



European
Commission

European Union

Public Finance

5th Edition

Budget

European Union

Public Finance

5th Edition

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CONTENTS	
FOREWORD	7
LIST OF ACRONYMS	8
COMMISSIONERS FOR FINANCIAL PROGRAMMING AND BUDGET	14
DIRECTORS GENERAL FOR BUDGET	16
INTRODUCTION	17
PART 1: THE DEVELOPMENT OF THE UNION'S FINANCIAL SYSTEM	19
Chapter 1: The development of an original financial system (1951–75)	20
1. The move towards unification of the budgetary instruments	20
2. Progress towards financial autonomy	21
3. The development of common policies	23
4. The search for a balance between the institutions	23
5. The first enlargement of the European Communities	24
Chapter 2: The crisis in the Community's finances (1975–87)	25
1. The climate of conflict in relations between the institutions	25
2. The question of budget imbalances	29
3. The inadequacy of resources to cover the Community's growing needs	30
4. Enlargements of the European Communities	32
Chapter 3: Reform of the Community's finances: the Delors I package (1988–92)	33
1. From the Delors I package proposals (February 1987) to the decisions in June 1988	33
2. The broad lines of the Community's financial reform	33
3. First assessment of the reform: 1988–92	39
Chapter 4: Consolidation of the 1988 reform: the Delors II package (1993–99)	44
1. The Commission's proposals	44
2. The Edinburgh European Council and the conclusion of the 1993–99 financial package	45
3. Application of the financial framework, 1993–99	50
Chapter 5: Establishment of a stable budgetary base for enlargement of the European Union: the Agenda 2000 package (2000–06)	58
1. The Commission's proposals	59
2. The outcome of the negotiations	63
3. Application of the financial framework, 2000–06	67
Chapter 6: The policy challenges and budgetary means of the enlarged Union: The Multiannual Financial Framework 2007–13	75
1. The Commission's proposals	76
2. The outcome of the negotiations	82
3. The entry into force of the Lisbon Treaty and its legal implications ()	89
4. Application of the financial framework, 2007–13	90
5. The budget review and the report on the functioning of the Interinstitutional Agreement	97

Chapter 7: A budget for Europe 2020 agreed in times of crisis: The Multiannual Financial Framework 2014–20	99
1. The Commission's proposals	101
2. The outcome of the negotiations	109
PART 2: THE CHARACTERISTICS OF THE PRESENT FINANCIAL SYSTEM	117
Chapter 8: The legal framework	118
1. The financial provisions of the Treaties	118
2. Secondary legislation: The Financial Regulation	122
3. Other secondary legislation	125
4. Rules adopted by agreement between the institutions	126
Chapter 9: The financial autonomy of the European Union: the own-resources system	128
1. The legislation on own resources	130
2. The essential characteristics of the present system of own resources	131
Chapter 10: The multiannual financial framework	136
1. Ceilings on expenditure within the financial framework	136
2. Application of the financial framework	138
3. The implications of the financial framework	145
PART 3: ESTABLISHMENT OF THE UNION'S ANNUAL BUDGET	147
Chapter 11: The general principles governing the Union's budget	148
1. The principle of unity	148
2. The principle of accuracy	149
3. The principle of universality	150
4. The principle of annuality	153
5. The principle of equilibrium	159
6. The principle of specification	162
7. The principle of the unit of account	172
8. The principle of transparency	173
9. The principle of sound financial management	174
10. Evaluation of Union action and sound financial management	175
11. Internal control and sound financial management	177
Chapter 12: The annual budgetary procedure	179
1. Introduction	179
2. The stages in the budgetary procedure	180
3. Amending budgets	183
4. Letters of amendment	184
5. Rejection of the budget and the consequences	184
6. Provisions of the Interinstitutional Agreement	186
PART 4: STRUCTURE OF THE UNION'S ANNUAL BUDGET	189
Chapter 13: Revenue	190
1. General overview	190
2. Own resources	191
3. Other revenue	197
4. The budgetary logic of the financing of the European Union	197

Chapter 14: Expenditure by heading	199
1. Introduction	199
2. Headings	202
PART 5: IMPLEMENTATION OF THE UNION'S ANNUAL BUDGET	219
Chapter 15: Implementation	220
1. Assignment of implementing powers	220
2. Implementation of expenditure	223
3. Grants, procurement and prizes	233
4. The system for making available own resources	235
5. Management of cash resources	238
Chapter 16: Bodies set up by the Union with legal personality	240
1. Decentralised agencies	240
2. European Institute of Innovation and Technology	244
3. Executive agencies	244
4. Joint Undertakings	245
Chapter 17: Leverage effect	247
1. Financial Instruments	247
2. EU Trust Funds for external action	250
3. Public-private partnerships	252
PART 6: ACCOUNTING AND CONTROL	255
Chapter 18: Consolidated annual accounts of the European Union	256
1. Content of the financial statements	256
2. The principles and rules governing the accounts	257
3. Accounting policies	258
4. Budgetary accounts	262
5. The accounting closure process	263
Chapter 19: Internal control and external scrutiny of the budget	265
1. Principles	265
2. Internal control in the Commission	266
3. External scrutiny by the European Court of Auditors	270
4. Political control exercised by the European Parliament	274
PART 7: BORROWING, LENDING AND FINANCIAL STABILISATION	281
Chapter 20: Union borrowing and lending operations	282
1. General presentation and development of lending operations	282
2. Characteristics of borrowing and lending instruments	283
3. The guarantee provided by the Union's general budget for borrowing operations	286
4. The relationship between the general budget and borrowing and lending operations and loan guarantees	286
Chapter 21: Instruments providing financial assistance to Member States	292
1. The Balance of Payments Facility	292
2. The European Financial Stabilisation Mechanism	293
3. The European Financial Stability Facility	294
4. European Stability Mechanism	295

PART 8: THE EUROPEAN DEVELOPMENT FUND	297
Chapter 22: The European Development Fund	298
1. The European Development Fund and agreements with the African, Caribbean and Pacific countries	298
2. The resources of the EDF	299
3. The financial regime of the EDF	299
ANNEXES	303
ANNEX 1: TREATY PROVISIONS: ARTICLES 310 TO 325 TFEU	304
ANNEX 2: MFF REGULATION OF 2 DECEMBER 2013	313
ANNEX 3: IIA OF 2 DECEMBER 2013	322
ANNEX 4: COUNCIL DECISION OF 7 JUNE 2007 ON THE SYSTEM OF OWN RESOURCES	334
ANNEX 5: COUNCIL DECISION OF 26 MAY 2014 ON THE SYSTEM OF OWN RESOURCES	340



Foreword

The book you have in front of you, 'European Union Public Finance', brings together a wealth of information about the EU budget.

This fifth edition is being released at the right moment, as we are at the start of the new EU programming period 2014–2020. It is the first multiannual budget established within the new competencies enshrined in the Lisbon Treaty. It also comes out at a time when a new European Commission takes office, charged with using the budgetary resources of the European Union in the best possible way to serve the people of Europe.

The new multiannual financial framework for the years 2014–2020 had to take into account the very difficult economic conditions prevailing in Europe. This has resulted in a financial framework which is, for the first time ever, lower than its predecessors. In short, Europe has to do more than in the past with a smaller budget.

As well as a presentation of the new 2014–2020 multiannual financial framework, this book covers the full history of the EU budget from 1953 on. It also offers an in-depth explanation of the legal framework governing the adoption and management of the EU budget as well as an overview of its structure. Last but not least, it features a detailed overview of the control mechanisms which apply to the EU budget so that it respects sound financial management principles.

This publication provides expert readers with the information needed to gain a more detailed understanding of how the EU budget can contribute to building a competitive and more prosperous Europe. I hope that it will serve as a solid reference work for all those interested in EU budgetary matters.

Kristalina GEORGIEVA
Vice-President for Budget and
Human Resources
European Commission

LIST OF ACRONYMS

I. General acronyms

Acronym	Full name
AAR	Annual Activity Report
ABB	Activity-Based Budgeting
ABM	Activity-Based Management
ACA	Accession Compensatory Amount
ACP States	African, Caribbean and Pacific Group of States
AOD	Authorising Officer by Delegation
APC	Audit Progress Committee
ARTEMIS	Advanced Research and Technology for Embedded Intelligence and Systems
ATM	Air Traffic Management
BoP	Balance of Payments (Facility)
CAP	Common Agricultural Policy
CBRN (risks)	Chemical, Biological, Radiological or Nuclear (risks)
CEF	Connecting Europe Facility
CFP	Common Fisheries Policy
CFSP	Common Foreign and Security Policy
COM	European Commission
COMBUD	Budget Committee of the Council of the European Union
CONT	Committee on Budgetary Control
COREPER	Committee of Permanent Representatives
COSME	Competitiveness of Enterprises and Small and Medium-sized Enterprises
CPM	Civil Protection Mechanism
DAS	Annual Statement of Assurance (French: déclaration d'assurance)
DB	Draft Budget
DCI	Development Cooperation Instrument
EAFRD	European Agricultural Fund for Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
EAR	Emergency Aid Reserve
EaSI	Employment and Social Innovation
EBRD	European Bank for Reconstruction and Development
ECA	European Court of Auditors
ECOFIN	Council of Economics and Finance Ministers
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EDF	European Development Fund
EEA	European Economic Area
EEAS	European External Action Service
EEC	European Economic Community

Acronym	Full name
EERP	European Economic Recovery Plan
EFSM	European Financial Stabilisation Mechanism
EFTA	European Free Trade Association
EGNOS	European Geostationary Navigation Overlay Service
EIDHR	European Instrument for Democracy and Human Rights
EIF	European Investment Fund
EIT	European Institute of Innovation and Technology
EMFF	European and Maritime Fisheries Fund
ENI	European Neighbourhood Instrument
ENIAC	European Nanoelectronics Initiative Advisory Council
EP	European Parliament
EPPO	European Public Prosecutor Office
ERDF	European Regional Development Fund
ESA	European System of Accounts
ESF	European Social Fund
ESIF	European Structural and Investment Funds
ESM	European Stability Mechanism
EU	European Union
EUAV	EU Aid Volunteers (European Voluntary Humanitarian Aid Corps)
EURATOM	European Atomic Energy Community (= EAEC)
FCH	Fuel Cells and Hydrogen
F4E	Fusion For Energy
FFR	Framework Financial Regulation
FIFG	Financial Instrument for Fisheries Guidance
FIFO	First-In, First-Out (inventory evaluation method)
FISIM	Financial Intermediation Services Indirectly Measured
FR	Financial Regulation
FTS	Financial Transparency System
FTT	Financial Transaction Tax
GAAP	Generally Accepted Accounting Principles
GAC	General Affairs Council
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GLONASS	Global Navigation Satellite System
GMES	Global Monitoring for Environment and Security (new name: Copernicus)
GNI	Gross National Income
GNP	Gross National Product
GPS	Global Positioning System
IAC	Internal Audit Capability

Acronym	Full name
IAS	Internal Audit Service
ICI	Instrument for Cooperation with Industrialised Countries
ICI+	Instrument for Cooperation with Industrialised and other High Income Countries
IcSP	Instrument Contributing to Stability and Peace
ICT	Information and Communication Technologies
IfS	Instrument for Stability
IIA	Interinstitutional Agreement
IMP	Integrated Maritime Policy
INSC	Instrument for Nuclear Safety Cooperation
IPA	Instrument for Pre-accession Assistance
IPSAS	International Public Sector Accounting Standards
ITER	International Thermonuclear Experimental Reactor
JU	Joint Undertaking
LGTT	Loan Guarantee Instrument for TEN-T
MFA	Macro-Financial Assistance
MFF	Multiannual Financial Framework
MFFR	Revised Multiannual Financial Framework
MP	Management Plan
NCI	New Community Instrument
NGO	Non-Governmental Organisation
OCTs	Overseas Countries and Territories
OLAF	European Commission Anti-Fraud Office
OP	Publications Office
ORD	Own Resources Decision
PI	Partnership Instrument
PPP	Public-Private Partnership
PS	Programme Statement
RAL	"Reste à liquider" (outstanding unpaid commitments)
RAP	Rules of Application
RFMO	Regional Fisheries Management Organisation
RSFF	Risk-Sharing Finance Facility
SAI	Supreme Audit Institution
SEC	Solution Envisaged by the Commission
SEPA	Single Euro Payments Area
SES	Single European Sky
SESAR	Single European Sky Air Traffic Management research
SFA	Sustainable Fisheries Agreement
SME	Small and Medium Enterprises
SPF	Statement of Preliminary Findings

Acronym	Full name
SWIFT	Society of Worldwide Interbank Financial Telecommunication
TAO	Technical Administrative Support Office (French: BAT)
TCC	Turkish Cypriot community
TEN-T	Trans-European Transport Network
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
TOR	Traditional Own Resources
UCLAF	European Commission's Task Force for the Coordination of the Fight against Fraud
VAT	Value-Added Tax
WTO	World Trade Organisation

II. ISO Country Codes

Acronym	Full name
AT	Austria
BE	Belgium
BG	Bulgaria
CY	Cyprus
CZ	Czech Republic
DE	Germany
DK	Denmark
EE	Estonia
IE	Ireland
EL	Greece
ES	Spain
FI	Finland
FR	France
HR	Croatia
HU	Hungary
IT	Italy
LT	Lithuania
LU	Luxembourg
LV	Latvia
MT	Malta
NL	The Netherlands
PL	Poland
PT	Portugal
RO	Romania
SE	Sweden
SI	Slovenia

Acronym	Full name
SK	Slovakia
UK	United Kingdom

III. Decentralised agencies

Acronym	Full name
ECHA	European Chemicals Agency
EASA	European Aviation Safety Agency
EMA	European Medicine Agency
EBA	European Banking Authority
EIOPA	European Insurance and Occupational Pensions Authority
ESMA	European Securities and Markets Authority
EUROFOUND	European Foundation for the Improvement of Living and Working Conditions
EU-OSHA	European Agency for Occupational Safety and Health
ERA	European Railway Agency
CEDEFOP	European Centre for the Development of Vocational Training
EIGE	European Institute for Gender Equality
EEA	European Environment Agency
EFCA	European Fisheries Control Agency
EUROPOL	European Police Office
CEPOL	European Police College
EMCDDA	European Monitoring Centre for Drugs and Drug Addiction
ECDC	European Centre for Disease Prevention and Control
EFSA	European Food Safety Authority
ETF	European Training Foundation
GSA	European GNSS Supervisory Authority
EMSA	European Maritime Safety Agency
ENISA	European Network and Information Security Agency
ACER	Agency for the Cooperation of Energy Regulators
FRONTEX	European Agency for the Management of Operational Cooperation at the External Borders of the Member States of the EU
EUROJUST	European Union's Judicial Cooperation Unit
BEREC	Office for the Body of European Regulators for Electronic Communications
EASO	European Asylum Support Office
IT Agency (Eu. LISA)	European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice
FRA	Fundamental Rights Agency
CdT	Translation Centre for the bodies of the EU
OHIM	Office for Harmonisation in the Internal Market
CPVO	Community Plant Variety Office

IV. Executive agencies

6 agencies, of which 3 obtained new names in 2014

Acronym	Full name
CHAFEA	Consumers, Health and Food Executive Agency (former EAHC)
EACEA	Education, Audiovisual and Culture Executive Agency
EACI	Executive Agency for Competitiveness and Innovation (new name: EASME)
EAHC	Executive Agency for Health and Consumers (new name: CHAFEA)
EASME	Executive Agency for Small and Medium-sized Enterprises (former EACI)
ERCEA	European Research Council Executive Agency
INEA	Innovation and Networks Executive Agency (former TEN-T EA)
REA	Research Executive Agency
TEN-T EA	Trans-European Transport Network Executive Agency (new name: INEA)

V. Joint Undertakings (JUs)

Acronym	Full name
BBI JU	The Bio-based Industries Joint Undertaking
Clean Sky 2 JU	Clean Sky 2 Joint Undertaking
ECSEL JU	Electronic Components and Systems for European Leadership Joint Undertaking
FCH2 JU	Fuel Cells and Hydrogen 2 Joint Undertaking
IMI2 JU	Innovative Medicines Initiative 2 Joint Undertaking
SJU	SESAR Joint Undertaking
S2R JU	Shift2Rail Joint Undertaking

COMMISSIONERS FOR FINANCIAL PROGRAMMING AND BUDGET

Albert Coppé
1967-1973



Claude Cheysson
1973-1977



Christopher Tugendhat
1977-1985



Henning Christophersen
1985-1989



Peter Schmidhuber
1989-1995



Erkki Liikanen
1995-1999



Michaele Schreyer
1999-2004



Markos Kyprianou
2004



Dalia Grybauskaitė
2004-2009



Algirdas Šemeta
2009-2010



Janusz Lewandowski
2010-2014



Jacek Dominik
2014



Kristalina Georgieva
Since 2014

DIRECTORS GENERAL FOR BUDGET

Lamberto Lambert
1968-1969



Jozef van Gronsveld
1969-1977



Daniel Strasser
1977-1986



Jean-Claude Morel
1986-1989



Jean-Paul Mingasson
1989-2002



Luis Romero Requena
2002-2009



Hervé Jouanjean
2009-2014



Nadia Calviño
Since 2014

Introduction

This document is divided into eight parts dealing with the various aspects of the European Union's system of public finance.

Part 1: The development of the Union's financial system looks back at the series of reforms throughout the history of the European Union, which together have produced the present system. Starting from the entirely novel system as it was first established (Chapter 1), it reviews the crisis in the Community's finances (Chapter 2), followed by the thorough overhaul at the end of the 1980s (Chapter 3) and the consolidation of the 1988 reform during the 1990s (Chapter 4). Chapters 5 to 7 look at the subsequent multiannual financial frameworks up to the current one.

Part 2: The characteristics of the present financial system sketch out the legal framework for the Union's budget and financing system (Chapter 8), before looking in more detail at the Union's system of own resources (Chapter 9) and at the purpose and content of the multiannual financial framework (Chapter 10).

Part 3: Establishment of the Union's annual budget describes the general principles governing the Union's budget (Chapter 11) which, in order to maintain a balance between the prerogatives of the institutions, underlie the annual budgetary procedure (Chapter 12).

Part 4: Structure of the Union's annual budget gives details of the major types of European Union revenue and expenditure. Whilst the financing system is based on a simple basket of resources (four main categories) its operation is complex, not least as a result of the arrangements which have been made to correct certain imbalances in the net positions of the Member States (Chapter 13). Chapter 14 presents the main expenditure categories broken down by headings of the multiannual financial framework.

Once the budget has been voted, the amount entered must be spent in accordance with the rules and in a cost-effective manner. The mechanisms for achieving this are set out in **Part 5: Implementation of the Union's annual budget** and **Part 6: Accounting and control**. Chapter 15 presents the main rules governing budget implementation. This is followed by a presentation of the bodies set up by the Union with legal personality (Chapter 16) and some of the key instruments by which the Union's budget can leverage additional public and private funds (Chapter 17). A broad description of the Union's accounting system is given in Chapter 18, whereas the internal control in the Commission and the arrangements for the external scrutiny of Union spending by the Court of Auditors and the European Parliament are presented in Chapter 19.

Part 7 on Borrowing, lending and financial stabilisation presents the Union's borrowing and lending operations (Chapter 20) and the Instruments providing financial assistance to the Member States, including the recent developments in the aftermath of the severe financial crisis which hit the Union in 2008 and during the following years (Chapter 21).

Finally, **Part 8**, Chapter 22 presents the European Development Fund.

In the **Annexes** the most important official documents are presented to which reference has been made throughout the above-mentioned Chapters.

Part 1

The development of the Union's financial system



Chapter 1

The development of an original financial system (1951–75)

A number of major developments marked the Community's financial system during its first 20 years of existence:

- the move towards the unification of the budgetary instruments;
- progress towards the financial autonomy of the Community;
- the development of common policies;
- the search for a balance between the institutions in the exercise of powers over the budget;
- the first enlargement of the European Communities.

These are examined in turn.

1. The move towards unification of the budgetary instruments

The creation, within a few years, of the European Coal and Steel Community, the European Economic Community and the European Atomic Energy Community led to the co-existence of a number of separate budgets for European policies.

- The 1951 ECSC Treaty ⁽¹⁾ provided for an administrative budget and an operating budget.
- The 1957 EEC Treaty ⁽²⁾ established a single budget.
- The 1957 Euratom Treaty set up an administrative budget and a research and investment budget.

Subsequently, an important effort was undertaken to unify and simplify the European institutions and, notably, their budgets.

- The 1965 Merger Treaty incorporated the ECSC and Euratom administrative budgets into the EEC budget. This Treaty replaced the three Councils of Ministers (EEC, ECSC and Euratom) and the two Commissions (EEC, Euratom) and the High Authority (ECSC) with a single Council and a single Commission, respectively. This administrative merger was supplemented by the institution of a single operative budget.
- The 1970 Luxembourg Treaty incorporated the Euratom research and investment budget into the general budget. This Treaty replaced the system whereby the Communities were

⁽¹⁾ The Treaty establishing the European Coal and Steel Community was signed in Paris on 18 April 1951 and entered into force on 24 July 1952, with a validity period limited to 50 years. The Treaty expired on 23 July 2002 after being amended on various occasions.

⁽²⁾ The 'Treaties of Rome' were signed in Rome in March 1957. The first Treaty established the European Economic Community (EEC) and the second the European Atomic Energy Community, better known as Euratom. These two Treaties entered into force on 1 January 1958.

funded by contributions from Member States with that of own resources. It also put in place a single budget for the Communities.

- The expiry of the ECSC Treaty in 2002 further simplified the budget of Community institutions. Between 1970 and 2002 two budgets co-existed: the general budget and the ECSC operating budget. The rules of the Treaty establishing the European Community have applied to the coal and steel trade since the expiry of the ECSC Treaty. A protocol on the financial consequences of the expiry of the ECSC Treaty and on the research fund for coal and steel is annexed to the Treaty of Nice (2001). This protocol provides for the transfer of all the assets and liabilities of the ECSC to the European Community and for the use of the net worth of these assets and liabilities for research in sectors related to the coal and steel industry.

2. Progress towards financial autonomy

2.1. ECSC

The original 1951 Paris Treaty gave the ECSC financial autonomy. Article 49 of the Treaty stated that ‘the High Authority is empowered to procure the funds it requires to carry out its tasks:

- by imposing levies on the production of coal and steel;
- by contracting loans.’

Further provisions of the ECSC Treaty defined which expenditure could be undertaken with the levies. The Treaty stipulated that the levies should be assessed annually on the various products according to their average value and that the rate thereof should ‘not exceed 1 % unless previously authorised by the Council, acting by a two-thirds majority’. The Treaty also stated that ‘the mode of assessment and collection shall be determined by a general decision of the High Authority taken after consulting the Council’ ⁽¹⁾.

In other words, the High Authority was granted extensive autonomy as to decisions regarding levies, within the limits laid out by the Treaty.

Since the 1965 Merger Treaty, the ECSC administrative budget has been incorporated into the general budget. The operating budget alone continued being treated separately until the Treaty expired in 2002, but in practical terms this became less and less significant as the levy yield diminished.

2.2. General budget

From 1958 to 1970 the EEC budget and the Euratom budget (and, from 1965 onwards, the ECSC administrative budget) were financed by a system of Member State contributions.

In addition to imposing an obligation to balance budgets, the EEC Treaty established a ‘scale’ applicable to the financial contributions of Member States (28 % for Germany, France and

⁽¹⁾ See Article 50, ECSC Treaty

Italy, 7.9 % for Belgium and the Netherlands and 0.2 % for Luxembourg), irrespective of any other revenue. At the same time, a different scale was applied for financing the European Social Fund (set up in 1957 by the Treaty of Rome and later reformed in 1971). Unanimity was required to modify these scales.

The Treaty further indicated that the Commission should submit proposals to the Council to replace the contributions of Member States by the Community's own resources, 'in particular by revenue accruing from the common customs tariff' ⁽¹⁾.

The Decision of 21 April 1970 ⁽²⁾ introduced the system of own resources for the general budget, as a progressive 'replacement of financial contributions from Member States', with effect from 1971. Own resources included:

- customs duties, which, in a gradual process lasting from 1971 to 1975, were transferred to the Community;
- agricultural levies, which have been paid in full to the Community since 1971;
- VAT-based revenue (initially limited to a 1 % rate): the Community VAT arrangements were applied gradually as progress was made in harmonising the VAT base (sixth directive in 1977 and ninth directive in 1979).

During the progressive implementation of this new system, financial contributions from the Member States were required to ensure that the budget of the Communities was in balance. However, Article 4 of the decision provided that, 'from 1 January 1975 the budget of the Communities [should], irrespective of other revenue, be financed entirely from the Communities' own resources'.

This would notably entail setting the rate applicable to value added tax 'within the framework of the budgetary procedure', that is, on a yearly basis with potentially frequent changes. In case the rate had not been adopted at the beginning of the financial year, the decision further stated that the rate previously fixed should remain applicable until the entry into force of a new rate.

This own-resources decision, which could not be changed unless unanimity was reached in the Council, thus created a stable basis for financing the Union. The general budget would henceforth not depend on Member State contributions, which could have placed the Community in a state of budgetary, as well as political, dependence on the Member States.

The Decision of 21 April 1970 started applying in 1971 and has been applied in full since 1979. Member States paid transitional contributions to balance the general budget over the period 1971–78, then very small residual contributions from 1979 to 1981 and exceptionally reimbursable and non-reimbursable advances in 1984 and 1985 before the 'balancing' GNP/GNI-based own resource was introduced in 1988 (see Chapter 3).

⁽¹⁾ See Articles 200–201 et seq. of the EEC Treaty (1957).

⁽²⁾ OJ L 94, 28.10.1970, p. 19.

3. The development of common policies

The early achievements were:

- the creation of the European Agricultural Guidance and Guarantee Fund (EAGGF) in April 1962;
- the research policy, initially based on the Euratom Treaty (and therefore confined at the outset to the nuclear field), but since extended to many other fields;
- the reform of the European Social Fund (ESF), set up by the Treaty of Rome in 1971;
- the establishment of the European Regional Development Fund (ERDF) in March 1975.

It is striking to note that the successors to these early programmes still constitute a significant part of the current EU budget.

4. The search for a balance between the institutions

4.1. ECSC budget

The 1951 Treaty of Paris provided that decision-making powers on budgetary matters were all exercised by the High Authority and an auditor was appointed for the purposes of budget control.

The 1975 Treaty of Brussels assigned budget control powers to the Court of Auditors.

4.2. General budget

Under the 1957 Treaties of Rome EEC and Euratom budget decisions were the exclusive prerogative of the Council, the sole budgetary authority. In practice, the institutions were responsible for the various stages of the budgetary procedure as follows:

- establishment of the preliminary draft budget: the Commission;
- adoption of budget: the Council, after consulting the Parliament;
- implementation of budget: the Commission;
- discharge: the Council.

Budget control was exercised by an autonomous body: the Audit Board.

The 1970 Luxembourg Treaty made the following changes to budgetary decision-making powers:

- introduction of the distinction between compulsory expenditure and non-compulsory expenditure;
- power to adopt the budget attributed to the Parliament, but not the power to decide (the last word) on non-compulsory expenditure;
- budgetary discharge given by joint Council/Parliament decision.

The next stage was the 1975 Brussels Treaty, which laid down the main rules applicable until the entry into force of the Lisbon Treaty ⁽¹⁾:

- decision-making powers on budgetary matters are shared between the Council and Parliament, which henceforth form the two arms of the budgetary authority. In this new legal set-up, Parliament has the last word on non-compulsory expenditure, can reject the budget, and acts alone in granting discharge.
- budget control is exercised by the Court of Auditors, which replaced the Audit Board from 1976 onwards.

5. The first enlargement of the European Communities

The first enlargement occurred on 1 January 1973 when three new Member States — the United Kingdom, Denmark and Ireland — joined the Communities. Accession negotiations were also held with Norway, which even signed the Accession Treaty ⁽²⁾ but eventually refused to accede, for the first time ⁽³⁾.

The enlargement coincided with the gradual implementation of the first own-resources decision and the new Member States had to respect its provisions. But their payments were phased in (45 % in 1973, 56 % in 1974, 67.5 % in 1976 and 92 % in 1977) to reach the total amounts due in 1978. For the United Kingdom a first correction was agreed in 1975 and was gradually introduced from 1976 (see Chapter 2).

The payments in these years consisted only of traditional own resources and financial contributions from the Member States needed to balance the budget and other specific contributions to finance some supplementary programmes. The VAT-based resource was paid for the first time in 1979 as described in Section 2.2 above.

⁽¹⁾ The changes to the budgetary procedure introduced by the Lisbon Treaty are discussed in Chapters 8 and 10.

⁽²⁾ OJ L 73, 27.3.1972.

⁽³⁾ The same situation occurred during the 1995 enlargement.

Chapter 2

The crisis in the Community's finances (1975–87)

The legal, political and institutional balance in the Community's financial arrangements established in the early 1970s was gradually upset over the next 10 years.

Relations among Member States and between the European institutions became increasingly strained during this period and the situation gradually degenerated into open conflict. As a result, the operation of the budgetary decision-making process became extremely difficult between 1980 and 1988 and the series of incidents was unending: numerous actions or counter-actions before the Court of Justice brought by the Council, the Commission or some Member States; delays in the adoption of the budget; rejection of the budget by Parliament; and the application of makeshift solutions, such as advances or special contributions, in order to finance expenditure. The budgets for 1980, 1985, 1986 and 1988 were not adopted until the financial year was well under way, so that the provisional-twelfths arrangements had to be applied for periods of five to six months.

There were three reasons for this state of affairs:

- the climate of conflict in relations between the institutions;
- the question of budgetary imbalances;
- the inadequacy of resources to cover the Community's growing needs.

1. The climate of conflict in relations between the institutions

The institutional arrangements for power-sharing between the Council and Parliament established from 1975 onwards proved difficult to implement, for two main reasons: first, some of the criteria applied were not defined in enough detail, were open to different interpretations or were difficult to adapt to changing developments in the Community budget — this was for instance the case for provisions related to compulsory vs non-compulsory expenditure; second, no specific procedures were laid down for resolving any conflicts that might arise by applying conciliation mechanisms or imposing solutions in the absence of agreement.

Moreover, the increased legitimacy and influence enjoyed by Parliament following the direct elections in June 1979 (Act signed in Brussels in September 1976) placed a constant strain on its relations with the Council in budgetary matters.

Nevertheless, the institutions concerned did establish a dialogue to try to overcome these difficulties, leading among other things to the joint declaration by the European Parliament, the Council and the Commission of 30 June 1982 on various measures to improve the budgetary procedure ⁽¹⁾. But these attempts, which prefigured the first Interinstitutional Agreement concluded in 1988 ⁽²⁾, proved to be somewhat makeshift.

⁽¹⁾ OJ C 194, 28.7.1982, p. 1.

⁽²⁾ See Chapter 3.

1.1. The distinction between compulsory and non-compulsory expenditure

Compulsory expenditure was defined in Article 272(4) of the EC Treaty as 'expenditure necessarily resulting from this Treaty or from acts adopted in accordance therewith', other expenditure being considered by contrast as non-compulsory. Such a distinction, which is in fact used in a number of national budget systems, can be useful when drawing up a budget in order to assess whether, in the light of the legislation, different categories of expenditure are more or less indispensable or, on the contrary, discretionary.

In terms of the Community budget, the problem was that, while technical and vaguely defined, this criterion had major institutional implications, since it determined the breakdown of budgetary responsibilities between the Council and Parliament and the basic framework for Parliament's own budgetary powers ⁽¹⁾.

1) The breakdown of budgetary responsibilities

Under the budgetary procedure laid down in Article 272, the Commission drew up its preliminary draft budget, which then passed back and forth between the two arms of the budgetary authority: first, the Council established the draft budget, which was then given two alternative readings by each of the institutions. The Council had the final say over compulsory expenditure, the amount of which was fixed at its second reading, while Parliament had the last word on the volume of non-compulsory expenditure at its final reading of the draft budget.

The Treaty did not provide for any mechanisms to overcome disagreement between the two institutions on applying the distinction between the two types of expenditure, which was nevertheless crucial for the demarcation of their respective budgetary powers.

2) The framework for Parliament's budgetary powers

However, there were limits on Parliament's power to set the final total of non-compulsory expenditure. Without prejudice to the constraints imposed by the volume of own resources available and the need to maintain strict budgetary balance, Article 272(9) laid down a maximum rate of increase for such expenditure in relation to expenditure of the same type to be incurred during the current year. The Commission determined this maximum rate on the basis of objective economic parameters.

There were two cases where the maximum rate of increase could be relaxed. If the rate of increase resulting from the draft budget established by the Council was over half the maximum rate, Parliament could further increase the volume of non-compulsory expenditure up to half of the maximum rate. The maximum rate could also be exceeded by agreement between the Council and Parliament. However, there were three potential problems with this mechanism with regard to the exercise of budgetary powers:

- The classification of expenditure for a given financial year determined not only the extent of Parliament's power in establishing the budget for that year, but also the actual margin

⁽¹⁾ The Lisbon Treaty has eliminated the distinction between compulsory and non-compulsory expenditure. For the new legal framework and the budgetary procedure resulting from it see Chapters 8, 10 and 12).

for manoeuvre enjoyed by Parliament in the next financial year or even subsequent years, since it served as a basis for applying the maximum rate of increase.

- The method of calculating the maximum rate of increase was not directly or immediately tied to changes in actual budgetary requirements arising, for example, from the introduction of new policies or, more drastically, from enlargement of the Community.
- There were no Treaty provisions laying down at exactly which stage of the budgetary procedure agreement was to be reached on exceeding the maximum rate of increase, or how that agreement was to be reached.

3) *The 1982 joint declaration*

In order to improve the budgetary procedure, the European Parliament, the Council and the Commission made a joint declaration on 30 June 1982 ⁽¹⁾.

The declaration defined compulsory expenditure as such expenditure the budgetary authority is obliged to enter in the budget to enable the Community to meet its obligations, both internally and externally, under the Treaties and acts adopted in accordance with the Treaties.

Annexed to the declaration was a list of all the then-existing budget lines, classified as compulsory or non-compulsory. A new procedure (the 'trilogue' between the Presidents of the three institutions) was introduced to determine the classification of new budget lines or existing lines for which the legal basis had changed.

The declaration also specified that the Commission should propose a classification of expenditure in its preliminary draft. If either arm of the budgetary authority could not agree with this classification, the Presidents would hold a trilogue meeting and endeavour to resolve the matter before the draft budget was established.

The declaration also laid down some rules for applying the maximum rate of increase: the basis for calculating the Parliament's margin of manoeuvre would be the draft budget established by the Council at its first reading, including any letters of amendment; the maximum rate of increase should be observed not only in the initial budget but also in supplementary or amending budgets for the same financial year; the rules on exceeding the maximum rate may be applied differently to appropriations for payments and appropriations for commitments.

In these respects, the 1982 declaration proved effective in the first few years following its adoption. However, disputes over the classification of expenditure and the maximum-rate-of-increase mechanism resurfaced in 1986, when the Community had to meet requirements arising from the accession of Spain and Portugal. In the absence of agreement between the two arms of the budgetary authority, the Council brought an action before the Court of Justice, which subsequently annulled the budget for the 1986 financial year.

⁽¹⁾ Joint declaration by the European Parliament, the Council and the Commission of 30 June 1982 on various measures to improve the budgetary procedure (OJ C 194, 28.7.1982, p. 1).

1.2. The clash between legislative power and budgetary power

The EEC and Euratom Treaties themselves contained the seeds of the dispute between the Council and Parliament from 1975 to 1982; while legislative power was vested exclusively in the Council, budgetary power was shared between the Council and Parliament.

Prior to this, when the Council — the legislative body — was the sole authority (up to and including the 1974 budget), powers over both fields were vested in a single institution, and so in practice no significant conflicts could arise.

After acquiring its budgetary powers, the Parliament took the view that the budget by itself was a sufficient legal basis for using the appropriations entered. So from the 1975 budget onwards, it inserted many new budget lines and entered appropriations which could sometimes be used to start up new actions; the amounts increased over the years.

For its part, the Council developed a practice of setting maximum amounts for relevant expenditure in the legislative instruments it adopted. Parliament argued that this had the effect of encroaching on its own budgetary powers over non-compulsory expenditure.

The joint declaration of 30 June 1982 also set out to find a compromise solution to this dispute.

The declaration laid down the principle that ‘in order that the full importance of the budget procedure may be preserved, the fixing of maximum amounts by regulation must be avoided’.

On the other hand, in this joint declaration, the Parliament, the Council and the Commission acknowledged that a legal basis separate from the budget was required for the utilisation of appropriations for any ‘significant action’: if such appropriations were entered into the budget before a proposal for a regulation had been presented, the Commission would present this proposal, and the Council and Parliament would then endeavour to adopt it as quickly as possible.

Implementation of these aspects of the declaration proved rather disappointing in practice.

- The ‘maximum amounts’ were, in practice, replaced by ‘amounts deemed necessary’, which the Council entered systematically in multiannual programmes. This new concept might appear legitimate if construed as representing purely indicative estimates of the budgetary implications of the action carried out. In reality it was interpreted differently by the two institutions. The Council saw these amounts as ceilings on expenditure set by the legislator, whereas the Parliament tended to consider them as minimum levels, which it could top up with additional allocations in line with its own priorities.
- As regards the need to have a legal base in order to utilise appropriations, the agreement implied that there was a consensus between the institutions on what was meant by ‘significant action’. In reality, there was a tendency in a number of fields to artificially prolong the preparatory measures that required no legal base, even though the projects in question had moved on to the operational stage.

2. The question of budget imbalances

Debates on budgetary imbalances in the 1970s and 1980s mainly evolved around the contributions of two net contributors, namely the United Kingdom and Germany.

2.1. The British issue

1) *The origin of the budgetary imbalance*

At the time of its accession, the UK had a per capita GDP well below the Community average.

Secondly, it had a small agricultural sector with a large proportion of farm products imported from outside the Community. As a result, very little of the Community's agricultural spending — which at that time represented the bulk of EU spending — benefited the UK.

And thirdly, the UK contributed a relatively large amount to the financing of the Community budget mainly because its VAT base represented a higher percentage of GNP compared to other Member States.

This structural imbalance in the UK's financial links with the Community became a major political headache for the Community as early as 1974. It was the issue underlying the 1975 referendum on the question of the UK's continued membership of the Community.

2) *Various arrangements introduced to resolve this matter*

A first correcting mechanism was agreed at the European Council meeting in Dublin in March 1975. It was formally enforced from 1976 to 1980. This mechanism was to provide compensation (in the form of a partial repayment of the VAT-based contribution) from the Community budget to any country bearing an unacceptable financial burden. It was to be triggered if three indicators coincided: per-capita GDP below 85 % of the Community average; a rate of growth less than 120 % of the Community average and a share of own-resources payments exceeding by 10 % the share of total Community GDP. The mechanism was never triggered.

A second correcting mechanism was agreed at the Dublin European Council in November 1979 ⁽¹⁾. It provided for a complex compensation mechanism limiting the UK's contribution to the Community budget.

Finally, a third compensation mechanism, applied to the UK contribution to Community revenue, was agreed at the Fontainebleau European Council in June 1984 and given effect by the Decision of 7 May 1985 ⁽²⁾.

This decision covered two distinct arrangements:

- For 1985, compensation was provided through an ECU 1 billion reduction of the UK VAT-based contribution.

⁽¹⁾ Council conclusions of 30 May 1980 on the United Kingdom contribution to the financing of the Community budget, Bulletin EC 5–1980.

⁽²⁾ OJ L 128, 14.5.1985.

- From 1986 onwards, two-thirds (66 %) of the difference between the UK share in VAT bases and its share of total allocated expenditure, applied to total allocated expenditure, was refunded to the UK by way of a reduction in the UK VAT-based payments. This was financed by all the other Member States, in accordance with their respective percentage share of VAT-based payments (with the exception of Germany, which paid only two thirds of its normal share, the balance being divided between the other Member States on the same scale).

2.2. The German issue

From 1981 onwards, Germany highlighted its position as the main contributor to the Community budget and demanded a reduction in its share of financing the rebate to the United Kingdom. The Fontainebleau Arrangement catered for this demand by making a one-third reduction in Germany's share of financing the rebate.

3. The inadequacy of resources to cover the Community's growing needs

3.1. The sources of the problem

1) *The erosion of own resources*

The erosion of own resources was an initial cause of the inadequacy of revenue. It was produced by the combination of two developments:

- The diminishing yield of traditional own resources (customs duties and agricultural levies) as a result of the progress made in dismantling tariffs under the international General Agreement on Tariffs and Trade (GATT) and the Community's increasing self-sufficiency in food and its impact on imports of agricultural products;
- The relative stagnation of VAT-based revenue, limited by a maximum rate of call, in relation to economic activity because of the declining share of GNP accounted for by consumer expenditure in the economies of Community countries.

2) *The rise in expenditure*

The rise in expenditure, triggered by four different factors, was the main reason why resources were increasingly unable to keep pace with the Community's needs.

- A number of existing policies were strengthened. This was in particular the case with the revision of the European Social Fund in October 1983 and the European Regional Development Fund in June 1984.
- New policies were being launched. These included a common fisheries policy, with a common organisation of the market in that sector, in December 1981, and the establishment in 1983 of a Community system of authorised quota (total allowable catches); the establishment of the first framework programme (1984–87) for Community research; the decision taken in February 1984 on new programmes and new arrangements for Community aid to research (Esprit); and the introduction of the Integrated Mediterranean programmes in July 1985.

- Inability to contain Community agricultural expenditure. Between 1982 and 1986 actual expenditure under the EAGGF Guarantee Section grew by an average of 16 % per year and systematically exceeded the estimates made in drawing up the preliminary draft budget.
- The financial impact of the accession of new members to the Community. Greece (member since 1981) and Spain and Portugal (members since 1986) were net beneficiaries from the Community budget.

3.2. The initial attempts at a solution and their limitations

1) Moves to raise additional Community resources (1984–86)

The period after 1984 was one of insecurity for the financing of the Community. The action taken to adjust the level of revenue to expenditure requirements tended to be passive, late and makeshift (e.g. the intergovernmental advances).

From the start of the 1984 budgetary procedure it was clear that the VAT-based resources available within the 1 % limit would not be sufficient to cover the real needs during the year.

Political agreement was reached at the Fontainebleau European Council in June 1984 on the principle of raising the VAT ceiling to 1.4 %. This agreement was given practical shape in the Decision of 7 May 1985 and took effect on 1 January 1986.

In the meantime, transitional financing solutions were applied for the budgets in 1984 (repayable intergovernmental advances outside the VAT ceiling) and 1985 (non-repayable advances).

The final outturn of the 1986 budget was virtually at the 1.4 % VAT limit. The balance was only maintained because certain items of agricultural expenditure were deferred to 1987.

The problem of the exhaustion of VAT resources under the 1.4 % ceiling became acute in 1987. To cover ECU 4 billion in excess agricultural requirements, two months' payments of EAGGF advances had to be deferred.

2) The outlines of budgetary discipline and the first disappointing results

Budgetary discipline was the second type of response to the various constraints affecting the Community's finances.

The first move came on 22 March 1979 when the Council agreed on an internal code of conduct ⁽¹⁾ to guide its decisions so that it would unilaterally restrict the growth of non-compulsory expenditure: the draft budget was to be established on its first reading within half of the maximum rate of increase, in order to limit the impact of the Parliament's margin of manoeuvre during the subsequent stages of the budgetary procedure.

The Fontainebleau European Council in June 1984 extended the scope of budgetary discipline. The Decision of 4 December 1984 ⁽²⁾, the first reference instrument on budgetary discipline,

⁽¹⁾ Bulletin EC 3-1979, point 2.3.2.

⁽²⁾ Bulletin EC 12-1984, point 1.3.3.

transformed the Fontainebleau guidelines into rules, the main ones being that EAGGF Guarantee expenditure should not increase faster than the own-resources base and the increase in non-compulsory expenditure should be kept below the maximum rate provided for by the Treaty (confirmation of the 1979 code of conduct).

These rules, however, turned out to have hardly any practical effect because of the growing disputes between the Council and Parliament (the Parliament refused to recognise the decision on budgetary discipline, which it considered a unilateral act binding solely on the Council) and the fragmentation of the decision-making process in the Council in its various compositions (particularly the reluctance of the agriculture ministers to accept the budgetary discipline arrangements for agricultural expenditure laid down by the finance ministers).

4. Enlargements of the European Communities

In the period described in this chapter two successive enlargements took place. Greece joined the Community on 1 January 1981, and Portugal and Spain on 1 January 1986.

All three Member States benefited from transitional measures in relation to the own resources based on VAT or GNP payments (applied for the Member States that did not have VAT bases in compliance with the Sixth Council Directive). Although they were obliged to pay these own resources in full from the first day of accession, they were immediately refunded by the percentages agreed in the relevant articles of the Accession Treaties ⁽¹⁾. In practice this meant reducing their payments.

The scenarios for the two enlargements were slightly different. In practice, Greece paid 30 % of its contributions in 1981, 50 % in 1982, 70 % in 1983, 80 % in 1984, 90 % in 1985 and 100 % from 1986 onwards. The scenario for the other two acceding Member States was more favourable to the new acceding countries, requiring Spain and Portugal to pay 13 % in 1986, 30 % in 1987, 45 % in 1988, 60 % in 1989, 75 % in 1990, 95 % in 1991 and 100 % from 1992. However, these reductions in payments for Spain and Portugal did not apply to their contribution to the financing of the UK rebate introduced by the own-resources decision of 7 May 1985.

The accession of Spain and Portugal had a significant impact on the expenditure side of the Community budget. This aspect of the third enlargement is developed in the following chapter.

⁽¹⁾ For Greece OJ L 291, 19.11.1979, p. 47. For Spain and Portugal OJ L 302, 15.11.1985, pp. 80 and 134.

Chapter 3

Reform of the Community's finances: the Delors I package (1988–92)

1. From the Delors I package proposals (February 1987) to the decisions in June 1988

The third enlargement in 1986 and the conclusion of the Single Act provided the Community with a new political stimulus. The accession of Spain and Portugal and a treaty which defined fresh ambitions for the enlarged Community (single market, economic and social cohesion, research framework programme) both provided a political base for a thorough reform of the Community's financial system.

In February 1987, the Commission presented comprehensive reform proposals, the Delors package, in two communications:

- the Single Act: A new frontier for Europe (COM(87) 100);
- report on the financing of the Community budget (COM(87) 101).

In the second half of 1987, the Commission produced a series of specific proposals on agricultural policy and the Structural Funds, as well as the general budgetary and financial framework (new own resources, amendment of the Financial Regulation, budgetary discipline and the correction of budgetary imbalances).

The Brussels European Council on 11 and 12 February 1988 adopted the broad lines of the financial reform of the Community. This reform covered three main political points. First of all, it was agreed that the Community should be given additional resources to enable it to operate properly during the period from 1988 to 92. In return, undertakings were given at the highest level concerning the overall distribution of the expenditure to be financed by these new resources: priority would be given to the cohesion policies, and budgetary discipline arrangements would be introduced to place an effective brake on agricultural expenditure.

Lastly, a more equitable system of financing the Community would be introduced, linking Member States' budget contributions more closely to their level of relative prosperity.

Most of the decisions giving practical effect to the conclusions of the Brussels European Council were formally adopted on 24 June 1988.

2. The broad lines of the Community's financial reform

2.1. Own resources

The February 1988 Brussels European Council agreed that the Community should be given suitable resources that would be sufficient, stable and guaranteed, and enable it to operate correctly throughout the period from 1988 to 1992.

The practical details for achieving this were contained in Council Decision 88/376/EEC, Euratom of 24 June 1988 ⁽¹⁾.

1) A new concept: the global own-resources ceiling

The total amount of available own resources was no longer determined by the yield of traditional own resources combined with the ceiling of the VAT-based resource, but was expressed as a percentage of the Community's total GNP, increasing from 1.15 % for 1988 to 1.20 % for 1992.

A further overall ceiling of 1.30 % of total Community GNP was set for 1992 in terms of appropriations for commitments.

2) The new own resources

The range of own resources was extended and the rules altered.

- The system of 'traditional' own resources was rationalised: customs duties on products covered by the ECSC Treaty were added to the common customs tariff duties; the 10 % collection costs were now to be deducted at source and no longer reimbursed separately and charged to the expenditure side.
- The arrangement for the VAT-based own resource was adjusted to better take into account the regressive nature of VAT (differences in the proportion of Member States' GNP accounted for by consumption). The VAT-based resource continued to be established by applying a 1.4 % rate to the uniform VAT base for all Member States, as determined by the Community rules. In addition, a 'capping' mechanism was introduced whereby a Member State's VAT base was not to exceed 55 % of its GNP at market prices.
- A new category of revenue — the fourth resource — was introduced, based on Member States' GNP, the most representative indicator of their economic activity, in order to match each Member State's payments more closely to its ability to pay. From now on, this 'balancing item' automatically provided the necessary financing for the Community budget, within the limit of the own-resources ceiling. It was calculated by applying to a base, made up of the sum of the Member States' gross national product at market prices, a rate to be determined during the budgetary procedure in the light of the yield of all the other categories of own resources.

3) Correction of budgetary imbalances

The UK correction was adjusted to neutralise the impact of the new elements in the system of own resources (VAT base capped at 55 % of GNP and the introduction of a fourth resource based on GNP). Indeed, the very objective of the June 1988 Decision was that the position of the United Kingdom should be exactly the same as it would have been if the Decision of 7 May 1985 had continued to apply (with VAT call-in rates above 1.4 %).

⁽¹⁾ OJ L 185, 15.7.1988, p. 24.

In technical terms, the amount of compensation was calculated as follows ⁽¹⁾:

- The amount was calculated in accordance with the Decision of 7 May 1985 on the assumption that the budget was to be financed in full by non-capped VAT;
- From this result was subtracted the saving which the United Kingdom enjoyed because of the capping of the VAT base at 55 % of GNP and the introduction of the fourth resource;
- The United Kingdom received the correction calculated in this way in the form of a reduction in its VAT payments.

The other 11 countries no longer financed this compensation in proportion to their VAT bases, but in proportion to their GNP. Germany was still allowed a one-third reduction of the amount it was supposed to pay.

2.2. Budgetary discipline

The European Council laid down the principles for tighter budgetary discipline in order to produce a better balance between the different categories of Community budget expenditure and to control their growth. Two documents, with different legal status, implemented these principles:

- Council Decision 88/377/EEC of 24 June 1988 concerning budgetary discipline ⁽²⁾;
- the Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure, signed by the European Parliament, the Council and the Commission on 29 June 1988 ⁽³⁾.

The new discipline arrangements covered all categories of expenditure and were binding on all the institutions associated in their operation: the Interinstitutional Agreement made budgetary discipline the shared responsibility of the three institutions party to it, without encroaching on the powers vested in them by the Treaties.

1) The financial perspective 1988–92

The financial perspective 1988–92 (see Table 3.1), an integral part of the Interinstitutional Agreement, was the key to the new budgetary discipline arrangements. It was designed to produce harmonious and controlled growth in the broad sectors of budget expenditure, while at the same time establishing a new balance in the allocation of expenditure by means of the guarantees for the development of policies connected with the Single Act and in particular the structural policies.

Subject to the technical adjustment and revision procedures provided for in the Interinstitutional Agreement, the European Parliament, the Council and the Commission accepted that the financial amounts set in this perspective were to be regarded as binding expenditure ceilings for the Community.

⁽¹⁾ A detailed description of the method for calculating the UK correction is provided in Chapter 13.

⁽²⁾ OJ L 185, 15.7.1988, p. 29.

⁽³⁾ OJ L 185, 15.7.1988, p. 33.

TABLE 3.1 – *Financial perspective 1988–92 (Interinstitutional Agreement of 29 June 1993 on budgetary discipline and improvement of the budgetary procedure)**(million ECU at 1988 prices)*

Appropriations for commitments	1988	1989	1990	1991	1992
1. EAGGF Guarantee	27 500	27 700	28 400	29 000	29 600
2. Structural operations	7 790	9 200	10 600	12 100	13 450
3. Policies with multiannual allocations (IMPs, research)	1 210	1 650	1 900	2 150	2 400
4. Other policies	2 103	2 385	2 500	2 700	2 800
of which: non-compulsory	1 646	1 801	1 860	1 910	1 970
5. Repayments and administration (including financing of stock disposal)	5 700	4 950	4 500	4 000	3 550
	1 240	1 400	1 400	1 400	1 400
6. Monetary reserve	1 000	1 000	1 000	1 000	1 000
Total	45 303	46 885	5 500	50 950	52 800
of which: compulsory	33 698	32 607	32 810	32 980	33 400
of which: non-compulsory	11 605	14 278	16 090	17 970	19 400
Payment appropriations required	43 779	45 300	46 900	48 600	50 100
of which: compulsory	33 640	32 604	32 740	32 910	33 110
of which: non-compulsory	10 139	12 696	14 160	15 690	16 990
Payment appropriations as % of GNP	1.12	1.14	1.15	1.16	1.17
Margin for unforeseen expenditure	0.03	0.03	0.03	0.03	0.03
Own-resources ceiling as % of GNP	1.15	1.17	1.18	1.19	1.20

So for the first time in the Community's history, a reference framework existed within which the various institutions would have to manoeuvre during each of the annual budgetary procedures.

This reduced the risk of clashes between legislative power and budgetary power, by requiring overall consistency between the budgetary implications of legislative decisions and the financial framework laid down.

2) Containment of agricultural expenditure

The Council laid down the principle of a guideline for controlling agricultural expenditure, setting out the practical arrangements for calculating and applying it in its decision on budgetary discipline. The agricultural guideline applied to expenditure under the EAGGF, Guarantee Section. It formed the ceiling for Heading 1 in the 1988–92 financial perspective.

(a) Annual rate of growth

The annual rate of growth in expenditure was not to exceed 74 % of the annual rate of growth of Community GNP. The 1988 expenditure figure, ECU 27 500 million, was taken as the base from which to calculate the agricultural guideline in later years. This led to a relative decrease of agricultural expenditure in relation to GNP.

(b) Agricultural stocks

Mechanisms were adopted for the systematic depreciation of existing and future agricultural stocks, so that the stock situation would return to normal by 1992.

(c) Stabilisers

The stabilisation mechanisms were reinforced and extended to other production sectors. Further measures were introduced aimed at limiting supply directly by encouraging the temporary abandonment of land (set-aside) with the possibility of direct income support.

(d) Early-warning system

An early-warning system on the development of EAGGF Guarantee Section expenditure was introduced. It monitored expenditure chapter by chapter (and not simply as an aggregate as in the past). If the Commission was to see that expenditure was exceeding the forecast profile, or seemed likely to do so, it would make use of the management powers at its disposal. If these measures were inadequate, the Commission would examine the functioning of the agricultural stabilisers and, if necessary, present proposals to the Council to enhance their action. The Council had two months within which to act to remedy the situation.

(e) Monetary reserve

In order to contend with developments caused by significant and unforeseen movements in the dollar/ECU market rate compared with the rate used in the budget, a monetary reserve of ECU 1 000 million would be entered in the budget each year as provisional appropriations. The appropriations for the monetary reserve were not included in the amount of the agricultural guideline.

3) Discipline arrangements for non-compulsory expenditure

The European Parliament and the Council agreed to accept, for the financial years 1988 to 1992, the maximum rates of increase for non-compulsory expenditure deriving from the budgets established within the ceilings set by the financial perspective. In practice, this meant that each year the Parliament could increase the non-compulsory expenditure up to the limit compatible with the ceilings in the financial perspective. This joint commitment on the part of the institutions therefore radically altered the scope of the Treaty provisions relating to the application of the maximum rate of increase, and eliminated the problems of reaching an agreement on exceeding this rate ⁽¹⁾ during the annual budgetary procedure.

⁽¹⁾ See Chapter 2.

The institutions also gave an undertaking that any revision of the compulsory expenditure in the financial perspective would not lead to a reduction in non-compulsory expenditure. This clause to 'protect' non-compulsory expenditure ensured that the application of budgetary discipline would not put compulsory expenditure in a priority category.

Certain other undertakings were also given in the Interinstitutional Agreement by the two arms of the budgetary authority. These included:

- The undertaking to bear in mind the assessment of the possibilities for implementing the budget made by the Commission in its preliminary draft;
- The undertaking to respect the allocations of commitment appropriations for the Structural Funds, the specific industrial development programme for Portugal, the integrated Mediterranean programmes and the research framework programme. These amounts were therefore not only expenditure ceilings but should also be regarded as expenditure targets. This expenditure therefore enjoyed preferential treatment, particularly as, under another provision, any part of these allocations which had not been used in the course of a given year would be carried over to subsequent years.

Improvement of budget management and reform of the Financial Regulation

The February 1988 European Council decided to improve the Community's budget management to strengthen the principle of annuality. This was done by Regulation (ECSC, EEC, Euratom) No 2049/88 of 24 June 1988 ⁽¹⁾, which amended a number of important provisions of the Financial Regulation:

- Differentiated appropriations would no longer be carried over automatically; the Commission could authorise certain carryovers provided they were duly substantiated on the basis of specific criteria spelled out in the Financial Regulation;
- Appropriations corresponding to commitments cancelled could, exceptionally, be made available again by Commission decision on the basis of specific criteria.

2.3. The reform of the Structural Funds

The Single Act provided for close coordination between the three existing Structural Funds (EAGGF Guidance Section, European Social Fund and European Regional Development Fund) with a view to clarifying and rationalising their tasks and enhancing their effectiveness. This coordination, the arrangements for which would be laid down in a single instrument covering all three Funds, was intended to promote the harmonious development of the entire Community, by reducing the gap between regions and helping the less-favoured regions to catch up.

The Brussels European Council decided that the growth of the Structural Funds had to be guaranteed in the medium term: the commitment appropriations in 1993 would be twice as high in real terms as in 1987.

⁽¹⁾ OJ L 185, 15.7.1988, p. 3.

For the purposes of rationalisation, the European Council also decided that Community action through the Funds would be targeted at the following five general objectives:

- Objective 1: promoting development and structural adjustment in less-developed regions;
- Objective 2: converting the regions, border regions or parts of regions (including employment areas and urban communities) seriously affected by industrial decline;
- Objective 3: combating long-term unemployment;
- Objective 4: facilitating the occupational integration of young people;
- Objectives 5a and 5b: with a view to reform of the common agricultural policy, speeding up the adjustment of agricultural structures and promoting the development of rural areas.

The detailed arrangements for giving effect to this decision were adopted by the Council on 24 June 1988 ⁽¹⁾.

To coordinate the operations of the Funds, it was specified that they would contribute as follows to the attainment of the five objectives set by the European Council:

- Objective 1: ERDF, ESF and EAGGF Guidance Section;
- Objective 2: ERDF and ESF;
- Objective 3: ESF;
- Objective 4: ESF;
- Objective 5a: EAGGF Guidance Section;
- Objective 5b: EAGGF Guidance Section, ESF and ERDF.

On the basis of the principles and general provisions laid down in the general Structural Funds regulation, the Commission presented proposals on 30 August 1988 for implementing regulations for the individual policies. These proposals were adopted by the Council on 19 December 1988 to take effect on 1 January 1989.

3. First assessment of the reform: 1988–92

Two reports on the implementation of the 1988 reform were presented on 10 March 1992 by the Commission to the Parliament and Council:

- a report on the application of the Interinstitutional Agreement (COM(92) 82);
- a report on the system of own resources (COM(92) 81).

⁽¹⁾ Council Regulation (EEC) No 2052/88 of 24 June 1988 on the tasks of the Structural Funds and their effectiveness and on coordination of their activities between themselves and with the operations of the European Investment Bank and the other existing financial instruments (OJ L 185, 15.7.1988, p. 9).

Their conclusions were largely positive as regards the main objectives pursued: the orderly progression of expenditure, improvement in the budgetary procedure and budget management, and adequate own resources.

Favourable economic conditions undoubtedly helped to achieve these results. Nevertheless, the application of the agreement met some difficulties, particularly as regards the revision of the financial framework. The Community budget was, however, able to cope with new tasks, deriving mainly from the considerable upheavals on the international scene during this period. There is little doubt that the problems encountered would have been far more acute in the absence of the financial framework imposed in 1988, which enabled the debate to be confined within agreed limits and rules.

3.1. Orderly progression of expenditure

1) *The successive revisions of the financial perspective*

Pursuant to the Interinstitutional Agreement, the financial perspective was revised or adjusted no less than seven times during the period, to accommodate new activities or to strengthen existing policies.

These revisions mainly concerned the introduction of new operations linked to changes in the international environment: cooperation with the countries of central and eastern Europe then technical assistance to the republics of the former USSR, German unification, the Gulf crisis, financial aid to Israel and the Occupied Territories, humanitarian aid to the Kurdish refugees and to the former Yugoslavia and combating famine in Africa, etc.

Some existing Community policies were strengthened halfway through the period, for example: internal policies and cooperation activities in favour of developing countries in the Mediterranean, Asia and Latin America.

The other revisions were of a more technical nature: adjustments to allow a more regular progression in the budget available for administrative expenditure, *ex post* adjustments to the appropriations for the Structural Funds in line with actual inflation, revaluation of the repayments to be made to Spain and Portugal following accession and to the Member States in respect of expenditure incurred on disposal of agricultural stocks, or the taking into account of the evolution of the rate of clearance of commitments under certain programmes (e.g. structural aid to the new German *Länder*, research).

2) *The actual shape of the financial framework*

Table 3.2 shows the changes (after adjustment and revision) in the financial perspective over the period 1988–92 in relation to the original table agreed.

In all, the ceiling on expenditure was raised in real terms by 5.5 % per year on average for appropriations for commitments, as opposed to the 3.9 % originally planned.

This overall trend covered changes in the structure of expenditure in accordance with the priorities adopted, but which were more pronounced than was envisaged in 1988.

TABLE 3.2 – *Actual application of the financial perspective 1988–92*

	Rate of increase (%) in real terms 1992/88		Distribution (%) of the total appropriations for commitments		
	Original financial perspective	Actual financial perspective	Original financial perspective		Actual financial perspective
			1988	1992	1992
EAGGF Guarantee Section	7.6	6.8	60.7	56.1	52.5
Structural operations	72.7	94.8	17.2	25.5	27.1
Multiannual policies	98.3	101.1	2.7	4.5	4.3
Other policies	33.1	136.5	4.6	5.3	8.9
Repayments and administration	-37.8	-42.8	12.6	6.7	5.8
Monetary reserve	-	-16.2	2.2	1.9	1.5
Total appropriations for commitments	16.5	23.7	100	100	100
Total appropriations for payments	14.4	22.6	96.6	94.9	95.8

As foreseen, the ceiling for the EAGGF Guarantee Section (agricultural guideline) rose by far less than that for total expenditure. Actual agricultural expenditure remained well within this ceiling. The additional cost in this field, resulting from German unification, could thus be covered without the guideline having to be raised.

However, this result was due as much to a favourable economic climate as it was to a reform of agricultural market mechanisms. Even though the guideline was respected, agricultural expenditure remained very sensitive to external parameters and the economic effects of the stabilisers proved to be limited. Under these circumstances, and in view of the commitments to be entered into at international level under the GATT, reform of the common agricultural policy was essential. This reform was to be orientated towards direct aid reflecting production capacity, rather than being based almost exclusively on a system of guaranteed prices.

The rise in the ceiling for the heading 'Other policies' (see Table 3.2) was much higher than planned, mainly as a result of the increase in the Community's external action over that period. The ceiling for the 'Structural operations' heading (see Table 3.2) also rose by more than expected. This was mainly due to the transfer of allocations, which could not be used in earlier years, to the end of the period, rather than to an increase in the total amounts originally planned.

3.2. Improvement in the budgetary procedure and budget management

1) Compliance with the basic principles of the Interinstitutional Agreement

The budget for each of the years covered by the agreement was adopted on time without any major conflicts between the institutions during the budgetary procedure. There was full compliance with the financial perspective in terms of both authorisation and implementation of the budget. The annual technical adjustments as well as the revisions of the financial perspective, were all made in accordance with the agreement. A solution acceptable to the parties was found whenever problems of interpretation arose in this respect.

However, these revision or adjustment procedures proved to be cumbersome in practice (taking an average of three months) and often coincided with the actual annual budgetary procedure, thereby diminishing the instrument's characteristics of containment and medium-term guidance. The two arms of the budgetary authority had differing views on how to finance the new needs which arose, with the Parliament advocating using the margin available under the own-resources ceiling, and the Council giving priority to redeployment of the expenditure budgeted under each heading.

2) More rigorous budget management

In line with the objectives adopted and by means of the new provisions in the Financial Regulation, there were significant improvements in budget management from the point of view of implementation, especially concerning:

- the principle of annuality, with a sharp reduction, in absolute amounts and in relative terms, of carry-overs from one financial year to the next and appropriations made available again;
- the principle of specification, with a substantial reduction in transfers between chapters during the financial year.

In addition, the average utilisation rate of appropriations was appreciably higher than it had been during the years preceding the reform. The clearance of commitments was also speeded up, in terms of both forecasts and actual outturn.

Finally, the Commission took a range of measures to make a cost-effectiveness approach more systematic in devising proposals for action and in organising its management.

3.3. Sufficient financial resources

Despite the successive upward revisions of the financial perspective, the total expenditure ceiling, and hence the actual amount of budget expenditure, remained beneath the ceiling of available own resources.

This result was, however, achieved through the combination of two favourable factors:

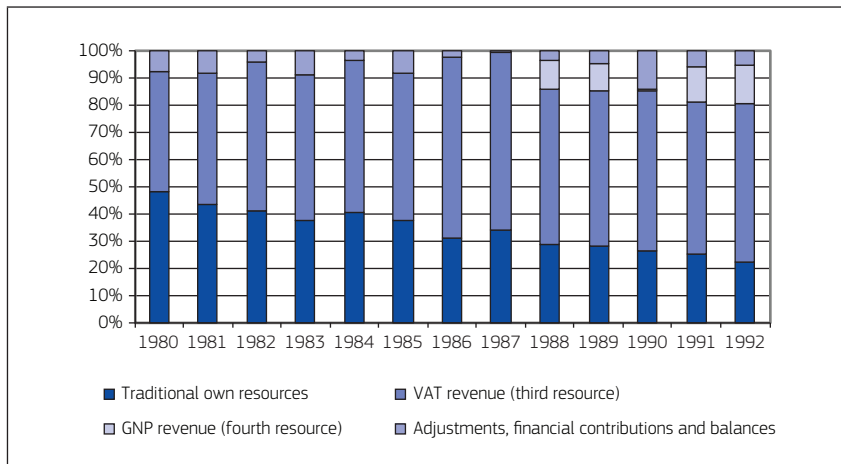
- a moderate increase in requirements for agricultural expenditure;
- more rapid economic growth than initially forecast, leading to a considerably larger volume of available own resources.

TABLE 3.3 – *Use of the own-resources ceiling*

	(% of GNP)				
	1988	1989	1990	1991	1992
Own-resources ceiling	1.15	1.17	1.18	1.19	1.20
Ceiling on appropriations for payments (actual financial perspective)	1.12	1.06	1.08	1.13	1.19
Total appropriations for payments entered in the budget and actually used	1.12	1.02	0.99	1.09	1.13

3.4. Structure of own resources

As far as the structure of own resources was concerned (see Figure 3.1), the proportion of traditional own resources continued to decline. The VAT-based resource remained by far the largest. The GNP-based resource amounted to less than 11 % of own resources in 1988 and 1989 and was negligible in 1990. It reached between 14 and 15 % of own resources payments in 1991 and 1992.

FIGURE 3.1 – *Structure of own resources (1980–92)*

Despite the 1988 reform, regressive elements remained in the system of own resources, principally because VAT bases were high in relation to GNP in the least prosperous Member States. Despite capping at 55 % of GNP, the VAT bases of Greece, Ireland and Portugal remained above the Community average, which in 1992 amounted to 49.3 % of GNP.

Chapter 4

Consolidation of the 1988 reform: the Delors II package (1993–99)

1. The Commission's proposals

1.1. The objectives of the Delors II package

1) Consolidating the achievements of the 1988 reform

The 1988–92 financial perspective and the Interinstitutional Agreement concluded in 1988 were due to expire at the end of 1992. Likewise, in the absence of a new decision on own resources, 1992 marked the end of the gradual rise in the own-resources ceiling, which would have been frozen at 1.20 % of GNP.

As the Commission's assessment of the system introduced in 1988 had been positive, it came to the conclusion that the financial perspective and the Interinstitutional Agreement should be renewed for a further period, even though certain improvements could be made in the light of experience.

2) Updating the financial framework

Several decisions with major implications for the budget had been made or were expected, making a review of the Community's financial framework inevitable. In particular, there was a need:

- to take account of the financial impact of the reform of the common agricultural policy which started in 1992;
- to take stock of the reform of the Structural Funds and to adopt a new regulation, since the framework established in 1988 would be expiring at the end of 1993;
- to guarantee the development of the policies needed for the internal market to run smoothly and to provide the Community with sufficient resources to meet its new international responsibilities.

3) Applying the Maastricht Treaty

The Delors II package flanked the Maastricht Treaty ⁽¹⁾ during its first years in the same way that the Delors I package contributed to the implementation of the Single Act. Nevertheless, the direct budgetary implications of the new Treaty were quite modest and left the institutions with a power of political appraisal regarding their implementation.

The main budgetary impact of the Maastricht Treaty was the establishment of the Cohesion Fund to finance infrastructure, transport and environment projects in countries with a per capita GNP below 90 % of the Community average (Greece, Spain, Ireland and Portugal) in order to support their efforts towards economic convergence in the context of the economic and monetary union.

⁽¹⁾ The Treaty on European Union, signed in Maastricht on 7 February 1992, entered into force on 1 November 1993.

The other budgetary implications of the Treaty included:

- the Protocol on economic and social cohesion annexed to the Treaty, which was a strong political signal in favour of strengthening all the regional policies of the Community;
- the new powers allocated explicitly to the Community in a large number of sectors, such as trans-European networks, education, industry and culture, which in certain cases implied stepping up Community action in these sectors;
- the provisions of the common foreign and security policy and of cooperation in the field of justice and home affairs, which stipulated that the administrative expenditure incurred by the institutions through the implementation of these policies was to be charged to the Community budget and that operating expenses might also be financed by the Community budget provided there was a unanimous decision by the Council.

1.2. The Commission proposals

In February 1992 the Commission presented its proposals in two communications:

- 'From the Single Act to Maastricht and beyond: The means to match our ambitions', better known as the Delors II package, COM(92) 2000 of 11 February 1992;
- 'The Community's finances between now and 1997', COM(92) 2001 of 10 March 1992.

The Commission proposed raising the annual ceiling on appropriations for payments by ECU 20 billion (1992 prices) over five years, which would mean raising the own-resources ceiling gradually from 1.20 % of GNP in 1992 to 1.37 % in 1997. Three major political priorities were adopted:

- economic and social cohesion, through the development of new structural operations;
- external action to take account of changes in the international environment;
- strengthening the competitiveness of European industry, notably by boosting research and participating in the financing of trans-European networks.

The first debate at the Lisbon European Council in June 1992 ended in deadlock, so the Commission proposed that achievement of these objectives be spread over seven years up to 1999 instead of 1997. The Commission's amended proposal required setting the own-resources ceiling at 1.32 % of GNP in 1999, giving a ceiling on appropriations for payments of 1.29 % of GNP, with a margin for unforeseen expenditure of 0.03 % of GNP.

2. The Edinburgh European Council and the conclusion of the 1993–99 financial package

2.1. The conclusions of the Edinburgh European Council

The Edinburgh European Council of 11 and 12 December 1992 finally opted for a gradual rise in the own-resources ceiling from 1.20 to 1.27 % of GNP in 1999, allowing a margin for unforeseen expenditure of 0.01 % of GNP. The overall ceiling on appropriations for commitments was fixed at 1.335 % of GNP.

1) Own resources

Apart from fixing new ceilings for the period, the European Council decided to alter the structure of own resources in order to reduce certain regressive aspects of the existing system by increasing the significance of the GNP-based 'fourth resource'.

- The maximum rate applicable to the uniform VAT base was reduced from 1.4 to 1 % in equal steps over the period 1995–99.
- For the least prosperous Member States (Greece, Spain, Ireland and Portugal), the threshold for the cap on the VAT base was reduced from 55 to 50 % of GNP from 1995 and, for the other Member States, in equal steps over the period 1995–99.

The mechanism for correcting budget imbalances in favour of the United Kingdom was retained.

2) Expenditure

The European Council selected two major priorities, structural operations and external action, and adopted the following main policies, whilst calling on the institutions to conclude a new Interinstitutional Agreement:

(a) Agriculture

As the Commission had proposed, the trend in agricultural expenditure continued to be governed by the agricultural guideline, with arrangements unchanged, i.e. an increase limited to 74 % of growth in GNP. The expenditure covered by the guideline was amended slightly, in particular to include all the expenditure under the reformed CAP, including the accompanying measures, and the Guarantee Fund for fisheries. The monetary reserve was cut to ECU 500 million from 1995, reflecting the lesser dependence of the reformed CAP on world farm prices.

(b) Structural operations

The European Council agreed with the Commission's priorities. The total amount of expenditure earmarked for economic and social cohesion increased by 75 % in real terms from just over ECU 17 billion in 1992 to ECU 30 billion in 1999. Community actions now focused on the Structural Funds and Cohesion Fund. The budgetary resources of the Structural Funds were more concentrated on the least-favoured regions (Objective 1 regions) and in 1999 the four beneficiary countries of the Cohesion Fund were to receive, under the Cohesion Fund and Objective 1 of the Structural Funds together, twice the amount they received in 1992 under Objective 1 of the Structural Funds.

(c) Internal policies

The amounts available under this heading increased by some 30 % over seven years, which was less than the Commission and the European Parliament would have wished. According to the conclusions of the European Council, research continued to represent the main item of expenditure and, as was already the case, accounted for between half and two thirds of the total for the heading. Growth in expenditure to finance trans-European networks had to be particularly strong, reflecting the new priority given to this sector.

(d) External action

Apart from the allocations provided for under this heading, which now grouped together all external action, including the external aspects of internal policies (fisheries, environment, etc.), two new reserves were established. Including these two reserves, intended for emergency aid in non-member countries and to cover possible calls on the guarantee granted by the Community for loans to non-member countries, the Edinburgh decisions entailed an ambitious increase of some 55 % in the resources for external action.

(e) Administrative expenditure

There was a strict budgetary constraint on administrative expenditure as most of the planned increase was earmarked for pensions.

3) Adoption of the financial framework for 1993–99

The European Council agreed on a new financial perspective for 1993–99 on the basis of these guidelines (see Table 4.1) ⁽¹⁾.

2.2. Renewal of the Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure

The European Council's agreement on a new financial framework for 1993–99 was not the end of the negotiations. Nearly a year of tough negotiations was needed before the European Parliament, the Council and the Commission were able to conclude a new Interinstitutional Agreement on 29 October 1993 ⁽²⁾, thereby bringing into force the financial perspective, which formed an integral part of this agreement.

Judging the financial framework agreed in Edinburgh to be disappointing in the sense of being too restrictive, the European Parliament gave its agreement to the figures subject to significant progress at institutional level.

1) Rules for the application of the financial perspective

The Commission had proposed renewing most of the provisions of the 1988 agreement, which was accepted by both the European Parliament and the Council. In particular, several undertakings entered into by the institutions in 1988 were reiterated.

- The rule on the maximum rate of increase for non-compulsory expenditure remained neutralised, since the two arms of the budgetary authority confirmed that for the period 1993–99 they would accept the maximum rates imposed by the ceilings of the financial perspective.
- Protection of non-compulsory expenditure continued to be assured: a revision of compulsory expenditure may not lead to a reduction in the amount available for non-compulsory expenditure.

⁽¹⁾ This table incorporates minor changes made for 1994 following negotiations with Parliament after the Edinburgh European Council, which led in October 1993 to the conclusion of a new Interinstitutional Agreement (see Point 2.2 of this chapter).

⁽²⁾ OJ C 331, 7.12.1993.

TABLE 4.1 – *Financial perspective 1993–99**(million ECU at 1992 prices)*

Appropriations for commitments	1993	1994	1995	1996	1997	1998	1999
1. Agricultural guideline	35 230	35 095	35 722	36 364	37 023	37 697	38 389
2. Structural operations	21 277	21 885	23 480	24 990	26 526	28 240	30 000
— Cohesion Fund	1 500	1 750	2 000	2 250	2 500	2 550	2600
— Structural Funds and other operations	19 777	20 135	21 480	22 740	24 026	25 690	27400
3. Internal policies	3 940	4 084	4 323	4 520	4 710	4 910	5 100
4. External action	3 950	4 000	4 280	4 560	4 830	5 180	5 600
5. Administrative expenditure	3 280	3 380	3 580	3 690	3 800	3 850	3 900
6. Reserves	1 500	1 500	1 100	1 100	1 100	1 100	1 100
— Monetary reserve	1 000	1 000	500	500	500	500	500
— External action							
* emergency aid	200	200	300	300	300	300	300
* loan guarantees	300	300	300	300	300	300	300
Total appropriations for commitments	69 177	69 944	72 485	75 224	77 989	80 977	84 089
Appropriations for payments required	65 908	67 036	69 150	71 290	74 491	77 249	80 114
Appropriations for payments (% GNP)	1.20	1.19	1.20	1.21	1.23	1.25	1.26
Margin for unforeseen expenditure (% GNP)		0.01	0.01	0.01	0.01	0.01	0.01
Own-resources ceiling (% GNP)	1.20	1.20	1.21	1.22	1.24	1.26	1.27
<i>Pro memoria</i> : total external expenditure	4 450	4 500	4 880	5 160	5 430	5 780	6 200
<i>Pro memoria</i> : the inflation rate applicable for the 1993 budget is 4.3 %.							

- Preferential treatment of expenditure for structural operations, including the new Cohesion Fund, was continued. The allocations for Heading 2 of the financial perspective consequently represented both a ceiling and an expenditure target, with the two arms of the budgetary authority undertaking, for these operations, to transfer the appropriations not used during a financial year to subsequent years. It should be noted that the expenditure for research and technological development no longer fell into the category of privileged expenditure.

The provisions relating to the procedures for the technical adjustment, the adjustment in line with the conditions of implementation and the revision of the financial perspective remained largely unchanged. However, when drawing up the budget, the institutions had to ensure that there was a margin beneath the ceilings for the various headings (except for Heading 2, which was an expenditure target) so that additional appropriations could be entered where necessary without first revising the financial perspective.

2) Provisions concerning the budgetary procedure

As a result of the institutional demands of the European Parliament, the new Interinstitutional Agreement's major innovations were to be found in this field.

- The institutions agreed that all expenditure under Headings 2 (structural action) and 3 (internal policies) of the financial perspective was non-compulsory expenditure. In a statement appended to the agreement, it was also agreed that expenditure on financial protocols with non-member countries which were concluded or renewed would be considered non-compulsory. The ongoing financial protocols, EAGGF Guarantee expenditure, some external expenditure (fisheries agreements, subscription to the capital of international financial organisations, etc) and expenditure on the pensions of former officials or other staff of the institutions were classified as compulsory expenditure.
- A new procedure for interinstitutional collaboration in budgetary matters was introduced, with an exchange of views on budget priorities and conciliation on compulsory expenditure, allowing Parliament to initiate a dialogue with the Council on the amount of compulsory expenditure to be entered in the budget, even though the Council had the last word on the matter.
- A 'negative co-decision' procedure was introduced to mobilise the reserves (the monetary reserve, the reserve for loan guarantees and the reserve for emergency aid). If the Commission's proposal failed to secure the agreement of the two arms of the budgetary authority, and if the budgetary authority was unable to agree on a common position, the proposal would be deemed to have been approved.

2.3. The legislative provisions of the Delors II package

The Commission submitted a series of proposals for legislation to the Council to implement the conclusions of the Edinburgh European Council and to put into legal form the commitments entered into by the institutions under the Institutional Agreement.

After lengthy discussions, these proposals led on 31 October 1994 to the Council adopting new texts and amending existing texts ⁽¹⁾.

- A new own-resources decision (Decision 94/728/EC, Euratom), incorporating the adjustments made to the system of own resources and the revised ceilings, was adopted after ratification by all Member States according to their respective constitutional requirements.
- The Council Decision of 24 June 1988 concerning budgetary discipline was replaced by Council Decision 94/729/EC.
- The entry in the budget of the two new reserves associated with external action required an appropriate legislative framework. The Council therefore amended both the Financial Regulation (Council Regulation (ECSC, EC, Euratom) No 2730/94 amending the Financial Regulation of 21 December 1977 applicable to the general budget of the European Communities) and Regulation No 1552/89 on the system of own resources (Regulation (EC, Euratom) No 2729/94). It also adopted Regulation (EC, Euratom) No 2728/94 creating a guarantee fund to cover the risks incurred as a result of guarantees granted under the general budget.

⁽¹⁾ OJ L 293, 12.11.1994.

- In the field of structural operations, the five 1988 regulations on the Structural Funds were revised and a sixth regulation on the financial instrument for fisheries guidance (FIFG) was adopted on 20 July 1993 ⁽¹⁾.

In accordance with the Treaty on European Union, a Cohesion Fund was established by Council Regulation (EC) No 1164/94 of 16 May 1994 ⁽²⁾, after the temporary application of a cohesion financial instrument established on 30 March 1993.

3. Application of the financial framework, 1993–99

3.1. The impact of the economic recession on the early years of this period

1) The deterioration in the economic situation over the period 1992–94

The management of the financial perspective 1988–92 was greatly facilitated by a favourable economic climate. Growth was stronger than originally expected, thus generating an increased volume of overall available own resources and providing cover for new costs arising in particular from the development of international activities ⁽³⁾.

The first years of application of the financial framework 1993–99 were characterised by the reverse economic climate. The successive downward revisions of forecast growth for 1992 to 1994 led to a big reduction in real GNP and, consequently, of overall available own resources. It was only during the second half of 1994 that signs of economic recovery appeared.

Despite this unfavourable situation, the principles of budgetary discipline underlying the Inter-institutional Agreement were not called into question.

2) Increased constraints for the application of the financial framework

(a) The constraint on agricultural expenditure

Lower economic growth resulted in a reduction of the agricultural guideline, and Community currency realignments (occurring since the end of 1992) resulted in additional costs for the common agricultural policy. Nevertheless, actual agricultural expenditure remained well within the reduced limits.

(b) The ceiling on own resources

The economic recession led to the disappearance of the small margin of 0.01 % of GNP (as opposed to 0.03 % in the financial perspective 1988–92), which had been left available between the total ceiling on appropriations for payments and the ceiling on own resources.

To forestall any overshooting of the own-resources ceiling in the implementation of the 1994 budget, the Commission took various measures during the year for economical management of the appropriations available.

⁽¹⁾ Council Regulations (EEC) Nos 2080/93, 2081/93, 2082/93, 2083/93, 2084/93 and 2085/93 (OJ L 193, 31.7.1993).

⁽²⁾ OJ L 130, 25.5.1994

⁽³⁾ See Chapter 3.

During the technical adjustment of the financial perspective ahead of the budgetary procedure for 1995, it even emerged that the ceiling on own resources was liable to be insufficient to cover the level of expenditure provided for in the financial framework. The preliminary draft budget presented by the Commission took account of this constraint. Had this situation persisted, it would have led to a downward revision of the financial perspective for the following years of the framework, as provided in the Interinstitutional Agreement.

(c) The shortfall in own resources

The economic recession brought about a reduction in the yield of traditional own resources and in the bases for the VAT and GNP resources compared with the levels forecast when the budget was established. This resulted in particularly large revenue shortfalls in 1992 (ECU 2 billion) and 1993 (about ECU 6.5 billion).

Even though the budgets for 1992 and 1993 were implemented within the own-resources ceiling, these shortfalls created negative balances in outturn which, in accordance with the Financial Regulation, had to be entered in the following year's budget as expenditure, thus reducing in principle the expenditure capacity defined in the financial perspective.

The Parliament had made its acceptance of the new Interinstitutional Agreement subject to the condition that the treatment of negative balances arising from revenue shortfalls would not reduce the amounts available under the expenditure ceilings. The Council had undertaken to find a suitable solution to this problem.

The Commission presented a proposal to amend the financial rules but thanks to very prudent management of available resources, sufficient margins could in fact be found to cover the revenue shortfalls. The budgetary authority therefore preferred not to amend the Financial Regulation.

3.2. Enlargement of the European Union

During the enlargement negotiations with Norway, Austria, Finland and Sweden, the budget was a decisive factor. In view of their relative prosperity, the applicant countries would contribute more to the Community budget than they might expect to receive by way of expenditure.

1) The stated positions

(a) The applicant countries had expressed two major concerns:

- They were worried about the 'shock' to their own finances of their contribution to the Community budget and therefore wished to obtain a gradual 'phasing-in' of the own-resources mechanism;
- They were worried about the consequences of the agriculture aspects of the negotiations for their national public finances. The Union had proposed an immediate alignment of their agricultural prices with the generally lower Community prices, accompanied by degressive aid financed exclusively by national budgets and designed to cushion the impact of this fall in prices on farmers' incomes. The applicant countries had expressed their preference for a system of 'accession compensatory amounts' (ACAs) which would have allowed the gradual adjustment of prices and made this budget aid unnecessary.

(b) For its part, the Union had three major concerns:

- Firstly, envisaging a permanent exemption from the system of own resources was out of the question;
- Secondly, if a transitional system were to be considered, its justification should lie in ‘loss of income’ for the acceding countries resulting from the fact that Community action in their favour would be implemented only gradually;
- Finally, care had to be taken not to cover the entire cost of adjustment of the agricultural sector of the applicant countries. In addition, the introduction of ACAs would have run counter to a single market without internal frontiers.

In any event, following enlargement, the Community should not find itself in a more difficult financial situation than previously.

2) The results of the negotiations

At the end of the negotiations, the applicant countries were offered budgetary compensation, commonly known as the ‘agri-budgetary’ package. These amounts, which were recorded in the Act of Accession, were made up of two components.

- Compensation for loss of earnings during the first year in the agriculture sector on account of the non-payment to the applicant countries of direct per hectare aid for major crops and beef and veal premiums. This payment should have been based on the statements to be made at the beginning of 1994, which was obviously impossible since these countries were not members of the Community at that time.
- Degressive compensation over four years, with the overall aim of supporting the budgetary efforts of the applicant countries in favour of their agricultural sectors following the fall in prices (direct compensatory aid and depreciation of stocks). All the applicant countries were allowed this compensation, which avoided penalising Sweden for having already adjusted its agricultural sector.

Furthermore, it was agreed that the Community budget would cover the financial commitments entered into by the applicant countries under the agreement establishing the European Economic Area (EEA).

The Act of Accession also provided for appropriations which the new Member States could claim under the Structural Funds.

- Only the Burgenland region of Austria was considered eligible for Objective 1 of the Structural Funds.
- A new Objective 6 was introduced in favour of regions with a population density not exceeding eight inhabitants per square kilometre, which boiled down to restricting its geographical cover to a few regions in the north of Scandinavia and Finland. Objective 6 was subject to rules similar to those of Objective 1 and received an allocation per inhabitant which was slightly lower.

- The applicant countries were obviously eligible for the other objectives of the Structural Funds on the same footing as the other Member States for a total amount also laid down in the Act of Accession.

3) *The adjustment of the financial perspective*

As provided for in the 1993 Interinstitutional Agreement, an adjustment of the financial perspective was necessary to take account of the new requirements and resources of the enlarged Community. Following the proposals put forward by the Commission in early October 1994, the institutions agreed on an adjusted financial perspective for 1995–99 on 29 November. The matter had been expedited so quickly that the 1995 budget could then immediately be adopted for a Community of 15 Member States (the Norwegians had voted against entry in their referendum).

The ceilings for the headings were raised to cover the requirements resulting from the enlargement of the Union and the outcome of the accession negotiations.

- Common agricultural policy: the agricultural guideline was raised by 74 % of the percentage increase in GNP generated by enlargement.
- Structural operations: the allocations for the Structural Funds were increased for the acceding countries in accordance with the Act of Accession. Simultaneously, the budget covered the contribution of the three acceding countries to the EEA financial mechanism and a new subheading was created specifically for this purpose under Heading 2.
- Internal policies: the ceiling for the heading was raised by 7 %, corresponding to the relative size of the GNP of the acceding countries.
- External action: the ceiling for the heading was raised by 6.3 %, allowing the development of external action in line with the increase in the European Union's ability to contribute.
- Administrative expenditure: Heading 5 was increased by an average 4.66 % over the period from 1995 to 1999.

A new Heading 7 was also added to accommodate the compensation to be received by the new Member States from 1995 to 1998 in accordance with the Act of Accession.

The institutions also availed themselves of this adjustment of the financial perspective and the new resources available to the Union to amend the ceilings for Headings 2 and 3, in order to meet specific requirements which had emerged more recently.

- Heading 2 was increased by ECU 200 million (1995 prices), divided into three equal annual instalments from 1995 to 1997. This lump-sum increase for Community initiatives was to finance the Northern Ireland peace programme as stipulated by the Essen European Council.
- Heading 3 was increased by ECU 400 million (1994 prices), divided into equal instalments over the next five years to finance the programme to modernise the textiles and clothing industry in Portugal, the principle of which had been adopted when the Uruguay Round was concluded.

As shown in Table 4.2 (1995 prices), the new framework for the financial perspective of the enlarged Community left a margin between the ceiling on appropriations for payments and

the own-resources ceiling which was distinctly larger than that provided for in Edinburgh; it now amounted to 0.03 % of GNP at the end of the period.

TABLE 4.2 – Financial perspective for the enlarged Community 1995–99

(million ECU at 1995 prices)

Appropriations for commitments	1995	1996	1997	1998	1999
1. Common agricultural policy	37 944	39 546	40 267	41 006	41 764
2. Structural operations	26 329	27 710	29 375	31 164	32 956
— Structural Funds ⁽¹⁾	24 069	25 206	26 604	28 340	30 187
— Cohesion Fund	2 152	2 396	2 663	2 716	2 769
— EEA financial mechanism ⁽²⁾ ⁽³⁾	108	108	108	108	0
3. Internal policies	5 060	5 233	5 449	5 677	5 894
4. External action	4 895	5 162	5 468	5 865	6 340
5. Administrative expenditure	4 022	4 110	4 232	4 295	4 359
6. Reserves	1 146	1 140	1 140	1 140	1 140
— Monetary reserve ⁽²⁾	500	500	500	500	500
— Guarantee reserve	323	320	320	320	320
— Emergency aid reserve	323	320	320	320	320
7. Compensation ⁽²⁾	1 547	701	212	99	0
8. Total appropriations for commitments	80 943	83 602	86 143	89 246	92 453
9. Total appropriations for payments	77 229	79 248	82 227	85 073	88 007
Appropriations for payments as % of GNP	1.20	1.21	1.22	1.23	1.24
Margin as % of GNP	0.01	0.01	0.02	0.03	0.03
Own-resources ceiling as % of GNP	1.21	1.22	1.24	1.26	1.27

⁽¹⁾ Between 1996 and 1999 the annual technical adjustment for the amounts intended for the new Member States, fixed at 1995 prices in the Act of Accession, were based on 1995 prices.

⁽²⁾ Current prices.

⁽³⁾ The ceiling for this sub-heading could be changed, if necessary, under the technical adjustment procedure provided for in Paragraph 9 of the Interinstitutional Agreement in line with the actual payments in the course of each financial year.

3.3. Results in terms of budgetary discipline and improvement of the budgetary procedure

1) Changes in the budget and in the financial framework

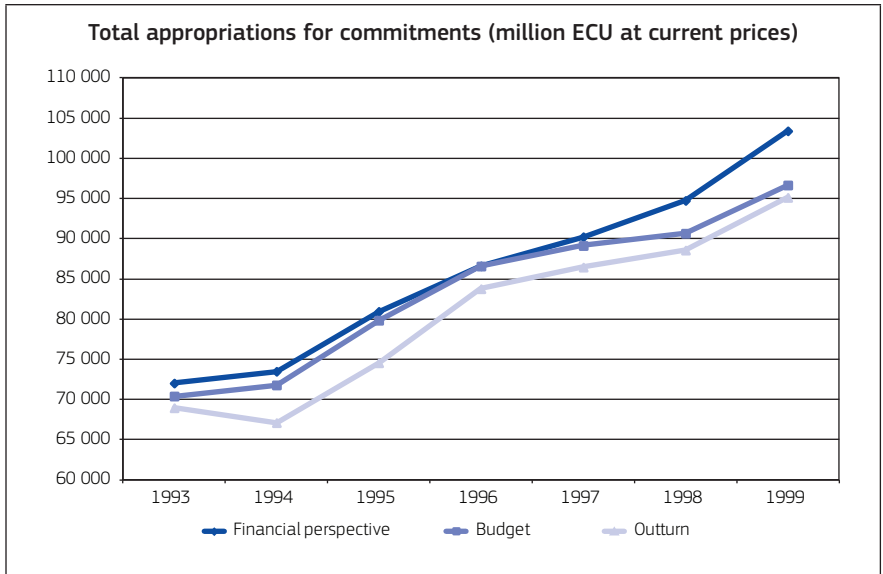
Apart from the adjustments made at the occasion of enlargement, the financial framework remained unchanged throughout its whole period of application. The proposal which the Commission presented in 1996 for redeploying and reclassifying expenditure in individual headings in order to strengthen certain internal policies which could promote growth and employment was not endorsed by the Council.

(a) Expenditure

Two distinct sub-periods may be noted in the application of the financial framework (see Figure 4.1).

- Between 1993 and 1996 the annual budgets adopted were close to the ceilings in the financial perspective but under-spending was significant in 1994 and 1995. This under-utilisation of appropriations was largely accounted for by agriculture and structural operations. In the case of agriculture, this demonstrated the need for improved expenditure forecasts and the monitoring of implementation. The under-spending on structural operations was due to delays in introducing the new programmes from 1994 onwards, particularly those relating to Community initiatives and Objectives 2, 5a and 5b. The transfer of unused appropriations provided for in the Interinstitutional Agreement was concentrated at the end of the period and came to almost EUR 3.3 billion in 1999, artificially inflating the level of expenditure for that financial year.
- However, from 1997 onwards, the annual budgets were adopted leaving substantial margins beneath the ceilings of the financial perspective and improved budget implementation reduced under-spending.

FIGURE 4.1 – *Financial perspective ceilings, expenditure entered in budget and outturn*



(b) Own resources

Since the level of GNP had to be revised downwards several times due to unfavourable economic conditions, the total appropriations for payments entered in the budget were close to the own-resources ceiling until 1996 and even turned out to be slightly higher in the first year

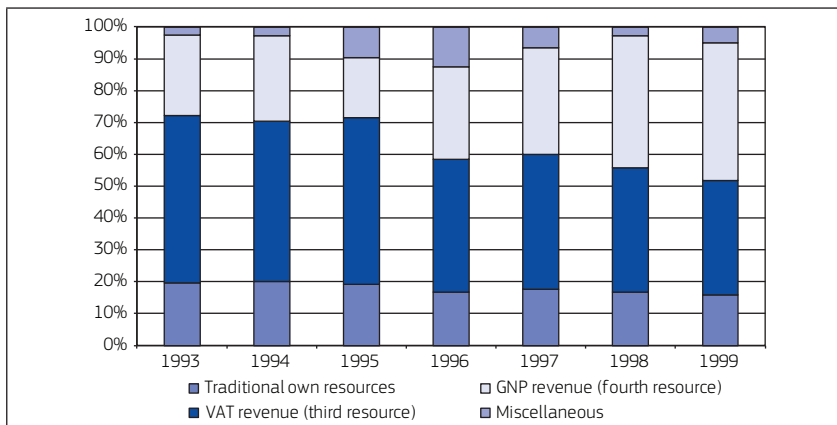
of the period ⁽¹⁾. A growing margin was then left available during the rest of the period. The trend in the implementation of appropriations for payments was similar to that for commitments: after a marked deterioration in 1994 and 1995, the rates of implementation picked up, but were still far below the own-resources ceiling.

TABLE 4.3 – *Own-resources ceilings, appropriations for payments entered in the budget and outturn*

	(% of GNP)						
	1993	1994	1995	1996	1997	1998	1999
	EU-12		EU-15				
Own-resources ceiling	1.20	1.20	1.21	1.22	1.24	1.26	1.27
Budget	1.21	1.18	1.17	1.21	1.16	1.12	1.10
Out-turn	1.17	1.03	1.03	1.14	1.12	1.09	1.07

As regards the structure of own resources, the yield from traditional own resources remained largely constant over the period, although the proportion of total revenue they accounted for continued to decline. The net drop in the proportion accounted for by the VAT-based resource (from 52.5 % in 1993 to 35.5 % in 1999) was in line with the objective pursued when the own-resources decision was amended. The proportion accounted for by the resource based on the GNP of the Member States thus came to slightly more than 48 % of receipts at the end of the period.

FIGURE 4.2 – *Structure of own resources, 1993–99*



⁽¹⁾ The amount of own resources actually called in during that year was still consistent with the ceiling laid down, as other revenue was used for the financing.

2) Improvement of the budgetary debate

At first, the procedure of interinstitutional collaboration introduced by the 1993 agreement encountered difficulties which were again related to the problem of classifying expenditure. The Parliament took the opportunity of conciliation on compulsory expenditure not only to discuss the amounts, but also to call the classification into question. The Parliament's unilateral reclassification of certain lines of expenditure in the 1995 budget was annulled by the Court of Justice after an action was brought by the Council. The situation was then regularised, albeit without any basic agreement on this issue.

After this difficult start, the procedure did gradually generate a conciliation mentality which tended to spread to all expenditure and continued throughout the budgetary procedure. Several agreements were subsequently reached to smooth the course of the budgetary procedure.

In March 1995 the institutions signed a joint declaration on the entry of financial provisions in legislative instruments to improve the 1982 declaration. Through this declaration, the institutions put an end to the practice of 'amounts deemed necessary' whilst taking account of the new legal situation resulting from the extension of the Parliament's legislative powers with the introduction, in certain areas, of the legislative co-decision procedure.

- Multiannual programmes adopted under the co-decision procedure include reference amounts which are binding on the institutions during the annual budgetary procedure.
- Multiannual programmes based on instruments not covered by the co-decision procedure do not include such amounts. Should the Council still wish to enter a financial reference in such an instrument, it will be taken as illustrative of the will of the legislative authority and is not, therefore, binding on the institutions during the budgetary procedure.
- In December 1996 a joint declaration was adopted on improving information to the budgetary authority on the negotiation and conclusion of fisheries agreements.
- In April 1997 the institutions agreed in principle that a letter of amendment should be presented towards the end of the budgetary procedure (October) to update expenditure forecasts for the agricultural sector.
- In July 1997 an Interinstitutional Agreement was concluded on the financing of the common foreign and security policy.
- In October 1998 agreement was reached on the question of legal bases and implementation of the budget, another point which had only partly been settled in the 1982 declaration. This agreement confirmed the principle that the utilisation of appropriations entered in the budget requires prior adoption of a basic legislative instrument. Exceptions to this principle were spelt out and may apply to three types of action: pilot projects, preparatory measures and one-off actions. In the first two cases, there are strict limits to these exceptions as regards both time and amounts.

Chapter 5

Establishment of a stable budgetary base for enlargement of the European Union: the Agenda 2000 package (2000–06)

In December 1995 the Madrid European Council called upon the Commission to present a communication on the future financial framework for the Union with a view to enlargement.

In response, the Commission produced its Agenda 2000 ⁽¹⁾ communication in July 1997. It followed this up in March 1998 with a detailed set of proposals for the reform of a number of Community policies, preparations for the accession of new Member States and the financial framework for the period ahead ⁽²⁾, and then in October 1998 a report on the own-resources system ⁽³⁾.

The context for the negotiations on these proposals was, in a number of respects, more difficult than at the time of the discussion of the Delors II package in 1992.

- Apart from establishing a new financial framework (taking into account the financial impact of the forthcoming enlargement), major decisions had to be taken on the reform of the CAP and structural operations. In contrast, at the time of the 1992 negotiations, the CAP had already undergone an initial reform prior to the establishment of the financial framework. In respect of structural operations, the primary concern had been the size of the allocations, with no substantial changes having been proposed in the basic rules. Enlargement to take in the Nordic countries and Austria was on the horizon, but these were relatively prosperous countries whose accession did not entail any additional net costs for the Union budget.
- There was far greater concern about imposing tight budget management in connection with the establishment of monetary union, whereas in 1992 the principle of raising the own-resources ceiling had been fairly broadly accepted from the outset.
- A number of Member States were very insistent on the issue of their net contribution to the Union budget, whereas in 1992 such demands had been more moderate.

Consequently, the negotiations on Agenda 2000 lasted nearly two years. The broad lines were agreed at the Berlin European Council in March 1999. A new Interinstitutional Agreement, containing the financial framework for 2000–06, was concluded on 6 May that year ⁽⁴⁾. The

⁽¹⁾ Agenda 2000: for a stronger and wider Union, COM(97) 2000; Bulletin EU, Supplement 5/97.

⁽²⁾ On these financial aspects: Communication from the Commission to the Council and the European Parliament on the establishment of a new financial perspective for the period 2000–2006, COM(98) 164, 18.3.1998. Report on the implementation of the Interinstitutional Agreement of 29 October 1993 on budgetary discipline and improvement of the budgetary procedure. Proposals for renewal, COM(98) 165, 18.3.1998. Commission working document. Draft Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure, SEC(1998) 698, 29.4.1998.

⁽³⁾ The financing of the European Union. Commission report on the operation of the own-resources system, COM(98) 560, 7.10.1998; Bulletin EU, Supplement 10/98.

⁽⁴⁾ Interinstitutional Agreement of 6 May 1999 between the European Parliament, the Council and the Commission on budgetary discipline and improvement of the budgetary procedure (OJ C 172, 18.6.1999, p. 1).

regulations on the reform of the CAP, on the new guidelines for structural operations and on the pre-accession financial instruments to be introduced were adopted in May and June. But it was not until September 2000 that the Council adopted the new regulation on budgetary discipline ⁽¹⁾ and the new decision on the own-resources system ⁽²⁾.

1. The Commission's proposals

1.1. The financial framework

The Commission's proposals maintained the own-resources ceiling at its 1999 level, i.e. 1.27 % of GNP, beneath which would be financed the reform of the common agricultural policy and structural operations, the continuation of the other internal policies and external action and an initial round of enlargement of the Union, while still leaving an adequate safety margin.

1) *Common agricultural policy*

The aim was to prevent any return to expensive surpluses, for which in future no export possibilities would exist under the new international rules, and so to be in the best possible position for the next round of WTO negotiations. The general guideline was to continue the path of the 1992 reform. Reductions in intervention prices were therefore proposed for arable crops (down by 20 % from the 2000/01 marketing year onwards), milk (down by 15 % over four years) and beef (down by 30 % over three years). These reductions would be largely offset by an increase in direct aid to producers. It was proposed that such aid should be degressive when it exceeded EUR 100 000 per holding. Reforms were also proposed for tobacco, olive oil and wine. Under these proposals, expenditure would initially have increased, before levelling off after 2003.

Another objective of the proposed reform was to back up the market organisation measures (intervention and compensatory aid) with a stronger and more uniform set of measures to promote rural development. The EAGGF Guarantee Section would have financed not only the rural accompanying measures brought in by the 1992 reform (forestry, early retirement and agri-environmental measures) but also operations which hitherto had come under Objectives 5a and 5b of the Structural Funds and structural measures for fisheries.

2) *Structural operations*

After the very sharp rise in allocations over the previous decade, the Commission's approach was to maintain the financial effort for cohesion at the relative level reached in 1999 (0.46 % of GNP), but to include in this overall amount the structural component of pre-accession aid and the cost of structural measures arising from the first round of enlargement of the Union. In the light of experience a three-fold approach was proposed.

- Concentration of resources, with the objectives assigned to the Structural Funds being reduced from seven to three: Objective 1 for the least well-off regions (per capita GDP less than 75 % of the Community average); a revised Objective 2 to cover areas undergoing change (in industry, services or fisheries), rural areas in decline and urban areas in

⁽¹⁾ Council Regulation (EC) No 2040/2000 of 26 September 2000 on budgetary discipline (OJ L 244, 29.9.2000, p. 27).

⁽²⁾ Council Decision 2000/597/EC, Euratom of 29 September 2000 (OJ L 253, 7.10.2000, p. 42).

difficulty; and a new Objective 3 to support the adaptation and modernisation of education, training and employment systems. It was also proposed that the number of Community initiatives be reduced from 14 to 3.

- Geographical concentration, achieved by strict application of the threshold of eligibility for Objective 1 and a reduction in the population numbers eligible for the new Objective 2. A phasing-out scheme was proposed for regions which would no longer be eligible.
- Simplification of the management rules.

3) The other areas of expenditure

The Commission's proposals reduced the pace of increases in ceilings for the other categories of expenditure compared with those which had been agreed for the previous period.

For internal policies the Commission proposed that priority be given to programmes which, at Community level, contributed most to growth and employment: the research framework programme, trans-European networks, education and training, environment and the promotion of small businesses. The ceiling for this category of expenditure was to rise in line with EU GNP.

On the other hand, the expenditure ceiling for external action would rise more slowly, following the sharp increase over the previous period. Apart from the candidate countries, the regions closest to the European Union would be given priority.

Administrative expenditure was set at levels which assumed there would be no increase in staff numbers, but an increase in foreseeable expenditure on pensions.

4) The impact of enlargement

The Commission proposed putting in place pre-accession aid for the 10 candidate countries of Central and Eastern Europe ⁽¹⁾ with three components.

- For these countries the Phare programme would be boosted and would focus on support for the development of administrative capacity and the investment required to take over the *acquis communautaire*.
- A second instrument (Sapard) would serve to modernise the agri-food chain and rural development projects.
- Lastly a structural instrument (ISPA) would contribute to financing projects on transport and the environment.

A constant annual allocation over the period 2000–06 was proposed for these three instruments. This amount would remain unchanged after the first accessions so that the remaining countries would then receive larger shares.

On enlargement, the assumption made was that six countries would join no earlier than 2002: Poland, Hungary, the Czech Republic, Slovenia, Estonia and Cyprus. The Commission proposed

⁽¹⁾ Cyprus and Malta qualified for the programmes for Mediterranean non-member countries.

that an overall amount be left available within the financial framework from that year on to cover the cost of this first round of enlargement.

- The assumptions concerning expenditure on agriculture were relatively limited. The Commission proposed that no direct compensatory aid should be granted to farmers in these countries, as accession should not, in principle, result in a lowering of internal agricultural prices for them. On the other hand, too sharp an increase in agricultural income in relation to other sectors of production would have a harmful distorting effect on the economy. In addition to market support measures, the bulk of spending would be on aid for rural development, which would take over from, and increase, the pre-accession aid granted for this.
- The largest amounts to be set aside for enlargement were on structural operations. The aim was to strike a balance between the enormous potential requirements of these countries and their ability to absorb and co-finance such aid, which would have to go to economically viable programmes.
- The other additional expenditure concerns the participation of the new Member States in internal Community policies and the administrative costs of the institutions.

1.2. The financing system

When the Delors II package was adopted, the Commission undertook to present a report on the own-resources system before the period ended in 1999. Given the importance of the budget financing aspects for the discussion of Agenda 2000 and the question of the distribution of the burden of financing raised by Germany, the Netherlands, Austria and Sweden, the Commission presented this report earlier than planned (October 1998). The report did not make specific proposals for reforming the existing system but analysed its functioning and reviewed possible amendments.

1) Operation of the system

The Commission found that the existing system had provided the necessary resources and had become fairer, insofar as the contributions from individual Member States were more or less in line with their 'ability to pay' in terms of their respective GNP. Two types of reform were considered:

- introduction of new own resources, closer in their nature to genuine tax resources;
- simplification of the system, which would involve replacing the VAT resource, and even traditional own resources, by the GNP resource alone.

2) The UK correction mechanism

The report noted that the context had changed since this mechanism was set up. The United Kingdom's relative prosperity had improved and it could not be considered the only country to experience a budgetary imbalance in relation to the EU budget. Originally the UK's budgetary imbalance had stemmed mainly from agricultural expenditure. However, the correction mechanism applied indistinctly to other categories of expenditure. Since these had come to account for a significantly larger proportion of the Community budget (in particular cohesion expenditure), the UK correction had departed from its original purpose. Similarly, upon enlargement, pre-accession expenditure, which benefited non-member countries and did not therefore

enter into the calculation of the correction, would be replaced (and the amounts increased) by internal EU expenditure, which would count towards the United Kingdom's correction.

3) *The issue of net contributions to the Community budget*

The report acknowledged the existence of a problem with the net contributions of Germany, the Netherlands, Austria and Sweden, and pointed to three possible ways, should a consensus be achieved, of dealing with this matter.

- One option would be to move towards a more straightforward and transparent own-resources system, stripped of all regressive aspects. This would include phasing out the UK correction, which imposed an additional burden on all the other Member States, and the full or partial replacement of the other resources by the GNP own resource.
- A second approach would be to introduce corrections on the expenditure side. The report considered, for instance, the possibility of only partial reimbursement of CAP direct aid to producers. The remainder, under regulations which would still be common to all Member States, would be paid from national budgets.
- A third possibility would be to introduce a generalised correction mechanism for negative balances with thresholds and parameters to be determined.

1.3. Renewal of the Interinstitutional Agreement

On the basis of the satisfactory application of the earlier agreement concluded in 1993, the Commission proposed that the instrument be renewed in its dual function of recording the agreement of the institutions on the financial framework and the arrangements for implementing it over the period covered and continuing with the improvement of the annual budgetary procedure.

The Commission took the view that the essential parts of the existing agreement should be retained. It proposed two adjustments of a more technical nature.

- The financial framework envisaged for 2000–06 offered less latitude than its predecessor. In particular it gave the Parliament a margin for manoeuvre over non-compulsory expenditure which, in overall terms over the period, was probably smaller than what the Parliament would have enjoyed under the terms of the Treaty. The Commission therefore proposed inserting flexibility mechanisms which would allow transfers between certain headings or allow amounts not used in one year to be spent the following year in excess of the ceilings. These procedures were less cumbersome than a revision of the financial framework but involved only limited amounts.
- The Commission also proposed consolidating and updating in the new agreement all the other arrangements for improving the budgetary procedure which the institutions had concluded in specific agreements or joint declarations. The conciliation procedure between the Parliament and the Council introduced in 1993 would be extended to all expenditure and would go on throughout the budget discussions, thereby confirming the practice which had been established *de facto*. In addition the rural development expenditure integrated in the reformed CAP would, under the Commission's proposal, be treated as non-compulsory expenditure.

2. The outcome of the negotiations

2.1. Stabilisation of Community expenditure

Stabilisation of expenditure was the main concern for the Member States during the negotiations, even beyond what was required to keep the own-resources ceiling at 1.27 % of GNP and to accommodate the first new Member States. Consolidation of expenditure was seen by all Member States as an essential contribution to the tight budgeting they had started to impose at national level. Stabilisation was also the means for net contributors to ensure that their deficit did not increase in absolute terms, especially as discussions revealed the difficulties in securing agreement on a substantial reform of the own-resources system.

TABLE 5.1 A – Financial perspective (EU-15)

EUR million at 1999 prices

Appropriations for commitments	2000	2001	2002	2003	2004	2005	2006
1. Agriculture	40 920	42 800	43 900	43 770	42 760	41 930	41 660
— CAP (not including rural development)	36 620	38 480	39 570	39 430	38 410	37 570	37 290
— Rural development and accompanying measures	4 300	4 320	4 330	4 340	4 350	4 360	4 370
2. Structural operations	32 045	31 455	30 865	30 285	29 595	29 595	29 170
— Structural Funds	29 430	28 840	28 250	27 670	27 080	27 080	26 660
— Cohesion Fund	2 615	2 615	2 615	2 615	2 515	2 515	2 510
3. Internal policies ⁽¹⁾	5 930	6 040	6 150	6 260	6 370	6 480	6 600
4. External action	4 550	4 560	4 570	4 580	4 590	4 600	4 610
5. Administration ⁽²⁾	4 560	4 600	4 700	4 800	4 900	5 000	5 100
6. Reserves	900	900	650	400	400	400	400
— Monetary reserve	500	500	250				
— Emergency aid reserve	200	200	200	200	200	200	200
— Guarantee reserve	200	200	200	200	200	200	200
7. Pre-accession aid	3 120	3 120	3 120	3 120	3 120	3 120	3 120
— Agriculture	520	520	520	520	520	520	520
— Pre-accession structural instrument	1 040	1 040	1 040	1 040	1 040	1 040	1 040
— Phare (applicant countries)	1 560	1 560	1 560	1 560	1 560	1 560	1 560
Total approps for commitments	92 025	93 475	93 955	93 215	91 735	91 125	90 660
Total appropriations for payments	89 600	91 110	94 220	94 880	91 910	90 160	89 620
Appropriations for payments as % of GNP	1.13%	1.12%	1.13%	1.11%	1.05%	1.00%	0.97%
Available for accession (approps for payments)			4 140	6 710	8 890	11 440	14 220
— Agriculture			1 600	2 030	2 450	2 930	3 400
— Other expenditure			2 540	4 680	6 440	8 510	10 820
Ceiling, appropriations for payments	89 600	91 110	98 360	101 590	100 800	101 600	103 840
Ceiling, payments as % of GNP	1.13%	1.12%	1.18%	1.19%	1.15%	1.13%	1.13%
Margin for unforeseen expenditure	0.14%	0.15%	0.09%	0.08%	0.12%	0.14%	0.14%
Own-resources ceiling	1.27%	1.27%	1.27%	1.27%	1.27%	1.27%	1.27%

⁽¹⁾ In accordance with Article 2 of Decision No 182/1999/EC of the European Parliament and of the Council and Article 2 of Council Decision 1999/64/Euratom (OJ L 26, 1.2.1999, p. 1 and p. 34), EUR 11 510 million at current prices is available for research over the period 2000-02.

⁽²⁾ The expenditure on pensions included under the ceiling for this heading is calculated net of staff contributions to the pension scheme, up to a maximum of EUR 1 100 million at 1999 prices for the period 2000-06.

TABLE 5.1 B – Financial framework (EU-21)*EUR million at 1999 prices*

APPROPRIATIONS FOR COMMITMENTS	2000	2001	2002	2003	2004	2005	2006
1. Agriculture	40 920	42 800	43 900	43 770	42 760	41 930	41 660
— Cap (not including rural development)	36 620	38 480	39 570	39 430	38 410	37 570	37 290
— Rural development and accompanying measures	4 300	4 320	4 330	4 340	4 350	4 360	4 370
2. Structural operations	32 045	31 455	30 865	30 285	29 595	29 595	29 170
— Structural funds	29 430	28 840	28 250	27 670	27 080	27 080	26 660
— Cohesion fund	2 615	2 615	2 615	2 615	2 515	2 515	2 510
3. Internal policies ⁽¹⁾	5 930	6 040	6 150	6 260	6 370	6 480	6 600
4. External action	4 550	4 560	4 570	4 580	4 590	4 600	4 610
5. Administration ⁽²⁾	4 560	4 600	4 700	4 800	4 900	5 000	5 100
6. Reserves	900	900	650	400	400	400	400
— Monetary reserve	500	500	250				
— Emergency aid reserve	200	200	200	200	200	200	200
— Guarantee reserve	200	200	200	200	200	200	200
7. Pre-accession aid	3 120	3 120	3 120	3 120	3 120	3 120	3 120
— Agriculture	520	520	520	520	520	520	520
— Pre-accession structural instrument	1 040	1 040	1 040	1 040	1 040	1 040	1 040
— Phare (applicant countries)	1 560	1 560	1 560	1 560	1 560	1 560	1 560
8. Enlargement			6 450	9 030	11 610	14 200	16 780
— Agriculture			1 600	2 030	2 450	2 930	3 400
— Structural operations			3 750	5 830	7 920	10 000	12 080
— Internal policies			730	760	790	820	850
— Administration			370	410	450	450	450
Total approps for commitments	92 025	93 475	100 405	102 245	103 345	105 325	107 440
Total appropriations for payments	89 600	91 110	98 360	101 590	100 800	101 600	103 840
of which: enlargement			4 140	6 710	8 890	11 440	14 220
Appropriations for payments as % of GNP	1.13%	1.12%	1.14%	1.15%	1.11%	1.09%	1.09%
Margin for unforeseen expenditure	0.14%	0.15%	0.13%	0.12%	0.16%	0.18%	0.18%
Own-resources ceiling	1.27%	1.27%	1.27%	1.27%	1.27%	1.27%	1.27%

⁽¹⁾ In accordance with Article 2 of Decision No 182/1999/EC of the European Parliament and of the Council and Article 2 of Council Decision 1999/64/Euratom (OJ L 26, 1.2.1999, p. 1 and p. 34), €11 510 million at current prices is available for research over the period 2000-02.

⁽²⁾ The expenditure on pensions included under the ceiling for this heading is calculated net of staff contributions to the pension scheme, up to a maximum of €1 100 million at 1999 prices for the period 2000-06.

1) Total expenditure

In the finally adopted financial framework, the overall ceiling on payments for the 15-member EU dropped appreciably, as a percentage of foreseeable GNP, from 2003 onwards to 0.97 % in 2006 as against 1.10 % in the 1999 budget. Including the amounts left available for an initial round of enlargement which was supposed to take place in 2002, there was still an unused margin beneath the own-resources ceiling ranging from 0.09 to 0.14 % of the GNP of the EU-15.

These payment ceilings took account of the need to cover the clearance of commitments entered into over the previous period. This meant that the constraints on the ceilings for new commitments were even tighter. These ceilings were, each year, lower than the amount in the 1999 budget, and of course lower than the ceilings set for that year in the previous financial framework.

2) Agricultural expenditure (Heading 1)

The definition of this heading was amended. It was agreed that the ceiling would no longer be the agricultural guideline but that it would correspond to the expenditure actually resulting from the reformed CAP. The guideline, a higher figure, continued to be calculated but it no longer appeared as such in the financial framework. Its scope was broadened to cover not only Heading 1 expenditure but also the agricultural components of pre-accession aid and the amount planned in this field for the forthcoming enlargement. Heading 1 also had two sub-headings: one applied to expenditure on common market organisations (intervention, direct aid for producers, veterinary and plant-health measures) and the other to rural development measures (measures accompanying the 1992 reform and structural measures previously coming under the Structural Funds).

The line taken during the negotiations was to set a level of expenditure for the reformed CAP of more or less the same amount as was entered in the 1999 budget. The necessary savings were first found by reducing intervention prices by less than proposed, hence the compensation in the form of aid to producers was less: the reduction in prices was 15 % in two stages for arable crops (instead of a single 25 % reduction) and 20 % (instead of 30 %) for beef. The reform of the milk sector was also postponed to the end of the period.

Other formulas were considered but not adopted:

- the possibility of reimbursing Member States only part of the expenditure they advance as direct aid to producers (a formula known as 'co-financing' expenditure);
- direct aid granted on a declining scale over time (known as 'degressivity') and/or above a certain threshold per farm (known as 'capping').

3) Structural operations (Heading 2)

The amounts set were lower than those proposed by the Commission. However, the proposals concerning the concentration of operations, the distribution criteria and the simplification of management methods were adopted without any major changes.

4) Other categories of expenditure

The ceilings for the internal policies, external action and administrative expenditure headings were appreciably lower than those proposed by the Commission. The reductions were imposed very much across the board, with no real discussion about the future content of these categories of expenditure. The starting point for this approach was not the existing 1999 ceilings but the lower figures of appropriations actually entered in the 1999 budget.

On the other hand, the amounts proposed by the Commission for pre-accession aid and for the estimated cost of the first round of enlargement were accepted without change.

2.2. Limited adjustment of the own-resources system

The Berlin European Council did not adopt any of the three options for rebalancing budget positions that the Commission had examined in its report. The solution to this problem was found instead in measures to contain expenditure growth and redirect flows. The results obtained were enhanced by relatively slight adjustments to the financing system.

The European Council decided:

- to lower the maximum call-in rate for the VAT resource to 0.75 % in 2002 and 0.50 % in 2004;
- to increase the percentage of traditional own resources that the Member States retain to cover collection costs from 10 to 25 %;
- to retain the United Kingdom correction, with some small adjustments, to offset for instance the benefit that would arise upon enlargement from the replacement of pre-accession aid by internal EU expenditure;
- to reduce the share paid by Germany, the Netherlands, Austria and Sweden in financing the UK correction to a quarter of their normal share.

2.3. Conclusion of a new Interinstitutional Agreement

1) *The rules for applying the financial framework*

These rules remained essentially unchanged. But some new provisions were added.

- Some restrictions were placed on the ‘privileged’ nature of expenditure on structural operations, in conjunction with the new basic regulations in this area. The allocations made in the financial framework continue to be expenditure targets, which must be entered into the budget each year. But the possibility of transferring to subsequent years the part of the allocations which could not be committed in a given year was confined to the first year of the period (2000) and then only if non-implementation was the result of a delay in the adoption of programmes.
- In the event of a revision of the financial framework, the ‘pre-accession’ heading and the amount left available for future enlargement were to be treated as ‘water-tight compartments’: in other words there could be no transfers between these two amounts nor between either of them and the ceilings for the other headings set for the EU-15.
- A ‘flexibility instrument’ was introduced. It was intended to allow financing, for a given financial year, of clearly identified expenditure which could not be financed beneath the ceilings available. This instrument was allocated EUR 200 million a year. The portion not used in a given year could be carried over for the following two years. Decisions to make use of the instrument were to be taken, during the budgetary procedure or in the course of the budget year, by joint agreement between the two arms of the budgetary authority, acting by qualified majority on a proposal from the Commission.

2) Budgetary procedure aspects

As proposed by the Commission the new agreement consolidated a number of arrangements made by the institutions to improve the operation of the budgetary procedure. Two additions were made.

- The conciliation procedure for the establishment of the budget was extended to cover all expenditure (compulsory and non-compulsory) and continued throughout the budgetary procedure.
- Guidelines were laid down, by broad categories, for the classification of expenditure.

3. Application of the financial framework, 2000–06

In general, the financial framework 2000–06 was applied following the implementing provisions as set out in the Interinstitutional Agreement (see Point 2.3. above). However, two issues deserve to be looked at more closely: the annual budget debates and the enlargement of the European Union.

3.1. The budget debates for 2000–06

The budget procedures for the years 2000–06 were undoubtedly smoothed by the existence of the new Interinstitutional Agreement (IIA). A series of challenges had to be faced, in particular in the field of external actions. The new flexibility instrument allowed for a financial response, which would not otherwise have been possible.

The limitations of the ceilings set by the European Council already became clear in 1999, with the impact on the budget of the conflict beginning in Kosovo at that time. Very quickly the Commission was forced to present two proposals (in November 1999 and May 2000) for the revision of the Heading 4 ceiling to accommodate the financing of a multi-annual programme of assistance for the Balkans region. These proposals, which were supported by the Parliament, met with Council opposition. For the 2000 and 2001 budgets, the solution found in each case was to apply the new flexibility instrument, the decision coming at the end of the budgetary procedure after difficult discussions on the necessary redeployment of expenditure on the other programmes covered by the heading.

In the budgetary procedures for 2002 and 2003 the Commission once again proposed using this instrument to finance, under Heading 2, a programme for the conversion of fishing vessels which, following the failure to renew the agreement with Morocco, could no longer operate in Moroccan waters.

The flexibility instrument was mobilised in each subsequent year of the financial framework. Part of the support for reconstruction in Iraq was financed through flexibility in 2004, 2005 and 2006. Rehabilitation and reconstruction needs in the countries affected by the Tsunami were funded in 2005 and 2006. Also under Heading 4 in 2006 compensation for the ACP sugar producers affected by the reform of the common market organisation for sugar, as well as part of the CFSP budget, was financed through flexibility.

Finally, in 2005, the mobilisation of the flexibility instrument allowed for financing part of the PEACE II programme ⁽¹⁾ (Heading 2) and of the budget for decentralised agencies (Heading 3).

3.2. Enlargement of the European Union

1) Determining the general budgetary framework

The overall Berlin framework envisaged annual amounts for 2002 to 2006, taking account of an enlargement in 2002 with a first group of six new Member States ⁽²⁾. A second group, lagging in progress, was not expected to join before 2007.

The Helsinki European Council in December 1999 opened up the possibility of more than six countries acceding during the period 2000–06.

While the assumption, made in Berlin, that the first round of enlargement would take place in 2002 was a justified precaution from the budgetary point of view, it turned out not to be realistic. Consequently, the accession date was moved back and the Laeken European Council of 14 and 15 December 2001 decided that 10 candidate countries ⁽³⁾ could be ready to join the EU in 2004. Negotiations with the remaining two (Bulgaria and Romania) would be opened on all chapters in 2002.

The delay created additional room under the ceilings because of the phasing-in of expenditure related to structural actions. Since the first accessions would take place later than 2002, the amounts foreseen for enlargement in 2002 and 2003 were no longer available ⁽⁴⁾. However, the annual amounts reserved for the period 2004–06, initially intended to cover the needs related to the third, fourth and fifth year of the accession of six new Member States, would now be available for the first three years of the accession of 10 new Member States.

On the other hand, the Berlin sub-ceiling for agriculture did not include any amounts for direct payments to farmers in the new Member States. In their position papers, however, all candidate countries demanded to be fully integrated into this aspect of the common agricultural policy upon accession. The Berlin ceiling did not provide for any transitional budgetary arrangements either, although such arrangements had been part of all accession agreements in the past.

As planned in Laeken, at the beginning of 2002 the Commission presented its global approach for the draft common positions in the fields of agriculture, regional policy and the budget ⁽⁵⁾. The Communication introduced the necessary adjustment of the Berlin scenario to take into account the later accession date and the increased number of acceding countries. It also presented the following new elements:

⁽¹⁾ The EU Programme for Peace and Reconciliation in Northern Ireland and the Border Region of Ireland.

⁽²⁾ Cyprus, the Czech Republic, Hungary, Poland, Estonia and Slovenia, also known as the ‘Luxembourg group’.

⁽³⁾ The Luxembourg group plus Latvia, Lithuania, Malta and Slovakia became from then on the ‘Laeken group’.

⁽⁴⁾ The annuality of the financial perspective ceilings did not allow transfer to later years.

⁽⁵⁾ Communication from the Commission — Information note — Common Financial Framework 2004–2006 for the Accession Negotiations, SEC(2002) 02 final.

- Given that immediate introduction of 100 % direct payments would have hampered rather than served modernisation in agriculture, it was proposed to phase in direct aids over a period of 10 years, thus well beyond the 2000–06 financial framework. This way the new Member States obtained assurance about when they would be fully integrated into the CAP.
- Certain measures were proposed to make the transition to the EU rural development policy better adapted to the needs of the new Member States, such as increasing the EU co-financing rate up to 80 % for the rural development measures financed by the EAGGF Guarantee Section.
- In order to find a middle ground between the limits on absorption capacity and a faster profile than envisaged in Berlin for the first three years after accession, it was proposed that the phasing-in for structural actions be increased, with Cohesion Fund expenditure boosted to 33 % of total structural actions, compared to 18 % for the other beneficiary Member States.
- Additional allocations would be made for nuclear safety, to support the effort to decommission nuclear plants, and for institution building, to enhance the building up of adequate administrative structures and administrative capacity.
- Transitional budgetary arrangements were proposed based on the principle that no new Member State should find itself in a net budgetary position vis-à-vis the EU budget which was worse than the year before enlargement.

2) Agreement on the EU common position

The Commission Communication was accepted as a general basis for discussion and most delegations found the overall approach to be balanced and realistic. There was general agreement that budgetary compensation, if any were to be granted, should be fully financed below the Berlin ceilings.

In October 2002 ⁽¹⁾, the Commission declared that, in line with the conclusions from the 2002 Regular Reports, the 10 countries of the Laeken group fulfilled the Copenhagen criteria and would be ready for membership from the beginning of 2004.

The Brussels European Council on 24–25 October endorsed these Commission findings and recommendations and took the final decisions with respect to the EU negotiating position. In Brussels EU leaders agreed on the following:

- Direct agricultural payments were to be introduced following a 10-year phasing-in schedule, expressed as a percentage of the level of such payments in the Union ⁽²⁾.
- A ceiling for Heading 1a (common agricultural policy) for the EU-25 covering the entire period up to 2013 was established on the basis of the 2006 ceiling, increased by 1 % per

⁽¹⁾ 'Towards the enlarged Union — Strategy paper and report of the European Commission on the progress towards accession by each of the candidate countries', COM(2002) 700 final.

⁽²⁾ 25% of the full EU rate in 2004, 30 % in 2005, 35 % in 2006, 40 % in 2007. Thereafter, in 10 % increments so as to ensure that the new Member States reach in 2013 the support level then applicable.

year in nominal terms. The overall expenditure for market-related expenditure and direct payments for each year in the period 2007–13 was to be kept below this ceiling.

- For reasons of absorption capacity, the total allocation for structural operations was reduced from EUR 25.5 billion to EUR 23 billion.
- The own resources *acquis* was to apply to the new Member States as from accession.
- Temporary budgetary compensation, offsetting any deterioration of the ex ante estimated net budgetary position of the new Member States in comparison with their situation in the year before accession, would be offered in the form of lump-sum, temporary payments on the expenditure side of the EU budget. The compensations had to remain within the annual margins left under the Berlin ceilings for enlargement.

After the Brussels Council the EU was now ready to negotiate the final terms of the accession with the candidate countries.

3) Agreement with the candidate countries in Copenhagen

After seven weeks of negotiations, on 13 December 2002, Heads of State or Government from the EU and 10 candidate countries reached agreement on the terms for enlarging the EU. Following the decision of the Copenhagen Summit, Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia would join the EU on 1 May 2004.

The Copenhagen agreement acknowledged the financial needs of new Member States, since they were all expected to enjoy the status of net beneficiary with regard to the EU budget from the very beginning, while respecting the ceilings established in the financial framework for enlargement.

Under the terms of the final agreement, the following elements had been added compared to the EU common position determined in Brussels:

- a lump-sum cash-flow facility in the year 2004 to help all countries improve their net budgetary position during the first year and to further reduce the risk of any country seeing its net position worsen in the first year of enlargement ⁽¹⁾;
- an extra package consisting of the Schengen facility, an increase in the rural development allocation and an increase in the transitional nuclear safety package;
- the cost of agricultural market measures had been recalculated to include the cost associated with some further concessions in this field.

All these measures, while increasing the expenditure, also automatically reduced the temporary budgetary compensation, which was calculated as the difference between each new Member State's estimated receipts from and payments to the EU budget (in comparison with the situation in the year before accession). To offset this mechanism, a further allocation was made available as additional budgetary compensation for the disadvantaged countries.

⁽¹⁾ This was justified by the fact that direct agricultural payments related to the year 2004 would only be reimbursed by the EU budget to Member States in 2005.

Finally, budgetary compensation was further increased for certain Member States, offset by an equivalent reduction of their cohesion expenditure.

4) The adjustment of the financial framework

As provided for by the 1999 Interinstitutional Agreement, the European Parliament and Council needed to adjust the financial framework to take account of the expenditure requirements resulting from enlargement. Following the proposals put forward by the Commission in February 2003 ⁽¹⁾, on 19 May 2003 the budgetary authority agreed on the adjustment of the financial framework in order to reconcile the EU-15 financial framework for the period 2004–06, at 1999 prices, with the situation of an enlarged Union of 25 members ⁽²⁾.

- The crucial modification was mainly technical and consisted in transferring appropriations for the 10 new Member States which had been earmarked in Heading 8 (enlargement) to the regular headings. Consequently, for agriculture, structural operations, internal policies and administration (Headings 1, 2, 3 and 5), the annual ceilings for commitments were raised in total by EUR 9 927 million for 2004, EUR 12 640 million for 2005 and EUR 14 901 million for 2006.
- As for pre-accession aid (Heading 7, renamed ‘pre-accession strategy’), the ceiling remained unchanged but it was set to also cover appropriations for pre-accession assistance concerning Turkey (previously included in Heading 4). For Bulgaria and Romania the amounts ear-marked for pre-accession instruments (Phare, Sapard and ISPA) were increased for the remaining years of the period by 20 %, 30 % and 40 % respectively compared to the average of the preceding years.
- A new Heading 8 (compensation) was introduced, including the amounts envisaged for the so-called ‘temporary budgetary compensation’ and ‘special lump-sum cash-flow facility’ in favour of the 10 acceding countries. The amounts were EUR 1 273 million in 2004, EUR 1 173 million in 2005 and EUR 940 million in 2006.
- A provision was included in the adjusted financial framework whereby, in the event of a political settlement leading to the reunification of Cyprus, supplementary amounts would be automatically added to each of the headings concerned. The budgetary implications resulting from the implementation of such a political settlement were estimated for the period at EUR 273 million at 1999 prices.

Compared to the situation envisaged in the Interinstitutional Agreement, the overall ceiling for commitment appropriations, at 1999 prices, was reduced by EUR 410 million for 2004, EUR 387 million for 2005 and EUR 939 million for 2006. In accordance with the Copenhagen European Council conclusions, the corresponding overall ceiling in payments (EU-25) for the years 2004–06 remained unchanged compared to the corresponding ceiling set out in Annex I

⁽¹⁾ Proposal for a Decision of the European Parliament and the Council on the adjustment of the financial perspective for enlargement, COM(2003) 70.

⁽²⁾ Decision 2003/429/EC of the European Parliament and of the Council of 19 May 2003 on the adjustment of the financial perspective for enlargement (OJ L 147, 14.6.2003, p. 25).

of the IIA. The own-resources ceiling for EU-25 remained unchanged in percentage terms and was established at 1.24 % of GNI-25.

Furthermore, following the joint decision of the European Parliament and Council on the adjustment of the financial framework for enlargement, both arms of the budgetary authority agreed to revise the financial framework, increasing the annual ceilings for commitments in Heading 3 (internal policies) by EUR 50 million for 2004, EUR 190 million for 2005 and EUR 240 million for 2006.

The resulting financial framework for an enlarged European Union with 25 members, at 1999 prices, is presented in Table 5.2 ⁽¹⁾.

The corresponding financial framework resulting from the technical adjustment for 2004, in line with movements in gross national income and prices, is presented in Table 5.3 ⁽²⁾.

5) *The accession of Bulgaria and Romania*

After the long and difficult negotiations on the budgetary aspects of the accession of the 10 new Member States, it was clear from the outset that the budgetary negotiation with Bulgaria and Romania would be very much predetermined by the outcome of the 2004 accession.

On the one hand, it would be hard to imagine that the 25 Member States (including the 10 that had recently acceded) would be willing to offer a different (i.e. more generous) package to Bulgaria and Romania. On the other hand, it would be inconceivable that both candidate countries, being less affluent than the 10 new Member States in terms of GDP per capita, would settle for anything less. In view of these particular circumstances, the negotiations on the budgetary package went quite smoothly and the final agreement was almost identical to the Commission proposal (which was in line with the outcome of the accession of the 10).

The main lines of the budgetary package for Bulgaria and Romania were:

- phasing-in of direct agricultural payments over a 10-year period;
- phasing-in of structural actions over a three-year period;
- a three-year lump-sum cash-flow facility, which included the Schengen facility;
- no temporary budgetary compensation, since it was clear that neither Bulgaria nor Romania were at risk of seeing their budgetary situation vis-à-vis the EU budget deteriorate after accession in comparison with the situation in 2006.

Finally, there was no need for an adjustment of the financial framework since the accession negotiations coincided with the negotiations on the new financial framework and all the amounts scheduled for both new Member States were already incorporated.

⁽¹⁾ Decision of the European Parliament and of the Council of 19 May 2003 on the revision of the financial perspective, OJ L 147, 14.6.2003, p. 31.

⁽²⁾ *idem*.

TABLE 5.2 – Financial framework (EU-25) adjusted for enlargement

(EUR million at 1999 prices)

Commitment appropriations	2000	2001	2002	2003	2004	2005	2006
1.a. Agriculture	40 920	42 800	43 900	43 770	44 657	45 677	45 807
2. Structural actions	32 045	31 455	30 865	30 285	35 665	36 502	37 940
— Structural Funds	29 430	28 840	28 250	27 670	30 533	31 835	32 608
— Cohesion Fund	2 615	2 615	2 615	2 615	5 132	4 667	5 332
3. Internal policies	5 930	6 040	6 150	6 260	7 877	8 098	8 212
4. External actions	4 550	4 560	4 570	4 580	4 590	4 600	4 610
5. Administration ⁽¹⁾	4 560	4 600	4 700	4 800	5 403	5 558	5 712
6. Reserves	900	900	650	400	400	400	400
— Monetary reserve	500	500	250	0	0	0	0
— Emergency aid reserve	200	200	200	200	200	200	200
— Guarantee reserve	200	200	200	200	200	200	200
7. Pre-accession strategy	3 120	3 120	3 120	3 120	3 120	3 120	3 120
— Agriculture	520	520	520	520			
— Pre-accession structural instrument	1 040	1 040	1 040	1 040			
— Phare (applicant countries)	1 560	1 560	1 560	1 560			
8. Compensation					1 273	1 173	940
Total appropriations for commitments	92 025	93 475	93 955	93 215	102 985	105 128	106 741
Total appropriations for payments	89 600	91 110	94 220	94 880	100 800	101 600	103 840
Ceiling, approps for payments as % of GNI (ESA 95)	1.07 %	1.08 %	1.11 %	1.10 %	1.08 %	1.06 %	1.06 %
Margin for unforeseen expenditure	0.17 %	0.16 %	0.13 %	0.14 %	0.16 %	0.18 %	0.18 %
Own-resources ceiling	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %

(1) The expenditure on pensions included under the ceiling for this heading is calculated net of staff contributions to the pension scheme, up to a maximum of EUR 1 100 million euros at 1999 prices for the period 2000–06.

TABLE 5.3 – *Financial framework (EU-25) adjusted for enlargement*

(EUR million at 2004 prices)

Commitment appropriations	Current prices				2004 prices		
	2000	2001	2002	2003	2004	2005	2006
1ac. Agriculture	41 738	44 530	46 587	47 378	49 305	50 431	50 575
— Common agricultural policy	37 352	40 035	41 992	42 680	42 769	43 724	43 735
— Rural development	4 386	4 495	4 595	4 698	6 536	6 707	6 840
2. Structural actions	32 678	32 720	33 638	33 968	41 035	41 685	42 932
— Structural Funds	30 019	30 005	30 849	31 129	35 353	36 517	37 028
— Cohesion Fund	2 659	2 715	2 789	2 839	5 682	5 168	5 904
3. Internal policies	6 031	6 272	6 558	6 796	8 722	8 967	9 093
4. External actions	4 627	4 735	4 873	4 972	5 082	5 093	5 104
5. Administration ⁽¹⁾	4 638	4 776	5 012	5 211	5 983	6 154	6 325
6. Reserves	906	916	676	434	442	442	442
— Monetary reserve	500	500	250	0	0	0	0
— Emergency aid reserve	203	208	213	217	221	221	221
— Guarantee reserve	203	208	213	217	221	221	221
7. Pre-accession strategy	3 174	3 240	3 328	3 386	3 455	3 455	3 455
— Agriculture	529	540	555	564			
— Pre-accession structural instrument	1 058	1 080	1 109	1 129			
— Phare (applicant countries)	1 587	1 620	1 664	1 693			
8. Compensation					1 410	1 299	1 041
Total appropriations for commitments	93 792	97 189	100 672	102 145	115 434	117 526	118 967
Total appropriations for payments	91 322	94 730	100 078	102 767	111 380	112 260	114 740
Ceiling, approps for payments as % of GNI (ESA 95)	1.07 %	1.08 %	1.11 %	1.09 %	1.08 %	1.06 %	1.06 %
Margin for unforeseen expenditure	0.17 %	0.16 %	0.13 %	0.15 %	0.16 %	0.18 %	0.18 %
Own-resources ceiling	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %	1.24 %

(1) The expenditure on pensions included under the ceiling for this heading is calculated net of staff contributions to the pension scheme, up to a maximum of EUR 1 100 million at 1999 prices for the period 2000–06.

Chapter 6

The policy challenges and budgetary means of the enlarged Union: The Multiannual Financial Framework 2007–13

In February 2004, the Commission presented its approach ⁽¹⁾ for the Multiannual Financial Framework (MFF) 2007–13. The document included the proposed breakdown of expenditure by broad category for the period 2007–13. In July 2004, the Commission confirmed and detailed its original stance ⁽²⁾ and proposed a new Interinstitutional Agreement (IIA) on budgetary discipline and improvement of the budgetary procedure ⁽³⁾. After intense negotiations at European Council level in June 2005, agreement on a MFF for 2007–13 was reached among Heads of State or Government at the Brussels European Council on 15–16 December 2005.

The European Council agreement was the starting point for negotiations between the European Parliament, the Council and the Commission which led to the three institutions signing the Interinstitutional Agreement on budgetary discipline and sound financial management on 17 May 2006 ⁽⁴⁾.

The Council adopted a new decision on the own resources of the Communities on 7 June 2007 ⁽⁵⁾.

Two influential factors shaping the negotiation context should be stressed in particular:

- The Treaty establishing a Constitution for Europe had been adopted by the European Council on 17 July 2003 but the ratification process in the Member States did not succeed. The rejection of the draft Constitution by France on 29 May 2005 and by the Netherlands on 1 June 2005 led to a prolonged period of institutional and political uncertainty in the EU.
- The discussions occurred in a context of disagreements among a number of Member States on key international issues, in particular the war in Iraq.

The negotiation was further influenced by three very important considerations:

- The enlargement to new Member States would add only 5 % to the Union's GDP — and to its revenues — but the increase in population would amount to 30 %. It followed that

⁽¹⁾ Communication from the Commission to the Council and the European Parliament 'Building our common future. Policy challenges and budgetary means of the enlarged Union 2007–2013', COM(2004) 101 final/2, 26.2.2004.

⁽²⁾ Communication from the Commission to the Council and the European Parliament 'Financial perspective 2007–2013', COM(2004) 487 final/2, 14.7.2004 and 'Financing the European Union. Commission report on the operation of the own-resources system', COM(2004) 505 final, Vol. I and II, 14.7.2004.

⁽³⁾ COM(2004) 498, 14.7.2004. The Commission's proposals were updated in April 2005 (see: Commission working document 'Technical adjustments to the Commission proposals for the multiannual financial framework 2007–2013', SEC(2005) 494 final, 12.4.2005).

⁽⁴⁾ OJ C 139, 14.6.2006.

⁽⁵⁾ Council Decision 2007/436/EC, Euratom of 7 June 2007 on the system of the European Communities' own resources (OJ L 163, 23.6.2007). The decision came into force on 1 March 2009 after being ratified by all Member States, with retroactive effect from 1 January 2007.

EU budget expenditure would increase more than revenue, particularly in view of the fact that — as stressed by the Commission — enlargement would mean four million additional farmers, an increase of 50 %, and a doubling of income disparities between rich and poor.

- During the final stage of the negotiation opening the way for enlargement, in October 2002, the European Council reached a compromise on agricultural spending in an enlarged Union until 2013 at the instigation of France and Germany. This decision predetermined a large share of the EU budget even before the Commission made its proposals (see Chapter 5 for more details on the budgetary impact of enlargement).
- Again prior to the Commission proposals, six Member States (Germany, France, the Netherlands, Austria, Sweden and the United Kingdom) — all net contributors to the EU budget — informed the Commission that they did not see room for an EU budget near the current ceiling for own resources. The ‘letter of the six’, sent to the President of the Commission on 15 December 2003 ⁽¹⁾, stressed that average expenditure during the next MFF should not exceed 1.0 % of EU GNI, including agriculture spending within the ceiling set by the European Council in October 2002. This letter did not specify whether the 1.0 % limit applied to payments or to commitment appropriations.

In such a context, obtaining an agreement proved particularly lengthy and difficult. The negotiations on the MFF and the new own-resources decision stretched over almost three and a half years. The negotiations were once again largely shaped by the issue of Member States’ net contributions and growing concerns about the level of national contributions.

1. The Commission’s proposals

1.1. The multiannual financial framework 2007–2013

The Commission’s proposal, published in February 2004, reflected an ambitious approach taking into account the various constraints imposed by the circumstances, notably the need for integrating the spending levels for the common agricultural policy agreed upon in October 2002 into its proposal.

As can be seen in Table 6.1, the initial Commission proposal contained a marked shift in the allocation of resources between the different budget headings, and, in particular, a ‘shift towards growth and employment with a focus on knowledge-based activities such as research and innovation’ ⁽²⁾.

Overall, the proposals made by the Commission entailed an increase in spending as a percentage of EU GNI from 1.09 % of GNI for payment appropriations in 2006 to a foreseen average 1.14 % of GNI, taking into account enlargement and the requirements related to both the renewed Lisbon agenda, and external objectives, e.g. in the context of the European Neighbourhood Policy. Right from the start, it was quite clear that the final result on commitment

⁽¹⁾ See Information to the Press — IP/03/173 from the Commission: <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/03/1731&format=HTML&aged=1&language=EN&guiLanguage=en>

⁽²⁾ Cf. European Commission: New proposals for growth and jobs under the next Financial Framework 2007–2013, Brussels, 6 April 2005 (IP/05/389).

TABLE 6.1 – *Shift in the allocation of resources between budget headings 2006–13 according to the Commission's original proposal from February 2004*

(EUR million at constant 2004 prices)

Commitment appropriations	2006 ⁽¹⁾	2007	2013	Difference
				2006–2013
1. Sustainable growth	47 582	59 675	76 785	+ 61.4 %
1a. Competitiveness for growth and employment	8 791	12 105	25 825	+ 193.8 %
1b. Cohesion for growth and employment ⁽²⁾	38 791	47 570	50 960	+ 31.4 %
2. Preservation and management of natural resources	56 015	57 180	57 805	+ 3.2 %
of which market-related expenditure and direct payments	43 735	43 500	42 293	- 3.3 %
3. Citizenship, freedom, security and justice	1 381	1 630	3 620	+ 162.1 %
4. The EU as a global partner ⁽³⁾	11 232	11 400	15 740	+ 40.1 %
5. Administration ⁽⁴⁾	3 436	3 675	4 500	+ 31.0 %
6. Compensations	1 041			
Total appropriations for commitments	120 688	133 560	158 450	+ 31.3 %
Total appropriations for payments ^(b) ^(c)	114 740	124 600	143 100	+ 24.7 %
% of GNI	1.09 %	1.15 %	1.15 %	
Margin	0.15 %	0.09 %	0.09 %	
Own-resources ceiling	1.24 %	1.24 %	1.24 %	

⁽¹⁾ 2006 expenditure under the MAFF 2000–06 has been broken down according to the proposed new nomenclature to facilitate comparisons.

⁽²⁾ Includes expenditure for the Solidarity Fund (EUR 1 billion in 2004 at current prices) as from 2006. However, corresponding payments are calculated only as from 2007.

⁽³⁾ Integration of the EDF into the EU budget is assumed to take effect in 2008. EDF commitments for 2006 and 2007 are included only for comparison purposes. Payments on commitments before 2008 are not taken into account in the payment figures.

⁽⁴⁾ Includes administrative expenditure for salaries, pensions, European Schools and institutions other than the Commission. Other administrative expenditures are included in the first four expenditure headings.

Source: Figures based on COM(2004) 101 final, 10.2.2004, p. 29.

appropriations would lie somewhere between the Commission's proposal and the 1.0 % limit set by six of the net contributors.

The agreement already reached on agricultural expenditure and the critical importance of cohesion policy for a number of Member States — and in particular the increased needs related to enlargement — *de facto* limited the room for manoeuvre for negotiations. As shown in Section 2, the Commission's ambitions, most notably regarding the Lisbon agenda, had to be significantly down-sized by the time of a final agreement.

However, examining the Commission proposals in greater detail, it is useful to highlight the following innovative elements pointing towards the realisation of the Lisbon goals. The Commission made budgetary but also qualitative proposals aimed at achieving these goals ⁽¹⁾.

⁽¹⁾ All quotes in this subsection refer to COM(2004) 101 final, op. cit.

1a) Competitiveness for growth and employment

The Commission made very ambitious proposals to strengthen the European effort in research and technological development. The proposals included the idea of creating a European research area, to act as an internal market for research and technology, and a very significant increase in direct financial support for research and student mobility.

Additional efforts were envisaged in the area of trans-European networks on the basis of the new TEN-guidelines which included interconnecting high-speed rail lines by 2012, developing a core rail freight network in central Europe by 2015, and a package to connect ports and land transport by 2010.

Another innovative element was a Growth Adjustment Fund of up to EUR 1 billion per year, available within the competitiveness for growth and employment heading. This new fund was intended to optimise the delivery of the growth and cohesion objectives by introducing flexibility margins in the budget to enable the EU to react swiftly to changing economic circumstances (a proposal which was subsequently rejected by the Council).

1b) Cohesion for growth and employment

The Commission pushed for the Lisbon goals to be integrated into the national or regional development plans to be negotiated as part of the cohesion policy. Resources would be concentrated on investment in order to increase and improve the stock of physical and human capital and thus exert maximum impact on competitiveness and growth. Emphasis would thus be placed on job creation in new activities. Particularly for the second objective of the cohesion policy, the 'regional competitiveness and employment' goal, the Commission made it clear that 'interventions would need to concentrate on a limited number of policy priorities linked to the Lisbon and Göteborg agenda'.

2) Sustainable management and protection of natural resources

The reform of the common agricultural policy (CAP), decided in the wake of the agreement of October 2002, was 'aimed at meeting the objectives of competitiveness, solidarity and better integration of environmental concerns thus becoming a key step in the Lisbon and Göteborg development strategy' and involved three key elements. First, a substantial simplification, by decoupling direct payments to farmers from production. Second, further strengthening rural development by transferring funds from market support to rural development through reductions in direct payments to bigger farms (modulation). Third, a financial discipline mechanism would set a ceiling on expenditure on market support and direct aid between 2007 and 2013.

In the environment area, priorities would include implementing the EC Climate Change programme, a number of thematic strategies addressing specific environmental priorities and the Environmental Technology Action Plan (ETAP), and developing and implementing the Natura 2000 network in the area of biodiversity.

3) Citizenship, freedom, security and justice

A starting point for the Commission proposals was the recognition that 'the challenges posed by immigration, asylum, and the fight against crime and terrorism can no longer be met adequately by measures taken only at the national level'. Besides, enlargement would bring

particular challenges, for example in terms of the security of 'our external borders'. Specific importance was thus given to a common asylum policy and a common policy on immigration, as well as an effective area of justice and preventing and fighting crime and terrorism.

4) *The EU as a global player*

The Commission stressed that the Union has developed a broad, though incomplete, spectrum of external relations tools and that enlargement would entrust the EU with even greater responsibilities, as a regional leader and as a global partner. Therefore, the expanded EU would stabilise its wider neighbourhood and support its development through close cooperation. It would create a 'stability circle' meaning a common space, a community of 'everything but the institutions'.

Cooperation with developing countries would focus on the eradication of poverty, making a 'strong and coherent contribution to progress towards reaching the Millennium development goals, set at the 2000 United Nations General Assembly'.

1.2. The financing system

According to own-resources decision 2000/597/EC, Euratom, the Commission was to undertake a general review of the own-resources system before 1 January 2006. In response to a request from the European Parliament, the Commission had furthermore undertaken (in a statement annexed to the Council minutes when Decision 2000/597/EC, Euratom was adopted) to submit this review before the end of 2004.

When the Commission subsequently adopted its first Communication on the post-2006 MFF on 1 February 2004 ⁽¹⁾, it set out the basic principles for the reform of the financing system. A communication, a detailed report ⁽²⁾ and a proposal for a new own-resources decision and related implementing regulation on a generalised correction mechanism ⁽³⁾ were adopted by the Commission on 14 July 2004, together with more detailed proposals on spending.

The 2004 own-resources report included two major features that could transform the own-resources system:

- The report proposed replacing the specific correction mechanism used for one country only (the United Kingdom) by a general correction mechanism applying to any country that fulfilled relevant pre-determined criteria. The new mechanism was to be effective from 2007, with phasing-in provisions to facilitate the transition for the UK.

⁽¹⁾ See COM(2004) 101 final, op. cit.

⁽²⁾ See 'Financing the European Union. Commission report on the operation of the own-resources system', COM(2004) 501 final, Vols I and II, 14.7.2004.

⁽³⁾ See Proposal for a Council Decision on the system of the European Communities' own resources and Proposal for a Council Regulation on the implementing measures for the correction of budgetary imbalances in accordance with Articles 4 and 5 of the Council Decision on the system of the European Communities' own resources, COM(2004) 501 final/2, 2004/0170 (CNS), 2004/0171 (CNS), 3.8.2004. NB: This is the reference of the proposals *cum corrigendum* only in English. COM(2004) 501 final was adopted on 14 July 2004.

- The report also presented ‘three main candidates as possible future fiscal own resources: a resource based on 1. energy consumption, 2. national VAT bases and 3. corporate income’. It called on the Council ‘to take note of the Commission’s intention to prepare a roadmap in view of replacing, on the basis of a Commission proposal, the current VAT resource by a genuine tax-based own resource by 2014’ ⁽¹⁾.

The Commission thus formally proposed a thorough reform of the system of correcting budgetary imbalances by progressively replacing the UK correction with a generalised correction mechanism with the same rules applying to all Member States without exception. For the first time since the introduction of the UK correction in 1984, there was consequently a concrete proposal on the Council’s table which placed the correction on the political agenda as an item for discussion.

This proposal was justified on two grounds:

- The necessity to treat equally Member States that are in comparable positions. The UK benefited from a special rebate mechanism, which did not benefit a number of net contributors with broadly similar levels of GNI. This was contrary to the principle adopted at the 1984 Fontainebleau European Council that ‘any Member State sustaining a budgetary burden which is excessive in relation to its relative prosperity may benefit from a correction at the appropriate time’.
- The analysis of the evolution of the UK correction following enlargement highlighted that the correction would increase over time to such an extent that the UK would become the smallest net contributor. In fact, it could be argued that the UK would not be contributing its fair share to the cost of enlargement, despite being one of the main advocates of such enlargement. This last argument proved instrumental in leading to a modification of the UK correction (see Chapter 12).

Under the Luxembourg and UK presidencies (first and second halves of 2005) the focus of the negotiations among Member States shifted away from the Commission’s proposals: there would be no generalised correction mechanism nor an implementing regulation. The ‘negotiating boxes’ of these Presidencies instead sought ad hoc changes to the current own-resources system in order to accommodate specific interests of the Member States in the context of a global agreement on the expenditure and revenue side of the post-2006 MFF.

Consequently, following broad political agreement achieved during the European Council on 15–16 December 2005, a new own-resources decision was adopted, more than a year later, in June 2007 ⁽²⁾. This long delay, necessary to reach a final consensus on the fine-tuning of the legal text, was symptomatic of the difficulties and complexity of the broad political agreement achieved.

⁽¹⁾ See COM(2004) 505 final, Vol. I, op. cit.

⁽²⁾ See Council Decision 2007/436/EC, Euratom, op. cit.

1.3. Renewal of the Interinstitutional Agreement

The preparation of a new IIA — until the entry into force of the Lisbon Treaty *the* document laying down the MFF and its accompanying rules on budgetary discipline and budgetary procedure — extended over two years:

On 14 July 2004 the Commission presented its proposal ⁽¹⁾ for the renewal of the IIA on budgetary discipline and improvement of the budgetary procedure for the period 2007–13.

This proposal was followed by a European Parliament resolution on ‘Policy challenges and budgetary means of the enlarged Union 2007–13’ ⁽²⁾, and a resolution on the Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure ⁽³⁾.

Following the political agreement on the MFF 2007–13 reached by the European Council on 15–16 December 2005 ⁽⁴⁾, the European Parliament adopted a resolution on the European Council’s position on the MFF and the renewal of the Interinstitutional Agreement 2007–13 ⁽⁵⁾.

On this basis, a working document on a revised proposal ⁽⁶⁾ was tabled by the Commission in February 2006. After further negotiation between the three institutions, the IIA was signed on 17 May 2006 ⁽⁷⁾.

The proposals made by the Commission for a new IIA suggested maintaining unchanged the main features of the MFF. Agenda 2000 had successfully fulfilled its main purposes as regards financial discipline, the orderly evolution of expenditure and interinstitutional collaboration during the budgetary procedure. The budget of the European Union had been adopted on time each year, and the two arms of the budgetary authority had jointly adjusted Agenda 2000 to face the supplementary financial requirements linked to the enlargement to 10 new Member States on 1 May 2004.

On the other hand, the Commission stressed the importance of flexibility as ‘the essential corollary to financial discipline’. If properly designed, it contributes to enhancing effective resources allocation while allowing responding to unforeseen needs or new priorities. Several parameters influence the degree of flexibility of the MFF: the length of the period covered by the MFF; the number of expenditure headings; the margins available within each expenditure ceiling; the margin below the own-resources ceiling; the share of EU spending pre-determined by ‘amounts of reference’ in co-decided legislation; pre-allocated multiannual programmes; and the general attitude towards using the revision procedure. The degree of flexibility has

(1) See Commission Working Document ‘Proposal for renewal of the Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure’, COM(2004) 498 final, 14.7.2004.

(2) See European Parliament document P6_TA(2005)0224.

(3) See European Parliament document P6_TA PROV(2005)0453.

(4) See Document 15915/05 Cadre fi n 268, 19.12.2005.

(5) See PE 368.274, B6-0049/2006.

(6) See Commission Working Document ‘Revised proposal for renewal of the Inter-institutional Agreement on budgetary discipline and improvement of the budgetary procedure’, COM(2006) 36 final, 1.2.2006, and Commission Working Document ‘Contribution to the interinstitutional negotiations on the proposal for renewal of the Interinstitutional Agreement on budgetary discipline and improvement of the budgetary procedure’, COM(2006) 75 final, 15.2.2006.

(7) OJ C 139, 14.6.2006, p. 1.

evolved over time with the changing mix of those parameters. As shown below, several modifications and new instruments, as well as a reduction in the number of headings, brought additional flexibility to the system and yet, as shown below, the MFF proved not to be flexible enough in the light of the unprecedented budgetary challenges faced in that period due to the evolution of the payments compared to implementation forecasts.

2. The outcome of the negotiations

2.1. Overall level of expenditure

Stabilisation or even reduction of contributions to the EU budget was a priority for a number of ‘net contributors’, as reflected in the ‘letter of the six’ (cf. *supra*) which argued that average expenditure during the next MFF should not exceed 1.0 % of EU GNI. The letter did not specify whether the 1.0 % related to commitment or to payment appropriations, which opened up a useful margin for negotiation. Indeed, during the negotiations this norm related first to commitment appropriations, then, at a later stage in the negotiation, to payment appropriations — an objective easier to comply with. Nevertheless, the constraint imposed by the letter weighed heavily in the negotiation, in particular as the new Member States were very keen on securing an agreement which would grant them access to substantial additional expenditure from the EU budget.

Table 6.2 below illustrates the dynamics of negotiation. The process started with a Commission proposal which intended to create a strong impetus for, notably, Lisbon-related expenditures. The European Parliament suggested limited shifts across headings, in particular an increase in Heading 3. The subsequent Council discussions led to markedly reduced overall levels of commitment appropriations under the Luxembourg and UK presidencies. The conclusion of the Interinstitutional Agreement allowed for a very limited upward adjustment to those reductions.

The agreed total amounts for commitment appropriations from 2007 to 2013 (Table 6.3) illustrate another facet of that MFF: The global ceiling for commitment appropriations was expected to fall sharply from 1.10 % of EU GNI in 2007 to 1.01 % in 2013 (and from 1.06 % to 0.94 % for payment appropriations). This included the (increasing) cost of enlargement, considering the phasing-in of various policies, in particular the CAP, in the new Member States. In real terms (euro at constant prices) however, the ceilings were still growing (moderately) each year from 2007 to 2013.

2.2. A moderate shift in the budget structure

Although the Council and the Member States agreed on the importance of an ambitious Lisbon and Göteborg agenda, and the related need to increase efforts in areas such as research or the environment, this proved difficult to translate into budgetary terms. For many Member States cohesion policy, agriculture, and specific rebates on their contributions came as priorities in the MFF negotiations. Sub-heading 1a (covering expenditure with the strongest link towards the Lisbon agenda) suffered most from the cuts made to the Commission proposal. Nevertheless, when comparing 2013 with 2006, the last year of the preceding financial framework, sizeable increases could still be secured for both sub-heading 1a and Heading 3 as shown in Table 6.4.

2.3. Limited adjustment of the own-resources system

In the agreement it reached on 15–16 December 2005, the European Council took the following main decisions on the future own-resources system:

- The ceilings laid down in the decision on own resources should be maintained at their current level of 1.24 % of EU GNI for appropriations for payments and of 1.31 % EU GNI for appropriations for commitments;
- The distinction between agricultural duties and customs duties would be abolished;
- ‘In the interests of transparency and simplicity’, in particular the elimination of the complex frozen rate mechanism, the uniform rate of call of the VAT-based resource would be fixed at 0.30 % (see Chapter 12).
- For the period 2007–13 only, the rate of call of the VAT-based resource would be fixed at 0.225 % for Austria, 0.15 % for Germany and 0.10 % for the Netherlands and Sweden.
- For the period 2007–13 only, the Netherlands would benefit from a gross reduction in its annual GNI contribution of EUR 605 million and Sweden from a gross reduction in its annual GNI contribution of EUR 150 million, measured in 2004 prices.
- The correction mechanism in favour of the United Kingdom should remain, along with the reduced financing share of the correction benefiting Germany, Austria, Sweden and the Netherlands (25 %). However, after a phasing-in period between 2009 and 2011, the United Kingdom should participate fully in financing the costs of enlargement, except for direct agricultural payments and market-related expenditure, and that part of rural development expenditure originating from the European Agricultural Guidance and Guarantee Fund (EAGGF), Guarantee Section. The corresponding reduction of the UK correction should not exceed EUR 10.5 billion in constant 2004 prices during the period 2007–13.

Whilst the Own-Resources Decision covers the same period as the MFF, its adoption usually proceeds with a certain time lag. In practice, it took more than a year to translate the above political agreements into legal texts. Secondly, the Council Decision had to be ratified by all Member States as provided for in Article 269 of the Treaty establishing the European Community. The ratification procedure that followed the adoption of the Council Decision on the system of the European Communities ⁽¹⁾ on 7 June 2007 lasted until February 2009. The decision entered into force on 1 March 2009 with retroactive effect on 1 January 2007 as provided for in the decision itself. The necessary budgetary adjustments were implemented by means of an Amending Budget in mid-2009.

Overall, the own-resources system remained largely unchanged. However, with the notable exception of fixing the rate of call of the VAT-based resource, the changes introduced rendered the system even more complex than before.

⁽¹⁾ OJ L 163, 23.6.2007, p.17.

TABLE 6.2 – Total 2007–13 commitments — from Commission proposal to agreement

(EUR million at 2004 constant prices)

	Commission proposal <i>(14 July 2004)</i>	Parliament resolution <i>(8 June 2005)</i>	European Council <i>(15–16 Dec. 2006)</i>	Final agreement <i>(17 May 2006)</i>	Change vs Commission proposal	
1. Sustainable growth	457 995	446 930	379 739	382 139	-75 856	-17 %
1a. Competitiveness	121 687	110 600	72 120	74 098	-47 589	-39 %
1b. Cohesion	336 308	336 330	307 619	308 041	-28 267	-8 %
2. Natural resources	400 294	392 306	371 244	371 344	-28 950	-7 %
of which CAP market-related expenditure and direct payments	301 074	293 105	293 105	293 105	-7 969	-3 %
3. Citizen, freedom, security, justice	14 724	16 053	10 270	10 770	-3 954	-27 %
3a. Freedom, security and justice	9 210	9 321	6 630	6 630	-2 580	-28 %
3b. Citizenship	5 514	6 732	3 640	4 140	-1 374	-25 %
4. The EU as a global player	61 223	62 436	48 463	49 463	-11 760	-19 %
5. Administration	57 670	54 765	50 300	49 800	-7 870	-14 %
6. Compensations (BG and RO)	800	800	800	800	—	—
Total commitments	992 706	973 290	860 816	864 316	-128 390	-13 %
% of EU-27 GNI	1.20 %	1.18 %	1.05 %	1.05 %		

NB: Original figures have been adjusted to ensure comparability with the final outcome. Heading 4 excludes the European Development Fund (EDF) as well as the Emergency Aid Reserve. The exclusion in the final agreement of EUR 500 million staff pension contributions under Heading 5 and of the Emergency Aid Reserve (EUR 1 547 million) allowed the actual increase of EUR 4 billion obtained by the European Parliament to be presented in the financial framework table as an increase of only EUR 2 billion. The original documents referred to in this chapter contain the unadjusted figures.

TABLE 6.3 – MFF 2007–2013 (Annex to the IIA of 17 May 2006)

(in EUR million at 2004 constant prices)

COMMITMENT APPROPRIATIONS	2007	2008	2009	2010	2011	2012	2013	Total 2007-2013
1. Sustainable Growth	51 267	52 415	53 616	54 294	55 368	56 876	58 303	382 139
1a. Competitiveness for Growth and Employment	8 404	9 097	9 754	10 434	11 295	12 153	12 961	74 098
1b. Cohesion for Growth and Employment	42 863	43 318	43 862	43 860	44 073	44 723	45 342	308 041
2. Preservation and Management of Natural Resources of which: market related expenditure and direct payments	54 985	54 322	53 666	53 035	52 400	51 775	51 161	371 344
3. Citizenship, freedom, security and justice	1 199	1 258	1 380	1 503	1 645	1 797	1 988	10 770
3a. Freedom, Security and Justice	600	690	790	910	1 050	1 200	1 390	6 630
3b. Citizenship	599	568	590	593	595	597	598	4 140
4. EU as a global player	6 199	6 469	6 739	7 009	7 339	7 679	8 029	49 463
5. Administration (1)	6 633	6 818	6 973	7 111	7 255	7 400	7 610	49 800
6. Compensations	419	191	190	0	0	0	0	800
TOTAL COMMITMENT APPROPRIATIONS as a percentage of GNI	120 702 1.10%	121 473 1.08%	122 564 1.07%	122 952 1.04%	124 007 1.03%	125 527 1.02%	127 091 1.01%	864 316 1.048%
TOTAL PAYMENT APPROPRIATIONS as a percentage of GNI	116 650 1.06%	119 620 1.06%	111 990 0.97%	118 280 1.00%	115 860 0.96%	119 410 0.97%	118 970 0.94%	820 780 1.00%
Margin available	0.18%	0.18%	0.27%	0.24%	0.28%	0.27%	0.30%	0.24%
Own-Resources Ceiling as a percentage of GNI	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%

(1) The expenditure on pensions included under the ceiling for this heading is calculated net of the staff contributions to the relevant scheme, within the limit of EUR 500 million at 2004 prices for the period 2007-2013.

TABLE 6.4 – Comparison of commitment appropriations 2013 vs 2006 ⁽¹⁾*(in EUR million at 2004 constant prices)*

	2006	2013	2007-13 TOTAL	Change 2013/2006
SUB-HEADING 1A Competitiveness for growth and employment				
TEN (transport and energy)	548	1 309	7 203	139%
Marco Polo II	34	61	400	81%
Spatial infrastructure 'Galileo'	148	0	900	
Nuclear decommissioning	138	161	1 328	17%
Life Long Learning + Erasmus Mundus	676	1 030	6 752	52%
7th Research framework programme	5 044	8 851	48 081	75%
Competitiveness and innovation (CIP)	339	542	3 284	60%
Progress (social policy agenda)	95	107	658	12%
CUSTOMS 2012, FISCALIS & EMCS programmes	56	79	490	42%
Other	491	821	5 003	67%
TOTAL SUB-HEADING 1A	7 570	12 961	74 098	71%
SUB-HEADING 1B Cohesion for growth and employment				
Structural funds	31 682	35 063	246 523	11%
Cohesion Fund	5 904	10 279	61 518	74%
TOTAL SUB-HEADING 1B	37 586	45 342	308 041	21%
HEADING 2 Preservation and management of natural resources				
Agriculture: direct aids & market support	43 735	40 645	293 105	-7%
Rural development	10 544	9 253	69 750	-12%
European fisheries fund	630	556	3 849	-12%
Other fisheries programmes/actions	272	333	2 300	23%
Life+	199	304	1 861	53%
Other	31	69	479	121%
TOTAL HEADING 2	55 411	51 161	371 344	-8%

⁽¹⁾ Indicative breakdown of expenditure with adjusted financial envelopes after the trilogue of 4 April 2006.

SUB-HEADING 3A Freedom, security and justice				
Solidarity and the management of migration flows	393	852	3 517	117%
Fundamental Rights and Justice	35	69	482	96%
Security and Safeguarding Liberties	12	123	654	967%
Other	88	346	1 977	294%
TOTAL SUB-HEADING 3A	528	1 390	6 630	163%
SUB-HEADING 3B Citizenship				
Health and consumer protection (incl. agencies)	139	185	1 214	33%
European Culture and Citizenship (Culture, Youth, Citizens for Europe)	176	193	1 330	9%
Media	91	99	671	9%
Institution building (Bulgaria and Romania)	66	0	82	-100%
TOTAL SUB-HEADING 3B	591	598	4 140	1%
HEADING 4 The EU as a global partner				
Instrument for Pre-Accession (IPA)	1 121	1 700	10 213	52%
Eur. neighbourhood & Partnership Instr. (ENPI)	1 274	1 720	10 587	35%
Development Coop & Ec. Coop Instr. (DCEC)	1 862	2 324	15 103	25%
Instrument for Stability	531	500	2 531	-6%
Common foreign and security policy	99	340	1 740	245%
Provisioning of Loan Guarantee Fund	220	167	1 244	-24%
Emergency aid reserve	221	0	0	-100%
Other	894	1 278	8 046	43%
TOTAL HEADING 4	6 222	8 029	49 463	29%
HEADING 5 Administration	6 499	7 610	49 800	17%
HEADING 6 Compensation	1 041	0	800	
TOTAL	115 448	127 091	864 316	10%

2.4. The Interinstitutional Agreement of 17 May 2006

The Interinstitutional Agreement on budgetary discipline and sound financial management of 17 May 2006 was largely based on the agreement adopted for the previous multiannual financial framework. This was in particular the case for the structure by headings and the use of ceilings.

Nevertheless, a number of useful changes, making for further simplification and flexibility, were introduced.

(a) Simplification, consolidation

- The agreement incorporated the Interinstitutional Agreement of 7 November 2002 on the creation of the European Union Solidarity Fund (EUSF), agreed on during the period of the 2000–06 financial framework as a separate supplementary Interinstitutional Agreement. The rules for mobilisation of the EUSF were maintained.
- Simplification of the method for the technical adjustment, by applying the fixed annual deflator of 2 % used for structural funds and agriculture to all areas of expenditure. The table of the MFF included in the IIA of 17 May 2006 is expressed in constant 2004 prices. However, in view of the fixed deflator the ceilings can be transformed in current prices for the entire period covered by the MFF which increased the predictability and stability of the framework.
- The provisioning of the guarantee fund for loans to third countries was rationalised so that there was no longer any need for a ‘reserve’ to this end. The related (reduced) expenditure to be budgeted became part of the instruments available for the Union’s external policy.

(b) Flexibility: taking stock of the experience of Agenda 2000

The expenditure ceilings agreed for the 2007–2013 period were significantly lower than those the Commission had proposed. Tighter expenditure ceilings fixed for a period of seven years risked undermining the Union’s ability to address future challenges or to react to unforeseen circumstances.

In order to find a better balance between budgetary discipline and efficient resource allocation, new flexibility instruments were introduced to facilitate the deployment or redeployment of financial resources within the expenditure ceilings:

- A new European Globalisation Adjustment Fund intended to provide additional support for workers who suffer the consequences of major structural changes in world trade patterns, to assist them with their reintegration into the labour market. The Fund could not exceed a maximum annual amount of EUR 500 million (current prices);
- The possibility for the budgetary authority, on the basis of a Commission proposal in the framework of the annual budgetary procedure, to depart by up to 5 % from the so-called ‘reference amounts’ laid down in the legislative acts concerning multiannual programmes adopted under the co-decision procedure (except for cohesion programmes).

Other flexibility instruments were maintained, to be mobilised above the agreed expenditure ceilings within certain limits. These instruments, to be used in the framework of the annual budget procedure according to the relevant provisions set out in the IIA, included:

- The European Union Solidarity Fund, with unchanged amount (EUR 1 billion at current prices) and mobilisation procedure;

- The Flexibility Instrument, with an annual ceiling of EUR 200 million at current prices, with the new possibility to cover requirements of a multiannual nature and unchanged mobilisation procedure;
- The Emergency Aid Reserve of EUR 221 million at constant 2004 prices was moved outside the MFF. Its purpose is to respond to emergency situations in third countries. Both the amount and the mobilisation procedure remained unchanged.

The possibility to revise the MFF for an amount of up to 0.03 % of the (annual) EU GNI with the Council acting by a qualified majority and the Parliament by a majority of its members and three fifths of the votes cast was maintained (Point 22 of the IIA).

3. The entry into force of the Lisbon Treaty and its legal implications ⁽¹⁾

With the entry into force on 1 December 2009 of the Lisbon Treaty, signed on 13 December 2007, the MFF was for the first time enshrined in the Union's primary law. Hence, the provisions of the IIA of 17 May 2006 had to be aligned with the legal requirements of the new Treaty. The provisions relating to the MFF were to be codified in a Council Regulation to be adopted by special legislative procedure pursuant to Article 312 of the new Treaty on the Functioning of the European Union (TFEU).

Those provisions of the IIA of 17 May 2006 that related to interinstitutional cooperation in budgetary matters were to be included in a new IIA adopted on the basis of Article 295 TFEU and adjusted to the provisions of the new Treaty. The latter introduced important changes in the annual budgetary procedure and made some provisions obsolete, such as the distinction between 'compulsory' and 'non-compulsory' expenditure and the maximum rate of increase.

Finally, some other provisions of the IIA were to be included in the Financial Regulation which was also to be amended on the basis of the new Treaty.

On 3 March 2010 the Commission presented the related package of proposals ⁽²⁾. The underlying Commission's approach was to limit the proposals to a mere 'transposition' of the provisions of the IIA of 17 May 2006 into the new legal framework stemming from the TFEU. However, for a number of reasons, the legislative process ran into difficulties:

- Splitting the provisions of a single IIA into three separate documents, each of which to be adopted under a different procedure, was a politically sensitive process as it affected the so-called interinstitutional balance. The three institutions disagreed on the appropriate place for placing those provisions, with the Council, notably, shifting a number of them from the new IIA to the Council Regulation.
- Institutions also disagreed on the legal effects of some of the provisions of the new Treaty, most notably with regard to the possibility to revise the MFF with the Council

⁽¹⁾ For a description of the new legal framework, see Part 2.

⁽²⁾ Proposal for a Council Regulation laying down the multiannual financial framework for the years 2007–2013 (COM(2010) 72), Draft Interinstitutional Agreement between the European Parliament, the Council and the Commission on cooperation in budgetary matters (COM(2010) 73), Proposal for a Regulation of the European Parliament and of the Council amending Council Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities (COM(2010) 71).

deciding by qualified majority rather than unanimity up to the equivalent of 0.03 % of EU GNI as foreseen under Point 22 of the IIA of 17 May 2006.

- These divergencies appeared against the background of increasing tensions between institutions over the annual budgetary procedure (see below, Point 3), amplified by the upcoming preparation of the next (post-2013) MFF. Institutions were eager not to set any precedent which could be perceived as limiting their room for manoeuvre both in the annual budgetary procedure and the upcoming negotiations on the next MFF.

After having reached a common position on both the Council Regulation and the new IIA towards the end of 2010, Council invited, on 18 January 2011, the European Parliament to give its consent to the Regulation and Parliament and the Commission to take a position on the draft IIA with a view to agreeing on the latter as soon as possible. On 6 July 2011, however, Parliament rejected both the Regulation and the new IIA which it deemed to be considerably less flexible than the IIA of 17 May 2006 and not to take its position sufficiently into account.

As a consequence, the IIA of 17 May 2006 remained applicable. In practice, however, the possibility offered by Point 22 (0.03 % flexibility) remained foreclosed, the Council insisting that any revision of the MFF be taken by unanimity in accordance with Article 312(2) TFEU.

In spite of the failure to agree on the new legal framework, the discussions on the Commission proposals proved to be useful as they facilitated the preparation and adoption of the package of proposals for the next MFF (2014–2020) ⁽¹⁾.

4. Application of the financial framework, 2007–13

4.1. MFF adjustments of a technical nature

1) Annual technical adjustments of the MFF

The application of a fixed deflator of 2 % per year for all headings to convert the MFF ceilings expressed in constant 2004 prices into current prices reduced the importance of the annual technical adjustment of the MFF ahead of the annual budgetary procedure. The nominal ceilings (in current prices) were now fixed in advance for the entire period, an improvement which increased the predictability and stability of the framework. Only the value of the ceilings expressed as a percentage of EU GNI would be subject to an adjustment on the basis of the latest available economic forecasts.

As a result of higher than foreseen economic growth, the MFF 2007–2013, which was originally agreed at the equivalent of 1.048 % of EU GNI in commitments and 1.00 % in payments, represented a lower percentage of EU GNI than foreseen during the first years of the framework. In the technical adjustment for 2009, presented by the Commission in March 2008, the MFF commitment ceilings represented only the equivalent of 1.02 % of EU GNI and the payment ceilings 0.96 %. This situation was completely reversed by the effect of the economic and financial crisis starting in 2008. By the time of the technical adjustment for the year 2013, presented in April 2012, the equivalent figures were 1.12 % and 1.06 % respectively. The fact

⁽¹⁾ See Chapters 7 and 10.

that the ceilings in the end represented a significantly higher share of EU GNI than originally foreseen would have an impact on the negotiations for the MFF 2014–2020.

2) Technical adjustment corresponding to point 17 of the IIA of 17 May 2006 (cohesion envelopes)

Particularly worth mentioning is the technical adjustment for the year 2011, presented in April 2010, which was accompanied by an adjustment of the amounts allocated to the funds supporting cohesion policy.

Point 17 of the IIA stipulated that if any Member State's cumulated GDP for 2007–2009 had diverged by more than +/- 5 % from the cumulated GDP estimated at the time the 2007–2013 IIA was agreed, the Commission would adjust the amounts allocated from the funds supporting cohesion to the Member State concerned.

Three Member States were concerned by a positive divergence in excess of 5 % (CZ, PL, SK) while HU, with a negative divergence of -4.9 % narrowly escaped a reduction of its envelopes. The envelopes of PL, CZ and SK were adjusted upwards by in total EUR 1.008 million in current prices.

Apart from an increase of the payment ceiling for 2013 related to the accession of Croatia, these additional EUR 1.008 million in commitment appropriations (and EUR 282 million in payment appropriations) would mark the only net increase of the MFF ceilings over the 2007–2013 period.

3) Adjustment based on Point 48 of the IIA of 17 May 2006

The adjustment of the MFF for implementation foreseen in Point 48 of the IIA (see Annex VI.2) represents a technical procedure set also for previous MFFs. It is unique to the first year of implementation of a new framework and aims at covering the impact of late adoption of programmes financed from the structural, cohesion, rural development and fisheries funds and consists of transferring the commitments which could not be made in 2007 to later years.

Unlike the annual technical adjustments adopted by the Commission, it requires a decision by the Parliament and the Council amending the IIA as regards the MFF. EUR 2 034 million in current prices were consequently transferred to later years, resulting in an increase of the commitment ceilings for the years 2008–2013 and a corresponding decrease for the year 2007 ⁽¹⁾.

4.2. Revisions of the MFF to cater for unforeseen expenditure

Whilst the two preceding financial frameworks were subject to very few revisions, the 2007–2013 MFF had to be revised a number of times (by means of amendments of the IIA). The Parliament and the Council, as the two branches of the budgetary authority, diverged in general on the modalities for such revisions. Negotiations on the revisions were often cumbersome and protracted, sometimes lasting up to 18 months from the Commission proposal to the agreement. They were in general intimately linked with the respective annual budgetary procedures.

⁽¹⁾ OJ L 128, 16.5.2008, p. 8

From the first MFF revision agreed in 2007, the Council imposed a condition which was not foreseen in the IIA: The adjustment of the ceilings had to be 'neutral' in terms of the global ceilings for commitment and payments over the whole (2007–13) period; in other words, any raising of ceilings for one heading had to be fully offset by the lowering of the ceiling for another heading for the current or future years. In practice, most additional financial needs were offset mainly through the successive reduction of the ceilings for Heading 2 (Preservation and Management of Natural Resources), made possible by the emergence of significant margins within that heading.

1) Galileo and European Institute of Innovation and Technology

The failure in early 2007 of the negotiations with a private consortium on the financing of the European Navigation Satellite System programme 'Galileo' through a public-private partnership resulted in an additional financing requirement from the EU budget of EUR 2.4 billion. Given that the possibilities for redeployment of funds within the MFF ceiling concerned (Sub-heading 1a) were too limited, the Commission made a proposal on 19 September 2007 to revise the financial framework.

This proposal was also intended to cover an additional financing need (EUR 309 million) for the European Institute of Innovation and Technology (EIT), whose establishment had been proposed by the Commission as part of the mid-term review of the Lisbon strategy.

On the basis of the Commission proposal, the European Parliament and Council decided on 18 December 2007 ⁽¹⁾ to provide this financing by:

- revising the MFF 2007–2013 (see Annex VI.2) to raise the ceilings for commitment appropriations under Sub-heading 1a for the years 2008 to 2013 by an amount of EUR 1 600 million in current prices. This increase was offset by lowering the ceiling for commitment appropriations under Heading 2 for the year 2007 by the same amount. The ceilings for payment appropriations were adjusted accordingly;
- using other sources: EUR 400 million were 're-profiled' within the transport-related activities of the Seventh Research Framework programme and EUR 200 million were redeployed from other programmes within Sub-heading 1a; the flexibility instrument was mobilised for an amount of EUR 200 million; the remaining amount (EUR 309 million for the EIT) was to be covered from the margin available under the ceiling of Sub-heading 1a for the years 2008–2013.

2) The Food Aid Facility

The debate on the 2009 budget was marked by discussions to set up a new 'facility for rapid response to soaring food prices in developing countries' (the Food Aid Facility). The Commission originally proposed to create a Food Aid Facility of EUR 1 billion to be included under Heading 2. This was refused by both arms of the budgetary authority and after long discussions a solution was agreed at the conciliation meeting of 21 November 2008.

⁽¹⁾ OJ L 6, 10.1.2008, p. 7.

The institutions refused to revise the MFF but the agreement involved an amendment of the IIA in order to increase the amount of the Emergency Aid Reserve. The EUR 1 billion food aid facility was financed under Heading 4 by:

- EUR 340 million from the Emergency Aid Reserve in 2008 and 2009. The European Parliament, the Council and the Commission agreed to increase the Emergency Aid Reserve by EUR 240 million (to EUR 479.2 million in current prices), uniquely for the year 2008 (Point 25 of the IIA was amended in this sense ⁽¹⁾);
- EUR 420 million from the Flexibility instrument in 2009;
- EUR 240 million by redeployment within Heading 4 in 2009 and 2010.

3) *The European Economic Recovery Plan*

As part of the arsenal of measures taken by the Union and its Member States to relaunch the European economy, the Commission presented a European Economic Recovery Plan (EERP) aimed at financing projects in the field of energy and broadband Internet as well as the 'new challenges' agreed upon under the Common Agricultural Policy's 'Health Check'.

Agreement was reached in April 2009 on a package amounting to EUR 5 000 million in current prices:

- An additional EUR 3 980 million to be made available for the financing of energy projects under Sub-heading 1a of the MFF: EUR 2 000 million in 2009 and EUR 1 980 million in 2010.
- In addition, EUR 1 020 million to be made available within Heading 2 for developing broadband Internet in rural areas and strengthening operations related to the 'new challenges' defined in the context of the Health Check.

The agreement was implemented in two steps:

- The Parliament and Council decided on a first EERP-related revision of the MFF in May 2009 ⁽²⁾, whereby the 2009 ceiling for Sub-heading 1a was increased by EUR 2 billion, fully offset by a corresponding reduction of the ceiling for Heading 2. In addition, EUR 600 million was financed under Heading 2 for broadband Internet.
- The financing of the remaining amount (EUR 2 400 million) was secured through a compensation mechanism at the conciliation of the 2010 budgetary procedure, resulting in a second MFF revision in December 2009 ⁽³⁾ whereby the 2010 ceiling for Sub-heading 1a was increased by EUR 1 779 million, again fully compensated by reductions of the 2009 ceilings for Sub-headings 1a and 1b, Heading 2, Sub-heading 3a and Heading 5 as well as the 2010 ceilings for Sub-heading 1b and Headings 2 and 5. The payment ceilings were adjusted accordingly.

⁽¹⁾ OJ C 326, 20.12.2008, p. 3.

⁽²⁾ OJ L 132, 29.5.2009, p. 8.

⁽³⁾ OJ L 347, 24.12.2009, p. 26.

4) *International Thermonuclear Experimental Reactor (ITER)*

Following the identification of additional financing needs for the financing of the ITER project of EUR 1.4 billion for the years 2012–2013, the Commission first presented a proposal to revise the MFF in July 2010. After protracted negotiations and taking into account progress made so far, a revised Commission proposal was submitted in April 2011 with a view to provide EUR 1.3 billion of additional funds:

- EUR 460 through redeployments within Sub-heading 1a from the Seventh Research Framework programme;
- EUR 840 through an increase of the 2012 and 2013 ceilings for Sub-heading 1a, fully compensated by corresponding decreases of Headings 2 and 5, and a corresponding adjustment of the annual payment ceilings.

The (fourth) revision of the MFF was decided by the Parliament and Council in December 2011 on that basis ⁽¹⁾.

4.3. Enlargement of the European Union

Upon conclusion of the accession negotiations with Croatia in June 2011 the Council adopted a unilateral declaration stating that the related financial package should not require any revision of the 2013 MFF ceiling for commitments. In other words, the Council made it clear that the total additional expenditure requirements should be fully financed from either redeployment or a corresponding reduction of other ceilings.

In March 2013 the Commission proposed to revise the MFF commitment and payment ceilings upwards for the amounts corresponding to the entire financial package for Croatia, i.e. EUR 666 million in commitments and EUR 374 million in payments. This proposal was fully in line with Point 29 of the 2007–2013 IIA which does not foresee any need to examine redeployment or offsetting in the case of a MFF revision due to the accession of a new Member State. The European Parliament supported the Commission's approach.

The compromise which was finally struck involved on the one hand the full offsetting of the commitment ceilings (thus respecting the Council's 2011 statement) by a lowering of the 2013 ceiling for Heading 5; on the other hand the payment ceiling was increased by the amount foreseen in the Commission proposal (as supported by the Parliament). Due to the difficult negotiations the revision of the MFF was decided as late as 22 July 2013 ⁽²⁾, three weeks after accession.

In total between 2007 and 2013 an additional EUR 10.355 million of commitment appropriations were made available for unexpected expenditure plus enlargement: MFF ceilings (exclusively under Sub-heading 1a, except for the revision for enlargement which covered also other headings) were raised by EUR 6.819 million by means of amendments of the IIA of 17 May 2006; the raising of those ceilings was fully offset in terms of the global amount

⁽¹⁾ OJ L4, 7.1.2012, p. 12

⁽²⁾ OJ L 209, 3.8.2013, p. 14.

of commitments over the MFF period by lowering other ceilings whose margins would otherwise have been lost; EUR 2.456 million was financed within the heading concerned from the margins left available under, or through redeployments from programmes within that ceiling; finally EUR 1.080 million came from the mobilisation of the special (flexibility) instruments.

The evolution of the ceilings over the period 2007–2013 stemming from the adjustments and revisions summarised in the above Sections 3.1 to 3.3. is shown in Table 6.5.

TABLE 6.5 – Adjustments to MFF ceilings 2007–2013

EVOLUTION OF MFF 2007-2013 in Commitment appropriations (current prices)								
	2007	2008	2009	2010	2011	2012	2013	2007-2013
Original MFF (included in the IIA of May 2006)	128 091	131 487	135 321	138 464	142 445	147 075	151 886	974 769
Galileo -EIT	-1 600	539	503	638	13	-36	-57	0
Point 48	-2 034	771	387	387	171	171	147	0
EERP 1	0	0	0	0	0	0	0	0
EERP 2	0	0	-1 489	1 489	0	0	0	0
Point 17	0	0	0	0	336	336	336	1 008
ITER	0	0	0	0	-693	503	190	0
CROATIA	0	0	0	0	0	0	0	0
MFF after Croatia	124 457	132 797	134 722	140 978	142 272	148 049	152 502	975 777

EVOLUTION OF MFF 2007-2013 in Payment appropriations (current prices)								
	2007	2008	2009	2010	2011	2012	2013	2007-2013
Original MFF (included in the IIA of May 2006)	123 790	129 481	123 646	133 202	133 087	139 908	142 180	925 294
Galileo -EIT	-1 600	200	212	303	365	292	228	0
Point 48	0	0	0	0	0	0	0	0
EERP 1		0	-1 924	650	430	569	275	0
EERP 2		0	-1 489	134	381	504	470	0
Point 17	0	0	0	0	17	87	178	282
ITER	0	0	0	0	-580	0	580	0
CROATIA	0	0	0	0	0	0	374	374
MFF after Croatia	122 190	129 681	120 445	134 289	133 700	141 360	144 285	925 950

4.4. Annual budgets: initial under-implementation in payments followed by a catching-up and shortage of payment appropriations

Budget implementation during the first three to four years of the 2007–13 period was significantly slower than had been expected when the respective MFF ceilings were agreed. In particular the new cohesion programmes got off to a slow start in terms of the implementation of payment appropriations, with Member States fully focused on the timely completion of the 2000–06 programmes.

As a result, the level of the annual budgets in payment appropriations remained significantly below the ceilings for the years 2007–10, with actual implementation levels lagging even further behind. The difference between the actual level of implementation and the MFF payment ceilings remained well in excess of EUR 10 billion per year in those years. However, since the implementation of commitments evolved much more closely in line with the MFF ceilings, the level of outstanding unpaid commitments (known as '*reste à liquider*'/ RAL in the EU budgetary jargon), which had amounted to EUR 131.7 billion at the start of the MFF period, rapidly increased to reach EUR 194.4 billion by the end of the year 2010.

When programme implementation started to speed up in 2011, the level of payment appropriations authorised in the budget should normally have increased accordingly. However, as national budgets were under severe stress over the years 2011–12, brought about by the ongoing impact of the economic and financial crisis, the Council displayed a strong reticence to allowing for the necessary increases in payments appropriations. As a result, payments were forced to lag behind the payment ceiling by many billions for two more years. It was only in the year 2013, not least because of the link between the 2013 budget and the negotiations on the MFF 2014–20 established by Parliament, that the 2013 budget was increased up to the level of the MFF payment ceiling through a number of amending budgets. Still, this was far from sufficient to cover the outstanding payment claims.

This situation added to the challenge of agreeing the annual budgets in this period, and in the case of the negotiations of both the 2011 and 2013 budgets it was not possible to reach an agreement during the 21 days of conciliation foreseen by the Treaty. Therefore, in accordance with Article 314(8) of the TFEU, the Commission had to submit a new draft budget.

The level of payments was an important issue in both years, but particularly for the 2013 budget. The conciliation committee called to negotiate the 2013 budget, was also discussing a draft amending budget proposal from the Commission (No 6/2012), to increase payment appropriations by EUR 9.0 billion. The European Parliament and the Council finally agreed to increase the 2012 budget by EUR 6.0 billion.

Ultimately, both for the 2011 and 2013 budgets, it proved possible to both arrive at a agreed solution, with the annual budget in place for 1 January, and with no need to have recourse to the system of provisional twelfths.

The RAL at the start of the new MFF amounted to EUR 222 billion, which will be progressively paid out during the period 2014 to 2020.

5. The budget review and the report on the functioning of the Interinstitutional Agreement

5.1. The budget review

A declaration on the review of the financial framework, attached to the IIA of 17 May 2006, recalled the conclusions of the December 2005 European Council with regard to the invitation issued to the Commission to undertake a full, wide ranging review covering all aspects of EU spending, including the Common Agricultural Policy, and of resources, including the United Kingdom rebate, and to report in 2008/2009. It also specified that the European Parliament would be associated with the review at all stages of the procedure.

Furthermore, Article 9 of the new decision on own resources adopted on 7 June 2007 stipulated that, in the framework of the budget review, the Commission must undertake a general review of the own-resources system.

The review started in September 2007 with a broad public consultation process launched by an issues paper ⁽¹⁾. The public consultation that closed in June 2008 gathered views from national and local governments, members of the European and national parliaments, universities, NGOs and citizens on the future of the EU budget. This was followed by a conference held in Brussels on 12 November 2008 ⁽²⁾.

In October 2010, the European Commission presented its Communication on the EU Budget Review ⁽³⁾. Against the background of the serious financial and economic crises which started hitting the world and Europe at the end of 2008, the delay to the timetable set in the declaration attached to the IIA resulted from a political decision to give the new Commission, which came into office in February 2010, the opportunity to present its long-term growth strategy ⁽⁴⁾ ahead of the finalisation of the budget review.

On this basis, the Budget Review Communication set out some of the most important issues facing the EU budget for the next framework and beyond: how to respond to the economic and fiscal crisis and long-term challenges like demographic change, the need to address climate change and pressure on natural resources. The issue was found not to be first and foremost about the level of spending, but about finding ways to spend more intelligently and to present a comprehensive vision of budget reform, covering both the expenditure and the revenue side of the budget.

The review made concrete suggestions on a number of issues such as the duration of the MFF and improving its flexibility, as well as increasing the leverage effect of the EU budget through innovative financial instruments.

⁽¹⁾ See Communication from the Commission 'Reforming the budget, changing Europe. A public consultation paper in view of the 2008/2009 Budget review', SEC(2007) 1188 final, 12.9.2007.

⁽²⁾ http://ec.europa.eu/budget/reform2008/conference/programme_en.htm

⁽³⁾ COM(2010) 700.

⁽⁴⁾ See: Communication from the Commission: Europe 2020. A strategy for smart, sustainable and inclusive growth, COM(2010) 2020, 3.3.2010. The strategy was endorsed by the June 2010 European Council.

Parallel to the work undertaken by the Commission, the European Parliament proceeded with its own reflection on the future financing system of the Union. In a resolution of 29 March 2007 ⁽¹⁾, Parliament stressed the importance of examining 'the creation of a new system of own resources based on a tax already levied in the Member States, the idea being that this tax, partly or in full, would be fed directly into the EU budget as a genuine own resource, thus establishing a direct link between the Union and European taxpayers'.

Parliament also expressed its wish to pursue the examination of options for the future financing of the EU budget in close cooperation with the national parliaments before taking a final position. At the same time, it intended 'to discuss and adopt its final position on a new system of own resources for the European Union in time for it to be taken into account in the deliberations concerning the comprehensive review of EU revenue and expenditure as agreed in the Interinstitutional Agreement of 17 May 2006'.

5.2. The report on the functioning of the IIA

Another declaration attached to the IIA of 17 May 2006 called upon the Commission to present, by the end of 2009, a report on the functioning of the IIA accompanied, if necessary, by relevant proposals.

The report presented by the Commission in April 2010 ⁽²⁾ provided a detailed analysis of the procedures of the IIA for adjusting and revising the MFF and for mobilising the flexibility instruments as well as of the use made of them so far. Margins were considered to be extremely tight and, seen in conjunction with the limited size of flexibility instruments plus the constraint imposed de facto on revisions, the remaining margin for manoeuvre within the MFF for the years to come was considered to be severely limited.

The report made a positive overall assessment of the procedures agreed in the IIA on cooperation between institutions in the budgetary procedure and regarding sound financial management.

⁽¹⁾ European Parliament resolution of 29 March 2007 on the future of the European Union's own resources (2006/2205(INI)), P6_TA-(2007)0098.

⁽²⁾ COM(2010) 185, 27.4.2010.

Chapter 7

A budget for Europe 2020 agreed in times of crisis: The Multiannual Financial Framework 2014–20

The Commission presented its proposals on the Multiannual Financial Framework and the Own Resources legislation at the end of June 2011 under the title A budget for Europe 2020. The package included the main Communication ⁽¹⁾ in Part I, a series of accompanying policy fiches in Part II, the proposal for a Council Regulation laying down the multiannual financial framework for the years 2014–20 ⁽²⁾ and the draft Interinstitutional Agreement on cooperation in budgetary matters and on sound financial management ⁽³⁾.

The package also included Commission staff working papers on ‘the current system of funding, the challenges ahead, the results of stakeholders consultation and different options on the main horizontal and sectorial issues’ ⁽⁴⁾ and on ‘The added value of the EU budget’ ⁽⁵⁾. Furthermore, the Commission tabled about 60 proposals for the legal acts concerning multiannual programmes in all policy areas covered by the MFF.

At the same time the Commission presented an own-resources package comprising three legislative proposals for the financing of the EU budget: respectively for a new own-resources decision ⁽⁶⁾, a horizontal implementing regulation ⁽⁷⁾ — a new element under the Lisbon Treaty — and for a regulation ‘on the methods and procedure for making available the traditional and GNI-based own resources’ ⁽⁸⁾. These proposals were complemented by the Commission report on the operation of the own-resources system ⁽⁹⁾.

⁽¹⁾ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions — A Budget For Europe 2020, COM(2011) 500 final, 29.6.2011.

⁽²⁾ Proposal for a Council Regulation laying down the multiannual financial framework for the years 2014–20, COM(2011) 398 final, 29.6.2011.

⁽³⁾ Draft Interinstitutional Agreement between the European Parliament, the Council and the Commission on cooperation in budgetary matters and on sound financial management, COM(2011) 403 final, 29.6.2011

⁽⁴⁾ Commission Staff Working Paper ‘A Budget for Europe 2020: the current system of funding, the challenges ahead, the results of stakeholders consultation and different options on the main horizontal and sectorial issues’, SEC(2011) 868 final, 29.6.2011.

⁽⁵⁾ Commission Staff Working Paper ‘The added value of the EU budget. Accompanying the document Commission Communication, A budget for Europe 2020’, SEC(2011) 867 final, 29.6.2011.

⁽⁶⁾ Proposal for a Council Decision on the system of own resources of the European Union, COM(2011) 510 final, 29.6.2011.

⁽⁷⁾ Proposal for a Council Regulation laying down implementing measures for the system of own resources of the European Union, COM(2011) 511 final, 29.6.2011.

⁽⁸⁾ Proposal for a Council Regulation on the methods and procedure for making available the traditional and GNI-based own resources and on the measures to meet cash requirements, COM(2011) 512 final, 29.6.2011.

⁽⁹⁾ Commission Staff Working Paper — Financing the EU budget: Report on the operation of the own-resources system. Accompanying the document Proposal for a Council Decision on the system of own resources of the European Union, SEC(2011) 876 final/2, 27.10.2011.

Following the Commission's proposal on the financial transaction tax (FTT) ⁽¹⁾ a complementary own-resources package was adopted in November 2011, comprising proposals for two additional regulations: 'on the methods and procedure for making available the own resource based on the value added tax' ⁽²⁾ and for 'making available the own resource based on the financial transaction tax' ⁽³⁾. The proposals of the initial package had to be adjusted to the final FTT proposal ⁽⁴⁾ as well.

Both the Commission proposals and the subsequent negotiations were heavily influenced by the following factors:

- The financial crisis that hit the world economy in 2007 had triggered the most severe recession ever in the EU. The economic crisis and the bail out of banks resulted in a dramatic deterioration of public deficits and debt levels. Against this background, the European budget faced a twofold challenge: contribute to achieving the ambitious targets set in the Europe 2020 strategy, e.g. by stimulating investment, while at the same time reflecting the Member States' efforts for fiscal consolidation. The latter objective was specifically included in the conclusions of the October 2010 European Council ⁽⁵⁾.
- Over the period 2007–10, national contributions were lower and the net balances of net contributors were better than expected when the framework was initially agreed. The level of payment appropriations was low, due to the late adoption and the slow start of programmes at the beginning of the 2007–13 MFF. This created an artificially low reference point for the negotiations and contributed to less flexible negotiation positions on behalf of some delegations.
- A letter signed by the heads of Government of five Member States (the UK, Germany, France, the Netherlands and Finland) was sent to the President of the Commission on 18 December 2010 ⁽⁶⁾, asking to freeze payment appropriations in the next MFF at the level of 2011 in real terms in order to support the Member States' fiscal consolidation efforts. Commitment appropriations should be compatible with the requested stabilisation of budgetary contributions and should not exceed the 2013 level with a growth rate below the rate of inflation.

⁽¹⁾ Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC, COM(2011) 594 final, 28.9.2011.

⁽²⁾ Proposal for a Council Regulation on the methods and procedure for making available the own resource based on the value added tax, COM(2011) 737, 9.11.2011.

⁽³⁾ Proposal for a Council Regulation on the methods and procedure for making available the own resource based on the financial transaction tax, COM(2011) 738 final, 9.11.2011.

⁽⁴⁾ Amended proposal for a Council Decision on the system of own resources of the European Union, COM(2011) 739 final, 9.11.2011; Amended proposal for a Council Regulation laying down implementing measures for the system of own resources of the European Union, COM(2011) 740 final, 9.11.2011; Amended proposal for a Council Regulation on the methods and procedure for making available the traditional and GNI-based own resources and on the measures to meet cash requirements (recast), COM(2011) 742 final, 9.11.2011.

⁽⁵⁾ Conclusions of the European Council of 29 October 2010, Point 3: 'Heads of State or Government stressed that, at the same time as fiscal discipline is reinforced in the European Union, it is essential that the European Union budget and the forthcoming Multiannual Financial Framework reflect the consolidation efforts being made by Member States to bring deficit and debt onto a more sustainable path.'

⁽⁶⁾ See Information to the Press: <https://www.gov.uk/government/news/letter-to-president-of-european-commission>.

- Prior to the adoption of the Commission proposals, the Parliament had adopted its SURE committee report. In this report, the Parliament had demanded an increase of the EU budget by 5 % on top of a constant MFF ceiling at the 2013 level for the year 2014–20 to reach 1.11 % of EU-GNI in commitments without specifying the exact breakdown per heading ⁽¹⁾.

Due to this particularly difficult context, the negotiations on the multiannual financial framework and the new own-resources decision stretched over almost three years. The negotiations in the Council first focused on containing gross contributions to the EU budget, whilst the issue of Member States' specific requirements from the EU budget played a major role towards the final phase. While there had been numerous exchanges of views beforehand, the Council engaged into proper negotiations with the European Parliament only once it had found an agreement, in February 2013. These negotiations included the MFF itself as well as a number of issues relating to the main policy areas covered by it.

1. The Commission's proposals

1.1. The financial framework

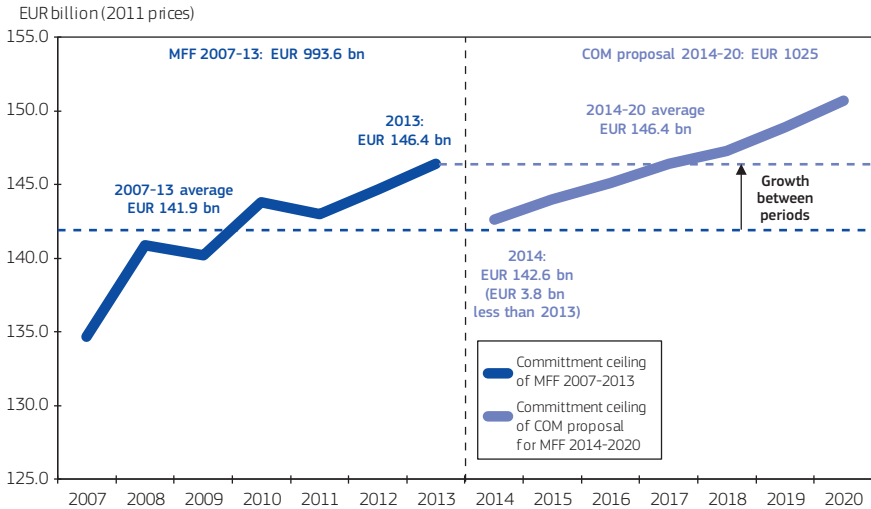
Against the background set out above, the Commission's proposal aimed at stabilising the new MFF in real terms at the level corresponding to the last year of the previous MFF (i.e. 2013), whilst considerably shifting spending priorities:

- With EUR 1 025 billion in commitments (in constant 2011 prices) the total volume of the MFF for 2014–20 was equivalent to the 2013 ceiling expressed in 2011 prices multiplied by seven (Graph 7.1).
- This ceiling for commitment appropriations was equivalent to 1.05 % of the EU-27 Gross National Income (GNI) based on the Spring 2011 macroeconomic projections. The payment ceiling was set at 1.00 % of the EU-GNI. Both ceilings expressed as a percentage of GNI were equivalent to the final agreement on the MFF 2007–13 as originally included in the IIA of 2006.
- In order to allow for targeted increases of specific programmes mainly in the area of 'smart growth' and 'security and citizenship' within that overall MFF spending volume 'frozen' in real terms, it was proposed to:
 1. stabilise the two largest expenditure items (CAP and cohesion) nominally at the 2013 level in current prices;
 2. shift ITER and GMES (Copernicus) outside the MFF as well as the new proposed Reserve for Crises in the Agricultural Sector in order to limit the negative impact of cost overruns or unforeseen crises on other expenditures programmed for seven years.

⁽¹⁾ European Parliament Resolution of 8 June 2011 on Investing in the future: a new Multiannual Financial Framework (MFF) for a competitive, sustainable and inclusive Europe.

With the assumption of 2 % annual inflation the share of CAP and cohesion within the MFF would decrease gradually to one third each in 2020, creating the necessary room for manoeuvre to expand the remaining headings to one third of the total ceilings in 2020.

GRAPH 7.1 – *Development of MFF commitment ceiling 2007–13 vs initial Commission proposal for 2014–20*



Echoing the European Parliament's proposal, all elements outside the MFF were included in an overall summary table illustrating that these would in total equal 0.06 % of GNI and together with the MFF amount to 1.11 % of EU-27 GNI. As an additional presentational novelty, the Commission proposal included a separate table presenting the indicative breakdown of each ceiling by multiannual programme for each year covered by the MFF plus the 'reference year' 2013.

As can be seen in Table 7.1, the Commission proposal entailed a marked shift in the allocation of resources between the different budget headings, and in particular a shift towards competitiveness and investment in infrastructure with a focus on knowledge-based activities such as research and education.

The Commission proposals aimed at making the EU budget a driving force in achieving the goals set in the Europe 2020 strategy in spite of its modest size. The following section lists some of the innovative elements put forward to that purpose ⁽¹⁾.

1) *Smart and Inclusive Growth*

The Commission proposed the creation of a common strategic framework for research and innovation (Horizon 2020), bringing together the three research and innovation instruments

⁽¹⁾ All quotes in this subsection refer to COM(2011) 500 final, op. cit.

TABLE 7.1 – *Shift of expenditures between budget headings 2013–20 according to the initial Commission proposal from June 2011*

(million EUR at constant 2011 prices)

	2013 ¹⁾	COM proposal		Difference 2020 vs. 2013
		2014	2020	
1. Smart and Inclusive Growth	66 293	64 696	76 179	14.9 %
of which competitiveness	13 886	18 142	26 589	91.5 %
of which infrastructure ²⁾	1 577	3 914	7 516	376.6 %
of which: cohesion	52 407	46 554	49 589	-5.4 %
2. Sustainable Growth: natural resources	58 574	57 386	51 784	-11.6 %
Sub-ceiling: Market related expenditure and direct payments	43 180	42 244	38 060	-11.9 %
3. Security and Citizenship	2 535	2 532	2 763	9.0 %
4. Global Europe	9 222	9 400	10 620	15.2 %
5. Administration (including pensions and European schools) ³⁾	8 824	8 542	9 371	6.2 %
Sub-ceiling: Administrative expenditure of EU institutions	6 794	6 967	7 485	10.2 %
Total commitment appropriations	145 449	142 556	150 718	3.6 %
in % of EU-27 GNI	1.12 %	1.08 %	1.03 %	
Total payment appropriations	137 765	133 851	137 994	0.2 %
— in % of EU-27 GNI	1.05 %	1.01 %	0.94 %	
— margin	0.19 %	0.23 %	0.30 %	
— Own resource ceiling	1.24 %	1.24 %	1.24 %	

- 1) 2013 expenditure under the MFF 2007-13 has been broken down according to the proposed new nomenclature to facilitate comparisons. Consequently, ITER and GMES are taken out and EUR 83 million of pension expenditures financed by staff contributions are included. This explains the difference of total commitment appropriations of EUR 149.4 million to the EUR 146.4 million compatible to the official MFF table for 2013.
- 2) For 2014-20 excluding the EUR 10 000 million earmarked in the cohesion fund allocations for the CEF. In the Commission proposal the allocations for infrastructure were subsumed under the subceiling for Economic, social and territorial cohesion.
- 3) Includes administrative expenditure for salaries, pensions, European Schools, and institutions other than the Commission. Other administrative expenditures are included in the first four expenditure headings.

Source: Figures based on COM(2011) 500 final, 29.6.2011, p. 4 and 23.

that existed in the 2007–13 MFF (the Seventh Research framework programme, the Competitiveness and Innovation Framework programme and the European Institute for Innovation and Technology). Spending was to target key societal challenges such as health, food security and the bio-economy, energy and climate change.

The proposed, more systematic approach towards the use of innovative financial instruments, Public-Private and Public-to-Public Partnerships would help in leveraging private investments. Just as important, funding schemes would be considerably streamlined and simplified (one single set of rules for participation, audit, support structures, dissemination of results and reimbursement schemes).

The Commission proposed to allocate EUR 80 billion in 2011 prices for the 2014–20 period for the Common Strategic Framework for Research and Innovation.

Similarly, in the area of education the Commission proposed a simplification of the previous structure to one main programme Erasmus for All in order to avoid fragmentation, overlapping and/or proliferation of projects lacking the critical mass necessary to produce a lasting impact. The new EU programme for education, training, youth and sport combined seven programmes from the 2007–13 period (Long Life Learning programme, Youth in Action and five international cooperation programmes). It included three key priorities: a) supporting trans-national learning mobility; b) fostering cooperation between education institutions and the world of work in order to promote the modernisation of education, innovation and entrepreneurship and c) providing policy support to gather evidence on the effectiveness of education investments and help Member States to implement effective policies. The Commission proposed to allocate EUR 15.2 billion to Erasmus for All.

A fully functioning single market depends on a modern, high performing infrastructure connecting Europe particularly in the areas of transport, energy and information and communication technologies (ICT). Therefore, the Commission proposed the creation of a new Connecting Europe Facility (CEF) for financing pre-identified transport, energy and ICT priority infrastructures of EU interest. The CEF was to focus on connections that provide better access to the internal market and terminate the isolation of certain economic areas. In addition, the CEF was to make a vital contribution to energy security, by ensuring pan-European access to different sources and providers inside and outside the Union.

The Commission proposed to allocate EUR 40 billion in 2011 prices for the 2014–20 period for the CEF to be complemented by an additional EUR 10 billion ring fenced for related transport investments inside the Cohesion Fund.

Sub-ceiling: economic, social and territorial cohesion

The Commission proposal foresaw the creation of a category of regions ‘in transition’ whose GDP was between 75 % and 90 % of the EU average. This new category was to complement the two existing ones (convergence regions and competitiveness regions). However, the Structural and Cohesion Funds would remain concentrated on the most disadvantaged regions and Member States in order to help them catch up with the more prosperous regions and Member States.

To help translate the Europe 2020 objectives into investment priorities, the Commission proposed a common strategic framework to cover the Structural Funds, the Cohesion Fund, the rural development as well as the maritime and fisheries fund. Partnership contracts with each Member State would be concluded for setting out the commitment of partners at national and regional level to utilise the allocated funds to implement a set of agreed objectives and targets.

The Commission put forward a number of new requirements in order to reinforce the compliance of cohesion policy with the EU legal framework (*ex-ante*-conditionality) and to better link it with the fiscal and structural reforms needed in the framework of economic governance to ensure effective use of the financial resources (macroeconomic conditionality). In the same vein, 5 % of the cohesion budget for each Member State would be set aside as a performance reserve and allocated, following a mid-term review, to those Member States whose

programmes have contributed most to progress in meeting the agreed milestones set in the partnership contracts.

2) Sustainable Growth: Natural Resources

To ensure a more equal distribution of direct payments, the level of direct support per hectare should converge towards the EU average across Member States (while taking account of the differences that still exist in wage levels and input costs). At the same time, the income support through direct payments for large agricultural holdings would be capped, taking account of the economies of scale of larger structures and the direct employment that these structures generate. The related savings would remain within the national envelopes and be used for rural development.

To ensure that the CAP helps the EU to deliver on its environmental and climate action objectives, 30 % of direct support would be made conditional on 'greening'. All farmers would have to engage in verifiable environmentally supportive practices defined in legislation in order to receive payments for delivering public goods.

Allocations for rural development would be based on more objective criteria and better targeted to the objectives of the policy while being subject to the same Europe 2020 performance-based conditionality provisions as the other structural funds. This would ensure a fairer treatment of farmers performing the same activities.

The Commission proposed to allocate EUR 281.8 billion to the first pillar (direct payments and market-related expenditure) of the CAP and EUR 89.9 billion to the second pillar (rural development). This funding was to be complemented by a further EUR 15.2 billion outside Heading 2 as shown in the box below.

Support for agriculture outside Heading 2 (EUR in 2011 prices):

- 4.5 billion for research and innovation on food security, the bio-economy and sustainable agriculture (in the Common strategic framework for research and innovation)
- 2.2 billion for food safety in Heading 3
- 2.5 billion for food support for the most deprived persons in Heading 1
- 3.5 billion in a new reserve for crises in the agriculture sector (outside the MFF)
- Up to 2.5 billion in the European Globalisation Fund (outside the MFF)

3) Security and Citizenship

Home affairs policies, covering security, migration and the management of external borders, have grown steadily in importance in the years preceding the MFF proposal and were significantly changed under the Lisbon Treaty. The Stockholm programme and its Action Plan confirmed their importance.

Proposals for simplification included the merging of Sub-headings 3a and 3b, reducing the number of programmes to a two-pillar structure (creating a Migration and Asylum Fund and an Internal Security Fund) and the introduction of multiannual programming (resulting in a reduced

workload for the Commission, Member States and final beneficiaries). Both funds would have an external dimension ensuring continuity of financing from the EU to third countries, for example concerning the resettlement of refugees, readmission and regional protection programmes.

The Lisbon Treaty foresees EU cooperation in the fight against criminal networks, trafficking in human beings and the smuggling of weapons and drugs as well as in civil protection to ensure better protection of people and the environment in the event of major natural and man-made disasters. The increase in disasters affecting European citizens calls for more systematic action at European level. Therefore, the Commission proposed to increase the efficiency, coherence and visibility of the EU's disaster response.

4) Global Europe

A key priority of the Commission proposal on the MFF in Heading 4 was to respect the EU's formal undertaking to commit 0.7 % of Gross National Product (GNP) to overseas development. By maintaining the share of the EU budget as part of the common effort made by the EU as a whole by 2015, a decisive step towards achieving the Millennium Development Goals would be made.

As the financial pillar of the Enlargement Strategy, the Commission proposed a single integrated pre-accession instrument, encompassing all dimensions of internal policies and thematic issues, to be implemented through national/multi-beneficiary programmes agreed with the beneficiaries and mirroring the Structural Funds, the Cohesion Fund and the European Agricultural Fund for Rural Development (EAFRD).

The European Neighbourhood Instrument (ENI) should continue to provide the bulk of EU assistance to neighbouring countries in support of the European Neighbourhood Policy and bilateral partnerships (including bilateral Association Agreements). In addition, partner countries would also benefit from other instruments, such as the European Initiative for Democracy and Human Rights or the Instrument for Nuclear Safety Co-operation. The instruments to respond to crises situations would be the Humanitarian Assistance, Macro Financial Assistance and the Instrument for Stability).

The Commission proposed to discontinue funding of programmes in industrialised and emerging countries and instead to create a new Partnership Instrument to support public diplomacy, common approaches and the promotion of trade and regulatory convergence in those cases where funding can contribute to strengthening the EU's partnerships around the world. The proposal also foresaw the creation of a pan-African instrument to support the implementation of the Joint Africa Europe Strategy, focusing on the clear added value of cross-regional and continental activities.

5) Administration

As part of its ongoing commitment to limit the costs of administering EU policies, the Commission reviewed administrative expenditure across the institutions to identify further sources of efficiency and savings. It proposed a 5 % reduction in the staffing levels of each institution/service, agency and other bodies starting in 2013, as part of the MFF 2014–20. At the same time, the Commission proposed a number of changes to the staff regulations applicable to EU civil servants in the EU institutions. These included a new method for calculating the adaptation of salaries, an increase in working time by 2.5 hours a week without compensatory wage adjustments, an increase of the pension age and the modernisation of certain conditions in line with similar trends in Member State administrations.

1.2. The financing system

The Commission proposals on own resources, submitted on 29 June 2011 and completed with amended and supplementary elements on 9 November 2011, comprised three main building blocks:

- the simplification of Member States' contributions;
- the introduction of new own resources;
- the reform of the correction mechanisms.

1) The simplification of Member State contributions

The first element of simplification consisted of streamlining the legal architecture of the own-resources legislation building on the new provisions of the Lisbon Treaty ⁽¹⁾.

As regards simplification of Member States' contributions, the Commission proposed the elimination of the VAT-based own resource, which is complex, requires much administrative work to arrive at a notionally harmonised base and offers little or no added value compared to the GNI-based own resource.

2) The introduction of new own resources

On new own resources, the Commission presented an in-depth analysis of six potential candidates for new own resources in its Staff Working Paper accompanying the legislative proposals. On this basis, the Commission decided to propose the introduction of a financial transaction tax (FTT) based own resources and a new VAT-based own resource, both from 1 January 2018 at the latest. According to the Commission estimates presented at the time, the two new own resources combined could provide sufficient income for the EU budget so that by 2020 only around 40 % of the financing needs of the EU budget would have to be covered by the residual GNI-based own resource.

In the context of the financial and economic crisis, the introduction of an EU-wide FTT based on a directive under Article 113 TFEU, with a broad tax base and differentiated rates would serve several purposes simultaneously:

- Revenue-raising objective: an FTT would generate a new stream of public revenue, which could be made available — at least in part — for the EU budget, thus leading to a reduction in Member States' contributions. Financial institutions would contribute their fair share of the costs of the recent crisis;
- Corrective objective: overly risky activities by financial institutions should not be encouraged;
- Internal Market objective: A harmonised introduction of an EU FTT would avoid the fragmentation of the internal market for financial services resulting from the setting up of uncoordinated national taxes.

⁽¹⁾ See Chapter 8, point 3.2.

The approach for the new VAT own resource was to apply a single EU rate of 1 % on the transactions of all goods and services currently subject to the standard rate in each and every EU Member State. The tax base would thus be fully harmonised and correspond to the common denominator of national VAT systems concerning the standard rate.

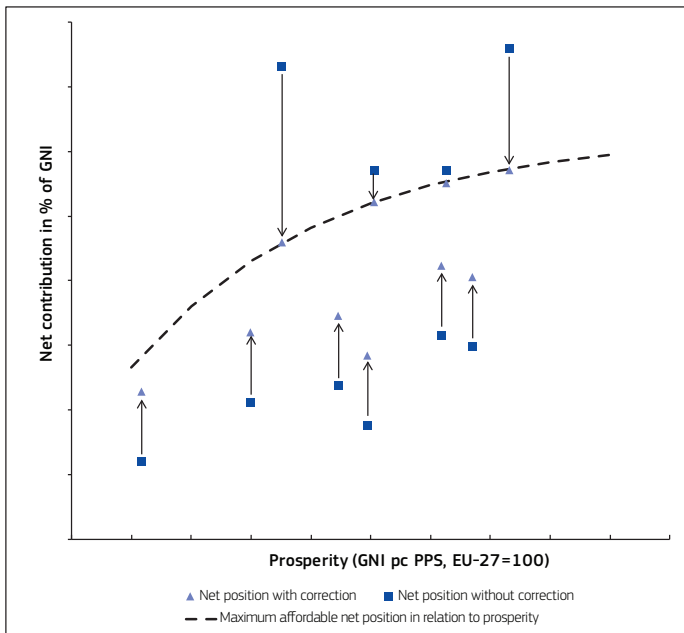
Unlike the existing VAT-based own resource, the revenue stream would not be capped at 50 % of GNI and would avoid complex statistical calculations and adjustments to a large extent. It would result from actual VAT receipts paid by all final consumers in the EU and then collected by the national tax authorities. The Member States would regularly transfer a share, corresponding to the EU rate, of the VAT receipts collected and stemming from transactions subject to the standard rate.

3) The reform of the correction mechanisms

The Commission proposed to replace all existing correction mechanisms, both temporary (reduced VAT call-rates and GNI lump sums) and permanent (UK rebate and the ‘hidden correction’ resulting from the 25 % collection costs on TOR) by a much simpler and fairer system of temporary lump-sum reductions of GNI contributions as well as a reduction of the TOR collection costs to 10 %.

Graph 7.2 illustrates the functioning of the system: net contributions (operating net balances) expressed in per cent of GNI were defined in relation to the relative prosperity of net contributing Member States. Relative national prosperity is measured as GNI per capita in purchasing power standards (PPS) related to the EU-27 average (EU-27=100).

GRAPH 7.2 – Maximum affordable net position according to the Commission proposal on lump-sum corrections



The dotted line represents the ‘maximum affordable net positions’ underlying the Commission proposal. This curve was established on the basis of the following considerations:

- The negative net balance of a country related to its relative prosperity level in the EU (measured in PPS) cannot exceed a certain level.
- The concave shape would assure a progressive link to relative prosperity, but as relative prosperity increases, progressivity would become less and less steep. This reflects the consideration that there is an absolute maximum level of acceptable net balance, even for Member States with the highest levels of relative prosperity.

The lump-sum corrections, agreed *ex ante*, would ensure that for all Member States whose net balance would be above the curve the estimated net positions would be reduced to the maximum affordable level defined in relation to their relative prosperity (i.e. they would be brought down to the point on the dotted curve that corresponds to their relative wealth). Similarly, since the gross lump-sums would have to be financed by all Member States on the basis of their GNI shares, the net position of net contributors not eligible for a correction would move closer to, but not exceed, the affordable maximum net position corresponding to their relative prosperity.

2. The outcome of the negotiations

2.1. Negotiations in the Council

2.1.1 *Decrease in Community expenditure*

The Commission proposal on the MFF was considered as a good basis for negotiations by nearly all delegations in the Council, even if the group of the net contributors regarded the overall level to be too high. However, it took more than a year until the Council reached the stage of negotiations at political level.

Under the Polish presidency (second half of 2011) and at the beginning of the Danish presidency (first half of 2012), work focused on technical discussions exploring the details of the Commission proposals at working group level (within the so called ‘Friends of the Presidency’ group), followed by exchanges of views at the General Affairs Council (GAC) ⁽¹⁾.

During the later months of the Danish presidency, the focus shifted towards the Committee of Permanent Representatives (Coreper) and the GAC, where so-called ‘negotiation boxes’ prepared by the Presidency were discussed and progressively completed. These negotiation boxes were embryonic European Council conclusions, listing all the elements that Member States considered should be part of the overall agreement, whilst remaining relatively uncontroversial at first. Multiple policy options were presented between square brackets and ranges were given rather than precise figures.

⁽¹⁾ The Friends of the Presidency Group was an ad hoc Council working group established for the duration of the MFF negotiations, with Member States being represented by budget counsellors and/or representatives of Ministries for European or Foreign Affairs. In this exploratory and explanatory phase the Commission produced more than 42 ‘fiches’ and non-papers illustrating the details of its proposal.

TABLE 7.2 – Comparison between 2007–13 MFF, COM proposal for 2014–20 and the agreed MFF 2014–20

(2011 prices)

COMMITMENT APPROPRIATIONS	2007–13		COM proposal (update July 2012) ¹⁾		MFF 2014–2020 (EC agreement February 2013)		Difference: Final MFF vs COM proposal		Difference: Final MFF vs 2007–13	
	mill. EUR	% of total CA	mill. EUR	% of total CA	mill. EUR	% of total CA	mill. EUR	%	mill. EUR	%
1. Smart and inclusive Growth	446 788	44.9 %	503 310	48.2 %	450 763	47.0 %	-52 547	-10.4 %	3 975	0.9 %
1.a. Competitiveness for Growth and Jobs ²⁾	91 541	9.2 %	164 316	15.7 %	125 614	13.1 %	-38 702	-23.6 %	34 073	37.2 %
1b. Economic, social and territorial cohesion	355 248	35.7 %	338 994	32.4 %	325 149	33.9 %	-13 845	-4.1 %	-30 099	-8.5 %
2. Sustainable Growth: Natural Resources of which: Market related expenditure and direct payments ³⁾	420 682	42.3 %	389 972	37.3 %	373 179	38.9 %	-16 793	-4.3 %	-47 503	-11.3 %
	318 820	32.1 %	286 551	27.4 %	277 851	28.9 %	-8 700	-3.0 %	-40 969	-12.9 %
3. Security and citizenship	12 396	1.2 %	18 809	1.8 %	15 686	1.6 %	-3 123	-16.6 %	3 290	26.5 %
4. Global Europe	56 815	5.7 %	70 000	6.7 %	58 704	6.1 %	-11 296	-16.1 %	1 889	3.3 %
5. Administration ⁴⁾ of which: Administrative expenditure of the institutions	56 503	5.7 %	63 165	6.0 %	61 629	6.4 %	-1 536	-2.4 %	5 126	9.1 %
	0	0.0 %	0	0.0 %	0	0.0 %	0	-13.1 %	0	#DIV/0!
6. Compensations ⁵⁾	991	0.1 %	27	0.0 %	27	0.0 %	0		-964	
TOTAL COMMITMENT APPROPRIATIONS	994 175		1 045 282		959 988		-85 294	-8.2 %	-34 187	-3.4 %
as a percentage of GNI	1.12 %		1.09 %		1.00 %		-0.09 %			
TOTAL PAYMENT APPROPRIATIONS	943 137		998 784		908 400		-90 384	-9.0 %	-34 737	-3.7 %
as a percentage of GNI	1.07 %		1.04 %		0.95 %		-0.09 %			
OUTSIDE THE MFF										
Emergency Aid reserve	1 777		2 450		1 960		-490	-20.0 %	183	10.3 %
European Globalisation Adjustment Fund	3 573		3 000		1 050		-1 950	-65.0 %	-2 523	-70.6 %
European Union Solidarity Fund	7 146		7 000		3 500		-3 500	-50.0 %	-3 646	-51.0 %
Flexibility Instrument	1 429		3 500		3 297		-203	-5.8 %	1 868	130.7 %
European Development Fund	26 930		30 319		26 984		-3 335	-11.0 %	54	0.2 %
TOTAL OUTSIDE THE MFF	40 855		46 269		36 791		-9 477	-20.5 %	-4 063	-9.9 %
as a percentage of GNI	0.05 %		0.05 %		0.04 %		-0.01 %			

¹⁾ The Commission proposal is presented here in the structure of the final MFF agreement with separate sub-headings 1a and 1b²⁾ For comparison purpose, the Commission proposal for H1a is increased for the amounts for ITER and GMES that were proposed to be financed outside the MFF but finally re-integrated in H1a.³⁾ For 2007–13, the net ceiling for 1 pillar (Commission Decision 379/2009 as last amended) is taken into account which is after deductions of the modulation and other transfers to rural development. This net ceiling is then adjusted to comply with the structure of the 2014–20 sub-celling (i.e. without market interventions in fisheries markets — to be financed under EMFF, and Food Safety — to be financed under H3; the voluntary modulation from rural development is added). For comparison purpose, the Commission proposal for H2 is increased by the amount of the reserve for crises that was proposed to be financed outside the MFF but finally integrated in H2.⁴⁾ For comparison purpose, the ceiling for H5 for 2007–13 is increased by the amount of staff contributions that are currently outside the MFF (i.e. EUR 500 million in 2004 prices).⁵⁾ Compensations: BG, RO for 2007–2009, HR for 2014.

Nevertheless, a number of elements became clear early in the negotiations:

- The Commission proposals would need to be cut significantly, both in terms of commitments and payments, since most net contributors (supported by the Czech Republic) were adamant on this.
- Given the strong political support for both the CAP and cohesion policy by a very large number of Member States, cuts in commitments would risk falling disproportionately on the other multiannual programmes.
- Given the expected high level of outstanding commitments from 2007–13 programmes at the end of 2013, the payment cuts sought would be problematic and would require specific solutions.

Meanwhile, in June 2012 the Commission updated its proposals to account for:

- the expected accession of Croatia by 1 July 2013;
- the impact of new regional statistics;
- the impact of the Spring 2012 macro-economic forecast and medium-term projections on cohesion eligibility and the size of the overall framework expressed as a percentage of GNI.

The integration of Croatia added commitments of EUR 13.7 billion and EUR 10.0 billion in payments (in 2011 prices) which equalled 0.01 percentage points in GNI. At the same time the new regional data led to an overall reduction of the cohesion allocations for the EU-27 by EUR 5.5 billion in 2011 prices. In total, the updated commitment ceiling for the EU-28 was EUR 1 033 billion in 2011 prices or 1.08 % of GNI and the payment ceiling amounted to EUR 988 billion or 1.03 % of GNI.

During the Cypriot presidency (second half of 2012) the President of the European Council, Herman van Rompuy, took the lead in the negotiations with a view to finding a common 'landing zone' for the 27 Heads of State and Government. This involved finding a careful equilibrium between the required overall cuts in commitments, the considerable political pressure for additional cohesion and rural development funding requested by individual Member States, and the need to accompany the even higher cuts in payments by specific measures so that budget implementation would not be compromised, and other specific measures.

After a failed attempt in November 2012, the European Council reached a unanimous agreement in February 2013 along the following lines:

- ITER, GMES and the agricultural crisis reserve were included within the overall MFF ceiling;
- Compared to the 2012 updated Commission proposals, commitments inside the MFF were cut by EUR 85.3 billion, and total commitments (including the items the Commission had proposed to finance outside the MFF) by EUR 94.8 billion. The MFF payment ceiling was reduced by EUR 90.4 billion;
- For the first time since the introduction of the multiannual financial frameworks, the political agreement resulted in a real cut compared to the ceilings of the previous (2007–13)

MFF. The overall ceiling for commitment appropriations at EUR 960.0 billion represents a reduction in real terms of EUR 33.6 billion (or -3.4 %) compared to the EUR 993.6 billion of the previous MFF (everything in 2011 prices). In payments the reduction amounts to EUR 34.7 billion (-3.7 %): EUR 908.4 billion for 2014–20 compared to EUR 943.1 billion for 2007–13;

- In nominal terms, applying, as for 2007–13, a fixed annual deflator of 2 %, the ceilings increase by EUR 106.8 billion in commitments (+10.9 % or EUR 1 082.6 billion for 2014–20 vs EUR 975.8 billion for 2007–13) and EUR 98 billion (+10.6 % or EUR 1 024.0 billion for 2014–20 vs EUR 926.0 billion for 2007–13).

The European Council agreed to reinstall the separation of Heading 1 into two separate sub-headings for 'Competitiveness for growth and jobs' (Sub-heading 1a included the CEF) and for 'Economic, social and territorial cohesion' (Sub-heading 1b). Sub-heading 1a was reduced by EUR 38.7 billion (of which a EUR 21.0 billion reduction for the CEF) compared to the Commission proposal but overall the sub-heading was still increased by EUR 34.1 billion in real terms (or +37 %) compared to 2007–13.

The allocations for cohesion policy were reduced by EUR 13.8 billion compared to the Commission proposal (-4.1 %), in spite of the long list of negotiated 'gifts'. The transition regions were created, but with financial allocations less generous than originally foreseen by the Commission. Macro-economic conditionality survived, although it was subject to additional constraints.

Heading 2 was cut in total by EUR 16.8 billion (-4.3 %) compared to the Commission proposal (of which EUR 8.7 billion came under the first pillar of the CAP). The convergence of direct aids survived more or less intact as proposed by the Commission, but greening measures were significantly weakened. Rural development was cut by more than 5 %. The distribution of individual top-ups together with the flexibility for Member States to shift individual allocations between the two pillars were the final building blocks of the financial picture to fall into place.

Heading 3 was cut by EUR 3.1 billion (-16.6 %) compared to the Commission proposal but it still increases significantly (by EUR 3.3 billion or 26.8 %) compared to 2007–13.

Heading 4 was cut by EUR 11.3 billion (-16.1 %) compared to the Commission proposal and maintains a small real increase of EUR 1.9 billion (+3.3 %) compared to the 2007–13 level.

Payments were cut particularly harshly by much more than the cut in commitments would have required. In spite of frequently expressed concerns about the evolution of the outstanding commitments (RAL), a number of elements were included to slow down payment implementation to make the extremely tight ceiling of EUR 908.4 billion compatible with the fulfilment of the Union's legal obligations:

The performance reserve was increased to 7 % (which was later scaled down to 6 % at the insistence of the Parliament) and a general n+3 rule for de-commitments was introduced, effectively lowering pressure on swift implementation by giving Member States one additional year to implement commitments compared to the general n+2 rule applicable in 2013 ⁽¹⁾. At

(1) The Commission had proposed a strict application of the n+2 rule.

the same time, however, the European Council conclusions stated that 'specific and maximum possible flexibility will be implemented', opening the door for negotiations with the Parliament on flexibility.

2.1.2 Limited adjustment to the own-resources system

In the course of the discussions in the Own-Resource Working Group of the Council, the Coreper and the GAC it became clear that:

- while the proposals for new own resources did receive some degree of support, they were far from obtaining the required unanimous approval;
- the UK did not accept any modification of its rebate.

In other words, there was insufficient support for a wide-ranging reform or modernisation of the own-resources system for the time being. The present system would have to be largely 'rolled over' with only some rather modest changes.

The February 2013 European Council concluded that:

- work on the Commission proposal for a new VAT own resources should continue and that this new VAT own resource could replace the existing VAT-based own resource;
- the Member States participating in the financial transaction tax on the basis of enhanced cooperation are invited to examine if it could become the base for a new own resource for the EU budget (which should not impact the non-participating Member State nor the calculation of the UK rebate);
- the UK correction would continue to apply;
- temporary rebates would be granted for the period 2014–20 only: (a) a reduced VAT rate of call of 0.15 % (half the normal rate) for Denmark, the Netherlands and SE; (b) lump sum gross reductions of the GNI contribution for NL and SE (already existing in 2007–13), as well as for DK (new rebate) and until 2016 for AT (phased-out GNI lump-sum replacing the current reduced VAT call rate);
- reduction of the TOR collection costs from 25 % to 20 %;
- Confirmation that there will be an implementing regulation on the basis of Article 311(4) TFEU.

The legislative package on own resources was discussed and agreed under the Lithuanian and Greek presidencies. Formal adoption of the legislation by the Council will be followed by the ratification procedure for the Own Resources Decision, which is expected to be concluded by late 2015 to early 2016. At that point, the legislative package will enter into force, with retroactive impact from 1 January 2014.

2.2 Negotiations with the European Parliament

Contrary to what happened in 2006, the Parliament did not succeed in challenging the MFF ceilings agreed by the European Council, acknowledging the particularly difficult context at the

time of this decision ⁽¹⁾. Instead, the Parliament's negotiation strategy focused on reaching a satisfactory outcome on the four following issues (as specified in the Parliament Resolution adopted on 13 March):

1. A mid-term revision of the MFF;
2. Flexibility;
3. Reform of the own-resources system;
4. Unity of the budget.

Negotiations with the Council (conducted by the Irish Presidency) were concluded at the end of June 2013 with an agreement between the three Presidents. The main results of these negotiations were:

- On the revision: inclusion of a compulsory review with a possibility for the Commission to propose a revision of the MFF by the end of 2016.
- On flexibility: Creation of a 'global margin for payments' and a 'global margin for commitments', and increased carry-over possibilities from one year to the next for the European Union Solidarity Fund, the Emergency Aid Reserve and the Flexibility Instrument. These additional flexibilities could, if fully used, entail an increase in actual spending higher than the top-up in commitments negotiated by the Parliament in 2006.
- A High-Level Group between the three institutions would be established to discuss the future of the own resource system of the European Union.
- On unity of the budget: inclusion of a point in the IIA covering Article 332 TFEU ⁽²⁾.

Following the successful conclusion of negotiations, the Parliament adopted a Resolution on 3 July 2013, expressing its willingness to put the MFFR and the IIA to the vote, subject to three conditions:

- The Council agreement to increase payment appropriations for 2013 by EUR 11.2 billion up to the MFF payment ceiling as proposed by the Commission. This was realised through the adoption of respectively AB 2/2013 (+ EUR 7.3 billion) and AB 8/2013 (+ EUR 3.9 billion);
- The establishment of a High-Level Group on own resources to be convened at the time of the formal adoption of the MFFR. In a Joint Declaration on Own Resources it was agreed that this group would be composed of members appointed by the three institutions. The mandate of the Group is to undertake a general review of the own-resources system: a first assessment is to be made available at the end of 2014, progress is to be assessed at the political level at least twice per year and the outcome of the work will be assessed by national parliaments at an interinstitutional conference during 2016. The Commission

⁽¹⁾ See the Parliament report prepared by MEPs Jean-Luc Dehaene and Ivalo Kalfin: On negotiations on the MFF 2014–20: lessons to be learned and the way forward (2014/2005(INI)) endorsed by the Parliament plenary on 15 April 2014 (A7-0254/2014).

⁽²⁾ See Chapter 10.

will take the work of the Group into account when it assesses whether to include proposals for reforms on own resources in its proposals for the period post-2020;

- Successful conclusion of the negotiations on the sectorial legislation, notably on CAP and cohesion.

The Parliament gave its consent to the MFFR and adopted the IIA on 19 November 2013 after concluding that these three related conditions had been met ⁽¹⁾.

The Council adopted the MFFR on 2 December 2013 and the IIA was approved by the three institutions on the same day.

⁽¹⁾ Although the High-Level Group on own resources did not meet in 2013, the EP judged that sufficient progress towards its establishment had been made.

Part 2

The characteristics of the present financial system



Chapter 8

The legal framework

The European Union's public finances are based on three types of legal instruments:

- the financial provisions of the Treaties (primary law) ⁽¹⁾;
- secondary legislation;
- provisions adopted by agreement between the institutions.

1. The financial provisions of the Treaties

The Treaty on European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU) ⁽²⁾, as they result from the amendments to the earlier Treaties introduced by the Treaty of Lisbon, introduced a number of changes in the EU public finances architecture whilst preserving the main features it had developed over time. Most strikingly, the multiannual financial framework was for the first time enshrined in primary law ⁽³⁾. But important changes to the annual budgetary procedure were also made.

Furthermore, Article 295 TFEU confers a binding nature to interinstitutional agreements concluded between the European Parliament, the Council and the Commission making arrangements for their cooperation.

1.1. The Treaty on the Functioning of the European Union

The financial provisions of the TFEU are contained in Title II (Articles 310 to 325) of Part Six, which deals with the Union's institutional and financial provisions, and they cover general rules and six chapters.

1) *The general principles governing the Union's budget* ⁽⁴⁾

- Article 310 TFEU establishes the principles of unity, universality, equilibrium, annuality, specification and sound financial management.

It also incorporates the concept of budgetary discipline into the Treaty as well as the obligation for the Union and the Member States to combat fraud and other illegal activities affecting the financial interests of the Union.

2) *The Union's own resources* ⁽⁵⁾

- Article 311 TFEU establishes the principle of financing the budget from own resources and sets out the procedure for adopting the Council decision laying down the provisions

⁽¹⁾ See Annex 1.

⁽²⁾ Consolidated versions of both Treaties have been published in OJ C83, 30.3.2010.

⁽³⁾ See also point 3 Chapter 6, point 2.5.

⁽⁴⁾ See Chapter 11.

⁽⁵⁾ See Chapter 9.

relating to the own-resources system. It does not alter the procedure for adopting that decision (see below, point 2.1.1), but as a novelty it introduces the explicit possibility for the Council to adopt by qualified majority, and after having obtained the consent of the European Parliament, a regulation laying down more detailed measures implementing that Decision ⁽¹⁾.

In view of the specific way in which it is adopted (pursuant to Article 311 TFEU), the Council decision on the system of own resources of the European Union is in fact equivalent to primary legislation.

The Member States have virtually absolute control over adoption of this decision, whilst the European Parliament is merely consulted. Not only must the Council act unanimously, thus giving each Member State a right of veto, but to enter into force the decision must be ratified by the national parliaments in the same way as the Treaties.

The first decision of this type was adopted in 1970. The most recent was taken by the Council in the form of Council Decision (EU, Euratom) No 2014/335 of 26 May 2014 on the system of own resources of the European Union ⁽²⁾. Subject to ratification it will apply retroactively from 1 January 2014.

3) *The Multiannual Financial Framework* ⁽³⁾

- Article 312 TFEU incorporates the multiannual financial framework, which was previously only part of Interinstitutional Agreements, into the Union's primary law. The overall aim of the MFF, covering at least five years and adopted in the form of a Council Regulation, is to ensure that the European Union's expenditure develops in an orderly manner and within the limits of its own resources.

The Council adopts the MFF regulation acting unanimously after obtaining the consent of the European Parliament. The European Council may, unanimously, adopt a decision authorising the Council to adopt the MFF regulation by qualified majority.

The financial framework must determine the annual ceilings on commitment appropriations by category of expenditure and the annual ceiling on payment appropriations. The categories of expenditure, limited in number, must correspond to the Union's major sectors of activity. In addition, the MFF regulation will lay down any other provisions required for the annual budgetary procedure to run smoothly.

The new provisions of Article 312 TFEU underline the common responsibility of the three institutions in taking any measure necessary to facilitate the adoption of the financial framework.

⁽¹⁾ Another novelty is that Article 322(2) allows Council to adopt by qualified majority (and no longer by unanimity) the methods and procedure whereby revenue provided under the own-resources decision shall be made available to the Commission.

⁽²⁾ OJ L 168, 07/06/2014, p. 105–111: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:JOL_2014_168_R_0013&qid=1402392861247

⁽³⁾ See Chapter 6.3 and Chapter 10.

In case of failure to agree on a new financial framework by the end of the previous one, the TFEU provides for legal and budgetary continuity based on the extension of the ceilings and other provisions corresponding to the last year of the previous financial framework until the new MFF Regulation is adopted.

4) *The Union's annual budget* ⁽¹⁾

- Article 314 TFEU provides for the timetable and stages in the Union's annual budgetary procedure.

The Lisbon Treaty has simplified the budgetary procedure, on the one hand by removing the distinction between compulsory and non-compulsory expenditure (and, hence, abolishing the 'maximum rate of increase') and, on the other hand, by amending the budgetary procedure which becomes analogous to a co-decision procedure with one reading and conciliation. This procedure for the adoption of the Union's budget is concluded by the act of the President of the European Parliament based on Article 314(9) TFEU by which he/she, after having verified that the procedure has been conducted lawfully, declares that the budget has been definitively adopted ⁽²⁾.

Both the Council and the Parliament have the possibility to reject the draft budget in the course of the procedure. The Commission may take all the necessary initiatives, e.g. it can call the Presidents of the Parliament and the Council to meet for consultations and conciliation.

The Conciliation Committee can be convened to reach agreement on a joint text. Several scenarios are envisaged in this respect, which may lead to two different results: either the budget is deemed to be adopted or a new draft budget has to be submitted by the Commission.

- If, within 21 days, the Conciliation Committee does not agree on a joint text, a new draft budget must be submitted by the Commission. Similarly, if the European Parliament and the Council both reject the joint text, or if one of these institutions rejects the joint text and the other fails to take a decision, a new draft budget must be submitted by the Commission. The same applies if the Parliament rejects the joint text but the Council approves it.
- Any other outcome of the conciliation procedure leads to the budget being deemed to be adopted.
- Article 315 TFEU contains the provisions necessary to allow the Community's financial activities to continue if the budget is not adopted on schedule.

5) *Implementation of the budget and discharge*

- Article 317 TFEU assigns to the Commission the essential powers and accountability for implementing the budget.

⁽¹⁾ See Chapter 12.

⁽²⁾ See Case C-77/11, *Council of the European Union v European Parliament*, of 17.9.2013.

The Lisbon Treaty takes into account the obligations and resultant responsibilities of the Member States in respect of budget implementation and discharge. Regarding budget implementation, where the majority of budgetary appropriations are implemented under the shared management system, Article 317 TFEU stipulates that ‘the Commission shall implement the budget in cooperation with the Member States’. The same article also provides that the financial regulations will lay down the control and audit obligations of the Member States in the implementation of the budget. Therefore the responsibility of the Member States emerging from close cooperation with the European Commission in implementation of the budget has been recognised.

- Article 318 TFEU lays down the procedures for the Commission to submit the accounts to the Council and to the Parliament.
- Article 319 TFEU lays down the procedure for the discharge which the Parliament, acting on a recommendation by the Council, gives to the Commission in respect of the implementation of the budget.

6) Common provisions

- With Article 322(1) TFEU the procedures for adopting supplementary rules (financial regulations) for establishing and implementing the budget and for presenting and auditing accounts, as well as for providing for checks on the responsibility of financial actors, in particular authorising officers and accounting officers, became subject to the ordinary legislative procedure, i.e. to co-decision by the Parliament and the Council.

7) Combating fraud

- Article 325 TFEU defines the roles of the Commission and the Member States in combating fraud affecting the Union’s financial interests. Here again, the procedure by which the measures needed in this area are adopted becomes subject to co-decision by the Parliament and the Council.

1.2. The Treaty on European Union

1) Financing of the Common Foreign and Security Policy

Article 41 TEU contains specific provisions on financing operations under the common foreign and security policy (CFSP), whilst the Lisbon Treaty has repealed similar specific provisions for cooperation in the fields of justice and home affairs.

A distinction is made between the administrative expenditure arising from these operations and the operational expenditure. The administrative expenditure is automatically charged to the Union budget. As a rule, operational expenditure is also charged to the budget, unless the Council unanimously votes otherwise, in which case the operational expenditure will normally be financed by the Member States, scaled to gross national product, unless the Council again unanimously votes otherwise.

Article 41 TEU rules out the possibility of charging budget expenditure to the Union under the CFSP relating to operations with military or defence implications. Such expenditure is therefore always financed by the Member States taking part in the operations.

Article 41 also lays down specific procedures allowing for urgent financing of initiatives in the framework of the CFSP.

2) Enhanced cooperation

Article 20 TEU allows Member States which intend to establish enhanced cooperation between themselves within the framework of the Union's non-exclusive competences to make use of its institutions and exercise those competencies subject to the detailed arrangements laid down in this Article and in Articles 326 to 334 of the TFEU.

Article 332 TFEU states that expenditure arising from implementation of enhanced cooperation, other than administrative costs entailed for the institutions, is to be financed by the participating Member States, unless the Council unanimously decides otherwise.

3) Non-participation by Member States in certain operations

Protocols annexed to the Treaties allow the United Kingdom, Ireland and Denmark not to take part in measures adopted pursuant to Title V of Part Three of the TFEU (on police and judicial cooperation, asylum and immigration and other policies relating to the area of freedom, security and justice). Denmark has also decided not to take part in the elaboration and implementation of Decisions under the common foreign and security policy which have defence implications.

The abovementioned Member States therefore do not have to cover the financial consequences of these measures, except for the administrative costs arising for the institutions.

2. Secondary legislation: The Financial Regulation

In accordance with Article 322 TFEU, the Financial Regulation is adopted by the European Parliament and the Council, acting in accordance with the ordinary legislative procedure after consulting the Court of Auditors. Co-decision on the Financial Regulation is a novelty introduced by the Lisbon Treaty; under the previous Treaty it was subject to a unanimous Council Decision after consulting the Parliament and having obtained an opinion from the Court.

The Financial Regulation was originally adopted on 21 December 1977 ⁽¹⁾, but has been amended repeatedly since then. It mainly contains provisions applicable to the general budget: principles, establishment, structure, implementation and auditing of the accounts. The regulation deals exhaustively with implementation and control, as these aspects are not covered comprehensively in the Treaty.

The 1977 text was amended fourteen times to take account of institutional changes (Maastricht and Amsterdam Treaties, joint financing by the EFTA countries for the EEA) and also to tighten up the management of Union finances ⁽²⁾.

⁽¹⁾ OJ L 356, 31.12.1977, p. 1.

⁽²⁾ See the explanatory memorandum accompanying the Commission proposal for a revised financial regulation, COM(2000)461 of 17.10.2000, p. 6.

2.1. The reform of 2002

Following the resignation of the Santer Commission, far-reaching administrative reforms were carried out in the Union. As the Financial Regulation contains the rules governing financial management, control and audit, the recasting of the Financial Regulation was inextricably linked to this process. In view of the technical complexity and scale of the task, which concerned all areas of Community activity and all the institutions, the Commission decided that the best approach was to present a working document intended to launch an interinstitutional discussion on the solutions envisaged by the Commission (SEC(1998) 1228 final, 22 July 1998), before presenting a legislative proposal. The main planks of the reform, such as the assertion of the responsibility of authorising officers under the supervision of the internal audit service and, in return, the dropping of centralised *ex ante* controls (in particular the Financial Controller's approval of commitments and payments) could not be implemented without substantially amending the Financial Regulation. The recasting exercise, however, went further than the goals identified by the internal reform of the Commission. Its scope encompassed many areas covered by the present Financial Regulation — the instrument which lays down rules for all aspects of the general budget of the European Communities from establishment to discharge ⁽¹⁾.

The Financial Regulation of 21 December 1977 was thus recast by Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 ⁽²⁾. The 2002 Financial Regulation goes beyond many financial regulations at national level, as it not only contains rules for budget establishment, but also contains detailed provisions on budget implementation, including procurement and grant rules.

Regulation 1605/2002 was amended by Council Regulation (EC, Euratom) No 1995/2006 of 13 December 2006 ⁽³⁾. Its essential elements have been maintained and strengthened. Transparency, in particular, has been reinforced by laying down that information on all categories of recipients of all kinds of expenditure financed by the Community budget will be released, irrespective of the entity or authority involved in implementing the budget, thus including decentralised and joint management of the budget with non-EU countries and international organisations.

A second amendment entered into force in 2007 ⁽⁴⁾ with a specific provision concerning the funding of political parties. Through a third amendment ⁽⁵⁾, specific clauses concerning the EEAS were introduced in the Financial Regulation.

⁽¹⁾ See the explanatory memorandum accompanying the Commission proposal for a revised financial regulation, COM(2000)461 of 17.10.2000, p. 6.

⁽²⁾ OJ L 248, 16.9.2002, p. 1.

⁽³⁾ OJ L 390, 30.12.2006, p. 1.

⁽⁴⁾ Council Regulation (EC) No 1525/2007 of 17 December 2007, OJ L 343 of 27.12.2007, p. 9.

⁽⁵⁾ Regulation (EU, Euratom) No 1081/2010 of the European Parliament and of the Council of 24 November 2010, OJ L 311 of 26.11.2010, p. 9.

2.2. The Financial Regulation 2012

Regulation 1605/2002 provided for the Commission to propose triennial revisions of the Financial Regulation. On this basis, the Commission prepared a legislative proposal adopted at the end of 2010. The proposal had three objectives. It ensured that delivery mechanisms are simple and transparent (especially to final recipients of EU funds), provided for the possibility for leveraging non-EU budget resources, and at the same time strengthened the Commission's accountability for implementation of the budget as set in Article 317 TFEU⁽¹⁾.

The revised Financial Regulation was adopted on 25 October 2012⁽²⁾, following an ordinary legislative procedure. Most of its provisions were applied from 1 January 2013. It meets the objectives mentioned above.

a) Simplification

The revised Financial Regulation (hereafter: FR) contains numerous improvements which facilitate the access of recipients to Union funds. The period between calls for proposals and the conclusion of grant agreements and payment deadlines is shortened. The emphasis of the grant system is shifted from reimbursing cost claims to payments for the delivery of results through a greater use of lump sums, flat rates, unit costs. A greater use of prizes, paid to the winner of a contest for developing the solution to a pre-defined problem ('inducement prizes') also contribute to simplifying administration and strengthening the result-orientation of EU funding. Beneficiaries of EU funds are no longer obliged to open separate interest-bearing bank accounts. Furthermore, even if interest is generated, it does not have to be returned to the EU Budget and neither is it counted as revenue of the project. This addresses a major concern of grant beneficiaries and other stakeholders, in particular from the research and the NGO community that was brought up during the public consultation of 2009 preceding the Commission's proposal of 2010.

b) More accountability

The new rules increase the accountability of those managing EU taxpayers' money, and in particular the Member States, which implement a large proportion of the EU budget, including the EU's regional policy. In future, Member State authorities managing EU funds have to sign and submit to the Commission annual declarations certifying that EU funds have been used correctly.

Mechanisms for financial corrections in cases of irregularities committed by beneficiaries and discovered through audit have been strengthened: as a deterrent, the Commission will publish decisions imposing sanctions for misuse of EU funds.

c) Enhancing the effectiveness of EU funds through innovative funding mechanisms

⁽¹⁾ Proposal for a Regulation of the European Parliament and of the Council on the financial rules applicable to the annual budget of the Union, COM(2010) 815 final of 22.12.2010.

⁽²⁾ Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002, OJ L 298 of 26.10.2012, p. 1.

Various financial instruments, such as loans, equity or guarantees are foreseen to enhance the effectiveness of EU funds and thus multiply their financial impact. The FR also foresees the creation of a more flexible implementation of public-private partnerships (PPPs) following the calls of European industry stakeholders who are the partners in such PPPs.

In the area of external action, the EU will be able to create EU trust funds pooling its own resources with those of its Member States and other donors in order to better coordinate and deliver external aid and increase its visibility ⁽¹⁾.

An in-depth description of the main provisions of the FR can be found in Chapters 11 and 15.

2.4. The rules of application

The provisions of Regulation 1605/2002 were complemented by a Commission Regulation ⁽²⁾, commonly referred to as the 'Implementing Rules'. With the entry into force of the Lisbon Treaty, the Implementing Rules had to be replaced by a delegated act in accordance with Article 290 TFEU, on the basis of empowerments included in the relevant articles of the FR. On this basis, the Commission adopted the delegated Regulation ⁽³⁾, the 'Rules of Application' (RAP). The RAP contain more detailed and technical rules, which are essential for the day-to-day implementation of the FR.

3. Other secondary legislation

3.1. Sectoral funding programmes for 2014–20

The legal framework to allocate funds in all the key sectoral policy objectives of the Union is in place and applies from 1 January 2014 ⁽⁴⁾. This new generation of sectoral financing programmes is a major step in simplifying the funding rules through notably the alignment with the Financial Regulation, the introduction of single funding models and the reduction of audit burden.

Another relevant achievement has been the streamlining of programmes per policy area with the objective of ensuring synergies and common implementation rules and procedures. Single sectoral frameworks have, for example, been introduced in the following key areas:

- Research and innovation policy — Rules for participation and dissemination in Horizon 2020 — the Framework Programme for Research and Innovation (2014–20) ⁽⁵⁾;

⁽¹⁾ See the press release IP/12/1133 of 29.10.2012.

⁽²⁾ Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities, OJ L 357, 31.12.2002, p. 1)

⁽³⁾ Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union, OJ L362 F 31.12.2012.

⁽⁴⁾ For a description of the policy areas covered by the MFF, see Chapter 14.

⁽⁵⁾ Regulation (EU) No 1290/2013 of the European Parliament and of the Council of 11 December 2013 laying down the rules for participation and dissemination in Horizon 2020 — the Framework Programme for Research and Innovation (2014–20) and repealing Regulation (EC) No 1906/2006, OJ L 347, 20.12.2013, p. 81.

- Cohesion, rural development and fisheries and maritime policies — the Common Provisions Regulation ⁽¹⁾;
- External relations: the common rules and procedures for the implementation of the Union's instrument for financing external actions ⁽²⁾.

3.2 Implementation of the own-resources decision

The Lisbon Treaty provides for an implementing Regulation, based on Article 311.4 TFEU, which opens up the possibility for more flexible practical arrangements to the extent that these are authorised by the Own-Resources Decision. However, the provisions related to making own resources available and meeting cash requirements continue to be included in a separate regulation based on Article 322.2 TFEU. Both regulations require qualified majority in the Council (previously unanimity for the latter) and the implementing regulation also requires the consent of the Parliament.

The implementation of the own-resources decision is thus governed by two other instruments ⁽³⁾:

- Council Regulation (EU, Euratom) No 608/2014 of 26 May 2014 laying down implementing measures for the system of own resources of the European Union ⁽⁴⁾ adopted pursuant to Article 311, fourth paragraph;
- Council Regulation (EU, Euratom) No 609/2014 of 26 May 2014 on the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements ⁽⁵⁾, adopted pursuant to Article 322(2) TFEU.

4. Rules adopted by agreement between the institutions

To prevent or overcome risks of conflict and gridlock in the budget procedures, the institutions concerned have often been prompted to conclude agreements on how to exercise the powers they are given by the Treaties. A number of interinstitutional agreements or joint declarations have thus been concluded since the mid-1970s including, as from 1988, the financial perspectives ⁽⁶⁾. The purpose of these agreements was to impose budgetary discipline, to improve the

⁽¹⁾ Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006, OJ L 347, 20.12.2013, p. 320.

⁽²⁾ Regulation (EU) No 236/2014 of the European Parliament and of the Council of 11 March 2014 laying down common rules and procedures for the implementation of the Union's instruments for financing external action, OJ L 77, 15.3.2014, p. 95.

⁽³⁾ See Chapter 9.

⁽⁴⁾ OJ L 168, 07/06/2014, p. 29–38: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1402393197416&uri=OJ:JOL_2014_168_R_0004

⁽⁵⁾ OJ L 168, 07/06/2014, p. 39–52: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1402393197416&uri=OJ:JOL_2014_168_R_0005

⁽⁶⁾ See Chapters 2 to 6.

functioning of the annual budgetary procedure and cooperation between the institutions on budgetary matters and to ensure sound financial management.

The Lisbon Treaty confers a legally binding nature to those agreements (Article 295 TFEU). Their content has also changed, since the provisions relating to the multiannual financial framework are now mainly laid down in the Council Regulation adopted pursuant to Article 312 TFEU. The Interinstitutional Agreement of 2 December 2013 on budgetary discipline, on cooperation in budgetary matters and on sound financial management covers a number of more detailed provisions relating to the MFF and provisions to improve interinstitutional cooperation in budgetary matters and sound financial management of Union funds ⁽¹⁾.

⁽¹⁾ See Chapter 10.

Chapter 9

The financial autonomy of the European Union: the own-resources system

The Union's own resources may be defined as revenue allocated irrevocably to the Union to finance its budget and accruing to it automatically without the need for any subsequent decision by the national authorities.

The own-resources system developed gradually into its present form. Unlike the ECSC Treaty, the Treaties of Rome did not immediately set up a system of own resources for financing the Communities they were establishing: the two Communities (EEC and EAEC) were initially financed by contributions from the Member States. However, these Treaties did anticipate the creation at a later date of a system of own resources which would include, in particular, revenue from the Common Customs Tariff once it had been finally set up.

The Decision of 21 April 1970, which progressively replaced national contributions was the basis for the establishment of own resources. Subsequent own-resources decisions have amended the system several times ⁽¹⁾.

Own-resources decisions are conceived in principle to cover the same period as and be complementary to the respective Multiannual Financial Framework. The legislative proposals are devised and negotiated as a package. However, the own-resources decision does not have an expiry date and continues to be valid until a new decision enters into force. Pending the adoption and approval by the Member States (ratification) of the new Council Decision on the system of own resources of the European Union '2014–20', the system of own resources remains based on Council Decision 2007/436, which was adopted in the wake of the MFF for 2007–13 ⁽²⁾. Once in force, the new own-resources decision will apply with retroactive effect, i.e. as of 1 January 2014. The present implementing legislation will also remain valid until the new own-resources decision enters into force.

The main components of the current system are:

- traditional own resources, which result directly from the existence of a unified customs area and are not attributable to the Member States for legal — and practical — reasons; these resources are sugar levies and customs duties;
- VAT-based own resources, derived from the application of a call rate to a VAT base determined uniformly for the Member States in accordance with EU rules;
- GNI-based own resources, resulting from the application of a set call rate to total EU GNI, to match the total volume of resources to the total volume of expenditure;
- correction mechanisms, which grant particular Member States a reduction of their contribution to the EU budget.

Figure 9.1 shows the evolution of EU budget revenue by type of resource over the period 2000–12.

⁽¹⁾ The development of the own-resources system and its structure are described more in detail in Part I and Part IV, Chapter 13.

⁽²⁾ See Chapter 6.

Chapter 13 provides a more detailed description of the categories of own resources and the correction mechanisms under the current system.

FIGURE 9.1 – EU Revenue 2000–12 (million EUR)

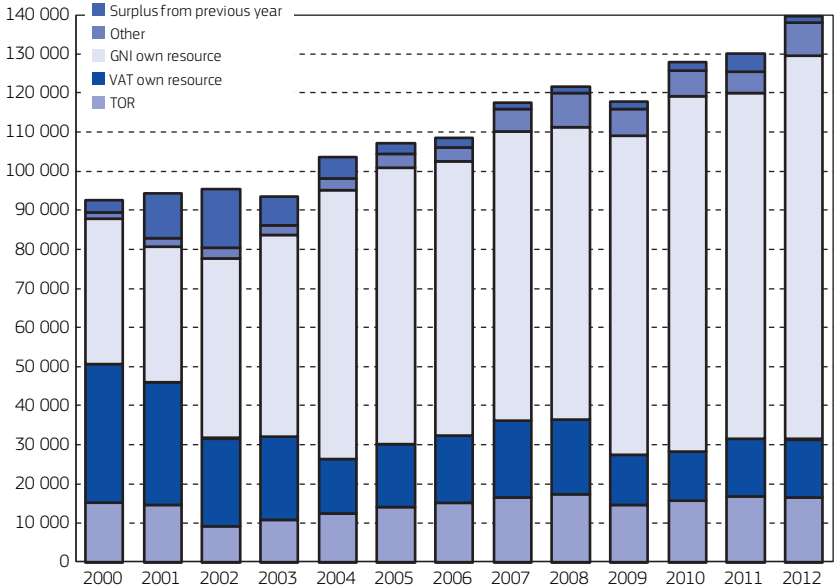
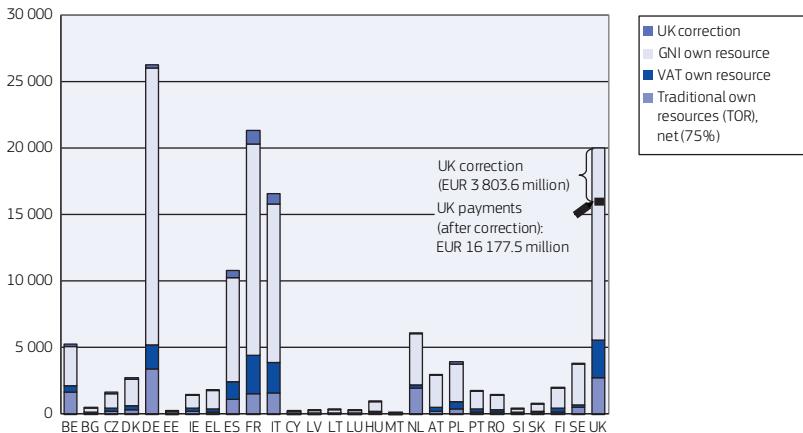


FIGURE 9.2 – National contribution per Member State and TOR collected on behalf of the EU in 2012 (million EUR)



1. The legislation on own resources

Subject to ratification of the Council Decision (EU, Euratom) No 2014/335 of 26 May 2014 on own resources, the main provisions applying to the 2014–20 period are laid down in the following legislative acts:

1) *The Own-Resources Decision*

COUNCIL DECISION (EU, Euratom) No 2014/335 of 26 May 2014 on the system of own resources of the European Union.

The own-resources decision (ORD) defines and establishes the different categories of own resources and the specific methods for their calculations ⁽¹⁾. It lays down the own-resources ceiling for payments (1.23 % of the sum of all the Member States' GNIs) and the ceiling for commitments entered in the Union's budget (1.29 % of the sum of all the Member States' GNIs).

The ORD furthermore sets out the principles of the correction mechanism in favour of the United Kingdom and its financing as well as the temporary corrections for certain other Member States ⁽²⁾.

Finally, the ORD includes provisions regarding the universality principle, the carry-over of surplus and the implementing measures which may be laid down in a regulation on the basis of Article 311(4) of the Treaty, i.e. requiring the consent of the European Parliament.

2) *The Implementing Regulation*

COUNCIL REGULATION (EU, Euratom) No 608/2014 of 26 May 2014 laying down implementing measures for the system of own resources of the European Union.

This regulation lays down implementing measures — in as far as authorised in the ORD — such as the calculation and budgeting of the balance or control and supervision measures.

3) *The 'making-available' Regulation*

COUNCIL REGULATION (EU, Euratom) No 609/2014 of 26 May 2014 on the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements (Recast).

This regulation lays down rules on making available to the Commission the own resources of the Union referred to in the Own Resources Decision. It contains provisions on the date of establishment of own resources, on the conservation of supporting documents, on administrative cooperation, applicable rates, entry in the accounts and reporting. It also includes provisions on treasury and accounting arrangements, the timing for making available own resources, opt-out adjustments, interest on amounts made available

⁽¹⁾ For more details, see Chapter 13.2.

⁽²⁾ The calculation, financing, payment and entry in the budget of the 'UK correction' is further specified in a Commission Working Document, which is unanimously endorsed by the Council.

belatedly, irrecoverable amounts, requirements on management of cash resources and the execution of payment orders ⁽¹⁾.

2. The essential characteristics of the present system of own resources

The system in place since 1988, when the GNI-based own resources were introduced, has three main objectives:

- Financially: it automatically ensures a level of resources in line with agreed expenditure;
- Legally: it guarantees the specific nature of the EU's resources;
- Economically: a number of provisions have been introduced to respect the principle, agreed at the 25 and 26 June 1984 Fontainebleau European Council, that 'any Member State sustaining a budgetary burden which is excessive in relation to its relative prosperity may benefit from a correction at the appropriate time' ⁽²⁾.

2.1. The financial dimension: a guaranteed level of resources for the European Union

The Community's financial difficulties in the early 1980s stemmed from the difficulty of meeting growing, inflexible expenditure requirements from the limited resources available (see Chapter 2). Until 1988, the amount of available own resources was not linked to expenditure requirements. This led to two diverging trends:

- limited availability of financing sources, due to a relative decrease in traditional own resources (on account of trade liberalisation) and the constraint imposed on the VAT-based resources by the ceiling;
- continually rising expenditure generated by the development of new policies and the reinforcement of existing ones.

The system put in place in 1988 introduced an overall own-resources ceiling plus the GNP-based (later GNI-based) resource, which would function as the residual resource, maintaining the necessary balance between revenue and expenditure.

1) *The own-resources ceiling*

The own-resources decision sets an overall ceiling for own resources, expressed as a percentage of EU GNI (initially 1.27 % of the European System of Accounts (ESA) 79 GNP, recalculated as 1.24 % of ESA 95 GNI in 2001). Under Decision 2007/436 the GNI base is established in accordance with ESA 95.

Since 1 January 2010, following a unanimous Council Decision, the ESA 95 GNI base for own resources purposes includes also the allocation of Financial Intermediation Services Indirectly Measured (FISIM). As a result the GNI was increased by around 1 % on average (however with a different impact on each Member State) and the own-resources ceiling was reduced from 1.24 %

⁽¹⁾ For more details, see Chapter 15.4.

⁽²⁾ Bull. EC 6-1984, page 10.

of EU GNI to 1.23 % ⁽¹⁾. Under the next own-resources decision the GNI base will be established on the basis of ESA 2010 and the own-resources ceiling will need to be revised accordingly.

The own-resources ceiling applies to own resources taken as a whole, for all Member States. It limits the maximum amount of own resources which can be allocated to the Union to cover all payment appropriations inscribed in the EU budget. The ceiling remains applicable, unless the basic decision is amended, even if the financial framework is not renewed when it expires. This ensures the continuity of the financing system, whilst imposing a limit on any increase in expenditure.

2) The link between revenue and expenditure

The compatibility between the expenditure trend and the ceilings laid down for own resources is ensured by a number of provisions:

- Under Article 3(2) of the own-resources decision, total appropriations for commitments entered in the budget may under no circumstances exceed a set percentage of EU GNI (initially 1.335 % of ESA 79 GNP, recalculated as 1.31 % of ESA 95 GNI in 2001 and 1.29 % in 2010);
- Article 312(1) TFEU provides for the multiannual financial framework to ensure that ‘Union expenditure develops in an orderly manner and within the limits of own resources’. The MFF Regulation includes specific provisions for making sure that the total appropriations for payments for each year covered by the MFF remain compliant with the own-resources ceiling ⁽²⁾.

3) The GNI-based resource as a ‘top-up’

In addition to the proceeds from traditional own resources and the VAT-based resource, which are determined by the rates applicable and the actual movement in the bases, expenditure is financed by revenue based on GNI. There is no particular limit on the rate of call for the GNI-based resource other than the own-resources ceiling, which limits the total amount of all own resources to a maximum of 1.23 % of EU GNI.

This resource is therefore intended to balance the budget, which is why it is often referred to as ‘the additional resource’ or ‘the residual resource’ in budget documents.

2.2. The legal dimension: the specific nature of the resources

1) The legal basis: a definitive transfer of revenue by Member States under a specific procedure

Unlike the earlier system of financial contributions, the present system of own resources can be defined as a definitive transfer to the EU. Pursuant to Article 17 of the Financial Regulation, the Union’s annual budget revenue and payment appropriations must be in balance, in line

⁽¹⁾ Communication from the Commission to the European Parliament and the Council: Adaptation of the ceiling of own resources and of the ceiling for appropriations for commitments following the decision to apply FISIM for own resources purposes.

⁽²⁾ Article 4 of the MFF Regulation. See Chapter 10, sections 1.2 and 2.1.

with the principle of equilibrium enshrined in the Treaty ⁽¹⁾. The final adoption of each year's budget thus imposes a legal obligation on each Member State to make over to the EU the payments due under this budget, which explains the particularly cumbersome, formal procedure needed for adoption of basic decisions in this field, under Article 311 of the Lisbon Treaty (former Article 269 of the Treaty of Rome).

2) *The consequence: automatic payment*

As the Union does not have its own tax authority, traditional own resources (customs duties, sugar and isoglucose levies) are collected by the authorities of the Member States. In accordance with Article 2 of Regulation (EC, Euratom) No 1150/2000, these resources are established by the Member States as soon as the conditions provided for by the customs and sugar regulations for entry of the entitlement in the accounts and notification of the debtor have been met. The entitlements established are entered in the accounts and then credited to an own-resources account opened in the name of the Commission with the Member State's Treasury or their appointed body.

The VAT-based and GNI-based resources are made available on the first working day of each month at the rate of one-twelfth of the amount inscribed in the EU budget. This payment is guaranteed by Article 11 of Regulation (EC, Euratom) No 1150/2000, as last amended by Regulation (EC, Euratom) No 105/2009, which provides that interest payments will be imposed on any Member State which fails to credit the amounts on time.

The specific nature of the own resources, and consequently the EU's financial autonomy, are sometimes obscured by the fact that the own resources payments often appear in the national budgets and may therefore seem to be conditional on the vote of the national parliaments and to compete with national expenditure. These national procedures have, however, no legal implications since under the Union's legislation the transfer of resources is automatic.

2.3. The economic dimension: the search for more fairness

1) *Partial and gradual replacement of the VAT-based own resources by GNP/GNI-based own resources*

The VAT-based own resource is structurally regressive, in that the proportion of consumption in GNI, and therefore in the VAT base, is often higher in the less prosperous Member States than in the richer States. Conversely, net exporting countries with high savings rates are favoured. Therefore, in an attempt to increase the fairness of Member States' gross contributions, the VAT bases have been capped in relation to the GNI ⁽²⁾ and the share of the VAT-based own resources in the financing of the budget has been progressively reduced. The foregone resources have been replaced by an increase of the GNP/GNI-based resources.

⁽¹⁾ See Chapter 11.

⁽²⁾ See Chapter 13.

2) *The issue of budgetary balances*

The European Union is a community of solidarity which amongst other principles and values shall also promote economic, social and territorial cohesion. Consequently, the Union's budget finances Union policies which in terms of mere spending may benefit the Member States to different degrees, depending on their needs and potential. Looking individually at each Member State, this gives rise to budgetary 'net balances' (i.e. net benefits or net contributions) vis-à-vis the EU budget, although the policy benefits accrue to the Union as a whole. Budgetary net balances, measured by the difference between contributions to and receipts from the EU budget, obviously fail to account for the direct and indirect benefits resulting from EU budget intervention in a common market and EU membership in general and give a very limited view of the overall cost-benefit relation. The Commission has stressed this point on many occasions ⁽¹⁾. Nevertheless, the size of some of these imbalances has been at the centre of political discussions.

Various measures have been introduced in the own-resources system in attempts to redress the perceived excessive budgetary imbalances of certain Member States.

In 1984 the Fontainebleau European Council introduced a correction mechanism with regard to one Member State — the United Kingdom — whereby 66 % of the UK's net contribution is reimbursed. Although the correction was only for the UK, the Fontainebleau European Council acknowledged the general principle of entitlement to a correction, based on the size of the budgetary imbalance and the relative wealth of a Member State compared with the EU as a whole.

Other ad hoc measures were introduced over time, adding to the complexity of the system, in particular:

- limits on the financing of the UK correction: one third reduction for Germany over 1985–2001 and a 75 % reduction for Germany, the Netherlands, Austria and Sweden since 2002;
- increase in the share retained as collection costs of traditional own resources from 10 % over 1970–2000 to 25 % since 2001, benefiting notably the Netherlands; to be reduced to 20 % for the period 2014–20;
- a call rate of 0.3 % to be applied retroactively from 1 January 2007 when the ORD 2007/436 entered into force. The same decision introduced, for the period 2007–13 only, a reduced call rate of 0.225 % for Austria, 0.15 % for Germany and 0.10 % for the Netherlands and Sweden; a reduced rate of 0.15 % for Germany, Sweden and the Netherlands has been agreed for 2014–20;

⁽¹⁾ A full statement on this policy and its rationale was made in Chapter 2 of the 1998 Commission Report Financing of the European Union (available on: http://ec.europa.eu/budget/documents/agenda_2000_reports_financing_en.htm) and in Budget Contributions, EU Expenditure, Budgetary Balances and Relative Prosperity of the Member States, a paper presented by President Santer to the Ecofin Council of 13 October 1997. The Presidency Conclusions of the Berlin European Council of 24 and 25 March 1999 endorsed this principle: '[...] it is recognised that the full benefits of Union membership cannot be measured solely in budgetary terms' (point 68).

- a gross reduction in the annual GNI contribution by the Netherlands and Sweden for the period 2007–13 only (also adopted in the ORD 2007/436) ⁽¹⁾ and again for Netherlands, Sweden as well as Denmark for the period 2014–20 and Austria for 2014–16 ⁽²⁾;
- downward adjustment of the UK correction, notably in relation to pre-accession expenditure and to expenditure in the Member States which joined the EU after 30 April 2004, so that the United Kingdom pays a fairer share of EU expenditure in the period of enlargement.

⁽¹⁾ See Article 2(5) of Council Decision 2007/436/EC, Euratom of 7 June 2007 on the system of the European Communities' own resources.

⁽²⁾ See Article 2(5) of Council Decision (EU, Euratom) No 2014/335 of 26 May 2014 on the system of own resources of the European Union.

Chapter 10

The multiannual financial framework

Since the 1988 reform, the budgetary procedure has been placed in a multiannual financial framework adding an additional constraint and a different type of ceilings to the overall ceilings set in the Council decision on own resources.

The decision on own resources sets an overall annual ceiling for the Union's own resources expressed in a percentage of the Union's Gross National Income. Since each year's budget has to be adopted and implemented in balance, without prejudice to other revenue, the ceilings set in the decision on own resources determine the maximum amount of annual Union expenditure, in terms of appropriations for payments and commitments. They are both a limit, in economic terms, on the size of the Union budget and a guarantee that the Union will have a maximum volume of financial resources at its disposal which will develop in line with economic activity in all the Member States.

Within the ceilings set in the decision on own resources, the multiannual financial framework sets annual limits by category of expenditure for commitment appropriations and on total expenditure for payment appropriations.

The introduction of the financial framework has appreciably altered the parameters of the annual budgetary debate and has facilitated the development of multiannual financial programmes.

The terms for application of the current multiannual financial framework are set out in the Council Regulation (EU, Euratom) No 1311/2013 of 2 December 2013 laying down the multiannual financial framework for the years 2014–20 (MFFR) and the Interinstitutional Agreement (IIA) of 2 December 2013 between the European Parliament, the Council and the Commission on budgetary discipline, on cooperation in budgetary management and sound financial management ⁽¹⁾.

1. Ceilings on expenditure within the financial framework

Based on an economic forecast it is possible to express the annual ceilings on appropriations for commitments and payments as a percentage of the estimated Union Gross National Income. In this way, it is possible to check that the MFF ceilings on Union expenditure are compatible with the ceilings laid down in the ORD. These are also expressed as a percentage of GNI and currently amount to 1.29 % and 1.23 % for commitments and payments respectively. The latter is known as the 'own-resources ceiling'.

1.1. Annual Ceilings per heading (commitments)

The financial framework breaks down commitment appropriations into broad categories of expenditure (headings, which can comprise sub-headings and sub-ceilings). From a budgetary viewpoint there is no difference between a heading and a sub-heading. They both set a maximum ceiling of expenditure and prevent the appropriations or margins available under

⁽¹⁾ *op.cit.*, see Annex.

one heading or sub-heading being used for expenditure in another heading or sub-heading. The present financial framework (2014–20) comprises six headings, one of which (Heading 1) is sub-divided into two sub-headings.

In addition, Headings 2 and 5 each comprise a sub-ceiling. The sub-ceiling creates an asymmetrical barrier within a heading. Like the sub-heading it sets a maximum ceiling for the expenditure contained within it. However, any unallocated margins under the sub-ceiling may — if necessary — be used for other expenditure within the heading but outside the sub-ceiling. The sub-ceiling also makes it possible to transfer appropriations budgeted for programmes/actions included under the sub-ceiling to other programmes/actions under the same heading.

Each heading must be sufficiently homogenous to clearly identify the Union's political priorities and sufficiently wide to allow for a certain flexibility in reallocating expenditure between programmes under the same heading. Each heading is complete in itself and covers a specific category of action. A budget item coming under one heading cannot be financed from another.

A description of these headings can be found in Chapter 14.

1.2. Annual ceilings on total expenditure (payments)

An annual ceiling is established for appropriations for payments on the basis of an orderly progression in relation to appropriations for commitments. In practice this means establishing a series of payment schedules for different expenditure categories. This overall annual ceiling is not broken down by headings.

The ceiling on own resources may not be exceeded. A 'margin available' is inserted between the ceiling on own resources and the annual MFF ceiling on appropriations for payments. It plays a threefold role:

- It allows for revision of the financial framework should it be necessary to meet expenditure not originally foreseen;
- it helps to cushion the consequences of an unexpectedly low economic growth rate. In these circumstances, the volume of own resources actually available, with a ceiling set as a percentage of GNI, is smaller than envisaged at the outset, while the total ceiling for expenditure, which is set as an absolute amount, remains unchanged. The difference is taken from the 'margin available';
- it covers any guarantees provided by the EU budget which could potentially result in an additional call on own resources to cover a third-party default.

In any event, the ceiling on own resources is an absolute limit. If the 'margin available' were completely used up, the budget adopted would still have to keep within that limit, which would mean that the total payment appropriations entered in the budget would be below the ceiling authorised in the financial framework. In such a situation, the budgetary authority would have to decide on the reductions needed in the ceilings set in the financial framework in order to comply with the own-resources ceiling (Article 4(2) MFFR). In the recent and current financial frameworks, however, the ceilings set for payment appropriations have been set well below the own-resources ceiling. Such a situation therefore remains rather hypothetical.

2. Application of the financial framework

2.1. The Council Regulation laying down the multiannual financial framework 2014–20

The MFFR includes, besides the MFF table itself and some general provisions, all the elements which determine if and how the ceilings can be exceeded or revised.

The MFFR comprises three chapters:

1. General provisions
2. Special instruments
3. Revision

1) General provisions

The Chapter on general provisions refers to the Annex setting out the financial framework itself.

It includes a provision on the mid-term review/revision of the MFF (Article 2 MFFR). The review, to be presented by the end of 2016 at the latest, will be a Commission assessment of the functioning of the MFF. It may be accompanied, as appropriate, by a legislative proposal from the Commission to revise the MFF ⁽¹⁾. The appropriate duration of the next MFF, fixed at seven years for the current one, will also be discussed in that context ‘with a view to striking the right balance between the duration of the respective terms of office of the members of the European Parliament and the European Commission and the need for stability for programming cycles and investment predictability’ ⁽²⁾.

Articles 3 and 4 of the MFFR deal, respectively, with compliance with the ceilings set for the MFF and for own resources. Article 3(2) lists the special (flexibility) instruments which can be mobilised ‘over and above the ceilings’, i.e. without need to revise the ceilings, in accordance with Articles 9 to 15. Article 3(3) represents a novelty: amounts mobilised in respect of guarantees for loans under the Balance of Payments or the European Financial Stabilisation Mechanism ⁽³⁾ are outside the MFF ceilings (but need to respect the own-resources ceiling).

The ‘global margin for payments’ (Article 5 MFFR) represents a major innovation introduced by the MFFR. It allows the Commission to adjust each year (from 2015) the payment ceiling of a given year upwards by an amount equivalent to the difference between the executed payments and the payment ceiling of the previous year ⁽⁴⁾.

This new instrument draws on the experience with the financial framework of the previous period ⁽⁵⁾: whilst large margins remained available under the ceilings at the beginning of

⁽¹⁾ In a Declaration relating to Article 2 MFFR, the Commission confirms its intention to submit legislative proposals for a revision of the MFF, paying particular attention to the functioning of the global margin for payments, examining the evolution of the global margin for commitments and taking into account the particular requirements of the Horizon 2020 programme.

⁽²⁾ Recital 3 of the MFFR.

⁽³⁾ See Chapter 21.

⁽⁴⁾ For the years 2018–20 this adjustment is limited to the maximum amounts defined in Article 5, paragraph 2 of the MFFR.

⁽⁵⁾ See Chapter 6, point 4.4.

the period, due to a slower than expected start of programme implementation, the budget ran short of appropriations towards the end of the period when execution caught up. The automaticity of the adjustment of payment ceilings under the global margin for payments should ensure that the overall level of payment appropriations agreed for the 2014–20 MFF (EUR 908.4 billion in 2011 prices) will effectively remain available over the whole period.

Article 6 MFFR maintains the established practice for annual technical adjustments: each year, the Commission makes a technical adjustment to the financial framework for the next year. Its function is twofold:

- The financial framework attached to the MFFR is expressed at constant prices, so it has to be adjusted each year to take account of inflation in order to maintain the original purchasing power of the ceiling for each heading. This adjustment is based on a fixed deflator of 2 % a year, which means that the amounts in current prices can already be set for the entire duration of the financial framework.
- The 'margin available', expressed as a percentage of GNI, must be updated to take account of actual economic activity, on which the maximum volume of own resources available depends. At this point it is possible to check the compatibility between total appropriations for payments and available own resources.

From the procedural point of view, this technical adjustment is made prior to the start of the budgetary procedure for year n+1 on the basis of the most recent economic data and forecasts available.

In order to set the annual budgetary procedure in a stable framework and to ensure budgetary discipline, no further adjustments are made for the year concerned.

The annual technical adjustments will also provide the amounts calculated by the Commission which are available in the year of the adjustment (year n) under three newly created instruments: the global margin for payments, the global margin for commitments and the Contingency Margin. The availability of a global margin for payments will, in addition, result in an adjustment of the payment ceilings for year n and n-1.

Article 7 on the adjustment of cohesion policy envelopes considerably expands a provision introduced for the 2007–13 period ⁽¹⁾. It now potentially applies to all Member States, i.e. not only those which are subject to a capping of their global cohesion envelopes. All national allocations will be recalculated in 2016 on the basis of the then available most recent statistics. If the difference with the agreed envelopes exceeds +/-5 % (subject to a maximum adjustment of +/- EUR 4 billion), the allocations to Member States and the MFF ceilings for the years 2017–20 shall be adjusted accordingly, the latter in the framework of the technical adjustment for 2017. This provision has been introduced to take account of the situation of Member States most suffering from the post-2008 financial and economic crisis.

The widening of the scope of Article 8 compared with similar rules previously applicable to the Cohesion Fund reflects the considerably strengthened measures now linking the effectiveness

⁽¹⁾ See Point 17 of the Interinstitutional Agreement of 17 May 2006.

of all European Structural Investments Funds to sound economic governance ⁽¹⁾. In case of a suspension of commitments in the context of such measures, the Commission shall — upon lifting of the suspension — transfer the suspended commitments to the following years (and adjust the ceilings for sub-heading 1b accordingly). However, commitments whose suspension has not been lifted within $n+3$ years shall be lost.

2) *Special instruments*

The Chapter on special instruments of the MFFR defines the various instruments which can be mobilised, on a Commission proposal, by a joint decision of the European Parliament and the Council in order to make additional amounts available to the annual budget. When special instruments are mobilised, the corresponding amounts are entered into the budget ‘over and above the ceilings’, i.e. without a revision of the ceilings themselves which would require Council to act unanimously. The MFFR also establishes the maximum amounts of each of those instruments, whilst the procedure for mobilising them is laid down in the IIA.

Table 10.1 summarises the changes made by the MFFR to the four pre-existing flexibility instruments (Articles 9 to 12), namely:

- The Emergency Aid Reserve: Its purpose is to allow a rapid response to the specific aid requirements of third countries following events which could not be foreseen when the budget was established, first and foremost for humanitarian operations, but also for civil crisis management and protection, and situations of particular pressure resulting from migratory flows at the Union’s external borders where circumstances so require. Its creation dates back to the IIA of 29 October 1993;
- The European Union Solidarity Fund, which was set up in November 2002 by means of a separate Interinstitutional Agreement ⁽²⁾ before being integrated into the IIA of 17 May 2006. It allows for financial assistance in the event of major disasters occurring on the territory of a Member State or a candidate country. The procedure and criteria to be observed for receiving support are defined in a specific Regulation ⁽³⁾;
- The flexibility instrument, first introduced in the IIA of 6 May 1999. It allows the financing, for a given financial year, of clearly identified expenditure which could not be financed within the limits of the ceilings available for one or more headings. Its size has more than doubled with the MFFR, which has also increased the possibility to ‘roll over’ to future years amounts which have not been used in a given financial year. Unlike the other three instruments, the flexibility instrument is not limited to a particular category of expenditure;

⁽¹⁾ See: Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320), and in particular Article 23 thereof.

⁽²⁾ OJ C 283, 20.11.2002, p. 1.

⁽³⁾ Regulation (EU) No 661/2014 of the European Parliament and of the Council of 15 May 2014 amending Council Regulation (EC) No 2012/2002 of 11 November 2002 establishing the European Union Solidarity Fund.

- The European Globalisation Adjustment Fund, first established in the IIA of 17 May 2006. It may provide additional support for workers who suffer from the consequences of major structural changes in world trade patterns and to assist them with their reintegration into the labour market ⁽¹⁾.

The changes introduced by the MFFR concern both the maximum annual amounts set for each instrument and the extent to which those parts of the annual amounts, which have not been entered in the budget, can be used in the following financial year(s). If amounts from the previous year or years can be used, they increase the maximum amount available in the financial year concerned accordingly. Under the MFFR, the 'transfer' to the next year (n+1) of unused amounts of year n becomes, for the first time, possible for the Emergency Aid Reserve and the European Union Solidarity Fund. For the flexibility instrument, this possibility is extended from year n+2 to year n+3.

TABLE 10.1 – *Special (flexibility) instruments: Comparison between the provisions of the 2014–20 MFF Regulation and the 2007–13 IIA*

Special Instruments	2007–13 IIA Maximum annual amounts in 2011 prices (average) and the extent to which unused amounts can be used in the following years	2014–20 MFFR Maximum annual amounts in 2011 prices and the extent to which unused amounts can be used in the following years
Emergency Aid Reserve	EUR 254 million No 'transfer' to next year of unused amounts	EUR 280 million Amounts not used in year n are available up to year n+1
European Union Solidarity Fund	EUR 1 020 million No 'transfer' to next year of unused amounts. In exceptional cases, and if the remaining resources for the year in question are insufficient, the Commission may propose that additional amounts are financed from the annual amount for the following year.	EUR 500 million Amounts not used in year n are available up to year n+1 In exceptional cases, and if the remaining resources for the year in question are insufficient, the Commission may propose that additional amounts are financed from the annual amount for the following year.
Flexibility Instrument	EUR 204 million Amounts not used in year n are available up to year n+2	EUR 471 million Amounts not used in year n are available up to year n+3
European Globalisation Adjustment Fund	EUR 510 million No 'transfer' to next year of unused amounts	EUR 150 million No 'transfer' to next year of unused amounts

⁽¹⁾ See the related basic legislative act: Regulation (EU) No 1309/2013 of the European Parliament and of the Council of 17 December 2013 on the European Globalisation Adjustment Fund (2014–20) and repealing Regulation (EC) No 1927/2006 [OJ L 347, 20.12.2013, p. 855].

The MFFR introduces two new special instruments:

- The ‘Contingency Margin’ (Article 13 MFFR) allows for the mobilisation (as an instrument of last resort) of commitment and payment appropriations up to an equivalent of 0.03 % of the Union’s GNI ⁽¹⁾ in the framework of the annual budgetary procedure. The ceilings of the MFF are not adjusted, but any amounts mobilised by means of the Contingency Margin must be fully offset against margins available in the current or later years (i.e. those margins will *de facto* no longer be available in the budgetary procedures) so that the overall ceilings set for commitment and payment appropriations shall not be exceeded over the seven-year period of the MFF. The Contingency Margin replaces the provision of the IIA of 17 May 2006 allowing for the revision of the MFF up to 0.03 % of the EU GNI by qualified majority in Council. This provision was no longer applicable following the entry into force of the Lisbon Treaty ⁽²⁾.
- The ‘Global margin for commitments’ (Article 14 MFFR): Any margins left below the commitment ceilings for the years 2014 to 2017 will constitute a Global margin for commitments, which can be made available for growth and employment policy objectives, in particular youth employment, in the framework of the annual budgetary procedures for the years 2016 to 2020. The expectation is that this margin will allow for the prolongation of the Youth Employment Initiative, which was frontloaded to the years 2014–15.

The Chapter on special instruments also includes a provision (Article 16) relating to the financing of three large-scale projects: The European satellite navigation programmes (EGNOS and Galileo), the International Thermonuclear Experimental Reactor (ITER) and the European Earth Observation Programme (Copernicus). Given that the lifetime of those projects extends well beyond the period set for the MFF, and in order to shield other projects or programmes financed from the Union budget from potential cost overruns that the three large-scale projects may occasion, the MFFR sets maximum amounts for the period 2014–20 for the contribution from the budget to each of those projects. This provision imposes a particular level of budgetary discipline so as to manage costs within the maximum amounts set in the MFFR.

3) Revision

Chapter 3 of the MFFR on revision regroups all pre-existing provisions for revising the financial framework, adding the one relating to a possible reunification of Cyprus.

Any revision of the MFF amends the MFFR and, therefore, requires a unanimous decision by Council after having obtained the consent of the European Parliament. Any revision must comply with the own-resources ceiling set in the relevant Council Decision.

The MFFR (Articles 17 to 22) distinguishes six types of revisions:

- In the event of unforeseen circumstances, the MFF can be revised to put additional means at the disposal of the Union budget. As any revision must maintain an appropriate relationship between commitments and payments, it shall, in general, modify the ceilings for

⁽¹⁾ For 2014 this corresponds to an amount of slightly more than EUR 4 billion in current prices. See: Commission Communication on the Technical Adjustment of the financial framework for 2014 in line with movements in GNI: COM(2013) 928 final, 20.12.2013, p.4 (http://ec.europa.eu/budget/mff/lib/COM-2013-928/COM_2013_928_en.pdf).

⁽²⁾ See Chapter 6.3.

both commitment and payment appropriations. When examining a proposal for revision, institutions must assess the scope for reallocating expenditure between the programmes covered by the heading concerned, in particular in case an under-utilisation of funds can be identified in that heading. This aims at limiting, as far as possible, the amounts by which the ceilings need to be increased in order to finance the new expenditure planned. Similarly, institutions have to examine the scope for offsetting any raising of a ceiling by the lowering of another one.

- Revision related to implementation: when notifying the European Parliament and the Council of the technical adjustments to the MFF, the Commission may also present proposals for revising the level of payment appropriations in the light of implementation of the programmes, to ensure an orderly progression in relation to commitment appropriations.
- The MFFR has extended to the Asylum and Migration Fund and the Internal Security Fund the provisions introduced in the previous Interinstitutional Agreements in respect of delays in the adoption of the new rules or programmes for the Structural, Cohesion, Rural Development and Fisheries Funds. In the event that appropriations from these Funds cannot be used in 2014 due to such delays, the MFF can be revised, before 1 May 2015, so as to transfer those appropriations to subsequent years.
- The MFFR also renews the provision that the financial framework shall be revised should a Treaty revision with budgetary implications occur within the period covered by it ⁽¹⁾.
- Enlargement: In the event that one or more countries accede to the Union during the period covered by the financial framework, the MFF shall be revised accordingly, i.e. by taking account of the new expenditure requirements resulting from the Accession Treaty or Treaties ⁽²⁾.
- Should the reunification of Cyprus occur in the period covered by the MFF, it will be revised to take account of the additional financial needs resulting from it.

Also included under this Chapter of the MFFR is a provision on unity of the budget negotiated by the Parliament (covering the case whereby the Council would unanimously decide under Article 332 TFEU to incorporate expenditure related to enhanced cooperation into the budget), as well as the obligation for the Commission to present its proposals for the period post-2020 before 1 January 2018 (i.e. a full six months earlier than the previous proposals which were presented at the end of June 2011).

2.2. The Interinstitutional Agreement

Whilst the main provisions with respect to the MFF are now included in the Council Regulation (MFFR), the Interinstitutional Agreement of 2 December 2013 on budgetary discipline, on cooperation in budgetary matters and on sound financial management contains a number of

⁽¹⁾ It should be noted that the 2007–13 MFF was not revised following the entry into force of the Lisbon Treaty on 1 December 2009. New expenditure resulting from the Treaty, e.g. for the establishment of the European External Action Service, was made available within the existing headings and ceilings.

⁽²⁾ See Chapter 6, point 4.3, on how this was handled in the case of the accession of Croatia in 2013.

important additional provisions agreed between the institutions. It comprises three parts as well as an annex:

- Part I. MFF and special instruments
- Part II. Improvement of interinstitutional cooperation in budgetary matters
- Part III. Sound financial management of Union funds
- Annex: Interinstitutional cooperation during the budgetary procedure

Part I of the IIA includes a few general provisions concerning the MFF, notably the need to maintain sufficient margins under the ceilings during the budgetary procedure, as well as the procedures for mobilisation of the various special instruments established by the MFFR.

Part II of the IIA focuses on the improvement of the interinstitutional collaboration during the budgetary procedure. This part covers, *inter alia*:

- the interinstitutional collaboration procedure, the details of which are laid down in the annex;
- the incorporation of financial provisions in legislative acts: the main new part in this section consists of the additional flexibility with respect to the financial envelopes laid down in each of the legislative acts concerning a multiannual programme. In future deviations up to 10 % (rather than 5 %) over the lifetime of the programme are now possible;
- specific rules for expenditure relating to fisheries agreements;
- the budgetary procedure for mobilising the new Reserve for crises in the agricultural sector, which is included under Heading 2 of the MFF. The appropriations are to be entered directly into the budget, but any amount not used for crisis measures is to be reimbursed to direct payments;
- the budgetary provisions for the financing of the Common Foreign and Security Policy (CFSP);
- the provisions on involvement of the institutions as regards development policy issues and the European development Fund (EDF). They also refer to the Commission's intention to propose the integration of the EDF into the Union's budget as from 2021;
- cooperation of the institutions in the budgetary procedure on administrative expenditure: This includes, *inter alia*, an agreement between the institutions on how to implement the progressive reduction of 5 % in staff.

Part III of the IIA on sound financial management of Union funds contains provisions on:

- information to be provided by the Commission to other institutions on Union funds spent through international organisations;
- the content of the evaluation report on the Union's finances to be submitted each year by the Commission in accordance with Article 318 TFEU;
- financial programming: the Commission needs to submit twice a year a complete financial programming for all headings except Sub-heading 1b and Headings 5 and 6; it shall identify the legislation in force and pending legislative proposals;

- the budgetary cooperation procedure accompanying the legislative process for the creation of a new agency or European school.

3. The implications of the financial framework

3.1. For the annual budget debate

The multiannual financial framework currently in force does not call into question the other basic provisions of the Treaty. The principle of annuality remains fully applicable. Budget appropriations are authorised and implemented on an annual basis. The ceilings set are annual limits on expenditure. Amounts not entered in the budget or not used for a particular year cannot be used in excess of the ceilings set for subsequent years without prejudice to the global margin for payments and special instruments provided for in the MFF Regulation ⁽¹⁾.

The financial framework has, however, resulted in substantial changes in the budget debate. Establishing a multiannual financial framework implies holding regular detailed discussions on the broad lines of the Union's finances: the volume of the budget, the methods of financing and a shared political assessment of the priorities to be pursued.

Longer-term financial decisions are taken outside the annual budgetary procedure, in the form of a joint decision by the European Parliament and the Council. Community budget policy becomes more predictable, which leads to greater security for defining and implementing the various Community activities and allows Member States to manage their own national budget planning better in relation to the trends in Community expenditure.

This means that the annual discussion on the budget can focus more on the necessary political negotiations and on effective allocation of available resources between various Union operations, taking account of the results achieved in relation to the objectives pursued.

3.2. For budgetary management

The corollary of setting a ceiling on expenditure for the medium term endows the Community with resources ensuring compatibility at all times between current or new operations and the financial framework laid down.

1) *The provisions*

Article 310 of the TFEU provides that 'With a view to maintaining budgetary discipline, the Union shall not adopt any act which is likely to have appreciable implications for the budget without providing the assurance that the expenditure arising from such an act is capable of being financed within the limit of the Union's own resources and in compliance with the multi-annual financial framework'.

Point 8 of the Interinstitutional Agreement provides that 'the institutions shall, for the purposes of sound financial management, ensure as far as possible during the budgetary procedure (...) that sufficient margins are left available beneath the ceilings for the various headings'. This

⁽¹⁾ See Section 2.1 above.

margin should allow supplementary appropriations to be entered as needed without having to revise the financial framework each time.

2) Financial planning of expenditure

The Commission must be in a position to know, at all times, the envisaged medium-term trend in expenditure regarding all Community operations, in order to be able to assess its compatibility with the financial framework laid down. To this end, rules were introduced on medium-term financial programming, starting in January 1991. More recently, point 30 of the IIA clearly defines how the financial programming is to be established by the Commission and transmitted to the budgetary authority.

Accordingly, a complete financial programming is submitted twice a year, once with the documents accompanying the draft budget, and once following the adoption of the annual budget. The headings concerned are Heading 1 (except the sub-heading for Economic, social and territorial cohesion), Heading 2 (for environment and fisheries only) and Headings 3 and 4. The details to be provided, by heading, policy area and budget line, are as follows:

- for multiannual programmes, the procedure under which they were adopted, their duration, the total financial envelope and the share allocated to administrative expenditure;
- multiannual estimates for all annual action (pilot projects, preparatory actions, agencies, prerogatives), and an indication of the margins left under the different expenditure ceilings of the financial framework.

The Commission is also asked to provide a financial programming for pending legislative proposals, with the latest updates.

As the majority of the multiannual programmes under the current financial framework cover the period 2014–20, the financial programming tables are established for the same period, thus enabling both the Commission and the budgetary authority to assess the implications in the short and medium term of any decisions with financial consequences with regard to the expenditure ceilings. The financial programming provides guidance but does not pre-empt options to be taken in the course of the annual budget procedure.

In addition, the financial programming is the instrument for projecting and verifying compliance with the financial envelopes of multiannual programmes throughout the duration of the programmes.

Apart from testing the consistency between the envisaged trend in expenditure and the ceilings laid down, this instrument performs two other functions:

- It makes authorising departments take a more systematic approach to medium-term, objective-based management, based on cost-effectiveness and regular evaluation of programmes;
- When the period covered by the financial framework comes to an end, the Commission is able to base its proposals for renewal of the framework on a reasoned, relatively detailed estimate of the requirements to be covered.

Part 3
Establishment of the Union's annual budget



Chapter 11

The general principles governing the Union's budget

1. The principle of unity

1.1. Definition of the principle of unity

The principle of unity of the Union budget stems from Article 310(1) TFEU which lays down that: 'All items of revenue and expenditure of the Union shall be included in estimates to be drawn up for each financial year and shall be shown in the budget.'

The principle of unity makes the budget the vehicle of all expenditure and all revenue. All Union revenue and expenditure should be incorporated in a single budget document. The principle is confirmed in Article 2 (c) of the Financial Regulation (FR) which defines the budget as 'the instrument which, for each financial year, forecasts and authorises all revenue and expenditure considered necessary for the Union'.

The unity of the budget means that it is clear what expenditure and revenue are authorised: only the revenue and expenditure included in the budget are authorised.

1.2. Application of the principle of unity in the budget

In practice, the principle of unity is not applied in full.

In the early years of the Communities ⁽¹⁾, the autonomy of the Community institutions set up under the ECSC, and subsequently under the EEC and Euratom, meant that as many as five budgets could exist at any one time.

Since 1971, when the Treaty of Luxembourg of 22 April 1970 entered into force, the main financial activities of the Community institutions have been incorporated into a single document, the general budget of the European Communities.

Under Article 7 FR, the budget shall comprise:

- the revenue and expenditure of the Union, including administrative expenditure occasioned for the institutions by the provisions of the TEU relating to the common foreign and security policy, and the operational expenditure occasioned by implementation of those provisions where this is charged to the budget; and
- the revenue and expenditure of the European Atomic Energy Community.

In addition, the budget must record the guarantee for borrowing-and-lending operations entered into by the Union ⁽²⁾, including the European Financial Stability Mechanism and Balance of Payment Facility operations ⁽³⁾.

⁽¹⁾ See Chapter 1.

⁽²⁾ See Chapter 18.

⁽³⁾ See Chapter 21.

1.3. Exceptions to the principle of unity

Financial activities and operations not incorporated in the general budget currently include:

- borrowing-and-lending operations, although the general budget contains the guarantee for the Union's borrowing-and-lending operations ⁽¹⁾;
- the European Development Fund ⁽²⁾;
- the financial activities of the European Investment Bank ⁽³⁾.

1.4. The special case of the common foreign and security policy ⁽⁴⁾

The common foreign and security policy (CFSP), the former second 'pillar' of the European Union, is not fully incorporated into the general budget.

Article 41(1) of the TEU provides that only the administrative expenditure is charged to the budget of the Union. This principle is reflected in Article 7(1)(a) FR.

Article 41(2) of the TEU provides for operating expenditure on the CFSP also to be charged to the budget, except for such expenditure arising from operations having military or defence implications and cases where the Council unanimously decides otherwise.

Expenditure which is not charged to the budget of the Union is charged to the Member States in accordance with the gross national product (GNP) scale, unless the Council unanimously decides otherwise. Some Member States (which have been given the right to opt out) are under no obligation to contribute to financing expenditure arising from operations with military or defence implications.

Whenever expenditure is charged to the general budget, the normal budgetary procedure applies.

2. The principle of accuracy

2.1. Definition of the principle of accuracy

The principle of accuracy basically means that the Union will not spend more than is necessary. This principle is defined in different ways (in Article 8 FR):

- 'no revenue shall be collected and no expenditure effected unless booked to a line in the budget;
- no expenditure may be committed or authorised in excess of the authorised appropriations;
- an appropriation may be entered in the budget only if it is for an item of expenditure considered necessary'.

⁽¹⁾ See Chapter 18.

⁽²⁾ See Chapter 22.

⁽³⁾ See Chapter 20.

⁽⁴⁾ See Chapter 7.

2.2. The specific case of interest generated by the funds which are the property of the Union

With the 2012 revision of the FR, the rules governing interest generated by pre-financing payments were considerably simplified. In view to the objective of reducing the administrative burden both for the recipients of Union funds and the Commission services and having regard to the principle of sound financial management, the obligation to generate interest on pre-financing payments and to recover such interest has been removed.

Thus, by way of principle, interest generated by pre-financing payments made from the Union budget shall no longer be due to the Union (Article 8(4) FR).

The only exception to this rule constitutes the delegation agreements under indirect management. In accordance with Article 8(4), the possibility remains to include such an obligation in a delegation agreement concluded with third countries or bodies designated by them in order to allow the reuse of interest generated by pre-financing payments for the following ends:

- the reuse of the generated interest for the action;
- the deduction of the generated interest from payment requests, or
- the recovery of the generated interest.

In the cases where such obligation to generate and recover the interest yielded on pre-financing is provided for in the delegation agreement, the accounting for the corresponding amounts shall follow the rules of Article 2 of the RAP.

3. The principle of universality

3.1. Definition of the principle of universality

The principle of universality is a corollary of the principle of unity. It does not stem directly from the Treaties, but from Article 20 FR, which states that:

‘Total revenue shall cover total payment appropriations ... All revenue and expenditure shall be entered in full [in the budget and in the accounts] without any adjustment against each other.’

In line with this principle, budget revenue may not be assigned to specific items of expenditure (non-assignment rule) and revenue and expenditure may not be set off against each other (gross budget rule). Consequently, revenue is pooled and used without distinction to finance all expenditure.

This principle supplements the unity principle by ensuring that budgetary authorisation for a given item of expenditure does not depend on the amount of a given item of revenue, which would restrict the scope of such authorisation and split the budget into watertight segments.

The non-assignment rule was enshrined in the Council Decision of 21 April 1970 creating own resources and was confirmed by subsequent decisions. In particular, Article 6 of the Own Resource Decision of 7 June 2007 as well as the forthcoming one adopted in 2014 ⁽¹⁾ states:

⁽¹⁾ See Chapter 9.

'The revenue ... shall be used without distinction to finance all expenditure entered in the ... budget'.

3.2. Exceptions to the non-assignment rule

However, Article 21 FR makes an exception to the non-assignment rule by providing a list of cases where the revenue shall be used to finance specific items of expenditure.

The FR makes a distinction between the external and the internal assigned revenue.

The following constitute external assigned revenue:

- financial contributions from Member States to certain research programmes pursuant to the Council Regulation implementing the Decision on the system of the Communities' own resources; the reason for this is because not all Member States take part in the programmes concerned;
- financial contributions from Member States and third countries, including in both cases their public agencies, entities or natural persons, to certain external aid projects or programmes financed by the Union and managed by the Commission on their behalf;
- interest on deposits and the fines provided for in the Regulation on speeding up and clarifying the implementation of the excessive deficit procedure;
- revenue earmarked for a specific purpose, such as income from foundations, subsidies, gifts and bequests, including the earmarked revenue specific to each institution;
- financial contributions to Union activities from third countries or from non-Union bodies;
- revenue generated by the Research Fund for Coal and Steel;
- revenue generated by the activities of the Joint Research Centre;
- internal assigned revenue ancillary to any of the above.

The following constitute internal assigned revenue:

- revenue from third parties in respect of goods, services or work supplied at their request;
- proceeds from the sale of vehicles, equipment, installations, materials and scientific and technical apparatus which are being replaced or scrapped when the book value is fully depreciated;
- revenues arising from the repayment of amounts wrongly paid;
- proceeds from the supply of goods, services and works for other departments within an institution, institutions or bodies, including refunds by other institutions or bodies of mission allowances paid on their behalf;
- insurance payments received;
- revenue from payments connected with lettings;
- revenue from the sale of publications and films, including those on an electronic medium;

- repayments to financial instruments;
- revenue arising from reimbursement of taxes by third countries.

Moreover, the basic act adopted by the legislative authority laying down the basis for a Union programme may also assign the revenue for which it provides to specific items of expenditure (Article 21(4) FR). Unless otherwise provided, such revenue shall constitute internal assigned revenue.

The abovementioned contributions to Union activities from third countries include, for example, the contribution by the European Free Trade Association (EFTA) countries to financing certain Union policies, such as the research programmes in which they participate. Their participation began with the establishment of the European Economic Area in 1994.

Their contributions are calculated by applying a 'proportionality factor', based on the ratio between the GDP of the Member States of the Union and that of the EFTA member countries, and are allocated to the budget items concerned. These contributions and the expenditure they finance are not included in the budget and appear in an Annex to the budget 'for information' only.

The same rule also applies to participation by the candidate countries in certain Union programmes as part of the pre-accession strategies. Their contributions are defined on a case-by-case basis in the association councils and allocated to the budget headings concerned.

3.3. Exceptions to the gross budget rule

Article 23 FR makes the following exceptions to the gross budget rule:

- The following deductions may be made from payment requests which will then be passed for payment of the net amount: penalties imposed on parties to procurement contracts or beneficiaries of a grant; discounts, refunds and rebates on individual invoices and payment requests; interests generated by pre-financing payments and adjustments for amounts unduly paid.
- Moreover, the cost of products or services provided to the Union incorporating taxes refunded by the Member States pursuant to the Protocol on the Privileges and Immunities of the European Union or by third countries on the basis of the relevant agreements will be charged to the budget for the ex-tax amount.
- Lastly, adjustments may be made in respect of exchange differences occurring in the implementation of the budget; the final balance will be included in the balance for the year.

All these exceptions are of a technical nature and are intended to simplify procedures.

3.4. The special case of negative revenue

The budget may not contain negative revenue (Article 45 FR). The own resources paid under the Council Decision on the system of own resources of the European Union must be net amounts and must be shown as such in the summary statement of revenue in the budget.

Nevertheless, Member States retain some amounts as collection costs for traditional own resources ⁽¹⁾. From 1971 to 1987, these amounts were entered in the accounts as budgetary expenditure. From 1988 until 2002, the collection costs were entered as 'negative revenue' in the Community budget. From 2003 on, only the net amounts of the traditional own resources are indicated and the collection costs as such are no longer mentioned in the budget.

4. The principle of annuality

The principle of annuality requires budget operations to relate to a specific financial year. This makes it easier to monitor the activities of the Union executive.

It is defined by the TFEU from two angles:

- As regards estimates: 'All items of revenue and expenditure of the Union shall be included in estimates to be drawn up for each financial year' (first paragraph of Article 310 of the TFEU);
- As regards implementation: 'The expenditure shown in the budget shall be authorised for the annual budgetary period in accordance with [the Financial Regulation]' (second paragraph of Article 310 TFEU); 'The appropriations entered in the budget shall be authorised for a financial year which shall run from 1 January to 31 December' (Article 9 FR);

The financial year (twelve-month period) coincides with the calendar year as specifically provided for in Article 313 TFEU and Article 9 FR.

Annuality is thus intended to guarantee the order and discipline necessary at the forecasting and authorisation stage (involving both the Commission, which is responsible for presenting the draft budget, and the European Parliament and the Council, which are responsible for its adoption) and at the execution stage; it is incumbent on each institution in respect of its section of the budget. All those involved in the execution of the budget must therefore comply with the principle.

However, the principle of annuality, as applied to the availability and utilisation of commitment and payment appropriations, does not prevent commitments against differentiated appropriations from remaining valid for longer than one financial year (see point 4.1 below).

4.1. Annuality and differentiated appropriations

The Union budget, like any public authority budget, has to reconcile the principle of annuality with the need to engage in multiannual operations, which means that commitments have to be entered for a longer period than the financial year in which they are made.

1) Differentiated appropriations

The answer to this twin requirement is to enter differentiated appropriations, which consist of commitment appropriations and payment appropriations. This distinction goes back to Article 176(1) of the Euratom Treaty and is widely applied by Article 10 FR.

⁽¹⁾ See Chapters 9 and 13.

- (1) Commitment appropriations cover the total cost of the legal commitments entered into, in principle, during the current financial year.
- (2) Payment appropriations cover payments made to honour the legal commitments entered into in the current financial year and/or earlier financial years.

In current budgetary practice, administrative expenditure (Articles 201–203 FR), most European Agricultural Guarantee Fund expenditure (Article 169 FR) and loan guarantees, for example, are entered in the budget in the form of non-differentiated appropriations (the other categories of expenditure are made up of differentiated appropriations). The terms ‘appropriations for commitments’/‘appropriations for payments’ are used when differentiated and non-differentiated commitment/payment appropriations are added together.

It must be stressed that the existence of differentiated appropriations does not constitute an exception to the principle of annuality. Commitment appropriations as such are authorised for one year under the annual budgetary procedure. It is simply the payments for the operations covered by these commitments which may be extended over a number of financial years, the payment appropriations themselves being subject to budget authorisation each year. This dual annual authorisation of commitment and payment appropriations is a unique feature of the Union budget.

2) The gap between ‘commitment appropriations’ and ‘payment appropriations’ (concept of ‘commitments outstanding’)

The introduction of the concept of differentiated appropriations automatically opened up a ‘gap’ between commitments entered into and payments made: this gap is the result of the time lag between when the commitments are entered into and when the corresponding payments are made. The sum of appropriations committed but not yet paid is called ‘commitments outstanding’ (often referred to by the French acronym RAL). Outstanding commitments have grown steadily in recent decades as Union policies and the multiannual operations carried out to implement them have developed. However, the situation needs to be assessed for each policy area individually, to take into account the specificity of each area of expenditure. For instance, the rules applicable to the structural funds explicitly take account of the time lag between commitments and payments: under the 2014–20 programming period, automatic decommitments will be made after a period of three years (under the so-called ‘n+3’ rule), if the Member State concerned does not send sufficient payment claims against outstanding commitments.

The level of outstanding commitments is to a certain extent affected by the difficulties sometimes encountered in clearing commitments. Any delay in conclusion of legal commitments (contracts, grant agreements, etc.) between the Union and the recipients of Union funding, as is often the case in the Union’s external activities, or in implementation of such legal commitments or payment of the balance of Union funding (where it is contested, for example) has the effect of stretching the time lag between commitments and payments and, hence, increasing the amount of commitments outstanding. Outstanding commitments can therefore be said to include a normal component linked to the system of differentiated appropriations and an abnormal component linked to problems with implementing some multiannual activities.

The level of outstanding commitments is important since it constitutes a liability for the Union budget and, hence, a medium-term constraint on the payment appropriations needed to honour this debt. The European Parliament and the Council on one side and the Commission on the other, the latter being responsible for implementing the budget, are therefore gradually developing measures and tools to control the level of outstanding commitments. A key factor, in this regard, is to agree, in the annual budget procedure, on a sufficient level of payment appropriations to cover payment obligations for the year.

The Council Decision on own resources requires commitment appropriations entered in the budget to follow an orderly progression and a strict relationship to be maintained between commitment and payment appropriations to guarantee their compatibility and to enable the own-resources ceiling to be respected in subsequent years.

Likewise, successive revisions of the FR have laid down strict rules on deadlines for implementing multiannual projects.

- Article 86(5) FR stipulates that the legal commitments entered into for more than one financial year must set a final date for implementation (FDI) which must be specified to the recipient when the Union funding is granted. The FDI constitutes the deadline for payments to be executed from a budgetary commitment.
- Similarly, as a rule, appropriations which have not been used by the end of the financial year for which they were entered are cancelled (Article 13(1) FR).

4.2. Adjustments to the principle of annuality

The principle of annuality is generally respected. Pursuant to the Treaty, however, the FR lays down a number of exceptions, or rather technical adjustments, to ensure more flexible budget management. The policy of tighter budgetary discipline and more transparent management of appropriations has, nonetheless, very much restricted the application of these exceptions.

1) *Carry-overs*

Because of management constraints, use of appropriations cannot always be made to coincide with the calendar year. Article 316 TFEU therefore allows the pragmatic solution of authorising carry-overs, except, however, in the case of expenditure on staff.

Articles 13 and 14 FR foresee that some appropriations of the financial year which have not been used at the end of that year may be carried over to the next year, as an exception to the principle of annuality:

- Automatic carry-overs (without the need of a Commission decision):
 - Non-differentiated appropriations corresponding to obligations duly contracted at the close of the financial year will be carried over automatically to the following financial year only.
- Non-automatic carry-overs (subject to a Commission decision):
 - Differentiated commitment appropriations and non-differentiated appropriations not yet committed at the close of the financial year may be carried over in respect of

amounts corresponding to commitment appropriations for which most of the preparatory stages of the commitment procedure have been completed by 31 December — these amounts may then be committed up to 31 March of the following year (Article 13(2)(a) FR) or amounts which are necessary when the legislative authority has adopted a basic act in the final quarter of the financial year and the Commission has been unable to commit the appropriations provided for this purpose by 31 December (Article 13(2)(b) FR).

- Non-differentiated appropriations for building projects not yet committed at the close of the financial year may be carried over to the following year provided most of the preparatory stages of the commitment procedure have been completed by 31 December. The budgetary and legal commitments must then be executed by 31 December of the following year (Article 13(2)(a) FR).
- Payment appropriations may be carried over in respect of amounts needed to cover existing commitments or commitments linked to commitment appropriations carried over, when the appropriations provided for the relevant lines in the budget for the following financial year do not cover requirements. The institution concerned must first use the appropriations authorised for the current financial year and must not use the appropriations carried over until the former are exhausted (Article 13(3) FR).

Requests for carry-overs of this type must be duly substantiated. The institution concerned must take the decision by 15 February of year n+1 at the latest (Article 13(1) FR).

— Carry-over rules for assigned revenue:

- The external assigned revenue within the meaning of Article 21(2) FR is carried over automatically until all the operations relating to the programme or action to which it is assigned have been carried out. The external assigned revenue received during the last year of the programme or action may be used in the first year of the succeeding programme or action.
- The internal assigned revenue within the meaning of Article 21(3) FR shall be carried over for one year only, with the exception of revenue from lettings which can be carried over automatically, and commitment appropriations arising from repayments of pre-financing payments in the framework of shared management which may be carried over until the closure of the programme in accordance with Article 177(4) FR.

— Further carry-over rules for projects financed under the Connecting Europe Facility and for the Emergency Aid Reserve.

In September 2013, the Commission adopted a proposal for a Regulation amending the FR in order to take into account the outcome of the negotiations on the multiannual financial framework for the years 2014–20 on the carry-over rules for the Emergency Aid Reserve and for projects financed under the Connecting Europe Facility ⁽¹⁾.

(1) COM(2013) 639 final of 20.09.2013.

On that basis, Parliament and Council agreed inter alia. the following modifications of the FR ⁽¹⁾:

- As regards Emergency Aid Reserve, Article 13 was revised in order to provide for the carry-over to year n+1 of the appropriations placed in reserve and not used in year n, in line with Article 9(2) of the MFF Regulation.
- As regards the projects financed under the Connecting Europe Facility, a new Article 178a was introduced to allow for carry-over to the following financial year of commitment appropriations not used at the end of the financial year 2014, 2015 and 2016.
- The carry-over will be subject to the approval by the European Parliament and Council similar to the approval procedure for transfers set out in Article 27 of the Financial Regulation, but without the possibility to reduce the proposed amount for carry-over for the European Parliament and Council. In this procedure the Council needs a qualified majority to reject the proposed carry-over.

2) Budgetary commitment broken into annual instalments

By way of exception from the principle of annuality, in accordance with Article 85(4) FR, budgetary commitments for actions extending over more than one financial year may be broken down over several years into annual instalments only where the basic act so provides or where they relate to administrative expenditure.

3) Additional periods

'Additional periods' means either an ad hoc extension of the financial year beyond the 12 months of the calendar year or an anticipation of the financial year.

At present, the general budget includes two types of additional periods:

- (1) entry in the accounts for the EAGF: because of the time needed at Union level to process the information supplied by the Member States, entry of EAGF expenditure in the accounts may be extended by one month into year n+1 (Article 172 FR);
- (2) commitments of appropriations or payment in advance.

In accordance with Article 202 FR, from 15 October each year, routine administrative expenditure may be committed in advance against the appropriations provided for the following financial year. For routine management expenditure for the EAGF, the trigger date is 15 November (Article 170(3) FR). Such commitments may not, however, exceed one quarter (for administrative expenditure) and three quarters (for EAGF expenditure) of the appropriations decided by the European Parliament and the Council on the corresponding budget line for the current financial year. For administrative expenditure, they may not apply to new expenditure of a kind not yet approved in principle in the last budget duly adopted, whereas for EAGF expenditure they may apply only to expenditure for which the principle is laid down in an existing basic act.

⁽¹⁾ Article 178a, Carry-over of commitment appropriations for the Connecting Europe Facility. REGULATION (EU, Euratom) No 547/2014 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 15 May 2014 amending Regulation (EU, Euratom) No 966/2012 on the financial rules applicable to the general budget of the Union.

Expenditure which must be paid in advance pursuant to legal or contractual provisions, for example rents, may give rise to payments from 1 December onwards to be charged to the appropriations for the following financial year (Article 202(2) FR).

3) Making appropriations available again

Where amounts are decommitted as a result of total or partial non-implementation of the actions for which they were earmarked, in any financial year after that in which the appropriations were entered in the budget, the appropriations concerned will be cancelled (Article 15 FR).

However, two possible ways of making appropriations available again are authorised by the FR:

- Under Article 178 FR and the specific Regulations governing the European Structural and Investment Funds (European Regional Development Fund, European Social Fund, Cohesion Fund, European Maritime and Fisheries Fund, European Agricultural Fund for Rural Development) and Funds in the area of freedom, security and justice managed in shared management, the Commission will automatically decommit appropriations that have been committed in accordance with Article 175 FR and the specific Regulations mentioned above. The decommitted appropriations may be made available again in the event of a manifest error attributable solely to the Commission. To this end, the Commission will examine decommitments made during the previous financial year and decide, by 15 February of the current year, on the basis of requirements, whether it is necessary to make the corresponding appropriations available again.
- Article 182 FR allows making decommitted amounts available again in the field of research, exceptionally and in duly justified cases, where it is essential to carry out the programme originally planned.

4.3. Implications of annuality for revenue

The various decisions on own resources have established the principle that own resources are allocated to the Union to finance its budget. Any surplus of revenue over total expenditure during a year is carried over to the following year.

Article 11(1) FR also states that the revenue of a financial year is entered in the accounts for the financial year on the basis of the amounts collected during the financial year.

These provisions demonstrate the legislator's clear intention to apply the principle of annuality as strictly as possible to revenue. Budgetary implementation of the statement of revenue is therefore based on the principle of the 'cash budget': only the amounts collected between 1 January and 31 December are entered in the accounts.

As a result, the annual implementation of the budget will produce a balance at the end of the financial year consisting of the difference between the revenue actually collected and the payments actually made (see details given on the principle of budgetary equilibrium).

Article 11 FR and Article 10(3) of Regulation 1150/2000 of 22 May 2000, as last amended by Regulation 105/2009 of 26 January 2009, provide for two cases where this strict annuality of revenue may be relaxed:

- (1) Advance payments made in December of the preceding financial year in respect of traditional own resources for January are not entered in the accounts for that year in accordance with the usual 'cash budget' principle. Instead, they are entered for the year in which payment should normally have been made;
- (2) Any readjustments of the twelfths paid in respect of the VAT and GNI resources, the correction granted to the United Kingdom for budgetary imbalances and other correction mechanisms made in the course of the financial year, following adoption of an amending budget affecting those resources, are also booked to the year to which they relate.

4.4. Annuality and multiannual financial framework

Since 1988, under the Interinstitutional Agreement renewed in 1993, 1999 and 2006 and, following the entry into force of the Lisbon Treaty, the MFF Regulation adopted in 2013 pursuant to Article 312 TFEU, the budget of each financial year must be placed within the multiannual financial framework ⁽¹⁾. This mechanism cannot be considered to conflict with the principle of budget annuality.

The multiannual financial framework sets expenditure 'ceilings' for each broad category of expenditure ('heading') over a period of no less than 5 years. The current MFF covers seven years: from 2014 to 2020.

The MFF sets the annual maximum amounts for commitment appropriations for each heading and fixes an overall annual ceiling on payment appropriations. The amounts appearing in the MFF do not therefore constitute expenditure authorisations, which are determined in the budget adopted annually. However, the MFF provides a framework for financial programming and budgetary discipline, ensuring that EU spending is predictable. It also allows the EU to carry out common policies over a period that is long enough to make them effective. By defining how much and in which areas the EU should be able to invest over seven years, the MFF is an expression of political priorities as much as a budgetary planning tool. The annual budget is adopted within this framework.

The annual ceilings apply to each financial year and may not be aggregated over the period. The calendar year, which is the same as the financial year, is therefore clearly the basic unit of time used for the multiannual financial framework.

The rules governing the structure and the functioning of the overall mechanism of the MFF are laid down in the MFFR and the accompanying Interinstitutional Agreement ⁽²⁾.

5. The principle of equilibrium

The principle of equilibrium means that budget revenue must equal budget expenditure. This rule is enshrined in the first paragraph of Article 310 TFEU which states that 'the revenue and expenditure shown in the budget shall be in balance'. It was incorporated in the successive

⁽¹⁾ See Part I and Part II, Chapter 8.

⁽²⁾ See Chapter 10.

own-resources decisions and in the FR (Article 17). The Union, unlike its Member States, is not allowed to borrow to cover its expenditure and cannot raise loans within the framework of the budget. The only exception to this rule are the building acquisition projects which may be financed through loans in accordance with Article 203(8) FR. This possibility to raise loans is without prejudice to the principle of equilibrium.

5.1. Achievement of budgetary equilibrium

For technical reasons, it is inevitable that there will be differences between the forecasts made at the authorisation stage and the final outturn. A distinction should be drawn between:

- the authorisation stage: the equilibrium principle is strictly applied, both formally and mathematically, when the budget is established, i.e. at the estimates and authorisation stage. In the budget finally adopted, revenue and payment appropriations have to be in balance (Article 17 FR);
- the implementation stage: the balance from the financial year, however, will inevitably diverge from the estimates on both the revenue and the expenditure sides. The revenue may in practice be either higher or lower than forecast. Since the appropriations authorised are absolute ceilings which, on no account, may be exceeded, actual expenditure will have to be below the estimates (or at best — which would be very rare — exactly the same as the estimates).

The revenue and expenditure account, which shows the end-of-year results, provides a comparison between estimates and outturn. The Union must, nonetheless, do all it can to ensure that the balance also complies with the equilibrium principle. Corrections are therefore sometimes necessary during the year, involving either management measures or, if it is essential to alter the amounts authorised, adoption of an amending budget (Article 41 FR).

5.2. Concept of budget balance

1) Definition of the balance

The balance for a given financial year consists of the difference between all the revenue collected in respect of that financial year and the amount of payments made against appropriations for that financial year, plus the amount of the appropriations for the same financial year carried over and taking account of possible exchange rate differences.

On the one side, the net amount of appropriations carried over from previous financial years which have been cancelled is added to this difference and, on the other, payments made in excess of non-differentiated appropriations carried over from the previous financial year as a result of variations in euro rates and the balance resulting from exchange gains and losses during the financial year are subtracted from it (Article 15 of Regulation (EC, Euratom) No 1150/2000, as last amended by Regulation (EC, Euratom) No 105/2009, implementing the decision on own resources).

2) Practical application

The balance from each financial year will be entered in the budget for the following financial year as revenue in the case of a surplus or as a payment appropriation in the case of a deficit (Article 18(1) FR).

The estimates of such revenue or payment appropriations will be entered in the budget during the budgetary procedure and in a letter of amendment (Article 18(2) FR).

Moreover, after presentation of the accounts for each financial year, any discrepancy with the estimates must be entered in the budget for the following financial year through an amending budget devoted solely to that discrepancy. In such a case, the draft amending budget must be submitted by the Commission within 15 days following the submission of the provisional accounts (Article 18(3) FR).

Headings with token entries are accordingly included in the statement of revenue and in the statement of expenditure to accommodate the balance ('surplus available from the preceding financial year' or 'deficit carried over from previous year').

In practice, two situations are possible:

- Positive balance (surplus): this is the normal situation, where the revenue outturn (resources collected) covered all expenditure requirements on the basis of the rules applicable (in particular, coverage of carry-overs). In this case, the surplus is carried forward to the following year, where it is entered on the revenue side. The FR provides for early entry in the budget for year *n* of the probable balance for year *n-1*, with the final adjustment being made after the closure of the accounts for year *n-1* through an amending budget;
- Negative balance (deficit): this is more of an exception (the last case was in 1986). However, the revenue outturn might prove to be less than the amount necessary to cover requirements determined in accordance with the rules applicable. When a deficit is recorded, a corresponding amount must be entered on the expenditure side of the following year's budget, by a procedure similar to that described in the event of a surplus.

5.3. Negative reserve

Under Article 47 FR, the Commission section of the budget may include a 'negative reserve' limited to a maximum amount of EUR 200 million. A 'negative reserve' mechanism has helped, albeit indirectly, to keep the budget in balance, even though it really amounts to a failure to achieve such a balance. This mechanism consists of financing new expenditure by assuming that savings will be made somewhere in the budget during the financial year, without it being possible to identify which items will generate these savings when the budget is adopted. A negative amount is therefore included in the budget which must be covered during the year by transfers from headings which are in surplus.

The negative reserve first appeared in the 1986 budget as a way of securing agreement between the European Parliament and the Council on the rate of increase for non-compulsory expenditure. Appropriations not used (i.e. savings made) were transferred to this negative reserve. The concept of 'negative reserve' was formally enshrined for the first time in the

revision of the FR dated 24 June 1988, with the maximum amount limited to ECU 200 million. Since the 2012 revision of the FR, the negative reserve is limited to payment appropriations only, for a maximum amount of EUR 200 million.

6. The principle of specification

6.1. The principle of specification

The principle of specification of expenditure is enshrined in Article 316 TFEU. It means that each appropriation must have a given purpose and be assigned to a specific objective in order to prevent any confusion between appropriations, at both the authorisation and execution stages, and thus to ensure that:

- the budget established is completely unambiguous;
- it is executed in accordance with the wishes of the European Parliament and the Council.

The principle of specification also applies to revenue and requires the various sources of revenue paid into the budget to be clearly identified. Articles 44 and 49 FR, which deal with the structure and presentation of the budget, describe very precisely how this principle is to be implemented.

6.2. Specification and structure of the budget

The principle of specification determines both the horizontal and the vertical structure of the budget.

1) *The horizontal structure of the budget*

The budget is divided into:

- a general statement of revenue;
- sections, subdivided into statements of revenue and of expenditure, for each institution: the European Parliament (Section I), the European Council and Council (Section II), the Commission (Section III, including Annexes on OLAF, the Publications Office), the Court of Justice (Section IV), the Court of Auditors (Section V), the European Economic and Social Committee (Section VI), the Committee of the Regions (Section VII), the European Ombudsman (Section VIII), the European Data Protection Supervisor (Section IX) and the European External Action Service (Section X);
- in addition, Section III (Commission), which accounts for 95 % of expenditure, is organised under titles corresponding to the Commission's policy areas. Each title is, in turn, subdivided into chapters, of which the first (01) includes all administrative appropriations for the policy area in question and the other ones correspond to the related operational activities. A general summary of administrative appropriations allocated to policy areas is also included. Finally, the budget includes a number of annexes with additional information on specific issues;
- the Commission Section of the budget (Section III) also covers the expenditure for pensions and European schools, which is common to all institutions.

2) *The vertical structure of the budget: the budget nomenclature*

Under the Activity Based Budgeting nomenclature, revenue and expenditure are classified according to their type or the use to which they are put under titles, chapters, articles and items (Article 41 FR). Under Article 8 FR ‘no revenue shall be collected and no expenditure effected unless booked to a line in the budget’.

The article is therefore the slot to accommodate revenue and expenditure, while the real organisation by specific area, which the European Parliament and the Council are responsible for determining, is at the level of chapters. As a rule, only the European Parliament and the Council may make decisions on transfers between chapters.

The nomenclature is determined during the budgetary procedure. The broad outline is currently as follows:

(a) General statement of revenue

Title 1	Own resources
Title 3	Surpluses, balances and adjustments
Title 4	Revenue accruing from persons working with the institutions and other Union bodies
Title 5	Revenue accruing from the administrative operation of the institutions
Title 6	Contributions and refunds in connection with Union agreements and programmes
Title 7	Interest on late payments and fines
Title 8	Borrowing and lending operations
Title 9	Miscellaneous revenue

(b) Statements of revenue and expenditure for each section

On the revenue side, the nomenclature is identical to that of the general statement of revenue.

For the statement of each institution’s administrative expenditure (in all Sections but Section III), the nomenclature is as follows:

Title 1	Expenditure relating to persons working with the institution
Title 2	Buildings, equipment and miscellaneous operating expenditure
Title 3	Expenditure resulting from special functions carried out by the institution
Title 4	Interinstitutional cooperation, interinstitutional services and activities
Title 5	Data processing
Title 6	Staff and administrative expenditure of Union delegations
Title 7	Decentralised expenditure on support staff and administration
Title 10	Other expenditure

However, the administrative expenditure of the Commission is found under the different titles of Section III, thereby providing a clear picture of the total expenditure on each of the Commission's policy areas. This administrative chapter follows a common structure across all policy areas:

Chapter NN 01

Article NN 01 01	Expenditure related to officials and temporary staff in policy areas
Article NN 01 02	External personnel and other management expenditure
Article NN 01 03	Expenditure related to information and communication technology equipment and services, and buildings
Article NN 01 04	External personnel and technical assistance directly linked to the implementation of programmes
Article NN 01 05	Support expenditure for the research and innovation programmes.
Article NN 01 06	Executive agencies

Section III of the budget is therefore organised under titles corresponding to the Commission's policy areas. In the 2014 budget, the titles are as follows:

- 01 Economic and financial affairs
- 02 Enterprise
- 03 Competition
- 04 Employment, social affairs and inclusion
- 05 Agriculture and rural development
- 06 Mobility and transport
- 07 Environment
- 08 Research and innovation
- 09 Communication networks, content and technology
- 10 Direct research
- 11 Maritime affairs and fisheries
- 12 Internal market and services
- 13 Regional and urban policy
- 14 Taxation and customs union
- 15 Education and culture
- 16 Communication
- 17 Health and consumer protection

- 18 Home affairs
- 19 Foreign policy instruments
- 20 Trade
- 21 Development and cooperation
- 22 Enlargement
- 23 Humanitarian aid and civil protection
- 24 Fight against fraud
- 25 Commission policy coordination and legal advice
- 26 Commission administration
- 27 Budget
- 28 Audit
- 29 Statistics
- 30 Pensions and related expenditure
- 31 Language services
- 32 Energy
- 33 Justice
- 34 Climate action
- 40 Reserves

3) *Structure by article or item*

The budget contains, for each individual item, article, chapter and title:

- (1) the appropriations provided for the financial year in question (year n), in the form of commitment appropriations and payment appropriations for differentiated appropriations;
- (2) the appropriations provided for the preceding financial year (year n-1);
- (3) the actual expenditure in the last financial year for which the accounts have been closed (year n-2);
- (4) appropriate remarks on each expenditure line. These remarks include the references of the basic legal instrument, if one exists, plus all necessary explanations concerning the nature and purpose of the appropriations.

In addition, the budget must include information on staff numbers and, in particular, the 'establishment plan' for each institution (Article 49(1)(c) FR).

In the absence of formal inclusion of borrowing-and-lending operations in the budget (Article 7(2) FR), these operations appear in the budget in the following form:

- in the general statement of revenue: the relevant budget lines intended to record any reimbursements received from recipients who initially defaulted, leading to the activation of the performance guarantee. These lines carry a token entry '*pro memoria*' and accompanied by appropriate remarks;
- in the Commission section: the budget lines containing the Union's performance guarantee relating to the categories of operation and carrying a token entry '*pro memoria*', as long as no effective charge which has to be covered by definitive resources has arisen, plus remarks giving references to the basic act and indicating the volume and duration of the operations envisaged and the financial guarantee given by the Union in respect of these operations;
- in a document annexed to the Commission section, as an indication: ongoing capital operations and debt management, plus the capital operations and debt management for the financial year in question.

The 2012 revision of the FR has, in addition, introduced specific requirements for the presentation of the operations related to financial instruments and the funding of the public-private partnerships (PPPs):

- With regard to financial instruments, the budget shall include a reference to the basic act, the budget lines corresponding to the relevant operations, a general description of the financial instruments and the envisaged operations;
- With regard to PPPs, the budget shall include a reference to the basic act of the relevant programme, the corresponding budget lines and a general description of the entrusted tasks, including their duration and their impact on the budget.

Lastly, the budget has to provide for the total amount of CFSP expenditure and shall contain specific lines identifying, as a minimum, the single major missions (Article 49 (1)(g)).

6.3. Specification and entry of appropriations against headings

There are three types of entry against budget headings:

1) *Headings with appropriations entered*

This is the usual situation.

2) *Headings with a token entry (pro memoria)*

Token entries are used in the following three cases:

- (1) where no basic act exists at the time the budget is adopted and the measure envisaged cannot be undertaken without a basic act ⁽¹⁾;

(1) See Chapter 10, Section 6.4 on legal bases.

- (2) where it is difficult at the outset to estimate the cost of new operations;
 - (3) where the European Parliament and Council wish to stop an operation temporarily.
- In these three cases, appropriations may be entered in a specific 'Reserves' title: Title 40.

Headings with a token entry may receive appropriations by transfer.

A token entry is therefore a sign that the European Parliament and Council accept the principle of expenditure under the heading concerned, but that any expenditure is subject to certain conditions.

3) Headings with a dash

A dash is entered to indicate headings which are no longer operational, but for which the appropriations entered for year n-1 and the outturn for year n-2 still have to be shown for reasons of comparison and to satisfy the technical requirements of budgetary presentation.

Headings with a dash may not be given appropriations by means of transfers. An amending budget must be adopted to allocate appropriations to these headings.

The dash therefore means that the European Parliament and Council no longer accept the principle of expenditure under the heading, as they consider the operation to be finished.

6.4. Flexibility in application of the rule of specification: transfers of appropriations

Transfers of appropriations within the budget is the procedure used to correct the estimates made by the European Parliament and Council by moving appropriations between budget lines. They help in improving the prospects of budget implementation which is subject to particularly careful scrutiny on the part of the European Parliament and the Council ⁽¹⁾.

Transfers imply the reallocation of appropriations from one budget line to another, in the course of the financial year and thereby they constitute an exception to the budgetary principle of specification.

They are, however, expressly authorised by the Treaty on the Functioning of the European Union (Article 317), under the conditions laid down in the FR. The latter identifies, in its Articles 24 to 29, different types of transfers depending on whether they are between or within budget titles, chapters, articles or headings. The FR also differentiates between administrative and staff appropriations and operational appropriations, and between institutions covered by the budget.

1) Transfers between titles

(a) Operational expenditure of the Commission

In accordance with Article 27 FR, the transfer proposals are prepared by the Commission, before being submitted simultaneously to the European Parliament and the Council which shall deliberate within six weeks of the receipt by both institutions.

⁽¹⁾ See Chapter 15.

This six-week period is reduced to three weeks where:

- (1) the transfer represents less than 10 % of the appropriations of the line from which the transfer is made and does not exceed EUR 5 000 000;
- (2) the transfer concerns only payment appropriations and the overall amount of the transfer does not exceed EUR 100 000 000.

The Commission proposal is deemed to be accepted if there is no decision from either institution.

(b) Expenditure on staff and administration of the Commission

For these transfers, different procedures may apply, given the impact of the transfers to be made. As is the case for operational expenditure, the Commission may propose transfers to the European Parliament and Council which may accept or reject the proposals, following the procedures described under point (a). There are, however, specific procedures related to particular situations:

- The Commission makes the transfers itself after giving the European Parliament and the Council three weeks' notice. This is the case for transfers from one title to another up to a maximum of 10 % of the appropriations for the year on the line from which the transfer is made, and up to a maximum of 30 % of the appropriations for the year on the line to which the transfer is made (Article 26(1)(b)). However, this procedure does not apply if duly justified reasons are raised within the three-week period by either the European Parliament or the Council, in which case the procedure described under point (a) applies.
- The Commission makes transfers autonomously and informs the European Parliament and Council within two weeks after its decisions. This applies during the last two months of the financial year to expenditure on staff, external staff and other agents up to a total limit of 5 % of the appropriations for the financial year.
- The Commission makes transfers autonomously and informs the European Parliament and Council immediately in case of transfers of appropriations from the 'provisions' title, as soon as the basic act is adopted pursuant to Article 294 TFEU, in cases where no basic act existed for the action concerned when the budget was established.

(c) For institutions other than the Commission

The institution concerned may make transfers within its own section of the budget after giving the European Parliament and the Council three weeks' notice. However, this procedure does not apply if duly justified reasons are raised within that period by either the European Parliament or the Council, in which case the procedure described under point (a) applies.

For transfers from one title to another up to a maximum of 10 % of the appropriations for the year on the line from which the transfer is made the procedure described under point (a) applies.

2) Transfers between chapters

(a) For the Commission

As regards operational expenditure, proposals for transfers from one chapter to another are prepared by the Commission and submitted to the European Parliament and Council, which take a decision following the procedure described under point 1(a).

However, for transfers from one chapter to another within the same title up to a maximum of 10 % of the appropriations for the year on the line from which the transfer is made, the Commission makes the transfers itself.

(b) For other institutions

The institution concerned may make transfers within its own section of the budget after giving the European Parliament and the Council three weeks' notice. However, this procedure does not apply if duly justified reasons are raised within that period by either the European Parliament or the Council, in which case the procedure described under point 1(a) applies.

3) Transfers within chapters

(a) For the Commission

The Commission may transfer appropriations within articles and between articles within each chapter without any need to inform the European Parliament or the Council and without any limit.

(b) For the other institutions

Without any limit, each institution may, within its own section of the budget, transfer appropriations from one article to another after giving the European Parliament and the Council three weeks' notice, except if duly justified reasons are raised within that three-week period by either the European Parliament or the Council, in which case the procedure described under point 1(a) shall apply.

4) Specific rules for transfers of appropriations

(a) European Agricultural Guarantee Fund

The specific rules concern the time limits for submitting proposals to the European Parliament and the Council or adopting decisions.

In cases where the Commission may transfer appropriations, it must take its decision by 31 January of the following financial year at the latest and inform the European Parliament and the Council three weeks before making the transfers (Article 173(1) FR).

Where the Commission is required to submit transfers to the European Parliament and the Council, it must submit its proposals by 10 January of the following financial year at the latest. In this case, the normal procedure, as described under point 1(a) shall apply, but within a time limit of three weeks instead of six weeks (Article 173(2) FR).

(b) European Regional Development Fund, European Social Fund, Cohesion Fund and European Maritime and Fisheries Fund and Funds in the area of freedom, security and justice managed in shared management

With regard to the operational expenditure in these fields, the Commission may make transfers from one title to another, provided the appropriations in question are for the same objective within the meaning of the Regulations governing these Funds or are Technical Assistance expenditure (Article 179 FR).

This rule does not apply to the European Agricultural Fund for Rural Development.

(c) Research appropriations

With regard to operational expenditure for research and technological development appropriations, the Commission may make transfers from one title to another, provided the appropriations in question are used for the same purpose (Article 181 FR).

(d) Reserve for emergency aid for third countries

Decisions on transfers to allow use of the reserve for emergency aid are taken by the European Parliament and the Council on a proposal from the Commission. The procedure described under point 1(a) applies.

If the Commission proposal is not agreed to by both the European Parliament and the Council and they fail to reach a common position on use of this reserve, the European Parliament and the Council must refrain from acting on the Commission proposal for a transfer (Article 29(2) FR).

(e) Humanitarian aid and crisis management

In duly justified exceptional cases of international humanitarian disasters and crises occurring after 1 December of the budgetary year, the Commission may transfer unused budgetary appropriations for the current budgetary year still available in the budget falling under heading 4 of the multiannual financial framework to the budget titles concerning the crisis management aid and humanitarian aid operations. The Commission must inform the European Parliament and the Council immediately after making such transfers (Article 26(2)(b) FR).

(f) Joint Research Centre

In this case, the Commission may, within the budget title relating to the policy area 'Direct research', make transfers between chapters of up to 15 % of the appropriation on the line from which the transfer is made (Article 183(6) FR).

(g) Offices

Specific rules also apply to European offices such as the Publications Office (OP). In such cases, the Director of each European office will take decisions on transfers within the statement of expenditure of the Office concerned. The Commission must inform the European Parliament and the Council of such transfers.

(5) End-of-Year Transfer for funds in shared management

The end-of-year transfer was introduced through Articles 177(5) and 179(2) and (3) FR. It is a new mechanism aimed at making use of any differentiated payment appropriations remaining available by the end of a financial year and at allowing funds in shared management to proceed with payments for corresponding amounts.

This new type of transfer addresses two shortcomings:

- some budgetary availabilities are only confirmed in the last weeks of the year;
- some payment claims for funds in shared management are sent to the Commission in the very last weeks of the year.

It constitutes a transfer decision taken by the European Parliament and the Council and it has the following characteristics:

- it concerns differentiated payment appropriations only;
- the appropriations are made available and the relevant payments take place before the end of the year, whereas the approval of the Budgetary Authority is given only at the end of January of the following year;
- the end-of-year transfer applies to all budget availabilities in differentiated payment appropriations, which may be collected from all headings of the multiannual financial framework.

The transfer proposal is submitted to the European Parliament and the Council by 10 January of the following year. The European Parliament and the Council take their decision within a time limit of three weeks (FR Art. 179(2)). If the transfer is not approved or only partially approved, the transfer is reversed before 31 January and the payments are regularised and finally charged to the payment appropriations of the following financial year (FR Art. 179(3)).

6.5. Reserves

The introduction of reserves in the budget can be considered an exception to the rule of specification from two points of view:

- the reserves set aside are not allocated to any precise purpose;
- the limit on authorised appropriations for a specific item of expenditure is weakened in this way.

The FR allows for three types of budget reserves:

- (1) provisions (Article 46);
- (2) a reserve for emergency aid for third countries (Article 48);
- (3) a negative reserve (Article 47) ⁽¹⁾.

⁽¹⁾ For the definition of negative reserve, see Section 5 (The principle of equilibrium).

The purpose of these reserves is to facilitate budget management. They make it possible, during the financial year, to endow a budget heading for operations for which full details had not been decided at the time the budget was adopted, or to increase authorised appropriations to meet unforeseen situations or to reduce them to make savings, depending on progress with implementation.

These reserves may be called upon only by means of a transfer procedure: the rule of specification is therefore restored in any case when the time comes to use them.

7. The principle of the unit of account

7.1. The principle of the unit of account

As in other international organisations, the question of which monetary unit to use arose for the Community budget.

The principle of adopting a unit of account distinct from the national currencies was established in the earliest days of the ECSC in Decision No 3/52 of 23 December 1952 and, in the case of the EEC and Euratom, by the Treaties themselves (Article 279 of the EC Treaty and Article 181 of the Euratom Treaty).

With the exceptions of 1958, 1959 and 1960, when preparations were being made for applying Article 279 of the EC Treaty and Article 181 of the Euratom Treaty and the EEC and Euratom budgets were drawn up in Belgian francs, the Community budget has always been expressed in units of account.

Finally, with economic and monetary union and the launch of the euro on 1 January 1999, the Community budget adopted the new single currency as its unit of account.

This principle is enshrined in Article 19 FR. Subject to two specific exceptions — in the case of imprest accounts or for the needs of administrative management of the Commission and the European External Action Service — the budget must be drawn up and implemented in euros and the accounts must be presented in euros.

7.2. From the dollar to the euro: successive units of account

1) *1951–58*: the ECSC adopted the unit of account used by the European Payments Union, namely the US dollar.

2) *1958–60*: The ECSC budget was expressed in a ‘gold parity’ unit of account which corresponded to a given weight of fine gold (0.88867088 grams) in accordance with the Bretton Woods Agreements.

3) *1961 onwards*: Use of this ‘gold parity’ unit of account was extended to the EEC and Euratom. Following the crisis in the international monetary system in the early 1970s, all reference to gold was dropped, and so this unit of account was no longer of any use and the search started for a replacement.

4) *1977/78–80*: A unit of account based on a ‘basket’ of different Community currencies was introduced; this was the European unit of account (EUA) which, it was hoped, would be unaffected by external monetary fluctuations and therefore more stable.

5) 1981–98: The ECU was applied to the general budget; it was based on the same basket as the EUA but, unlike its predecessor, was subject to regular revision of the amounts.

6) 1999 onwards: The euro became the single currency of the new economic and monetary union and was applied to the Union's general budget.

7.3. Simplification brought about by use of the euro

The Union budget is expressed in euros, which is a significant simplification. The euro is the only instrument used to express and settle the debts and claims of the Union, eliminating any exchange risks between the Union unit of account and national currencies, which still existed with the ECU. Exchange risks have been transferred from the EU to those Member States not participating in monetary union. Now the only exchange risks borne by the EU are in its relations with non-EU countries, where the corresponding debts or claims are expressed in a unit other than the euro.

The euro money market is the same as that of the participating Member States and is obviously much bigger than the ECU market, thus safeguarding its stability and the 'purchasing power' of the Union budget.

8. The principle of transparency

Articles 34 and 35 FR enshrine the principle of transparency.

Transparency applies to the entire budget cycle, but is particularly visible in the requirements concerning publication. Under Article 34, the budget must be established and implemented and the accounts presented in compliance with the principle of transparency.

The President of the European Parliament shall have the budget and any amending budget, as definitively adopted, published in the Official Journal of the European Union. The budgets shall be published within three months of the date on which they are declared definitively adopted.

The consolidated annual accounts and the report on budgetary and financial management drawn up by each institution shall be published in the Official Journal of the European Union.

Information on borrowing-and-lending operations contracted by the Union for third parties must be given in an Annex to the budget (Article 35(1) FR).

The basic requirement for the Commission to publish information on recipients of EU funds is given in Article 35 FR. The Commission has put in place a web based search engine called 'Financial Transparency System' (FTS). FTS is available on Europa, the official website of the European Union ⁽¹⁾.

The FTS publishes only the recipients of the following sources of funding: EU budget directly administered by the Commission's departments, its staff in the EU delegations, or through executive agencies, and the European Development Fund.

(¹) http://ec.europa.eu/budget/fts/index_en.htm.

The following funding types are published on this site, in accordance with Article 21 of the Rules of Application: prizes, grants and contracts. Waiver of publication applies to protect the personal data of natural persons: data related scholarship and contracts below EUR 15 000 are exempted from publication.

Data for any given year is not published until the following year.

Search results include inter alia: who receives the funds (recipient), subject, i.e. the purpose of the expenditure, where the recipient is located, amount and type of expenditure, which responsible department awarded the funding, which part of the EU budget (budget line) it comes from, when (year) the amount was booked in the accounts.

Very low value contracts, scholarships and support paid to persons most in need will not be published.

9. The principle of sound financial management

The principle of sound financial management is based on Article 317 of the TFEU, which provides that 'the Commission shall implement the budget ... on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management'.

Article 30 FR links this principle to the principles of economy, efficiency and effectiveness. The principle of economy requires that the resources used by the institution to engage in its activities are available in due time, in appropriate quantity and quality and at the best price. The principle of efficiency is concerned with the best relationship between resources employed and results achieved. The principle of effectiveness is concerned with attaining the specific objectives set and achieving the intended results.

In practice, sound financial management is based on setting verifiable objectives which can be monitored by measurable indicators, in order to switch from means-based management to results-oriented management. Allocation of resources to activities (using activity-based budgeting or ABB) makes it possible to integrate the cost of the activities and their objectives. It also means that the total costs of the various operations can be verified and the Commission's work programme can be better tailored to ensure an appropriate relationship between policy priorities and the allocation of resources.

Appropriate application of this principle requires that the planning, budgeting, management and reporting processes take place within a single common conceptual framework. Consequently, a common structure of activities and policy areas provides the framework for defining policy priorities, allocating and managing resources in line with those priorities, and reporting the results achieved. In this context, activity-based budgeting is the budgetary component of a wider 'activity-based management' (ABM) approach. The main instruments of ABM are:

- The Europe 2020 Strategy, which sets out the policy priorities in the long term and the Multiannual Financial Framework 2014–20, which provides for the overall resources required to meet them;
- The State of the Union speech delivered by the President of the Commission which outlines the annual priorities;

- The draft budget (DB), which is accompanied by the Programme Statements (PS) as the main instrument for justifying the request for appropriations for spending programmes, in terms of performance information on objectives and indicators, and according to their corresponding legal basis;
- The management plans (MPs), which are prepared by all Commission departments and include specific objectives and performance indicators for all activities with the resources (financial and human), which are managed in line with predefined policy priorities;
- The annual activity reports (AARs), which constitute the ‘mirror’ of the MP, and by which authorising officers by delegation (Directors General and Heads of Service), report on policy results, management performance, internal control and financial statements of their service. They include the declarations by Directors General on the legality and regularity of operations and on achievement of the objectives.

10. Evaluation of Union action and sound financial management

The concept of evaluation is fully integrated throughout the programme cycle and is understood as a continuous process which must cover the entire duration of a measure: from the preparation stage in order to define the objectives and means, through allocation of resources in the budget to completion of the measure, when the results will be assessed and conclusions drawn on whether the measure should be renewed.

10.1. Decision making

1) Ex ante evaluation, an essential requirement for sound and efficient management of Union programmes

Ex-ante evaluation is a process that supports preparation of proposals for new or renewed Union action. Its purpose is to gather information and carry out analyses which help to ensure the delivery of policy objectives, the cost-effectiveness of the instruments used and the possibility of reliable evaluation at a later stage.

An *ex ante* evaluation should be seen as an analytical process, which can stretch over a long period of time. Different steps can be followed separately. An *ex-ante* exercise is not necessarily a one-off project, which merely produces a report, but rather a process consisting of separate phases and different pieces of analysis.

The FR states that *ex ante* and *ex post* evaluations ‘shall be applied to all programmes and activities which entail significant spending and evaluation results disseminated to the European Parliament, the Council and spending administrative authorities’ (Article 30 FR).

Ex ante evaluation must address:

- the need to be met in the short or long term;
- the added value of Union involvement;

- the policy and management objectives to be achieved, which include measures necessary to safeguard the financial interests of the Union in the field of fraud prevention, detection, investigation, reparation and sanctions;
- the policy options available, including the risks associated with them;
- the results and impact expected, in particular economic, social and environmental impact, and the indicators and evaluation arrangements needed to measure them;
- the most appropriate method of implementation for the preferred option(s);
- the internal coherence of the proposed programme or activity and its relations with other relevant instruments;
- the volume of appropriations, human resources and other administrative expenditure to be allocated with due regard for the cost-effectiveness principle;
- the lessons learned from similar experiences in the past.

In addition to this *ex ante* evaluation, each proposal for a programme or activities leading to budget expenditure must set out the monitoring, reporting and evaluation arrangements. These must take account of the responsibilities of each level of government that will be involved in implementing the proposed programme or activity. This will avoid any duplication of evaluations, in particular in case of shared management with Member States.

2) *Compulsory financial statement*

At the Commission, any proposal or initiative submitted to the legislative authority which may have an impact on the budget, is accompanied by a financial statement which contains the financial and economic data for the assessment of the need of the Union action. The same obligation is also imposed on Member States when they submit proposals in conformity with the relevant provisions of the EU Treaty and on any institution submitting an amendment to a proposal or initiative which may have appreciable implications for the budget, including changes in the number of posts (Article 31 FR).

The financial statement is designed to provide information on both administrative and human resources and operational appropriations. A financial statement is referred to as 'budgetary' when it accompanies the draft budget and as 'legislative' when it accompanies legislative proposals with budgetary implications.

A legislative financial statement analyses the reasons for the appropriations requested in two different ways. Firstly, it demonstrates the need for the Union action envisaged by clarifying its general objective and value added. It also gives an overall description of the logic behind the proposal in order to give reasons for the particular action to be financed and demonstrate its cost-effectiveness in achieving the stated objectives. Secondly, the financial statement provides output and costing information by specifying the predicted nature and volume of output and establishing the unit cost. The purpose of this is to facilitate assessment of the proposed level of funding and of its impact on the expected results.

In addition to these explanations, the legislative financial statement will also provide information on the fraud prevention and protection measures in place or planned.

Lastly, in order to reduce the risk of fraud and irregularities, the financial statement shall provide information on the internal control system set up, an estimate of the cost and benefits of the proposed controls and an assessment of the expected level of risk of error.

10.2. Budget decisions

In the Commission, the budgetary decision-making process centres around the draft budget (DB). The role of evaluation is to support this process by providing fact-based evidence on the performance and progress of the Union programmes.

The findings of the individual evaluations provide relevant input for preparation of the draft budget. In addition, the Commission decides annually on a limited number of strategic evaluations. These evaluations, which cut across a number of areas, are designed to supplement the results of the evaluations carried out by operational departments. They assess the impact of any policy that uses the resources of several departments.

10.3. Implementation of the budget

In order to provide relevant and timely information for subsequent decision making, all programmes or activities, including pilot projects and preparatory action, mobilising resources exceeding EUR 5 million will be subject to an interim and/or *ex post* evaluation of the human and financial resources allocated and the results obtained (Article 18 of the Rules of Application).

In this context, mid-term and *ex post* evaluations need to be adapted both to decision-making needs and to the lifecycle and nature of each activity. However, as a general guideline, activities should be subject to an overall evaluation at least every six years. In the case of multi-annual programmes or activities, at least one thorough evaluation during the lifecycle of the action is needed.

Mid-term evaluations carried out during implementation of a programme generally focus on the relevance of the objectives, the implementing arrangements and the initial results. Since new programmes are often prepared long before their predecessors are completed, mid-term evaluation is an important source of information for planning the next programme.

Ex post evaluation is typically carried out after the programme expires, focusing mainly on its impact and cost-effectiveness. Since it is not usually completed until after the following programme has started, its results can be used if any revisions or changes are made to the new programme during its lifecycle.

11. Internal control and sound financial management

Under Article 32 FR, the budget must be implemented in compliance with effective and efficient internal control, which is defined as a process applicable at all levels of the management and designed to provide reasonable assurance of achieving the following objectives:

- effectiveness, efficiency and economy of operations;
- reliability of reporting;

- safeguarding of assets and information;
- prevention, detection, correction and follow up of fraud and irregularities;
- adequate management of the risks related to the legality and regularity of the underlying transactions, taking into account the multiannual character of programmes as well as the nature of the payments concerned.

Paragraphs (2) and (3) of Article 32 FR further define the requirements for an effective and efficient internal control ⁽¹⁾.

⁽¹⁾ For more details on the internal control framework, see Chapter 19.

Chapter 12

The annual budgetary procedure

1. Introduction

1.1 The institutional and legal aspects of the budgetary procedure

The Treaty on the Functioning of the European Union introduced a number of important changes to the budget procedure and timetable, which are explained in this chapter. Article 314 TFEU defines the successive stages of the budgetary procedure, and establishes the powers of each of the two arms of the budgetary authority (European Parliament and Council) and the Commission in this procedure.

Council Regulation (EU, Euratom) No 1311/2013 of 2 December 2013 laying down the multiannual financial framework for the years 2014–20 (MFF Regulation) calls for the three institutions to ‘cooperate in good faith throughout the procedure with a view to reconciling their positions’, and the practical means to facilitating this cooperation are set out in the Interinstitutional Agreement (IIA) on budgetary discipline, on cooperation in budgetary matters and on sound financial management, in particular in its annex.

1.2. The timetable for the budgetary procedure

The official timetable for the budget procedure is set out in Article 314 TFEU, which stipulates that all institutions shall draw up estimates of expenditure before 1 July, the Commission shall transmit the Draft Budget (DB) to the Council not later than 1 September, and the DB shall be transmitted to the European Parliament not later than 1 October. Although the budget calendar is set out in the Treaty, in practice much tighter deadlines are foreseen.

Up to the adoption of the 2013 DB, the Commission followed the so-called ‘pragmatic calendar’, which stems from a political agreement between the European Parliament, the Council and the Commission, and which had been used since the 1977 financial year. The purpose was to increase the time available to the budgetary authority for its deliberations. Due to the lack of an agreed multiannual financial framework and the timing of the European elections, respectively, the draft budgets for 2014 and 2015 were prepared according to a slightly later calendar, while still allowing sufficient time for Parliament and Council.

Both the pragmatic calendar and the calendars used for the 2014 and 2015 draft budgets bring forward the official deadlines and provide for documents to be transmitted unofficially to each of the institutions concerned before the dates set in Article 314. This allows the Council to adopt its position on the DB by end July and send it to the European Parliament in the first half of September, to enable Parliament to vote on its amendments on the Council position by the end of October.

1.3. The impact of the Treaty on the Functioning of the European Union

The TFEU introduced a number of changes to the annual budget procedure. As explained in detail below, the system of two readings by each arm of the budgetary authority, is now replaced. The Council, followed by Parliament, now conducts its reading, and unless the European Parliament approves the position of the Council in full, or does not take a decision, in which cases the budget is adopted, a conciliation committee is convened for a period of 21 days. The budget will then be adopted on the basis of a joint text to be agreed by the Parliament and the Council.

2. The stages in the budgetary procedure

2.1 Preparation of the draft budget by the Commission

1) The statements of estimates of the various institutions

As required by Article 314(1) TFEU, each institution, with the exception of the European Central Bank, draws up an estimate of its expenditure for the following year. In principle, the other institutions must send the Commission their statements of estimates before 1 July; in practice, however, under the pragmatic timetable, most institutions do this by 1 May. The Commission consolidates all these estimates in a draft budget, which is the overall forecast of revenue and expenditure for the year ahead, and the Commission may modify the estimates of the other institutions.

2) The internal Commission procedure for preparing the draft budget

The internal procedure for preparing the draft budget is organised by the DG Budget, which gathers together the requests from the other directorates-general and departments, submits to the Commission possible outstanding issues and prepares the documents for compilation into the draft budget.

Stage 1: Budget Circular

Usually, in December of year $n-2$, the Director-General for the Budget sends out a circular containing instructions for the spending departments and provides them with details of the overall economic and financial framework. This circular marks the start of the Commission's internal work on preparing the detailed draft budget for the year n .

Spending departments then provide detailed information and justifications for the budgetary requests, usually by mid-February.

Stage 2: Budget Hearings

Usually in March, the DG Budget holds budget hearings with individual spending departments. Given the constraints imposed by the financial framework, the requests for appropriations are examined on the basis of the priority to be given to the various operations to be financed, the foreseeable trend in requirements (including payment appropriations and administrative resources) and the consistency, in terms of cost-effectiveness, between the resources considered necessary and the objectives pursued.

On the basis of the inter-departmental hearings, the DG Budget prepares a proposal for the draft budget (incorporating the other institutions' statements of estimates) for the approval of the Commission.

The draft budget includes a large number of documents, either for formal adoption by the Commission, or as supporting information in the form of working documents. Full details of these are set out in Article 38 of the Financial Regulation, whereas Articles 44 to 49 set out the structure and presentation of the draft budget.

2.3. The role of the Budgetary Authority

There are two arms to the Budgetary Authority — the Council and the European Parliament. The Council decisions are prepared by the Budget Committee (COMBUD, made up of the budget attachés in the Permanent Representations), then by Coreper II (Permanent Representatives Committee). Those of the European Parliament are prepared by the Committee on Budgets.

The procedure begins for both arms of the Budgetary Authority well in advance of the presentation of the Draft Budget by the Commission. In late January of each year, the Council (COMBUD) begins the preparation of the Council's Guidelines for the coming budget procedure. This text, traditionally calling for budgetary rigour, sufficient margins, and realistic levels of expenditure, makes its way to Coreper II and then to the Ecofin by mid- February.

In a similar way, in the Parliament, the Committee on Budgets prepares its guidelines for the new budget. The Rapporteurs for the annual procedure (one for the Commission — Section III — and one for the other institutions), prepare a report, which is usually voted in the Committee in February and at plenary in March. These two documents are the subject of an exchange of views with the Commission in a trilogue, which normally takes place in late March.

Once the Commission presents the Statement of Estimates, shortly followed by the formal decision on the DB, the Council (COMBUD) begins its examination of the Commission's proposals, and those of the other institutions, and prepares its reading. Although this work may begin before 1 July, it is always chaired by the rotating Presidency which will negotiate the budget in the autumn.

If there is agreement at the level of COMBUD, the Council's position passes to Coreper II as an 'I' point (i.e. no discussion) for approval. If agreement has not yet been reached, it will be an 'II' point for discussion and vote by qualified majority. If necessary, an ECOFIN-Budget can be held in July at ministerial level to seek an agreement. However, regardless of the level at which agreement is reached, the Council will only finalise its reading via a written procedure in August/early September, as it applies Protocol 1 of the TFEU to the budget procedure, giving the national parliaments eight weeks to examine the proposal.

For adoption of the DB, a qualified majority is required in the Council, 260 votes from a majority of the members, out of a total of 352 votes distributed in accordance with the weightings shown in Table 12.1 below.

TABLE 12.1 – *Qualified majority voting and country weights*

Member State	Votes for each country	Total votes
DE, FR, IT, UK	29	116
ES, PL	27	54
RO	14	14
NL	13	13
BE, CZ, EL, HU, PT	12	60
BG, AT, SE	10	30
DK, IE, HR, LT, SK, FI	7	42
EE, CY, LV, L, SL	4	20
MT	3	3
All Member States		352

These voting rules make it possible for ‘blocking minorities’ to be formed, when Member States with a combined total of 93 votes align.

In accordance with the provisions of the IIA, a trilogue is convened before the Council’s reading (usually in July), to allow for an exchange of views on the DB. This trilogue also allows for a first discussion on the intentions of either the European Parliament or the Council to propose new pilot projects or preparatory actions, or to prolong existing ones.

In September the focus turns to the Parliament, with the preparation of amendments in the various specialised committees, and by the political groups, for presentation to and vote at the Committee on Budgets (end September — beginning October). On this basis the amendments for presentation to the October plenary are established, as well as an opinion in textual form. A further trilogue is held before the plenary session. Although the Council could, theoretically, give its agreement to all the Parliament amendments, at which point the budget would be considered adopted, this is certainly not the practice, and so begins the 21-day period of conciliation.

As part of the ‘input documents’ made available to the conciliation committee, the Commission produces a letter of executability on the Council’s position and the European Parliament’s amendments, including a detailed assessment of the implementability of pilot projects and preparatory actions proposed by the Council and the European Parliament.

The goal during the conciliation period is to arrive at an agreement of a ‘joint text’ on the basis of ‘joint conclusions’ agreed during the conciliation meeting, which can then be translated ‘mechanically’ in the line-by-line budget. Although the conciliation is supposed to focus only on the agreement of the new budget, negotiations usually also include outstanding draft amending budgets.

If agreement is reached, both arms of the Budgetary Authority have 14 days in which to adopt the agreement, at which point the President of the Parliament signs the budget into force. In the first procedure following the entry into force of the TFEU, the Council contested this

practice, stating that it too should sign. At the end of 2013, this matter was ruled on by the Court of Justice which ruled against the Council's claim.

If agreement cannot be reached in the 21 days, the Commission must present a new DB.

For details of the consequences of a rejection of the budget, see Section 5 below.

3. Amending budgets

3.1. Definition and procedure

The purpose of amending budgets is to provide a suitable means of adjusting the budget to real requirements during the year.

Article 41(1) of the Financial Regulation states that the Commission may present draft amending budgets, which are primarily revenue driven for the following reasons:

- to enter in the budget the balance of the preceding financial year;
- to revise the forecast of own resources on the basis of updated economic forecasts;
- to update the revised forecast of own resources and other revenue, as well as to review the availability of, and need for, payment appropriations.

The Commission may also present draft amending budgets which are primarily expenditure-driven 'if there are unavoidable, exceptional and unforeseen circumstances, in particular in view of the mobilisation of the European Union Solidarity Fund'. Before presenting an amending budget, the possibilities for redeployment of appropriations must be examined. As regards the date for presentation, Article 41(3) of the Financial Regulation states: 'The Commission shall, except in duly justified exceptional circumstances or in the case of the mobilisation of the European Union Solidarity Fund (...), submit its draft amending budgets simultaneously to the European Parliament and the Council by 1 September of each financial year'.

Amending budgets are subject to the same rules of procedure as the general budget. However, bearing in mind that amending budgets may be intended to address urgent needs, they tend to be addressed avoiding recourse to the conciliation process. The annex of the IIA sets out a number of principles to facilitate this, including discussion at trilogues, with a view to reconciling positions.

3.2. 'Balance' amending budget

The submission of the provisional accounts for the previous year by 31 March each year allows calculation of the positive or negative balance resulting from the differences between the receipts forecast in the budget and those which actually materialise, and from any under-spending of the payment appropriations provided for in the budget.

Article 18 of the Financial Regulation states that 'the balance from each financial year shall be entered in the budget for the following financial year as revenue in the case of a surplus or as a payment appropriation in the case of a deficit'.

Entry of the balance for year *n* in the budget is proposed in a draft amending budget, which must be presented within 15 days of the submission of the provisional accounts.

4. Letters of amendment

The Commission may, on its own initiative, or at the request of the other institutions in respect of their own sections of the budget, present a letter of amendment to the DB in the light of information which was not available when this DB was established. Irrespective of the stage reached in the procedure, the letter of amendment always relates to the DB, rather than to the position of either Council or Parliament. In accordance with Article 314(2) TFEU the Commission may amend the DB until such time as the Conciliation Committee is convened.

It is not unusual to have between one and three letters of amendment during the budgetary procedure, and at the very least, there is one concerning agricultural expenditure and the fisheries agreements. In October each year, the Commission submits to the European Parliament and the Council a letter of amendment to update the figures underlying the estimate of agricultural expenditure in the DB and/or to correct, on the basis of the most recent information available concerning fisheries agreements in force on 1 January of the financial year concerned, the breakdown between the appropriations entered in the operational items for international fisheries agreements and those entered in reserve.

5. Rejection of the budget and the consequences

The challenging nature of the budgetary negotiations has meant that in some years discussions have had to continue beyond the planned date for the conclusion of the conciliation, and since the entry into force of the TFEU, the Commission has been called upon to present a new draft budget, in accordance with Article 314(8) on two occasions — in 2010 for budget 2011, and in 2012 for budget 2013. However, the number of occasions on which the budget has formally been rejected have been very limited. This happened in December 1979 for the 1980 budget and in December 1984 for the 1985 budget ⁽¹⁾. In the case of the 1986 budget, it was annulled by judgement of the Court of Justice (Case 34/86), when the Council challenged the definitive adoption by the European Parliament. The adoption of the 1988 budget was delayed until 1 June 1988 due to interinstitutional conflict.

5.1. Conditions required to reject the budget

On the two occasions when the budget was actually rejected, this was done by vote of the European Parliament, acting by a majority of its members and two thirds of the votes cast.

Under the provisions of the TFEU the permutations are more complex, but also create a situation where work can continue to arrive at an agreement, with the submission by the Commission of a new draft budget. This was the case in 2010 and 2012, when the conciliation committee could not reach an agreement within 21 days. Following the presentation of a new draft budget, and intensive cooperation from all sides, including trilogues, agreement was ensured, allowing for approval by both the Council and the European Parliament, and the definitive adoption of the budget before the year's end.

(1) See Part 1 'The development of the Union's financial system'.

Article 314(7) TFEU sets out the other situations which might arise if a joint text is agreed in conciliation, but cannot be endorsed within the 14 days foreseen:

- If the European Parliament and the Council both approve the joint text or fail to take a decision, or if one of these institutions approves the joint text while the other one fails to take a decision, the budget shall be deemed to be definitively adopted in accordance with the joint text;
- If the European Parliament, acting by a majority of its component members, and the Council both reject the joint text, or if one of these institutions rejects the joint text while the other one fails to take a decision, a new draft budget shall be submitted by the Commission;
- If the European Parliament, acting by a majority of its component members, rejects the joint text while the Council approves it, a new draft budget shall be submitted by the Commission;

However, there is still a possibility for the European Parliament to approve the budget, even if the Council rejects it. In such a case, the European Parliament may, within fourteen days from the date of the rejection by the Council and acting by a majority of its component members and three-fifths of the votes cast, decide to confirm all or some of the amendments it voted in its reading. Where a European Parliament amendment is not confirmed, the position agreed in the Conciliation Committee on the budget heading which is the subject of the amendment shall be retained. The budget shall be deemed to be definitively adopted on this basis.

5.2. The consequences of rejection

In the absence of agreement between the European Parliament and the Council, either in Conciliation or on a Commission proposal for a second DB, the Union would find itself having to start the budgetary year without a budget. Continuity of EU action is, however, guaranteed by the system of *provisional twelfths* provided for by the Treaty, while the budgetary procedure goes on until such time as the budget is eventually adopted (Article 315 TFEU and Article 16 of the Financial Regulation).

Commitments may be made per chapter up to a maximum of one quarter of the total appropriations authorised in the relevant chapter of the previous financial year plus one twelfth for each month which has elapsed. Payments may be made monthly per chapter up to a maximum of one twelfth of the appropriations authorised in the relevant chapter of the preceding financial year. In both cases, the limits of the appropriations provided for in the DB may not be exceeded, which is known as the 'dual limit' rule.

In order to ensure the continuity of EU action at a minimum level until a new budget is adopted, the Council, acting by a qualified majority and on a proposal of the Commission, may authorise expenditure in excess of one provisional twelfth but not exceeding the total of four provisional twelfths, except in duly justified cases. The European Parliament may decide to reduce the additional twelfths, within a period of 30 days from the Council decision to authorise the additional twelfths.

6. Provisions of the Interinstitutional Agreement

The Interinstitutional Agreements of 1988, 1993, 1999 and 2006 considerably improved the course of the budgetary procedure by establishing a formal procedure for interinstitutional collaboration, which provided a framework for discussing and resolving disputes between the two arms of the budgetary authority, and by setting out specific provisions in certain areas of dispute, such as the classification of expenditure, the maximum rate of increase for non-compulsory expenditure in the absence of a financial framework, the entry of financial provisions in legislative instruments, legal bases, expenditure relating to fisheries agreements and the financing of the common foreign and security policy (CFSP), agencies and European Schools ⁽¹⁾.

The IIA of 2 December 2013 ⁽²⁾ reflects the budgetary procedure under the TFEU, in particular as regards the entry into force of the MFF Regulation, which includes a number of important elements which were previously included in the IIA. There is no longer any distinction between compulsory and non-compulsory expenditure, and therefore no maximum rate of increase for non-compulsory expenditure. However, the other elements set out above remain, as well as provisions on the new reserve for crises in the agricultural sector.

The annex to the IIA sets out the steps to be taken from agreement of the pragmatic calendar to the number and timing of trilogues and the form of the joint text to be established in the context of agreement on the budget.

6.1. Incorporation of financial provisions in legislative acts

Legislative acts concerning multiannual programmes adopted under the ordinary legislative procedure contain a provision laying down the financial allocation for the programme for its entire duration. That amount will be the prime reference figure during the annual budgetary procedure. The budgetary authority undertakes not to depart from this amount by more than 10 %, except in duly justified circumstances, and the resulting expenditure must remain beneath the ceiling for the heading concerned. An increase in allocations is not possible for cohesion policy, nor for the large-scale projects of EGNOS and Galileo, ITER or Copernicus.

Legislative acts concerning multiannual programmes not subject to the co-decision procedure do not have to contain an ‘amount deemed necessary’. If a financial reference amount is nevertheless included by the Council, it must be made clear that it is illustrative, and does not affect the budgetary powers of the European Parliament and the Council as set out in the TFEU.

These provisions reaffirm the role of the financial statement provided for in the Financial Regulation (Article 31). During the budgetary procedure, the Commission shall provide the information necessary for a comparison between the initial financial statement and the appropriations required, in the light of the progress of deliberations on the proposal or initiatives submitted to the legislative authority.

⁽¹⁾ See Part I.

⁽²⁾ See Chapters 8 and 10.

6.2. Legal bases

Implementation of appropriations entered in the budget requires prior adoption of a basic act (an act of secondary legislation which provides a legal basis for the Union action — whether a regulation, directive or decision).

However, in accordance with Article 54(2) of the Financial Regulation, the following may be implemented, within certain limits, without a basic act:

- appropriations for pilot schemes of an experimental nature designed to test the feasibility of an action and its usefulness. The relevant commitment appropriations may be entered in the budget for not more than two successive financial years and may not exceed EUR 40 million a year for all the pilot projects;
- appropriations for preparatory actions in the field of application of the TFEU and the Euratom Treaty, designed to prepare proposals with a view to the adoption of future action (subject to a limit of three financial years and EUR 50 million per financial year for the total amount of the new budget lines concerned, and a further limit of EUR 100 million for the total amount of appropriations actually committed);
- appropriations for preparatory measures in the field of Title V of the Treaty on European Union (concerning the common foreign and security policy (CFSP)). These measures must be limited to a short period of time and designed to establish the conditions for European Union action in fulfilment of the objectives of the CFSP and for the adoption of the necessary legal instruments;
- appropriations for one-off actions, or even actions for an indefinite duration, carried out by the Commission by virtue of tasks resulting from its prerogatives at institutional level pursuant to the TFEU and the Euratom Treaty other than its right of legislative initiative and under specific powers directly conferred on it by those Treaties;
- appropriations for the operation of each institution under its administrative autonomy.

The first two exceptions listed above — pilot projects and preparatory actions — introduce an element of flexibility at both institutional and legislative levels: Parliament often initiates these activities, although not exclusively, thus deviating from the Commission's monopoly of initiative within the strict limits provided for in the Interinstitutional Agreement. It should also be noted that the budgetary decision relating to these activities precedes and gives rise to the legislative decision, reversing the usual order.

The pilot projects and preparatory actions must not relate to activities which are already covered by legal bases in force as this would introduce some redundancy and impair the budgetary decisions relating to the legal bases concerned. It is also routine to allow a pilot project to become a preparatory action when there are plans to draw up a legal base. Finally, preparatory actions cannot be adopted for three consecutive years unless a legal base has already been proposed, in which case the preparatory action would maintain continuity pending introduction of the legal base.

6.3 Expenditure relating to fisheries agreements, the reserve for crises in the agricultural sector and the financing of the Common Foreign and Security Policy (CFSP)

Amounts relating to the fisheries agreements in force on 1 January of the year in question will be entered on the appropriate budget line, for agreements which are to come into force after that date, the amounts are entered in the reserve.

If the appropriations (including the reserve) prove insufficient, a preliminary consultation takes place, based on information and, possibly, proposals presented by the Commission on what measures should be taken.

Appropriations for the Reserve for crises in the agricultural sector provided for in Article 25 of Regulation (EU) No 1306/2013 of the European Parliament and of the Council ⁽¹⁾ shall be entered directly into the general budget of the Union. Any amount of the Reserve not made available for crisis measures shall be reimbursed to direct payments. If the Commission considers that the Reserve should be mobilised, it shall present a proposal for transfer. Expenditure related to measures for crises occurring between 16 October and the end of the financial year may be financed from the reserve of the following financial year.

For the financing of the CFSP, the institutions must come to an agreement in the interinstitutional conciliation procedure on the amount of operational expenditure to be entered into the budget. In the absence of an agreement, the amount contained in the previous budget or the amount proposed in the draft budget is entered, whichever is the lower. The forecasts must be based on foreseeable needs and allowing a reasonable safety margin.

Should the allocations prove insufficient in the course of the financial year, the two arms of the budgetary authority must seek a solution as a matter of urgency, on a proposal from the Commission.

⁽¹⁾ Regulation (EU) No 1306/2013 of the European Parliament and of the Council of 17 December 2013 on the financing, management and monitoring of the Common Agricultural Policy (OJ L 347, 20.12.2013, p. 549).

Part 4

Structure of the Union's annual budget



Chapter 13

Revenue

1. General overview

The revenue of the general budget of the European Union can be divided into two main categories: own resources and other revenue. This is laid down in Article 311 of the Treaty on the Functioning of the European Union, which states that ‘Without prejudice to other revenue, the budget shall be financed wholly from own resources’.

The bulk of budgetary expenditure is financed by the system of own resources, as introduced in 1970 by Council Decision 70/243/ECSC, EEC, Euratom of 21 April 1970 (ORD 1970). Other revenue represents only a very minor part of total financing ⁽¹⁾.

There are now three main categories of own resources: traditional own resources, the VAT-based resource and the GNI-based resource. These are supplemented by correction mechanisms.

Revenue from traditional own resources is not sufficient to cover EU budget expenditure. On average, the share of traditional own resources (net 75 %, i.e. after deduction of 25 % retained as collection costs) in total own resources reached around 14 % over 2007–13.

This is why ORD 1970 established a second own resource, based on value added tax (VAT), to finance the Community budget. Revenue from this resource, which accrued as of 1979, gradually became the main source of financing, but turned out also to be insufficient to cover Community expenditure in the mid-1980s. Thus Council Decision 88/376/EEC, Euratom of 24 June 1988 (ORD 1988) introduced a new resource based on Member States’ Gross National Income indicating their respective ‘wealth’ (ESA 79 GNP, replaced in 2002 by ESA 95 GNI).

The GNI-based resource (the ‘residual’ resource) is determined so that total revenue balances total expenditure. It has gradually become the most important source of financing of the EU budget, representing on average 73 % of total own resources payments over 2007–13.

The different own resources are explained in more detail in Section 2 and other revenue in Section 3 of this chapter. Finally, the sequential use of the different sources of revenue to finance budgeted expenditure is explained in Section 4. Figures and tables presenting the system of own resources can be found on the European Commission Internet site ⁽²⁾.

⁽¹⁾ On average, other revenue amounted to around 5 % of total revenue over 2007–13 (excluding the surpluses carried over from the previous year, which themselves are mainly a consequence of the difference between the outturn of own resources payments and of expenditure in the preceding year). For detailed historical data on revenue, see the annexes of the EU Budget Financial Report, as available on: http://ec.europa.eu/budget/biblio/publications/publications_en.cfm

⁽²⁾ http://ec.europa.eu/budget/figures/index_en.cfm

2. Own resources

2.1. Traditional own resources

Traditional own resources (comprising customs duties, agricultural duties, and sugar and iso-glucose levies) were introduced in 1970 and are levied on economic operators and collected by Member States on behalf of the EU.

Revenue deriving from traditional own resources are: 'levies, premiums, additional or compensatory amounts, additional amounts or factors, Common Customs Tariff duties and other duties established or to be established by the institutions of the Communities in respect of trade with non-member countries ... as well as contributions and other duties provided for within the framework of the common organisation of the markets in sugar' (Article 2(1)(a) of Council Decision 2007/436/EC, Euratom of 7 June 2007 (ORD 2007)). This definition remains unchanged under ORD 2014 (Article 2(1)a of Council Decision 2014/335/EU, Euratom).

Following the implementation into EU law of the Uruguay round agreements on multilateral trade, there is no longer any material difference between agricultural duties and customs duties. Therefore this distinction was removed when the ORD 2007 entered into force.

Since 2001 Member States have retained, as collection costs, 25 % of the established amounts of traditional own resources. Before 2001, 10 % was retained, but this percentage was increased to 25 % by Council Decision 2000/597/EC, Euratom of 29 September 2000 (ORD 2000). Under ORD 2014 (Council Decision (EU, Euratom) No 2014/335 of 26 May 2014 on the system of own resources of the European Union) the collection costs to be retained will be reduced to 20 %.

The area of customs union falls under the exclusive competence of the Union. In a single market with a common EU custom code and tariff for external trade and free movement of goods, it seems natural to assign revenue from custom duties to the financing of common expenditure through the EU budget.

2.2. The VAT-based own resource

1) Definition

VAT-based payments derive from the application of a call rate to Member States' VAT bases set according to harmonised rules (see below).

However, VAT bases are capped at 50 % of GNI. This percentage was 55 % from 1988 to 1994 and then gradually reduced to 50 % of GNP as of 1999 under Council Decision 94/728/EC, Euratom of 31 October 1994 (ORD 1994).

The capping of the VAT base reflects the intention to remedy the regressive aspects of the VAT-based resource, which could be seen as penalising the less wealthy Member States with higher shares of consumption.

2) Calculation of the base

In order to minimise distortions due to diverging VAT rates and structures in the Member States, the VAT base is notionally harmonised for the purpose of own resource calculations.

This harmonised VAT base is calculated by each Member State using what is known as the ‘revenue method’. It consists of dividing the total annual net VAT revenue collected by the Member State in question by the weighted average rate of VAT, i.e. an estimate of the average rate applicable to the various categories of taxable goods and services, to obtain the intermediate VAT base. The intermediate base is subsequently adjusted with negative or positive compensations in order to obtain a harmonised VAT base pursuant to the Sixth Council Directive 77/388/EEC of 17 May 1977, and subsequent amendments.

3) *The call rate of the VAT-based resource*

ORD 2014 fixed the VAT call rate at 0.3 % with a reduced rate of 0.15 % for Germany, the Netherlands and Sweden for the period 2014–20 only. Under ORD 2007 the rate was identical with a reduced rate of 0.225 % for Austria, 0.15 % for Germany and 0.10 % for the Netherlands and Sweden for the period 2007–13.

Before that, under ORD 2000, the actual VAT call rate (the ‘uniform’ rate) corresponded to the difference between the ‘maximum’ call rate and what was known as the ‘frozen’ rate (conditional upon the size of the UK correction, see hereafter).

The ‘maximum’ call rate, initially set at 1 % over the period 1974–79, was later increased to 1.4 % by ORD 1985 and then gradually reduced by ORD 1994 (by 0.08 % per year to 1.32 % in 1995, 1.24 % in 1996, 1.16 % in 1997, 1.08 % in 1998 and 1.0 % in 1999 and onwards). ORD 2000 further reduced the ‘maximum’ call rate to 0.75 % in 2002 and 2003 and, from 2004 onwards, to 0.50 %.

The ‘frozen’ rate was a relic from the pre-1988 period, when it was needed to ensure that no Member State would contribute more than the maximum rate of call for the VAT-based resource, including its contribution to the financing of the UK correction (which was added to Member States’ VAT-based payments). The ‘frozen rate’ corresponds to the ratio between the amount of the UK correction ⁽¹⁾ and the sum of the capped VAT bases of all the Member States, taking into account the fact that the United Kingdom is excluded from the financing of its correction and that the share of Austria, Germany, the Netherlands and Sweden in the financing of the correction is reduced by three quarters. The ‘frozen rate’ was deducted from the maximum rate of call. The result gave the actual rate of call Member States had to pay (the ‘uniform’ rate).

ORD 2007 provided for significant improvements in transparency and simplicity, as compared to the very complex ‘frozen’ rate system, by fixing the VAT call rate at 0.30 % (with reduced call rates for four Member States as indicated above).

Even though the need for further simplification and transparency of the VAT-based own resource is generally recognised, the ORD 2014 effectively prolongs the relevant provisions for the next financial framework period. However, the European Council of 7–8 February 2013 called upon the Council to continue working on the proposal of the Commission for a new VAT own resource which could replace the existing own resource based on VAT ⁽²⁾.

⁽¹⁾ The UK correction in question was the one for the preceding year; see hereafter.

⁽²⁾ For details see Chapter 7.

2.3. The GNI-based resource

1) Definition

Since 1988, GNP/GNI-based payments also constitute own resources. These payments result from the application of a call rate — set so that total revenue balances total expenditure — to Member States' GNP/GNI bases.

Since 1988, this resource has been the cornerstone of the own-resources system for financing the EU budget, notably for the following reasons:

- The GNI-based resource provides the revenue required to cover expenditure in excess of the amount yielded by traditional own resources and VAT-based payments in any particular year. By implication, the GNI-based resource ensures that the EU budget is always balanced *ex ante*.
- The GNI-based resource guarantees stability in budget revenues in the medium term, within the overall ceiling for the total amount of own resources that may be collected for the EU budget (1.23 % of EU GNI). ORD 1988 initially created this ceiling, fixed it at 1.15 % of GNP in 1988 and raised it to 1.20 % in 1992, a level which was further raised by ORD 1994 from 1.21 % in 1995 to 1.27 % in 1999, later recalculated as 1.24 % of GNI in 2001 — see COM(2001) 801 final of 28 December 2001 and 1.23 % in 2010 ⁽¹⁾.

2) The call rate of the GNI-based resource

The GNI call rate is determined by the additional revenue needed to finance the budgeted expenditure not covered by the other resources (VAT-based payments, traditional own resources and other revenue). As in the case of VAT, a uniform call rate is applied to the GNI of each of the Member States.

To mitigate perceived imbalances of net contributions, corrections by means of lump sum reductions have been introduced. ORD 2007 introduced a temporary reduction in their GNI resource contribution for the Netherlands and Sweden for the period 2007–13 only, of an annual amount of EUR 605 million and EUR 150 million respectively (in constant 2004 prices). The cost of these lump sums is borne by all Member States in proportion to their GNI (including the Netherlands and Sweden, which thus finance their own lump sums).

Under ORD 2014, these lump sums will be replaced by new ones, which were agreed for the period 2014–20 only: EUR 695 million for the Netherlands, EUR 185 million for Sweden and EUR 130 million for Denmark (in constant 2011 prices). Austria will benefit from a phased-out lump sum of EUR 30, 20 and 10 million for 2014, 2015 and 2016 respectively. The lump sums are granted after the calculation of the UK correction and therefore have no impact on the UK correction itself.

⁽¹⁾ Under ORD 2007/436 the GNI base is established in accordance with the European System of Accounts (ESA 95). Since 1 January 2010, following a unanimous Council Decision, the ESA 95 GNI base for own resources purposes includes also the allocation of Financial Intermediation Services Indirectly Measured (FISIM). As a result the GNI was increased by around 1 % on average; however with a different impact on each Member State, and the own resources ceiling was reduced from 1.24 % of EU GNI to 1.23 % following a Commission communication in April 2010. Under the next ORD, the GNI base will be established on the basis of ESA 2010.

2.4 The UK correction

The budgetary imbalance correction mechanism in favour of the United Kingdom (UK correction) was introduced by the European Council in Fontainebleau in June 1984 and the resulting ORD 1985. The purpose of the mechanism was to reduce the UK budgetary imbalance between their contributions to the EU budget and EU expenditures allocated to the UK through a reduction in its contributions to the Union. The imbalance was initially calculated as the difference between the UK share in total EU (uncapped) VAT bases and the UK share in total EU expenditure allocated to Member States, this difference then being multiplied by the total EU expenditure allocated to Member States. The UK contribution was subsequently reduced by 66 % of the budgetary imbalance thus calculated.

The mechanism was subsequently modified by ORD 1988 to neutralise the introduction of the GNP/GNI-based resource and the capping of the VAT-based resource. The idea behind this so-called 'UK advantage' is to neutralise for the UK all changes to own-resources decisions since 1985, resulting in a global UK contribution to the Community budget as if the financing system created by the Fontainebleau European Council were still in force. ORD 1994 essentially confirmed the previous arrangements. ORD 2000 established new rules for the UK correction financing (further reducing the contribution of Germany, from two thirds as was the case from 1985 to 2001, to one quarter as of 2002, and extending this later reduction to the Netherlands, Austria and Sweden) and provided that certain windfall gains, resulting from changes extraneous to the UK correction mechanism but potentially benefiting the United Kingdom, should be neutralised (notably windfall gains related to the increase, from 10 % to 25 % as of 2001, in the share of traditional own resources retained as collection costs and windfall gains related to pre-accession expenditure in countries which joined the EU after 30 April 2004). ORD 2007 suppresses these later windfall gains from 2014 onwards and progressively introduces a new enlargement-related deduction from 2009 onwards. ORD 2014 provides that in essence the correction will continue unchanged for the period post-2013.

1) Calculation of the amount of the correction

The initial steps, pursuant to ORD 1985, consist of:

- (i) calculating the difference between:
 - the UK share of total EU (uncapped) VAT bases;
 - the UK share of total EU expenditure allocated to Member States;
- (ii) multiplying the difference thus obtained by total EU expenditure allocated to Member States;
- (iii) multiplying the result under (ii) by 0.66.

The result obtained under (iii) is called the 'original amount' of the UK correction.

Additional steps were later introduced, by subtracting the following elements:

- (iv) since 1988, from the result under (iii): the effect of the introduction, under ORD 1988, of the capping on VAT bases and of the GNP/GNI-based resource, namely the difference between:

- what the UK payments would have been in the absence of the GNP/ GNI resource and of the capping of VAT bases;
- the actual UK GNP/GNI- and VAT-based payments.

The difference referred to in step (iv) is called the 'UK advantage', since it corresponds to the (usually positive) effect for the UK following the reforms introduced by ORD 1988. By deducting this difference from the original amount of the UK correction, this effect is neutralised. The resulting amount is called the 'core UK correction'.

- (v) since 2001, from the result under (iii): the effect of the increase, from 10 to 25 %, in the share of traditional own resources (TOR) retained by Member States as collection costs. This effect, referred to as 'TOR wind-fall gains' is the result of the multiplication between:
- 20 % of the TOR collected, the percentage of 20 % being the ratio of the additional share of the TOR (15 %) retained as collections costs divided by the net TOR collected (75 %), and
 - the difference between the UK share in the total TOR collected and the UK share in EU (uncapped) VAT bases.

Introduced under ORD 2000, the increase in the share of the TOR retained by Member States as collection costs implies a shortfall in EU revenue that is made up through additional GNI-based payments. Since Member States' share of EU GNI is different from their share of traditional own resources, this affects the level of their overall contribution. According to a logic similar to that of the 'UK advantage', the effect on the overall UK contribution is being neutralised by deducting the above difference from the 'core UK correction'.

- (vi) over the period 2004–13, the amount of EU pre-accession expenditure to each country which joined the EU after 30 April 2004, in the last year before its accession is deducted from the total allocated expenditure, see (i) and (ii) above. These amounts are carried forward to subsequent years and adjusted annually by applying the EU GDP deflator.

From 2014 onwards, ORD 2007 removes the above deduction (vi) introduced under ORD 2000 and introduces, from 2009 onwards, a new enlargement-related deduction, see (vii) below.

Total allocated expenditure used for the calculation of the UK correction excludes expenditure in non-member countries (notably pre-accession expenditure in applicant countries) but includes, upon enlargement, EU expenditure allocated to new Member States. Accession of a new Member State therefore decreases the UK share in total allocated expenditure and increases total allocated expenditure, both leading to an increase in the UK correction. The above deduction from total allocated expenditure ensures that expenditure which is unabated before enlargement remains unabated after enlargement.

- (vii) since 2009, EU expenditure allocated to each Member State which joined the EU after 30 April 2004 except for agricultural expenditure originating from the EAGGF Guarantee

Section (Article 4(g) of Council Decision 2007/436/EC, Euratom) is deducted from total allocated expenditure, see (i) and (ii) above ⁽¹⁾. However, only 20 % of this expenditure was deducted in 2009 (i.e. 2008 correction), 70 % in 2010 (i.e. 2009 correction) and 100 % from 2011 (i.e. 2010 correction) onwards.

The above deduction aims at full UK participation in the financing of the costs of enlargement (except for agricultural expenditure). However, the accumulated additional UK contribution resulting from the above deduction could not exceed a ceiling of EUR 10.5 billion, in 2004 prices, during the period 2007–13. Even with the accession of Croatia in 2013 this ceiling did not need to be adjusted.

In order to be able to continue applying the ‘existing’ UK correction during the period covered by the ORD 2014, as was politically agreed, it is necessary to make yet another adjustment in the calculation. Unlike in previous periods, the rural development envelope for the period 2014–20 was established completely independently from the CAP first pillar and the cohesion envelopes. As regards the exclusion of the expenditure in the new Member States from the calculation base, a specific agreement needed to be found at the June 2013 European Council with respect to the breakdown of the rural development expenditures as this split effectively no longer exists: a table with notional percentage shares which will continue to be included in the calculation was published in the format of a European Council statement to the minutes.

The final amount of the UK correction is obtained by deducting from (iii) the elements (iv) and (v) and by deducting from total allocated expenditure, as used in steps (i) and (ii), the elements (vi) and (vii).

2) Financing the correction

The financing of the UK correction is distributed among Member States according to their shares in EU GNI. The United Kingdom is excluded from the financing of its own correction. From 1985, Germany’s contribution to financing the UK correction was limited to two thirds of its normal share. Since 2002, this has been limited to one quarter and extended to the Netherlands, Austria and Sweden.

This extension was introduced primarily in response to arguments by Austria, Germany, the Netherlands and Sweden that their EU budgetary burden was excessive and that they deserved more favourable budgetary treatment. An inevitable result of this arrangement is that the burden of financing the UK correction has now shifted to the remaining Member States, a group that includes those benefiting from the Cohesion Fund.

⁽¹⁾ This includes the share of rural development expenditure (EADRF) deemed to originate from the EAGGF Guarantee Section. The part originating from the EAGGF Guidance Section is deducted from allocated expenditure.

3. Other revenue

Other revenue is covered by Titles 4 to 9 of the general statement of revenue of the EU budget ⁽¹⁾.

Title 4 covers revenue accruing from persons working with the institutions and other EU bodies (taxes on salaries and pensions, and staff contributions to the pension scheme).

Title 5 covers revenue accruing from the administrative operation of the institutions, such as proceeds from the sale of property, from letting and hiring, from the supply of services and from bank interest.

Title 6 covers contributions and refunds in connection with Union agreements and programmes (contributions to Union programmes, repayment of miscellaneous expenditure, revenue from services rendered against payment, contributions under specific agreements, financial corrections, and revenue relating to the European Agricultural Guarantee Fund and the European Agricultural Fund for Rural Development).

Title 7 covers interest on late payments and fines (e.g. interest on late payment of own resources by Member States or fines on companies for infringing EU competition rules).

Title 8 covers revenue from EU borrowing and lending operations.

Title 9 covers miscellaneous revenue.

Other revenue is the result of the European Union's normal activities; this revenue bears witness to the EU's status as a legal entity and its power of independent action.

4. The budgetary logic of the financing of the European Union

4.1. Equilibrium *ex ante*

The EU budget is known as an expenditure budget, in that expenditure is estimated prior to the calculation of the revenue that will be needed to finance it. The budget is always in balance *ex ante*.

Recourse to the different sources of revenue is sequential, i.e. a series of successive balances is calculated.

First, the expected proceeds from other revenue and any estimated surpluses from the previous year are subtracted from the total forecast volume of expenditure. The remaining expenditure is financed by own resources.

Within the category of own resources, the estimated revenue from traditional own resources is deducted first. The next step is to calculate the amount of the VAT-based resource. The remaining amount of expenditure is financed by the GNI-based resource. The GNI-based resource is the 'residual' resource that provides the revenue required to cover expenditure in excess of the sum of all the other sources of revenue.

⁽¹⁾ The surplus available from the preceding financial year is recorded in Title 3 (Article 300). However, this surplus is itself mainly a consequence of the difference between the revenue outturn and expenditure in the previous year.

4.2. Balance for the year

The balance of the budgetary year is determined by the actual outturn of revenue and expenditure. A surplus is carried over to the following budgetary year, thus reducing the amount of own resources needed in that year by means of a lower call rate for the GNI resource. A deficit would be likewise carried over, increasing the rate of call of GNI needed to balance the budget *ex ante*. A deficit is, however, exceptional and has occurred only three times, in 1977, 1984 and 1986.

The precise rules for drawing up the balance of the financial year are laid down in Council Regulation (EC, Euratom) No 1150/2000 of 22 May 2000 ⁽¹⁾ and in Regulation (EU, Euratom) No 966/2012 of 25 October 2012.

The balance of a given financial year is made up of the difference between:

- (1) all the revenue collected in respect of that financial year, which means traditional own resources established and made available to the Commission, called and paid VAT-based and GNI-based resources, and proceeds from other revenue;
- (2) payments made against appropriations for that financial year increased by the amount of appropriations for the same financial year carried over to the following budgetary year.

To this difference is then added (or subtracted from it if the difference is negative) the net amount of appropriations carried over from the previous financial year that have been cancelled, together with some other items resulting from exchange rate variations.

The resulting surplus is usually included in an amending budget in the following year. Typically, the Commission tries to minimise the surplus proposing amendments to the budget of the ongoing year to reflect the most recent budget estimates.

4.3. VAT and GNI balances

Member States' VAT- and GNI-based payments are calculated using the VAT and GNI bases for the year in question, as forecast in the draft budget. This forecast is later revised once during the budgetary year in question and budgeted in an amending budget. Member States' payments are adjusted accordingly.

However, final data for the VAT and GNI bases of year *n* are only available towards the end of the following year. The difference between what Member States should have paid in year *n* according to the final bases and what they actually paid is called in at the end of year *n+1*. These VAT and GNI balances are calculated by the Commission and Member States have to make them available on the first working day of December. Further corrections to the final VAT and GNI bases can also be made in subsequent years, leading to additional balance adjustments, which are called together with the VAT and GNI balances for the previous year.

⁽¹⁾ Council Regulation (EC, Euratom) No 1150/2000 of 22 May 2000 implementing Decision 2007/436/EC, Euratom on the system of the European Communities' own resources (OJ L 130, 31.5.2000, p. 1).

Chapter 14

Expenditure by heading

1. Introduction

1.1. Adoption of the multiannual financial framework

The multiannual financial framework 2014–20 was formally adopted on 2 December 2013, with the adoption of Council Regulation (EU, Euratom) No 1311/2013 laying down the multiannual financial framework for the years 2014–20, and with the signature by the European Parliament, the Council and the Commission of the Interinstitutional Agreement on budgetary discipline, on cooperation in budgetary matters and on sound financial management. For full details of the negotiations, see Chapter 7.

1.2. Structure and ceilings of the multiannual financial framework 2014–20

The structure of the MFF 2014–20 is not very different to that of the 2007–13 framework, containing six headings. The main difference is that while Heading 1 remains sub-divided into two sub-headings ⁽¹⁾ — competitiveness and cohesion, Heading 3 is no longer sub-divided, but addresses security and citizenship together. These headings reflect the broad policy goals, as follows:

- Heading 1: Smart and Inclusive Growth

This heading is divided into two separate, but interlinked sub-headings:

Sub-heading 1a. Competitiveness for growth and jobs, encompassing expenditure on research and innovation, education and training, trans-European networks, social policy, the internal market and accompanying policies, as well as major infrastructure projects;

Sub-heading 1b. Economic, social and territorial cohesion, designed to enhance convergence of the least developed Member States and regions, to complement the EU strategy for sustainable development outside the less prosperous regions and to support inter-regional cooperation.

- Heading 2: Sustainable Growth: Natural Resources

This includes the common agricultural policy (including direct payments and market related expenditure, both placed under a sub-ceiling, and rural development), maritime affairs and fisheries, environment and climate action.

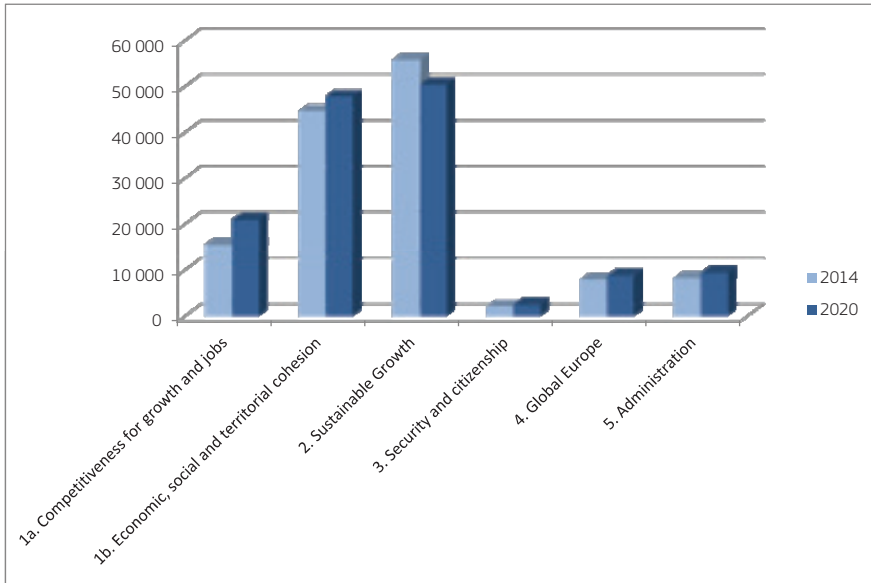
- Heading 3: Security and Citizenship

This heading includes asylum and migration, internal security (including border protection and police cooperation), justice, civil protection, public health and consumer protection, food safety, culture and media, information and dialogue with citizens.

⁽¹⁾ On the legal and budgetary distinction between headings, sub-headings and sub-ceilings, see Chapter 10.1.1.

Graph 14.1 shows how the structure in terms of commitment appropriations will evolve between 2014 and 2020 (in million euro at constant 2011 prices).

GRAPH 14.1 – *The structure of expenditure 2014–20*



2. Headings ⁽¹⁾

2.1. Sub-Heading 1a — Competitiveness for growth and jobs

The expenditure allocated under ‘Competitiveness for growth and jobs’ is at the heart of the drive to turn the EU into a smart, sustainable and inclusive economy, delivering high levels of employment, productivity and social cohesion. Many of the flagship initiatives set out in the Europe 2020 strategy are covered under this part of the budget, including ‘Innovation Union’, ‘Youth on the move’, ‘A resource-efficient Europe’, ‘An agenda for new skills and jobs’ and ‘An industrial policy for the globalisation era’. The EU budget to promote competitiveness for growth and jobs for 2014–20 comes to EUR 142.13 billion, i.e. 13.1 % of the total MFF ceiling.

1) Key Initiatives

Horizon 2020 — Horizon 2020 is the biggest EU Research and Innovation programme ever, with nearly EUR 80 billion of funding available over seven years. It promises more breakthroughs, discoveries and world firsts by taking great ideas from the lab to the market. Horizon 2020 is the framework programme implementing the Innovation Union, a Europe 2020

⁽¹⁾ Unless stated otherwise, figures provided in this section are all expressed in current prices and refer to the period 2014–20. The programmes of the 2014–20 multiannual financial framework, the amounts allocated to each of them and their legal bases (when adopted) may be found at the following link: http://ec.europa.eu/budget/mff/programmes/index_en.cfm

flagship initiative aimed at securing Europe's global competitiveness. By coupling research and innovation, Horizon 2020 is helping to achieve this with its emphasis on excellent science, industrial leadership and tackling societal challenges. The goal is to ensure that Europe produces world-class science, removes barriers to innovation and makes it easier for the public and private sectors to work together in delivering innovation. There are seven programme sections:

- **Excellent Science** — Activities under this pillar aim to reinforce and extend the excellence of the Union's science base and to consolidate the European Research Area in order to make the Union's research and innovation system more competitive on a global scale.
- **Industrial Leadership** — This pillar aims to speed up development of the technologies and innovations that will underpin tomorrow's businesses and help innovative European SMEs to grow into world-leading companies.
- **Societal Challenges** — Horizon 2020 reflects the policy priorities of the Europe 2020 strategy and addresses major concerns shared by citizens in Europe and elsewhere.
- **Spreading Excellence and Widening Participation** — Maximising investment in research and innovation will enable the European Research Area to function in a more streamlined and homogeneous way, allowing the individual strengths of each Member State to be optimised.
- **Science with and for Society** — The aim of this programme is to build effective cooperation between science and society, to recruit new talent for science and to pair scientific excellence with social awareness and responsibility.
- **European Institute of Innovation and Technology (EIT)** — The EIT is bringing real and lasting change to the European Union's innovation landscape, by creating new environments where higher education, research, public administrations and business work together to produce disruptive innovation.
- **Euratom** — Euratom is a complementary research programme for nuclear research and training.

Connecting Europe Facility (CEF) — With a budget of EUR 33 billion between 2014 and 2020, the Connecting Europe Facility will be a key instrument to promote growth, jobs and competitiveness through targeted infrastructure investment at European level. It will support the development of high-performing, sustainable and efficiently interconnected trans-European networks in the fields of transport, energy and digital services. The CEF is divided into three sub-programmes:

- **Energy** — An amount of EUR 5.85 billion will be made available for improving the trans-European energy infrastructure.
- **Digital** — An amount of EUR 1.14 billion will be provided to support fast and very fast broadband networks and for pan-European digital services (such as eID, eProcurement, eHealth, Europeana, eJustice etc.).
- **Transport** — This financing will act as 'seed capital' to stimulate further investment by Member States to complete difficult cross-border connections and links which might not

otherwise get built. The CEF will provide EUR 26 billion to support actions contributing to projects of common interest in accordance with the Union guidelines for the development of the trans-European transport network ⁽¹⁾.

Galileo — The Galileo programme is Europe's initiative for a state-of-the-art global satellite navigation system and positioning infrastructure specifically designed for civilian purposes, which can be used by a variety of public and private actors in Europe and worldwide. The fully deployed system will consist of 30 satellites and the associated ground infrastructure. Galileo will be inter-operable with GPS and GLONASS, the two other global satellite navigation systems. A total amount of EUR 7.1 billion is provided for years 2014–20.

Copernicus — With a contribution from the Union budget of EUR 4.3 billion, Copernicus is the European Earth Observation Programme and the successor of GMES (Global Monitoring for Environment and Security). The objectives of the Copernicus programme are to provide accurate and reliable information in the field of the environment and security, tailored to the needs of users and supporting other Union's policies, in particular relating to the internal market, transport, environment, energy, civil protection, cooperation with third countries and humanitarian aid. It builds on capabilities existing in Europe, complemented by new assets developed in common.

International Thermonuclear Experimental Reactor (ITER) — The ITER project aims to demonstrate fusion as a viable and sustainable source of energy by building an experimental fusion reactor as a major step towards the creation of prototype reactors or fusion power stations that are safe, sustainable, environmentally responsible and economically viable. This programme will contribute to the Europe 2020 strategy and in particular to its Innovation Union flagship initiative as the mobilisation of European high-tech industries, which are involved in the construction of ITER, should provide the EU with a global competitive advantage in this promising sector. The project brings together seven parties: the European Union, China, India, Japan, South Korea, Russia and the United States. A total amount of EUR 3.0 billion is provided for the years 2014–20.

Erasmus+ — It is the new EU programme for education, training, youth and sport. It aims at boosting skills and employability, and modernising education, training and youth work. The seven-year programme will have a budget of EUR 14.8 billion. This represents a 40 % increase compared to spending levels in the 2007–13 period and shows the EU's commitment to investing in these areas. Erasmus+ brings together seven existing EU programmes, and for the first time provides support for sport.

Competitiveness of Enterprises and Small and Medium-sized Enterprises (COSME) — The COSME programme aims at facilitating access to finance for small and medium-sized enterprises (SMEs), creating an environment favourable to SME creation and growth, encouraging an entrepreneurial culture in Europe, strengthening the sustainable competitiveness of EU enterprises, supporting the internationalisation of SMEs and improving their access to markets. The financial envelope for the implementation of the programme is set at EUR 2.3 billion for the seven-year programme, of which no less than 60 % would be allocated to financial instruments.

⁽¹⁾ Of which EUR 11.3 billion shall be transferred from the Cohesion Fund to be spent in line with the CEF Regulation exclusively in Member States eligible for funding from the Cohesion Fund.

Employment and Social Innovation (EaSI) — The Employment and Social Innovation programme will support Member States' efforts in the design and implementation of employment and social reforms at European, national as well as regional and local levels by means of policy coordination and the identification, analysis and sharing of best practices. The amount attributed to the EaSI programme is EUR 919 million. The new programme integrates and extends the coverage of three previous programmes: Progress (Programme for Employment and Social Solidarity), EURES (European Employment Services) and the European Progress Microfinance Facility.

Nuclear decommissioning — An amount of EUR 969 million has been assigned to the nuclear decommissioning programme, which aims at closing down old nuclear power plants and ensures adequate handling of contaminated elements and locations. The nuclear power plants concerned are V-1 Jaslovské Bohunice in Slovakia, Ignalina in Lithuania and Units 1 and 2 — Kozloduy in Bulgaria.

Customs, Taxation and Fight against Fraud — The Customs 2020 and Fiscalis 2020 programmes support cooperation between EU countries' customs and tax authorities, promote networking and knowledge-sharing and fund a highly secured communication network connecting national customs and tax administrations. In the field of the fight against fraud, the Pericles 2020 programme aims at combating euro-counterfeiting in Europe and worldwide, and the Hercule III programme is dedicated to fighting fraud, corruption and any other illegal activities affecting the financial interests of the EU. The total amount dedicated to these initiatives is EUR 908 million.

2) *Financial Instruments* ⁽¹⁾

Scarce public money increases the need to unlock other sources of finance and thus generate a leverage effect for the EU budget compared to straight grant funding. This is the purpose of financial instruments, such as loans, guarantees, equity and other risk-sharing instruments, which can be used more widely in the 2014–20 framework. They will be implemented in cooperation with the European Investment Bank (EIB), the European Investment Fund (EIF) and national promotional banks. The purpose of these instruments is to address specific market failures in areas such as financing for SMEs, research and development projects, energy efficiency and key infrastructure.

For example, the Commission's new SME Initiative will support bank lending to SMEs in Member States particularly affected by the financial crisis through partial loan guarantees and securitisation instruments.

Another innovative instrument, the Project Bond initiative, provides an alternative, non-bank financing channel for key infrastructure projects such as railway lines, motorways and energy transmission networks. It thus opens up these projects for institutional investors, such as pension funds and insurance companies, seeking stable, long-term cash flows, while developing an alternative to traditional bank loans as a source of finance.

⁽¹⁾ See Chapter 17 on the definition of and new regulatory framework applying to financial instruments.

Financial instruments will be used in programmes such as COSME (facilitating access to finance for SMEs), Horizon 2020 (Research & Innovation), Erasmus+ (for its loan guarantee scheme) and the Connecting Europe Facility (infrastructure).

2.2. Sub-Heading 1b — Economic, Social and Territorial Cohesion

The EU's cohesion policy aims at strengthening the economic, social and territorial cohesion of the enlarged Union in order to promote balanced and sustainable development. It is designed to reduce disparities between the levels of development of the various regions and Member States and the specific difficulties of the least favoured regions or islands. Cohesion support is implemented by the Commission and the Member States under shared management. The aid is intended to complement rather than replace structural expenditure by a Member State.

Cohesion policy has undergone significant development over time. While the European Social Fund (ESF) and the European Regional Development Fund (ERDF) were set up in 1958 and 1975 respectively, it was the Single European Act in 1986 that laid the basis for a genuine cohesion policy. One of the objectives of the policy was to counterbalance the effects of the completion of the internal market on less developed Member States. While the budget for cohesion amounted to about 17 % of the first financial framework, the EU cohesion budget for 2014–20 is EUR 351.8 billion (including EUR 1.2 billion for technical assistance), about 34 % of the total EU budget.

1) *Key initiatives*

There are two main goals for Cohesion Policy:

- Investment for growth and jobs in Member States and regions, to be supported by the financial instruments (Funds);
- European territorial cooperation, to be supported by the ERDF.

For the programming period 2014–20 cohesion policy is refocused for maximum impact on growth and jobs and new features are introduced notably to focus the policy on performance ('performance reserve') and attainment of the objectives of the Europe 2020 strategy for smart, sustainable and inclusive growth and to create a closer link between cohesion policy and the economic governance of the Union ('macroeconomic conditionality').

Resources for the Investment for growth and jobs goal are allocated for the period 2014–20 among three categories of regions:

- Less developed regions (EUR 182.2 billion or 52 % of total cohesion policy allocation 2014–20), whose GDP per capita is less than 75 % of the average GDP of the EU-27;
- Transition regions (EUR 35.4 billion or 10 % of total cohesion policy allocation 2014–20), whose GDP per capita is between 75 % and 90 % of the average GDP of the EU-27;
- More developed regions (EUR 54.4 billion or 15 % of total cohesion policy allocation 2014–20), whose GDP per capita is above 90 % of the average GDP of the EU-27.

The Cohesion Fund (EUR 63.4 billion or 18 % of total cohesion policy allocation 2014–20) supports those Member States, whose GNI per capita is less than 90 % of the average GNI of

the EU-27. EUR 11.3 billion (EUR 10 billion in 2011 prices) of the Cohesion Fund is transferred to the Connecting Europe Facility to be spent for transport infrastructure projects exclusively in Member States eligible for funding from the Cohesion Fund.

The resources for the Youth Employment Initiative consist of EUR 3.2 billion (EUR 3 billion in 2011 prices) from the specific allocation and at least EUR 3.2 billion from European Social Fund targeted investment.

The support from the Structural Funds for aid to the most deprived persons under the Investment for growth and jobs goal is set at EUR 3.8 billion which includes additional support decided on a voluntary basis by Member States.

A further 2.75 % of cohesion policy allocation goes to territorial cooperation at cross-border, transnational and inter regional levels. EUR 9.6 billion is available for European territorial cooperation.

Financial allocations for specific Member States are calculated on the basis of objective criteria such as the eligible population, regional prosperity, national prosperity, surface area and unemployment.

2) Funds and financial instruments ⁽¹⁾

Cohesion policy including the Fund for European Aid to the Most Deprived is implemented through four Funds:

- The European Regional Development Fund operates in all Member States and co-finances infrastructure and productive investment together with other measures supporting regional and local development.
- The Cohesion Fund co-finances trans-European networks in the area of transport infrastructure and environment projects, including areas related to sustainable development and energy which presents environmental benefits in Member States in which GNI per capita is less than 90 % of the average GNI of the EU-27.
- The European Social Fund operates in all Member States and supports measures to promote high levels of employment and job quality, improve access to the labour market, support mobility of workers and facilitate their adaptation to industrial change. A Youth Employment Initiative has been created to support the fight against youth unemployment in the most effected regions.
- The Fund for European Aid to the Most Deprived supports national schemes whereby food and/or basic material assistance and social inclusion activities are provided to the most deprived persons through partner organisations selected by Member States.

The new policy also encourages the increased use of financial instruments to give SMEs more support and access to credit. Loans, guarantees and equity/venture capital will be supported by EU funds through common rules for all funds, a broadening of their scope and providing incentives (higher co-financing rates). This emphasis on loans rather than grants should improve project quality and discourage subsidy dependence.

⁽¹⁾ See Chapter 17 on the definition of and new regulatory framework applying to financial instruments.

2.3. Heading 2 — Sustainable Growth: Natural Resources

The European Union has a strong mandate and policy responsibility in the fields of agriculture and rural development, maritime and fisheries policy, and the environment. The Union's budget for Heading 2 comes to EUR 420.0 billion, which is about 38 % of the total. Funding is provided mainly to agriculture, rural development, fisheries and environment projects. By far the most important policy in terms of funding is the Common Agricultural Policy (CAP) with its two pillars: (1) Market-related expenditure and direct payments financed by the European Agricultural Guarantee Fund (EAGF) and (2) Rural Development financed by the European Agricultural Fund for Rural Development (EAFRD), with around 74 % of the money going to EAGF.

In terms of funding mechanisms, around 94 % of the budget for the EAGF will be channelled through direct payments to farmers subject to 'cross-compliance', which represents the compulsory basic layer of environmental requirements and obligations to be met in order to receive full funding. Most of the remaining funds will be used for interventions aimed at stabilising agricultural markets for various products.

Financing for rural development takes the form of co-financing national and/or regional rural development programmes proposed by the Member States. While overall priorities are agreed at EU level, there is plenty of scope for Member States and regions to design their programmes so they reflect an appropriate balance between the three main objectives of the fund.

With regard to fisheries, the European and Maritime Fisheries Fund (EMFF) not only replaces the previous 'European Fisheries Fund' (EFF) but also integrates all other measures in the field of maritime affairs and fisheries, except 'Sustainable Fisheries Agreements' (SFAs) and compulsory contributions to international organisations and 'Regional Fisheries Management Organisations' (RFMOs), which are not included in the financial envelope of the EMFF. The new fund will be used mainly to co-finance projects, along with national funding.

1) Key initiatives

For more than 20 years, starting in 1992, the **Common Agricultural Policy (CAP)** has been through successive reforms which have increased market orientation for agriculture while providing income support and safety net mechanisms for producers, improved integration of environmental requirements and reinforced support for rural development across the EU. The new policy reform continues along this reform path in response to the challenges facing the sector, many of them external to agriculture:

- Economic factors (food security and globalisation, declining rate of productivity growth, price volatility, pressure on production costs due to high input prices and the deteriorating position of farmers in the food supply chain),
- Environmental factors (resource efficiency, soil and water quality, threats to habitats and biodiversity, climate change), and
- Territorial factors (rural areas faced with demographic, economic and social developments including depopulation and relocation of businesses).

This translates into three long-term CAP objectives: (a) viable food production, (b) sustainable management of natural resources and climate action, and (c) balanced territorial development.

The most important elements in the 2014 CAP reform package are the following:

- End of all existing restrictions on production volumes for sugar, dairy and the wine sector allowing farmers to respond to growing world demand.
- Reinforced legal framework for producer organisations/groups (collective bargaining and delivery contracts) accompanied by measures to facilitate producer cooperation under both pillars of the CAP.
- Better harmonised and more responsive market measures to deal with the potential threats of market volatility and disturbances, in particular through safety-net mechanisms, flexible exceptional measures and the creation of a new crisis reserve under the EAGF, while offering a new risk-management toolkit under the EAFRD, including insurance schemes for crops, animals and plants as well as mutual funds and an income stabilisation tool.
- Improved sustainability by the combined and complementary effects of various instruments: simplified and more targeted cross-compliance, a compulsory greening component in the direct aid regime and co-financing of voluntary measures beneficial to the environment and climate change under rural development.
- New design of the system of direct payments with a compulsory greening component, the possibility for additional support for young farmers under the first pillar complementing the start-up aid under the second pillar, a redistributive element (capping for large farms and/or top-up for first hectares of small/medium-sized ones) and a simplified support scheme for small farms, as well as the possibility for granting limited coupled support to secure the future of potentially vulnerable sectors and for areas with natural constraints.
- Increased flexibility between the two pillars of the CAP with the possibility for transferring funds in both directions, depending on the specific situation and priorities in the Member States.

Over the last two decades the share of the EAGF in the EU budget has fallen from 70 % to less than 40 %. Over the 2014–20 period it declines to 29 % of the EU budget. The global amount for this period is EUR 312.7 billion (without taking into account the effect of transfers to rural development).

Rural development constitutes the second pillar of the CAP. The rural development policy is focused on three main objectives: (1) Competitiveness of agriculture; (2) Sustainable management of natural resources and climate action, and (3) Balanced territorial development of rural economies and communities including the creation and maintenance of employment.

The rural development policy is implemented through co-financed national and/or regional rural development programmes for a seven-year period proposed by the Member States in the framework of their 'envelope' under the European Agricultural Fund for Rural Development. Member States will have to build their programmes based upon at least four of six common EU priorities: innovation; competitiveness; preserving ecosystems, including Natura 2000; resource efficiency; and social inclusion.

The global amount available for the EAFRD is EUR 95.6 billion (before net-transfer from EAGF and including technical assistance).

EUR 7.4 billion are available for **fisheries and maritime affairs**, around 86 % of which will be devoted to the European Maritime and Fisheries Fund (EMFF). The EMFF aims at achieving the objectives of the reformed Common Fisheries Policy (CFP) and of the Integrated Maritime Policy, which are: (i) promotion of sustainable and competitive fisheries and aquaculture; (ii) fostering the development and implementation of the Union's IMP, in a complementary manner to the cohesion policy and to the CFP; (iii) promotion of balanced and inclusive territorial development of fisheries areas (including aquaculture and inland fishing); (iv) contribution to the implementation of the CFP. Activities financed outside the EMFF are the 'Sustainable Fisheries Agreements' (SFAs) with third countries and the compulsory contributions to international organisations and 'Regional Fisheries Management Organisations' (RFMOs).

The **European environment programme (LIFE)**, now entering in its third generation, should be used as a catalyst to promote the implementation and integration of environment and climate objectives in other policies and Member State practices, including mainstreaming. The new LIFE programme comprises two sub-programmes: (1) The Environment sub-programme covering the following thematic priorities for funding: Nature and Biodiversity; Water including the marine environment; Waste; Resource efficiency including soil and forest and green and circular economy; Environment and Health including chemicals and noise; Air Quality and Emissions including the urban environment and, finally, Information and Governance. (2) The Climate Action sub-programme covering the following priorities areas: Climate Change Mitigation contributing to the reduction of greenhouse gas emissions; Climate Change Adaptation supporting efforts leading to increased resilience to climate change and, thirdly, Governance and Information. The global amount for 2014–20 is EUR 3.5 billion.

2.4. Heading 3 — Security and Citizenship

Pursuant to Article 3(2) of the Treaty on European Union, the Union shall offer its citizens an area of freedom, security and justice without internal frontiers. In a context of ever stronger inter-dependence brought about by globalisation, responsibilities in that area include the management of the Union's external borders, the development of a common asylum area, cooperation between law enforcement agencies and judicial authorities to prevent and fight terrorism and crime, respect for fundamental rights and a global approach to drug issues. Under this heading are also financed programmes that support actions promoting active citizenship, health and consumer protection, programmes, fostering European culture and diversity and an instrument for major emergencies to increase the efficiency and effectiveness of civil protection. The total amount available for Security and Citizenship actions is EUR 17.73 billion.

1) Key initiatives

Asylum and Migration Fund — The Asylum and Migration Fund will focus on migration flows and the integrated management of migration. It will support actions addressing all aspects of migration, including asylum, legal migration, integration and the return of irregularly staying non-EU nationals. The total amount available for the programmes under this fund is EUR 3.14 billion.

Internal Security Fund — The Internal Security Fund will support the implementation of the Internal Security Strategy and the EU approach to law enforcement cooperation, including the management of the Union's external borders. It will also cover the development of new IT systems, such as the future entry/exit system and the Registered Traveller Programme. The total amount available for the Internal Security Fund is EUR 3.76 billion.

Creative Europe — The aim of the Creative Europe programme is supporting European media and the cultural and creative sector and enabling them to increase their contribution to growth and jobs. The programme will support tens of thousands of artists, cultural professionals and cultural organisations in the performing arts, fine arts, publishing, film, TV, music, interdisciplinary arts, heritage and the video-games industry, allowing them to operate across Europe, to reach new audiences and to develop the skills that are needed in the digital age. By helping European cultural works to reach new audiences in other countries, the new programme will also contribute to safeguarding and promoting Europe's cultural and linguistic diversity. The total amount available for Creative Europe over the period is EUR 1.46 billion.

Food safety — Food safety measures financed from the Union's budget will contribute to securing a high level of health for humans, animals and plants all along the food chain by supporting, for example, risk-based rules to strength the control and eradication of animal diseases and plant pests. They will also provide a high level of protection and information to consumers whilst taking into account the environment, competition, growth and jobs. The programme will also aim at improving the effectiveness of official controls and other official activities carried out by the Member States to ensure the correct application of EU agri-food chain rules. The amount foreseen for these measures is EUR 1.9 billion.

Civil Protection Mechanism — The EU Civil Protection Mechanism within the Union aims to strengthen the cooperation between the Union and the Member States and facilitates coordination in the field of civil protection in order to improve the effectiveness of systems for preventing, preparing for and responding to natural and man-made disasters. The financial envelope for the implementation of the Union Mechanism is EUR 223.8 million.

Consumer Programme — The Consumer programme is placing consumers at the centre of the Single Market and empowering them to participate actively in the market and make it work for them. Actions will focus on: monitoring and enforcing safety; information and education initiatives to make consumers aware of their rights, delivering legislation aimed at enhancing consumer rights and enforcement action to see where consumer rights are being compromised or denied. The programme will run from 2014–20 with a budget of EUR 188.8 million.

Europe for Citizens — The Europe for Citizens programme aims at supporting activities to increase awareness and citizens' understanding of the EU, its values and history, such as the remembrance of Europe's past and partnerships between cities (town-twinning). The programme will also help people to become more engaged in civic and democratic activities through debates and discussions on EU-related issues. The total amount of the programme is EUR 185.5 million.

Health for Growth — The Health for Growth programme aims to complement, support and add value to the policies of the Member States to improve the health of EU citizens and reduce health inequalities across the EU. By promoting health, encouraging health

innovation, increasing the sustainability of health systems and responding effectively to cross-border health threats, the new programme follows the principles and objectives set in the EU Health Strategy. It also builds on the achievements of the previous health programmes and brings forward the EU 2020 Strategy. The total amount dedicated to the programme is EUR 449.4 million.

Justice Programme — The Justice programme shall contribute to the further development of a European area of justice based on mutual recognition and mutual trust, in particular by promoting judicial cooperation in civil and criminal matters. This will help in ensuring proper access to justice for people and businesses in cross-border legal cases in Europe and support EU actions to tackle drugs and crime. An amount of EUR 377.6 million is budgeted for the programme.

Rights, Equality and Citizenship — The programme will help to make people's rights and freedoms effective in practice by making them better known and more consistently applied across the EU. It will also promote the rights of the child, the principles of non-discrimination (racial or ethnic origin, religion or belief, disability, age or sexual orientation) and gender equality (including projects to combat violence against women and children). The total amount of the programme is EUR 439.5 million.

2.5. Heading 4 — Global Europe

Global Europe is the umbrella title covering the external actions of the Union's budget. The EU has allocated EUR 66.3 billion for 2014–20, i.e. 6.1 % of its total budget, for the external projection of its policies, as compared to 5.7 % for the 2007–13 period.

In accordance with the EU Treaties, all external actions are closely coordinated with the activities of the European External Action Service (EEAS) and many projects are implemented through the EU delegations in third countries.

The main geographic and thematic instruments of the EU's external action have been revised for the 2014–20 period. This concerns notably the Instrument for Pre-accession Assistance (IPA II), the European Neighbourhood Instrument (ENI), the Development Cooperation Instrument (DCI), the European Instrument for Democracy and Human Rights (EIDHR), the former Instrument for Stability (IFS), now renamed to the Instrument contributing to Stability and Peace (IcSP) and the Instrument for Nuclear Safety Cooperation (INSC).

These revised instruments provide continuity with the activities covered in the 2007–13 MFF, but they are much simplified, and therefore expected to be more efficient than their predecessors. Due to their more flexible nature, they are better capable of adapting to the changing circumstances that prevail in the external actions environment.

In addition to the revised financing instruments, a new instrument has also been created — the Partnership Instrument (PI) — in order to complement the current array of instruments. The PI is the successor of the financing instrument for cooperation with industrialised and other high income countries (ICI/ICI+). It is an instrument with a truly global geographical scope complementing other thematic and geographic financial instruments. Its overarching objective is to advance and promote EU and mutual interests. The EU will thus benefit from and extend the

external reach of the economic actors within its own internal market, promoting sustainable economic development and job creation also within the EU.

Moreover, following the completion of the precursor pilot projects, the EU Aid Volunteers initiative is set up in order to directly engage EU citizens in the delivery of humanitarian aid and is funded as from 2014.

Finally, the four main geographic instruments of heading 4 — IPA, ENI, DCI and PI — will also contribute to the international dimension of the new Erasmus+ programme.

Heading 4 also includes a number of activities for which the legal bases do not have to be updated as they are either ad-hoc Decisions or not time-bound. These include Humanitarian Aid and the Common Foreign and Security Policy (CFSP) as well as macro-financial assistance — which is an instrument for balance-of-payments support — and the EU budget guarantee to, notably, the European Investment Bank's financing operations outside the Union. The guarantee from the EU budget is underpinned by the Guarantee fund for external actions.

Regarding development assistance it should be noted that the European development aid policy is also channelled through the European Development Fund (EDF), which is an important part of external policy but is financed as a separate instrument and outside the general budget. The EDF covers development cooperation with members of the African, Caribbean and Pacific Group of States ('ACP States') as well as to the Overseas Countries and Territories (OCTs). For more details on the EDF, see Chapter 19.

The Financial Regulation also allows the Member States and other bodies to supplement the budgetary funds allocated to external policy instruments by way of contributions to EU Trust Funds.

1) Key Initiatives

The Instrument for Pre-Accession Assistance (IPA II) — The general objective of the pre-accession assistance is to support the EU's enlargement policy, i.e. to help the aspirant countries in adopting and implementing the reforms required to comply with EU values, rules, standards, policies and practices, with a view to EU membership.

IPA II aims to implement the assistance in a more strategic and coherent way compared to the past, concentrating the funding on key reforms. Core themes will be democracy and the rule of law, competitiveness and growth, including a new approach to economic governance with a focus on tackling the economic fundamentals first. An important change is the introduction of a sector-based approach, i.e. a logic for financing sector policy strategies instead of individual projects, including a broader use of budget support.

Financial assistance is now available to candidate as well as potential candidate countries, irrespective of their status. Eligible for IPA II are the Western Balkans (Albania, Bosnia and Herzegovina, Kosovo ⁽¹⁾, Montenegro, Serbia and the former Yugoslav Republic of Macedonia), Turkey and Iceland. The global amount for 2014–20 is EUR 11.7 billion.

⁽¹⁾ This designation is without prejudice to positions on status, and is in line with UNSCR 1244/1999 and the ICJ Opinion on the Kosovo declaration of independence.

The European Neighbourhood Instrument (ENI) — This instrument is the basis for the EU's engagement with its neighbours. The policy offers the neighbouring countries a privileged relationship with the EU, building upon mutual commitments to the values and principles of democracy and the respect for human rights, rule of law, good governance, market economy principles and sustainable development, including action to fight climate change. The policy also provides for political association and deeper economic integration, increased mobility and enhanced people-to-people contacts.

The partner countries within the scope of the ENP are those in the southern and eastern Mediterranean, including Palestine, and six Eastern partners: Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine. The relationship with Russia is not covered by the ENP, but Russia may benefit from — and is also expected to co-finance — cross-border and multi-country programmes.

The ENP enshrines the key principle of differentiation, so that support provided may be differentiated in form and amounts according to the partner country's commitment to reforms and its progress in implementing these reforms. The long-term objective is to have Association Agreements or similarly comprehensive Agreements in force, and Action Plans or similar documents adopted by 2020 with as many of the 16 ENI countries as possible. The global amount for 2014–20 is EUR 15.5 billion.

The Development Cooperation Instrument (DCI) — The primary and overarching objective of the DCI is the reduction and in the longer term, the eradication of poverty. In this context, the EU and its Member States have reaffirmed their commitment to help achieve the Millennium Development Goals (MDGs) by 2015. The DCI will also contribute to the achievement of other objectives of EU external action, in particular: (i) Fostering sustainable economic, social and environmental development, and (ii) Promoting democracy, the rule of law, good governance and respect for human rights. The Instrument is divided into Geographic and Thematic Programmes. The geographical programmes will support actions in Latin America, Asia, Central Asia, the Middle East (Iran, Iraq and Yemen) and South Africa. The programmes distinguish between regional and bilateral cooperation, the latter focusing on those partner countries which need the most assistance.

Geographic programmes encompass cooperation with partner countries and regions determined on a geographical basis. They cover five regions, namely Latin America, Asia, Central Asia, the Middle East DCI countries (Iran, Iraq and Yemen) and South Africa, supporting various actions in order to achieve the mentioned objectives of the development cooperation policy. The measures taken vary according to the specific needs of each country, taking into account its specific situation. A principle of differentiation will be applied meaning that bilateral development assistance would be provided to those partner countries which need it the most, and lack the required financial capacities for their own development.

The thematic programmes, which have worldwide reach, include programmes on global public goods and challenges that should strengthen cooperation in the areas of environment and climate change, sustainable energy, human development, food security and sustainable agriculture as well as migration and asylum. Fighting climate change and protecting biodiversity are key priorities within the global public goods and challenges programme. In addition,

a thematic programme on 'Civil Society Organisations' and 'Local Authorities' in development will finance initiatives in the area of development by or for such organisations.

Finally, a **Pan-African programme** will provide support for the objectives, initiatives and activities agreed in the Joint Africa-EU Strategy in the areas of: peace and security, democratic governance and human rights, trade, regional integration and infrastructure (including transport), MDGs, energy, climate change and environment, migration, mobility and employment, science, information society and space, as well as cross-cutting issues. The Pan-African programme will further promote complementarity and consistency with other financial instruments of the Union's external action, notably the European Development Fund (EDF) and the European Neighbourhood Instrument (ENI). The global amount for 2014–20 is EUR 19.7 billion.

The Partnership Instrument (PI) — The PI is a new instrument which replaces the Financing Instrument for Cooperation with Industrialised and other high income countries and territories (ICI/ICI+), which has been the EU's main non-official development assistance vehicle for collaboration with developed countries.

The specific objectives are to support the Union's bilateral, regional or inter-regional cooperation partnership strategies, to implement the international dimension of the EU 2020 strategy, to improve market access and develop trade, investment and business opportunities for European companies and to support public diplomacy, people-to-people contacts, education/academic/think tank cooperation and outreach activities to promote the Union's values and interests. The global amount for 2014–20 is EUR 1.0 billion.

The European Instrument for Democracy and Human Rights (EIDHR) — This instrument reflects the specific Treaty mandates relating to the development and consolidation of democracy and the rule of law, and respect for human rights and fundamental freedoms. It addresses these issues mainly in partnership with civil society and independently from the consent of third country governments and other public authorities. This independence facilitates cooperation with civil society and allows for interventions at international level which are neither geographically linked nor crisis-related, and which require a transnational approach.

The EIDHR supports, inter alia, actions encouraging the ratification of international human rights conventions, aiming for an additional 10 such ratifications per year. The Commission strives to support around 300 Human Rights Defender cases a year. The instrument also supports and consolidates democratic reforms in third countries, by enhancing participatory and representative democracy and strengthening the overall democratic cycle. It provides the necessary framework to support independent EU Election Observation Missions, which contribute to democratic processes in third countries. The global amount for 2014–20 is EUR 1.3 billion.

The Instrument contributing to Stability and Peace (IcSP) (former Instrument for Stability (IfS)) — This instrument is designed to provide an adequate response both to instability and crises and to longer-term challenges with a stability or security aspect. It complements the Pre-Accession, European Neighbourhood and Development Cooperation instruments as well as Humanitarian aid, and provides assistance designed to establish the necessary conditions for implementing policies supported by the IPA, ENI and DCI.

The IcSP contributes to increasing EU's ability to preserve peace and strengthen international security through interventions in crisis situations at all stages of the conflict cycle. It also foresees actions in the area of conflict prevention, preparedness and peace building through the development of partnerships with peace-building stakeholders including civil society.

The EU addresses global and regional trans-border challenges with a security or stability dimension arising in third countries, including issues such as organised crime (including drugs trafficking routes and illegal trafficking of human beings), countering terrorism, actions against the spread of Weapons of Mass Destruction, as well as the security of critical infrastructure, countering cybercrime and Chemical, Biological, Radiological or Nuclear (CBRN) risk mitigation. The global amount for 2014–20 is EUR 2.3 billion.

The Humanitarian Aid Instrument — Humanitarian aid activities will continue under the existing Regulation on humanitarian aid as a legal basis. Humanitarian aid activities will continue to fund assistance, relief and protection in complex and possibly long-standing crisis situations, including 'forgotten crises', in the most vulnerable countries (especially in Africa), as well as to provide aid to regions affected by the consequences of natural disasters such as cyclones/hurricanes, droughts, earthquakes and floods. Efforts will be directed to building resilience amongst communities recurrently affected by natural and man-made disasters. The global amount for 2014–20 is EUR 6.6 billion.

The Union Civil Protection Mechanism (CPM) — The Mechanism aims at helping Member States to ensure a rapid, cost-effective and efficient mobilisation of European civil protection assistance in case of major emergency in the EU and in third countries. The global amount for 2014–20 is EUR 0.1 billion.

The Emergency Aid Reserve (EAR) — The Emergency Aid Reserve is set aside for major unforeseen natural or man-made crises and conflicts, and is one of the special instruments, outside the ceilings of the MFF headings. It is mobilised through budgetary transfers. The global amount for 2014–20 is EUR 2.2 billion.

The Common Foreign and Security Policy (CFSP) — CFSP activities will continue to support EU's international role in conflict resolution and stabilisation activities in Kosovo, Afghanistan, Georgia, as well as the Middle East, Africa and other conflict regions of the world. The CFSP missions require close collaboration with the EEAS and the EU delegations. CFSP expenditure is based on Council Decisions on the basis of Title V of the EU Treaty. The global amount for 2014–20 is EUR 2.3 billion.

Macro-financial Assistance — Macro-financial Assistance (MFA) is an instrument for economic stabilisation, exceptional in nature and mobilised on a case-by-case basis, to help the recipient country deal with short-term balance-of-payments difficulties. It is also a driver for structural reforms in the beneficiary neighbouring countries, in line with the European Union's pre-accession and neighbourhood policies. The global amount for 2014–20 is EUR 0.6 billion.

The Guarantee fund for External Actions — The Guarantee Fund was established in order to shield the EU budget in the event of a default on loans granted or guaranteed by the European Union. The lending operations covered by the Guarantee Fund for External Actions relate to three different instruments which benefit from a guarantee from the EU budget: European

Investment Bank (EIB) external loans and loan guarantees, Euratom external lending and EU macro-financial assistance loans to third countries. More than 95 % of the total outstanding amount covered by the Guarantee Fund concerns guarantees issued with respect to loans and loan guarantees granted for projects in third countries by the EIB. The Guarantee Fund is provisioned once a year from the EU budget in order to ensure that it corresponds to 9 % of net outstanding loan disbursements. The global amount for 2014–20 is EUR 1.2 billion.

Support to the Turkish Cypriot community (TCC) — The support to the Turkish Cypriot community is provided under Council Regulation No 389/2006 (the Aid Regulation) with the objective of facilitating the reunification of Cyprus through various measures. EU support concerns, for example, actions for rural development, improvement of infrastructure (such as wastewater treatment), reconciliation and confidence building measures such as the support to the Committee on Missing Persons, and scholarships in EU Member States for Turkish Cypriot students. The TAIEX facility (Technical Assistance and Information Exchange) is also used for the preparations for the application of the EU *acquis* immediately following any political settlement for reunification. The global amount for 2014–20 is EUR 0.2 billion.

The EU-Greenland Partnership — The partnership programme with Greenland has as its main objective to assist Greenland in addressing its major challenges. It focuses in particular on reinforcing the capacity of the Greenlandic administration to better formulate and implement national policies especially in new areas of mutual interest. The global amount for 2014–20 is EUR 0.2 billion.

The Instrument for Nuclear Safety and Cooperation (INSC) — The assistance provided to third countries in the nuclear sector (focusing mainly on promotion of an effective nuclear safety culture) will continue through the INSC. The global amount for 2014–20 is EUR 0.2 billion.

The European Voluntary Humanitarian Aid Corps EU Aid Volunteers (EUAV) — This is a new programme as from 2014. It is intended as a framework, which will comprise: the development of standards for volunteers and for their management and deployment; certification of sending and hosting organisations; identification and selection of volunteers and their training; and maintaining a register of EU aid volunteers. Activities will also include actual deployment of EU aid volunteers in third countries and capacity-building of the hosting organisations. The global amount for 2014–20 is EUR 0.1 billion.

2.6. Heading 5 — Administration

Administrative expenditure for all institutions accounts for approximately 6 % of the overall EU budget, covering expenditure on active and retired staff, buildings, offices, equipment, furniture, European schools, missions or conference and meeting costs. Out of these appropriations approximately 39 % relate to the Commission, 42 % to the other institutions and bodies (European Parliament, European Council and Council, Court of Justice of the European Union, Court of Auditors, European Economic and Social Committee, Committee of the Regions, European Ombudsman, European Data Protection Supervisor, and European External Action Service) and the rest to Pensions and European Schools. The ceiling for administrative expenditure has been revised downwards by 5 % in real terms between the last year of the previous financial

framework (2013) and 2014, thus ensuring budgetary discipline for the EU and reflecting the particular budgetary pressure that Member States currently face at national level. The expenditure ceiling for administrative expenditure for all Institutions is set at EUR 69.6 billion for 2014–20, i.e. 6.4 % of total expenditure.

In this context of strong budgetary constraints, the IIA accompanying the MFFR foresees a 5 % reduction in staffing levels for all Institutions, bodies and agencies over a five-year period. Furthermore, a freeze of salaries applies for the years 2013 and 2014.

After a zero-growth of human resources i.e. for establishment plan posts and appropriations for external personnel from 2010 until 2012, the Commission has already proceeded to two successive reductions of 1 % in its staffing levels in the 2013 and 2014 budgets ⁽¹⁾, and will continue until reaching the 5 % target set in the IIA. This takes place in a context of increased tasks entrusted to the Commission, requiring a continuous adaptation and pursuit of efficiency gains.

2.7. Heading 6 — Compensations

Heading 6 (Compensations) is temporary and includes some compensation amounts related to the enlargement of the Union. Compensations, provided for in the accession Treaties, ensure that new Member States retain a positive budgetary balance during the first three years of accession as compared to the year prior to accession. For Croatia, these compensations were fixed at EUR 75 million in 2013, and EUR 28.6 million in 2014, that is a total of EUR 103.6 million over 2013—14. Croatia will no longer receive compensations as of 2015.

⁽¹⁾ Excluding the limited increase in the number of staff to cope with the accession of Croatia.

Part 5
Implementation of the Union's annual budget



Chapter 15

Implementation

1. Assignment of implementing powers

1.1. The role of the Commission

1) Principle: Commission responsibility

Under Article 317 TFEU:

‘The Commission shall implement the budget in cooperation with the Member States, in accordance with the provisions of the regulations made pursuant to Article 322, on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management. Member States shall cooperate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management.’

2) Application of the principle

The way in which this principle is applied is determined by the provisions laid down in Articles 53 to 63 of the 2012 FR.

(a) Prior adoption of a basic act

The FR requires a legal basis separate from the budget for the implementation of appropriations for any action, with the exception of certain cases defined in the FR (pilot projects, preparatory actions, etc). The notion of ‘basic act’ is defined in Article 2 FR.

(b) Delegation of implementing powers

The FR provides for delegation of the budgetary implementation powers of the institutions in accordance with the conditions they lay down in their internal rules and within the limits of the act of delegation.

The FR clarifies the conditions under which the Commission may delegate powers ⁽¹⁾: the Commission may not delegate to third parties the implementing powers it enjoys under the Treaties where they involve a large measure of discretion implying political choices. Within these limits, the Commission may delegate tasks of public authority, and in particular budget implementation tasks, to certain entities (see point 2.1 below); in any case, the implementing tasks delegated must be clearly defined and fully supervised as to the use made of them.

As a general rule, the Commission may not entrust measures for the implementation of funds deriving from the budget, including payment and recovery, to external private-sector entities unless they have a public service mission. Only technical expertise tasks and administrative, preparatory or ancillary tasks involving neither the exercise of public authority nor the use of discretionary powers of judgment can be entrusted, by contract, to external private-sector entities.

⁽¹⁾ See Section 2.

1.2. Limits to the Commission's executive powers

1) *Principle of institutional autonomy*

Under Article 55 FR, the Commission's implementing powers do not extend to the sections of the budget relating to the other institutions, given the principle of institutional autonomy on budgetary matters: each institution exercises the requisite powers for the implementation of these sections, in accordance with the FR.

2) *Delegating and implementing acts*

The executive powers of the Commission can concern two different types of measures:

- (a) measures of general scope that supplement or amend non-essential elements of the basic legislative act, also known as 'delegated acts'; or
- (b) measures that implement provisions of the basic act, also known as 'implementing acts'.

The provisions of the EC Treaty did not make a distinction between the powers conferred to the Commission for adopting these two measures. The TFEU enshrines this distinction by providing a set of rules for delegated and implementing acts.

- **Delegated acts**

The legislator delegates the power to adopt acts amending the non-essential elements of a legislative act to the Commission.

For example, delegated acts may specify certain technical details or they may consist of a subsequent amendment to certain elements of a legislative act. The legislator can therefore concentrate on policy direction and objectives without entering into overly technical debates.

However, this delegation of power has strict limits. In effect, only the Commission can be authorised to adopt delegated acts. Furthermore, the legislator sets the conditions under which this delegation may be implemented. Article 290 of the TFEU specifies that the Council and the Parliament may revoke a delegation or limit its duration.

- **Implementing acts**

The TFEU strengthens the implementing powers of the Commission. The implementation of Union law on Member States' territories is, as a matter of principle, the responsibility of Member States. However, when the European measures require uniform implementation across the EU, the Commission is authorised to adopt implementing acts relating to the implementation of such measures.

Until the entry into force of the TFEU, implementing power was held by the Council, which delegated the adoption of implementing acts to the Commission. Article 291 of the TFEU recognises the competence of principle of the Commission. Therefore, European measures which require uniform implementation in the Member States directly authorise the Commission to adopt implementing acts.

At the same time, the TFEU increases the powers of the Parliament with regard to monitoring the implementing powers of the Commission. The modalities of this monitoring were previously

determined by the Council. From now on, these modalities shall be adopted by the ordinary legislative procedure, within which the Parliament is on an equal footing with the Council.

3) *The comitology committees*

In the exercise of its implementing powers, the legislator usually provides for the Commission to be assisted by Committees made up of Member State representatives. A typical example are the work programmes (annual or multiannual) adopted by the Commission in the framework of the EU spending programmes.

The term ‘comitology’ is used to describe the various procedures through which these Committees operate. The primary role of these Committees is to provide an opinion on the draft measures that the Commission intends to adopt. These opinions can be more or less binding upon the Commission according to the procedure which has been foreseen by the legislator.

The rules and general principles concerning mechanisms for control by Member States of the Commission’s exercise of implementing powers are laid down in secondary legislation — the Comitology Regulation adopted by the European Parliament and Council in February 2011 ⁽¹⁾.

The Regulation provides for the following two procedures: the advisory procedure, which mirrors the former advisory procedure, and a new ‘examination’ procedure, which replaced the previous management and regulatory procedures.

Like in the past ⁽²⁾, the influence of the committee’s opinion varies depending on the procedure:

- Advisory: the Commission shall take the utmost account of the committee’s opinion.
- Examination: implementing acts cannot be adopted by the Commission if they are not in accordance with the opinion of the committee, except in very exceptional circumstances, where they may apply for a limited period of time.

The examination procedure applies, in particular, for the adoption of acts of general scope designed to implement basic acts and specific implementing acts with a potentially important impact.

Specific procedures are foreseen for measures to apply immediately on imperative grounds of urgency. In this case, the Commission adopts an implementing act of immediate application, without its prior submission to a committee.

Whilst only the Member States have a role to play in controlling the exercise of the implementing powers by the Commission, the legislator’s right of scrutiny is foreseen in Article 11 of the new Comitology Regulation. Where the basic act is adopted under the ordinary legislative procedure, the European Parliament and the Council may at any time indicate to the Commission that they consider a draft implementing measure to exceed the implementing powers provided for in the basic act. In such a case, the Commission shall review the draft measure in question and shall inform the European Parliament and the Council whether it intends to maintain, amend or withdraw the draft implementing measure.

⁽¹⁾ Regulation (EU) 182/2011, OJ L 55, 28.2.2011, p. 13.

⁽²⁾ Under the Comitology Decision — Council Decision 1999/468/EC.

2. Implementation of expenditure

2.1. The principles governing the various management methods

The FR adopted in 2012 has introduced a major simplification with regard to the previous Financial Regulations in the architecture of the management modes with the objective of reducing the lack of coherence and the complexity of the legal framework. The five management modes existing under the previous FR have been merged into three: indirect centralised management, decentralised management with third countries and joint management with international organisations now fall under indirect management. A common coherent framework has been introduced, including common reporting requirements (such as the annual submission of a mandatory management declaration aiming at increasing the assurance the Commission gets from its implementation partners and at creating a single chain of accountability). The specificities of external actions implemented by international organisations are taken into account.

1) Three different types of management

Enlargement of the European Union, the growing volume of amounts to administer and, in particular, the gradual extension of the Commission's tasks as Union policies have developed have prompted the Commission to adopt a variety of management methods. The FR provides for three methods of implementation of the budget:

- direct;
- shared;
- indirect.

(a) Direct management

The Commission may implement the budget directly, which means that implementation is handled directly:

(1) By its departments

In this case the Commission and its departments perform the operations required to carry out the measures concerned without any involvement of the Member States or non-member countries where the recipients of the expenditure reside; this method of management concerns the administrative appropriations and some operational appropriations (mainly for the internal policies under Heading 3 of the multiannual financial framework 2007–13 and some external actions). This includes the implementation of the budget by its staff in the Union Delegations under the authority of their respective Head of Delegation. In this case the implementation tasks performed by the financial actors is as explained in point 2.2 below.

(2) Through executive agencies

The multiplication and diversification of the management tasks of the Commission, along with the efficiency to be gained by means of specialisation, justifies the externalisation of some programme management tasks to executive agencies.

If the management of programmes is delegated by the Commission to executive agencies, they are responsible for implementing tasks that are simply executive and do not entail a large measure of discretion implying political choices, such as the launch and conclusion of grant and procurement procedures, the adoption of award decisions, project monitoring, financial control and accounting, the contribution to programme evaluation and various support tasks. These implementing tasks are carried out by the executive agencies under the control of the Commission ⁽¹⁾.

(b) Shared management

Shared management is explicitly referred to in the Treaty, which provides that ‘the Commission shall implement the budget on its own responsibility in cooperation with the Member States’ and that ‘Member States shall cooperate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management’ (Article 317 TFEU). Discharge is granted to the Commission alone (Article 319 TFEU).

The Treaty (Article 317 TFEU) also provides that the financial rules shall lay down the control and audit obligations of the Member States in the implementation of the budget and the resulting responsibilities.

Although shared management has been a long-established practice, it was governed for a long time only by rules laid down in secondary legislation which stipulate, for each sector, the respective roles of the Commission and the national authorities ⁽²⁾. However, the 2012 FR (Article 59) clarifies the obligations of the Member States and the Commission in the case of shared management. It aims at increasing ownership for the management of the funds entrusted and, thus, at introducing greater accountability for the Member States. The FR determines the main principles applicable to shared management:

- the responsibilities of the Member States, which are required to take all the legislative, regulatory and administrative or other measures necessary for protecting the Union financial interests;
- the setting up by the Member States of an effective and efficient internal control system;
- designation by the Member States of bodies responsible for the management and control of Union funds;
- introduction of streamlined reporting obligations for all funds managed under shared management, including the annual submission of a management declaration which aims at establishing a single chain of assurance which will enable the Commission to better discharge its responsibilities in respect of the implementation of the budget;

⁽¹⁾ For more detailed information on executive agencies, see Chapter 16.

⁽²⁾ The obligation on Member States to supply the Commission with information, the Commission's powers of control and the clearance of accounts procedure in the common agricultural policy were laid down in Council Regulation (EC) No 1290/2005 of 21 June 2005 on the financing of the Common Agricultural Policy (OJ L 209, 11.8.2005, p. 1). For the Structural Funds the relevant provisions were those in Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund (OJ L 210, 31.7.2006, p. 25).

- the possibility to complement the annual management declaration by an annual political declaration at Member-State level which would complement the chain of assurance and would encompass the technical level of the management declaration. The national declarations are voluntary (Article 59(5) FR). In December 2013, the European Commission established a Working Group with participants from the European Parliament, the Council and the European Commission to establish practical recommendations supporting Member States who are reflecting on the possibility of establishing a national declaration;
- examination and acceptance of the accounts of the designated bodies and financial corrections for the Member States.

Shared management with Member States applies to the bulk of the budget: the European Agricultural Guarantee Fund (EAGF), the European Structural and Investment Funds, and funds in the field of Home affairs. This expenditure, which is financed in full or in part by the EU budget, is handled by the Member States in accordance with the Union rules via national structures.

(c) Indirect management

The Commission may finally implement the budget indirectly by entrusting budget implementation tasks to third entities.

(1) Entities to which the implementation of the budget may be entrusted:

- third countries or the bodies they have designated;
- international organisations and their agencies;
- the EIB and the European Investment Fund;
- bodies under Articles 208 and 209 FR (decentralised agencies and PPP bodies);
- public law bodies;
- private law body with a public service mission;
- bodies governed by the private law of a Member State that are entrusted with the implementation of a public-private partnership;
- persons entrusted with the implementation of specific actions in the CFSP.

(2) Conditions under which the Commission may entrust budget implementation tasks to third entities

The Commission may have recourse to indirect management and entrust third entities with the implementation of budget implementation tasks provided this is foreseen in the basic act of the relevant programme. This is an additional requirement foreseen in the FR.

Before entrusting third entities with budget implementation tasks, the Commission should obtain evidence that the systems and rules of those third entities guarantee a level of protection of the Union financial interest which is equivalent to the one guaranteed by the FR. The Commission carries out an *ex ante* assessment of the systems and rules of the third entity and if those rules are considered equivalent to its own it may proceed with the delegation.

The entrusted entity should respect the principles of sound financial management, transparency and non-discrimination and should ensure the visibility of Union action when it manages Union funds. The Commission is responsible for the supervision of the entities and for applying procedures for the examination and acceptance of the accounts and for excluding from Union financing expenditure which is made in breach of the applicable rules.

2.2. Roles of the various actors

Expenditure operations are governed by a set of technical rules for using appropriations which are contained in the FR and its Rules of Application. The administrative reform put in place in the institutions since 2003 has been designed to enhance the responsibility of authorising officers, under the supervision of the internal audit service, and to do away with centralised *ex ante* controls.

1) Separation of duties

The budget is implemented by the two actors referred to in Article 332 of the TFEU: the authorising officer and the accounting officer. Their tasks and responsibilities are set out in the FR.

The principle of the segregation of duties is laid down in Article 64 FR.

(a) Role of the authorising officer

The institution performs the duties of authorising officer, but may delegate these duties to staff. The scope of the powers delegated and the possibility for persons to whom these powers are delegated to sub-delegate them are laid down in the internal administrative rules of the institution.

The authorising officers are responsible for the entire management process, from determining the measures deemed necessary to meet the targets set by the institution to the production of results and the evaluation of these results.

To this end, authorising officers should themselves, more so and more effectively than before, perform a whole series of control functions within their departments. They must therefore put in place the appropriate organisational structures (internal management and control systems) and equip their departments with practical instruments and tools satisfying minimum standards in terms of rules and effectiveness, control lists, etc. Authorising officers should also be able to benefit at all times from advice given by horizontal departments. For this reason, a central financial service has been set up within DG Budget.

The tasks of authorising officers by delegation are to implement revenue and expenditure in accordance with the principles of sound financial management and to ensure that the requirements of legality and regularity are complied with. To do so, they:

- make budgetary commitments and legal commitments that bind the institution to third parties (contracts, grant agreements and grant decisions);
- validate expenditure and authorise payments;
- undertake the preliminaries for the implementation of appropriations;
- establish entitlements to be recovered and issue recovery orders.

In the performance of their duties, authorising officers have to apply the principles of legality, regularity and sound financial management, and to set up and maintain local management systems to ensure compliance with these principles and the quality of the financial information relating to these operations.

In compliance with the minimum standards adopted by each institution and having due regard to the risks associated with the management environment and the nature of the actions financed, they must put in place the organisational structure and the internal management and control procedures suited to the performance of their duties. The establishment of the structure and systems shall be supported by a comprehensive risk analysis, which takes into account their cost-effectiveness.

Each operation shall be subject at least to an *ex ante* control: the operational and financial aspects have to be verified by members of staff other than the person who initiated the operation. The staff which carry out the verification shall not be subordinate to the members of staff which initiated the operation.

The authorising officer may put in place *ex post* controls to verify operations already approved following *ex ante* controls. The *ex ante* controls are carried out by members of staff other than those responsible for *ex ante* controls.

Authorising officers by delegation report to their institution on the performance of their duties in the form of an annual activity report together with financial and management information, including the results of controls, confirming that the information contained in the report presents a true and fair view except as otherwise specified in any reservations regarding certain areas of revenue and expenditure. The report sets out the results of the operations performed with reference to the objectives set, the risks associated with these operations, the use made of the resources provided, the efficiency and effectiveness of the internal control systems and an overall assessment of the costs and benefits of the controls. The internal auditor takes note of the annual report and any other items of information supplied. The Commission sends the budgetary authority a summary of the annual reports for the previous year no later than 15 June of every year.

(b) Role of the accounting officer

In each institution, the accounting officer is responsible for:

- proper implementation of payments, collection of revenue and recovery of amounts established as being receivable;
- keeping the accounts; preparing and presenting the accounts;
- laying down the accounting rules and methods and the chart of accounts;
- laying down and validating the accounting systems and, where appropriate, validating systems put in place by the authorising officer to supply or justify accounting information, whereby the accounting officer is empowered to verify compliance with validation criteria;
- treasury management.

The 2003 revision of the FR enhanced the powers of the accounting officer in relation to the authorising officer at the level of accounting rules and the supply of accounting information. Authorising officers are, for example, formally required to supply whatever information the accounting officer requests in order to fulfil his duties.

To ensure harmonisation, the Commission accounting officer has to lay down accounting standards (accounting and consolidation methods) to apply to the accounts of all the institutions. It is also the duty of the Commission accounting officer, in the presentation of the accounts process, to consolidate the financial statements prepared by each institution.

Finally, the accounting officer has to prepare the Commission's definitive accounts. Before the adoption of the accounts by the institution, the accounting officer has to sign them off, thereby certifying that (s)he has a reasonable assurance that the accounts present a true and fair view of the financial situation of the institution.

For that purpose, the accounting officer must satisfy him/herself that the accounts have been prepared in accordance with the accounting rules, methods and accounting systems established under his/her responsibility as laid down in the FR for the accounts of his or her institution, and that all revenue and expenditure is entered in the accounts. For that purpose, the accounting officer is empowered to check the information received as well as to carry out any further checks (s)he deems necessary in order to sign off the accounts.

2) Role of the internal auditor

At central level, an internal auditor is required to supply the institution, in accordance with international standards, with an assurance concerning the sound operation of budget implementation systems and procedures. This auditor is responsible for evaluating the effectiveness and efficiency of internal control and management systems put in place by authorising officers. In order to be able to work effectively, the internal auditor must have a strong and independent position within the institution, in accordance with the principle of the separation of duties. His or her independence is guaranteed by the FR.

The internal auditor is not involved in the implementation of the budget and is not therefore a financial actor.

An audit progress committee has the task of ensuring that Commission departments take appropriate action to improve internal control systems in response to recommendations from the Internal Audit Service, the Internal Audit Capabilities and the European Court of Auditors. The Audit Progress Committee has nine members comprised of seven Commissioners, including the Commissioner for Taxation and Customs Union, Audit and Anti-Fraud, who chairs the Committee, and two external members with proven professional expertise in audit and related fields.

3) Liability

(a) General principles

The liability of the financial actors is governed by the provisions of the Staff Regulations and the FR. The general rule is that the responsibilities of authorising officers or the accounting

officer may be withdrawn at any time temporarily or definitively by the authority that appointed them, without prejudice to:

- any disciplinary action and payment of compensation as laid down in the Staff Regulations;
- any liability under criminal law which the financial actors may incur on the basis of the applicable national law and in the provisions in force concerning the protection of the Union's financial interests and the fight against corruption involving Union officials or officials of Member States.

In addition, the FR prohibits any conflict of interests which applies not only to the financial actors but to every person involved in budget implementation and management. For the notion of conflict of interests, please refer to point 3) below.

The FR provides, in its Articles 73, 74 and 75, specific cases where financial actors carry liability.

(b) Authorising officers

The obligation to pay compensation applies in particular if the authorising officer responsible, whether intentionally or through gross negligence:

- determines entitlements to be recovered or issues recovery orders, commits expenditure or signs a payment order without complying with the FR and its Rules of Application;
- omits to draw up a document establishing an amount receivable, neglects to issue a recovery order or is late in issuing it, or is late in issuing a payment order, thereby rendering the institution liable to civil action by third parties.

Each institution is to set up a specialised financial irregularities panel or participate in a joint panel established by several institutions, the role of which should be to determine whether a financial irregularity has occurred and what the consequences, if any, should be. On the basis of the opinion of this panel, the institution decides whether to initiate proceedings leading to disciplinary action or to payment of compensation. In addition, if the panel detects systemic problems, it is to send a report with recommendations.

(c) Accounting officer

For the accounting officer, any of the following forms of misconduct may render him or her liable to disciplinary action and payment of compensation:

- (s)he loses or damages funds, assets or documents in his/her keeping;
- (s)he wrongly alters bank accounts or postal giro accounts;
- (s)he recovers or pays amounts that are not in conformity with the corresponding recovery or payment orders;
- (s)he fails to collect revenue due.

4) Conflict of interests

The 2002 revision of the FR introduced the concept of conflict of interests and its prohibition.

The conflict of interests was defined as a situation where the impartial and objective exercise of the functions of a financial actor, or other person involved in budget implementation, is compromised for reasons involving family, emotional life, political or national affinity, economic interest or any other shared interest with the recipients of Union funds.

The 2012 revision of the FR reinforced the prohibition by extending the scope of the notion of conflict of interests to:

- the persons involved in preparatory acts related to budget implementation and management;
- the obligation to refrain from also acting in cases of ‘risk’ of conflict of interests;
- the referral of the matter to the authorising officer by delegation in order to align as far as possible the FR to the Staff Regulation which foresees an obligation to inform the appointing authority.

Article 57 FR now requires that where a ‘risk’ of conflict of interests exists, the person in question has to declare it to the authorising officer by delegation who shall confirm in writing whether a conflict of interests exists. Where a conflict of interests is found to exist, the person may no longer be involved in any part of the related activities.

5) OLAF and EPPO

(a) The role of the European Commission Anti-Fraud Office

The European Commission Anti-Fraud Office (OLAF) was set up in 1999 ⁽¹⁾ in order to fight against fraud and any other illegal activities detrimental to the Communities’ financial interests. It is the successor of the Commission’s Task Force for the Coordination of the Fight against Fraud (UCLAF).

OLAF began operating on 1 June 1999 as a Commission department with independent investigative function under the authority of the Commissioner responsible for the budget. Since 2010, OLAF is under the authority of the Commissioner for Taxation, Customs, Statistics, Audit and Anti-Fraud.

The new Regulation No 883/2013 ⁽²⁾ governing the work of OLAF entered into force on 1 October 2013. The aim of this reform is to allow OLAF to operate more efficiently and to step up the fight against fraud, corruption or any illegal activity affecting the financial interests of the EU. The Regulation also sets the basis for a better exchange of information between OLAF and its partners.

⁽¹⁾ 1999/352/EC, ECSC, Euratom: Commission decision of 28 April 1999 establishing the European Anti-Fraud Office (OLAF) (OJ L 136, 31.5.1999, p. 20).

⁽²⁾ REGULATION (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) and repealing Regulation (EC) No 1073/1999 of the European Parliament and of the Council and Council Regulation (Euratom) No 1074/1999. REGULATION (EU, Euratom) No 883/2013 of the European Parliament and of the Council of 11 September 2013 concerning investigations conducted by the European Anti-Fraud Office (OLAF) and repealing Regulation (EC) No 1073/1999 of the European Parliament and of the Council and Council Regulation (Euratom) No 1074/1999.

Under the new Regulation, OLAF's mandate extends beyond the protection of financial interests to include all activities relating to safeguarding EU interests against irregular conduct liable to result in administrative or criminal proceedings. In addition, the investigative powers of OLAF are clarified and consolidated. These include the power to conduct on-the-spot checks and inspections.

OLAF is subject to scrutiny by a Supervisory Committee whose monitoring role was confirmed by the 2013 Regulation. It is made up of five independent outside experts qualified in the fight against fraud. The task of OLAF's Supervisory Committee is to regularly monitor the implementation of OLAF's investigative function and the application of procedural guarantees and the duration of its investigations.

In order to coordinate Member States' action in combating fraud against the Union's financial interests, OLAF organises close and regular cooperation between the relevant national authorities. Each EU Member State is required to designate a service to grant support to the Office at various stages of an investigation.

Outside the Union institutions, as part of its investigative function, OLAF shall exercise the power conferred on the Commission by Regulation (Euratom, EC) No 2185/96 to carry out on-the-spot checks and inspections in the Member States, third countries and on the premises of international organisations in accordance with the respective agreements.

Within the institutions, OLAF may conduct administrative investigations into any activities of departments of Union institutions, bodies, offices and agencies for the purpose of fighting fraud, corruption and any other illegal activity affecting the financial interests of the Union.

(b) The European Public Prosecutor Office

In 2013, the Commission proposed the setting-up of the European Public Prosecutor Office (EPPO) who would have exclusive competence to deal with crimes affecting the financial interests of the Union, in accordance with Article 86(1) of the TFEU ⁽¹⁾.

The EPPO would be a decentralised structure composed of a European Public Prosecutor and European Delegated Prosecutors in Member States.

The independence of the EPPO would be guaranteed by various safeguards, in particular through its appointment and dismissal procedures, rules on tenure and conflicts of interests.

In its proposal, the Commission envisages that the EPPO will conduct administrative anti-fraud investigations where there are suspicions of a criminal behaviour. In order to avoid duplication of work between the EPPO and OLAF, further adjustments to OLAF's legislative framework may be required.

⁽¹⁾ Proposal for a Council Regulation on the establishment of the European Public Prosecutor's Office of 17.7.2013, COM(2013) 534 final.

2.3. Stages in the expenditure procedure

1) *The stages in the expenditure procedure*

An expenditure operation is divided into four parts: every item of expenditure has to be committed, validated, authorised and paid.

- *Commitment of expenditure by the authorising officer:* the budgetary commitment is the operation reserving the appropriation necessary to cover subsequent payments to honour a legal commitment ⁽¹⁾. The commitment may be individual (when the beneficiary and the amount are known in advance), global (if one of these elements is still not known), or provisional (for administrative and agriculture expenditure).
- *Validation of expenditure:* the act whereby the authorising officer verifies the existence of the creditor's entitlement, and determines or verifies the reality and the amount of the sum due and the conditions under which payment is due. Validation is based on supporting documents within the meaning of Article 110 of the Rules of Application of the FR attesting the creditor's entitlement, and is confirmed by the signing of a 'passed for payment' voucher by the authorising officer.
- *Authorisation:* the act whereby the authorising officer, by issuing a payment order after having verified that the appropriations are available, instructs the accounting officer to pay an item of expenditure that he or she has validated.
- *Payment:* the final action whereby the institution is discharged of its obligations towards its creditors; payment is made by the accounting officer within the limits of the funds available. For payment of certain categories of expenditure, imprest accounts may be set up. Payments are divided into four types: payment of the entire amount due; payment of part of the amount due in any of the following ways: pre-financing, which may be divided into a number of payments, one or more interim payments, and payment of the balance of the amount due.

2) *Conditions under which expenditure is made*

The completion of these different stages is subject to compliance with certain conditions. The main conditions are the following:

- the budget commitment must come before the legal commitment. However, in order to bring the FR into line with sectoral provisions authorising the use of annual instalments, the FR provides explicitly for the possibility of splitting budget commitments where they relate to operations that will extend over more than one financial year, provided this is allowed by the relevant basic act;
- every payment has to be justified by supporting documents;

⁽¹⁾ Confusion has to be avoided with the concept of legal commitment, which is the act whereby the authorising officer enters into or establishes an obligation that results in a charge.

- the stages in the expenditure procedure must be completed within certain time limits, whereby creditors paid late are entitled to receive default interest charged to the Community budget.

3. Grants, procurement and prizes

The award of prizes, grants and contracts by the Commission is a process involving the Commission (i.e. the College or the authority to which powers have been delegated) and the competent authorising officers. A competitive selection procedure must be followed for all: call for tenders for procurement, contest for prizes and call for proposals for grants.

3.1. Prior authorisation

The Commission must first adopt a financing decision before implementing the budget. It may be merged with the annual work programme, if the latter provides the essential elements of the actions to be financed and a sufficient detailed framework for the implementation.

For grants, the annual programme constituting a financing decision details the priorities, the objectives and the results expected, the priorities of the year and their indicative amounts, the eligibility criteria, the main selection and award criteria, the co-financing rate as well as the timetable for the publication of calls for proposals.

For prizes, the annual programme constituting a financing decision details the objectives and the results expected, the conditions for participation and award criteria, the amount of the prize, as well as the timetable for the contest.

For procurement, the annual programme constituting a financing decision details the subject, the indicative number and types of contracts, as well as the amounts and the indicative timetable for the publication of calls for tenders.

3.2. Implementation cycle

The competent authorising officer is responsible for the implementation of the annual work programme on the basis of the financing decision. He has to conform to fundamental principles and procedures laid down by the FR and its Rules of Application. All procurement contracts, prizes and grants awarded by the Commission must comply with the principles of sound financial management, transparency and equal treatment.

To safeguard these three principles, the competent authorising officer:

- publishes calls for tenders (procurement), except in well-defined cases for which a negotiated procedure is authorised by the Rules of Application. Grants, on the other hand, are awarded after calls for proposals, except in duly substantiated exceptional cases of urgency or where the characteristics of the beneficiary leave no other choice for a given action. Prizes are awarded after a contest;
- appoints an evaluation committee for the assessment of tenders (procurement) and proposals (grants) or a panel of experts for prizes. This evaluation is made on the basis of the pre-announced exclusion, selection and award criteria.

Procurement contracts, prizes and grants may not be awarded to legal or natural persons who are excluded under the FR because of their particular situation (e.g. bankrupt, wound up, convicted of an offence concerning their professional conduct, fraud, corruption, but also persons who are guilty of misrepresentation, have attempted to obtain confidential information or have been declared to be in serious breach of contract for failure to comply with their previous contractual obligations).

The evaluation committee or the panel of experts examines tenders, entries or proposals according to:

- the selection criteria, which aim at evaluating the technical and financial capability of candidates and tenderers (for procurement) or applicants (for grants);
- the award criteria, which are used to evaluate the content and quality of the tender, entry or proposal.

In addition to this:

- procurement contracts may be awarded either to the tender offering the lowest price (so-called automatic award procedure) or to the one offering best-value-for-money or the best price-quality ratio;
- prizes are awarded on the basis of the quality of the entries with regards to the objectives pursued and expected results;
- grants shall be awarded to the best quality proposals in light of the objectives and priorities set. However, they may not be cumulative or awarded retrospectively and they must involve co-financing.

The award decision is in principle adopted by the competent authorising officer. However, for grants, it is adopted by the Commission whenever a comitology procedure is imposed by the basic act for the award decision.

Finally, the competent authorising officer must inform the applicants, participants and candidates or tenderers in writing of the results of their application, entry or tender. Following the 2012 revision of the FR and its Rules of Application, it has been clarified that all adverse decisions must include information regarding means of redress as part of the principle of good administration.

The procedure ends with the authorising officer signing a contract in the case of procurement and a grant agreement or a grant decision in the case of grants, with respectively the appointed contractor or grant beneficiary. The award of prizes is simply notified to the winner.

4. The system for making available own resources

Own resources are made available according to the relevant provisions of Council Decision 2007/436 on own resources ⁽¹⁾ (ORD 2007) and the detailed rules in Regulation (EC, Euratom) No 1150/2000 ⁽²⁾ implementing the own-resources decision. After the adoption of the ORD 2014, this regulation will be replaced by the Council Regulation (EU, Euratom) No 609/2014 of 26 May 2014 on the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements, which will apply retroactively from 1 January 2014 onwards.

The various categories of own resources (traditional own resources, the resource accruing from VAT and the GNI-based own resource) are assigned to the Union in order to finance the budget of the European Union. Member States enter them into accounts for own resources kept by the Treasury of each Member State or the body appointed by each Member State on behalf of the Commission (the 'own resources accounts').

The procedure for making available traditional own resources is different from the one applicable to the VAT and the GNI-based own resources, as explained below.

4.1. Establishment and entry into the Commission's accounts

4.1.1. Traditional own resources

Under Article 8 of the Decision on the own-resources system, Member States collect traditional own resources on behalf of the European Union in accordance with their national provisions, which must be adapted to the Union's requirements.

(a) Establishment of traditional own resources by the Member States

In accordance with Article 2 of Regulation (EEC, Euratom) No 1150/2000, these resources are established as soon as the conditions provided by in the customs regulations have been met for the entry of the entitlement in the accounts and the notification of the debtor (for sugar levies, the relevant date is that of the notification provided for in the Union's regulations governing the sugar sector). The same provision was kept in the Council Regulation which lays down the rules on making available to the Commission the own resources of the Union according with ORD 2014.

Member States are required to make good any shortfall in traditional own resources resulting from deficiencies in the way they manage the collection system.

(b) Entry of traditional own resources in the accounts

All established amounts of traditional own resources must be entered into one of the accounts kept by the competent authorities.

⁽¹⁾ Council Decision (EC, Euratom) No 2007/436 of 7 June 2007 on the system of the European Communities' own resources (OJ L 163, 23.6.2007, p. 17).

⁽²⁾ Council Regulation (EC, Euratom) No 1150/2000 of 22 May 2000 implementing Decision 2007/436/EC, Euratom on the system of the European Communities' own resources (OJ L 130, 31.5.2000, p. 1), as last amended by Regulation (EC, Euratom) No 105/2009 (OJ L 36, 5.2.2009, p. 1).

- In the ordinary account provided for in Article 6(3)(a) of Regulation (EC, Euratom) No 1150/2000: all amounts recovered or secured and not challenged.
- In the separate account provided for in Article 6(3)(b) of Regulation (EC, Euratom) No 1150/2000: all amounts that have not yet been recovered and for which no security has been provided; amounts for which security has been provided and that have been challenged and might, upon settlement of the disputes, be subject to change may also be entered in this account.

Traditional own resources must be entered in the accounts no later than the first working day after the nineteenth of the second month following the month in which the entitlements were established. Member States retain 25 % ⁽¹⁾ of the established amounts in order to cover the collection costs borne by them.

4.1.2. VAT and GNI based own resources

For the VAT and the GNI-based own resources, there is no distinction between the date of establishment and the date when Member States are required to credit these resources in the Commission's own resource accounts.

On the first working day of each month Member States must credit to the Commission's own resource accounts one twelfth of the total amount of the VAT and GNI-based resource (including the amounts for correction mechanisms) entered in the Union's budget. For the specific needs of paying EAGF expenditure and depending on the Commission's cash position, Member States may be invited in the first quarter of the year to bring forward by one or two months one twelfth or a fraction of one twelfth of the VAT and GNI-based resources (including the amounts for correction mechanisms).

Every month, the Commission sends the Member States a call-for-funds letter informing them of the precise amounts of the VAT and GNI-based own resources (including the amounts for the correction mechanisms) due on the first working day of the following month.

The budgets for the VAT and the GNI-based own resources are based on the most recent available macroeconomic estimates for the corresponding VAT and GNI bases of the Member States. The annual revisions or updates of these estimates give rise in the four years after a budget year ⁽²⁾ to annual adjustments of Member States' VAT and GNI-based contributions. These adjustments are referred to as 'VAT and GNI balances'.

The VAT and GNI balance adjustments are made in accordance with dedicated legal basis, respectively Regulation (EEC, Euratom) No 1553/89 of 29 May 1989 ⁽³⁾ for VAT own resources

⁽¹⁾ 20 % once the ORD 2014 will enter in force — see Chapter 9, point 2.5, paragraph 4).

⁽²⁾ There is no time limit for points notified within the four years period, either by the Commission or by the Member State.

⁽³⁾ Council Regulation (EEC, Euratom) No 1553/89 of 29 May 1989 on the definitive uniform arrangements for the collection of own resources accruing from value added tax (OJ L 155, 7.6.1989, p. 9).

and Council Directive 89/130/EEC of 13 February 1989 ⁽¹⁾ and Council Regulation (EC, Euratom) No 1287/2003 of 15 July 2003 ⁽²⁾, for the GNI-based own resource.

Member States must enter the VAT and GNI balances in the own resources account on the first working day of December of each year.

4.2. Own resources currencies and interest for belated payments

Member States belonging to the eurozone make own resources available in euros. The other Member States make own resources payments in their national currencies.

Any delay in making available own resources gives rise to the payment of interest by the Member State concerned.

4.3. System of scrutiny

As resources are collected at national level, it is firstly for the Member States' authorities to put in place an appropriate (internal) control infrastructure. As the Commission is the authorising body for revenue and therefore accountable to the budgetary authority, it must, of course, obtain assurances that the Member States collect own resources in accordance with the Union's rules. It may therefore ask to be associated with national inspections and also ask Member States to conduct additional inspections. For traditional own resources, the Commission may, itself and on its own initiative, carry out on-the-spot inspections. For VAT own resources the Commission checks that the national authorities have correctly performed the calculations for determining the amounts.

These controls and inspections are carried out on behalf of the Union by agents authorised by the Commission under Regulation (EC, Euratom) No 1026/1999 of 10 May 1999 ⁽³⁾.

Inspection findings are set out in a report sent to the Member State concerned. This report, together with the Member State's comments, is then considered by the Advisory Committee on Own Resources (ACOR), made up of representatives of the Member States and the Commission (which chairs the meetings and provides secretariat services). This ensures openness, as each Member State is aware of the findings of controls carried out in the other Member States. After discussion in ACOR, the Commission finalises its position and follows up the observations made until the matter is settled. ACOR can also examine any matters relating to the collection of own resources.

For the control of VAT resources, the Commission draws up a report every three years on the procedures applied in the Member States and on any improvements envisaged. A similar report on the system for collecting traditional own resources is also produced every three

⁽¹⁾ Council Directive 89/130/EEC, Euratom of 13 February 1989 on the harmonisation of the compilation of gross national product at market prices (OJ L 49, 21.2.1989, p. 26).

⁽²⁾ Council Regulation (EC, Euratom) No 1287/2003 of 15 July 2003 on the harmonisation of gross national income at market prices (OJ L 181, 19.7.2003, p. 1).

⁽³⁾ Council Regulation (EC, Euratom) No 1026/1999 of 10 May 1999 determining the powers and obligations of agents authorised by the Commission to carry out controls and inspections of the Communities' own resources (OJ L 116, 20.5.1999, p. 1).

years and sent to the budgetary authority. Payments of the GNI-based resource are based on Member States' GNI aggregates. These are established in accordance with Eurostat. It is also Eurostat that controls Member State methodologies and procedures for establishing the respective GNI aggregates.

5. Management of cash resources

The Commission has different types of accounts where its funds are kept and from which its treasury transactions are executed.

5.1. Accounts with Member State treasuries or with national central banks (pursuant to Article 9 of Council Regulation (EC, Euratom) No 1150/2000 on own resources) ⁽¹⁾

Article 9 of Council Regulation (EC, Euratom) No 1150/2000 requires each Member State to credit own resources to an account opened in the name of the Commission with its treasury or the body it has appointed.

A number of Member States have opened these accounts with their national treasuries while in other cases they have been opened at national central banks.

The national treasuries do not usually operate as banks. Consequently, where 'Article 9' accounts are opened with them, most of the Commission's transfers of funds from these accounts are routed through the national central banks, where the Commission also has accounts.

The 'Article 9' accounts are kept in euros for Member States whose currency is the euro and in national currencies in the other Member States. These accounts serve for collecting own resources and, in several cases, for payments to Member State governments (in particular for the EAGGF and the Structural Funds).

'Article 9' accounts are not interest-bearing and are free of charge (Article 9(1) of Council Regulation (EC, Euratom) No 1150/2000). Article 12(1) of this Regulation requires that the Commission funds be kept on these accounts and be drawn on only to meet budgetary needs.

This means that only funds actually needed for immediate payments are placed on commercial bank accounts (see below). The remainder is kept on the accounts opened with the Member State treasuries and/or national central banks.

Under Article 12(4) of Regulation (EC, Euratom) No 1150/2000, the funds are divided among accounts held in the different Member States, as much as possible in proportion to the estimated budget revenue from each of them.

While the main own resources, i.e. those based on VAT and GNI, are generally credited to the Commission's account in equal monthly instalments, the Commission's payments are not spread evenly over the year. At present, more than half of EAGGF payments are made in January and February. As a consequence, additional amounts may have to be called in from

⁽¹⁾ Council Regulation (EC, Euratom) No 1150/2000 of 22 May 2000 implementing Decision 2007/436/EC, Euratom on the system of the Communities' own resources.

the Member States during the first months of each year. This is authorised by Article 10(3) of Regulation (EC, Euratom) No 1150/2000. Depending on the Commission's cash position, Member States may be invited to bring forward by one or two months in the first quarter of a budget year the entry in the Commission account of the VAT resource and/or the GNI-based resource. After the first quarter the monthly entry may not exceed one twelfth of the VAT and GNI-based resources. These advance payments are calculated each month on the basis of actual cash flow and credited at the same time as the current VAT and GNI resources.

5.2. Accounts with commercial banks

Commercial banks where accounts are opened are generally chosen by open tendering procedures. These accounts are used in most of the cases for the execution of payments to beneficiaries, other than Member State governments.

They are held in euros and, where necessary, in national currencies and are interest-bearing.

As mentioned above, EU cash resources are kept in the accounts held with Member States' treasuries and central banks and drawn solely for the purpose of executing payments. The cash needs of commercial bank accounts are covered by funds transferred to them from the accounts in the Member States, 'just-in-time' to cover for payments execution. Minimum overnight balances are kept on all commercial bank accounts to ensure the continuity of payment operations.

The SEPA (Single Euro Payments Area) is an initiative of the European banking industry and its aim is to improve the efficiency of cross-border payments and turn the fragmented markets for euro payments into a single domestic one. The Commission migrated to a SEPA-compliant payment architecture and became an 'early adopter of SEPA' at the beginning of 2010. This contributed to enhancing the efficiency of the Commission's euro payment operations, which can now be effectively carried out using a very limited number of banks.

The Commission also keeps bank accounts in some non-euro currencies in order to execute payments in these currencies' domestic markets.

The Commission's accounts cannot be overdrawn.

Since most Commission payments (with very few exceptions) are made in euros, the majority of currency exchange operations concern the conversion into euros of own resources paid in national currency by the Member States not belonging to the eurozone. Such currency conversions are mainly performed, on the instruction of the Commission, by central banks.

All payments ordered by the Commission's treasury are transmitted to banks electronically.

The Commission is a member of SWIFT (Society of Worldwide Interbank Financial Telecommunication), has its own SWIFT code, and uses the SWIFT network to communicate with banks.

For transactions with the national treasuries that are not connected to SWIFT, instructions in SWIFT format are generated and transmitted via secured e-mail.

The number of payments executed by the Commission and the European External Action Service in 2013 was approximately 1.9 million.

Chapter 16

Bodies set up by the Union with legal personality

The main types of EU bodies are as follows:

1. Decentralised agencies (32 in budget 2014);
2. The European Institute of innovation and technology;
3. Executive agencies (6 in budget 2014);
4. Joint undertakings (7 in budget 2014).

1. Decentralised agencies

1.1. Definition and scope of intervention

EU law does not provide for a general/explicit definition of what is intended by decentralised (or 'regulatory' or 'traditional') Union agencies. They are bodies governed by European public law, distinct from the Union Institutions and have their own legal personality. They are set up by an act of secondary legislation and are under the control of a management board, mostly composed by Member States representatives.

The European Parliament, the Council and the Commission have agreed that all bodies falling into the scope of Article 208 FR should be considered as decentralised agencies. In order to be considered decentralised agencies for the application of this Article, Union bodies must fulfil the following criteria:

- being set up under the TFEU and the Euratom Treaty;
- having legal personality;
- receiving contributions charged to the Union budget.

Decentralised agencies are either created jointly by the European Parliament and the Council on the basis of a specific Treaty provision concerning a given policy area (ordinary legislative procedure) or in some rare cases by Council on the basis of Article 352 TFEU (special legislative procedure).

The objectives and tasks conferred on each agency are set out in its legal basis (founding regulation or decision).

Agencies are created for a variety of reasons:

- to support the decision-making process in areas requiring a high level of technical or specialist expertise;
- to take over responsibilities normally falling within the competence of the Member States but for which coordination at Union level is desirable;
- to give more visibility for the Union outside Brussels, through agencies located across the Union territory.

Some agencies have regulatory power: they can adopt binding rules and/or individual decisions with direct legal effect (example: the Office for Harmonisation in the Internal Market). Others provide assistance to the Commission and, where necessary, to the Member States in the interests of the Union, in the form of technical or scientific opinions and/or inspection reports (example: the European Food Safety Authority). Finally, some agencies focus on organising the cooperation between national competent authorities and the Union level in order to exchange and compare information and good practices (example: European Network and Information Security Agency).

1.2. Financing of decentralised agencies

Financial principles and rules which govern the preparation and adoption of the budget of an agency, as well as the implementation, control and discharge are set out in the financial rules of each agency. They are adopted by the agencies' management boards on the basis of a Framework Financial Regulation (FFR) ⁽¹⁾ and cannot depart from it except where the Agency's specific needs so require and with the Commission's prior consent.

Agencies which do not fulfil all criteria of Article 208 FR, in particular agencies which do not receive any contribution from the EU budget, are not formally obliged to follow the FFR. Nevertheless, their constituent acts oblige them to follow it or to adopt similar financial rules for the sake of consistency.

The majority of decentralised agencies (i.e. 23 out of 32 existing agencies listed in Table 1) are financed entirely from the EU budget.

Other agencies are, however, fully or partially financed from revenue received from industry (fees and charges):

- partially self-financed agencies: European Medicines Agency (EMA), European Chemicals Agency (ECHA) and European Aviation Safety Agency (EASA);
- fully self-financed agencies: Office of Harmonisation for the Internal Market (OHIM), Community Plant Variety Office (CPVO) and Translation Centre for the bodies of the European Union (CdT). In addition, in July 2013 the Commission proposed to create a new fully self-financed agency, the European Resolution Board, which is expected to become operational in 2015 ⁽²⁾.

Three agencies are partially co-financed by national public authorities: the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA), and the European Insurance and Occupational Pensions Authority (EIOPA).

The EU contribution to the agencies for a given financial year is meant to balance the agency's revenue (taking into account all sources, including fee revenue if applicable) and expenditure

⁽¹⁾ Commission Delegated Regulation (EU) No 1271/2013 of 30 September 2013 on the framework financial regulation for the bodies referred to in Article 208 of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council sets essential rules for the implementation of the budget of the Union bodies. It is aligned with and follows the structure of general FR.

⁽²⁾ COM(2013)520, 10.7.2013.

for that given year (balancing contribution). In turn, an agency surplus for a given financial year has to be repaid to the EU budget up to the level of the total EU contribution paid.

The payment of the Union balancing contribution to the agency is typically made available in a number of instalments throughout the year, depending on the actual cash requirements of the agency in question.

The FFR (Articles 7 and 8) also allows in exceptional cases and under strict legal conditions, that additional tasks (i.e. not foreseen in the founding regulation of the agency) are financed through ad hoc grants or delegation agreements with the Commission.

1.3. Internal and external control of the budget implementation and discharge

The FFR foresees that the Director of Agency (exercising the duties of the authorising officer) is responsible for implementation of the agency's budget in accordance with the principle of sound financial management and for ensuring the compliance with the requirements of legality and regularity. Therefore, he/she is obliged to put in place an appropriate organisational structure and internal control system, taking into account the nature and risk associated with the actions to be financed.

The internal audit function is performed by the Commission's internal auditor. Additionally, where necessary the possibility of establishment of an Internal Audit Capability (IAC) is explicitly foreseen. The responsibilities of the IAC should be coordinated and complementary with those of the internal auditor.

Decentralised agencies, as all other bodies and institutions, are subject to external audit.

Article 287 of the TFEU provides that the Court of Auditors, as external auditor, examines the accounts of all revenue and expenditure of all bodies set up by the Union in so far as the relevant constituent instrument does not preclude such examination.

Additionally, in the case of decentralised agencies, Article 208 FR foresees the involvement of independent private auditors in the exercise of the external audit of annual accounts. The Court of Auditors has to consider their audit work while preparing its annual specific report on the agency.

By analogy with the general discharge procedure described in Article 319 of the TFEU and in accordance with Article 208 FR, decentralised agencies receive a separate discharge. The European Parliament, upon a recommendation from the Council, gives the discharge for the implementation of the budget of the agency that receives a contribution from the EU budget to its Director.

However, discharge regarding the implementation of delegation agreements remains part of the discharge given to the Commission. In this case, the agency has to ensure a separation of reporting and accounting in order to avoid confusion as regards who is accountable for what.

List of existing Union decentralised agencies (2014)

DECENTRALISED AGENCIES			
Acronym	Full Name	Location	Year of Creation
ECHA	European Chemicals Agency	Helsinki	2006
EASA	European Aviation Safety Agency	Köln	2002
EMA	European Medicine Agency	London	1993
EBA	European Banking Authority	London	2010
EIOPA	European Insurance and Occupational Pensions Authority	Frankfurt	2010
ESMA	European Securities and Markets Authority	Paris	2010
EUROFOUND	European Foundation for the Improvement of Living and Working Conditions	Dublin	1975
EU-OSHA	European Agency for Occupational Safety and Health	Bilbao	1994
ERA	European Railway Agency	Lille-Valenciennes	2002
Cedefop	European Centre for the Development of Vocational Training	Thessaloniki	1975
EIGE	European Institute for Gender Equality	Vilnius	2006
EEA	European Environment Agency	Copenhagen	1990
EFCA	European Fisheries Control Agency	Vigo	2005
Europol	European Police Office	The Hague	1995
CEPOL	European Police College	Bramshill	2005
EMCDDA	European Monitoring Centre for Drugs and Drug Addiction	Lisbon	1993
ECDC	European Centre for Disease Prevention and Control	Stockholm	2004
EFSA	European Food Safety Authority	Parma	2002
ETF	European Training Foundation	Turin	1990
GSA	European GNSS Supervisory Authority	Prague	2005
EMSA	European Maritime Safety Agency	Lisbon	2002
ENISA	European Network and Information Security Agency	Heraklion	2004
ACER	Agency for the Cooperation of Energy Regulators	Ljubljana	2009
FRONTEX	European Agency for the Management of Operational Cooperation at the External Borders of the Member States of the EU	Warsaw	2005
EUROJUST	European Union's Judicial Cooperation Unit	The Hague	2002
BEREC	Office for the Body of European Regulators for Electronic Communications	Riga	2009
EASO	European Asylum Support Office	Valletta	2010
IT Agency (Eu.LISA)	European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice	Tallinn — Strasbourg	2011
FRA	Fundamental Rights Agency	Vienna	2007
CdT	Translation Centre for the bodies of the EU	Luxembourg	1994
OHIM	Office for Harmonisation in the Internal Market	Alicante	1993
CPVO	Community Plant Variety Office	Angers	1994

2. European Institute of Innovation and Technology

The task of the European Institute of Innovation and Technology (EIT) is to reinforce the innovation capacity of the Union and the Member States, by bringing together the best actors operating in the 'knowledge triangle' (higher education, research and innovation). In terms of budgetary and financial arrangements, the EIT largely follows the example of the decentralised agencies as described above. Its financing is included in the financial envelope of the Horizon 2020 programme (see chapter 14, Section 2.1).

3. Executive agencies

In December 1999, the Commission undertook a major review of its externalisation policy⁽¹⁾ in order to correct the shortcomings detected previously due to the poor control of some technical administrative support offices (TAOs, also known under the French acronym of BATs).

Essentially, the guidelines aimed to re-focus the Commission's attention and staff on its core tasks, i.e. the development and monitoring of policies under the Treaty, and to define acceptable forms of externalisation, including a new type of implementing bodies: executive agencies.

Executive agencies are legal persons under Union law created by a Commission decision to which powers can be delegated to implement all or a part of a Union programme on behalf of the Commission and under its responsibility in accordance with Council Regulation (EC) No 58/2003 of 19 December 2002⁽²⁾. The executive agencies intended to replace the TAOs.

The originality of the executive agency concept lies in the combination of the autonomy of the agency (with a separate legal personality), which allows more flexible management, and supervision of the performance of its tasks by the Commission (through the Steering Committee), which guarantees the protection of the Union interests.

There is a clear division of programme management tasks between the Commission and the executive agencies. The Commission's departments perform tasks involving a large measure of discretion implying policy choices, in particular: setting objectives and priorities, adopting work programmes (including financing decisions), representing the Commission in the programme committee and adopting award decisions subject to comitology. The agencies are responsible for implementing tasks, such as the launch and conclusion of grant and procurement procedures, the adoption of award decisions, project monitoring, financial control and accounting, the contribution to programme evaluation and various support tasks.

In view of the positive experience of management of EU programmes by the executive agencies, the Commission proposals for the 2014–20 MFF also included making more use of the existing executive agencies to implement certain new programmes.

⁽¹⁾ Guidelines for the Commission's externalisation policy; Communication of Mrs Schreyer and Mr Kinnock, SEC(1999) 2051, 14.12.1999.

⁽²⁾ Regulation (EC) No 58/2003 of 19 December 2002 laying down the statute for executive agencies to be entrusted with certain tasks in the management of Community programmes (OJ L 11, 16.1.2003, p. 1).

The six executive agencies, set up under Council Regulation No 58/2003 are maintained for the 2014–20 period, however, the names of three of the six are adapted, to reflect the extended scope of their mandates, namely:

- The Executive Agency for Competitiveness and Innovation (EACI) becomes the Executive Agency for Small and Medium-sized Enterprises (EASME);
- The Executive Agency for Health and Consumers (EAHC) becomes the Consumers, Health and Food Executive Agency (CHAFEA);
- The Trans-European Transport Network Executive Agency (TEN-T EA) becomes the Innovation and Networks Executive Agency (INEA);
- The Education, Audiovisual and Culture Executive Agency (EACEA), the European Research Council Executive Agency (ERCEA) and the Research Executive Agency (REA), retain their original names.

4. Joint Undertakings

Essentially, the joint undertakings have been set up to attract private knowledge and capital, as public-private partnerships in key areas where research and development could contribute to Europe's wider competitiveness goals and where traditional instruments are not adequate ⁽¹⁾. The bodies will lead to the establishment of wide partnerships that will involve a large number of players from industry, including notably SMEs, the research community and wider society.

Seven joint undertakings were operating under the previous MFF ⁽²⁾. Of these seven joint undertakings, the ITER-F4E JU was set up for a longer period, bearing in mind the time required for its tasks as regards the development of fusion energy, whereas the other joint undertakings were set up for a more limited period, until 2017. Building on the experience gained with Joint Technology Initiatives (JTIs) during the current Seventh Research Framework Programme (FP7) and the clear commitments from the industry partners, JTIs under Horizon 2020 will benefit from a legal framework that is better suited to strong industrial involvement. Major simplification was achieved by making full use of the new provisions in the FR, which includes dedicated provisions on public-private partnerships, including the explicit recognition of JTIs as public-private partnership bodies with the possibility to apply financial rules better adapted to their specific needs.

⁽¹⁾ See also Chapter 17.3.

⁽²⁾ ITER — F4E: implementation of an international agreement on the development of Fusion Energy; IMI: Innovative Medicines Initiative on pre-competitive pharmaceutical R & D; FCH: Fuel Cells & Hydrogen technology research, to overcome market failure and to focus on developing market applications; Clean Sky: promoting clean Aeronautics and Air Transport technology development; ARTEMIS: development of key Embedded Computing Systems technologies; ENIAC: public-private partnership in the sector of nano-electronics technologies; SESAR: development of the new generation European air traffic management system.

For the period 2014–20, the Commission established ⁽¹⁾ six JTI within Horizon 2020, each with clearly defined objectives to achieve breakthroughs in the following areas:

- Innovative Medicines Initiative (IMI2): to improve European citizens' health and well-being by providing new and more effective diagnostics and treatments such as new anti-microbial treatments;
- Bio-based Industries (BBI): to develop new and competitive bio-based value chains that replace the need for fossil fuels and have a strong impact on rural development;
- Fuel Cells and Hydrogen (FCH2): to develop commercially viable, clean, solutions that use hydrogen as an energy carrier and of fuel cells as energy converters;
- Clean Sky (Clean Sky 2): to radically reduce the environmental impact of the next generation of aircraft;
- Electronic Components and Systems for European Leadership (ECSEL): to keep Europe at the forefront of electronic components and systems and bridge faster the gap to exploitation;
- Shift2Rail: to promote the shift to sustainable rail transport.

Four of these proposals represent the next stage for JTIs established under FP7 (including ECSEL JTI that merges the existing ARTEMIS and ENIAC JTIs). The Bio-based Industries JTI (BBI) and Shift2Rail have been identified as new initiatives.

In parallel with the JTIs, the Commission has proposed ⁽²⁾ to extend the SESAR (Single European Sky Air Traffic Management Research) Joint Undertaking under Horizon 2020. The SESAR JU coordinates the SESAR project, the technical pillar of the Single European Sky initiative which aims at modernising Air Traffic Management (ATM) in Europe. Due to its specific policy-orientated activities, SESAR was not set up as a JTI. The proposed extension will ensure that the coordination of research and innovation in the field of ATM is continued under Horizon 2020 in full consistency with the Single European Sky (SES) policy objectives.

⁽¹⁾ Council Regulations (EU) No 557-61/2014 of 6 May 2014 and Council Regulation (EU) No 642/2014 of 16 June 2014.

⁽²⁾ COM(2013) 503, 10.7.2013.

Chapter 17

Leverage effect

1. Financial Instruments

1.1. Introduction

Financial instruments are not new. For more than ten years, the EU budget has been using financial instruments such as guarantees and equity investment for SMEs. In the 2007–13 financial framework, a new generation of financial instruments have been put in place in cooperation with the EIB, including also risk-sharing arrangements, such as the Risk-Sharing Finance Facility (RSFF) under the Seventh R & D Framework Programme, or the Loan Guarantee Instrument for TEN-T projects (LGTT) ⁽¹⁾. In the area of structural funds, financial instruments have been set up to support enterprises, mainly SMEs, urban development and energy efficiency through revolving funds. However, there was no horizontal legal framework for these instruments in the FR. They were set up according to sector specific rules.

As outlined in the Communication “A Budget for Europe 2020 ⁽²⁾”, it is expected that financial instruments will be used more extensively in the 2014–20 MFF. In order to avoid fragmentation of the legal framework for financial instruments in sector-specific basic acts, the Commission considered it indispensable to include general rules and principles on financial instruments under the new Title VIII FR.

1.2. Definition and scope

According to Article 2(p) FR, financial instruments are: ‘Union measures of financial support provided on a complementary basis from the budget in order to address one or more specific policy objectives of the Union. Such instruments may take the form of equity or quasi-equity investments, loans or guarantees, or other risk-sharing instruments, and may, where appropriate, be combined with grants.’

A combination of financial instruments with other forms of support may take two different forms. Elements directly linked to a financial instrument (e.g. technical assistance, interest rate subsidies and guarantee fee subsidies) fall under the rules of Title VIII. In practice, this means that they are included in the contractual arrangement for the specific financial instrument (for example a delegation agreement). For elements not directly linked to financial instruments (e.g. a grant for the same large infrastructure project), separate contractual arrangements, including grant agreements, will be concluded ⁽³⁾.

At the EU level, financial instruments will be used in three main areas:

- Research, development and innovation (equity and risk-sharing instruments under the Horizon 2020 programme);

⁽¹⁾ The Commission reports about them annually to the Budgetary Authority on the basis of Article 38.5, 49.1(e) and 140.8 FR.

⁽²⁾ COM(2011) 500 final of 29.6.2011, p. 9.

⁽³⁾ See Articles 139(2) and (3) FR.

- Growth, jobs and social cohesion (including equity and guarantees under the Competitiveness and SME programme COSME, the Guarantee Facility under the Creative Europe programme and a Student Loan Facility under the Erasmus + programme);
- Transport infrastructure, energy, and Digital Agenda (Financial instruments under the Connecting Europe Facility).

Additionally, the ESIF can be used to implement financial instruments under shared management, in line with the rules defined in Title IV of Part Two of Regulation 1303/2013 ⁽¹⁾.

Sections 1.3 and 1.4 below focus on EU level instruments, i.e. in direct or indirect management. Direct management by the Commission is the exception.

Indirect management by certain categories of entities listed in Article 58(1)(c) FR:

- International organisations (e.g. EBRD, World Bank);
- EIB and EIF;
- Public bodies or private bodies with public service mission (e.g. KfW or *Cassa depositi e prestiti*).

1.3. Differences with regard to other forms of financial support

Financial instruments generally constitute a reimbursable form of financial assistance. Article 121(2)(c) FR therefore clarifies that financial instruments are not grants, which are a direct financial contribution by way of donation.

Further, the FR also specifies that shareholdings or equity participation in international financial institutions such as the European Bank for Reconstruction and Development (EBRD) or specialised Union bodies such as the European Investment Fund ⁽²⁾ are not classified as financial instruments.

Finally, financial instruments must be distinguished from borrowing-and-lending operations ⁽³⁾. Financial instruments constitute support from the budget, whereas borrowing-and-lending operations are off-budget transactions.

⁽¹⁾ Regulation 1303/2013 of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006, OJ L 347, 20.12.2013, p. 320.

⁽²⁾ Council Decision 94/375/EC of 6 June 1994 on Community membership of the European Investment Fund, OJ L173, 7.7.1994, p. 12.

⁽³⁾ See Chapter 20.

1.4. Principles and requirements

The general principles applicable to financial instruments are sound financial management, transparency, proportionality, non-discrimination and equal treatment ⁽¹⁾. The transparency principle is implemented through a set of detailed reporting ⁽²⁾ and publication ⁽³⁾ requirements.

Additionally, the FR contains some specific requirements ⁽⁴⁾:

- (a) Financial instruments should address market failures or sub-optimal investment situations, which have proven to be financially viable but do not give rise to sufficient funding from market sources;
- (b) Financial instruments shall not be aimed at replacing those of a Member State, private funding or another Union financial intervention (additionality);
- (c) non-distortion of competition in the internal market and consistency with State aid rules;
- (d) leverage effect: the Union contribution to a financial instrument shall aim at mobilising a global investment exceeding the size of the Union contribution according to the indicators defined in advance;
- (e) alignment of interest: when implementing financial instruments, the Commission shall ensure that there is a common interest in achieving the policy objectives defined for a financial instrument, possibly fostered by provisions such as co-investment, risk-sharing requirements or financial incentives, while preventing a conflict of interests with other activities of the entrusted entity;
- (f) financial instruments shall be established on the basis of on an *ex ante* evaluation, including an evaluation of the possible re-use of additional resources referred to in point (f) of paragraph 8.

Additionally, Title VIII (Articles 139 and 140) FR contains specific rules that strictly limit the risks of the Commission; in particular, expenditure made for a financial instrument and the Union's financial liability must be limited to the amount of the relevant budgetary commitment made to the financial instrument. Further, entrusted entities and financial intermediaries involved in the implementation shall comply with relevant standards and applicable legislation on the prevention of money laundering, the fight against terrorism and tax fraud. Moreover, there is a robust framework for the selection of financial intermediaries, detailed provisions on monitoring and a clause ensuring that the Court of Auditors and OLAF can exercise their tasks throughout the implementation chain.

The nature of financial instruments implies that normally the assistance is returned, e.g. the guarantee on a loan is paid back to the general budget when the loan is repaid to the intermediary and the guarantee is no longer needed. Therefore, it was necessary to define detailed

⁽¹⁾ Article 140(1) FR.

⁽²⁾ Articles 39(5), 49(1)(e) and 140(8) FR.

⁽³⁾ Article 35 FR and 21 RAP.

⁽⁴⁾ Article 140(2) FR.

rules for such reflows, which do not exist in a comparable form in the case of other financing mechanisms foreseen in the FR.

The relevant provision in the FR ⁽¹⁾ provides for a different treatment of two types of reflows attributable to the Union contribution, namely revenues (including dividends, capital gains, guarantee fees and interest on loans and on amounts on fiduciary accounts) and repayments (including capital repayments, guarantees released and repayments) of the principal of loans. Subject to specific derogations, revenues must be entered into the general budget, following the deduction of management cost and fees, and therefore cannot be re-used for the financial instruments. Repayments shall be re-used in the form of internal assigned revenues, normally for a period not exceeding the period for the commitment of appropriations plus two years. This reuse will also increase the leverage effect which may add value in view of fostering the achievement of the policy objectives under the specific instruments.

Finally, it is important to avoid that the amounts paid by the Commission to fiduciary accounts managed by entrusted entities on behalf of the Commission are disproportionately high. Payments to fiduciary accounts shall therefore be made by the Commission on the basis of payment requests that are duly substantiated with disbursement forecasts, taking into account the need to cover disbursements estimated under the specific instruments and the balances already available on the accounts. In case the amounts on the fiduciary accounts are sufficient to cover the contractually stipulated minimum reserve on the fiduciary accounts, as increased by the disbursement forecasts for the current financial year and to cover the amounts needed to exclude contingent liabilities in relation to payment obligations in currencies other than euro, no further payment to the fiduciary accounts shall be made ⁽²⁾. All these conditions are specified further in the delegation agreements between the Commission and entrusted entities involved in the implementation.

2. EU Trust Funds for external action

2.1. Context and purpose

In order to strengthen the international role of the Union in external action and development and to increase its visibility and efficiency, the Commission may create and manage Union trust funds for emergency, post-emergency or thematic actions.

Article 187 FR provides a legal basis for the establishment of such Union trust funds for external actions. Union Trust Funds are also foreseen in Article 4 of Regulation (EU) No 236/2014 laying down common rules and procedures for the implementation of the Union's instruments for external action as well as in Article 42 of the Financial Regulation applicable to the 11th EDF (European Development Fund).

⁽¹⁾ Article 140(6) FR.

⁽²⁾ Article 140(7) FR.

2.2. Establishment

Union trust funds are established only when there is added value to the Union intervention: they are created and implemented at Union level where their objectives, in particular by reason of their scale or potential effects, can be better achieved at Union level than at national level.

Union trust funds should entail clear Union political visibility and managerial advantages as well as better Union control of risks and disbursements of the Union and other donors' contributions. They should not be created if they merely duplicate other existing funding channels or similar instruments.

The Commission may create trust funds under an agreement concluded with other donors. The constitutive act of each trust fund defines the objectives of the trust fund.

The Commission submits its draft decisions concerning the creation, the extension and the liquidation of a Union trust fund to the competent committee provided for in the basic act under which the Union contribution to the Union trust fund is provided.

2.3. Implementation and financing

Implementation:

Union trust funds should be implemented in accordance with the principles of sound financial management, transparency, proportionality, non-discrimination and equal treatment, and in accordance with the specific objectives defined in each constitutive act.

Union trust funds are implemented directly by the Commission, with the exception of Union trust funds for emergency or post-emergency action, which may also be implemented indirectly by entrusting budget implementation tasks to entities pursuant to Article 58(1)(c) FR.

Contributions:

The contributions of the Union and of the donors are lodged in a specific bank account. The contributions of the Union are transferred to this account on the basis of payment requests that are duly substantiated with disbursement forecasts, taking into account the balance available on the account and the resulting need for additional payments. Disbursement forecasts are to be provided on an annual, or where appropriate on a semi-annual, basis.

Contributions are not integrated in the budget and they are managed by the Commission under the responsibility of the authorising officer by delegation.

Governance:

Although not integrated in the budget, the EU trust funds are managed in accordance with the FR to the extent necessary for the security and transparency of the use of Union funds. Thus, the Commission chairs the governing board established for each trust fund to ensure the representation of donors and to decide upon the use of the funds. Moreover, the accounting officer of a Union trust fund is the accounting officer of the Commission. He or she is responsible for laying down accounting procedures and chart of accounts common to all Union trust funds. The Commission's internal auditor and the Court of Auditors exercise the same powers over the trust fund as they do in respect of other actions carried out by the Commission. The specific

bank account of the trust fund is opened and closed by the accounting officer. The Commission ensures a strict separation of duties between accounting and authorising officers. Funds are committed and paid by financial actors of the Commission.

Management costs:

The Commission is authorised to withdraw a maximum of 5 % of the amounts pooled into the trust fund to cover its management costs from the years in which the contributions have begun to be used. For the duration of the trust fund, such management fees are assimilated to assigned revenue.

Recovery orders:

The accounting officer acts on the recovery orders relating to actions funded by the trust fund. Revenue arising from the repayment of these recovery orders are returned to the specific bank account of the trust fund.

Reporting:

The Commission submits annually a comprehensive and detailed report to the European Parliament and the Council on the activities supported by Union trust funds, on their implementation and performance, as well as on their accounts.

2.4. Duration and closure

Union trust funds are created for a limited duration determined in their constitutive act. This duration may be extended by a decision of the Commission upon request of the board of the trust fund concerned. The European Parliament and/or the Council may request the Commission to discontinue appropriations for that trust fund or to revise the constitutive act with a view to the liquidation of the trust fund, where appropriate. In such an event, any remaining funds should be returned on a pro rata basis to the budget as general revenue and to the contributing Member States and other donors.

3. Public-private partnerships

3.1. Introduction

During the last decade, public-private partnerships (PPP) developed in many fields falling within the scope of the public sector. Various factors explain the increased recourse to PPPs, mainly the desire to benefit in the public sphere from the know-how and working methods of the private sector and to leverage private capital.

EU-level PPPs were first introduced in the research and innovation area under the Seventh research Framework Programme in the form of Joint Technology Initiatives whereby the Union and the industry jointly funded and implemented certain areas of the programme. These initiatives were implemented through dedicated legal entities — Joint Undertakings — established under what was then the equivalent of the current Article 187 TFEU.

Six Joint Undertakings have been established in the areas of aeronautics (Clean Sky), air traffic management (SESAR), pharmaceutical research (Innovative Medicines Initiative), fuel cells and hydrogen (FCH), embedded systems (ARTEMIS) and nano-electronics (ENIAC).

These PPPs at EU level have proven to be a useful instrument to make EU spending more effective by pooling the complementary expertise and resources of the public and private sectors.

3.2. Different models of public-private partnerships

The 2012 revision of the Financial Regulation enshrined the concept of PPP bodies by distinguishing two main types of PPP bodies.

(1) PPP bodies set up by a basic act under the TFEU or the Euratom Treaty

At EU level, PPPs set up as Union bodies can either operate under the framework financial regulation for the bodies referred to in Article 208 FR ⁽¹⁾, i.e. the legal, financial and operational framework for the decentralised agencies (see Chapter 16), or under the model financial regulation specifically designed for PPP bodies, as further explained under point 3 below.

(2) A private entity entrusted with the implementation of a PPP

The FR includes a second possibility to implement PPPs under Article 58(1)(c)(vii): a private entity entrusted with the implementation of a PPP to which budget implementation tasks may be entrusted in indirect management ⁽²⁾.

Such entity may be any private entity pre-existing or established for the purpose of the PPP implementation under the national law of any Member State.

In accordance with the general rules governing the management of Union funds in indirect management, the concerned entity has to provide the same level of guarantees in terms of management and control of the Union funds as the public law bodies.

3.3. Simplified financial and legal framework

Article 209 FR establishes a simplified framework for operation of the PPP bodies at EU level by introducing a model financial regulation specifically designed for PPP bodies to be adopted by the Commission in the form of a delegated act (Article 290 TFEU).

The model financial regulation was adopted in September 2013 and entered into force on 8 February 2014 ⁽³⁾. This regulation lays down the principles on the basis of which PPP bodies referred to in Article 209 FR should adopt their own financial rules.

⁽¹⁾ Commission Delegated Regulation (EU) No 1271/2013 of 30 September 2013 on the framework financial regulation for the bodies referred to in Article 208 of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council, OJ L 328, 7.12.2013, pp. 42–68.

⁽²⁾ See Chapter 15.

⁽³⁾ Commission Delegated Regulation (EU) No 110/2014 of 30 September 2013 on the model financial regulation for public-private partnership bodies referred to in Article 209 of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council, OJ L 38, 7.2.2014, pp. 2–15.

In light of the experience up to now with the functioning of the Joint Undertakings set up under the Seventh Research Framework Programme, the model financial regulation establishes the necessary principles to ensure sound financial management of Union funds delegated to the PPP bodies while removing red tape to the maximum extent possible and taking into account the specific structure of PPP bodies and in particular the participation of the private sector in their budget.

The PPP bodies which will operate under this new legal framework will benefit from more flexible financial rules, notably: simplified reporting to the Commission in the planning phase of the budget; a simplified procedure for the adoption of the budget, including the staff establishment plan; increased flexibility in terms of staff and simplified procurement procedures (e.g. the possibility of using the procedures for low-value contracts for contracts up to the thresholds of the Procurement Directive, Service Level Agreements between Joint Undertakings and joint procurement with Member States, as well as with the private members of the PPP body).

Part 6
Accounting and control



Chapter 18

Consolidated annual accounts of the European Union

The consolidated annual accounts of the European Union are drawn up in accordance with Articles 141 to 148 FR.

The annual accounts comprise: (a) the financial statements (based on accrual accounting rules) and (b) the budgetary accounts (the reports on budget implementation prepared on a modified cash basis).

A dual accounting system is thus in place in the European Commission and other EU bodies so as to produce these two sets of accounts — the accounting system has both a general accounting element (based on accrual accounting rules) and a budgetary accounting element (based on cash accounting principles).

The consolidated annual accounts of the EU include all EU institutions, agencies and other bodies falling under the scope of consolidation.

1. Content of the financial statements

The financial statements of the European Union comprise the following elements:

1.1. Balance sheet

The balance sheet shows the financial position of the European Union at the end of each year, and all assets and liabilities are displayed. Both the assets and liabilities are further differentiated between current and non-current amounts. The difference between total assets and total liabilities is referred to as the ‘net assets’ of the European Union.

1.2. Statement of financial performance

The statement of financial performance displays the revenue and expenses of the European Union, on an accrual basis, for a given year. Revenue and expenses are recorded when the revenue is earned and the expenses are incurred, rather than simply when the cash is received or paid out.

Revenue is split on the face of the statement of financial performance between own resource and contribution revenue (such as VAT and other Member State contributions) and operating revenue. Operating revenues include such amounts as fines issued and the recovery of amounts previously paid out.

Expenses are shown on the statement of financial performance under the headings ‘Administrative expenses’ (such as staff and building costs) and the more significant ‘Operating expenses’. Information is given on the split of operating expenses by the different management types.

Finally, information is also presented in a ‘segment’ report, which provides a breakdown of operating revenues and expenses by policy area.

1.3. Cash flow statement

The cash flow statement provides an overview of the cash movements during the year. Cash flow information is used to assess the ability of the Union to generate cash and cash equivalents, and its need to utilise such cash flows.

1.4. Statement of changes in net assets

The statement of changes in net assets displays the movements in reserves and net assets during the year.

1.5. Notes to the financial statements

The notes to the financial statements provide further disclosures and explanations of the items mentioned above, including accounting policies and other disclosures. The notes also include details of the contingent assets and liabilities and other disclosures.

2. The principles and rules governing the accounts

The accounts are kept in accordance with the FR, generally accepted accounting principles and the EU accounting rules.

2.1. Accounting principles

The objective of financial statements is to provide information about the financial position, performance and cash flows of an entity in a form useful to a wide range of users, i.e. the service recipients and resource providers. For a public sector entity such as the European Union, the objectives are more specifically to provide information useful for decision making, and to demonstrate the accountability of the entity for the resources entrusted to it.

If they are to present a true and fair view, financial statements must not only supply relevant and reliable information to describe the nature and range of an entity's activities, explain how it is financed and supply definitive information on its operations, but also do so in a clear and understandable manner allowing comparisons between financial years. It is with these goals in mind that the European Union financial statements are drawn up. The qualitative characteristics of information included in the European Union financial statements are thus relevance, reliability, understandability and comparability. Other characteristics such as timeliness, verifiability, materiality, cost-benefit and balance between the qualitative characteristics are also taken into account so as to make information useful for accountability and decision-making purposes.

The general accounting system allows for the preparation of the financial statements as it contains all revenue and expenses recorded for the financial year (displayed in the statement of financial performance) and all assets and liabilities recorded (used to establish the financial position in the form of a balance sheet as at 31 December). It also provides the necessary accounting information for the preparation of the cash flow statement and the statement of changes in net assets.

As stated in Article 144 FR, the overall considerations to be applied in drawing up the financial statements are outlined in the EU accounting rules (see 2.3 below) and are:

- fair presentation;
- accrual-basis;
- going-concern basis;
- consistency of presentation;
- aggregation;
- offsetting;
- comparative information.

Preparation of the financial statements in accordance with the appropriate rules and principles requires management to make estimates that affect the reported amounts of certain items in the balance sheet and statement of financial performance, as well as the disclosures of contingent assets and liabilities.

2.2. The European Union's accounting rules

In accordance with Article 152 FR, all bodies that are included in the European Union consolidated annual accounts shall apply the European Union accounting rules, as adopted by the Accounting Officer of the Commission. These accrual accounting rules are based on the International Public Sector Accounting Standards (IPSAS). They are adopted and updated following the opinion of an Advisory Expert Group for Accounting Standards, which provides independent professional guidance on this matter, and following a consultation with the accounting officers of the other EU consolidated bodies.

3. Accounting policies

A summary of the most important accounting policies applied in the European Union is provided below.

3.1. Consolidation

The scope of consolidation for the European Union comprises controlled entities, associates and joint ventures. The complete list of consolidated entities can be found in the financial statements. Controlled entities are all entities over which the European Union has the power to govern their financial and operating policies so as to be able to benefit from their activities. This power must be currently exercisable. In practice this means the institutions, bodies and executive agencies of the European Union. These entities are consolidated using the full consolidation method.

3.2. Currency and basis for conversion

The consolidated financial statements are presented in euros, the euro being the European Union functional and reporting currency. Foreign currency transactions are converted into euros

using the exchange rates prevailing at the dates of the transactions. Year-end balances of monetary assets and liabilities denominated in foreign currencies are converted into euros on the basis of the exchange rates applying on 31 December of that year.

3.3. Balance sheet

1) Intangible assets and property, plant and equipment

Fixed assets are stated at historical cost less depreciation (excluding land) and impairment. Leases of assets, where the European Union has substantially all the risks and rewards of ownership, are classified as financial leases.

2) Investments and financial assets

Investments in associates (for example the European Investment Fund) and joint ventures are accounted for using the equity method.

Financial assets are recognised at fair value and subsequently measured at amortised cost (loans and receivables) or fair value (available for sale assets) depending on their nature.

3) Receivables

Receivables are carried at the original amount less write-down for impairment. A write-down for impairment of receivables is established when there is objective evidence that the European Union may not be able to collect all amounts due under the original terms of receivables. This does not mean that the European Union will not continue its efforts to recover these amounts.

4) Pre-financing amounts

Pre-financing is a payment intended to provide the beneficiary with a cash advance, i.e. a float. At year-end, outstanding pre-financing amounts are valued at the original amount(s) paid, less amounts returned, eligible amounts cleared, estimated eligible amounts not yet cleared at year-end and value reductions.

5) Inventories

Inventories are stated at the lower of cost and net realisable value, cost being determined using the first-in, first-out (FIFO) method. Net realisable value is the estimated selling price in the ordinary course of business, less the costs of completion and selling expenses.

6) Cash and cash equivalents

Cash and cash equivalents are financial instruments and defined as current assets. They are valued at their face value converted into euros at the rate applying at the end of the year.

7) Employee benefit obligations

The European Union includes a liability on its balance sheet to cover its employee benefit obligations, primarily pensions of its staff. The liability is valued at each year-end using actuarial techniques, in accordance with international accounting rules.

8) Provisions for risks and charges

Provisions for risks and charges are recognised when the European Union has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated.

9) Financial liabilities

Financial liabilities include primarily borrowings and they are recognised initially at fair value, i.e. their issue proceeds (fair value of consideration received) net of transaction costs incurred, then subsequently carried at an amortised cost using the effective interest method.

10) Payables

A significant amount of the payables of the Union are not related to the purchase of goods or services — instead they are unpaid cost claims from beneficiaries of grants or other Union funding. They are valued at the accepted eligible amount.

11) Accrued and deferred income and charges

In applying accrual accounting, it is necessary to ensure that income and expenditure are included in the correct accounting periods, regardless of when the cash is received or paid out. Therefore a significant effort is needed at each year-end to identify such amounts. In particular, an assessment has to be made of eligible expenses incurred by beneficiaries of Union funds but not yet reported (accrued charges). Different methods are used depending on the type of activities and the information available so as to arrive at a best estimate of these amounts. Conversely, some expenses are recorded in the current year although they relate to subsequent periods (deferred charges), so they have to be identified and included in the relevant future period.

Revenue should also be accounted for in the period to which it relates. At year-end, when a service has been rendered or supplies have been delivered or a contractual agreement exists (i.e. by reference to a contract) even though the invoice has not been sent, the amount should be assessed and recorded in the financial statements as accrued revenue. Conversely, when an invoice has been sent but does not relate to the reporting period, the amount should be deferred to a future period.

3.4. Revenue

Exchange revenue: revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods are transferred to the purchaser. Revenue from a transaction involving the provision of services is recognised by reference to the stage of completion of the transaction at the reporting date.

Non-exchange revenue makes up the vast majority of the Union's revenue and includes mainly direct and indirect taxes and own resource amounts. In addition to taxes, the European Union may also receive payments from other parties, such as duties, fines and donations.

3.5. Expenses

Exchange expenses arising from the purchase of goods are recognised when the supplies are delivered and accepted by the European Union and are valued at original invoice cost.

Non-exchange expenses account for the majority of the expenditure of the European Union. They relate to transfers to beneficiaries and can be of three types: entitlements, transfers under agreement, and discretionary grants, contributions and donations.

Transfers are recognised as expenses in the period during which the events giving rise to the transfer occurred, on condition that: the nature of the transfer is allowed by a Regulation (FR, Staff Regulations or another regulation) or a contract has been signed authorising the transfer; any eligibility criteria have been met by the beneficiary; and a reasonable estimate of the amount can be made.

When a request for payment or cost claim is received and meets the recognition criteria, it is recognised as an expense for the eligible amount. At year-end, incurred eligible expenses already due to the beneficiaries but not yet reported are estimated and recorded as accrued expenses.

3.6. Contingent assets and liabilities and other disclosures

1) Contingent assets

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the European Union. A contingent asset is disclosed when an inflow of economic benefits or service potential is probable.

2) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the European Union. In addition, a contingent liability may be a present obligation that arises from past events but is not recognised, either because an outflow of resources embodying economic benefits or service potential is unlikely to be required to settle the obligation or because the amount of the obligation cannot be measured with sufficient reliability. A contingent liability is disclosed unless the possibility of an outflow of resources embodying economic benefits or service potential is remote.

3) Commitments for future funding

A commitment for future funding represents a legal or constructive commitment, usually contractual, that the European Union has entered into and which may require a future outflow of resources.

4) Guarantees

Guarantees are possible assets or obligations that arise from past events and whose existence will be confirmed by the occurrence or non-occurrence of the object of the guarantee.

3.7. Use of estimates

In accordance with generally accepted accounting principles, the European Union's financial statements necessarily include amounts based on estimates and assumptions by management based on the most reliable information available. The use of estimates is an essential part of the accrual basis of accounting. Significant estimates include, but are not limited to, amounts for pensions, provision for future charges, valuation of publication stocks, financial risk on inventories and accounts receivable, accrued income and charges, contingent assets and liabilities, and degree of impairment of fixed assets. The methodology applied must be consistent. Actual results could differ from those estimates. Changes in estimates are reflected in the period in which they become known.

4. Budgetary accounts

The aggregated budgetary accounts referred to in Article 141 FR are based on the modified cash accounting principle ⁽¹⁾. They include the budget implementation reports, which aggregate all budgetary operations for the year and provide the budgetary result, plus explanatory notes and annexes (which provide more detail and comment on the information presented).

4.1. Budgetary principles

The budgetary principles are explained in Chapter 11, but in summary they are: unity and budget accuracy; annuality; equilibrium; unit of account; universality; specification; sound financial management; and transparency.

4.2. The budgetary implementation reports

According to Article 146 FR, the budgetary implementation reports set out all budgetary operations for a year in terms of revenue and expenditure. The structure is the same as that of the budget itself.

The budget result comprises the result of the European Union and the result of the participation of the EFTA countries. It represents the difference between total revenue received for that year and total payments made against that year's appropriations plus the total amount of that year's appropriations carried over to the following year.

The following are added to or subtracted from the resulting figure:

- the net balance of cancellations of payment appropriations carried over from previous years and any payments which, because of fluctuations in the euro rate, exceed the non-differentiated appropriations carried over from the previous year,
- the balance of exchange-rate gains and losses recorded during the year.

A budget result surplus is paid back to the Member States the following year by deduction from their contributions for that year.

⁽¹⁾ This differs from pure cash-based implementation because of elements such as carry-overs.

4.3. Revenue

The amounts of own resources entered in the accounts are those credited in the course of the year to the accounts opened in the Commission's name by the national treasuries and other bodies appointed by the Member States. The difference between the amount of VAT own resources and GNI-based resources entered in the budget and the amount actually due is calculated by the Commission and the resulting amount has to be settled by 1 December of the following year. This amount can be entered in the budget of that year via an amending budget. Other revenue entered in the accounts is the amount actually received in the course of the year.

4.4. Expenditure

For calculating the budget result for the year, expenditure comprises payments made against the year's appropriations for payments plus any of these appropriations that are carried over. Payments made against the year's appropriations for payments are payments validated by the authorising officer by 31 December. The payments taken into account for the European Agricultural Guarantee Fund and the European Agricultural Fund for Rural Development are those made by the Member States between 16 October year n-1 and 15 October year n.

5. The accounting closure process

5.1. Overview

The Accounting Officer of the Commission is required to prepare the consolidated annual accounts of the EU every year, submit them for audit by the European Court of Auditors (ECA) and then present them for adoption by the Commission. The main steps, as outlined in the FR Articles 147–148 are as follows:

- The provisional consolidated annual accounts of the EU are transmitted to the ECA by 31 March of the following year;
- The ECA provides its observations on these accounts by 15 June;
- The Accounting Officer of the Commission signs off the accounts and they are adopted by the Commission by 31 July;
- The ECA's annual report, including declaration of assurance, is presented by 15 November;
- The EU accounts are published in the Official Journal of the EU, together with the ECA's declaration of assurance, by 15 November.

5.2. Main elements of the process

1) Closure of the accounting system

The last payments are made on 31 December and the accounting system is closed for that financial year. The authorising officer services are then required to make standard closure entries, known as the cut-off exercise. According to Article 68(3) FR, the authorising officers shall guarantee the reliability of the accounting information provided for inclusion in the annual accounts.

2) Year-end cut-off exercise

A key element in preparing accrual-based accounts is ensuring that revenue and expenses are recorded in the accounting period to which they relate. Therefore, a significant exercise has to be performed by the European Union at each year-end to estimate the accounting entries that need to be made to assign revenue and expenses to the correct accounting periods. The result of this exercise is a very significant amount of accrued expenses appearing on the Union balance sheet.

Based on its accounting rules, the Union must evaluate and recognise in its financial statements the expenses to be financed by the general budget but which have not yet been declared by year-end. Consequently, many expenses are recognised under accrual accounting rules in year n although they may be actually paid in year $n+1$ using the budget of year $n+1$. Nevertheless, the Union can only call in resources from the Member States when they need money to pay an amount due. This inclusion of the Union's liabilities in the accounts, coupled with the fact that the corresponding amounts needed to fund these are only recognised in future years, results in liabilities greatly exceeding assets at year-end (i.e. negative net assets).

To present this situation in the most comprehensible way, a vertical balance sheet showing the Union's assets first, then its liabilities, was adopted. The difference principally represents the amounts to be called in from Member States. The existence of negative net assets simply reflects the difference between cash-based accounting and accrual accounting for an entity financed according to its cash-flow needs by the general budget. The budget does not take into account the obligation of Member States to provide the necessary resources in the future to pay for the expenses incurred when it falls due. It should be remembered that the Union cannot make a payment unless it is provided for in the budget, and all budgeted expenditure is covered by budgeted revenue from the Member States.

3) Consolidation of other entities

A consolidation of the Commission accounts together with the other bodies referred to in Article 208 FR is made by the accounting services of the Commission based on the accounts submitted by the accounting officers of these bodies.

4) Disclosures and explanations

The annual accounts contain significant explanatory notes and disclosures so as to respond to the information needs of users. The notes to the financial statements provide complete and clear explanations that enhance, complement and supplement those statements.

5) Preparation of other financial information

Additional reporting outside of, but linked to, the financial statements, can also play a significant role in communicating the information necessary to support the discharge of the Union's budget. Therefore, the Commissions Accounting Officer prepares other reports and communications for the addressees of financial reporting for informational and decision-making purposes.

The most important example is the annual Communication of the Commission to the Parliament and Council on the protection of the EU budget, which provides more extensive information than the annual accounts on the actions taken by the Commission and Member States to recover and/or reallocate amounts that have not been correctly spent by beneficiaries of EU monies.

Chapter 19

Internal control and external scrutiny of the budget

1. Principles

1.1 Internal control

The overall responsibility for the implementation of the EU budget lies with the European Commission. Article 317 TFEU states:

‘The Commission shall implement the budget in cooperation with the Member States, in accordance with the provisions of the regulations made pursuant to Article 322, on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management.’

The principle of sound financial management is spelled out in Article 30 FR, which requires that appropriations are used in accordance with the principles of economy, efficiency and effectiveness.

The Commission has a wide range of financial and managerial tasks. In line with existing financial rules, the internal arrangements set up by the Commission add up to a structure of robust control and management tools which allows the Commission to take its political responsibility for management by its Directors-General and Heads of Service.

While parts of the budget are implemented directly by the Commission services (direct management), the major proportion of the budget is managed in cooperation with the Member States under shared management, notably the Cohesion Policy and the Common Agricultural Policy. The Commission can also entrust budget implementation tasks to third parties (indirect management) such as national agencies, international organisations, third countries, the European Investment Bank or other bodies as defined in Article 58(1)(c) FR. In all these cases, effective and efficient internal control systems need to be set up to ensure that the policy and operational objectives are achieved. In the case of shared and indirect management the Commission needs to obtain assurance from the Member States and from the entrusted entities that the internal control systems are set up and are functioning properly.

Internal control is defined in Article 32(2) FR as follows:

‘... internal control is a process applicable to all levels of management and designed to provide reasonable assurance of achieving the following objectives:

- (a) effectiveness, efficiency and economy of operations;
- (b) reliability of reporting;
- (c) safeguarding of assets and information;
- (d) prevention, detection, correction and follow up of fraud and irregularities;
- (e) adequate management of the risks relating to the legality and regularity of the underlying transactions, taking into account the multiannual character of programmes as well as the nature of the payments concerned.’

The definition of internal control is wide; it is not limited only to financial aspects. An effective and efficient internal control system requires taking a view on risks and focusing control resources on areas where risk is the highest, while ensuring adequate control of all activities.

1.2. External scrutiny and accountability

Among other things, democratic control of the executive means that the executive has to account in public to the Parliament for its use of the public funds voted by parliament for its activities. This is the crucial moment for the executive. Does the democratically elected body consider that the executive has correctly used the funds voted by it for the policy purposes agreed? The Parliament needs an independent auditor to scrutinise what the executive has done and verify whether it has done what it was instructed to do and to report to the Parliament.

These principles are also reflected in the Treaties. Article 317 TFEU requires the Commission to implement the budget in cooperation with the Member States, in accordance with Article 322 TFEU. Article 318 TFEU requires the Commission to submit the annual accounts and a financial statement of assets and liabilities to the Council and the European Parliament. Articles 285, 286 and 287 establish an independent Court of Auditors that carries out the annual audit and reports to Parliament and Council each year. Article 319 gives the European Parliament the power to grant discharge to the Commission for the implementation of the budget, upon a recommendation from the Council and taking into account the work of the European Court of Auditors (hereafter the 'Court') and the work of the Commission.

The Parliament is helped in the discharge procedure by the Court, which 'shall carry out the Union's audit' (Article 285 TFEU). The Court is an independent institution of the Union (Article 286) and assists the European Parliament and the Council in exercising their powers of control over the implementation of the budget (Article 287).

2. Internal control in the Commission

The European Commission's governance structure is defined by the Treaties. It has evolved to match the Commission's changing role and to reflect advances in European governance. The Commission's internal governance framework fully empowers authorising officers by delegation and defines the control and accountability structures to be put in place to ensure sound financial management. Over the years, this framework has been adapted in the light of experience.

2.1. Management accountability in the Commission

Article 317 TFEU gives the Commission responsibility for implementing the EU budget. The College delegates the operational implementation of policy and operational objectives to the Directors-General and Heads of Service, who, as Authorising Officers by Delegation (AODs) receive the means to act. The FR constitutes the legal basis for the decentralised financial and accountability arrangements and defines the responsibilities of each financial actor. The delegation of power for the management of the funds is decided annually through the Internal Rules based on the approved budget structure of the year. The AODs are responsible for the

sound financial management of resources and for setting up effective and efficient internal control systems to ensure the achievement of policy and operational objectives.

To assist the Directorates-General (DG) and Heads of Services in implementing internal controls, the Commission has adopted a set of Internal Control Standards for effective management, based on international good practice ⁽¹⁾. The FR requires that the organisational structure and the internal control systems used for the implementation of the budget are set up in accordance with these standards. DGs and Services are required to put in place monitoring measures to assess whether the internal control systems are effective and report on the outcome annually in the Annual Activity Report. The standards are flexible, allowing services to tailor their interpretation to their own specific environment.

Annual Activity Report by the Directors-General and Heads of Service

The Annual Activity Report (AAR), together with the AOD's declaration of assurance, is the main instrument of internal accountability within the Commission. It is a management report of each Director-General and Head of Service to the College in which he or she gives account of the achievements of the key policy objectives and core activities of the DG or Service, taking into account the corresponding resources used during one year's activities. In the AAR, the Directors-General and Heads of Service are required to draw a conclusion on the efficiency and effectiveness of the internal control systems in their DG or Service, including an overall assessment of the costs and benefits of the controls they carry out.

The report includes a signed declaration of assurance in which the Director-General or Head of Service takes his or her responsibility as AOD by stating whether the information contained in the report gives a true and fair view, whether he or she has reasonable assurance that the resources assigned to the activities described in the report have been used for their intended purpose and in accordance with the principle of sound financial management, and whether the control procedures put in place give the necessary guarantees concerning the legality and regularity of the underlying transactions. The statement may contain reservations where there are significant issues affecting the declaration of assurance. In all cases, action plans must be established to address the identified weaknesses.

Although the prime responsibility for internal control rests with Directors-General and Heads of Service, with appropriate delegation to their staff, Resource Directors have a role in overseeing internal control within their DG or Service based on information provided by those responsible for implementing the systems. They are required to sign a statement in the AAR certifying that the information provided in the report and annexes is accurate and exhaustive. The competent Commissioner supervises the implementation of the budget by the Director-General or Head of service.

The quality of the AAR is vital as they form the basis of the Commission's acceptance of responsibility for the management of its activities. The AARs also contain information useful for other interested parties, namely those who have the mission to scrutinise the management of EU funds by the Commission: the European Parliament and the Council. The AARs are

⁽¹⁾ COSO (Committee of Sponsoring Organizations) framework — <http://www.coso.org/>.

also increasingly being used as complementary evidence by the Court in its assessment of the supervisory and control systems. Finally, they are all made available to the citizens on the Europa website of the Commission. The quality and consistency of the various AAR is ensured by a peer review exercise carried out by the Central Services (Secretariat General and DG Budget) and the annual revision of the guidelines for the preparation of the AARs in light of the experience of the peer reviews and the annual discharge process. This is evidence of continued efforts by the Commission to strengthen the AARs as management reports.

Annual synthesis report on management achievements by the Commission

Through the Synthesis report on management achievements the Commission assumes its political responsibility for management by its Directors-General and Heads of Service. The synthesis is drawn up by the Secretariat-General and is mainly based on the AARs, the DG Budget Overview report on the state of internal control and the Commission's Internal Audit Service's annual Overall Opinion on the Commission's financial management.

The synthesis report is the main document in which the Commission takes stock of the management achievements of the DGs and Services, including the progress being made with regard to internal control. It represents the political expression of the College on the issues raised by Directors-General in individual AARs and on the recommendations and actions planned to address any weaknesses identified. It also constitutes the formal means by which the European Parliament and the Court are informed of such issues. The synthesis is transmitted to the Discharge Authority (i.e. the European Parliament), the Council and to the Court at the latest by 15 June each year.

Accounting Officer of the Commission

The Commission's Accounting Officer executes payment and recovery orders approved by AODs and is responsible for managing the treasury; laying down accounting rules and methods, validating accounting systems, keeping the accounts and drawing up the institution's financial statements, as well as for consolidating these accounts with those of the other institutions. The Accounting Officer also signs off the accounts, certifying that (s)he has made the checks that (s)he considers necessary and is satisfied that they have been prepared in accordance with the accounting rules, methods and accounting systems established under his/her responsibility, that (s)he has made any adjustments which are necessary for a true and fair presentation of the accounts in accordance with the financial rules, and that they are therefore reliable.

DG Budget's role with respect to internal control and accountability within the Commission

The DG Budget (Central Financial Service) assists the Commission in the achievement of its policy and management objectives, allowing the College to take overall political responsibility for the management by its AODs and the reasonable assurance as declared by them. The DG Budget, in close cooperation with the Secretary General, is responsible for monitoring the quality of the AAR, compliance with the Standing Instructions and consistency throughout the Commission. This is notably achieved by the annual revision of the Standing Instructions and the peer review exercise.

Whereas DG Budget is not responsible for the internal control systems in the DGs and Services, it plays a key role in supporting the DG and Services in setting-up and ensuring the effective

functioning of the internal control systems. This is achieved by promoting sound internal control techniques and providing methodological guidance, implementation tools and advice to Commission services based on best professional standards. DG Budget also provides expert advice on the definition, design and development of the Commission accountability structures and its internal control systems, and by monitoring their effective implementation by the AODs.

The DG Budget also reports annually on the state of internal control in the Commission in the overview report. The report is based on a desk review of the services' AARs and takes account of key developments in risk management and internal control as well as findings reported by the Court and the Internal Audit Service as well as any other relevant available information. The report summarises the main findings and conclusions resulting from the analysis of the management reports and other available information and maps the possible way forward.

2.2. Internal audit architecture in the Commission

The Internal Audit architecture in the Commission is structured as follows:

- the Internal Audit Service (IAS), which is a centralised internal audit function;
- the Internal Audit Capabilities (IACs), which are a decentralised audit function at the level of Directorates-General or Services. The IACs are independent from the IAS;
- the Audit Progress Committee (APC).

Internal Audit Service

The IAS is a Service of the Commission headed by the Internal Auditor of the Commission. The mission of the IAS is to provide to the institution independent, objective assurance and consulting services designed to add value and improve the operations of the Commission. The IAS helps the Commission accomplish its objectives by bringing a systematic, disciplined approach in order to evaluate and make recommendations for improving the effectiveness of risk management, control and governance processes.

The IAS's operational responsibilities include the development and establishment of audit procedures, the creation and maintenance of the risk-based audit strategie and annual plan, the coordination of work with the IACs and the Court. Furthermore, the IAS maintains a quality assurance programme that covers all its activities and establishes a follow-up process in order to monitor the implementation of its recommendations and inform the Audit Progress Committee accordingly.

The IAS adheres to the International Standards for the Professional Practice of Internal Auditing as drawn up by the Institute of Internal Auditors.

Internal Audit Capabilities

The IACs were established in 2001 and are found in each Commission Directorate-General or Service. In line with the applicable professional standards, the mission of the IACs is also to provide independent and objective assurance and consulting services designed to add value and improve the operations, but only within their DG/ Service.

In general, the IACs' role is to assist the Director-General and management in controlling risks and monitoring compliance with the Internal Control Standards. They provide an independent and objective opinion on the quality of management and internal control systems and make recommendations in order to improve the efficiency and effectiveness of operations and to ensure economic use of resources.

The IACs adhere to the International Standards for the Professional Practice of Internal Auditing as drawn up by the Institute of Internal Auditors.

An internal network (Auditnet) has been created to provide a forum where the IACs and the IAS share their methodologies and experiences.

Audit Progress Committee

The Audit Progress Committee (APC) assists the College of Commissioners in fulfilling its obligations under the Treaties and under other statutory instruments and agreements by ensuring that the work of the IAS, IACs and of the Court is appropriately taken into account and followed up by Commission Services. The Committee has no management powers.

The APC reports annually to the College of the Commissioners and ensures that the risks that might affect the achievement of the Commission's objectives are appropriately managed.

The APC has nine members comprised of seven Commissioners, including the Commissioner for Taxation and Customs Union, Audit and Anti-Fraud, who chairs the Committee, and two external members with proven professional expertise in audit and related fields.

The Committee ensures the independence of the IAS. It monitors and draws the attention of the College to the reports of the IAS, the implementation by Commission Services of the Court's recommendations and the audit matters related to the resolutions adopted by the discharge authorities. In exceptional cases, the APC may make proposals for the IAS or IACs to carry out audits where a particular need is perceived. At the request of the APC, the IAS or IACs should provide all of the information necessary for the Committee to carry out its functions.

2.3. Actions to improve the internal control framework

The new requirements in the revised FR have a far-reaching impact on management accountability and reporting. In response to these requirements, the services across the Commission are required to review their control strategies and systems in order to ensure that they are cost-effective and proportional to the risks. The primary purpose of assessing the cost-effectiveness of controls is to support internal management, fostering effective decision-making throughout the Commission, which in turn should contribute to the efficient and economic use of resources. This requires rethinking control strategies and systems to ensure higher control intensity and frequency on riskier areas and that controls consistently add value.

3. External scrutiny by the European Court of Auditors

3.1. Historical background and Treaty mandate

The Court was set up by the 1975 Brussels Treaty and was installed on 1 July 1977, meeting for the first time on 18 October 1977.

The Maastricht Treaty promoted the Court, in 1993, to the rank of a European Community institution (Article 7 of the EC Treaty) and introduced the requirement for the Court to publish an annual statement of assurance (known as DAS, from the French *declaration d'assurance*) on the reliability of the Communities' accounts and on the legality and regularity of the transactions underlying these accounts. This statement is published as part of the annual report on the accounts of the European Union.

The Amsterdam Treaty gave the Court the status of a European Union institution, thus enlarging the Court's audit scope to cover the policy areas referred to at that time as the second and third pillars of the Union (foreign and security policy, and justice and home affairs). It also extended the Court's mandate, asking it to assess the assurance by major sector of the budget. The DAS constitutes a genuine certification of the accounts, a task very different in nature from the traditional tasks of the Court, which were preparing and publishing observations or drawing up opinions on legislative and other proposals with important financial consequences. The Court also provides a separate statement of assurance relating to the accounts of the European Development Fund (EDF) and the underlying transactions.

The Nice Treaty provided that the statement of assurance 'may be supplemented by specific assessments for each major area of Community activity'.

Unlike certain national supreme audit courts, the Court has no judicial powers. Nor does it have any power to take decisions, impose penalties or give orders. Article 287 TFEU requires the Court to examine the accounts of all revenue and expenditure of the Union. The Court aims to contribute to improving the financial management of Union funds, so as to ensure maximum value for money for all citizens of the Union. All bodies set up by the Union are included where the relevant constituent instrument does not preclude such examination.

The Court can also prepare special reports on specific questions and may give an opinion on draft legislation.

3.2. The Court's mission

The Court independently audits the collection and spending of Union funds and assesses the way that the European institutions discharge these functions. It examines whether financial operations have been properly recorded, legally and regularly executed, and managed so as to ensure economy, efficiency and effectiveness. It makes the results of its work known through the publication of relevant, objective and timely reports. In its work, the Court aims to contribute to improving the financial management of Union funds at all levels, so as to ensure maximum value for money for the citizens of the Union.

1) Coverage of the annual audit

The accounts of the European Union to be scrutinised comprise the consolidated financial statements and aggregated budgetary accounts. A description of the content of these annual accounts is to be found in Chapter 18.

The annual audit covers the accounts relating to the general budget and the accounts of the EDF, which is not included in the budget.

2) Documentation and information required

The Court's investigative powers are very extensive, as set out in Article 287(4) TFEU and detailed in Articles 158 to 163 FR. It may, among other things, request the institutions, the Member States, and the bodies administering revenue or expenditure to provide any document or information it considers necessary to carry out the tasks entrusted to it by the Treaties.

The audit is based on records and, if necessary, performed on the spot in the Union institutions and in the Member States, at the premises of anybody that manages revenue and expenditure on behalf of the Union or any natural or legal person in receipt of payments from the Union budget.

The Court receives regular information about the implementation of the budget throughout the year. Once a month within 10 working days following the end of each month, the Commission's accounting officer sends to the European Parliament and to the Council, as well as to the Court, in electronic form, figures, aggregated at chapter level at least, on the implementation of the budget, both for revenue and for expenditure against all appropriations.

Three times a year, within the 30 working days following 31 May, 31 August and 31 December, the Commission's accounting officer sends to the European Parliament and to the Council, as well as to the Court, a report on the implementation of the budget, covering both revenue and expenditure broken down by chapter, article and item (Article 15 FR).

The Commission also has to present a report on budgetary and financial management for the financial year in question as well as the provisional accounts, which are sent to the Court by 31 March of the following year.

In addition, the Commission has to send the provisional accounts before 31 March of the following year to the Court.

Once a year, the Commission also sends to the European Parliament and to the Council, as well as to the Court, information on budgetary guarantees and the corresponding risks (Article 149 FR).

The Commission also provides to the Court the annual activity reports of the Directors-General and heads of service, the 'Synthesis' report and the Commission's annual summary of the audits undertaken by the IAS, which keeps the Court fully informed of the work it undertakes.

3) The Court's reports

The findings of the Court's audit are set out in an annual report ⁽¹⁾, the draft of which is sent to the institutions not later than 30 June of the year following the closure of the year under audit.

They are based on statements of preliminary findings (SPFs) sent by the Court to Commissioners, Commission Directorates-General and/or national government departments, via their supreme audit institutions, in which the Court sets out its observations arising from findings made during audits. The statements are sent to the auditees to obtain their replies, and can form part of the content of a special report or part of the annual report. The Court requests

⁽¹⁾ Article 287(3) TFEU.

confirmation of the accuracy of its findings, proof where the findings are contested, and the provision of further details.

The annual report is published in the *Official Journal of the European Union*, together with the replies of the institutions, by 15 November of the same year ⁽¹⁾.

In addition to this annual report, the Court may at any time submit observations on specific questions — for example in the form of special reports — and deliver opinions at the request of one of the other institutions of the Union ⁽²⁾. These too are published as a rule.

The Court adopts its reports and opinions by a majority of its members ⁽³⁾.

4) The work of the Court has several facets

These clearly reflect the two complementary approaches that generally underpin the external scrutiny of public finances:

- (a) Audits of the annual accounts — the more traditional approach — are common to all external audit bodies. This involves examining the accounts and supporting documents to assess whether the annual accounts provide a true and fair view of the Union's financial activities during the year and the Union's financial position at year-end.
- (b) Audit of the underlying transactions to ensure that the accounting and financial operations have been conducted in a proper manner and in accordance with the relevant legal rules (treaties, secondary legislation, agreements, contracts, etc.) This is the 'financial audit' in the strict sense of the term. This leads to the DAS.
- (c) The audit of sound financial management represents a different type of scrutiny that is essentially qualitative: the object is to ensure that the internal control systems and resulting decisions taken by the Union executive allow an optimum balance to be achieved between attaining a given objective and the means used, in terms of economy, efficiency and effectiveness ⁽⁴⁾:
 - The check on economy consists of verifying that the resources used are made available in due time, in the appropriate quantity and quality and at the best price;
 - The check on efficiency concerns the best relationship between the resources employed and the results achieved;
 - The measurement of effectiveness concerns the attainment of the specific objectives set and the achievement of the intended results.

5) Cooperation with national supreme audit courts

The Court, as the EU's external audit institution, seeks good contacts and working relations with similar organisations all over the world. Particular attention is given to the Supreme Audit

⁽¹⁾ First sub-paragraph of Article 287(4) TFEU and Article 162(4) FR.

⁽²⁾ Second sub-paragraph of Article 287(4) TFEU.

⁽³⁾ Third sub-paragraph of Article 287(4) TFEU.

⁽⁴⁾ Article 3 FR.

Institutions (SAIs) in Europe, where cooperation with the SAIs of EU Member States (required under Article 287(3) TFEU ⁽¹⁾) and EU candidate and potential candidate countries is amply justified by the fact that the Member States collect and pay out the lion's share of Union revenue and expenditure and that accession states also have control responsibilities over pre-accession funding.

The objective of this cooperation is closely linked to the Court's responsibility for the audit of EU funds. As these funds generally pass through the national administrations of the countries concerned and the respective SAIs audit those administrations, close cooperation between the Court and national SAIs is essential for effective and efficient implementation of the Court's tasks.

The Court applies generally accepted international public sector auditing standards, and international cooperation provides valuable opportunities to exchange views and experiences on their use.

Nevertheless, at the time of writing of this publication, the reliance of the Court on audit work performed by SAIs is practically non-existent.

4. Political control exercised by the European Parliament

Although budgetary powers are shared between the European Parliament and the Council, the former assumes the essential responsibility for political control over the implementation of the budget under Article 319 TFEU, Article 180b of the Euratom Treaty and under Articles 164 to 167 FR.

4.1. Constant monitoring of budget implementation during the financial year

1) Development of the procedure

Historically, the Parliament as an institution was first given responsibility for *ex post* control through preparation of the decision giving discharge. The Parliament set up a specialised committee, the Committee on Budgetary Control (CONT, which began life as a mere sub-committee of the Committee on Budgets), which gradually imposed a system whereby budget implementation is monitored constantly.

The Maastricht Treaty enshrined this in law through changes to Article 276(2) of the EC Treaty (now Article 319(2) TFEU), which introduced a system for hearing evidence from the Commission on the implementation of expenditure or the operation of financial control systems, as part of the preparation of the discharge. This Article also provides that the Parliament can ask for documents concerning 'any other purpose in connection with the exercise of the Commission's powers over the implementation of the budget'.

In practice, in agreement with the Commission, the CONT acquired the right to obtain relevant documents or information from the Commission departments in the field of budgetary control, subject to specific requests and confidential handling in a secure archive

⁽¹⁾ Article 287(3) TFEU calls on the Court and national audit institutions to 'cooperate in a spirit of trust while maintaining their independence'.

upon agreement between the Parliament or its relevant body and the Commission. The Commission also accepted that Union officials could be called on by the committee to give evidence.

The Framework Agreement of 20 November 2010 on relations between the European Parliament and the Commission formalised the arrangements for transmitting confidential information to the Parliament, particularly as regards the annual discharge procedure (see point 31 and Annex II).

The CONT has also been refining its competences and responsibilities in successive revisions of the Parliament's internal rules of procedure. These permit scrutiny on many different fronts, although the discharge procedure forms the main component. The CONT examines the accounts, financial statements and analyses mentioned above and submits its conclusions to the full House, which adopts the decision giving discharge.

2) Powers of inquiry

The Parliament has extensive powers of investigation. Article 226 TFEU reads as follows:

'In the course of its duties, the European Parliament may, at the request of a quarter of its component Members, set up a temporary Committee of Inquiry to investigate, without prejudice to the powers conferred by the Treaties on other institutions or bodies, alleged contraventions or maladministration in the implementation of Union law, except where the alleged facts are being examined before a court and while the case is still subject to legal proceedings.

The temporary Committee of Inquiry shall cease to exist on the submission of its report.

The detailed provisions governing the exercise of the right of inquiry shall be determined by the European Parliament acting by means of regulations on its own initiative in accordance with a special legislative procedure, after obtaining the consent of the Council and the Commission.'

Although this article is not designed exclusively to cover financial matters, it may enable the Parliament, in appropriate cases, to examine the substance of allegations of infringements or maladministration relating to budget implementation.

4.2. Budget discharge

1) Definition and significance

The discharge is the decision taken by the authority empowered to do so (Parliament), after having received a recommendation from the Council, releasing the executive (Commission) from any further liability in respect of its management of the budget, thus marking final closure of the budget. It is a decisive moment. At worst, it can lead to a vote of no confidence in the Commission or similar actions.

The discharge procedure is provided for in Article 319 TFEU and set out in detail in Articles 164 to 167 FR and in Annex VI of Parliament's rules of procedure, to which Rule 76 of these rules refers.

The discharge decision is the culmination of a procedure that starts in year $n+1$ (n being the year in which the budget concerned is implemented) and is normally completed by 15 May of year $n+2$.

After the Council has drawn up a recommendation, the Parliament examines the accounts, financial statement and the evaluation report referred to in Article 318 TFEU, the annual report and any relevant special reports by the Court, together with the replies of the audited institutions to the observations of the Court, and the DAS referred to in Article 287 TFEU. For this purpose, the Court examines whether revenue and expenditure have been properly and lawfully received and incurred, checks that financial management has been sound and, in particular, points out any irregularities. The DAS deals specifically with the reliability of the accounts and the legality and regularity of the underlying transactions.

By 15 May of year $n+2$ the Parliament gives a discharge by voting on the draft decision and resolution drawn up by CONT. In accordance with Article 231 TFEU, the Parliament takes the decision by an absolute majority of the votes cast.

The Commission must take all appropriate steps to act on the observations in the decision giving discharge and on the comments accompanying the Council's discharge recommendations. If so requested by the European Parliament or the Council, the Commission must report on the measures taken in the light of these observations and in particular on the instructions given to the departments responsible for the implementation of the budget. These reports are also sent to the Court.

In preparation for the discharge debate, the Parliament (or the Council in the course of drawing up its recommendations) may request further information. In this event, it postpones the discharge decision and notifies the Commission of the reasons, so that it can take, as quickly as possible, whatever steps may be necessary to overcome the obstacles preventing the Parliament from taking action.

The discharge decision has a double significance. First, it is the budgetary discharge authority's political verdict on the manner in which the Commission exercises its responsibility for implementing the budget. Secondly, in a purely technical, accounting sense, it paves the way for the final closure of the accounts.

As a rule, discharge is based on the examination of:

- the accounts and the financial statement;
- the evaluation report referred to in Article 318 TFEU;
- the annual report and relevant special reports by the Court;
- the DAS (as to the reliability of the accounts and the legality and regularity of the underlying transactions, as provided for in Article 287(1) TFEU);
- the Council's recommendation prior to discharge;
- other reports and information provided by the Commission on the implementation of the budget.

2) Annual discharge procedure

In accordance with Article 319 TFEU, Articles 147, 148, and 158 to 166 FR lay down the following stages and timetable:

- The accounting officers of the other institutions and bodies send to the Commission's accounting officer and to the Court by 1 March of the following year at the latest their provisional accounts together with the reporting package;
- The Commission's accounting officer consolidates these provisional accounts with the Commission's provisional accounts and sends to the Court, by 31 March of the following year at the latest, the Commission's provisional accounts together with the provisional consolidated accounts of the Union;
- Each institution and body also sends a report on budgetary and financial management to the European Parliament, the Council and the Court by 31 March of the following year;
- By 1 June at the latest, the Court makes its observations on the provisional accounts of each institution and each body;
- The institutions other than the Commission and each of the bodies draw up their final accounts and send them to the Commission's accounting officer, the Court, the European Parliament and the Council by 1 July of the following year at the latest for the final consolidated accounts to be drawn up;
- The Commission's accounting officer draws up the final consolidated accounts on the basis of this information presented by the other institutions and bodies. The final consolidated accounts are accompanied by a note drawn up by the Commission's accounting officer in which the latter declares that they were prepared in accordance with Title IX FR and with the accounting principles, rules and methods set out in the notes to the financial statements;
- After approving the final consolidated accounts and its own final accounts, the Commission sends them both to the European Parliament, the Council and the Court by 31 July of the following financial year;
- The final consolidated accounts are published in the *Official Journal of the European Union* together with the DAS given by the Court in accordance with Article 287 TFEU and Article 160a of the Euratom Treaty by 15 November of the following financial year;
- The Court transmits to the Commission and the institutions concerned, by 30 June at the latest, any observations that are in its opinion such that they should appear in the annual report. These observations must remain confidential. Each institution sends its reply to the Court by 15 October at the latest. The replies of institutions other than the Commission are sent to the Commission at the same time;
- The Court transmits to the authorities responsible for giving discharge and to the other institutions, by 15 November at the latest, its annual report accompanied by the replies of the institutions and ensures their publication in the *Official Journal of the European Union*;

- As soon as the Court has transmitted the annual report, the Commission immediately informs the Member States concerned of the details of the report which relate to the management of the funds for which they are responsible under the applicable rules. Following receipt of this information, the Member States must reply to the Commission within 60 days. The latter transmits a summary to the Court, the European Parliament and the Council before 28 February;
- The European Parliament may ask to hear the Commission give evidence on the execution of expenditure or the operation of financial control systems. After having heard the Commission and assessing the information provided, and upon a recommendation from the Council acting by a qualified majority, the Parliament gives discharge to the Commission, by 15 May of year $n+2$, for the implementation of the budget for year n ;
- If this date cannot be met, the European Parliament or the Council informs the Commission of the reasons for postponement (Article 164 FR). If the European Parliament postpones the decision giving discharge, the Commission has to make every effort to take measures, as soon as possible, to remove or facilitate removal of the obstacles to that decision;
- The Parliament decides on the discharge by voting on the draft decisions and motions for a resolution prepared by CONT by a majority of votes cast (in accordance with the general rules in Article 231 TFEU).

3) The role of the Council

The Council's scope for intervention is limited to the drafting of the recommendation addressed to Parliament at the outset of the discharge procedure. Although not legally binding, this recommendation is significant. In practical terms, the Council's Budget Committee analyses the annual report of the Court and questions the Commission and the Court before submitting a draft recommendation to the Ecofin Council. The Council President presents the recommendation to the Parliament's CONT before that committee votes its discharge report.

Parliament pays close attention to the technical analysis underpinning the recommendation, and the Commission is required to follow up the recommendation.

4) The role of the Member States

The Lisbon Treaty has reinforced the Member States' responsibilities with regard to the implementation of the EU budget. Article 317(1) TFEU states that the Commission shall implement the budget in cooperation with the Member States and that Member States shall cooperate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management. This provision has importance as for some 80 % of the budget, Member States are directly involved in the management. The FR and the sector related rules are further defining the Member States' concrete responsibilities and implementation tasks.

5) Exceptional cases: postponement and refusal of discharge

(a) Postponement of discharge

When preparing the discharge debate, Parliament may find that certain points relating to implementation have not been made sufficiently clear. In this case, the discharge decision is postponed and the Commission is informed of the reasons for this postponement (Article 164 FR).

The Parliament may postpone the discharge decision:

- in order to impose on the Commission certain conditions which must be fulfilled beforehand (1996 discharge) ⁽¹⁾;
- in order to have more time to examine all the documents (as was the case, on the eve of the June 1979 elections, with the discharge for 1977);
- when the Commission has been asked to amend some of the documents on which the discharge is to be based (as was the case for the 1980 and 1985 discharges) or to provide further information (1990 discharge). The procedure for dialogue between the Parliament and the Commission laid down in Article 319 TFEU, introduced by the Maastricht Treaty, is designed to avoid recourse to refusal of discharge where Parliament's reluctance to vote the discharge may be overcome by obtaining supplementary information.

Should it be decided to postpone the discharge, Article 164 FR calls for the rapid removal of the obstacles.

(b) Refusal of discharge

Neither Article 319 TFEU nor the FR makes any provision for the principle of refusing discharge, let alone the procedure for doing so. These points are covered by Articles 3 and 5 of Annex VI to the Parliament's rules of procedure.

A decision by the Parliament to refuse the Commission a discharge because of serious objections must be considered exceptional. Discharge has in fact only been refused twice — in 1984 in respect of the 1982 financial year and in 1998 in respect of the 1996 financial year.

Since then the European Parliament has laid down a procedure in its rules of procedure:

- The first decision on the discharge can only be to grant or to postpone discharge (for 6 months); if a proposal to grant discharge is not adopted, it will be deemed to be postponed; if a proposal to postpone discharge fails to secure a majority, it shall be deemed granted;
- after a postponement, the second decision can only be to grant or to refuse discharge; separate decisions on the closure of the accounts and on the discharge itself are taken in case of postponements or refusal of the discharge.

Experience has shown that this political reasoning has no legal relevance. First, after the discharge for 1982 was refused in November 1984, the Commission (presided over by Gaston Thorn and only a few weeks from the end of its term) did not resign. Acknowledging that the closure of the budgetary cycle was unavoidable, Parliament eventually gave the discharge for 1982 on 15 March 1985.

Second, when the discharge for 1996 was refused in 1998, the Commission, under Jacques Santer, did not resign until March 1999 following a report by a Committee of Independent Experts, the content of which suggested that the Parliament might adopt a censure motion.

⁽¹⁾ Resolution of 31 March 1998 (OJ C 138, 4.5.1998, p. 29).

A special procedure governs the adoption of a censure motion, which requires a majority of the Parliament's members and two thirds of the votes cast.

6) Follow up

Article 319 TFEU requires that:

'The Commission shall take all appropriate steps to act on the observations in the decisions giving discharge and on other observations by the European Parliament relating to the execution of expenditure, as well as on comments accompanying the recommendations on discharge adopted by the Council.'

Article 166 FR provides that the institutions shall take all appropriate steps to act on the observations accompanying the European Parliament's discharge decision and on the comments accompanying the recommendation for discharge adopted by the Council. At the request of Parliament or the Council, they shall report on the measures taken in the light of those observations and, in particular, on the instructions given to their departments which are responsible for the implementation of the budget. These reports shall also be sent to the Court. In practice, the Commission prepares the follow-up report spontaneously every year and presents it to the European Parliament at the start of the next discharge procedure.

Part 7
Borrowing, lending and financial stabilisation



Chapter 20

Union borrowing and lending operations

1. General presentation and development of lending operations

Under the principle of budgetary equilibrium, the Union may not finance its activities by borrowing. A budget deficit cannot therefore be financed through recourse to borrowing. However, a certain number of provisions of the Treaties establishing the Union, together with the need to achieve the Treaty objectives, have led to the gradual creation of various instruments authorising the Commission, on behalf of the Union, to borrow on the financial markets to make loans in order to enable their final recipients to benefit from the advantageous conditions which the Union can secure with its very high credit rating.

The Union has developed several instruments enabling it to obtain access to the capital markets to finance various categories of loan.

Several periods can be identified in the development of the Community's financial instruments supported by the general budget.

- The first period is characterised by the total absence of activities of this type under the EEC Treaty, since they were only carried out by the ECSC, Euratom and the EIB.
- Towards the end of the 1960s, the need for Community solidarity within the Customs Union that had been created led to the emergence of operations to support Member States facing balance-of-payments problems. Euratom operations were also integrated into the general budget. The economic crisis that arose in 1973 after the first oil price shock gave rise to an even greater need to strengthen solidarity within the Community and the creation of the Balance of Payments Facility.
- In the 1970s, two instruments emerged. First, there was the New Community Instrument (NCI) to support investment by small and medium-sized firms. The second instrument was the blanket guarantee given from the general budget to EIB loans for micro-economic purposes in Mediterranean countries.
- The events that started in eastern Europe in 1989 led to an extension of the guarantee given to the EIB, enabling it to grant loans in central and eastern Europe (Poland and Hungary, to start with, then Czechoslovakia, Bulgaria and Romania) and to start the first borrowing and lending operation for a third country, Hungary, at the start of 1990.
- After the entry into force of the Maastricht Treaty in 1993 and the creation of the European Monetary Union, only Member States outside the euro area remained eligible for Balance of Payments support. Between 1994 and 2008 there were no requests for such financial assistance. However, in 2008, the international financial crisis led to the reactivation of this facility and to the raise of its lending capacity to EUR 50 billion.
- The financial crisis led to the deterioration of the budget deficits and debt positions of many euro-area Member States threatening the financial stability of the European Union as a whole. In this context, the European Financial Stabilisation Mechanism was set up in

May 2010, as an EU financial assistance instrument to euro-area Member States under Article 122(2) of the Treaty with a limited ceiling of up to EUR 60 billion ⁽¹⁾.

In addition, other borrowing and lending operations for macroeconomic purposes have been launched, not only for the countries of central and eastern Europe but also for Mediterranean countries such as Israel and Algeria.

2. Characteristics of borrowing and lending instruments

2.1. Sectoral instruments

1) ECSC

Article 49 of the ECSC Treaty empowered the High Authority to borrow funds, provided they were used solely to grant loans.

Loans were granted for three main purposes:

- to finance investment in the coal and steel sector;
- to finance conversion programmes for restructuring the coal and steel industry;
- to finance the construction of subsidised housing for workers in the coal and steel industries (second paragraph of Article 54).

In 1990 and 1991, the scope for loans was extended to certain eastern European countries, principally to finance projects promoting the sale of Community steel and industrial products which could be implemented within joint ventures.

Under the second paragraph of Article 54, the ECSC financed major infrastructure projects of Community interest between 1990 and 1994.

In 1994, the ECSC decided to review its borrowing and lending policy in preparation for the expiry of the Treaty (23 July 2002). On the basis of this decision, the last loans were made in 1997, except for loans for subsidised housing, which ended in 1998 with the 12th programme.

Over the course of its existence, the ECSC disbursed loans amounting to EUR 24.7 billion, of which EUR 24.08 billion came from borrowed funds and EUR 644 million from own funds (special reserve and former pension fund). On 31 December 2006, loans from borrowed funds worth EUR 281.8 million and loans from own funds worth EUR 55.5 million were still outstanding.

2) Euratom

Borrowing and lending operations are authorised under Article 172 of the Euratom Treaty of 25 March 1957.

Council Decision 77/270/Euratom of 29 March 1977 empowers the Commission to issue Euratom loans to finance investment projects in the Member States relating to industrial nuclear fuel cycle installations (mainly for the production of electricity).

⁽¹⁾ On both the Balance of Payments Facility and the European Financial Stabilisation Mechanisms, see Chapter 21.

Council Decision 94/179/Euratom of 21 March 1994 introduced a similar possibility for certain non-EU countries, for projects to increase the safety and efficiency of installations that are in service or under construction and for the dismantling of installations that cannot be preserved for technical or economical reasons.

The non-EU countries eligible for such loans were Armenia, Bulgaria, the Czech Republic, Hungary, Lithuania, Romania, Slovenia, Slovakia, the Russian Federation and Ukraine, some of which later became Member States.

Council Decision 77/271/Euratom of 29 March 1977, last amended in 1990, set a ceiling on the borrowing operations required for the funding of Euratom loans. The overall ceiling is EUR 4 000 million. Loans approved since 1977 total EUR 3.7 billion.

2.2. Macro-economic instruments

1) Borrowing and lending in connection with assistance to Member States

Currently there are two EU instruments for providing macroeconomic and financial support to Member States: the Balance of Payments Facility and the European Financial Stabilisation Mechanism. Details on these two instruments are given in Chapter 21.

2) Borrowing and lending in connection with cooperation with non-Member States

The Union provides financial assistance in the form of medium-term loans to a number of non-EU countries experiencing serious but generally short-term balance-of-payments or budget difficulties. This macro-financial assistance is designed to support the implementation of strong adjustment and structural reform measures to remedy these difficulties, but is to be discontinued as soon as the country's external financial situation has been brought back onto a sustainable path. The loans are financed from the EU borrowing operations. They are in some cases complemented or combined with a grant component.

This form of cooperation started in the early 1990s to help the countries of central and eastern Europe to implement economic reforms (Hungary, Czechoslovakia, the Baltic states, Bulgaria, and Romania) and was subsequently extended to some Mediterranean countries (Israel, Algeria). In the second half of the 1990s, it was mainly the Newly Independent States (most of the former Soviet Republics) which benefited from such assistance (notably Ukraine, Moldova, Belarus, Georgia, Armenia, and Tajikistan). Since 2000, the main recipients of macro-financial assistance have been the Balkan countries for the reconstruction and stabilisation of the region.

For the Balkan countries, the total volume of loans disbursed over 2007–13 amounted to EUR 200 million. As of 31 December 2013, outstanding loans for these countries totalled EUR 462 million.

For the countries earlier referred to as Newly Independent States, loans disbursed over the period 2007–13 were limited to EUR 65 million (corresponding to two loan disbursements to Armenia). As of 31 December 2013, outstanding loans for these countries totalled EUR 78 million.

For Mediterranean countries, loans disbursed over the period 2007–13 were limited to EUR 25 million (corresponding to one loan disbursement to Lebanon). This loan was the only macro-financial assistance loan outstanding towards a Mediterranean country as of 31 December 2013.

2.3. European Investment Bank (EIB) loans outside the EU

The European Union provides a budgetary guarantee to the European Investment Bank (EIB), which covers risks of a sovereign and political nature in connection with its financing operations carried out outside the Union in support of the Union's external policy objectives. The EU guarantee for the EIB's external operations is an effective means to combine EU budgetary funds, through the provisioning of the Guarantee Fund for external actions, with the EIB own resources. The need for an EU budget guarantee for the EIB's external operations stems from the Bank's obligation under its Statute to ensure adequate security for all its lending operations and, more broadly, from the need to safeguard the creditworthiness of the EIB and not compromise its task of contributing to the steady development of EU Member States.

The overall scope and general conditions of the EU guarantee coverage for EIB external operations are set out in Decisions of the European Parliament and of the Council. The most recent decision covering the EIB financing operations outside the Union over the period beginning on 1 February 2007 and ending on 31 December 2013 was established by Decision No 1080/2011/EU of the European Parliament and of the Council of 25 October 2011 granting an EU guarantee to the European Investment Bank against losses under loans and loan guarantees for projects outside the Union ⁽¹⁾. The overall ceiling of the mandate amounted to EUR 29.5 billion of which EUR 27.5 billion broken down in regional ceilings and EUR 2 billion dedicated to climate change operations. This mandate strengthened the capacity of the EIB to support EU development objectives through enhanced EIB appraisal and monitoring of social, environmental, human rights and development aspects of projects, and increased the focus of EIB intervention in sectors which will further the development of third countries. Moreover, the mandate reinforced the alignment of EIB activity and EU external policies, notably through the development of the Commission and the EIB of operational guidelines for each region, reflecting EU regional strategies.

For the period 2014–20, the Commission adopted a legislative proposal on 23 May 2013 which was endorsed by the legislative authority on 16 April 2014 ⁽²⁾. In addition to the objectives defined in the previous mandate, the key objectives of the new Decision are to:

- focus the geographical scope of the mandate on less creditworthy beneficiaries where the use of the guarantee would provide the highest value added;
- reinforce the climate change dimension of the mandate in order to incentivise EIB operations in this key sector of the Union external action through the introduction of an overall

⁽¹⁾ OJ L 280, 27.10.2011, p. 1.

⁽²⁾ Decision No 466/2014/EU of the European Parliament and the Council of 16 April 2014 granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union.

signature target accompanied by the introduction of a tracking system allowing to monitor absolute and relative greenhouse gases emission reduction of all significant EIB projects supported under the mandate;

- better align EIB financing with the Union policies and reinforce coherence and complementarity with EU instruments to more satisfactorily mirror policy developments in a timely manner through the provision to update the technical operational regional guidelines in line with the multiannual indicative programming of EU external financial instruments;
- increase transparency and improve the monitoring of the EIB's financing operations, zero tolerance on tax evasion and fraud, better evaluation of the social impact and human rights questions.

The new EU guarantee will have a fixed ceiling of a maximum amount of EUR 27 billion over the period 2014–20 and an optional additional amount of EUR 3 billion which can be activated following the mid-term review to be carried out by the end of 2016. A decision to activate the optional amount shall be made by the European Parliament and the Council in accordance with the ordinary legislative procedure.

3. The guarantee provided by the Union's general budget for borrowing operations

3.1. Borrowing and lending operations

This involves borrowings contracted by the Commission on behalf of the Union, which are then on-lent to third parties under the same conditions regarding the amount, term, rate and dates of payment of interest. The risk for the budget therefore derives from the need to ensure reimbursement of the sum borrowed by the Union in the event of default by the beneficiary of the loan on the due date of payment.

This type of guarantee to lenders concerns the macro-economic-types 'balance-of-payments', 'financial stabilisation' and 'medium-term financial assistance' loans and the micro-economic loans (Euratom).

3.2. EIB loan guarantees

The Union provides a guarantee for loans granted by the European Investment Bank to finance projects outside the Community (see also Section 2.3). The guarantee covers all (Comprehensive Guarantee) or part (Political Risk Guarantee) of the amount of the loans granted.

4. The relationship between the general budget and borrowing and lending operations and loan guarantees

4.1. The budget and lending operations

1) The non-inclusion of borrowing and lending operations in the budget

Unlike the first Euratom borrowings, current borrowing and lending operations do not appear in the budget as revenue and expenditure. In 1978, at the instigation of the European Parliament, the Commission proposed that these operations be shown in full in the budget, assimilating borrowing to revenue and loans to expenditure, in a 'Part II' of the general budget. The

Council's rejection of this proposal was one of the 'important reasons' which led Parliament to reject the draft budget for 1979. The Council's stance derived from the wish to maintain exclusive control over decisions concerning borrowing and lending.

As borrowing and lending operations do not appear in the budget, they are not financial instruments (i.e. Union measures of financial support provided on a complementary basis from the budget) within the meaning of Title VIII FR.

2) Limited consequences for the budget

Under its structure resulting from the FR, the budget does, however, contain a document showing all borrowing and lending operations, which is annexed to the Commission section. This document serves solely for guidance.

Furthermore, while the basic decision authorising an operation is adopted by the legislative authority, it is the budgetary authority which authorises the granting of the guarantee. This 'performance guarantee' is granted by including budget lines carrying a token entry in the 'expenditure' side of the budget. Where it necessary to activate the guarantee, appropriations would be allocated to these budget lines by transfer or by means of an amending budget.

4.2. Greater transparency in the treatment of these operations in the budget and procedures in the event of defaults

A statement annexed to the Financial Regulation resulting from the 1990 revision specifies that: 'The Commission undertakes to study the possibility of improving the treatment of borrowing/lending operations in Community budget documents. It will submit the conclusions of its study before the end of 1991.' Although the outcome of this exercise was then incorporated in the procedure for establishing the budget, the principles of transparency and sound financial management were introduced in the Financial Regulation of 2002, setting out clear requirements in this respect. Moreover, the development of the Union's external action and the growing use of the budget guarantee instrument made it necessary to apply the rules of budgetary discipline to these operations as well: the economic, social and political instability of certain countries benefiting from the guarantee for their loans increases the probability that the guarantee will in fact be activated. For example, the general budget has had to pay the EIB substantial amounts under this guarantee following the defaults of Lebanon, Syria and the Republics of the former Yugoslavia between 1988 and 1993, and in relation to loans granted to the Federal Republic of Yugoslavia and to Bosnia and Herzegovina between 1992 and 2000. The latter eventually paid the amounts due. In 2003 and 2004, the guarantee was called upon to cover EIB loans to Argentina, but also in this case the amounts due were eventually fully reimbursed. As from November 2011, the EIB is facing arrears on loans granted to the Syrian Arab Republic which has led to calls upon the guarantee in 2012, 2013 and 2014.

1) A new structure for budget documents

Articles 35 and 49 FR ensure greater transparency in the presentation of budget documents by providing that information on borrowing and lending operations contracted by the Union for third parties is to appear in an Annex to the budget. In addition to the information in this annex, the FR requires the budget to show:

- in the general statement of revenue, the budget lines that correspond to the relevant operations and are intended to record any reimbursements received from recipients who have initially defaulted, leading to activation of the performance guarantee. These lines carry a token entry '*pro memoria*' and are accompanied by appropriate remarks;
- in the Commission section, the budget lines containing the Union's performance guarantees in respect of the operations in question. These lines carry a token entry '*pro memoria*', so long as no effective charge to be covered by actual resources has arisen, and are accompanied by remarks indicating the basic act and the volume of the operations envisaged, the duration, and the financial guarantee given by the Union in respect of these operations.

2) Management of a default by a beneficiary Member State

In the event of a default on a loan repayment to the Union by a beneficiary Member State, the Commission can use its own treasury availability to service the debt. Were the treasury balances not large enough, Article 12 of Council Regulation 1150/2000 implementing the system of the European Union's own resources allows the Commission to call from Member States the resources needed to service the debt over and above their normal payments to the Union budget.

Moreover, in case of defaults the Commission is not forced to call from the Member States the additional resources needed to service the Union's debt in proportion to the each Member State's share in the GNI own resource.

However, according to the Own Resources Decision ⁽¹⁾ the budgeting of the cash resources called from Member States to honour the Union's legal obligations needs to respect the Own-resources ceiling (1.23 % of EU GNI). This means that the amounts budgeted to cover for the defaults must be within the margin between the Own-resources ceiling and the annual payment appropriations for the other Union expenditure. For this reason, the total annual debt service, and more specifically the reimbursement schedules (interest + capital) of the combined Balance of Payments Facility and the European Financial Stabilisation Mechanism loan disbursements are managed so that they always remains under the available margin. Thus, even in the extreme event where all beneficiaries of loans in any given year would default on all reimbursements, the ceiling would still be respected. This conservative management ensures that the EU budget will always and under any condition be able to honour the guarantee provided.

Additionally, the Balance of Payments Facility and the European Financial Stabilisation Mechanism loans (assistance can also take the form of credit lines) are funded and reimbursed back to back but the beneficiary Member States must transfer the principal and interest payments to the European Central Bank 7 and 14 days in advance of the due date, respectively. This is an additional safety buffer, allowing the Commission time enough to launch the procedures necessary to service the EU debt in case of defaults.

⁽¹⁾ Council Decision of 7 June 2007 on the system of the European Communities' own resources (2007/436/EC, Euratom), (OJ L 163, 23.6.2007, p. 17).

3) *Better cover of potential risks related to loan guarantees for non-member countries*

(a) Guarantee Fund for external actions

The Guarantee Fund, introduced by Council Regulation (EC, Euratom) No 2728/94 of 31 October 1994, together with subsequent amendments codified as Council Regulation 480/2009 of 25 May 2009, is intended to cover the activation of general budget guarantees for third countries in order to avoid possible disruptions to the implementation of the budget in the event of defaults. Its function is to provide a cushion for external shocks that would otherwise affect the budget directly and to create an instrument of budgetary discipline by laying down a financial framework for the evolution of the EU budget guarantees for Commission and EIB loans to non-Member countries. It intervenes in cases of default and subsequent activation of the EU guarantee, for the following three types of loans guaranteed by the budget (as described in the above sections):

- Euratom loans to certain third countries, for projects to increase the safety and efficiency of installations that are in service or under construction or for the dismantling of installations that cannot be pre-served for technical or economic reasons;
- macro-financial assistance loans to third countries to tackle short-term balance-of-payments or budget difficulties;
- EIB loans to third countries covered by an EU guarantee.

The EIB loans represent the bulk of the loans with over 95 % of the out-standing volume.

(b) The budget provisioning of the Guarantee Fund

The Regulation was amended by Council Regulation (EC, Euratom) No 89/2007 of 30 January 2007 to adjust the provisioning rules of the Guarantee Fund to the suppression of the reserve for loan guarantees to third countries. Council Regulation 480/2009 subsequently codified all amendments to the original Regulation 2728/94 into one single Regulation. Under the new financial framework 2007–13, it was decided that the financial resources necessary to provision the Guarantee Fund would be budgeted directly under the heading for external actions (Heading 4), since such expenditure directly supports the EU's external policies. The basic principle of the Guarantee Fund is not affected by the new provisioning mechanism. The relationship between the amount of outstanding loans and the Guarantee Fund at the target level of 9 % is maintained as the best assessment of the risk profile of the Guarantee Fund, as confirmed also by the 2010 mid-term review of EIB external lending. Under the new provisioning rules, the amount necessary to keep the Fund at its target level is budgeted directly in the budget of year $n+1$ on the basis of the amount in the Fund and the amount of outstanding loans as at 31 December of the year $n-1$. There is, in other words, a time-lag of two years between loan disbursements and their effect on the budget. The indicative financial envelope for the provisioning of the Guarantee Fund under the heading 'Global Europe' amounts to EUR 1.2 billion over the 2014–20 multiannual financial framework.

TABLE 16.1 – Total Annual Risk borne by the EU budget in EUR million based on the amounts (capital and interest) due under all operations (MFA, BoP, Euratom, EFSM and EIB) disbursed at 31.12.2013

Ranking	Country	Grand Total	2014	2015	2016	2017	2018	2019	2020	2021-43
1	Portugal	29 451,38	644,88	644,88	5 394,88	514,25	1 114,25	500,00	500,00	20 138,25
2	Ireland	29 078,75	661,00	5 661,00	536,00	536,00	4 436,00	413,63	413,63	16 421,50
3	Turkey	9 252,72	542,67	619,28	612,15	1 031,23	597,68	931,31	547,30	4 371,09
4	Romania	7 466,03	377,02	1 879,73	310,56	1 450,89	1 601,86	1 186,69	141,25	518,03
5	Hungary	3 752,31	2 128,42	62,98	1 558,78	2,12	0,00	0,00	0,00	0,00
6	Latvia	3 200,56	1 096,43	1 265,04	26,69	25,90	25,85	524,04	7,16	229,45
7	Morocco	3 020,72	217,77	315,74	209,79	211,04	222,68	214,52	201,43	1 427,75
8	Tunisia	2 699,35	221,59	235,12	249,33	241,47	223,64	211,14	190,03	1 127,04
9	Serbia	2 173,58	195,00	255,39	210,06	201,31	214,30	174,21	120,21	803,10
10	Egypt	2 086,90	184,11	178,82	187,43	203,68	203,55	202,72	168,32	758,28
11	Bosnia and Herzegovina	1 024,81	63,24	102,2	62,21	73,46	67,05	75,97	70,51	510,16
12	Brazil	1 001,66	102,45	229,41	226,14	81,81	76,44	134,18	87,33	63,90
13	South Africa	981,96	74,51	74,21	83,43	81,63	99,95	58,75	74,71	434,77
14	Bulgaria	639,58	87,52	85,80	83,12	77,78	67,32	54,93	46,55	136,56
15	Syrian Arab Republic	584,36	72,52	90,86	89,27	55,65	55,28	54,47	52,12	114,19
16	Ukraine	548,74	10,61	11,23	20,83	42,72	45,36	44,35	44,35	329,29
17	Israel	511,60	26,38	21,16	18,13	17,75	18,05	90,93	19,14	300,07
18	Lebanon	499,80	99,91	79,68	72,92	61,85	55,21	39,20	27,37	63,66
19	Panama	440,97	7,94	6,37	6,63	7,13	7,13	43,29	42,92	319,55
20	Jordan	414,06	42,78	35,30	34,07	36,31	38,85	30,01	28,90	167,83
21	Croatia	389,96	42,62	40,51	38,86	38,00	35,77	34,11	32,63	127,45
22	Albania	301,68	23,75	24,64	24,33	26,96	26,46	25,94	25,20	124,41
23	Argentina	264,72	38,63	42,28	41,86	40,33	38,79	37,26	10,41	15,15
24	Poland	237,48	52,49	42,80	29,35	21,54	20,69	18,90	18,07	33,65
25	India	236,08	29,86	32,74	34,29	30,84	20,84	18,47	14,66	54,38
26	Czech Republic	232,13	56,44	45,73	43,66	25,93	13,16	12,62	12,07	22,52
27	Georgia	222,88	5,85	7,99	13,13	18,06	18,90	18,74	15,33	124,89
28	Montenegro	218,43	20,48	22,41	23,21	22,07	26,06	18,31	13,48	72,40
29	Viet Nam	212,38	23,36	19,60	20,19	20,56	18,91	17,04	14,80	77,92

30	Russian Federation	205.08	12.02	13.87	21.27	19.66	16.59	16.52	16.45	88.70
31	The Former Yugoslav Republic Of Macedonia	193.66	45.36	39.88	27.75	21.49	16.54	8.57	8.39	25.67
32	Slovak Republic	156.95	25.78	15.08	14.66	14.24	13.82	13.40	12.98	46.99
33	Sri Lanka	123.82	14.14	15.32	13.72	13.58	14.43	14.38	12.93	25.35
34	Colombia	121.91	24.66	24.21	24.21	24.21	16.92	6.96	0.74	0.00
35	Armenia	121.53	2.69	3.01	3.68	4.01	4.31	4.49	4.45	94.89
36	Republic of Moldova	117.15	3.49	4.51	8.02	10.89	12.44	12.68	12.55	52.57
37	China	95.24	7.79	9.26	4.71	4.96	5.56	6.15	6.53	50.26
38	Lac People's Democratic Republic	67.96	2.56	2.59	2.63	2.66	2.69	2.73	2.78	49.32
39	Peru	61.48	15.32	15.20	12.59	12.59	5.27	0.52	0.00	0.00
40	Philippines	54.89	13.08	11.89	10.70	6.63	2.53	2.33	2.28	5.44
41	Indonesia	53.35	12.09	12.07	7.91	7.91	5.82	5.03	2.51	0.00
42	Paraguay	47.22	14.59	14.50	10.88	7.25	0.00	0.00	0.00	0.00
43	Regional – Central America	30.88	1.33	1.72	2.35	1.94	1.94	1.94	1.94	17.73
44	Gaza /West Bank	30.13	3.00	3.01	3.44	3.87	3.43	1.57	1.48	10.33
45	Nicaragua	28.72	0.77	0.77	0.87	1.37	1.76	2.02	1.97	19.19
46	Maldives	28.23	5.39	5.32	5.32	3.64	3.64	3.26	1.66	0.00
47	Lithuania	27.59	4.95	4.78	4.60	4.42	3.49	2.74	1.83	0.78
48	Pakistan	26.38	6.46	6.43	4.43	3.63	3.63	1.81	0.00	0.00
49	Ecuador	22.72	4.17	4.12	4.12	4.12	4.12	2.06	0.00	0.00
50	Mexico	20.09	3.36	3.34	3.34	3.34	3.34	3.34	0.00	0.00
51	Uruguay	14.52	4.78	3.90	3.90	1.95	0.00	0.00	0.00	0.00
52	Slovenia	13.92	7.44	4.39	2.09	0.00	0.00	0.00	0.00	0.00
53	Tadjiikistan	4.01	4.01	0.00	0.00	0.00	0.00	0.00	0.00	0.00
54	Cyprus	3.29	3.29	0.00	0.00	0.00	0.00	0.00	0.00	0.00
55	Thailand	2.09	2.09	0.00	0.00	0.00	0.00	0.00	0.00	0.00
	Grand Total	102 818.37	7 394.86	12 352.05	10 458.49	5 376.63	9 532.29	5 298.24	3 031.35	49 374.46
	Total IMS	74 649.93	5 188.29	9 752.71	8 043.26	2 711.08	7 332.21	2 761.05	1 186.16	37 675.18
	Percentage MS	72.60 %	70.16 %	78.96 %	76.91 %	50.42 %	76.92 %	52.11 %	39.13 %	76.30 %
	Total non MS	28 168.44	2 206.57	2 599.35	2 415.23	2 665.55	2 200.08	2 537.19	1 845.19	11 699.28

Chapter 21

Instruments providing financial assistance to Member States

A major new development of the period covered by the MFF 2007–13, linked to the financial crisis, has been the deployment of two sovereign lending instruments guaranteed by the EU budget:

- the long-dormant Balance of Payments Facility (BoP), which enables the Commission to grant, on behalf of the EU, loans to Member States outside the eurozone experiencing balance-of-payments difficulties, was reactivated and its lending capacity increased in two steps, to EUR 50 billion in May 2009;
- the European Financial Stabilisation Mechanism (EFSM) was set up in May 2010 to provide financial assistance to Member States under Article 122(2) TFEU, with an indicative ceiling of up to EUR 60 billion. The EFSM was complemented by the EFSF, a special-purpose vehicle not guaranteed by the EU budget but by Member States directly.

1. The Balance of Payments Facility

The BoP was created in 1975 ⁽¹⁾, in the wake of the first oil shock, to provide Community loans to Member States with balance-of-payments difficulties. The first loans were granted in 1976 and by 31 December 2000, all borrowings had been repaid. During this period, the Council increased the volume of Community borrowings authorised under this facility to EUR 8 billion in 1984 and to EUR 16 billion in 1988. Between 1994 and 2008 no Member State requested new financial assistance.

In 2002, a new Council Regulation ⁽²⁾ was adopted decreasing the lending ceiling of this facility to EUR 12 billion given that potential needs had decreased since January 1999 after Member States participating in the European Monetary Union stopped qualifying for medium-term assistance under this facility.

Under this Regulation, the European Union may grant financial assistance to Member States outside the eurozone that are experiencing, or are seriously threatened with, difficulties in their balance of current payments or capital movements. The financial assistance is granted by the Council and is conditional upon the adoption by the beneficiary Member State of economic policy measures designed to re-establish or ensure a sustainable balance of payments.

The international financial crisis in 2008 led to the reactivation of the BoP to provide financial assistance to Hungary, Latvia and Romania. The international finance crisis and the increasing potential demand for financial assistance of a larger number of eligible Member States outside the euro area led the Council to increase twice the ceiling for the outstanding amount

⁽¹⁾ The current legal basis is Article 143 TFEU.

⁽²⁾ Council Regulation (EC) No 332/2002 of 18 February 2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments (OJ L 53, 23.2.2002, p. 1).

of loans or credit lines. In December 2008 ⁽¹⁾, from EUR 12 billion to EUR 25 billion, and again in May 2009 ⁽²⁾ to the current ceiling of EUR 50 billion.

Between December 2008 and the end of 2013, European Union loans amounting to EUR 14.6 billion have been granted under this facility to Hungary (EUR 6.50 billion), Latvia (EUR 3.10 billion) and Romania (EUR 5.0 billion). In addition, a first precautionary financial assistance of EUR 1.4 billion (essentially a credit line) was granted to Romania in 2011 and after its expiry, a second precautionary financial assistance of EUR 2.0 billion was granted to this country in 2013, raising the total amount of financial assistance granted under the BoP to EUR 18.0 billion. The first precautionary financial assistance was not activated. The second precautionary assistance will remain available until end September 2015.

Of the assistance granted, EUR 1.0 billion expired in November 2010, without being requested by Hungary, and EUR 0.2 billion in January 2012, without being requested by Latvia, making the total amount actually disbursed EUR 13.4 billion. Taking into account Hungary's first reimbursement of principal (EUR 2.0 billion) in December 2011 and the EUR 2.0 billion precautionary assistance granted to Romania, the total amount of loans outstanding at the end of the 2007–13 MFF is EUR 11.4 billion (EUR 13.4 billion considering loans and precautionary assistance).

2. The European Financial Stabilisation Mechanism

The financial crisis that hit the global economy in 2008, destabilised financial markets, damaged economic growth and led to the deterioration of the fiscal and debt positions of many Member States.

The financial difficulties experienced by some Member States could threaten the financial stability of the European Union as a whole, thus the European Financial Stabilisation Mechanism (EFSM) was set up by a Council Regulation ⁽³⁾ in May 2010 to provide financial assistance to Member States ⁽⁴⁾. Under this Regulation, the European Union could grant financial assistance to Member States in difficulties or seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond their control. The EFSM was designed to give assistance together with the European Financial Stability Facility, a euro area special-purpose vehicle, and with the International Monetary Fund.

EFSM financial assistance is granted by the Council, linked with strong economic policy conditions aimed at preserving the sustainability of the beneficiary Member State's public finances and restoring its capacity to finance itself on the financial markets. The general economic policy conditions are the subject of a Memorandum of Understanding agreed between the

⁽¹⁾ Council Regulation (EC) No 1360/2008 of 2 December 2008 amending Regulation (EC) No 332/2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments (OJ L 352, 31.12.2008, p. 11).

⁽²⁾ Council Regulation (EC) No 431/2009 of 18 May 2009 amending Regulation (EC) No 332/2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments (OJ L 128, 27.5.2009, p. 1).

⁽³⁾ Council Regulation (EU) No 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism (OJ L 118, 12.5.2010, p. 1).

⁽⁴⁾ Current legal basis provided by Article 122(2) TFEU.

beneficiary Member State and the Commission. The Commission monitors compliance with these conditions regularly in collaboration with the European Central Bank and proposes changes to the adjustment programme of the Member State as needed.

The EFSM Regulation does not set a fixed ceiling for outstanding financial assistance, rather limiting it to the available margin under the own-resources ceiling. Considering in particular the ceiling for balance-of-payments assistance, the Ecofin Council of 9 May 2010 set an approximate ceiling for the EFSM of EUR 60 billion.

Since December 2010, a total amount of up to EUR 48.5 billion EFSM assistance has been granted to Ireland (up to EUR 22.5 billion) and to Portugal (up to EUR 26 billion), to be disbursed over three years. The implementation of both economic and financial adjustment programmes has been considered satisfactory by the Commission and the International Monetary Fund.

Following the conclusions of the Ecofin Council of 21 July 2011, both Council Decisions on Union financial assistance to Ireland ⁽¹⁾ and Portugal ⁽²⁾ were amended to cancel the interest rate margin and to extend the loans maximum maturity to up to 30 years ⁽³⁾ ⁽⁴⁾, and amended again to extend the average maturity to 19.5 years ⁽⁵⁾ ⁽⁶⁾.

Both programmes expire in 2014, which is the deadline for new disbursements under the programmes. However, given the relatively long maturities, the last outstanding loans will only be fully repaid after 2040.

The EFSM was designed as a temporary instrument and no new financial assistance programmes were granted by it after July 2013, though it will remain active until the full repayment of the Irish and Portuguese outstanding loans.

3. The European Financial Stability Facility

The European Financial Stability Facility (EFSF) was also created in response to the unprecedented financial crisis that began in 2008. It was established, along with the EFSM, as a temporary rescue mechanism to euro-area Member States.

It is a *société anonyme* incorporated in Luxembourg on 7 June 2010, mandated to provide financial assistance on a temporary basis until 30 June 2013.

⁽¹⁾ Council Implementing Decision (2011/77/EU) of 7 December 2010 on granting Union financial assistance to Ireland (OJ L 30, 4.2.2011, p. 34).

⁽²⁾ Council Implementing Decision (2011/344/EU) of 30 May 2011 on granting Union financial assistance to Portugal (OJ L 159, 17.6.2011, p. 88).

⁽³⁾ Council Implementing Decision (2011/682/EU) of 11 October 2011 amending Council Implementing Decision (2011/77/EU) of 7 December 2010 on granting Union financial assistance to Ireland (OJ L 269, 14.10.2011, p. 31).

⁽⁴⁾ Council Implementing Decision (2011/683/EU) of 11 October 2011 amending Council Implementing Decision (2011/344/EU) of 30 May 2011 on granting Union financial assistance to Portugal (OJ L 269, 14.10.2011, p. 32).

⁽⁵⁾ Council Implementing Decision (2013/313/EU) of 21 June 2013 amending Council Implementing Decision (2011/77/EU) of 7 December 2010 on granting Union financial assistance to Ireland (OJ L 173, 26.6.2013, p. 40).

⁽⁶⁾ Council Implementing Decision (2013/323/EU) of 21 June 2013 amending Council Implementing Decision (2011/344/EU) of 30 May 2011 on granting Union financial assistance to Portugal (OJ L 175, 27.6.2013, p. 47).

The EFSF provided financial assistance to euro-area Member States, linked to appropriate conditionality. It obtains financing by issuing bonds or other debt instruments on the financial markets backed by guarantees of the shareholding Member States. These guarantees total EUR 780 billion.

After its activation for the financial assistance programmes to Greece, Ireland and Portugal, the European Financial Stability Facility has currently effective guarantees totalling EUR 726 billion that provided a lending capacity of EUR 440 billion.

The EFSF, just like the EFSM, will not grant new loans after July 2013. However, it will continue to service the existing commitments.

4. European Stability Mechanism

The European Stability Mechanism (ESM) Treaty entered in force on 27 September 2012 and the ESM is now the sole and permanent mechanism for responding to new requests for financial assistance by euro-area Member States. Since 1 July 2013, it has taken over from the EFSM and EFSF the granting of new financial assistance to euro-area member States. The ESM is a permanent international financial institution created with the objective of preserving the financial stability of the European Union monetary union. It is an intergovernmental organisation under public international law and is currently the primary support mechanism for euro-area Member States.

It issues bonds or other debt instruments on the financial markets to raise capital to provide assistance to Member States. Unlike the EFSF, which was based upon euro-area Member State guarantees, the European Stability Mechanism has total subscribed capital of EUR 700 billion provided by euro-area Member States (EUR 80 billion in the form of paid-in capital and EUR 620 billion in callable capital). This subscribed capital provides the ESM with a total lending capacity of EUR 500 billion.

Financial assistance from the ESM will in all cases be activated upon a request from a euro-area Member State to its Board of Governors and will be provided subject to conditionality appropriate to the specific assistance chosen. The ESM can grant loans to euro-area Member States in financial difficulties, intervene in the debt primary and secondary markets and grant precautionary financial assistance and loans to governments for the purpose of recapitalising financial institutions.

Each type of financial assistance programme will be linked to a Memorandum of Understanding, negotiated between the beneficiary Member State and the European Commission in liaison with the European Central Bank, describing the measures to be taken by the beneficiary Member State. The implementation of these measures is subject to continuous monitoring and surveillance until the expiry of the programme.

Part 8
The European Development Fund



Chapter 22

The European Development Fund

1. The European Development Fund and agreements with the African, Caribbean and Pacific countries

Since 1958, the European Development Fund (EDF) has been the main geographic instrument for financial and technical cooperation between the European Union (EU) and developing countries and territories which, for historic reasons, maintained special links with certain Member States. Unlike other external policy actions (see Chapter 13), the EDF is not financed from the general budget of the EU.

The EDF falls within the broader context of comprehensive cooperation agreements signed between the EU and the group of African, Caribbean and Pacific States (ACP), the Member States being signatories to these Conventions independently of the EU. Seventy-nine ACP countries are now parties to the ACP-EC Partnership Agreement ⁽¹⁾ and 21 overseas countries and territories (OCTs) come under the Council Decision on the association of overseas countries and territories.

Apart from the EDF, the ACP Partnership Agreement covers the following:

- financing: loans from the own resources of the European Investment Bank to finance national and regional development programmes;
- trade: a trade regime based on WTO-compatible Economic Partnership Agreements or the Generalised System of Preferences as from 1 January 2008 onwards. The ACP-EU Economic Partnership Agreements (EPAs) are special trade agreements which aim mainly to ensure the development of ACP countries and their gradual integration into the global economy.

First EDF:	1959–64	Convention on overseas countries and territories annexed to the Treaty
Second EDF:	1964–70	First Yaoundé Convention
Third EDF:	1970–75	Second Yaoundé Convention
Fourth EDF:	1975–80	First Lomé Convention
Fifth EDF:	1980–85	Second Lomé Convention
Sixth EDF:	1985–90	Third Lomé Convention
Seventh EDF:	1990–95	Fourth Lomé Convention
Eighth EDF:	1995–2000	Fourth (revised) Lomé Convention
Ninth EDF:	2000–07	Cotonou Agreement
Tenth EDF:	2008–13	Revised Cotonou Agreement
Eleventh EDF:	2014–20	Revised Cotonou Agreement

⁽¹⁾ Geographic cooperation with South Africa, although signatory to the Agreement, is funded from the EU budget and not from the European Development Fund.

The Partnership Agreement, known as the ‘Cotonou Agreement’, signed on 23 June 2000 and revised on 25 June 2005, replaces all previous conventions and is notable for the long period it covers (20 years). It contains all the principles, objectives and rules governing cooperation between the EU and ACP States. Its financial aspects are specified in a financial protocol annexed to the Partnership Agreement (ninth, tenth, and now eleventh EDF) and in a multiannual financial framework. The current multiannual financial framework is the period 2014 to 2020, and the protocol is determined by a separate decision of the ACP-EU Council of Ministers, to be funded from the eleventh EDF. Such a protocol or financial framework determines the contribution key and volume of resources that Member States commit themselves to making available to the EDF and the EIB.

2. The resources of the EDF

The Member States will provide resources amounting to over EUR 29 billion (excluding support expenditure) to the ACP countries under the eleventh EDF, of which EUR 1.1 billion are contributions to risk capital, (concessional) loans and quasi-capital managed by the EIB through the Investment Facility. The tenth EDF, which entered into force in July 2008, had an allocation of over EUR 22 billion. In addition, EUR 364 million are available to the overseas countries and territories under the eleventh EDF, as against EUR 286 million under the tenth EDF.

3. The financial regime of the EDF

3.1. Non-inclusion in the budget

Like the rest of EU expenditure, the resources of the EDF originally came from financial contributions by the Member States, but the cost-sharing formula or contribution keys were different from those used to determine the expenditure of the general budget. This EDF formula took into account the special relations between certain Member States and the ACP countries.

The Commission has proposed many times to integrate the EDF into the EU general budget. The Council has consistently rejected this proposal.

This refusal to incorporate the EDF into the budget was one of the ‘important reasons’ put forward by the European Parliament when rejecting the budget for 1980 on 13 December 1979, for example.

In its Communication A budget for Europe 2020, the Commission put forward its opinion that, in the current circumstances, with the Cotonou agreement due to expire in 2020, the conditions for integrating the EDF fully into the budget were not yet met. The Commission however stated that, in order to create a perspective of future inclusion, it would consider proposing to bring the EDF contribution key closer to the key used for the EU budget. This will also contribute to the visibility of the absolute amounts provided in development aid. The Commission also proposed measures to improve the democratic scrutiny of the EDF.

The objective of a possible future integration of the EDF in the general budget is explicitly mentioned in the Interinstitutional Agreement of 2 April 2013 on budgetary discipline, on cooperation in budgetary matters and on sound financial management ⁽¹⁾.

3.2. The cost-sharing formula for national contributions of Member States to the financing of the eleventh EDF

The scale applicable to the eleventh EDF (2014–20) is as follows:

Member State	Contribution key (%)
Belgium	3.24927
Bulgaria	0.21853
Czech Republic	0.79745
Denmark	1.98045
Germany	20.5798
Estonia	0.08635
Ireland	0.94006
Greece	1.50735
Spain	7.93248
France	17.81269
Croatia (*)	0.22518
Italy	12.53009
Cyprus	0.11162
Latvia	0.11612
Lithuania	0.18077
Luxembourg	0.25509
Hungary	0.61456
Malta	0.03801
Netherlands	4.77678
Austria	2.39757
Poland	2.00734
Portugal	1.19679
Romania	0.71815
Slovenia	0.22452
Slovakia	0.37616
Finland	1.50909
Sweden	2.93911
United Kingdom	14.67862

* Estimated amount.

⁽¹⁾ 'The European Parliament and the Council note that the Commission, with a view to, inter alia, enhancing the democratic scrutiny of development policy, intends to propose the budgetisation of the EDF as of 2021.'; point 26§2 of the IIA, op. cit.

3.3. A distinctive financial regime

1) Control by the Member States

Through the Council of Ministers and Committee of Ambassadors, set up by the Cotonou Agreement itself, and the EDF Committee, which issues an opinion prior to any Commission decision on country or regional programming documents and on annual action programmes prepared jointly with the ACP partners, the Member States retain a direct influence on these financial measures.

2) Financial implementation

Although the European Development Fund is a true financial instrument separate from the general budget, it has neither legal personality nor real autonomy of management since its administrator is a Commission department: the Directorate-General for Development and Cooperation — EuropeAid. The European External Action Service is responsible, together with the European Commission, for programming EU financial assistance and cooperation, and the Commission is responsible for implementing the budget and managing programmes.

Given the specificities of the EDF rules, the EDF accounts are not consolidated with those of the general budget. However, financial statements comply with accrual accounting principles, i.e. conform to the accounting rules and methods drawn up for the EDF on the basis of International Accounting Standards (IPSAS/IAS) and Generally Accepted Accounting Principles (GAAP).

The EDF also has an accounting officer, in accordance with the principle that authorising officers and accounting officers should not be one and the same person. This principle of separate roles is made more visible by the fact that the EDF accounting officer's department is part of the DG Budget and the Commission's accounting officer also has the role of EDF accounting officer.

The Director-General of EuropeAid is the authorising officer by delegation, but a large proportion of EDF expenditure is implemented at local level through the indirect management method, by a national or regional authorising officer designated by each ACP country or region and under the supervision of an EU delegation. Heads of EU delegations receive sub-delegated powers to authorise transactions from the Director-General of EuropeAid.

The implementing rules for expenditure and revenue under each EDF are the subject of a specific Financial Regulation, as far as possible aligned with the Union Financial Regulation.

The EDF's revenue and expenditure, like operations under the general budget, are subject to internal and external controls. The external audit is carried out by the Court of Auditors, which produces an annual report exclusively devoted to the management of the EDF.

3.4. Multiannual management

The principle of annuality, applicable to the general budget, is not applicable to the implementation of the EDF. Commitments do not have to be made to consume annual budgetary appropriations. The EDF has rather developed to work with 'global commitments' (which consist of setting aside overall allocations for projects and programmes on the basis of a financing

agreement) and 'individual commitments' (which are the actual actions giving rise to expenditure). The management of the EDF is aligned as much as possible with the management of the external relations instruments funded from the general budget.

The European Development Fund is thus an important part of the EU's spending, even though it remains outside the general budget for the time being. Together with the Development Cooperation Instrument, funded from the general budget, it is the most focused of the European Union's financial instruments in supporting the Millennium Development Goals and the sustainable development goals which are planned to succeed them.

Annexes

1. Treaty provisions: Articles 310 to 325 TFEU
2. MFF Regulation of 2 December 2013
3. IIA of 2 December 2013
4. Council Decision of 7 June 2007 on the system of own resources
5. Council Decision of 26 May 2014 on the system of own resources

Annex 1

*Treaty provisions: Articles 310 to 325 TFEU***CONSOLIDATED VERSIONS****OF THE TREATY ON EUROPEAN UNION AND THE TREATY
ON THE FUNCTIONING OF THE EUROPEAN UNION**

2012/C 326/01

**TITLE II
FINANCIAL PROVISIONS***Article 310**(ex Article 268 TEC)*

1. All items of revenue and expenditure of the Union shall be included in estimates to be drawn up for each financial year and shall be shown in the budget.

The Union's annual budget shall be established by the European Parliament and the Council in accordance with Article 314.

The revenue and expenditure shown in the budget shall be in balance.

2. The expenditure shown in the budget shall be authorised for the annual budgetary period in accordance with the regulation referred to in Article 322.

3. The implementation of expenditure shown in the budget shall require the prior adoption of a legally binding Union act providing a legal basis for its action and for the implementation of the corresponding expenditure in accordance with the regulation referred to in Article 322, except in cases for which that law provides.

4. With a view to maintaining budgetary discipline, the Union shall not adopt any act which is likely to have appreciable implications for the budget without providing an assurance that the expenditure arising from such an act is capable of being financed within the limit of the Union's own resources and in compliance with the multiannual financial framework referred to in Article 312.

5. The budget shall be implemented in accordance with the principle of sound financial management. Member States shall cooperate with the Union to ensure that the appropriations entered in the budget are used in accordance with this principle.

6. The Union and the Member States, in accordance with Article 325, shall counter fraud and any other illegal activities affecting the financial interests of the Union.

CHAPTER 1 THE UNION'S OWN RESOURCES

Article 311 (*ex Article 269 TEC*)

The Union shall provide itself with the means necessary to attain its objectives and carry through its policies.

Without prejudice to other revenue, the budget shall be financed wholly from own resources.

The Council, acting in accordance with a special legislative procedure, shall unanimously and after consulting the European Parliament adopt a decision laying down the provisions relating to the system of own resources of the Union. In this context it may establish new categories of own resources or abolish an existing category. That decision shall not enter into force until it is approved by the Member States in accordance with their respective constitutional requirements.

The Council, acting by means of regulations in accordance with a special legislative procedure, shall lay down implementing measures for the Union's own resources system in so far as this is provided for in the decision adopted on the basis of the third paragraph. The Council shall act after obtaining the consent of the European Parliament.

CHAPTER 2 THE MULTIANNUAL FINANCIAL FRAMEWORK

Article 312

1. The multiannual financial framework shall ensure that Union expenditure develops in an orderly manner and within the limits of its own resources.

It shall be established for a period of at least five years.

The annual budget of the Union shall comply with the multiannual financial framework.

2. The Council, acting in accordance with a special legislative procedure, shall adopt a regulation laying down the multiannual financial framework. The Council shall act unanimously after obtaining the consent of the European Parliament, which shall be given by a majority of its component members.

The European Council may, unanimously, adopt a decision authorising the Council to act by a qualified majority when adopting the regulation referred to in the first subparagraph.

3. The financial framework shall determine the amounts of the annual ceilings on commitment appropriations by category of expenditure and of the annual ceiling on payment appropriations. The categories of expenditure, limited in number, shall correspond to the Union's major sectors of activity.

The financial framework shall lay down any other provisions required for the annual budgetary procedure to run smoothly.

4. Where no Council regulation determining a new financial framework has been adopted by the end of the previous financial framework, the ceilings and other provisions corresponding to the last year of that framework shall be extended until such time as that act is adopted.

5. Throughout the procedure leading to the adoption of the financial framework, the European Parliament, the Council and the Commission shall take any measure necessary to facilitate its adoption.

CHAPTER 3 THE UNION'S ANNUAL BUDGET

Article 313

(ex Article 272(1), TEC)

The financial year shall run from 1 January to 31 December.

Article 314

(ex Article 272(2) to (10), TEC)

The European Parliament and the Council, acting in accordance with a special legislative procedure, shall establish the Union's annual budget in accordance with the following provisions.

1. With the exception of the European Central Bank, each institution shall, before 1 July, draw up estimates of its expenditure for the following financial year. The Commission shall consolidate these estimates in a draft budget, which may contain different estimates.

The draft budget shall contain an estimate of revenue and an estimate of expenditure.

2. The Commission shall submit a proposal containing the draft budget to the European Parliament and to the Council not later than 1 September of the year preceding that in which the budget is to be implemented.

The Commission may amend the draft budget during the procedure until such time as the Conciliation Committee, referred to in paragraph 5, is convened.

3. The Council shall adopt its position on the draft budget and forward it to the European Parliament not later than 1 October of the year preceding that in which the budget is to be implemented. The Council shall inform the European Parliament in full of the reasons which led it to adopt its position.

4. If, within forty-two days of such communication, the European Parliament:

(a) approves the position of the Council, the budget shall be adopted;

(b) has not taken a decision, the budget shall be deemed to have been adopted;

(c) adopts amendments by a majority of its component members, the amended draft shall be forwarded to the Council and to the Commission. The President of the European Parliament, in agreement with the President of the Council, shall immediately convene a meeting of the Conciliation Committee. However, if within ten days of the draft being forwarded the Council informs the European Parliament that it has approved all its amendments, the Conciliation Committee shall not meet.

5. The Conciliation Committee, which shall be composed of the members of the Council or their representatives and an equal number of members representing the European Parliament, shall have the task of reaching agreement on a joint text, by a qualified majority of the members of the Council or their representatives and by a majority of the representatives of the European Parliament within twenty-one days of its being convened, on the basis of the positions of the European Parliament and the Council.

The Commission shall take part in the Conciliation Committee's proceedings and shall take all the necessary initiatives with a view to reconciling the positions of the European Parliament and the Council.

6. If, within the twenty-one days referred to in paragraph 5, the Conciliation Committee agrees on a joint text, the European Parliament and the Council shall each have a period of fourteen days from the date of that agreement in which to approve the joint text.

7. If, within the period of fourteen days referred to in paragraph 6:

(a) the European Parliament and the Council both approve the joint text or fail to take a decision, or if one of these institutions approves the joint text while the other one fails to take a decision, the budget shall be deemed to be definitively adopted in accordance with the joint text; or

(b) the European Parliament, acting by a majority of its component members, and the Council both reject the joint text, or if one of these institutions rejects the joint text while the other one fails to take a decision, a new draft budget shall be submitted by the Commission; or

(c) the European Parliament, acting by a majority of its component members, rejects the joint text while the Council approves it, a new draft budget shall be submitted by the Commission; or

(d) the European Parliament approves the joint text whilst the Council rejects it, the European Parliament may, within fourteen days from the date of the rejection by the Council and acting by a majority of its component members and three-fifths of the votes cast, decide to confirm all or some of the amendments referred to in paragraph 4(c). Where a European Parliament amendment is not confirmed, the position agreed in the Conciliation Committee on the budget heading which is the subject of the amendment shall be retained. The budget shall be deemed to be definitively adopted on this basis.

8. If, within the twenty-one days referred to in paragraph 5, the Conciliation Committee does not agree on a joint text, a new draft budget shall be submitted by the Commission.

9. When the procedure provided for in this Article has been completed, the President of the European Parliament shall declare that the budget has been definitively adopted.

10. Each institution shall exercise the powers conferred upon it under this Article in compliance with the Treaties and the acts adopted thereunder, with particular regard to the Union's own resources and the balance between revenue and expenditure.

Article 315

(ex Article 273 TEC)

If, at the beginning of a financial year, the budget has not yet been definitively adopted, a sum equivalent to not more than one twelfth of the budget appropriations for the preceding financial year may be spent each month in respect of any chapter of the budget in accordance with the provisions of the Regulations made pursuant to Article 322; that sum shall not, however, exceed one twelfth of the appropriations provided for in the same chapter of the draft budget.

The Council on a proposal by the Commission, may, provided that the other conditions laid down in the first paragraph are observed, authorise expenditure in excess of one twelfth in accordance with the regulations made pursuant to Article 322. The Council shall forward the decision immediately to the European Parliament.

The decision referred to in the second paragraph shall lay down the necessary measures relating to resources to ensure application of this Article, in accordance with the acts referred to in Article 311.

It shall enter into force thirty days following its adoption if the European Parliament, acting by a majority of its component Members, has not decided to reduce this expenditure within that time-limit.

Article 316
(*ex Article 271 TEC*)

In accordance with conditions to be laid down pursuant to Article 322, any appropriations, other than those relating to staff expenditure, that are unexpended at the end of the financial year may be carried forward to the next financial year only.

Appropriations shall be classified under different chapters grouping items of expenditure according to their nature or purpose and subdivided in accordance with the regulations made pursuant to Article 322.

The expenditure of the European Parliament, the European Council and the Council, the Commission and the Court of Justice of the European Union shall be set out in separate parts of the budget, without prejudice to special arrangements for certain common items of expenditure.

CHAPTER 4 **IMPLEMENTATION OF THE BUDGET AND DISCHARGE**

Article 317
(*ex Article 274 TEC*)

The Commission shall implement the budget in cooperation with the Member States, in accordance with the provisions of the regulations made pursuant to Article 322, on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management. Member States shall cooperate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management.

The regulations shall lay down the control and audit obligations of the Member States in the implementation of the budget and the resulting responsibilities. They shall also lay down the responsibilities and detailed rules for each institution concerning its part in effecting its own expenditure.

Within the budget, the Commission may, subject to the limits and conditions laid down in the regulations made pursuant to Article 322, transfer appropriations from one chapter to another or from one subdivision to another.

Article 318
(*ex Article 275 TEC*)

The Commission shall submit annually to the European Parliament and to the Council the accounts of the preceding financial year relating to the implementation of the budget. The Commission shall also forward to them a financial statement of the assets and liabilities of the Union.

The Commission shall also submit to the European Parliament and to the Council an evaluation report on the Union's finances based on the results achieved, in particular in relation to the indications given by the European Parliament and the Council pursuant to Article 319.

Article 319

(ex Article 276 TEC)

1. The European Parliament, acting on a recommendation from the Council, shall give a discharge to the Commission in respect of the implementation of the budget. To this end, the Council and the European Parliament in turn shall examine the accounts, the financial statement and the evaluation report referred to in Article 318, the annual report by the Court of Auditors together with the replies of the institutions under audit to the observations of the Court of Auditors, the statement of assurance referred to in Article 287(1), second subparagraph and any relevant special reports by the Court of Auditors.

2. Before giving a discharge to the Commission, or for any other purpose in connection with the exercise of its powers over the implementation of the budget, the European Parliament may ask to hear the Commission give evidence with regard to the execution of expenditure or the operation of financial control systems. The Commission shall submit any necessary information to the European Parliament at the latter's request.

3. The Commission shall take all appropriate steps to act on the observations in the decisions giving discharge and on other observations by the European Parliament relating to the execution of expenditure, as well as on comments accompanying the recommendations on discharge adopted by the Council.

At the request of the European Parliament or the Council, the Commission shall report on the measures taken in the light of these observations and comments and in particular on the instructions given to the departments which are responsible for the implementation of the budget. These reports shall also be forwarded to the Court of Auditors.

CHAPTER 5 COMMON PROVISIONS

Article 320

(ex Article 277 TEC)

The multiannual financial framework and the annual budget shall be drawn up in euro.

Article 321
(*ex Article 278 TEC*)

The Commission may, provided it notifies the competent authorities of the Member States concerned, transfer into the currency of one of the Member States its holdings in the currency of another Member State, to the extent necessary to enable them to be used for purposes which come within the scope of the Treaties. The Commission shall as far as possible avoid making such transfers if it possesses cash or liquid assets in the currencies which it needs.

The Commission shall deal with each Member State through the authority designated by the State concerned. In carrying out financial operations the Commission shall employ the services of the bank of issue of the Member State concerned or of any other financial institution approved by that State.

Article 322
(*ex Article 279 TEC*)

1. The European Parliament and the Council, acting in accordance with the ordinary legislative procedure, and after consulting the Court of Auditors, shall adopt by means of regulations:

- (a) the financial rules which determine in particular the procedure to be adopted for establishing and implementing the budget and for presenting and auditing accounts;
- (b) rules providing for checks on the responsibility of financial actors, in particular authorising officers and accounting officers.

2. The Council, acting on a proposal from the Commission and after consulting the European Parliament and the Court of Auditors, shall determine the methods and procedure whereby the budget revenue provided under the arrangements relating to the Union's own resources shall be made available to the Commission, and determine the measures to be applied, if need be, to meet cash requirements.

Article 323

The European Parliament, the Council and the Commission shall ensure that the financial means are made available to allow the Union to fulfil its legal obligations in respect of third parties.

Article 324

Regular meetings between the Presidents of the European Parliament, the Council and the Commission shall be convened, on the initiative of the Commission, under the budgetary procedures referred to in this Title. The Presidents shall take all the necessary steps to promote consultation and the reconciliation of the positions of the institutions over which they preside in order to facilitate the implementation of this Title.

CHAPTER 6 COMBATTING FRAUD

Article 325

(ex Article 280 TEC)

1. The Union and the Member States shall counter fraud and any other illegal activities affecting the financial interests of the Union through measures to be taken in accordance with this Article, which shall act as a deterrent and be such as to afford effective protection in the Member States, and in all the Union's institutions, bodies, offices and agencies.
2. Member States shall take the same measures to counter fraud affecting the financial interests of the Union as they take to counter fraud affecting their own financial interests.
3. Without prejudice to other provisions of the Treaties, the Member States shall coordinate their action aimed at protecting the financial interests of the Union against fraud. To this end they shall organise, together with the Commission, close and regular cooperation between the competent authorities.
4. The European Parliament and the Council, acting in accordance with the ordinary legislative procedure, after consulting the Court of Auditors, shall adopt the necessary measures in the fields of the prevention of and fight against fraud affecting the financial interests of the Union with a view to affording effective and equivalent protection in the Member States and in all the Union's institutions, bodies, offices and agencies.
5. The Commission, in cooperation with Member States, shall each year submit to the European Parliament and to the Council a report on the measures taken for the implementation of this Article.

Annex 2

MFF Regulation of 2 December 2013

COUNCIL REGULATION (EU, EURATOM) No 1311/2013

of 2 December 2013

laying down the multiannual financial framework for the years 2014-2020

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 312 thereof,

Having regard to the Treaty establishing the European Atomic Energy Community, and in particular Article 106a thereof,

Having regard to the proposal from the European Commission,

Having regard to the consent of the European Parliament,

After transmission of the draft legislative act to national parliaments,

Acting in accordance with a special legislative procedure,

Whereas:

- (1) The annual ceilings on commitments appropriations by category of expenditure and the annual ceilings on payment appropriations established by this Regulation must respect the ceilings set for commitments and own resources in Council Decision 2007/436/EC, Euratom ⁽¹⁾,
- (2) Taking into account the need for an adequate level of predictability for preparing and implementing medium-term investments, the duration of the multiannual financial framework (MFF) should be set at seven years starting on 1 January 2014. A review will take place in 2016 at the latest, following the European Parliament elections. This will allow the institutions, including the European Parliament elected in 2014, to reassess the priorities. The results of this review should be taken into account in any revision of this Regulation for the remaining years of the MFF. This arrangement is hereinafter referred to as "review/revision".
- (3) In the context of the mid-term review/revision of the MFF, the European Parliament, the Council and the Commission agree to jointly examine the most suitable

duration for the subsequent MFF before the Commission presents its proposals with a view to striking the right balance between the duration of the respective terms of office of the members of the European Parliament and the European Commission - and the need for stability for programming cycles and investment predictability.

- (4) Specific and maximum possible flexibility should be implemented to allow the Union to fulfil its obligations in compliance with Article 323 of the Treaty on the Functioning of the European Union (TFEU).
- (5) The following special instruments are necessary to allow the Union to react to specified unforeseen circumstances, or to allow the financing of clearly identified expenditure which cannot be financed within the limits of the ceilings available for one or more headings as laid down in the MFF, thereby facilitating the budgetary procedure: the Emergency Aid Reserve, the European Union Solidarity Fund, the Flexibility Instrument, the European Globalisation Adjustment Fund, the Contingency Margin, the specific flexibility to tackle youth unemployment and strengthen research and the global margin for commitments for growth and employment, in particular youth employment. Specific provision should therefore be made for a possibility to enter commitment appropriations into the budget over and above the ceilings set out in the MFF where it is necessary to use special instruments.
- (6) If it is necessary to mobilise the guarantees given under the general budget of the Union for the loans provided under the Balance of Payment Facility or the European Financial Stabilisation Mechanism set out in Council Regulation (EC) No 332/2002 ⁽²⁾ and in Council Regulation (EU) No 407/2010 ⁽³⁾, respectively, the necessary amount should be mobilised over and above the ceilings of the commitments and payments appropriations of the MFF, while respecting the own-resources ceiling.
- (7) The MFF should be laid down in 2011 prices. The rules for technical adjustments to the MFF to recalculate the ceilings and margins available should also be laid down.

⁽¹⁾ Council Decision 2007/436/EC, Euratom of 7 June 2007 on the system of the European Communities' own resources (OJ L 163, 23.6.2007, p. 17).

⁽²⁾ Council Regulation (EC) No 332/2002 of 18 February 2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments (OJ L 53, 23.2.2002, p. 1).

⁽³⁾ Council Regulation (EU) No 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism (OJ L 118, 12.5.2010, p. 1).

- (8) The MFF should not take account of budget items financed by assigned revenue within the meaning of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council⁽¹⁾ (the "Financial Regulation").
- (9) This Regulation might need to be revised in case of unforeseen circumstances that cannot be dealt with within ceilings established as part of the MFF. It is therefore necessary to provide for revision of the MFF in such cases.
- (10) Rules should be laid down for other situations that might require the MFF to be adjusted or revised. Such adjustments or revisions might be related to the implementation of the budget, measures linking effectiveness of funds to sound economic governance, revision of the Treaties, enlargements, the reunification of Cyprus, or delayed adoption of new rules governing certain policy areas.
- (11) The national envelopes for cohesion policy are established on the basis of the statistical data and forecasts used for the July 2012 update of the Commission proposal for this Regulation. Given the forecasting uncertainties and the impact for the capped Member States, and to take account of the particularly difficult situation of Member States suffering from the crisis, the Commission will, in 2016, review all Member States' total allocations under the "Investment for growth and jobs" goal of cohesion policy for the years 2017 to 2020.
- (12) It is necessary to provide for general rules on interinstitutional cooperation in the budgetary procedure.
- (13) Specific rules are also necessary for dealing with large-scale infrastructure projects whose lifetime extends well beyond the period set for the MFF. It is necessary to establish maximum amounts for the contributions from the general budget of the Union to those projects, thereby ensuring that they do not have any impact on other projects financed from that budget.
- (14) The Commission should present a proposal for a new multiannual financial framework before 1 January 2018, to enable the institutions to adopt it sufficiently in advance of the start of the subsequent multiannual financial framework. This Regulation should continue to apply in the event that a new financial framework is not adopted before the end of the term of the MFF laid down in this Regulation.
- (15) The Economic and Social Committee and the Committee of the Regions were consulted and have adopted opinions⁽²⁾,

HAS ADOPTED THIS REGULATION:

CHAPTER 1

General provisions

Article 1

Multiannual Financial Framework

The multiannual financial framework for the period 2014 to 2020 (the "MFF") is set out in the Annex.

Article 2

Mid-term review/revision of the MFF

By the end of 2016 at the latest, the Commission shall present a review of the functioning of the MFF taking full account of the economic situation at that time as well as the latest macro-economic projections. This compulsory review shall, as appropriate, be accompanied by a legislative proposal for the revision of this Regulation in accordance with the procedures set out in the TFEU. Without prejudice to Article 7 of this Regulation, preallocated national envelopes shall not be reduced through such a revision.

Article 3

Compliance with the ceilings of the MFF

1. The European Parliament, the Council and the Commission shall, during each budgetary procedure and when implementing the budget for the year concerned, comply with the annual expenditure ceilings set out in the MFF.

The sub-ceiling for Heading 2 as set out in the Annex is established without prejudice to the flexibility between the two pillars of the Common Agricultural Policy (CAP). The adjusted ceiling to be applied to pillar 1 of the CAP following the transfers between the European Agricultural Fund for Rural Development and direct payments shall be laid down in the relevant legal act and the MFF shall be adjusted accordingly under the technical adjustment provided for in Article 6(1) of this Regulation.

2. The special instruments provided for in Articles 9 to 15 shall ensure the flexibility of the MFF and shall be laid down in order to allow the budget procedure to run smoothly. The commitment appropriations may be entered in the budget over and above the ceilings of the relevant headings laid down in the MFF where it is necessary to use the resources

⁽¹⁾ Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (OJ L 298, 26.10.2012, p. 1).

⁽²⁾ Opinion of the European Economic and Social Committee on the 'Proposal for a Council Regulation laying down the multiannual financial framework for the years 2014-2020' (OJ C 229, 31.7.2012, p. 32); Opinion of the Committee of the Regions on 'New Multiannual Financial Framework post-2013' (OJ C 391, 18.12.2012, p. 31).

from the Emergency Aid Reserve, the European Union Solidarity Fund, the Flexibility Instrument, the European Globalisation Adjustment Fund, the Contingency Margin, the specific flexibility to tackle youth unemployment and strengthen research and the global margin for commitments for growth and employment, in particular youth employment, in accordance with Council Regulation (EC) No 1012/2002 (¹), Regulation (EC) No 1927/2006 of the European Parliament and of the Council (²), and the Interinstitutional Agreement between the European Parliament, the Council and the Commission (³).

3. Where a guarantee for a loan covered by the general budget of the Union in accordance with Regulation (EC) No 332/2002 or Regulation (EU) No 407/2010 needs to be mobilised, it shall be over and above the ceilings laid down in the MFF.

Article 4

Respect of own resources ceiling

1. For each of the years covered by the MFF, the total appropriations for payments required, after annual adjustment and taking account of any other adjustments and revisions as well as the application of paragraphs 2 and 3 of Article 3, shall not be such as to produce a call-in rate for own resources that exceeds the own resources ceiling set in accordance with Decision 2007/436/EC, Euratom.

2. Where necessary, the ceilings set in the MFF shall be lowered by way of revision in order to ensure compliance with the own-resources ceiling set in accordance with Decision 2007/436/EC, Euratom.

Article 5

Global margin for payments

1. Every year, starting in 2015, as part of the technical adjustment referred to in Article 6, the Commission shall adjust the payment ceiling for the years 2015-2020 upwards by an amount equivalent to the difference between the executed payments and the MFF payment ceiling of the year $n-1$.

2. The annual adjustments shall not exceed the following maximum amounts (in 2011 prices) for the years 2018-2020 as compared to the original payment ceiling of the relevant years:

2018 - EUR 7 billion

2019 - EUR 9 billion

2020 - EUR 10 billion.

(¹) Council Regulation (EC) No 1012/2002 of 11 November 2002 establishing the European Union Solidarity Fund (OJ L 311, 14.11.2002, p. 3).

(²) Regulation (EC) No 1927/2006 of the European Parliament and of the Council of 20 December 2006 on establishing the European Globalisation Adjustment Fund (OJ L 406, 30.12.2006, p. 1).

(³) Interinstitutional Agreement between the European Parliament, the Council and the Commission of 2 December 2013 on budgetary discipline, cooperation in budgetary matters and on sound financial management (OJ C 373, 20.12.2013, p. 1).

3. Any upward adjustment shall be fully offset by a corresponding reduction of the payment ceiling for year $n-1$.

Article 6

Technical adjustments

1. Each year the Commission, acting ahead of the budgetary procedure for year $n+1$, shall make the following technical adjustments to the MFF:

- (a) revaluation, at year $n+1$ prices, of the ceilings and of the overall figures for appropriations for commitments and appropriations for payments;
- (b) calculation of the margin available under the own-resources ceiling set in accordance with Decision 2007/436/EC, Euratom;
- (c) calculation of the absolute amount of the Contingency Margin provided for in Article 13;
- (d) calculation of the global margin for payments provided for in Article 5;
- (e) calculation of the global margin for commitments provided for in Article 14.

2. The Commission shall make the technical adjustments referred to in paragraph 1 on the basis of a fixed deflator of 2 % per year.

3. The Commission shall communicate the results of the technical adjustments referred to in paragraph 1 and the underlying economic forecasts to the European Parliament and the Council.

4. Without prejudice to Article 7 and 8, no further technical adjustments shall be made in respect of the year concerned, either during the year or as ex-post corrections during subsequent years.

Article 7

Adjustment of cohesion policy envelopes

1. To take account of the particularly difficult situation of Member States suffering from the crisis, the Commission shall in 2016, together with the technical adjustment for the year 2017, review all Member States' total allocations under the "Investment for growth and jobs" goal of cohesion policy for the years 2017 to 2020, applying the allocation method defined in the relevant basic act on the basis of the then available most recent statistics and of the comparison, for the capped Member States, between the cumulated national GDP observed for the years 2014 and 2015 and the cumulated national GDP estimated in 2012. It shall adjust those total allocations whenever there is a cumulative divergence of more than +/- 5%.

2. The adjustments required shall be spread in equal proportions over the years 2017-2020 and the corresponding ceilings of the MFF shall be modified accordingly. The payment ceilings shall also be modified accordingly to ensure an orderly progression in relation to the appropriations for commitments.

3. In its technical adjustment for the year 2017, following the mid-term review of the eligibility of Member States for the Cohesion Fund provided for in Article 90(5) of Regulation (EU) No 1303/2013 of the European Parliament and of the Council⁽¹⁾, in case a Member State either becomes newly eligible to the Cohesion Fund or loses its existing eligibility, the Commission shall add or subtract the resulting amounts to or from the funds allocated to the Member State for the years 2017 to 2020.

4. The required adjustments resulting from paragraph 3 shall be spread in equal proportions over the years 2017-2020 and the corresponding ceilings of the MFF shall be modified accordingly. The payment ceilings shall also be modified accordingly to ensure an orderly progression in relation to the appropriations for commitments.

5. The total net effect, whether positive or negative, of the adjustments referred to in paragraphs 1 and 3 shall not exceed EUR 4 billion.

Article 8

Adjustments related to measures linking effectiveness of funds to sound economic governance

In the case of the lifting by the Commission of a suspension of budgetary commitments concerning the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development or the European Maritime and Fisheries Fund in the context of measures linking effectiveness of funds to sound economic governance, the Commission, in accordance with the relevant basic act, shall transfer the suspended commitments to the following years. Suspended commitments of year *n* may not be re-budgeted beyond year *n*+3.

CHAPTER 2

Special instruments

Article 9

Emergency Aid Reserve

1. The Emergency Aid Reserve is intended to allow for a rapid response to specific aid requirements of third countries

⁽¹⁾ Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund covered by the Common Strategic Framework and laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Council Regulation (EC) No 1083/2006 (See page 320 of this Official Journal).

following events which could not be foreseen when the budget was established, first and foremost for humanitarian operations, but also for civil crisis management and protection, and situations of particular pressure resulting from migratory flows at the Union's external borders where circumstances so require.

2. The annual amount of the Reserve is fixed at EUR 280 million (2011 prices) and may be used up to year *n*+1 in accordance with the Financial Regulation. The Reserve shall be entered in the general budget of the Union as a provision. The portion of the annual amount stemming from the previous year shall be drawn on first. That portion of the annual amount from year *n* which is not used in year *n*+1 shall lapse.

Article 10

European Union Solidarity Fund

1. The European Union Solidarity Fund is intended to allow financial assistance in the event of major disasters occurring on the territory of a Member State or of a candidate country, as defined in the relevant basic act. There shall be a ceiling on the annual amount available for that Fund of EUR 500 million (2011 prices). On 1 October each year, at least one quarter of the annual amount shall remain available in order to cover needs arising until the end of that year. The portion of the annual amount not entered in the budget may be used up to year *n*+1. The portion of the annual amount stemming from the previous year shall be drawn on first. That portion of the annual amount from year *n* which is not used in year *n*+1 shall lapse.

2. In exceptional cases and if the remaining financial resources available in the European Union Solidarity Fund in the year of occurrence of the disaster, as defined in the relevant basic act, are not sufficient to cover the amount of assistance considered necessary by the European Parliament and the Council, the Commission may propose that the difference be financed through the annual amounts available for the following year.

Article 11

Flexibility Instrument

1. The Flexibility Instrument is intended to allow the financing, for a given financial year, of clearly identified expenditure which could not be financed within the limits of the ceilings available for one or more other headings. There shall be a ceiling on the annual amount available for the Flexibility Instrument of EUR 471 million (2011 prices).

2. The unused portion of the annual amount of the Flexibility Instrument may be used up to year *n*+3. The portion of the annual amount stemming from previous years shall be used first, in order of age. That portion of the annual amount from year *n* which is not used in year *n*+3 shall lapse.

*Article 12***European Globalisation Adjustment Fund**

1. The European Globalisation Adjustment Fund, the objectives and scope of which are defined in Regulation (EC) No 1927/2006 of the European Parliament and of the Council, shall not exceed a maximum annual amount of EUR 150 million (2011 prices).

2. The appropriations for the European Globalisation Adjustment Fund shall be entered in the general budget of the Union as a provision.

*Article 13***Contingency Margin**

1. A Contingency Margin of up to 0,03 % of the Gross National Income of the Union shall be constituted outside the ceilings of the MFF, as a last-resort instrument to react to unforeseen circumstances. It may be mobilised only in relation to an amending or annual budget.

2. Recourse to the Contingency Margin shall not exceed, at any given year, the maximum amount foreseen in the annual technical adjustment of the MFF, and shall be consistent with the own-resources ceiling.

3. Amounts made available through the mobilisation of the Contingency Margin shall be fully offset against the margins in one or more MFF headings for the current or future financial years.

4. The amounts thus offset shall not be further mobilised in the context of the MFF. Recourse to the Contingency Margin shall not result in exceeding the total ceilings of commitment and payment appropriations laid down in the MFF for the current and future financial years.

*Article 14***Global margin for commitments for growth and employment, in particular youth employment**

1. Margins left available below the MFF ceilings for commitment appropriations for the years 2014-2017 shall constitute a Global MFF Margin for commitments, to be made available over and above the ceilings established in the MFF for the years 2016 to 2020 for policy objectives related to growth and employment, in particular youth employment.

2. Each year, as part of the technical adjustment provided for in Article 6, the Commission shall calculate the amount available. The Global MFF Margin or part thereof may be mobilised by the European Parliament and the Council in the framework of the budgetary procedure pursuant to Article 314 TFEU.

*Article 15***Specific flexibility to tackle youth unemployment and strengthen research**

Up to EUR 2 543 million (in 2011 prices) may be frontloaded in 2014 and 2015, as part of the annual budgetary procedure, for specified policy objectives relating to youth employment, research, ERASMUS in particular for apprenticeships, and Small and Medium-sized Enterprises. That amount shall be fully offset against appropriations within and/or between headings in order to leave unchanged the total annual ceilings for the period 2014-2020 and the total allocation per heading or sub-heading over the period.

*Article 16***Contribution to the financing of large-scale projects**

1. A maximum amount of EUR 6 300 million (in 2011 prices) shall be available for the European satellite navigation programmes (EGNOS and Galileo) from the general budget of the Union for the period 2014-2020.

2. A maximum amount of EUR 2 707 million (in 2011 prices) shall be available for the International Thermonuclear Experimental Reactor project (ITER) from the general budget of the Union for the period 2014-2020.

3. A maximum amount of EUR 3 786 million (in 2011 prices) shall be available for Copernicus (the European Earth Observation Programme) from the general budget of the Union for the period 2014-2020.

CHAPTER 3

Revision*Article 17***Revision of the MFF**

1. Without prejudice to Article 4(2), Articles 18 to 22 and Article 25, in the event of unforeseen circumstances, the MFF may be revised in compliance with the own-resources ceiling set in accordance with Decision 2007/436/EC, Euratom.

2. As a general rule, any proposal for a revision of the MFF in accordance with paragraph 1 shall be presented and adopted before the start of the budgetary procedure for the year or the first of the years concerned.

3. Any proposal for revision of the MFF in accordance with paragraph 1 shall examine the scope for reallocating expenditure between the programmes covered by the heading concerned by the revision, with particular reference to any expected under-utilisation of appropriations. The objective should be that a significant amount, in absolute terms and as a percentage of the new expenditure planned, shall be within the existing ceiling for the heading.

4. Any revision of the MFF in accordance with paragraph 1 shall take into account the scope for offsetting any raising of the ceiling for one heading by the lowering of the ceiling for another.

5. Any revision of the MFF in accordance with paragraph 1 shall maintain an appropriate relationship between commitments and payments.

Article 18

Revision related to implementation

When notifying the European Parliament and the Council of the results of the technical adjustments to the MFF, the Commission shall present any proposals to revise the total appropriations for payments which it considers necessary, in the light of implementation, to ensure a sound management of the yearly payments ceilings and, in particular, their orderly progression in relation to the appropriations for commitments. The European Parliament and the Council shall decide on those proposals before 1 May of year *n*.

Article 19

Revision following new rules or programmes for the Structural Funds, the Cohesion Fund the European Agricultural Fund for Rural Development, the European Maritime and Fisheries Fund, the Asylum and Migration Fund and the Internal Security Fund

1. In the event of the adoption after 1 January 2014 of new rules or programmes under shared management for the Structural Funds, the Cohesion Fund, the European Agricultural Fund for Rural Development, the European Maritime and Fisheries Fund, the Asylum and Migration Fund and the Internal Security Fund, the MFF shall be revised in order to transfer to subsequent years, in excess of the corresponding expenditure ceilings, allocations not used in 2014.

2. The revision concerning the transfer of unused allocation for the year 2014 shall be adopted before 1 May 2015.

Article 20

Revision of the MFF in case of a revision of the Treaties

Should a revision of the Treaties with budgetary implications occur between 2014 and 2020, the MFF shall be revised accordingly.

Article 21

Revision of the MFF in the event of enlargement of the Union

If there is an accession or accessions to the Union between 2014 and 2020, the MFF shall be revised to take account of the expenditure requirements resulting therefrom.

Article 22

Revision of the MFF in the event of the reunification of Cyprus

In the event of the reunification of Cyprus between 2014 and 2020, the MFF shall be revised to take account of the comprehensive settlement of the Cyprus problem and the additional financial needs resulting from the reunification.

Article 23

Interinstitutional cooperation in the budgetary procedure

The European Parliament, the Council and the Commission (hereinafter "the institutions") shall take measures to facilitate the annual budgetary procedure.

The institutions shall cooperate in good faith throughout the procedure with a view to reconciling their positions. The institutions shall, at all stages of the procedure, cooperate through appropriate interinstitutional contacts in order to monitor the progress of the work and analyse the degree of convergence.

The institutions shall ensure that their respective calendars of work are coordinated as far as possible, in order to enable proceedings to be conducted in a coherent and convergent fashion, leading to the final adoption of the general budget of the Union.

Trilogues may be held at all stages of the procedure and at different levels of representation, depending on the nature of the expected discussions. Each institution, in accordance with its own rules of procedure, shall designate its participants for each meeting, define its mandate for the negotiations and inform the other institutions in good time of the arrangements for the meetings.

Article 24

Unity of the budget

All expenditure and revenue of the Union and Euratom shall be included in the general budget of the Union in accordance with Article 7 of the Financial Regulation, including expenditure resulting from any relevant decision taken unanimously by the Council after consulting the European Parliament, in the framework of Article 332 TFEU.

Article 25

Transition towards the next multiannual financial framework

Before 1 January 2018, the Commission shall present a proposal for a new multiannual financial framework.

If no Council regulation determining a new multiannual financial framework has been adopted before 31 December 2020, the ceilings and other provisions corresponding to the last year of the MFF shall be extended until a regulation determining a new financial framework is adopted. If a new Member State accedes to the Union after 2020, the extended financial framework shall, if necessary, be revised in order to take the accession into account.

*Article 26***Entry into force**

This Regulation shall enter into force on the third day following that of its publication in the *Official Journal of the European Union*.

It shall apply from 1 January 2014.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 2 December 2013.

For the Council
The President
E. GUSTAS

ANNEX I

MULTIANNUAL FINANCIAL FRAMEWORK (EU-28)

COMMITMENT APPROPRIATIONS	(EUR million - 2011 prices)									
	2014	2015	2016	2017	2018	2019	2020	Total 2014-2020		
1. Smart and Inclusive Growth	60 283	61 725	62 771	64 238	65 528	67 214	69 004	450 763		
1a: Competitiveness for growth and jobs	15 605	16 321	16 726	17 693	18 490	19 700	21 079	125 614		
1b: Economic, social and territorial cohesion	44 678	45 404	46 045	46 545	47 038	47 514	47 925	325 149		
2. Sustainable Growth: Natural Resources	55 883	55 060	54 261	53 448	52 466	51 503	50 558	373 179		
of which: Market related expenditure and direct payments	41 585	40 989	40 421	39 837	39 079	38 335	37 605	277 851		
3. Security and citizenship	2 053	2 075	2 154	2 232	2 312	2 391	2 469	15 686		
4. Global Europe	7 854	8 083	8 281	8 375	8 553	8 764	8 794	58 704		
5. Administration	8 218	8 385	8 589	8 807	9 007	9 206	9 417	61 629		
of which: Administrative expenditure of the institutions	6 649	6 791	6 955	7 110	7 278	7 425	7 590	49 798		
6. Compensations	27	0	0	0	0	0	0	27		
TOTAL COMMITMENT APPROPRIATIONS	134 318	135 328	136 056	137 100	137 866	139 078	140 242	959 988		
as a percentage of GNI	1,03 %	1,02 %	1,00 %	1,00 %	0,99 %	0,98 %	0,98 %	1,00 %		
TOTAL PAYMENT APPROPRIATIONS	128 030	131 095	131 046	126 777	129 778	130 893	130 781	908 400		
as a percentage of GNI	0,98 %	0,98 %	0,97 %	0,92 %	0,93 %	0,93 %	0,91 %	0,95 %		
Margin available	0,25 %	0,25 %	0,26 %	0,31 %	0,30 %	0,30 %	0,32 %	0,28 %		
Own Resources Ceiling as a percentage of GNI	1,23 %	1,23 %	1,23 %	1,23 %	1,23 %	1,23 %	1,23 %	1,23 %		

Annex 3

IIA of 2 December 2013

II

(Information)

INTERINSTITUTIONAL AGREEMENTS

EUROPEAN PARLIAMENT
COUNCIL
EUROPEAN COMMISSION

INTERINSTITUTIONAL AGREEMENT

of 2 December 2013

between the European Parliament, the Council and the Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management

(2013/C 373/01)

THE EUROPEAN PARLIAMENT, THE COUNCIL OF THE EUROPEAN UNION AND THE EUROPEAN COMMISSION,

hereinafter referred to as the 'institutions',

HAVE AGREED AS FOLLOWS:

1. The purpose of this Agreement, adopted in accordance with Article 295 of the Treaty on the Functioning of the European Union (TFEU), is to implement budgetary discipline and improve the functioning of the annual budgetary procedure and cooperation between the institutions on budgetary matters as well as to ensure sound financial management.
2. Budgetary discipline in this Agreement covers all expenditure. The Agreement is binding on all the institutions for as long as it is in force.
3. This Agreement does not alter the respective budgetary powers of the institutions as laid down in the Treaties, in Council Regulation (EU, Euratom) No 1311/2013⁽¹⁾ (the 'MFF Regulation') and in Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council⁽²⁾ (the 'Financial Regulation').

4. Any amendment of this Agreement requires the common agreement of all the institutions.

5. This Agreement is in three parts:

- Part I contains complementary provisions related to the multiannual financial framework (MFF) and provisions on special instruments not included in the MFF.
- Part II relates to interinstitutional cooperation during the budgetary procedure.
- Part III contains provisions related to the sound financial management of Union funds.

6. This Agreement enters into force on 23 December 2013 and replaces the Interinstitutional Agreement of 17 May 2006 between the European Parliament, the Council and the Commission on budgetary discipline and sound financial management⁽³⁾.

PART I

MFF AND SPECIAL INSTRUMENTS

A. Provisions related to the MFF

7. Information relating to operations not included in the general budget of the Union and to the foreseeable development of the various categories of the Union's own

⁽¹⁾ Council Regulation (EU, Euratom) No 1311/2013 of 20 December 2013 laying down the Multiannual Financial Framework for the years 2014-2020 (OJ L 347, 20.12.2013, p. 884).

⁽²⁾ Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (OJ L 298, 26.10.2012, p. 1).

⁽³⁾ OJ C 139, 14.6.2006, p. 1.

resources is set out, by way of indication, in separate tables. That information shall be updated annually together with the documents accompanying the draft budget.

8. The institutions shall, for the purposes of sound financial management, ensure as far as possible during the budgetary procedure and at the time of the budget's adoption that sufficient margins are left available beneath the ceilings for the various headings of the MFF, except in the sub-heading 'Economic, social and territorial cohesion'.

Updating of forecasts for payment appropriations after 2020

9. In 2017, the Commission shall update the forecasts for payment appropriations after 2020. That update shall take into account all relevant information, including the real implementation of budget appropriations for commitments and budget appropriations for payments, as well as the implementation forecasts. It shall also consider the rules designed to ensure that payment appropriations develop in an orderly manner compared to commitment appropriations and the growth forecasts of the Union's Gross National Income.

B. Provisions related to the special instruments not included in the MFF

Emergency Aid Reserve

10. When the Commission considers that the Emergency Aid Reserve needs to be called on, it shall present to the European Parliament and the Council a proposal for a transfer from the Reserve to the corresponding budgetary lines.

Any Commission proposal for a transfer from the Reserve, however, shall be preceded by an examination of the scope for reallocating appropriations.

In the event of disagreement, a trilogue procedure shall be initiated.

Transfers from the Reserve shall be made in accordance with the Financial Regulation.

European Union Solidarity Fund

11. When the conditions for mobilising the European Union Solidarity Fund as set out in the relevant basic act are met, the Commission shall make a proposal to mobilise it. Where there is scope for reallocating appropriations under the heading requiring additional expenditure, the Commission shall take that into account when making the necessary proposal, in accordance with the Financial Regulation, by means of the appropriate budgetary instrument. The decision to mobilise the Solidarity Fund shall be taken jointly by the European Parliament and the Council. The Council shall act by a qualified majority and the European Parliament shall act by a majority of its component members and three fifths of the votes cast.

In the event of disagreement, a trilogue procedure shall be initiated.

Flexibility Instrument

12. The Commission shall make a proposal for the Flexibility Instrument to be mobilised after it has examined all possibilities for re-allocating appropriations under the heading requiring additional expenditure.

The proposal shall identify the needs to be covered and the amount. It may be presented, for any given financial year, during the budgetary procedure.

The decision to mobilise the Flexibility Instrument shall be taken jointly by the European Parliament and the Council. The Council shall act by a qualified majority and the European Parliament shall act by a majority of its component members and three fifths of the votes cast.

Agreement shall be reached in the framework of the annual budgetary procedure.

European Globalisation Adjustment Fund

13. When the conditions for mobilising the European Globalisation Adjustment Fund, as set out in the relevant basic act, are met, the Commission shall make a proposal to mobilise it. The decision to mobilise the Globalisation Adjustment Fund shall be taken jointly by the European Parliament and the Council. The Council shall act by a qualified majority and the European Parliament shall act by a majority of its component members and three fifths of the votes cast.

At the same time as it presents its proposal for a decision to mobilise the Globalisation Adjustment Fund, the Commission shall present to the European Parliament and the Council a proposal for a transfer to the relevant budgetary lines.

In the event of disagreement, a trilogue procedure shall be initiated.

Transfers related to the Globalisation Adjustment Fund shall be made in accordance with the Financial Regulation.

Contingency Margin

14. The mobilisation of the Contingency Margin, or part thereof, shall be proposed by the Commission after a thorough analysis of all other financial possibilities. Such a proposal may only be made in relation to a draft amending or annual budget, for the adoption of which such a proposal would be necessary. The Commission shall accompany the proposal for the mobilisation of the Contingency Margin with a proposal for the reallocation, within the existing budget, of a significant amount, as far as supported by the Commission's analysis.

The decision to mobilise the Contingency Margin shall be taken jointly by the European Parliament and the Council simultaneously with their approval of the amending budget or general budget of the Union the adoption of which the Contingency Margin facilitates. The European Parliament and the Council shall act in accordance with the voting rules provided for in Article 314 TFEU for the approval of the general budget of the Union.

PART II

IMPROVEMENT OF INTERINSTITUTIONAL COOPERATION IN BUDGETARY MATTERS

A. Interinstitutional cooperation procedure

15. The details of interinstitutional cooperation during the budgetary procedure are set out in the Annex.

Budgetary Transparency

16. The Commission shall prepare an annual report to accompany the general budget of the Union, bringing together available and non-confidential information relating to:

- the assets and liabilities of the Union, including those arising from borrowing and lending operations carried out by the Union in accordance with its powers under the Treaties,
- the revenue, expenditure, assets and liabilities of the European Development Fund (EDF), the European Financial Stability Facility (EFSF), the European Stability Mechanism (ESM), and other possible future mechanisms, including trust funds,
- the expenditure incurred by Member States in the framework of enhanced cooperation, to the extent that it is not included in the general budget of the Union.

B. Incorporation of financial provisions in legislative acts

17. Each legislative act, concerning a multiannual programme, adopted under the ordinary legislative procedure shall contain a provision in which the legislator lays down the financial envelope for the programme.

That amount shall constitute the prime reference amount for the European Parliament and the Council during the annual budgetary procedure.

The European Parliament and the Council, and the Commission when it draws up the draft budget, undertake not to depart by more than 10 % from that amount for the entire duration of the programme concerned, unless new, objective, long-term circumstances arise for which explicit and precise reasons are given, with account being taken of the results obtained from implementing the programme, in particular on the basis of assessments. Any increase resulting from such variation

shall remain beneath the existing ceiling for the heading concerned, without prejudice to the use of instruments mentioned in the MFF Regulation and in this Agreement.

This Point applies neither to appropriations for cohesion adopted under the ordinary legislative procedure and pre-allocated by Member States, which contain a financial envelope for the entire duration of the programme nor to the large scale projects referred to in Article 16 of the MFF Regulation.

18. Legislative acts, concerning multiannual programmes, not subject to the ordinary legislative procedure shall not contain an 'amount deemed necessary'.

Should the Council wish to include a financial reference amount, that amount shall be taken as illustrating the will of the legislator and shall not affect the budgetary powers of the European Parliament and the Council as set out in the TFEU. A provision to this effect shall be included in all legislative acts which contain such a financial reference amount.

If the financial reference amount concerned has been the subject of an agreement pursuant to the conciliation procedure provided for in the Joint Declaration of the European Parliament, the Council and the Commission of 4 March 1975 ⁽¹⁾, it shall be considered a reference amount within the meaning of Point 17 of this Agreement.

C. Expenditure relating to fisheries agreements

19. Expenditure on fisheries agreements shall be subject to the following specific rules.

The Commission undertakes to keep the European Parliament regularly informed about the preparation and conduct of the negotiations, including their budgetary implications.

In the course of the legislative procedure relating to fisheries agreements, the institutions undertake to make every effort to ensure that all procedures are carried out as quickly as possible.

Amounts provided for in the budget for new fisheries agreements or for the renewal of fisheries agreements which come into force after January 1 of the related financial year shall be put in reserve.

If appropriations relating to fisheries agreements (including the reserve) prove insufficient, the Commission shall provide the European Parliament and the Council with the necessary information for an exchange of views in the form of a trilogue, possibly in a simplified form, on the causes of the situation, and on measures which might be adopted under established procedures. Where necessary, the Commission shall propose appropriate measures.

⁽¹⁾ OJ C 89, 22.4.1975, p. 1.

Each quarter, the Commission shall present to the European Parliament and the Council detailed information about the implementation of fisheries agreements in force and a financial forecast for the remainder of the year.

20. Representatives of the European Parliament may take part, with observer status, in bilateral and multilateral conferences negotiating international fisheries agreements, taking account of the European Parliament's powers in the field of fisheries agreements and in accordance with points 25 and 26 of the Framework Agreement on relations between the European Parliament and the European Commission⁽¹⁾.
21. Without prejudice to the relevant procedure governing the negotiation of fisheries agreements, the European Parliament and the Council commit themselves, in the framework of budgetary cooperation, to arrive at a timely agreement on the adequate financing of fisheries agreements.

D. Expenditure relating to the reserve for crises in the agricultural sector

22. Appropriations for the Reserve for crises in the agricultural sector provided for in Article 25 of Regulation (EU) No 1306/2013 of the European Parliament and of the Council⁽²⁾ shall be entered directly in the general budget of the Union. Any amount of the Reserve not made available for crisis measures shall be reimbursed to direct payments.

Expenditure related to measures for crises occurring between 16 October and the end of the financial year may be financed from the reserve of the following financial year in accordance with the requirements laid down in the third paragraph.

If the Commission considers that the Reserve needs to be called on, in accordance with the relevant legislative act, it shall present to the European Parliament and to the Council a proposal for a transfer from the Reserve to the budget lines financing the measures it considers necessary. Any Commission proposal for a transfer from the Reserve shall be preceded by an examination of the scope for real-locating appropriations.

Transfers from the Reserve shall be made in accordance with the Financial Regulation.

In the event of disagreement, a trilogue procedure shall be initiated.

E. Financing of the common foreign and security policy (CFSP)

23. The total amount of CFSP operating expenditure shall be entered entirely in one budget chapter, entitled CFSP. That amount shall cover the real predictable needs, assessed in the framework of the establishment of the draft budget, on

the basis of forecasts drawn up annually by the High Representative of the Union for Foreign Affairs and Security Policy (the 'High Representative'), and a reasonable margin for unforeseen actions. No funds may be entered in a reserve.

24. As regards CFSP expenditure which is charged to the general budget of the Union in accordance with Article 41 of the Treaty on European Union, the institutions shall endeavour, in the Conciliation Committee, and on the basis of the draft budget established by the Commission, to secure agreement each year on the amount of the operating expenditure to be charged to the general budget of the Union, and on the distribution of that amount between the articles of the CFSP budget chapter suggested in the fourth paragraph of this Point. In the absence of agreement, it is understood that the European Parliament and the Council shall enter in the budget the amount contained in the previous budget or the amount proposed in the draft budget, whichever is the lower.

The total amount of CFSP operating expenditure shall be distributed between the articles of the CFSP budget chapter as suggested in the fourth paragraph. Each article shall cover instruments already adopted, instruments which are foreseen but not yet adopted and all other future — that is unforeseen — instruments to be adopted by the Council during the financial year concerned.

Since, under the Financial Regulation, the Commission has the authority to transfer appropriations autonomously between articles within the CFSP budget chapter, the flexibility deemed necessary for speedy implementation of CFSP actions shall accordingly be assured. In the event of the amount of the CFSP budget chapter during the financial year being insufficient to cover the necessary expenses, the European Parliament and the Council shall seek a solution as a matter of urgency, on a proposal from the Commission, taking into account Article 3 of the MFF Regulation and Point 10 of this Agreement.

Within the CFSP budget chapter, the articles into which the CFSP actions are to be entered could read along the following lines:

- single major missions as referred to in Article 49(1)(g) of the Financial Regulation,
- crisis management operations, conflict prevention, resolution and stabilisation, and monitoring and implementation of peace and security processes,
- non-proliferation and disarmament,
- emergency measures,
- preparatory and follow-up measures,
- European Union Special Representatives.

⁽¹⁾ OJ L 304, 20.11.2010, p. 47.

⁽²⁾ Regulation (EU) No 1306/2013 of the European Parliament and of the Council of 17 December 2013 on the financing, management and monitoring of the Common Agricultural Policy (OJ L 347, 20.12.2013, p. 549).

25. Each year, the High Representative shall consult the European Parliament on a forward-looking document, which shall be transmitted by June 15 of the year in question, setting out the main aspects and basic choices of the CFSP, including the financial implications for the general budget of the Union, an evaluation of the measures launched in the year n-1 and an assessment of the coordination and complementarity of CFSP with the Union's other external financial instruments. Furthermore, the High Representative shall keep the European Parliament regularly informed by holding joint consultation meetings at least five times a year, in the framework of the regular political dialogue on the CFSP, to be agreed at the latest in the Conciliation Committee. Participation in those meetings shall be determined by the European Parliament and the Council respectively, bearing in mind the objective, and the nature of the information exchanged in those meetings.

The Commission shall be invited to participate in those meetings.

If the Council adopts a decision in the field of the CFSP entailing expenditure, the High Representative shall immediately, and in any event no later than five working days thereafter, send the European Parliament an estimate of the costs envisaged (a 'financial statement'), in particular those costs regarding time-frame, staff employed, use of premises and other infrastructure, transport facilities, training requirements and security arrangements.

Once a quarter, the Commission shall inform the European Parliament and the Council about the implementation of CFSP actions and the financial forecasts for the remainder of the financial year.

F. Involvement of the institutions as regards development policy issues and the European Development Fund

26. The Commission shall establish an informal dialogue with the European Parliament on development policy issues regardless of their source of financing. The scrutiny of the European Parliament of the European Development Fund (EDF) will be aligned on a voluntary basis to the scrutiny rights that exist under the general budget of the Union, specifically in relation to the Development Cooperation Instrument, pursuant to detailed arrangements to be fixed in the informal dialogue.

The European Parliament and the Council note that the Commission, with a view to, *inter alia*, enhancing the democratic scrutiny of development policy, intends to propose the budgetisation of the EDF as of 2021.

G. Cooperation of the institutions in the budgetary procedure on administrative expenditure

27. The savings implied by the ceiling for heading 5 as set out in the Annex to the MFF Regulation, shall be proportionately shared between all institutions as well as other Union bodies based on their respective share of the administrative budgets.

Each institution, body or agency is expected to present estimates of expenditure in the annual budgetary procedure consistent with the orientations referred to in the first paragraph.

To neutralise the additional capacity built up by the increase of working time to 40 hours per week, the European Parliament, the Council and the Commission agree to progressively render 5 % of the staff as in the establishment plan on 1 January 2013⁽¹⁾. This reduction should apply to all institutions, bodies and agencies, and be effected between 2013 and 2017. This does not prejudice the budgetary rights of the European Parliament and the Council.

PART III

SOUND FINANCIAL MANAGEMENT OF UNION FUNDS

A. Joint management

28. The Commission shall ensure that the European Parliament, the Council and the Court of Auditors, at their request, receive any information and documentation related to Union funds spent through international organisations, obtained under the verification agreements concluded with those organisations, which are considered necessary for the exercise of the competences of the European Parliament, the Council or the Court of Auditors under the TFEU.

Evaluation report

29. In the evaluation report provided for by Article 318 TFEU, the Commission shall distinguish between internal policies, focused on the Europe 2020 strategy, and the external policies and shall use more performance information, including performance audit results, to evaluate the finances of the Union based on the results achieved.

Financial programming

30. The Commission shall submit twice a year, the first time in April or May (together with the documents accompanying the draft budget) and the second time in December or January (after the adoption of the general budget of the Union), a complete financial programming for headings 1 (except the sub-heading for 'Economic, social and territorial cohesion'), 2 (for 'environment' and 'fisheries' only), 3 and 4 of the MFF. That programming, structured by heading, policy area and budget line, should identify:

- (a) the legislation in force, with a distinction being drawn between multiannual programmes and annual actions:
 - for multiannual programmes, the Commission should indicate the procedure under which they were adopted (ordinary or special legislative procedure), their duration, the total financial envelope and the share allocated to administrative expenditure,

⁽¹⁾ The Council and the Commission have already implemented a first reduction of 1 % of staff as in their establishment plan on 1 January 2013.

- for annual actions (relating to pilot projects, preparatory actions and agencies) and actions financed under the prerogatives of the Commission, the Commission should provide multiannual estimates and indicate the margins left under the authorised ceilings fixed in Commission Delegated Regulation (EU) No 1268/2012 ⁽¹⁾;

- (b) pending legislative proposals: ongoing Commission proposals, with the latest update.

The Commission should consider ways of cross-referencing the financial programming with its legislative programming to provide more precise and reliable forecasts. For each legislative proposal, the Commission should indicate whether it is included in the April programme or in the December programme. The European Parliament and the Council should in particular be informed of:

- (a) all new legislative acts adopted and all pending proposals presented but not included in the April or the December programme (with the corresponding amounts);
- (b) legislation foreseen in the Commission's annual legislative work programme, with an indication of whether the actions are likely to have a financial impact.

Whenever necessary, the Commission should indicate the reprogramming entailed by new legislative proposals.

B. Agencies and European schools

31. Before presenting a proposal for the creation of a new agency, the Commission should produce a sound, complete and objective impact assessment, taking into account, *inter alia*, the critical mass of staff and competencies, cost-benefit aspects, subsidiarity and proportionality, the impact on national and Union activities, and the budgetary implications for the expenditure heading concerned. On the basis of that information and without prejudice to the legislative procedures governing the setting up of the agency, the European Parliament and the Council commit themselves, in the framework of budgetary cooperation, to arrive at a timely agreement on the financing of the proposed agency.

The following procedural steps shall be applied:

- firstly, the Commission shall systematically present any proposal for setting up a new agency to the first

trilogue following the adoption of its proposal, and shall present the financial statement accompanying the draft legal act proposing the creation of the agency and shall illustrate the consequences thereof for the remaining period of the financial programming,

- secondly, during the legislative process, the Commission shall assist the legislator in assessing the financial consequences of the amendments proposed. Those financial consequences should be considered during the relevant legislative trilogues,

- thirdly, before the conclusion of the legislative process, the Commission shall present an updated financial statement taking into account potential modifications by the legislator; this final financial statement shall be placed on the agenda of the final legislative trilogue and formally endorsed by the legislator. It shall also be placed on the agenda of a subsequent budgetary trilogue (in urgent cases, in simplified form), in view of reaching an agreement on the financing,

- fourthly, the agreement reached during a trilogue, taking into account the Commission's budgetary assessment with regard to the content of the legislative process, shall be confirmed in a joint declaration. That agreement shall be subject to approval by the European Parliament and the Council, each in accordance with its own rules of procedure.

The same procedure would be applied to any amendment to a legal act concerning an agency which would have an impact on the resources of the agency in question.

Should the tasks of an agency be modified substantially without an amendment to the legal act setting up the agency in question, the Commission shall inform the European Parliament and the Council by means of a revised financial statement, so as to allow the European Parliament and the Council to arrive at a timely agreement on the financing of the agency.

32. Relevant provisions from the Common Approach annexed to the Joint Statement of the European Parliament, the Council of the European Union and the European Commission on decentralised agencies signed on 19 July 2012 should be duly taken into account in the budgetary procedure.

⁽¹⁾ Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union (OJ L 362, 31.12.2012, p. 1).

33. When the creation of a new European school is envisaged by the Board of Governors, a similar procedure is to be applied, *mutatis mutandis*, for its budgetary implications on the general budget of the Union.

Done at Brussels, 9 December 2013.

For the Council
The President
J. BERNATONIS

For the Commission
J. LEWANDOWSKI
Member of the Commission

Done at Strasbourg, 10 December 2013.

For the European Parliament
The President
M. SCHULZ

ANNEX

Interinstitutional cooperation during the budgetary procedure**Part A. Calendar of the budgetary procedure**

1. The institutions shall agree a pragmatic calendar each year in due time before the start of the budgetary procedure on the basis of present practice.

Part B. Priorities for the budgetary procedure

2. In due time before the adoption of the draft budget by the Commission, a trilogue shall be convened to discuss the possible priorities for the budget of the coming financial year.

Part C. Establishment of the draft budget and updating of estimates

3. The institutions, other than the Commission, are invited to adopt their statement of estimates before the end of March.

4. The Commission shall, each year, present a draft budget showing the Union's actual financing requirements.

It shall take into account:

- (a) forecasts provided by the Member States in relation to the Structural Funds;
 - (b) the capacity for utilising appropriations, while endeavouring to maintain a strict relationship between appropriations for commitments and appropriations for payments;
 - (c) possibilities for starting up new policies through pilot projects, new preparatory actions or both, or for continuing multiannual actions which are coming to an end, after assessing whether it is possible to secure a basic act, within the meaning of the Financial Regulation (definition of a basic act, necessity of a basic act for implementation and exceptions);
 - (d) the need to ensure that any change in expenditure in relation to the previous year is in accordance with the constraints of budgetary discipline.
5. The institutions shall, as far as possible, avoid entering items in the budget involving insignificant amounts of expenditure on operations.
 6. The European Parliament and the Council also undertake to bear in mind the assessment of the possibilities for implementing the budget made by the Commission in its drafts and in connection with the implementation of the current budget.
 7. In the interests of sound financial management and owing to the effect of major changes in the titles and chapters of the budget nomenclature on the management reporting responsibilities of Commission departments, the European Parliament and the Council undertake to discuss any major changes with the Commission during the conciliation.
 8. In the interest of loyal and sound institutional cooperation, the European Parliament and the Council commit to maintaining regular and active contacts at all levels, through their respective negotiators, throughout the whole budgetary procedure and, in particular, during the conciliation period. The European Parliament and the Council undertake to ensure the timely and constant mutual exchange of relevant information and documents at both formal and informal levels, as well as to hold technical or informal meetings as needed, during the conciliation period, in cooperation with the Commission. The Commission shall ensure timely and equal access to information and documents for the European Parliament and the Council.
 9. Until such time as the Conciliation Committee is convened, the Commission may, if necessary, amend the draft budget in accordance with Article 314(2) TFEU, including by an amending letter updating expenditure estimates for agriculture. The Commission shall submit information on updates to the European Parliament and the Council for their consideration as soon as it is available. It shall supply the European Parliament and the Council with all the duly justified reasons they may require.

Part D. Budgetary procedure before the conciliation procedure

10. A trilogue shall be convened in good time before the Council's reading, to allow the institutions to have an exchange of views on the draft budget.
11. In order for the Commission to be able to assess in due time the implementability of amendments, envisaged by the European Parliament and the Council, which create new preparatory actions or pilot projects or which prolong existing ones, the European Parliament and the Council shall inform the Commission of their intentions in this regard, so that a first discussion may already take place at that trilogue.
12. A trilogue could be convened before the votes in plenary of the European Parliament.

Part E. **Conciliation procedure**

13. If the European Parliament adopts amendments to the Council's position, the President of the Council shall, during the same plenary sitting, take note of the differences in the position of the two institutions and give his/her agreement for the President of the European Parliament to convene the Conciliation Committee immediately. The letter convening the Conciliation Committee shall be sent at the latest on the first working day of the week following the end of the parliamentary part-session during which the plenary vote was delivered, and the conciliation period shall start on the following day. The 21-day time period shall be calculated in accordance with Regulation (EEC, Euratom) No 1182/71 of the Council ⁽¹⁾.
14. If the Council cannot agree on all the amendments adopted by the European Parliament, it should confirm its position by letter sent before the first meeting foreseen during the conciliation period. In such case, the Conciliation Committee shall proceed in accordance with the conditions laid down in the following points.
15. The Conciliation Committee shall be chaired jointly by representatives of the European Parliament and of the Council. Meetings of the Conciliation Committee shall be chaired by the co-chair from the institution hosting the meeting. Each institution, in accordance with its own rules of procedure, shall designate its participants for each meeting and define its mandate for the negotiations. The European Parliament and the Council shall be represented at an appropriate level in the Conciliation Committee, such that each delegation can commit politically its respective institution, and that actual progress towards the final agreement may be made.
16. In accordance with the second subparagraph of Article 314(5) TFEU, the Commission shall take part in the Conciliation Committee's proceedings and shall take all necessary initiatives with a view to reconciling the positions of the European Parliament and the Council.
17. Trilogues shall take place throughout the conciliation procedure, at different levels of representation, with the aim of resolving outstanding issues and preparing the ground for an agreement to be reached in the Conciliation Committee.
18. Meetings of the Conciliation Committee and trilogues shall be held alternately at the premises of the European Parliament and of the Council, with a view to an equal sharing of facilities, including interpretation facilities.
19. The dates of the meetings of the Conciliation Committee and the trilogues shall be set in advance by agreement of the three institutions.
20. A common set of documents ('input documents') comparing the various steps of the budgetary procedure shall be made available to the Conciliation Committee ⁽²⁾. Those documents shall include 'line by line' figures, totals by MFF headings and a consolidated document with figures and remarks for all budget lines deemed technically 'open'. Without prejudice to the final decision of the Conciliation Committee, a specific document shall list all budget lines deemed technically closed ⁽³⁾. Those documents shall be classified by budgetary nomenclature.

Other documents shall also be attached to the input documents for the Conciliation Committee, including a letter of executability from the Commission on the Council's position and the European Parliament's amendments, and any letter(s) from other institutions concerning the Council's position or the European Parliament's amendments.

21. With a view to reaching agreement by the end of the conciliation period, trilogues shall:
 - define the scope of the negotiations on the budgetary issues to be addressed,
 - endorse the list of the budget lines deemed technically closed, subject to the final agreement on the entire budget of the financial year,
 - discuss issues identified under the first indent with a view to reaching possible agreements to be endorsed by the Conciliation Committee,
 - address thematic issues, including by headings of the MFF.

Tentative conclusions shall be drawn jointly during or immediately after each trilogue, and, simultaneously, the agenda of the following meeting shall be agreed. Those conclusions shall be registered by the institution hosting the trilogue and shall be deemed provisionally approved after 24 hours, without prejudice to the final decision of the Conciliation Committee.

22. The conclusions of trilogues and a document for possible endorsement shall be available to the Conciliation Committee at its meetings, together with the budget lines in respect of which an agreement has been tentatively reached during the trilogues.

⁽¹⁾ Regulation (EEC, Euratom) No 1182/71 of the Council of 3 June 1971 determining the rules applicable to periods, dates and time limits (OJ L 124, 8.6.1971, p. 1).

⁽²⁾ The various steps include: the budget of the current financial year (including adopted amending budgets); the initial draft budget; the Council's position on the draft budget; the European Parliament's amendments to the Council's position and the letters of amendment presented by the Commission (if not yet fully approved by all institutions).

⁽³⁾ A budget line deemed technically closed is a line for which there is no disagreement between the European Parliament and the Council, and for which no letter of amendment has been presented.

23. The joint text provided for in Article 314(5) TFEU shall be established by the secretariats of the European Parliament and of the Council with the assistance of the Commission. It shall consist of a letter of transmission addressed by the chairs of the two delegations to the Presidents of the European Parliament and Council, containing the date of the agreement at the Conciliation Committee, and annexes which shall include:

- line by line figures for all budget items and summary figures by MFF headings,
- a consolidated document, indicating the figures and final text of all lines that have been modified during the conciliation procedure,
- the list of the lines not modified with regard to the draft budget or the Council's position on it.

The Conciliation Committee may also approve conclusions and possible joint statements in relation to the budget.

24. The joint text shall be translated into the official languages of the institutions of the Union (by the services of the European Parliament) and shall be submitted for the approval of the European Parliament and the Council within a period of 14 days from the date of the agreement on the joint text pursuant to point 23.

The budget shall be subject to legal-linguistic finalisation after the adoption of the joint text by integrating the annexes of the joint text with the budget lines not modified during the conciliation procedure.

25. The institution hosting the meeting (trilogue or conciliation) shall provide interpretation facilities with a full linguistic regime applicable to the Conciliation Committee meetings and an ad hoc linguistic regime for the trilogues.

The institution hosting the meeting shall provide for the copying and distribution of room documents.

The services of the three institutions shall cooperate in the encoding of the results of the negotiations in order to finalise the joint text.

Part F. Amending budgets

General principles

26. Bearing in mind that amending budgets are frequently focused on specific and sometimes urgent issues, the institutions agree on the following principles to ensure appropriate interinstitutional cooperation for a smooth and swift decision-making process for amending budgets while avoiding, as far as possible, having to convene a conciliation meeting for amending budgets.
27. As far as possible, the institutions shall endeavour to limit the number of amending budgets.

Calendar

28. The Commission shall inform the European Parliament and the Council in advance of the possible dates of adoption of draft amending budgets, without prejudice to the final date of adoption.
29. Each in accordance with its internal rules of procedure, the European Parliament and the Council shall endeavour to examine the draft amending budget proposed by the Commission at an early opportunity after its adoption by the Commission.
30. In order to speed up the procedure, the European Parliament and the Council shall ensure that their respective calendars of work are coordinated as far as possible in order to enable proceedings to be conducted in a coherent and convergent fashion. They shall therefore seek as soon as possible to establish an indicative timetable for the various stages leading to the final adoption of the amending budget.

The European Parliament and the Council shall take into account the relative urgency of the amending budget and the need to approve it in due time to be effective during the financial year concerned.

Cooperation during the readings

31. The institutions shall cooperate in good faith throughout the procedure, clearing the way, as far as possible, for the adoption of amending budgets at an early stage of the procedure.

When appropriate, and when there is a potential divergence, the European Parliament or the Council, before each takes its final position on the amending budget, or the Commission at any time, may propose that a specific trilogue be convened to discuss the divergences and to try to reach a compromise.

32. All draft amending budgets proposed by the Commission and not yet finally approved shall be entered systematically on the agenda of trilogues planned for the annual budgetary procedure. The Commission shall present the draft amending budgets and the European Parliament and the Council shall, as far as possible, make known their respective positions ahead of the trilogue.

33. If a compromise is reached during a trilogue, the European Parliament and the Council undertake to consider the results of the trilogue when deliberating on the amending budget in accordance with the TFEU and their rules of procedure.

Cooperation after the readings

34. If the European Parliament approves the position of the Council without amendments, the amending budget shall be adopted in accordance with the TFEU.
35. If the European Parliament adopts amendments by a majority of its component members, Article 314(4)(c) TFEU shall apply. However, before the Conciliation Committee meets, a trilogue shall be called:
- if an agreement is reached during the trilogue and subject to the agreement of the European Parliament and the Council on the results of the trilogue, the conciliation shall be closed by an exchange of letters without a meeting of the Conciliation Committee,
 - if no agreement is reached during the trilogue, the Conciliation Committee shall meet and organise its work in accordance with the circumstances, with a view to completing the decision-making process as much as possible before the 21-day deadline laid down in Article 314(5) TFEU. The Conciliation Committee may conclude by an exchange of letters.

Part G. *Reste à liquider (RAL)*

36. Given the need to ensure an orderly progression of the total appropriations for payments in relation to the appropriations for commitments so as to avoid any abnormal shift of RAL from one year to another, the European Parliament, the Council and the Commission agree to monitor closely the level of the RAL so as to mitigate the risk of hampering the implementation of Union programmes because of a lack of payment appropriations at the end of the MFF.

In order to ensure a manageable level and profile for the payments in all headings, de-commitment rules shall be applied strictly in all headings, in particular the rules for automatic de-commitments.

In the course of the budgetary procedure, the institutions shall meet regularly with a view to jointly assessing the state of play and the outlook for budgetary implementation in the current and future years. This shall take the form of dedicated interinstitutional meetings at the appropriate level, before which the Commission shall provide the detailed state of play, broken down by fund and Member State, on payment implementation, reimbursement claims received and revised forecasts. In particular, in order to ensure that the Union can fulfill all its financial obligations stemming from existing and future commitments in the period 2014-2020 in accordance with Article 323 TFEU, the European Parliament and the Council shall analyse and discuss the Commission's estimates as to the required level of payment appropriations.

Annex 4

Council Decision of 7 June 2007 on the system of own resources

II

(Acts adopted under the EC Treaty/Euratom Treaty whose publication is not obligatory)

DECISIONS

COUNCIL

COUNCIL DECISION

of 7 June 2007

on the system of the European Communities' own resources

(2007/436/EC, Euratom)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 269 thereof,

Having regard to the Treaty establishing the European Atomic Energy Community, and in particular Article 173 thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the European Parliament ⁽¹⁾,

Having regard to the opinion of the Court of Auditors ⁽²⁾,

Having regard to the opinion of the European Economic and Social Committee ⁽³⁾,

Whereas:

- (1) The European Council meeting in Brussels on 15 and 16 December 2005 concluded, *inter alia*, that the own resources arrangements should be guided by the overall objective of equity. Those arrangements should therefore ensure, in line with the relevant conclusions of the 1984 Fontainebleau European Council, that no Member State sustains a budgetary burden which is excessive in relation to its relative prosperity. It is therefore appropriate to introduce provisions covering specific Member States.

- (2) The Communities' own resources system must ensure adequate resources for the orderly development of the Communities' policies, subject to the need for strict budgetary discipline.

- (3) For the purposes of this Decision, gross national income (GNI) should be defined as annual GNI at market prices as provided by the Commission in application of the European system of national and regional accounts in the Community (hereinafter referred to as the ESA 95) in accordance with Council Regulation (EC) No 2223/96 ⁽⁴⁾.

- (4) In view of the changeover from ESA 79 to ESA 95 for budgetary and own resources purposes, and in order to maintain unchanged the amount of financial resources put at the disposal of the Communities the Commission recalculated, in accordance with Article 3(1) and 3(2) of Council Decision 2000/597/EC, Euratom of 29 September 2000 on the system of the European Communities' own resources ⁽⁵⁾, the ceiling of own resources and the ceiling for appropriations for commitments, expressed to two decimal places, on the basis of the formula in that Article. The Commission communicated the new ceilings to the Council and the European Parliament on 28 December 2001. The ceiling of own resources was set at 1,24 % of the total GNIs of the Member States at market prices and a ceiling of 1,31 % of the total GNIs of the Member States was set for appropriations for commitments. The European Council of 15 and 16 December 2005 concluded that these ceilings should be maintained at their current levels.

⁽¹⁾ Opinion delivered on 4 July 2006 (not yet published in the Official Journal).

⁽²⁾ OJ C 203, 25.8.2006, p. 50.

⁽³⁾ OJ C 309, 16.12.2006, p. 103.

⁽⁴⁾ OJ L 310, 30.11.1996, p. 1. Regulation as last amended by Regulation (EC) No 1267/2003 of the European Parliament and of the Council (OJ L 180, 18.7.2003, p. 1).

⁽⁵⁾ OJ L 253, 7.10.2000, p. 42.

- (5) In order to maintain unchanged the amount of financial resources put at the disposal of the Communities, it is appropriate to adapt those ceilings expressed in per cent of GNI in case of modifications to the ESA 95 which entail a significant change in the level of GNI.
- (6) Following the implementation in European Union law of the agreements concluded during the Uruguay round of multilateral trade negotiations there is no longer any material difference between agricultural duties and customs duties. It is therefore appropriate to remove this distinction from the field of the general budget of the European Union.
- (7) In the interests of transparency and simplicity, the European Council of 15 and 16 December 2005 concluded that the uniform rate of call of the Value Added Tax (VAT) resource shall be fixed at 0,30 %.
- (8) The European Council of 15 and 16 December 2005 concluded that Austria, Germany, the Netherlands and Sweden shall benefit from reduced VAT rates of call during the period 2007-2013 and that the Netherlands and Sweden shall benefit from gross reductions in their annual GNI-based contributions during the same period.
- (9) The European Council of 15 and 16 December 2005 concluded that the correction mechanism in favour of the United Kingdom shall remain, along with the reduced financing of the correction benefiting Germany, Austria, Sweden and the Netherlands. However, after a phasing-in period between 2009 and 2011, the United Kingdom shall participate fully in the financing of the costs of enlargement, except for agricultural direct payments and market-related expenditure, and that part of rural development expenditure originating from the European Agricultural Guidance and Guarantee Fund (EAGGF), Guarantee Section. The calculation of the correction in favour of the United Kingdom shall therefore be adjusted by progressively excluding expenditure allocated to Member States which have acceded to the EU after 30 April 2004, except for the agricultural and rural development expenditure mentioned above. The additional contribution of the United Kingdom resulting from the reduction in allocated expenditure shall not exceed EU-10,5 billion in 2004 prices during the period 2007-2013. In the event of further enlargement before 2013, except for the accession of Bulgaria and Romania, the amount will be adjusted accordingly.
- (10) The European Council of 15 and 16 December 2005 concluded that point (f) of the second paragraph of Article 4 of Decision 2000/597/EC, Euratom regarding the exclusion of the annual pre-accession expenditure in acceding countries from the calculation of the correction in favour of the United Kingdom shall cease to apply at the end of 2013.
- (11) The European Council of 15 and 16 December 2005 invited the Commission to undertake a full, wide-ranging review covering all aspects of EU spending, including the Common Agricultural Policy (CAP), and of resources, including the United Kingdom rebate, and to report in 2008/2009.
- (12) Provisions should be laid down to cover the changeover from the system laid down by Decision 2000/597/EC, Euratom to that introduced by this Decision.
- (13) The European Council of 15 and 16 December 2005 concluded that this Decision shall take effect on 1 January 2007,

HAS LAID DOWN THESE PROVISIONS, WHICH IT RECOMMENDS TO THE MEMBER STATES FOR ADOPTION:

Article 1

The Communities shall be allocated own resources in accordance with the rules laid down in the following Articles in order to ensure, in accordance with Article 269 of the Treaty establishing the European Community (hereinafter referred to as the EC Treaty) and Article 173 of the Treaty establishing the European Atomic Energy Community (hereinafter referred to as the Euratom Treaty), the financing of the general budget of the European Union.

The general budget of the European Union shall, without prejudice to other revenue, be financed wholly from the Communities' own resources.

Article 2

1. Revenue from the following shall constitute own resources entered in the general budget of the European Union:

- (a) levies, premiums, additional or compensatory amounts, additional amounts or factors, Common Customs Tariff duties and other duties established or to be established by the institutions of the Communities in respect of trade with non-member countries, customs duties on products under the expired Treaty establishing the European Coal and Steel Community as well as contributions and other duties provided for within the framework of the common organisation of the markets in sugar;

(b) without prejudice to the second subparagraph of paragraph 4, the application of a uniform rate valid for all Member States to the harmonised VAT assessment bases determined according to Community rules. The assessment base to be taken into account for this purpose shall not exceed 50 % of GNI for each Member State, as defined in paragraph 7;

(c) without prejudice to the second subparagraph of paragraph 5, the application of a uniform rate — to be determined pursuant to the budgetary procedure in the light of the total of all other revenue — to the sum of all the Member States' GNIs.

2. Revenue deriving from any new charges introduced within the framework of a common policy, in accordance with the EC Treaty or the Euratom Treaty, provided that the procedure laid down in Article 269 of the EC Treaty or in Article 173 of the Euratom Treaty has been followed, shall also constitute own resources entered in the general budget of the European Union.

3. Member States shall retain, by way of collection costs, 25 % of the amounts referred to in paragraph 1(a).

4. The uniform rate referred to in paragraph 1(b) shall be fixed at 0,30 %.

For the period 2007-2013 only, the rate of call of the VAT resource for Austria shall be fixed at 0,225 %, for Germany at 0,15 % and for the Netherlands and Sweden at 0,10 %.

5. The uniform rate referred to in paragraph 1(c) shall apply to the GNI of each Member State.

For the period 2007-2013 only, the Netherlands shall benefit from a gross reduction in its annual GNI contribution of EUR 605 million and Sweden from a gross reduction in its annual GNI contribution of EUR 150 million, measured in 2004 prices. These amounts shall be adjusted to current prices by applying the most recent GDP deflator for the EU expressed in euro, as provided by the Commission, which is available when the preliminary draft budget is drawn up. These gross reductions shall be granted after the calculation of the correction in favour of the United Kingdom and its financing referred to in Articles 4 and 5 of this Decision and shall have no impact thereupon.

6. If, at the beginning of the financial year, the budget has not been adopted, the existing VAT and GNI rates of call shall remain applicable until the entry into force of the new rates.

7. For the purposes of this Decision, GNI shall mean GNI for the year at market prices as provided by the Commission in application of the ESA 95 in accordance with Regulation (EC) No 2223/96.

Should modifications to the ESA 95 result in significant changes in the GNI as provided by the Commission, the Council, acting unanimously on a proposal of the Commission and after consulting the European Parliament, shall decide whether these modifications shall apply for the purposes of this Decision.

Article 3

1. The total amount of own resources allocated to the Communities to cover annual appropriations for payments shall not exceed 1,24 % of the sum of all the Member States' GNIs.

2. The total annual amount of appropriations for commitments entered in the general budget of the European Union shall not exceed 1,31 % of the sum of all the Member States' GNIs.

An orderly ratio between appropriations for commitments and appropriations for payments shall be maintained to guarantee their compatibility and to enable the ceiling pursuant to paragraph 1 to be respected in subsequent years.

3. Should modifications to the ESA 95 result in significant changes in the GNI that apply for the purposes of this Decision, the ceilings for payments and commitments as determined in paragraphs 1 and 2 shall be recalculated by the Commission on the basis of the following formula:

$$1,24 \% (1,31 \%) \times \frac{\text{GNI}_{t-2} + \text{GNI}_{t-1} + \text{GNI}_t \text{ ESA current}}{\text{GNI}_{t-2} + \text{GNI}_{t-1} + \text{GNI}_t \text{ ESA modified}}$$

where t is the latest full year for which data according to Council Regulation (EC, Euratom) No 1287/2003 of 15 July 2003 on the harmonisation of gross national income at market prices (GNI Regulation) ⁽¹⁾ is available.

Article 4

1. The United Kingdom shall be granted a correction in respect of budgetary imbalances.

This correction shall be established by:

(a) calculating the difference, in the preceding financial year, between:

— the percentage share of the United Kingdom in the sum of uncapped VAT assessment bases, and

⁽¹⁾ OJ L 181, 19.7.2003, p. 1.

- the percentage share of the United Kingdom in total allocated expenditure;
- (b) multiplying the difference thus obtained by total allocated expenditure;
- (c) multiplying the result under (b) by 0,66;
- (d) subtracting from the result under (c) the effects arising for the United Kingdom from the changeover to capped VAT and the payments referred to in Article 2(1)(c), namely the difference between:
- what the United Kingdom would have had to pay for the amounts financed by the resources referred to in Article 2(1)(b) and (c), if the uniform rate had been applied to non-capped VAT bases, and
- the payments of the United Kingdom pursuant to Article 2(1)(b) and (c);
- (e) subtracting from the result under (d) the net gains of the United Kingdom resulting from the increase in the percentage of resources referred to in Article 2(1)(a) retained by Member States to cover collection and related costs;
- (f) calculating, at the time of each enlargement of the EU, an adjustment to the result under (e) so as to reduce the compensation, thereby ensuring that expenditure which is unabated before enlargement remains so after enlargement. This adjustment shall be made by reducing total allocated expenditure by an amount equivalent to the annual pre-accession expenditure in the acceding countries. All amounts so calculated shall be carried forward to subsequent years and shall be adjusted annually by applying the latest available GDP deflator for the EU expressed in euro, as provided by the Commission. This point shall cease to apply as from the correction to be budgeted for the first time in 2014;
- (g) adjusting the calculation, by reducing total allocated expenditure by total allocated expenditure in Member States that have acceded to the EU after 30 April 2004, except for agricultural direct payments and market-related expenditure as well as that part of rural development expenditure originating from the EAGGF, Guarantee Section.

This reduction shall be phased in progressively according to the schedule below:

United Kingdom correction to be budgeted for the first time in the year	Percentage of enlargement-related expenditure (as defined above) to be excluded from the calculation of the correction in favour of the United Kingdom
2009	20
2010	70
2011	100

2. During the period 2007-2013 the additional contribution of the United Kingdom resulting from the reduction of allocated expenditure referred to in paragraph (1)(g) shall not exceed EU-10,5 billion, measured in 2004 prices. Each year, the Commission services shall verify whether the cumulated adjustment of the correction exceeds this amount. For the purpose of this calculation, amounts in current prices shall be converted into 2004 prices by applying the latest available GDP deflator for the EU expressed in euro, as provided by the Commission. If the ceiling of EU-10,5 billion is exceeded, the United Kingdom's contribution shall be reduced accordingly.

In the event of further enlargement before 2013, the ceiling of EU-10,5 billion shall be adjusted upwards accordingly.

Article 5

1. The cost of the correction shall be borne by the other Member States in accordance with the following arrangements:

- (a) the distribution of the cost shall first be calculated by reference to each Member State's share of the payments referred to in Article 2(1)(c), the United Kingdom being excluded and without taking account of the gross reductions in the GNI-based contributions of the Netherlands and Sweden referred to in Article 2(5);
- (b) it shall then be adjusted in such a way as to restrict the financing share of Austria, Germany, the Netherlands and Sweden to one fourth of their normal share resulting from this calculation.

2. The correction shall be granted to the United Kingdom by a reduction in its payments resulting from the application of Article 2(1)(c). The costs borne by the other Member States shall be added to their payments resulting from the application for each Member State of Article 2(1)(c).

3. The Commission shall perform the calculations required for the application of Article 2(5), Article 4 and this Article.

4. If, at the beginning of the financial year, the budget has not been adopted, the correction granted to the United Kingdom and the costs borne by the other Member States as entered in the last budget finally adopted shall remain applicable.

Article 6

The revenue referred to in Article 2 shall be used without distinction to finance all expenditure entered in the general budget of the European Union.

Article 7

Any surplus of the Communities' revenue over total actual expenditure during a financial year shall be carried over to the following financial year.

Article 8

1. The Communities' own resources referred to in Article 2(1)(a) shall be collected by the Member States in accordance with the national provisions imposed by law, regulation or administrative action, which shall, where appropriate, be adapted to meet the requirements of Community rules.

The Commission shall examine at regular intervals the national provisions communicated to it by the Member States, transmit to the Member States the adjustments it deems necessary in order to ensure that they comply with Community rules and report to the budgetary authority.

Member States shall make the resources provided for in Article 2(1)(a), (b) and (c) available to the Commission.

2. The Council shall, in accordance with the procedures laid down in Article 279(2) of the EC Treaty and Article 183 of the Euratom Treaty, adopt the provisions necessary to apply this Decision and to make possible the inspection of the collection, the making available to the Commission and payment of the revenue referred to in Articles 2 and 5.

Article 9

In the framework of the full, wide-ranging review covering all aspects of EU spending, including the CAP, and of resources, including the United Kingdom rebate, on which it shall report in 2008/2009, the Commission shall undertake a general review of the own resources system.

Article 10

1. Subject to paragraph 2, Decision 2000/597/EC, Euratom shall be repealed as of 1 January 2007. Any references to the Council Decision of 21 April 1970 on the replacement of financial contributions from Member States by the Communities' own resources⁽¹⁾, to Council Decision 85/257/EEC, Euratom of 7 May 1985 on the Communities' system of own resources⁽²⁾, to Council Decision 88/376/EEC, Euratom of 24 June 1988 on the system of the Communities' own resources⁽³⁾, to Council Decision 94/728/EC, Euratom of 31

October 1994 on the system of the European Communities' own resources⁽⁴⁾ or to Decision 2000/597/EC, Euratom shall be construed as references to this Decision.

2. Articles 2, 4 and 5 of Decisions 88/376/EEC, Euratom, 94/728/EC, Euratom and 2000/597/EC, Euratom shall continue to apply to the calculation and adjustment of revenue accruing from the application of a uniform rate valid for all Member States to the VAT base determined in a uniform manner and limited between 50 % and 55 % of the GNP or GNI of each Member State, depending on the relevant year, and to the calculation of the correction of budgetary imbalances granted to the United Kingdom for the years 1988 to 2006.

3. Member States shall continue to retain, by way of collection costs, 10 % of the amounts referred to in Article 2(1)(a) which should have been made available by the Member States before 28 February 2001 in accordance with the applicable Community rules.

Article 11

Member States shall be notified of this Decision by the Secretary-General of the Council.

Member States shall notify the Secretary-General of the Council without delay of the completion of the procedures for the adoption of this Decision in accordance with their respective constitutional requirements.

This Decision shall enter into force on the first day of the month following receipt of the last of the notifications referred to in the second subparagraph.

It shall take effect on 1 January 2007.

Article 12

This Decision shall be published in the *Official Journal of the European Union*.

Done at Luxembourg, 7 June 2007.

For the Council
The President
M. GLOS

⁽¹⁾ OJ L 94, 28.4.1970, p. 19.
⁽²⁾ OJ L 128, 14.5.1985, p. 15.
⁽³⁾ OJ L 185, 15.7.1988, p. 24.

⁽⁴⁾ OJ L 293, 12.11.1994, p. 9.

Annex 5

Council Decision of 26 May 2014 on the system of own resources

DECISIONS

COUNCIL DECISION

of 26 May 2014

on the system of own resources of the European Union

(2014/335/EU, Euratom)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the third paragraph of Article 311 thereof,

Having regard to the Treaty establishing the European Atomic Energy Community, and in particular Article 106a thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national Parliaments,

Having regard to the opinion of the European Parliament,

Acting in accordance with a special legislative procedure,

Whereas:

- (1) The own resources system of the Union must ensure adequate resources for the orderly development of the policies of the Union, subject to the need for strict budgetary discipline. The development of the own resources system can and should also contribute to wider budgetary consolidation efforts undertaken in Member States and participate, to the greatest extent possible, in the development of the policies of the Union.
- (2) This Decision should enter into force only once it has been approved by all Member States in accordance with their respective constitutional requirements, thus fully respecting national sovereignty.
- (3) The European Council of 7 and 8 February 2013 concluded, inter alia, that the own resources arrangements should be guided by the overall objectives of simplicity, transparency and equity. Those arrangements should therefore ensure, in line with the relevant conclusions of the 1984 Fontainebleau European Council, that no Member State sustain a budgetary burden which is excessive in relation to its relative prosperity. It is therefore appropriate to introduce provisions covering specific Member States.
- (4) The European Council of 7 and 8 February 2013 concluded that Germany, the Netherlands and Sweden are to benefit from reduced call rates for the own resource based on value added tax (VAT) for the period 2014-2020 only. It also concluded that Denmark, the Netherlands and Sweden are to benefit from gross reductions in their annual contributions based on gross national income (GNI) for the period 2014-2020 only and that Austria is to benefit from gross reductions in its annual GNI-based contributions for the period 2014-2016 only. The European Council of 7 and 8 February 2013 concluded that the existing correction mechanism in favour of the United Kingdom is to continue to apply.
- (5) The European Council of 7 and 8 February 2013 concluded that the system for collection of traditional own resources is to remain unchanged. However, from 1 January 2014, Member States are to retain, by way of collection costs, 20 % of the amounts collected by them.

- (6) In order to ensure strict budgetary discipline, and taking into account the Commission Communication of 16 April 2010 on the adaptation of the ceiling of own resources and of the ceiling for appropriations for commitments following the decision to apply FISIM for own resources purposes, the ceiling of own resources should be equal to 1,23 % of the sum of the Member States' GNI at market prices for appropriations for payments and the ceiling of 1,29 % of the sum of the Member States' GNI should be set for appropriations for commitments. Those ceilings are based on ESA 95 including financial intermediation services indirectly measured (FISIM) as the data based on the revised European System of Accounts set up by Regulation (EU) No 549/2013 of the European Parliament and of the Council ⁽¹⁾ ('ESA 2010') has not been available at the time of the adoption of this Decision. In order to maintain unchanged the amount of financial resources put at the disposal of the Union, it is appropriate to adapt these ceilings expressed in percentages of GNI. Those ceilings should be adapted as soon as all Member States have transmitted their data on the basis of ESA 2010. In the event that there are any amendments to ESA 2010 which entail a significant change in the level of GNI, the ceilings for own resources and for commitment appropriations should be adapted again.
- (7) The European Council of 7 and 8 February 2013 called upon the Council to continue working on the proposal of the Commission for a new own resource based on VAT to make it as simple and transparent as possible, to strengthen the link with EU VAT policy and actual VAT receipts, and to ensure equal treatment of taxpayers in all Member States. The European Council concluded that the new VAT own resource could replace the existing own resource based on VAT. The European Council also noted that on 22 January 2013 the Council adopted the Council Decision authorising enhanced cooperation in the area of financial transaction tax ⁽²⁾. It invited the participating Member States to examine if it could become the base for a new own resource for the EU budget. It concluded that this would not impact non-participating Member States and would not impact the calculation of the United Kingdom correction.
- (8) The European Council of 7 and 8 February 2013 concluded that a Council regulation laying down implementing measures for the Union's own resources system will be established, as set out under the fourth paragraph of Article 311 of the Treaty on the Functioning of the European Union (TFEU). Accordingly, provisions of a general nature, applicable to all types of own resources and for which appropriate parliamentary oversight, as set out in the Treaties, is required, should be included in that regulation, such as, in particular, the procedure for calculating and budgeting the annual budgetary balance and aspects of control and supervision of revenues.
- (9) For reasons of coherence, continuity and legal certainty, provisions should be laid down to cover the transition from the system introduced by Council Decision 2007/436/EC, Euratom ⁽³⁾ to that arising from this Decision.
- (10) Decision 2007/436/EC, Euratom should be repealed.
- (11) For the purposes of this Decision, all monetary amounts should be expressed in euros.
- (12) The European Court of Auditors and the European Economic and Social Committee were consulted and have adopted opinions ⁽⁴⁾.
- (13) In order to ensure transition to the revised system of own resources and to coincide with the financial year, this Decision should apply from 1 January 2014,

HAS ADOPTED THIS DECISION:

Article 1

Subject matter

This Decision lays down rules on the allocation of own resources of the Union in order to ensure, pursuant to Article 311 of the Treaty on the Functioning of the European Union (TFEU), the financing of the Union's annual budget.

⁽¹⁾ Regulation (EU) No 549/2013 of the European Parliament and of the Council of 21 May 2013 on the European system of national and regional accounts in the European Union (OJ L 174, 26.6.2013, p. 1).

⁽²⁾ OJ L 22, 25.1.2013, p. 11.

⁽³⁾ Council Decision 2007/436/EC, Euratom of 7 June 2007 on the system of the European Communities' own resources (OJ L 163, 23.6.2007, p. 17).

⁽⁴⁾ Opinion No 2/2012 of the European Court of Auditors of 20 March 2012 (OJ C 112, 18.4.2012, p. 1) and Opinion of the European Economic and Social Committee of 29 March 2012 (OJ C 181, 21.6.2012, p. 45).

Article 2

Categories of own resources and specific methods for their calculation

1. Revenue from the following shall constitute own resources entered in the budget of the Union:
 - (a) traditional own resources consisting of levies, premiums, additional or compensatory amounts, additional amounts or factors, Common Customs Tariff duties and other duties established or to be established by the institutions of the Union in respect of trade with third countries, customs duties on products under the expired Treaty establishing the European Coal and Steel Community, as well as contributions and other duties provided for within the framework of the common organisation of the markets in sugar;
 - (b) without prejudice to the second subparagraph of paragraph 4, the application of a uniform rate valid for all Member States to the harmonised VAT assessment bases determined in accordance with Union rules. For each Member State the assessment base to be taken into account for this purpose shall not exceed 50 % of gross national income (GNI), as defined in paragraph 7;
 - (c) without prejudice to the second subparagraph of paragraph 5, the application of a uniform rate, to be determined pursuant to the budgetary procedure in the light of the total of all other revenue, to the sum of GNI of all the Member States.
2. Revenue deriving from any new charges introduced within the framework of a common policy, in accordance with the TFEU, provided that the procedure laid down in Article 311 TFEU has been followed, shall also constitute own resources entered in the budget of the Union.
3. Member States shall retain, by way of collection costs, 20 % of the amounts referred to in point (a) of paragraph 1.
4. The uniform rate referred to in paragraph 1(b) shall be fixed at 0,30 %.

For the period 2014-2020 only, the rate of call of the VAT-based own resource for Germany, the Netherlands and Sweden shall be fixed at 0,15 %.

5. The uniform rate referred to in paragraph 1(c) shall apply to the GNI of each Member State.

For the period 2014-2020 only, Denmark, the Netherlands and Sweden shall benefit from gross reductions in their annual GNI-based contribution of EUR 130 million, EUR 695 million and EUR 185 million respectively. Austria shall benefit from a gross reduction in its annual GNI-based contribution of EUR 30 million in 2014, EUR 20 million in 2015 and EUR 10 million in 2016. All these amounts shall be measured in 2011 prices and adjusted to current prices by applying the most recent GDP deflator for the EU expressed in euro, as provided by the Commission, which is available when the draft budget is drawn up. These gross reductions shall be granted after the calculation of the correction in favour of the United Kingdom and its financing referred to in Articles 4 and 5 of this Decision and shall have no impact thereon. These gross reductions shall be financed by all Member States.

6. If, at the beginning of the financial year, the budget has not been adopted, the existing VAT and GNI rates of call shall remain applicable until the entry into force of the new rates.
7. GNI referred to in paragraph 1(c) shall mean an annual GNI at market price, as provided by the Commission in application of Regulation (EU) No 549/2013 ('ESA 2010').

Should amendments to ESA 2010 result in significant changes in the GNI referred to in paragraph 1(c), the Council, acting unanimously on a proposal of the Commission and after consulting the European Parliament, shall decide whether these amendments are to apply for the purposes of this Decision.

Article 3

Own resources ceiling

1. The total amount of own resources allocated to the Union to cover annual appropriations for payments shall not exceed 1,23 % of the sum of all the Member States' GNIs.

2. The total annual amount of appropriations for commitments entered in the Union's budget shall not exceed 1,29 % of the sum of all the Member States' GNIs.

An orderly ratio between appropriations for commitments and appropriations for payments shall be maintained to guarantee their compatibility and to enable the ceiling pursuant to paragraph 1 to be respected in subsequent years.

3. For the purposes of this Decision, as soon as all Member States have transmitted their data on the basis of ESA 2010, the Commission shall recalculate the ceilings set out in paragraphs 1 and 2 on the basis of the following formula:

$$1,23\% (1,29\%) \times \frac{\text{GNIt} - 2 + \text{GNIt} - 1 + \text{GNIt ESA 95}}{\text{GNIt} - 2 + \text{GNIt} - 1 + \text{GNIt ESA 2010}}$$

In that formula, 't' is the latest full year for which the data for the calculation of GNI are available.

4. Where amendments to ESA 2010 result in significant changes in the level of GNI, the Commission shall recalculate the ceilings set out in paragraphs 1 and 2, as recalculated in accordance with paragraph 3, on the basis of the following formula:

$$x\% (y\%) \times \frac{\text{GNIt} - 2 + \text{GNIt} - 1 + \text{GNIt ESA current}}{\text{GNIt} - 2 + \text{GNIt} - 1 + \text{GNIt ESA amended}}$$

In that formula, 't' is the latest full year for which the data for the calculation of GNI are available.

In that formula, 'x' and 'y' respectively are the ceilings as recalculated according to paragraph 3.

Article 4

Correction mechanism in favour of the United Kingdom

The United Kingdom shall be granted a correction in respect of budgetary imbalances.

This correction shall be established by:

- (a) calculating the difference, in the preceding financial year, between:
 - the percentage share of the United Kingdom in the sum of uncapped VAT assessment bases, and
 - the percentage share of the United Kingdom in total allocated expenditure;
- (b) multiplying the difference thus obtained by total allocated expenditure;
- (c) multiplying the result under point (b) by 0,66;
- (d) subtracting from the result under point (c) the effects arising for the United Kingdom from the transition to capped VAT and the payments referred to in Article 2(1)(c), namely the difference between:
 - what the United Kingdom would have had to pay for the amounts financed by the resources referred to in Article 2(1)(b) and (c), if the uniform rate had been applied to non-capped VAT bases, and
 - the payments of the United Kingdom pursuant to Article 2(1)(b) and (c);
- (e) subtracting from the result under point (d) the net gains of the United Kingdom resulting from the increase in the percentage of resources referred to in Article 2(1)(a) retained by Member States to cover collection and related costs;
- (f) adjusting the calculation, by reducing total allocated expenditure by total allocated expenditure in Member States that have acceded to the Union after 30 April 2004, except for agricultural direct payments and market-related expenditure as well as that part of rural development expenditure originating from the EAGGF, Guarantee Section.

*Article 5***Financing the correction mechanism in favour of the United Kingdom**

1. The cost of the correction set out in Article 4 shall be borne by the Member States other than the United Kingdom in accordance with the following arrangements:
 - (a) the distribution of the cost shall first be calculated by reference to each Member State's share of the payments referred to in Article 2(1)(c), the United Kingdom being excluded and without taking account of the gross reductions in the GNI-based contributions of Denmark, the Netherlands, Austria and Sweden referred to in Article 2(5);
 - (b) it shall then be adjusted in such a way as to restrict the financing share of Germany, the Netherlands, Austria and Sweden to one fourth of their normal share resulting from this calculation.
2. The correction shall be granted to the United Kingdom by a reduction in its payments resulting from the application of Article 2(1)(c). The costs borne by the other Member States shall be added to their payments resulting from the application for each Member State of Article 2(1)(c).
3. The Commission shall perform the calculations required for the application of Article 2(5), Article 4 and this Article.
4. If, at the beginning of the financial year, the budget has not been adopted, the correction granted to the United Kingdom and the costs borne by the other Member States as entered in the last budget finally adopted shall remain applicable.

*Article 6***Universality principle**

The revenue referred to in Article 2 shall be used without distinction to finance all expenditure entered in the Union's annual budget.

*Article 7***Surplus carry-over**

Any surplus of the Union's revenue over total actual expenditure during a financial year shall be carried over to the following financial year.

*Article 8***Collecting own resources and making them available to the Commission**

1. The Union's own resources referred to in Article 2(1)(a) shall be collected by the Member States in accordance with the national provisions imposed by law, regulation or administrative action, which shall, where appropriate, be adapted to meet the requirements of Union rules.

The Commission shall examine the relevant national provisions communicated to it by Member States, transmit to Member States the adjustments it deems necessary in order to ensure that they comply with Union rules and report, if necessary, to the budgetary authority.

2. Member States shall make the resources provided for in Article 2(1)(a), (b) and (c) available to the Commission, in accordance with regulations adopted under Article 322(2) TFEU.

*Article 9***Implementing measures**

The Council shall, in accordance with the procedure set out in the fourth paragraph of Article 311 TFEU, lay down implementing measures as regards the following elements of the own resources system:

- (a) the procedure for calculating and budgeting the annual budgetary balance as set out in Article 7;
- (b) the provisions and arrangements necessary for controlling and supervising the revenue referred to in Article 2, including any relevant reporting requirements.

*Article 10***Final and transitional provisions**

1. Subject to paragraph 2, Decision 2007/436/EC, Euratom is repealed. Any references to the Council Decision 70/243/ECSC, EEC, Euratom ⁽¹⁾, to Council Decision 85/257/EEC, Euratom ⁽²⁾, to Council Decision 88/376/EEC, Euratom ⁽³⁾, to Council Decision 94/728/EC, Euratom ⁽⁴⁾, to Council Decision 2000/597/EC, Euratom ⁽⁵⁾ or to Decision 2007/436/EC, Euratom shall be construed as references to this Decision and shall be read in accordance with the correlation table set out in the Annex to this Decision.

2. Articles 2, 4 and 5 of Decisions 94/728/EC, Euratom, 2000/597/EC, Euratom and 2007/436/EC, Euratom shall continue to apply to the calculation and adjustment of revenue accruing from the application of a rate of call to the VAT base determined in a uniform manner and limited between 50 % and 55 % of the GNP or GNI of each Member State, depending on the relevant year, and to the calculation of the correction of budgetary imbalances granted to the United Kingdom for the years 1995 to 2013.

3. Member States shall continue to retain, by way of collection costs, 10 % of the amounts referred to in Article 2(1) (a) which should have been made available by the Member States before 28 February 2001 in accordance with the applicable Union rules.

Member States shall continue to retain, by way of collection costs, 25 % of the amounts referred to in Article 2(1)(a) which should have been made available by the Member States between 1 March 2001 and 28 February 2014 in accordance with the applicable Union rules.

4. For the purposes of this Decision, all monetary amounts shall be expressed in euros.

*Article 11***Entry into force**

Member States shall be notified of this Decision by the Secretary-General of the Council.

Member States shall notify the Secretary-General of the Council without delay of the completion of the procedures for the adoption of this Decision in accordance with their respective constitutional requirements.

This Decision shall enter into force on the first day of the month following receipt of the last of the notifications referred to in the second paragraph.

It shall apply from 1 January 2014.

⁽¹⁾ Council Decision 70/243/ECSC, EEC, Euratom of 21 April 1970 on the replacement of financial contributions from Member States by the Communities' own resources (OJ L 94, 28.4.1970, p. 19).

⁽²⁾ Council Decision 85/257/EEC, Euratom of 7 May 1985 on the Communities' system of own resources (OJ L 128, 14.5.1985, p. 15).

⁽³⁾ Council Decision 88/376/EEC, Euratom of 24 June 1988 on the system of the Communities' own resources (OJ L 185, 15.7.1988, p. 24).

⁽⁴⁾ Council Decision 94/728/EC, Euratom of 31 October 1994 on the system of the Communities' own resources (OJ L 293, 12.11.1994, p. 9).

⁽⁵⁾ Council Decision 2000/597/EC, Euratom of 29 September 2000 on the system of the Communities' own resources (OJ L 253, 7.10.2000, p. 42).

Article 12

Publication

This Decision shall be published in the *Official Journal of the European Union*.

Done at Brussels, 26 May 2014.

For the Council
The President
Ch. VASILAKOS

ANNEX

CORRELATION TABLE

Decision 2007/436/EC, Euratom	This Decision
Article 1	Article 1
Article 2	Article 2
Article 3(1)	Article 3(1)
Article 3(2)	Article 3(2)
—	Article 3(3)
Article 3(3)	Article 3(4)
Article 4(1), first subparagraph	Article 4, first paragraph
Article 4(1), second subparagraph, point (a) to (e)	Article 4, second paragraph, point (a) to (e)
Article 4(1), second subparagraph, point (f)	—
Article 4(1), second subparagraph, point (g)	Article 4, second paragraph, point (f)
Article 4(2)	—
Article 5	Article 5
Article 6	Article 6
Article 7	Article 7
Article 8(1), first and second subparagraph	Article 8(1)
Article 8(1), third subparagraph	Article 8(2)
Article 8(2)	—
—	Article 9
Article 9	—
Article 10	—
—	Article 10
Article 11	—
—	Article 11
Article 12	Article 12

Glossary

Term	Definition
ABAC	This is the name given to the Commission's accounting system, which since 2005 has been based on accrual accounting rules. The Commission produces accrual-based accounts which recognise revenue when earned, rather than when collected. Expenses are recognised when incurred rather than when paid. This contrasts with cash basis accounting that recognises transactions and other events only when cash is received or paid.
Accounting	The act of recording and reporting financial transactions, including the origination of the transaction, its recognition, processing and summarisation in the financial statements.
Agencies	EU bodies having a distinct legal personality, and to whom budget implementing powers may be delegated under strict conditions. They are subject to a distinct discharge from the discharge authority.
Annuality	The budgetary principle according to which expenditure and revenue is programmed and authorised for 1 year, starting on 1 January and ending on 31 December.
Appropriations	Budget funding. The budget forecasts both commitments (legal pledges to provide finance, provided that certain conditions are fulfilled) and payments (cash or bank transfers to the beneficiaries). Appropriations for commitments and payments often differ — differentiated appropriations — because multiannual programmes and projects are usually committed in the year they are decided and are paid over the years as the implementation of the programme and project progresses. Thus, if the EU budget increases, due for example to enlargement, commitments will increase before payments do. Not all projects and programmes are concluded, and appropriations for payments are therefore lower than for commitments. Non-differentiated appropriations apply for administrative expenditure, for agricultural market support and direct payments.
Budget	Annual financial plan, drawn up according to budgetary principles, that provides forecasts and authorises, for each financial year, an estimate of future costs and revenue and expenditures and their detailed description and justification, the latter included in budgetary remarks. Amending budget: an instrument adopted during the budget year to amend aspects of the adopted budget of that year.
Budgetary authority	Institutions with decisional powers on budgetary matters: the European Parliament and the Council of Ministers.
Cancellation of appropriations	Appropriations cancelled may no longer be used in a given budget year.

Capping (of the VAT resource)	The maximum VAT base to be taken into account in calculating the rate of call is set at 50 % of each Member State's GNI ('capping of the VAT resource'). For the period 2007–13 the rate of call of the VAT resource is set at 0.225 % for Austria, 0.15 % for Germany and 0.10 % for the Netherlands and Sweden. According to Council Decision 2007/436 of 7 June 2007 on the system of the European Communities' own resources (ORD 2007), the uniform rate of call of the VAT own resource is fixed at 0.30 % from 1 January 2007.
Carryover of appropriations	An exception to the principle of annuality insofar as appropriations that could not be used in a given budget year may, under very strict conditions, be exceptionally carried over for use during the following year.
Ceiling	Limits of expenditure or revenue fixed by law or by agreement, such as in the own-resources decision or in the multiannual financial framework. The latter defines an annual ceiling for each expenditure heading in commitment appropriations and an annual global ceiling for payment appropriations.
Common Customs Tariff	The external tariff applied to products imported into the Union.
Earmarked revenue	Revenue earmarked for a specific purpose, such as income from foundations, subsidies, gifts and bequests, including the earmarked revenue specific to each institution (Article 21 of the Financial Regulation).
Ecofin	The Economic and Financial Affairs Council is, together with the Agriculture Council and the General Affairs Council, one of the oldest configurations of the Council. It is commonly known as the Ecofin Council, or simply Ecofin and is composed of the economics and finance ministers of the Member States, as well as budget ministers when budgetary issues are discussed. It meets once a month.
ECU	European Currency Unit, a currency medium and unit of account created to act as the reserve asset and accounting unit of the European Monetary System, replaced by the euro. The value of the ECU was calculated as a weighted average of a basket of specified amounts of European Union (EU) currencies.
EU-6, EU-9, EU-12, EU-15, EU-25, EU-27, EU-28	EU-28 means the EU as constituted in 2013: Belgium (BE), Bulgaria (BG), Czech Republic (CZ), Denmark (DK), Germany (DE), Estonia (EE), Ireland (IE), Greece (EL), Spain (ES), France (FR), Croatia (HR), Italy (IT), Cyprus (CY), Latvia (LV), Lithuania (LT), Luxembourg (LU), Hungary (HU), Malta (MT), Netherlands (NL), Austria (AT), Poland (PL), Portugal (PT), Romania (RO), Slovenia (SI), Slovakia (SK), Finland (FI), Sweden (SE), United Kingdom (UK) EU-27 means the EU as constituted in 2007: BE, BG, CZ, DK, DE, EE, IE, EL, ES, FR, IT, CY, LV, LT, LU, HU, MT, NL, AT, PL, PT, RO, SI, SK, FI, SE, UK.

	<p>EU-25 means the EU as constituted in 2004: BE, CZ, DK, DE, EE, IE, EL, ES, FR, IT, CY, LV, LT, LU, HU, MT, NL, AT, PL, PT, SI, SK, FI, SE, UK.</p> <p>EU-15 means the EU as constituted in 1995: BE, DK, DE, IE, EL, ES, FR, IT, LU, NL, AT, PT, FI, SE, UK.</p> <p>EU-12 means the EU as constituted in 1986: BE, DK, DE, IE, EL, ES, FR, IT, LU, NL, PT, UK.</p> <p>EU-10 means the EU as constituted in 1981: BE, DK, DE, IE, EL, FR, IT, LU, NL, UK.</p> <p>EU-9 means the EU as constituted in 1973: BE, DK, DE, IE, FR, IT, LU, NL, UK.</p> <p>EU-6 means the EU as constituted in 1957: BE, DE, FR, IT, LU, NL.</p>
Evaluations	Tools to provide a reliable and objective assessment of how efficient and effective interventions have been or are expected to be (in the case of <i>ex ante</i> evaluation). Commission services assess to what extent they have reached their policy objectives, and how they could improve their performance in the future.
Exchange difference	The difference resulting from the exchange rates applied to the transactions concerning countries outside the euro area.
Expenditure allocated	EU expenditure that it is possible to allocate to individual Member States. Non-allocated expenditure concerns notably expenditure paid to beneficiaries in third countries. Allocation of expenditure by country is necessary in order to calculate budgetary balances.
Financial regulation	Adopted through the ordinary legislative procedure after consulting the European Court of Auditors, this regulation lays down the rules for the establishment and implementation of the general budget of the European Union.
Grants	Direct financial contributions, by way of donation, from the budget in order to finance either an action intended to help achieve an objective part of an EU policy or the functioning of a body which pursues an aim of general European interest or has an objective forming part of an EU policy.
Gross domestic product (GDP) at market prices	Final result of the production activity of resident producer units. It corresponds to the economy's total output of goods and services, less intermediate consumption, plus taxes and less subsidies on products.
Gross national income (GNI)	At market prices GNI represents total primary income receivable by resident institutional units: compensation of employees, taxes on production and imports less subsidies, property income (receivable less payable), operating surplus and mixed income.

	<p>Gross national income equals gross domestic product (GDP) (see above) minus primary income payable by resident units to non-resident units plus primary income receivable by resident units from the rest of the world.</p> <p>GNI has widely replaced gross national product (GNP) as an indicator of income. In the area of the EU budget this change took effect as from the year 2002. In order to maintain unchanged the cash value of the ceiling of EU revenue, referred to as the 'own-resources ceiling', the ceiling had to be recalculated in percentage terms. It is now established at 1.23 % of GNI instead of the previous 1.27 % of EU GNP.</p>
Headings	In the multiannual financial framework or financial perspective headings are groups of EU activities in broad categories of expenditure.
Impact assessment	A tool to analyse the potential benefits and costs of different policy options to tackle a particular problem.
Interinstitutional agreement	(IIA) on budgetary discipline and sound financial management: the IIA is adopted by common agreement of the European Parliament, the Council and the Commission and contains the table of the financial framework, as well as the rules to implement it. As Treaty rules concerning the EU budget haven't been modified since 1975 until the Lisbon Treaty entered into force on 1 December 2009, the IIA has allowed for the necessary changes and improvements of the cooperation between institutions on budgetary matters (OJ C 139 of 14.6.2006). The introduction of the multiannual financial framework into the Treaty via the Lisbon Treaty, and its link to the annual budgetary procedure, led among others to proposals for an adaptation of the Interinstitutional Agreement. Corresponding proposals were made by the Commission on 29 June 2011.
Legal base	The legal base or basis is, as a general rule, a law based on an article in the Treaty giving competence to the Community for a specific policy area and setting out the conditions for fulfilling that competence including budget implementation. Certain Treaty articles authorise the Commission to undertake certain actions, which imply spending, without there being a further legal act.
Macroeconomic equilibrium	The situation where there is no tendency for change. The economy can be in equilibrium at any level of economic activity.
Macrofinancial assistance	Form of financial support to neighbouring regions, which is mobilised on a case-by-case basis with a view to helping the beneficiary countries in dealing with serious but generally short-term balance-of-payments or budget difficulties. It takes the form of medium-/long-term loans or grants (or an appropriate combination thereof) and generally complements financing provided in the context of an International Monetary Fund's reform programme.

Operating balances	The difference between what a country receives from and pays into the EU budget. There are many possible methods of calculating budgetary balances. In its Financial report, the Commission uses a method based on the same principles as the calculation of the correction of budgetary imbalances granted to the United Kingdom (the UK correction). It is, however, important to point out that constructing estimates of budgetary balances is merely an accounting exercise of the purely financial costs and benefits that each Member State derives from the Union and it gives no indication of many of the other benefits gained from EU policies such as those relating to the internal market and economic integration, not to mention political stability and security.
Outtum	Any of the three possible outcomes of the budget resulting from the difference between revenue and expenditure: a positive difference (surplus), a negative difference (deficit) and no difference (i.e. zero, or perfect balance between revenue and expenditure).
Own resources	The revenue flowing automatically to the European Union budget, pursuant to the Treaties and implementing legislation, without the need for any subsequent decision by national authorities.
Reprogramming	In this financial report the term 'reprogramming' has the following meaning: when the state of implementation in the expenditure areas of Structural Funds, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Fund for Fisheries suggests the need for reprogramming, the European Parliament and the Council will take decisions on Commission proposals concerning the transfer of part of unused allocations during the first year of the multiannual financial framework onto the following years (see point 48 of the IIA).
Revenue	The term used to describe the income, from all sources, that finances the budget. Almost all revenue going into the EU budget is in the form of own resources, of three kinds: traditional own resources — duties that are charged on imports of products originating from a non-EU State; the resource based on value added tax (VAT); and the resource based on GNI. The budget also receives other revenue, such as income from third countries for participating in EU programmes, the unused balance from the previous year, taxes paid by EU staff, competition fines, interest on late payments and so on.
Rules of application	These lay down detailed rules for the implementation of the financial regulation. They are set out in a Commission regulation adopted after consulting all institutions and cannot alter the financial regulation upon which they depend.
Surplus	Positive difference between revenue and expenditure (see outturn) which has to be returned to the Member States.

UA	Unit of account, also known as European Unit of Account (EUA), a book-keeping device for recording the relative value of payments into and from EC accounts, replaced by the European currency unit (ECU) which has been replaced by the euro.
UK correction	At the Fontainebleau European Council in France on 25 and 26 June 1984, the then 10 Member States (Germany, Belgium, Denmark, France, Greece, Ireland, Italy, Luxembourg, the Netherlands and the UK) agreed on the rebate to be granted to the UK to reduce its contribution to the EU budget.
VAT (value added tax)	An indirect tax, expressed as a percentage applied to the selling price of most goods and services. At each stage of the commercial chain, the seller charges VAT on sales but owes the administration this amount of tax minus the VAT paid on purchases made in the course of business. This process continues until the final consumer, who pays VAT on the whole value of what is purchased. VAT is broadly harmonised in the European Union but Member States may fix their own rates of tax, within parameters set at EU level, and also enjoy a limited option to tax or not to tax certain goods and services.

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