POLICY BRIEF

4i TRACTION
innovation · investment
infrastructure · integration

Towards Transformative EU Climate Policy

Ten Recommendations from the 4i-TRACTION Project

Main messages:

1. Despite recent EU policy efforts, **significant policy gaps remain to manage the transformation** to climate neutrality. Sectoral policymaking lacks integration, infrastructure expansion is too slow, the EU lacks 400 billion Euro of climate investment annually and EU innovation policy needs more funding and direction.

2. EU policymaking can be improved by **strengthening climate policy integration** across all sectors and **enhancing public participation** and accountability, creating broader societal ownership. Regular **updates to the EU Long-Term Strategy** can provide overall guidance and coordination for policy decisions towards 2050.

3. Existing challenges could further be overcome through stronger **integration of EU infrastructure planning**, and a **coordinated phase-out of fossil fuels and fossil value chains.** This can project a clear pathway for the transition to a climate-neutral economy and provide greater certainty for businesses and consumers.

4. To address shortcomings in innovation and finance, net zero public procurement rules could help create **green lead markets**, and a European Long-Term **Climate Investment Plan** could facilitate closure of the climate investment gap and align financial flows with climate objectives. **Regional innovation clusters** would provide necessary space for experimentation at national level, pioneering deployment of climate neutral technology and new business models.

Introduction

The EU has set itself the goal to become the first climate-neutral continent. The European Green Deal, the European Climate Law and the Fit-for-55 package are core steps to strengthen EU climate policy, and to deliver on the EU's ambition to create a net-zero emissions economy. But despite these efforts, the EU is not on track to climate neutrality by 2050.

Based on extensive analysis of the EU's existing climate policy instruments and current governance framework, the 4i-TRACTION project finds that several gaps remain across the entire EU climate governance. In the new legislative term 2024-2029, the EU has the chance to close these gaps and accelerate the necessary changes towards climate neutrality. In this policy brief, we outline **ten recommendations** for EU climate policy going forward.

Gaps In the transformation towards climate neutrality

Several transformation gaps remain in the fields of **integration** of policymaking, rolling out the **infrastructure** for a climate-neutral economy, mobilising the necessary public and private **investments** and deploying climate-friendly **innovations** at scale (Görlach et al., 2024).

Climate policy **integration** is still uneven across sectors and limited, for example, in agriculture and transport. Moreover, the coordination of innovation, investment, and infrastructure is deficient. To reach climate neutrality, the EU needs a whole-of-government approach that ensures all its policies are aligned with climate neutrality across all sectors, institutions, laws and policies.

The roll-out of **infrastructure** for a climate-neutral economy is currently too slow, especially for energy and transport infrastructure, in part due to a lacking comprehensive strategy for transnational infrastructure. The EU therefore needs to strengthen its policy efforts to deliver an EU-wide infrastructure fit for climate neutrality.

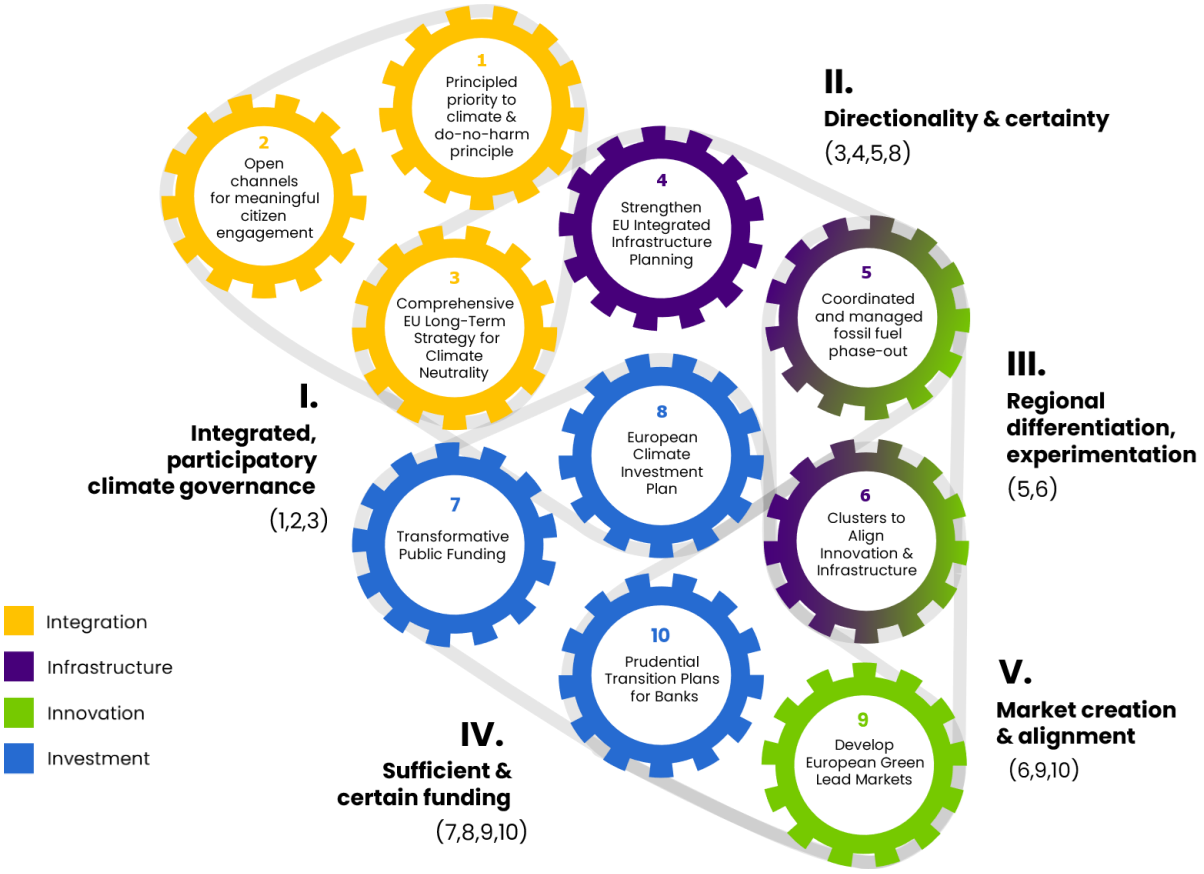
The EU faces a climate **investment** gap of more than €400 billion annually and the existing framework is insufficient to mobilise funding at this scale. Moreover, the EU faces a two-fold challenge regarding investment: not only to scale up climate-friendly investments, but also end investments that perpetuate the fossil-based economy. The EU needs to increase the quantity of public funding and coordinated policies in order to ensure sufficient and predictable funding in the future.

Progress is also lacking across the **innovation** chain, including limited and incoherent funding and lack of directionality. But the main bottleneck is demonstration and deployment of innovations. With only two and a half decades left to get to net zero emissions, the focus must be on deploying near- or market-ready technologies at scale. Policy support, in the form of regulations, funding, and strategic direction, is crucial for this.

Transformative Governance Needs

The challenge of transforming the EU economy to climate neutrality requires a transformative climate policy meeting several needs: (1) it must ensure **integrated and participatory governance** to coordinate parallel and interdependent developments across sectors, address cross-cutting challenges of innovation, infrastructure, and investment, and secure societal support by involving stakeholders and ensuring buy-in; (2) it needs to **provide directionality and certainty** amid considerable uncertainty by aligning infrastructure, investment, and regulatory frameworks, in this way providing greater predictability to businesses, investors and consumers about the necessary actions; (3) it should **encourage regional differentiation and experimentation** to capitalize on Europe's diverse regional strengths, allowing regions to innovate based on their unique resources, skills, and infrastructure; (4) it must ensure **sufficient and certain funding** through a coordinated approach that combines public and private investments, leveraging fiscal policy and financial regulation to align with climate neutrality and ensure a stable investment framework; and (5) use market dynamics by **aligning existing markets or creating new ones** to scale up solutions, mobilise private funding, and stimulate demand for climate-neutral solutions by strengthening market-based elements like the EU Emissions Trading System and addressing bottlenecks on the supply side.

Recommendations



1: Give Climate Principled Priority and Avoid Policies that Significantly Harm Climate Objectives

Climate policy integration (CPI) is crucial to prevent climate change from being treated as an isolated issue, but instead to consider it in and coordinate it across all sectors and policy areas. The following actions could ensure a whole-of-government approach towards the climate-neutrality transition.

- Inclusion of new provision in the European Climate Law to prioritize CPI for EU policy-making and implementation. Strengthening of institutional coordination and ensuring climate policy expertise in all relevant bodies and processes. Making CPI a requirement in regulatory fitness-checks.
- Further develop the principles of *Do No Significant Harm* and *synergy,* to extend their application beyond funding and investment instruments. This could minimise inconsistency and maximise coherence between climate and other policy objectives.
- Amend the Governance Regulation to include CPI, *Do No Significant Harm* and synergy principles in EU and Member-State-level long term strategies and related transition planning and monitoring processes.

2: Open Channels for Meaningful Citizen Engagement

Broad societal ownership and support are crucial for enabling the climate transition across the EU (and beyond). The upcoming revision of the EU's Governance Regulation and the European Climate Law provide a unique opportunity for a quantum leap towards firmly anchoring such ownership and support and bringing related EU policy in line with the Aarhus Convention. The EU should fully exploit this opportunity by:

- Establishing high standards and a comprehensive approach to public participation in EU climate governance in a dedicated section on public participation in the Governance Regulation; and
- Enhancing accountability to citizens by ensuring general and consistent access to justice in climate-related matters across the EU, anchored in the Governance Regulation.

3: A Comprehensive EU Long-Term Strategy for Climate Neutrality

Planning plays a key role in the transition towards climate neutrality. Through planning, policymakers are able to identify and evaluate policy options and their impacts and solicit independent scientific advice and public input. There is currently no requirement to update the EU Long-term Strategy (LTS), or to prepare a new one.

- An EU-level long-term strategy for climate neutrality should be prepared at 10-year intervals and updated at least every five years. The requirement should be included in the Governance Regulation.
- The preparation of the EU-level LTS should be informed by the latest science, including advice by the European Scientific Advisory Board on Climate Change. The preparatory process of the EU-level LTS must be transparent and inclusive.

- The EU LTS should assess innovation, investment, and infrastructure needs, and integrate social aspects of a just transition and the objective of 'leaving no one behind.'
- Include a provision in the European Climate Law requiring key economic sectors to create net-zero transition roadmaps and require the Commission to provide guidance and supervision.

4: Strengthen EU Integrated Infrastructure Planning

Transforming the EU's infrastructure to match the needs of a climate-neutral energy and transport system requires significant efforts and investments. Achieving these changes in time is crucial to meet future climate goals, since lack of infrastructure may cause delays in the decarbonisation of industry, transport and the built environment, increase energy costs and endanger security of supply. The following actions could help avoid these risks.

- Building on existing EU-coordination programmes and institutions, the EU should take a stronger role in ensuring the necessary transnational infrastructure is planned and implemented.
- Develop an EU Integrated Infrastructure Plan aligned with the EU's climate goals and its long-term strategy (see #3 above).
- Strengthen EU governance by designating infrastructure as one of the key dimensions of the EU climate and energy Governance Regulation. Strengthen and expand infrastructure-related planning requirements in National Energy and Climate Plans and LTSs.
- Initially, EU infrastructure policy should focus on expanding electricity infrastructure. Interoperability should support the electrification of end uses and their expansion.

5: Coordinated and Managed Fossil Fuel Phase-Out

The EU economy and its infrastructure has developed around fossil-based value chains. An uncoordinated demise of these, as they are rendered obsolete by the rising carbon price, stricter regulations, changing consumer tastes or superior climate-neutral alternatives could have disruptive effects leading to social hardship, public resistance, and welfare losses in the form of stranded assets. To counter this, the EU could establish the managed phase-out of fossil technologies and value chains as a distinct element of climate policy, including through the following elements:

- Anchor timelines and end dates for fossil-based technologies in relevant EU legislation, for example the Ecodesign Directive, the Directive on the Energy Performance of Buildings (e.g. for gas boilers in buildings) and the (Industrial Emissions Directive (industrial heat, blast furnace steelmaking).
- Plan the decommissioning or repurposing of the infrastructure that supports fossil-based technologies, such as gas grids, also considering social aspects.
- Agree to end all public funding for fossil assets and infrastructure and revise EU Taxonomy Regulation to ensure private investments in fossil-based value chains are not labelled as Paris-aligned and are identified as incompatible with climate goals.

6: Clusters to Align Innovation and Infrastructure for Climate-Neutrality Solutions

Local clusters can spearhead the transformation to climate neutrality: particularly to align innovation support, infrastructure deployment and finance in line with regional transformation strategies, to deploy and scale up new climate solutions and the supporting business and innovation ecosystems. This includes the following elements:

- Use local clusters specifically to test and facilitate the co-evolution of technology development and the reconfiguration of value chains with the deployment of supporting infrastructure, an enabling regulatory framework, and new business models.
- Include a clustering element in EU Missions calls, allowing regional clusters to apply for EU level funding that supports their regional transformation.
- Monitor the dynamics of different clusters to facilitate learning from successes and failures, avoid both over-emphasis of particular technologies but also neglect of other options, and to ensure cluster dynamics are aligned with the EU long-term strategy.
- Develop a governance structure to oversee the emergence of different clusters – while cluster definition is primarily a bottom-up process, this can be complemented with oversight elements to ensure coordination with infrastructure policies and EU funding instruments.

7: Transformative Public Funding

The EU already has an extensive and complex funding landscape at its disposal to provide public funding for the transition. To ensure that a shortage of public funding does not obstruct the transition and a robust European Long-Term Climate Investment Plan (see recommendation 8) can be drawn up, the EU should:

- Increase the quantity of public funding. Higher interest rates, changing political priorities, and the phase-out of Next Generation EU threaten to reduce public funding for the transition. However, more, rather than less public funding is needed, especially in a period in which the transition could face pushback. To avoid thinking in terms of *net contributors* and *net beneficiaries* these funds would ideally be generated by the EU's own resources, e.g., EU ETS revenues.
- Improve the distribution between centralised EU-level and decentralised funding. Member states should consider whether EU-level systems could deploy funds more effectively for aims relating to issues that transcend national borders, e.g., Horizon Europe. Meanwhile, building on the example of the EU Hydrogen Bank, the EU should also make it easier for member states to do this.

8: A European Long-Term Climate Investment Plan to Close the Climate Investment Deficit

For the EU to reach its climate objectives, significant additional investments are needed. An EU climate investment plan can be a solution to close the climate investment deficit at EU level. This EU climate investment plan should:

- Be aligned with the EU long-term strategy (LTS) (see recommendation 3) and describe how it intends to finance identified needs.
- Explain how much EU funding should be mobilized and how. The long-term investment plan will have to explain how the EU intends to finance which sectors of the climate investment deficit. To this end, EU funds must be mobilised more effectively to close this deficit and, if necessary, their volume must be increased (see recommendation 7).
- Explain how much money is expected to come from public budgets at Member States level or even sub-national level, based on Member States' estimation of their NECPs' investment needs.
- Point out options to align subsidies, taxation and fiscal policies with EU climate objectives, in order to provide a clear price signal for private investments.

9: Develop European Green Lead Markets for Climate-Friendly Basic Materials

Green lead markets ensure predictable demand for low-emission products and processes, particularly in basic materials such as steel, cement or fertilisers. Lead markets for such products can reduce uncertainty and incentivise transformative investments into climate-friendly production methods. To foster the emergence of green lead markets, the EU should:

- Develop an EU strategy for creating lead markets for basic materials, streamlining existing processes.
- Work towards common methodologies for calculate the emission intensity of products and associated (dynamic) standards to establish which products qualify as "climate-friendly" or "low-emissions" and can thus be traded on lead markets.
- Use public procurement strategically to create demand for climate-friendly basic materials: To this end, revise the public procurement directives to make the environmentally sustainable option the norm, oblige procuring authorities to take environmental criteria into account and mandate the strategic use of public procurement (by Member States as well as Commission Services).
- Consider the introduction of (tradable) quotas or standards for end products.

10: Prudential Transition Plans for Banks

There is as substantial gap between current banking practices – their lending and investment – and the EU's ambitious climate. The European Banking Authority (EBA) should introduce clear guidelines on prudential transition plans for EU banks to align their investment and lending practices with the Union's climate goals.

- These guidelines should require banks to develop detailed, actionable strategies for decarbonization, setting scientifically credible targets for 2050 and intermediate milestones, tailored by sector.
- The plans should be verified by banking supervisors and their implementation monitored. If implementation proved to be deficient, banking supervisors should prescribe corrective action e.g. through requesting an evolution in the governance and the risk management, prescribing trainings or setting concentration limits that prevent excessive investment in any single sector.

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