparable EU support for other priorities where resources will be insufficient to match needs, such as housing and the inclusion of refugees, migrants, ethnic minorities and people with disabilities.

Moreover, over 86% of mayors said the current high level of inflation had affected their ability to make strategic long-term investments.

Therefore, mayors point out that EU funding schemes were more helpful in the form of direct support or, more generally, if funds were deployed by taking the local needs into account and empowering them in their implementation.

In this context, mayors see a worrying centralisation trend in EU funds, a sentiment felt particularly strongly among Eastern European mayors who highlight how EU funds are being used by national governments as a political weapon against opposition mayors (see below the case of Budapest).

Finally, given the growing role of cities in achieving EU objectives, more than 50% of EU-mayors see the need for a preferential mechanism for engaging cities and their elected representatives in EU decision-making, both regarding the preparation and the implementation of EU policies and legislation.

How do mayors expect the EU to support them with their priorities?

1. A more direct dialogue between cities and the EU on joint challenges and to improve the design of EU policies impacting cities
2. Simplification of procedures for the absorption (and direct funding) of EU funding to react ongoing and future crises (including refugees, energy, economic)
3. Direct EU funding to empower cities to better reach joint EU targets
4. EU to develop new policies and fund options for local administrations of candidate countries through city-specific approaches
5. Less bureaucratic funding programmes and more targeted legislation to support cities' climate neutrality objectives

(Source: Eurocities Pulse Mayors Survey 2023)

4.2. Arguments in favor of more direct funding for cities

There are several reasons why the EU should consider more direct funding for cities and municipalities. Most of them are linked to general challenges the EU is facing, the need to tackle them in an efficient way and to delivering already existing EU political objectives.

A contribution to achieving the ambitious EU climate policy goals

The most important of these EU political objectives is probably achieving the ambitious EU climate policy goals including climate neutrality by 2050. Clearly, MSs and the EU as a whole will not be able to meet CO2 emission reduction targets without an important commitment in the cities. As one of the interviewees for this study stressed, "cities on the ground are bringing the Green Deal objectives to life". That raises the question of whether the available funding model channeling the sources through shared management would be efficient enough or is an approach more tailored to the cities through direct or semi-direct management of funds necessary.

A contribution to the costs of integrating refugees and legal migrants

The budgetary, infrastructural and demographic costs of the integration of those fleeing war and legal migrants are increasingly burdening cities and urban agglomerations. With the influx of millions of Ukrainian refugees enjoying temporary protection in the EU, this problem has become ever more palpable. According to the EC, in the context of the FAST-CARE comprehensive funding package, meant to address the consequences of Russia's aggression against Ukraine, 30% of the financial support by the EU should go to local authorities.[16]

A contribution to strategic autonomy

The EU's plan for strategic autonomy also shed new light on the role of cities, especially large ones. In recent years, a number of urban infrastructure investments (metro, railway and port facilities) have been implemented by or with the participation of Chinese or Russian companies across Europe. Heeding the EU’s commitment to reduced dependence on Russia and China, greater commitment must be shown to investments in critical urban infrastructures, notably with the help of funds distributed directly from Brussels.

[16] https://ec.europa.eu/european-social-fund-plus/en/news/ukraine-flexible-assistance

An instrument to enforce the rule of law and counter political discrimination

The series of crises in recent years have led many MSs to centralize the investment resources available from the EU budget, often to the detriment of the interests of large cities and towns. In some MSs, the government went so far as to openly discriminate against non-government-led cities, as has been the case in Hungary with Budapest, Pécs and other opposition-led cities. The issue is exacerbated when national governments' mismanagement of EU funding hinders the achievement of EU objectives and prevents local actors, municipalities and cities from meeting them. To counter this, the EU should channel more of its funding directly to municipalities, which are also included in EU programs (i.e., the 100 cities mission). While the Commission has little to no input into how and to what extent governments distribute money under shared management – if they otherwise meet the legal requirements – direct management can offer a solution against politically-based discrimination of cities. The EU would therefore additionally ensure to help cities and municipalities meet EU objectives effectively and efficiently.

The move can also be justified by the consistent enforcement of the rule of law principles, in line with the general political direction aimed at protecting the EU's financial interests and budget resources.

Need for increased decentralization of Cohesion Policy

As mentioned above, many MSs have increasingly brought the use of Cohesion Policy funds under their own powers in recent years, and centralized them during crises. However, according to the 8th Cohesion Report published by the EC in February 2022, the differences in development within individual countries have not decreased at all or only slightly in recent years.[17] All of the aforementioned arguments, combined with the need for local solutions that have come to the fore due to the globalization crisis, may increase the demand for greater decentralization of Cohesion Policy. Another issue is that - as we will see in subchapter 5.2 - this would not necessarily lead to an increase in the role of cities.

4.3. A case study: Budapest, Hungary

Budapest is in a unique position in terms of EU funding, but its case also highlights the failings and risks of the current system of EU funding. The political conflict between the capital and the Hungarian government has resulted in a serious funding crisis, where the government not

[17] https://ec.europa.eu/regional_policy/sources/reports/cohesion8/8cr.pdf

only withholds national funds or reduces revenues, but also uses European funds as a means of political punishment, abusing the powers of the shared management system. By the second quarter of 2023, Budapest found itself in such a critical financial situation that it is unlikely to be able to meet all its governmental obligations; in fact, the city government expects a deficit of HUF 76 billion (around EUR 200 million) by autumn 2023.

The financial situation of Budapest as a result of budget cuts

The city government led by parties in opposition in the national parliament was elected in autumn 2019, and has since been subject to restrictive government measures. During 2020, in parallel with and partly related to the COVID crisis, the national government introduced a series of measures to reduce municipal revenues, and for Budapest in particular. By law, the local business tax collected by municipalities was halved (from 2% to 1%), resulting in a revenue loss for Budapest of around HUF 20 billion (EUR 54 million) in 2021 and HUF 20.5 billion (EUR 55 million) in 2022, which represents more than 10% of the capital's total revenue. The government increased the so-called solidarity tax to be paid by Budapest from HUF 10 billion (EUR 27 million) in 2019 to HUF 21.7 billion (EUR 59 million) in 2020, an amount that has been steadily increasing since, with the budget law foreseeing a HUF 54 billion (EUR 146 million) contribution from Budapest (a quarter of the city's budget) in 2023.[18]

The government also made parking free for over a year during the pandemic (April 2020 - July 2021), permanently withdrew the collection of vehicle taxes from municipalities and banned municipalities from raising their service charges during the COVID emergency. Compensation for lost revenues was implemented selectively by the government, whereby broad financial support was provided to pro-government municipalities and little or no compensation to most opposition-led municipalities. In addition to the HUF 40 billion (EUR 112 million) loss of revenue in 2020 due to the consequences of the coronavirus pandemic (e.g., foregone tourism revenues, non-payment of public transport fares, etc.), the government's aforementioned punitive measures resulted in a financial loss of roughly the same amount for Budapest. The loss of HUF 80 billion (EUR 224 million) amounts to almost 40% of Budapest's budget.

Diversion of EU funds

In effect, the Fidesz government uses EU funds as a tool for politically motivated reward and punishment. In all decisions on the allocation of the Recovery and Resilience Fund and the

---

[18] https://newseu.cgtn.com/news/2023-05-30/Orban-blamed-by-Budapest-deputy-mayor-as-city-faces-bankruptcy-1kevJE69mFy/index.html

Cohesion and Structural Funds since 2019, the government has used all the means at its disposal to ensure that Budapest does not benefit from the various EU funding envelopes.

During the preparation of the National Hungarian Recovery and Resilience Plan (RRP), the national government did not meaningfully consult with the municipalities, as Budapest repeatedly complained to the Commission, and the capital was left out of the HUF 2,200 billion (EUR 5.8 billion) plan that was adopted. In the case of the so-called 'Green Bus' tender, which was announced in a discriminatory way by excluding Budapest by name, the Commission's involvement allowed Budapest to access this RRP program as a result of the capital's lobbying.[19] The program is expected to enable the capital to purchase vehicles worth around HUF 10 billion (EUR 27 million), amounting to 0.45% of the total RRP, as the only benefit from the RRF for Budapest.

Plans for the European Regional Development Fund (ERDF) and European Social Fund (ESF) under the operational programs, totaling nearly HUF 10,000 billion (over EUR 25 billion), were also originally planned to exclude Budapest. After more than a year of negotiations and lobbying with the Commission, Budapest is expected to benefit from the operational programs in the order of HUF 200-220 billion (EUR 540 million)[20], which represents around 2.2% of the total allocation.

Failure to achieve common EU goals

Meanwhile, Budapest has not only made tackling climate change a top priority, adopting a new climate strategy, but has also successfully applied to participate in the '100 Climate Neutral Cities 2030' program of the EU's Horizon Europe Climate Neutral and Smart Cities Mission. The program explicitly encourages MSs to target European funds to recipient cities and requires an investment of hundreds of billions of Forints to achieve the decarbonization targets set by the EU. Thus, mitigating investments are already a priority among Budapest's development goals. However, their financing is questionable due to national government cuts in revenues and domestic subsidies, increased burdens on the capital, and reduced access to EU funds.

[19] The government's Green Bus Program is planned to replace 50% of conventional buses in Hungary's largest cities by low carbon emission ones within the next ten years. The goal of making transport greener was presented as a key component in the government's commitment to achieving climate neutrality by 2050 in Hungary. Cities with a population of over 25,000 will only be able to buy emissions-free buses for public transport as the government will provide co-financing for the acquisition of electric buses. See, https://hungarytoday.hu/green-bus-programme-help-cities-electric-transport/. https://hungarytoday.hu/karacsony-govt-prevent-green-transport-development-budapest/

[20] Integrated Transport OP: HUF 120-130 billion; Regional and Urban Development OP: HUF 80 billion; Environment and Energy Efficiency OP: HUF 10-20 billion.

Moreover, the government's financial obstruction of Budapest's climate efforts not only jeopardizes the plans undertaken in the 100 Cities Mission but could also threaten the climate objectives of Hungary as a whole. The capital city is responsible for 16 to 17% of Hungary's greenhouse gas (GHG) emissions[21] and failing to take appropriate action to reduce its emissions could make it impossible to meet the country's climate targets, as set forth by the EU objectives. The internal political conflict and the ensuing funding crisis in Budapest could jeopardize the implementation of EU-recognized and supported climate plans, including the 100 Cities Mission.

21 https://budapest.hu/Documents/Bp_Klimastrategi%C3%A1ja_v2.0_tarsadalmi_egyeztet%C3%A9sre.pdf

5. LEGAL, POLITICAL AND TECHNICAL HURDLES TO THE EXTENSION OF EU FUNDS' DIRECT MANAGEMENT

In the following, we take into account the legal, political, technical and practical obstacles to the direct financing model of cities and its expansion. In our opinion, none of these are insurmountable, even if overcoming them has different degrees of difficulty.

5.1 Legal hurdle: Amending legislation

Increase the current share of direct management from 1/5 of the EU budget

Although approximately four-fifths of the resources of the EU budget fall under shared management, the share of direct management reaches 20 percent. Consequently, if the political will is there, there is in principle no legal obstacle to amending the rules. But, as many interviewees pointed out, legislation must be amended for more extensive use of direct financing. This is especially true if individual situations and needs justify a greater use of direct financing. The purpose of this study is not to examine the problem of possible legislative amendments. However, it can be said that the transition to direct management would require, among other things, the amendment of the MFF and the Common Provisions Regulation (CPR).

5.2 Political hurdles: National multilevel reluctance

Gaining political consensus union-wide

Obtaining a political consensus could present a considerable challenge, however. One impediment to success is the discrepancy between the higher levels of development of Budapest and other European cities, and the less economically important conglomerates: the big cities are winners already accumulating advantages of the single market. Were Budapest and Warsaw, Poland, to ask Brussels for more money, many people would want to know why.

National grip on EU funds

In addition, national governments are reluctant to relinquish power over EU-distributed funds. According to many observers, the chances of this are almost zero. Ultimately, governments have principal control over how funding is allocated.

Regional anxieties of power curtailing

Equally so, the idea may have opponents not only from above but also somewhat unexpectedly from below. While the representatives of the regions generally have a positive attitude towards the decentralization of regional politics, they, like the governments, tend to see a curtailment of their powers in the cities' direct access to EU funds.

Thomas Wobben, Director of the European Committee of the Regions (CoR) has noted: "Cohesion Policy requires cities and regions to work together in implementing structural funds programs while this partnership should be supported by all levels of government. The principles of Partnership and Multi-level Governance are therefore key delivery mechanisms for the policy and are enshrined in the Structural Funds regulations."

The regions are nervous about direct funding because it also creates a division between regions and cities. Many regions have operational programs at NUTS 2 or 3 level.[22] In some countries, the programs are implemented by both the national and regional governments. "When a city says I want direct management, this could mean the competence of the region is shifted to the local level, and regions are not so keen on doing so" - pointed out an interviewee.

It is suggested that giving cities the possibility of direct funding would open a 'Pandora's box' with the poorest regions and the rural community also asking for the same opportunity.

Funder's objectives vs. local needs

There is a more practical argument against shifting to more direct financing of cities or local authorities, which relates to the way the direct funding model functions. According to Thomas Wobben, "applying for directly managed EU funds does not necessarily support what you do, rather, what others want you to do. Those who ask for direct funding underestimate that it means the agenda is often not set by themselves but by the funder".

Another expert commented, "We are not advocating to increase direct funding from Brussels because it is based on European-wide calls which are not necessarily about what is needed in a region or a city, but what is most successful in the call".

[22] The nomenclature of territorial units for statistics (NUTS) is a hierarchical system for dividing the economic territory of the EU, with one its purposes being the socio-economic analysis of the regions divided in three categories: NUTS 1: major socio-economic regions; NUTS 2: basic regions for the application of regional policies; NUTS 3: small regions for specific diagnoses. See, https://ec.europa.eu/eurostat/web/nuts/background.

Risk of increasing bureaucratic impediments

Kata Tüttő, deputy mayor of Budapest and a Hungarian member of the Committee of the Regions, admits that since there are very different local government structures within the EU, the creation of a universal direct financing system does not seem realistic. This, she adds, would unnecessarily increase the bureaucracy anyway.

5.3 Technical hurdles: Overcoming structural deficiencies

Lack of human and administrative resources

This argument could amount to what can be seen as a technical hurdle. The Commission, in its current shape, is not sufficiently staffed to increase direct management in a significant way. At the same time, MSs refuse to increase administrative funding from the EU budget that would be needed to enhance the staff at the national level.

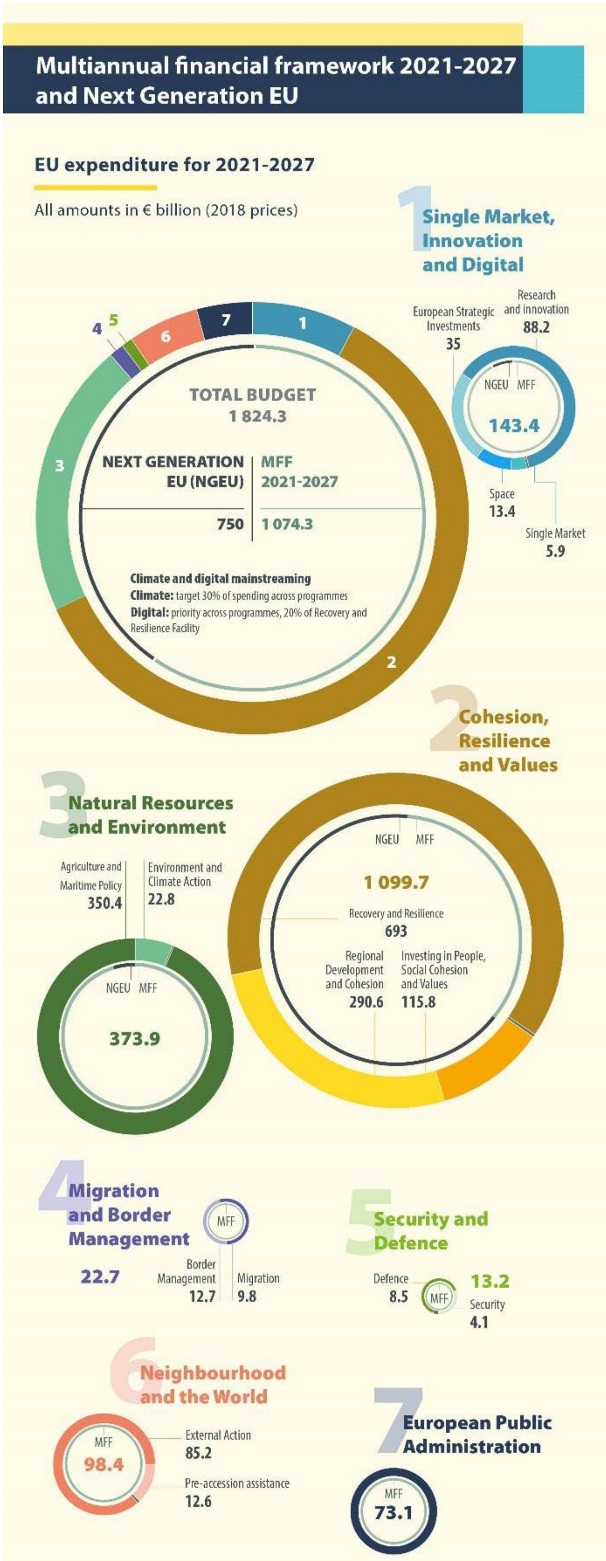
Encroaching national centralization

According to Tüttő and others, Budapest's problem is that it does not have the freedom to set prices and charges. It runs a deficit because the national government does not provide the possibility to manage the entire budget. "Can you solve this problem with direct funding from Brussels? Or should it rather be solved with effective decentralization based on the OECD guidelines for effective decentralization that for example include the clarification of the responsibilities assigned to different government levels and foresees ensuring that all responsibilities are sufficiently funded?" – asks Thomas Wobben.

6. THE ROLE OF THE MULTIANNUAL FINANCIAL FRAMEWORK AND THE RECOVERY AND RESILIENCE FACILITY

In the period between 2021 and 2027, EU MSs will be receiving an unprecedented financial transfer from the EU budget. In addition to the seven-year Multiannual Financial Framework (MFF), which amounts to approximately 1% of the EU27's GNI annually, governments can also use Next Generation EU (NGEU) resources, worth approximately 800 billion euros, created to offset the effects of the coronavirus crisis.

The EU will finance crisis recovery through grants and loans made available within the framework of the Recovery and Resilience Facility (RRF) by offering joint borrowing, the repayment of which will only begin after 2035. The primary goal of the essentially double budget is to restore the economic damage caused by the series of crises but also to improve the resilience of the European economy against future shocks.



There are many similarities between the two funds, such as the significant overlaps concerning goals and investments. At the same time, there are differences with regard to:

1. Timing: in the case of the Cohesion Policy financed from the MFF, the final deadline is 2030, while RRF resources must be spent by the end of 2026 at the latest).
2. Governance: the Cohesion Policy has shared management with greater involvement of the regions, while the RRF is directly managed by governments.
3. Distribution criteria of the framework: the bulk of the RRF goes to the Southern MSs.

7. POSSIBLE SOLUTIONS FOR THE EXTENSION OF DIRECT FUNDING

Due to the aforementioned constraints, in the short and medium term, until the end of the current MFF, we do not envisage an opportunity to increase the EU funds directly accessible to cities and to substantially modify the current financing model. The mid-term review of the MFF will predictably set limited goals instead of a substantive review. These include increasing the flexibility of the budget, which will facilitate some internal reallocation of resources, and an increase in the budget framework, primarily to help finance goals related to the Russo-Ukraine war and strategic autonomy.

Before the European elections in June 2024, nobody, including the EC, will be taking the risk to propose an overhaul of the Cohesion Policy funding rules, thus paving the way for substantially more direct payments. But after 2027, it could be less controversial.

According to most of the politicians, officials and experts we interviewed, a window may open for the adoption of funds that better meet the needs of cities during the preparation and negotiation of the next multi-year framework budget after 2027.

There is no silver bullet but rather a set of different measures that could lead to an improvement of the situation and an extension of direct funding. We have highlighted below some of them.

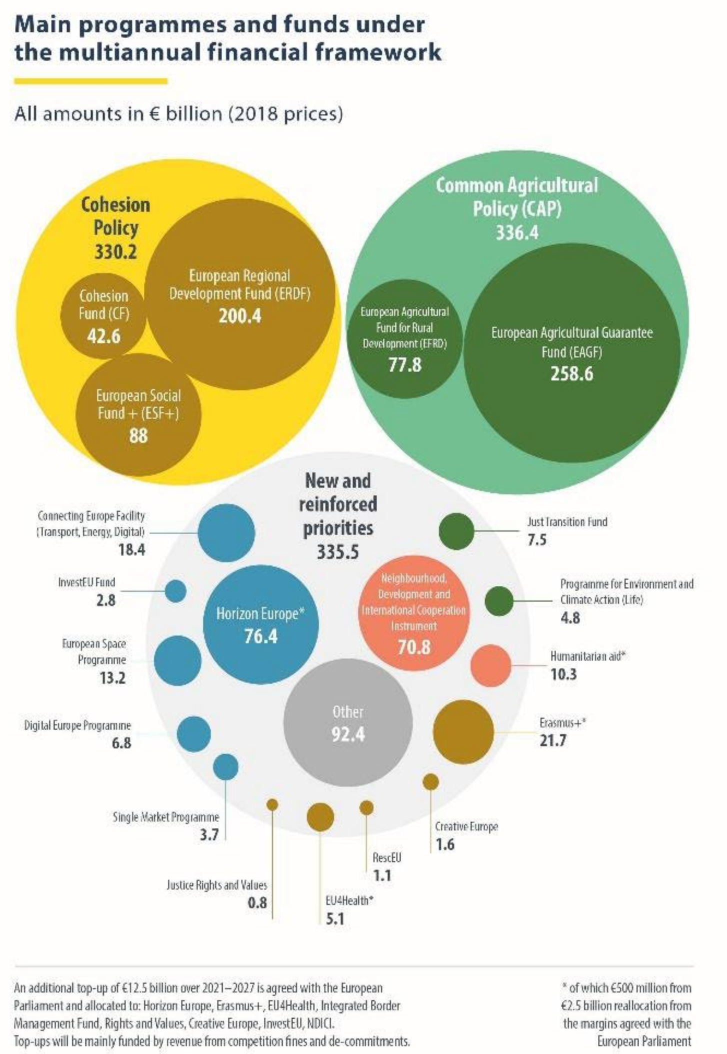
7.1. Short-term opportunities

As it was already mentioned before, there are very limited opportunities to improve the access of cities to EU funding in a limited time-scale. The structures of the 2021-2027 MFF and the RRF are given, their fundamental or systemic amendment is not realistic. Still, some actions can be considered as useful.

Mid-term review of the MFF

The EC published its proposal for the mid-term review of the MFF on the 20th June 2023, without even mentioning cities' needs or problems. The European Parliament is expected to treat the proposal merely as a technical exercise, a quick procedure is foreseen for the file without opening major battles with the Commission or the Council.

While the EU and its MSs seem to be swimming in an abundance of money, the reality is that unplanned events such as the war in Ukraine and the related acceleration of the transition to clean energy have already stretched the EU budget and redrawn priorities two years after the start of the new MFF. This is partly why the EC brought forward the mid-term review of the MFF from the previously planned 2024 to summer 2023, in the hopes of concluding it this autumn.



It is telling that the name of the process is not revision but review, which is much lower in ambition and denotes an evolution of the process rather than a revolution. Obviously, the leitmotiv of the review would be to increase the EU's capacity to support Ukraine and the EU's road to achieving strategic autonomy. However, that would also logically require more resources. Since MSs, especially the so-called 'frugal four'[23], the net payers, are traditionally very reluctant to increase their contribution, the name of the game, according to observers, could be more flexibility. This is also a way to respond more quickly and effectively to new emerging crises that are difficult to predict. It does not exclude an increase of the MFF, though a limited one.

However, despite all constraints, there could be some opportunities for cities in the upcoming review. One of them would be the increase of available funds to cover their costs of receiving Ukrainian refugees. Another opportunity is pointed to by Pietro Reviglio, policy expert of Eurocities, who believes that the role of cities regarding industrial development within the future European Sovereignty Fund could be an argument to create multi-country projects related to decarbonization and energy transition. According to him, the MFF could also be used as a guarantee to provide loans to cities where it is necessary.

[23] The 'frugal four' refers to an informal cooperation between Austria, Denmark, the Netherlands, and Sweden, which are fiscally-conservative countries that sustain EU budget rebates and tight fiscal policy in the eurozone. They usually oppose a large allocable EU budget and collective EU debt.

Moreover, while it will probably not be the time for big changes, the mid-term review offers a golden opportunity for cities to prepare the ground for the future Cohesion Policy after 2027. As the process to negotiate greater direct-management funding will be a lengthy and challenging one, potential beneficiaries would do well and take advantage of the opportunity at hand to begin lobbying at this time.

The RRF

Two years after the establishment of the RRF, the EC disbursed EUR 150 billion in non-refundable grants and loans to the MSs. This is less than 20 percent of the total available budget. Although the resources can be called up until the end of 2026, the question arises as to what happens if a Member State cannot use the financial framework allocated to it at all or only partially. Such a situation may arise, for example, if a Member State is not able to fulfill the previously fixed milestones to the required extent.

Since there is no provision in the decree on the RRF regarding the fate of subsidies and loans that may become stuck, some stakeholders see them as sources that can potentially be paid out in the form of direct management. According to this logic, to put the money to good use, the Commission could make the unpaid funds, or a part of them, directly available to cities, covering the costs of various projects.

At the same time, there is only one deadline for drawing RRF funds, the end of 2026, and otherwise there is no decommitment rule, as EC experts have pointed out. Another feature of the RRF is that, unlike Cohesion Policy resources, the money does not sit in a central account waiting to be allocated. Rather, the Commission lends it on the market when the conditions are ripe for it, and if the Member State concerned fulfills the conditions for payment. If not, the Commission will simply not be allowed by MSs to borrow funding, and thus the final bill will be that much less, as MSs will have less debt to repay. Hence, funds not used remain non-existent, so there are no sources to be redistributed.

Still, even in the case of the RRF, especially regarding its additional, REPowerEU-related programs, cities could point out the importance of their interests and their crucial role in achieving the EU’s common goals in increasing energy independence. The EC could require from MSs stronger domestic partnerships in the preparation of the additional plans, meaningful stakeholder consultations, and cities’ participation in the design and implementation of the national REPowerEU plans, to improve cities’ inclusion in the RRF programming and implementation process, and widen cities’ access to these sources.

The Conditionality Mechanism

Similarly to the RRF, in the national Cohesion Policy envelope between 2021 and 2027, the financial commitments suspended and threatened by the loss of funds within the framework of the rule of law conditionality mechanism are also in a gray zone. As a rule of thumb, resources being withheld, suspended or subject to financial corrections remain available for the Member State for later use (once the conditions are met), or for other programs/projects. On the other hand, the Conditionality Mechanism Regulation is not crystal clear in this sense, especially if we take into consideration the interim deadlines of the 2021-2027 MFF funding. Therefore, the Member State can factually lose funds under the conditionality mechanism, if it is not closed before these deadlines. Hence, sources irrecoverably lost for the MSs' governments could also be regrouped to projects in a direct funding scheme.

Horizon Europe 100 Climate-neutral and Smart Cities Mission

One of the novelties in the 2021-2027 MFF's Horizon Europe program is the establishment of focus areas, called 'Missions', to boost stakeholders' activity, research, development and investment in the EU's priority areas. Among others a 'Climate-neutral and Smart Cities' Mission was also created to help and incentivize cities to speed up their mitigation and adaptation efforts. In the framework of the mission, the EC launched its '100 Climate-neutral and Smart Cities by 2030' program. Over 100 cities were selected, and the project helps them to prepare sound and well-founded decarbonization plans and roadmaps to become - at least partially - climate-neutral by 2030. However, while the program provides expertise, knowledge, access to information and peer-to-peer experiences to help cities, allocated financial sources are rather limited, hardly contributing to real decarbonization beyond the preparation of plans and strategies.

A quick and easy way to provide financial tools to cities could be to fill up the '100 Climate-neutral and Smart Cities by 2030' program with considerable financial sources. The European Parliament regularly makes proposals to top-up the Horizon Europe program during the yearly EU budget debates, with an extra € 311 million for 2023, for example.[24] Additional sources could be redirected to cities already in the 2024 budget if this top-up proposal of Horizon Europe targeted the '100 Climate-neutral and Smart Cities by 2030' program, to allocate additional €3-500 million to finance climate neutrality efforts of cities in the program. This solution does not require fundamental changes in the Common Provisions Regulation (CPR)

---

[24] [Parliament to fight for €311M top-up for Horizon Europe in 2023 | Science|Business (sciencebusiness.net)]

or European Regional Development Funds (ERDF) regulation, neither difficult political debates over European and MSs' competencies, nor major increase in the management capacity of the EC. Elegant, simple and politically viable way to ensure access to additional EU funding for cities, strictly in line with the existing regulations and priorities of the EU.

7.2. Long-term opportunities

While short-term possibilities are rather limited, we see much more chance to improve cities' direct access to EU funding in the long run. Preparatory works of the new, post-2027 MFF have just started, early involvement and lobby work in this process could substantially influence the characteristics and structure of the next multiannual financial scheme.

A hybrid solution

One obvious step could be to increase the proportion of the ERDF (now at 8%) that should be spent on sustainable urban development (SUD). As Benedek Jávor, the former Hungarian Green MEP and the head of Budapest representation in Brussels, proposes, it could be combined with changes in the management of the funds. Then, part of the ERDF could function on a basis of a semi-direct management system, whereby the Commission would participate in the selection of projects labeled as an SUD project by the MSs. This method would then guarantee a politically unbiased distribution of the funds. As we have seen in the case of Budapest, the EC has intervened several times to prevent discriminatory treatment of the Hungarian capital. In the future, it could happen in a preventive way by giving the Commission a say in the selection of the related ERDF projects. Even if raising the earmarked parts from ERDF from 8 to 10% did not make a huge difference, shifting to a form of direct management would probably make it.

Targeted funding

The budget available for the already directly managed European Urban Initiative (EUI) could also be increased from the EUR 500 million available now. An enhanced EUI could become the core of a special fund to support cities in reaching their climate and other objectives related to sustainability. Alternatively, in the next MFF, the EU could establish specially dedicated funds for the green transition, including one for cities. They could operate on different models including a more direct management. Urban earmarking in the national programs could also be a solution.

The same goal can be achieved in other ways, for example, by amending legislation to allow more direct funding than before to meet unique needs and situations. However, it would be quite difficult to determine which specific situations and why they might justify special treatment in the budget.

As it was highlighted by Pietro Reviglio, expert of Eurocities, the role of cities regarding industrial development within the future Strategic Technologies for Europe Platform (STEP) is an argument to create multi-country projects dedicated to energy transition and decarbonization. Hence, cities and other municipalities do most of the public procurement. The EU could fund multi-country projects that address common challenges like building renovation.

The European Semester and the power of country-specific recommendations

Effective decentralization of Cohesion Policy after 2027 was called desirable by several of our interviewees. However, decentralization does not necessarily mean the same to everyone, especially when considering the potential conflict of interest between regions and cities. According to Thomas Wobben, director of the Committee of the Regions, decentralization could be promoted by strengthening the partnership of multi-level governance or by using the European Semester process through country-specific recommendations (CSRs). In the framework of CSRs, the EC encourages MSs to reform, and in the framework of the RRPs, it can make resources dependent on these reforms.

One of the reforms could be the promotion of effective decentralization based on the rule of law in the MSs. The CSRs in their current form are closely related to the use of RRF resources and milestones. To such an extent that their fulfillment has become a quasi-mandatory prerequisite for the payment of funds. For such a connection to be established between the fulfillment of CSRs and access to Cohesion Policy resources, both the MFF and the Common Provision Regulation (CPR) would have to be amended.

The market-based solution

The CSRs could also include a golden rule for cities' long-term investment needs that would allow cities to borrow from capital markets. For example, in cases such as Budapest not being able to take out the necessary loans for larger-scale investments, the smaller-scale subsidies available through direct financing from Brussels may not be sufficient to do so. But if they had the right to cover the costs of certain types of investment projects by issuing bonds, that would be a significant help. However, some experts are skeptical about cities issuing bonds given the uncertainty of where the guarantee would come.

The "Norwegian model"

A creative solution could be the distribution of funds along the lines of the European Economic Area and Norway Grants, in which part of the resources are managed by civil society organizations rather than governments.[25] According to an EC official, who asked to remain anonymous, such a money distribution center could be appointed for cities and money could be managed more directly (without government intervention).

Review of the principle of excellence

The Horizon Europe EU research framework program under direct management operates based on the principle of excellence. This usually favors already prominent research centers, universities and the consortia they form. The poorer Central and Eastern European MSs of the EU have long been urging the redefinition of the concept of excellence and adapting it to local needs so that their institutions and their regions and local governments become eligible to also get more resources.

---

[25] The Agreement on the European Economic Area, entered into force in 1994, has brought together the EU Member States and the EEA EFTA States – Iceland, Liechtenstein, and Norway – in a single market. The objective of the EEA and Norway Grants is to reduce social and economic disparities in the EEA, as they are intended to put the beneficiary countries in a better position to make use of the internal market.

8. CONCLUSION

The budget framework of the EU reflects a rather outdated expenditure model and cost structure, within which, despite the changes, the bulk of the resources goes to traditional policies, such as the Common Agricultural Policy and the Cohesion Policy. This structure, although partially justifiable, does not sufficiently consider the strategic goals of the EU, such as the fight against climate change, decarbonization, digitalization, or the achievement of greater strategic independence of the EU in a geopolitical environment that is more unfriendly than before.

Cities are key actors in achieving the EU's common climate, digital, social or health objectives and, therefore, deserve the EU's special attention and protection against restrictive measures by national governments, in the spirit of EU principles such as subsidiarity, partnership and political non-discrimination. As illustrated through the Budapest case study, Member State governments can directly hinder the achievement of either common European objectives or the decarbonization commitments of programs such as the 100 Cities Mission, by allocating (or withholding) EU funding based on political bias.

The successful completion of the EU goals would require more than structural changes: an approach that pays more attention to possible bottlenecks and their elimination. Such an obstacle could emerge should cities, particularly large ones most responsible for greenhouse gas emission, not receive enough support for energy efficiency or the construction of sustainable transport systems. This could jeopardize the achievement of the decarbonization and climate neutrality objectives of the MSs and the EU as a whole.

In our study, informed by conversations with important stakeholders, we have listed the main arguments for and against direct financing, outlining several possible solutions, far from exhaustive. We came to the conclusion that meeting the special financing needs of cities is politically justified, can be solved legally, and resources can be provided for them even before 2027.

Considering that funds from the EU budget can be quite fragmented and may not always entail the desired effect, it is recommended to reconsider the support system affecting cities according to the principle of efficiency. Increasing direct management financing can play a useful role in this.

In principle, in the time horizon after 2027, several solution directions can be envisaged. One of these is a separate European urban policy with independent budget resources. While this solution posits advantages, it can have several drawbacks, with one of the main risks being cities ultimately have less resources at their disposal than at present.

One of the most tangible solutions would be to increase the proportion of the ERDF budget that must be devoted to sustainable urban development from the current 8% to 10%, for instance, as the European Parliament has already proposed for the period 2021-2027. However, its effects may remain limited since the governments decide about the allocation. To prevent political discrimination and ensure the recipients' accountability, the earmarked amount should be placed under direct or semi-direct management, thus not necessarily entailing an increase of the EC's capacities.

An additional solution could be to top-up Horizon Europe's '100 Climate-neutral and Smart Cities by 2030' program with an extra €3-500 million to finance cities' climate neutrality efforts. The proposal could be made by the European Parliament, which regularly makes its top-up proposals for the Horizon Europe program. This solution does not require fundamental changes in the CPR or ERDF regulation, neither difficult political debates over European and MSs' competencies, nor major increase in the management capacity of the EC.

In recent years, the EU has demonstrated that, despite existing limitations, it has been able to adapt its budget and expenditures to changing circumstances. There is good reason to assume that this trend will continue in the near future, starting with the MFF mid-term review, given that it became necessary to re-prioritize and adjust the budget already after the first two years of the MFF.

The authors of the study are aware of the difficulties and counter-interests that appear primarily, but not exclusively, on the side of the MSs' governments. However, the EU has often been able to manage seemingly irreconcilable differences. We are convinced that there is also the possibility of a smart compromise in this dossier, which results in a win-win situation for all stakeholders, the EC, MSs, regions, and cities.

ANNEX

1. Shared-management funds/programs

Name of the program	General information	Fields	Additional information
EU Mission: Climate-Neutral and Smart Cities	Part of the EU missions, the aim of the Climate-Neutral and Smart Cities program is to involve local authorities, citizens, businesses, investors, and regional and national authorities to deliver 100 climate-neutral and smart cities by 2030 and to ensure that these will become experimentation and innovation hubs to permit all European cities to achieve this goal by 2050.	The program covers: zero-emission mobility, positive clean energy districts, urban greening and re-naturing, as well as associating Ukrainian cities to the climate-neutral and smart cities Mission.	The goals of the program have extended to Ukrainian cities that will partner with twin cities in Europe to ensure the development of selected Ukrainian cities in the hopes that those will become models of innovation for non-selected Ukrainian cities in the future. Tailor-made advice and assistance from the Mission Platform will be available to the selected cities in addition to more funding and financing opportunities through a Mission label.
Circular Cities and Regions Initiative (CCRI)	CCRI aims to implement circular economies across European cities and regions by supporting Europe's green transition. By boosting circularity at local and regional level, through multi-stakeholder collaboration and support scheme, CCRI will ensure collaboration, knowledge sharing, innovation, and upscaling. Exchange of know-how is key to enable CCRI to share replicable best practices to help cities and regions find	CCRI has a focus on ● Knowledge sharing; ● Easily actionable guidance for the development and implementation of Circular Economy Action Plans and CSS; ● Quick access to relevant resources to address	CCRI provides financial support through the Horizon Europe, PDA, and the Circular Economy Technical Assistance Facility from the EIB. The initiative is open to any European city, region and territorial cluster, and organizations interested in learning more about

Name of the program	General information	Fields	Additional information
	concrete Circular Systemic Solutions (CSS) that suit their own needs.	knowledge or capacity gaps; ● First-hand information about upcoming funding opportunities; ● Facilitated evaluation and monitoring of the implementation process of a CSS through a dedicated self-assessment tool	the circular economy at local and regional level.
European Guarantee Fund (EGF)	The European Investment Bank Group established a European Guarantee Fund of EUR 25 billion that will increase its support up to EUR 200 billion of finance for companies, with a special focus on SMEs. There is an additional special focus that remains on supporting investment in a green and sustainable recovery for Europe.	The aim is to recover after the COVID-19 pandemic with special emphasis on: ● Environment and Climate Action; ● Funding Researchers; ● ICT Research and Innovation; ● International Cooperation; ● Partnerships with Industry and MS; ● Research Infrastructures; ● Culture and Creativity	The EGF will financially help SMEs, Large Enterprises, Government, Cities, Communities and NGOs, Knowledge Centers through loans and investments, equity financing and guarantees. This funding program provides guarantees to free up capital for national promotional banks, local banks, and other financial intermediaries to make more financing available for small and medium companies, mid-caps and corporates. Cities can apply as the Promoter/Financial Intermediary for projects.
Recovery Assistance for	The program aims to prevent the widening of disparities and an uneven	The program will invest in projects that foster crisis-	REACT-EU is not a new funding source, but a top-up to 2014-2020

Name of the program	General information	Fields	Additional information
Cohesion and the Territories of Europe (REACT-EU)	recovery process after the COVID-19 pandemic. Funds will be allocated to aid Member States (MSs) to focus on rebuilding resilience of healthcare systems, restoring labor markers, supporting workers and enterprises, and addressing the social impact of the crisis. REACT-EU will aim for the development of a green, digital, inclusive, and resilient economy.	repair capacities and contribute to a green, digital and resilient recovery.	ERDF, ESF, FEAD, and YEI allocations, which will continue to be allocated to support access to the labor market, job creation, and quality employment. The extra EUR 47.5 billion available will be allocated with special attention to regions that require the most assistance and that have been most disturbed economically by the pandemic.
Interreg Europe	Interreg is an interregional cooperation program, co-funded by the European Union with the aim of reducing disparities in the levels of development, growth and quality of life in and across Europe's regions. With a budget of EUR 379 million, it seeks to help local, regional, and national governments across the 27 MSs, Norway, and Switzerland to develop and deliver better policy by supporting exchange of good practices.	The program adopts two paths to better policies: interregional cooperation programs and policy learning platform. It covers better regional governance through building capacity to ensure the development of a smarter, greener, more connected, more social Europe that is closer to its citizens.	Criteria include: 1. Partners from at least three countries, from which at least two partners must be from the EU Member States, financed by the Interreg Europe program. 2. A mix of regions with different levels of development 3. Going beyond the cross-border and transnational cooperation areas 4. Usual ERDF budget will range from 1-2 million euros

2. Direct-management funds/programs

Name of the program	General information	Fields	Additional information
Urban Innovative Actions/European Urban Initiative (EUI)	The aim of the funding program is to respond to increasing urbanization in European cities by supporting the design of sustainable urban development strategies, policies, and projects. EUI-IA collects and shares the results of projects to ensure the capitalization and transfer of knowledge and union-wide cooperation. EUI-IA co-finances up to 80% of projects' activities and can provide up to EUR 5 million European Regional Development Funds (ERDF) to implement projects. Urban authorities, delivery partners, and transfer partners can apply for funding.	• Urbanization • Air quality • Climate change • Culture and cultural heritage • Demographic change and digital transition • urban mobility, poverty, and security • integration of migrants and refugees sustainable use of land and nature-based solutions	EUI supports cities of more than 50 000 inhabitants or groups of urban authorities with a total population of at least 50 000 inhabitants. EUI understands cities to be hotbeds for innovation and considers city-to-city exchanges and peer reviews to be crucial in the design and implementation of sustainable urban development strategies, policies, and practices.
URBACT	Since 2002, the program has aimed to develop the cooperation and knowledge exchange to enhance the skills of local stakeholders in the design and implementation of policies. URBACT emphasizes multi-level cooperation (regional, national, EU) through horizontal and vertical policy integration. Different levels of governance work together in collaboration with local people to create a new development strategy for the EU sustainable urban	URBACT IV (2021-2027), the new program, crosscuts EU priorities of digital, green and gender-equal policymaking into its activities. It also seeks to tackle the challenges facing urban environments today such as climate change, intergenerational gaps and digital disruption.	The program has 3 aims: 1. Transnational networks for which the main beneficiaries will be cities from EU MSs, Norway, Switzerland, and IPA countries. 2. Capacity building activities for which all URBACT networks and local stakeholders are eligible. 3. Knowledge sharing action for which cities, urban

Name of the program	General information	Fields	Additional information
	development driven by action-oriented strategies.		authorities/policy makers, local practitioners and regional authorities are eligible. The program is co-financed by ERDF and IPA.
EU4Health program 2021-2027	EU4Health is the main European Commission (EC) instrument to implement the EU health strategy with a EUR 5.3-billion budget during the 2021-27 period. The priorities for 2021-2027 include a focus on urgent and long-term health priorities such as the response to COVID-19 and other cross-border health threats, Europe's Beating Cancer Plan, the Pharmaceutical Strategy for Europe, and digital health. The program aims to improve and foster health, protect people, increase accessibility to medicinal products, medical services, and crisis-relevant products, and strengthen health systems.	EU4Health supports a broad range of actions categorized under four overarching "strands" with a cross-cutting focus on cancer: 1. Crisis preparedness 2. Health promotion & disease prevention 3. Health systems & healthcare workforce 4. Digital	EU MSs and Associated non-MSs (Norway, Iceland, Ukraine and Moldova) are included in this program. Funding opportunities under the EU4Health Program are published by the Health and Digital Executive Agency (HaDEA), where potential beneficiaries can find the calls for proposals.
Education, Audiovisual and Culture Executive Agency (EACEA)	The EACEA program aims to create and share knowledge, to preserve and protect European cultural heritage, enrich Europe's cultural diversity while also fostering innovation, cross-border cooperation, and mutual respect. EACEA manages funding for education, culture, audio-visual content, sport, citizenship and volunteering, and provides grants,	The EACEA has four funding programs: Erasmus+, Creative Europe, the European Solidarity Corps, the Citizens, Equality, Rights and Values program (CERV), and Intra-Africa Academic Mobility Scheme.	Potential beneficiaries may also apply for Pilot Projects (PP) and Preparatory Actions (PA), which have their calls for proposals and fall under the EACEA.

Name of the program	General information	Fields	Additional information
	lump sums, loans and investments, and equity financing.		
Justice and Consumer Funding	The objective of Justice and Consumer Funding is to contribute to the development of a European area of justice based on the rule of law, mutual recognition and mutual trust. It aims to facilitate legal cooperation in civil and criminal matters and promote the rule of law; support legal training; and facilitate access to justice for all.	Focuses on focuses on justice and citizenship by raising awareness of good policies and law, promoting mutual learning and exchange of good practices, implementing monitoring and training to improve the understanding of barriers to the rule of law, and developing key European networks and judicial networks.	Eligible entities can apply to the funded program Citizens, Equality, Rights and Values (CERV), with a focus on gender-based violence, or the Justice Program 2021-2027. Amounts range from approximately 2 million euros to approximately 11 million euros depending on the call.
European Local Energy Assistance (ELENA)	This funding program provides assistance for energy efficiency and renewable energy investments targeting buildings and innovative urban transport. Activities that can receive ELENA grants include: technical studies, energy audits; business plans and financial advisory; legal advice; tendering procedure preparation; project bundling; and project management.	The ELENA program provides support to three different sectors that were categorized under three umbrellas: energy efficiency, sustainable residential, and urban transport and mobility.	The program has no calls for funding. Proposals are reviewed and assistance is granted on a first-come, first-served basis. The process has four steps: Pre-application stage; Application Stage; Request to the EC; and Funding Agreement between the EIB and the Final Beneficiary. ELENA typically provides Investment Programs above 30 million euros.
Talent Booster Mechanism	The aim of this new EU mechanism is to bring a fresh impetus for re- and upskilling to support EU regions affected	EU mechanism will offer tailor-made, place based and multi-dimensional solutions	Cities and affected regions will be helped through existing EU programs such as the Cohesion

Name of the program	General information	Fields	Additional information
	by the accelerated decline of the working age population and to prevent the emergence of new and increased territorial disparities within the EU. It will train, retrain, and attract the people, skills, and competences needed to address the impact of demographic transition.	to use existing EU funds. The mechanism considers an ageing as well as declining population, a shrinking working-age population, increasing territorial disparities, and a growing urban-rural divide.	Policy programs, European Urban Initiative, and Technical Support Instrument (TSI).
Environment and climate action (LIFE) under (CINEA)	Launched in 1992, LIFE is the EU's funding instrument for the environment and climate action, meant to support environment, nature conservation, and climate action programs throughout the EU. It provides loans and investment and equity financing to projects tied to Environment & Climate Action, Funding Researchers, Innovation, International Cooperation, Partnerships with Industry & MS, SMEs, Social Sciences and Humanities, and Manufacturing.	It contains two main fields of action: environment and climate change and has four sub-programs: 1. Nature and biodiversity 2. Circular economy and quality of life 3. Climate change mitigation and adaptation 4. Clean energy transition	All LIFE calls for proposals will be published on CINEA's website as well as the EC's Funding & Tenders portal. CINEA also holds virtual EU info days to guide potential applicants. Dedicated virtual information session on the specificities of the calls take place throughout the year.
Connecting Europe Facility (CEF Digital)	CEF Digital is meant to support and catalyze both public and private investments in digital connectivity infrastructures between 2021 and 2027. CEF Digital will particularly allocate investments devoted to safe, secure, and sustainable high-performance infrastructure. Their aim also includes increased capacity and resilience of digital infrastructures to ensure Europe's	Topics covered by the program include: • Developing very high-capacity networks; • Guaranteeing uninterrupted coverage with 5G systems of all major transport paths; • Deploying new or a significant upgrade of	The grants and loans and investments will be largely allocated to transport (75% of funding), followed by energy and digital.

Name of the program	General information	Fields	Additional information
	goal of remaining digitally sovereign and independent.	existing backbone networks; • Implementing and supporting digital connectivity infrastructure related to cross-border projects in the areas of transport or energy.	
The Citizens, Equality, Rights and Values program (CERV) under EACEA	CERV was created along with the 2021-2027 Justice program under the Justice, Rights and Values Fund and is meant to support and develop open, rights-based, democratic, equal, and inclusive societies based on the rule of law. Hence, an involvement of civil society and people's civic engagement is key in the realization of the program.	The program has 5 pillars: 1. Equality, Rights and Gender Equality 2. Citizens' engagement and participation 3. Daphne – Combating violence 4. European Union values	All grants involve co-financing and depending on the project proposed, the maximum possible rate of EU funding is 90%.
The Digital Europe Program (DIGITAL) and European Digital Innovation Hubs (EDIH)	The Digital Europe Program (DIGITAL) is a new EU funding program focused on bringing digital technology to businesses, citizens and public administrations. The project overall aims to accelerate the economic recovery and shape the digital transformation of Europe's society and economy. EDIH's core mission is to build up the digital capacities of SMEs and public sector organizations. Through EDIHs,	Digital will provide strategic funding and support projects in five key capacity areas: supercomputing, artificial intelligence, cybersecurity, advanced digital skills, and widespread use of digital technologies. EDIH aims for opportunities for interaction and collaboration between EDIHs, SMEs and the public	The program works in tandem with the Green Deal to make Europe greener and more digital. The initial network of EDIHs will be established from a list of hubs designated by MSs, which have an essential role in the selection process. The EC will launch an expression of interest for MSs to designate their candidate hubs.

Name of the program	General information	Fields	Additional information
	SMEs gain access to essential technical expertise and innovation services, such as financing advice, training, and skills development, etc.	sector. Key aims are: accelerating the digital transformation of the private and public sector across the EU; driving the uptake of advanced digital technologies; ensuring that 90% of SMEs in the EU have at least a basic level of digital maturity; and creating new European value chains.	

3. Funding Advice Programs

Name of the program	General information	Fields	Additional information
InvestEU Advisory Hub	The InvestEU Advisory Hub aims to give an additional boost to investment, innovation, and job creation in Europe over the period 2021-2027. It acts as the single entry point for project promoters and intermediaries seeking advisory support, capacity building, and technical assistance related to the 13 existing, centrally-managed EU investment funds. The Hub will support the identification, preparation, development, structuring, procurement and implementation of investment projects; enhance the capacity of promoters and financial intermediaries; and support awareness raising and market development for investment areas experiencing a market failure.	As part of the broader InvestEU program, the Advisory Hub has four main policy areas: sustainable infrastructure; research, innovation, and digitalization; SMEs; and social investment and skills.	Advisory Hub is managed by the EC and financed by the EU with the EIBG acting as the main advisory partner to the EC by providing strategic support to develop and reinforce advisory initiative. Application for help with financing from the Hub are to be made separately from the ones to InvestEU, as they will be submitted and assessed in accordance with the respective eligibility criteria of the Hub and not of InvestEU. Applications are to be made through the 'Advisory Support' online platform
JASPERS (Joint Assistance to Support Projects in European Regions)	JASPERS is meant to enhance project quality and helps cities and regions absorb European funds (ESIF, CEF, and IPA funds) for high-quality projects. It advises authorities on strategic planning to initiate better projects, supports promoters in preparing projects in areas benefiting from EU funds, improves the capacity of administrations by transferring knowledge about project	JASPERS offers support for (1) strategies and plans, (2) advisory support in project preparation, (3) project-appraisal support, and (4) capacity building. It is involved in the sectors of circular economy and solid waste, energy, innovation, transport, urban	Entities do not need to go through a tender process as the services provided by JASPERS are free of charge, as they are funded by the EU and EIB. Throughout the collaboration, the city or urban authority remains the owner of its project but needs to collaborate with the appropriate national managing authority, which

Name of the program	General information	Fields	Additional information
	preparation, environmental issues, and EU legislation, and speeds up the EU approval process by carrying out an independent quality review.	development, and water and wastewater.	acts as the central coordinator of requests for support from JASPERS.
fi-compass	fi-compass is a one-stop-shop advisory platform launched by the EC in partnership with the EIB to provide financial and technical assistance to better equip authorities and private investors to make efficient use of the financial instruments under the EU shared management agreement (i.e., European Social Fund Plus (ESF+)). The platform compass publishes practical know-how and learning tools on the available EU structural funds.	fi-compass includes 'how-to' manuals, factsheets and case study publications for the EU's financial instruments such as ERDF and ESF+ shared management, EAFRD and EMFF investments, and AMIF, as well as face-to-face training seminars, networking events, and video information.	Specific advice can be offered also on the use of financial instruments under each of the EU shared management Funds section of the website.