

CIRCLE II

Working Document 12

"Discussion circle" on the budgetary procedure

Subject : Answers from Lord Tomlinson to the questions put to the Discussion Circle on the incorporation of the financial perspective in the Constitution (WD02) and on the budgetary procedures (WD04), including proposed Part I and Part II Treaty articles.

Members of the "Discussion circle" on the budgetary procedure will find hereafter a paper from Lord Tomlinson, alternate Member of the Convention.

Answers from Lord Tomlinson to the questions put to the Discussion Circle on the incorporation of the financial perspective in the Constitution (WD02) and on the budgetary procedures (WD04), including proposed Part I and Part II Treaty articles.

Incorporating the financial perspective in the Constitution (WD02)

General

A Treaty-based and legally binding financial perspective, determined (as now) predominantly by the European Council, would be a valuable improvement in its own right, in terms of budget discipline, transparency and the legitimacy of EU spending.

In addition, this could provide one element of the budget discipline safeguards which would be required as a quid pro quo for the abolition of the procedural differences between compulsory and non-compulsory expenditure. Other safeguards also needed include provision for a tie-break mechanism, respecting the institutional balance between the arms of the budgetary authority, which will ensure the timely adoption of an annual budget offering good value for money within the financial perspective ceilings.

The Council's and Member States' role in relation to revenues and the Own Resources ceiling is quite separate and must be maintained independently of any change to the current financial perspective or annual budget arrangements.

Part One of the Constitution

The European Council's predominant role in establishing the financial perspectives is a matter of constitutional importance and should be reflected in Part I of the Treaty. Part I should also make clear that the Union's annual budget must comply with the financial perspective. Other elements of procedure and substance relating to the financial perspective could be reflected in Part II.

Part II of the Constitution

The procedure for adopting the financial perspective could be by unanimity in the Council, at the level of Heads of State or Government, on a Commission recommendation, and consulting the European Parliament.

On other aspects:

1. The Part II articles should stipulate that the financial perspective should indicate binding ceilings for commitments, under broad headings, and a total annual binding ceiling for payments.
2. In order to maintain budget discipline and transparency while providing the necessary level of flexibility, the Part II articles should stipulate that the financial perspective should include one or more reserves in order to meet unforeseen expenditure.
3. The duration of the financial perspective could be set by the European Council, although this should normally be not less than 5 years.
4. A tie break is needed in the event of no agreement in the Council on a new financial perspective. This should provide for the previous financial perspective to remain in force until a replacement is agreed.
5. Provision for other measures needed for the smooth operation of the budgetary procedure should be included in the Part II articles dealing with the Financial Regulation, rather than those dealing with the financial perspective.
6. Each institution (the Commission as well as the budgetary authority) should take the necessary steps to ensure that the necessary financial resources are available in order to allow the Union to fulfil its legal obligations to third parties. This provision should be included in the Part II articles dealing with the annual budget procedure.

Legal instrument

It would make sense for the financial perspective to be a Law.

Questionnaire on the budgetary procedure (WD04)

1. The current procedure for adopting the annual budget includes no formal right of initiative or decision making power for the Commission. There is thus a clear separation between the Commission's responsibility (and accountability) for implementing the budget and the budgetary authority's responsibility for adopting the budget and giving discharge to the Commission for budget implementation. It is important for reasons of transparency and sound financial management that this clear distinction is maintained.

2. Abolition of the distinction between compulsory and non-compulsory expenditure could bring benefits (in terms of transparency, and by allowing for greater attention to be paid in the budgetary process to the value for money of EU spending), but could be considered only if there are adequate safeguards for budget discipline and good value for money. Incorporation of the financial perspective into the Treaty would be one critical safeguard - this is also desirable in its own right. A measure stipulating that the budget authority must ensure that the necessary financial resources are available to meet legal obligations to third parties is another important safeguard. Procedures providing for proper attention to be paid to value for money criteria is a third. A tie-break mechanism respecting the institutional balance within the budgetary authority is a fourth.

3 and 4. Negotiation and conciliation arrangements have a useful role in improving the involvement of both arms of the budgetary authority in budgetary decisions, while ensuring that the necessary choices are made to ensure that budget discipline is respected. However there is a danger that negotiation of budgetary inputs, divorced from proper consideration of policy outcomes, leads to irresponsible budgetary posturing – whether to increase or reduce spending – rather than to securing more efficient and effective budget spending.

Enhancing the budgetary authority's role in ensuring that budget allocations are determined on the best available value for money basis would be a real prize in any procedural simplification. In order to develop its current role for granting discharge to the Commission, and in view of the “democratic deficit” which currently results from a poor correlation between EU spending and the citizen's perception of what is good value for

money, the European Parliament should take a leading role here. To achieve that, and subject to the budget discipline safeguards spelt out above, I propose:

- A simplified budgetary procedure with a single reading by each arm of the budgetary authority, starting with the European Parliament, followed by conciliation. This would give the European Parliament in particular the opportunity to focus on the relationship between inputs and outputs, as well as on the level of inputs themselves, in establishing the draft budget. The current requirements of the Financial Regulation in this area would be bolstered by ensuring that the principle of sound financial management – which encompasses the principles of economy, efficiency and effectiveness – are included in the Part I budgetary principles article (article 39).
- A tie-break mechanism for commitments to apply to specific budget items for which there is no agreement in conciliation (as proposed in my paper of 25 March, CONV 634/03). Applying a tie-break at this level of disaggregation would ensure that real and substantial differences are settled on the merits of the budget item itself, rather than by an unprincipled trade-off between levels of spending under different financial perspective headings, irrespective of value for money concerns.
- A requirement on the Commission to produce annual performance reports, alongside annual financial statements and accounts, and for this to be taken into account by the European Parliament and Council as part of the annual discharge process.

Treaty articles

Proposed Part I and Part II Treaty articles are annexed.

Budgetary and financial provisionsPART ONE (changes to Secretariat's draft articles shown in bold type)*Article 38 – the Union's resources*

1. Without prejudice to other revenue, the Union's budget shall be financed wholly from own resources.
2. The Council, acting unanimously on a proposal from the Commission and after consultation of the European Parliament, shall lay down provisions relating to the system of own resources of the Union, which it shall recommend to the Member States for adoption in accordance with their respective constitutional requirements.

Article 39 – the budgetary and financial principles

1. All items of revenue and expenditure shall be included in estimates to be drawn up for each financial year and shall be shown in the budget, in accordance with the provision of Part II of the Constitution.
2. The revenue and expenditure shown in the budget shall be in balance.
3. The expenditure shown in the budget shall be authorized for the annual budgetary period in accordance with the law referred to in Article [I].
4. **As a general rule**, the implementation of expenditure shown the budget shall require the prior adoption of a binding legal act which provides a legal basis for Union action and for the implementation of the expenditure in accordance with the law referred to in Article [I]. This act must take the form of a European law, a European framework law [, a European regulation] or a European decision.
5. With a view to maintaining budget discipline, the Commission shall not make any proposal for a Union act, or alter its proposals, or adopt any implementing **or delegated** measure which is likely to have appreciable implications for the budget without providing the assurance that that proposal or that measure is capable of being financed within the limit of the Union's own **and the ceilings of the financial perspective established in accordance with article 40. The ceilings of the financial perspective shall be binding on all institutions throughout the budget process and on the Commission in the implementation of the budget.**
6. The Union's budget shall be **adopted and** implemented in accordance with the principles of sound financial management, **which encompasses the principles of economy, efficiency and effectiveness**. Member States shall co-operate with the Union to ensure that the appropriations entered in the budget are used in accordance with the principles of sound financial management.

7. The Union and the Member States shall counter fraud and any other illegal activities affecting the financial interest of the Union in accordance with the provisions of Article [J].

Article 39bis – the multiannual financial perspective

The Union's budget shall be established in compliance with the multiannual financial perspective **adopted by the Council, acting at the level of Heads of State and Government, in accordance with arrangements laid down [...]** in Article [C].

Article 40 – the Union's budgetary procedure

The European Parliament and the Council shall, **having regard to a preliminary draft budget drawn up by the Commission [...]**, and in accordance with the arrangements laid down in Article [D], jointly adopt the Union's annual budget.

PART TWO

Article [A] – scope of budget

1. All items of revenue and expenditure of the Union shall be included in the budget, provided that expenditure on the common foreign and security policy, the common defence policy, the policy on police matters and crime, and on the implementation of enhanced co-operation, shall be included only to the extent set out below.
2. Administrative expenditure occasioned for the institutions by the provisions of the Constitution on the common foreign and security policy, the common defence policy, and the policy on police matters shall be charged to the budget.

Operational expenditure to which the implementation of those provisions gives rise shall also be charged to the budget, except for such expenditure arising from operations having military or defence implications and cases where the Council acting unanimously decides otherwise.

In cases where such expenditure is not charged to the budget of the European Communities it shall be charged to the Member States in accordance with the gross national product scale, unless the Council acting unanimously decides otherwise. As for expenditure arising from operations having military or defence implications, Member States whose representatives in the Council have made a formal declaration under [Article 23(1), second subparagraph] shall not be obliged to contribute to the financing thereof.

3. Administrative expenditure occasioned for the institutions from the implementation of the provisions of the Constitution on enhanced co-operation shall be charged to the budget. Other expenditure occasioned by such co-operation shall be borne by the

participating Member States, unless the Council, acting unanimously, decides otherwise.

Article [B] – financial year

The financial year shall run from 1 January to 31 December.

Article [C] – financial perspective

1. The financial perspective shall constitute the reference framework for interinstitutional budgetary discipline. It shall ensure that, in the medium term, the expenditure of the Union, broken down by broad category, develops in an orderly manner and within the limits of own resources to be made available to the Union. The Council, acting unanimously at the level of Head of State or Government, on a recommendation from the Commission and after consulting the European Parliament, shall adopt the financial perspective for a period of not less than 5 years.
2. For each financial year, the financial perspective shall:
 - a) indicate the maximum volume and broad categories of Union expenditure, and maximum amounts of expenditure in terms of appropriations for commitments for each heading or subheading, including expenditure for new policies;
 - b) include one or more reserves in order to meet unforeseen expenditure;
 - c) indicate overall total payment appropriations, which shall remain within the forecast limit of own resources to be made available to the Union.
3. Except where otherwise provided in the financial perspective, for the purposes of sound financial management the institutions will 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.
4. In the event of unforeseen circumstances, the financial perspective may be modified by the Council in accordance with the procedure specified in paragraph 1. If need be, the financial perspective shall be so modified to ensure compliance with the limit on own resources to be made available to the Union.
5. In the absence of any decision on a proposal for a new financial perspective, the figures laid down for the latest year shall also apply to the following year.

Article [D] – budgetary procedure

1. The annual budget shall be adopted jointly by the European Parliament, acting by a majority of its members, and by the Council, acting by qualified majority, under the following procedure.
2. For each financial year, the Commission shall place a preliminary draft budget before the Council and the European Parliament not later than [1 June] of the preceding year. The preliminary draft budget shall contain an estimate of expenditure and an estimate of revenue.
3. The European Parliament, after consulting the Commission and the Council, shall establish a draft budget, which it shall forward to the Council no later than [31 July].
4. The Council shall have the right to amend the draft budget. If [by 30 September] the Council has not made amendments, the draft budget shall stand as finally adopted. If within this period the Council has made amendments, the draft budget together with the amendments shall be forwarded to the European Parliament.
5. If, within 21 days of the amended draft budget being placed before it, the European Parliament approves all the Council's amendments, the budget thus amended shall stand as finally adopted. If the European Parliament does not approve all the amendments, the President of the European Parliament, in agreement with the President of the Council, shall within the same period convene a meeting of the Conciliation Committee.
6. The Conciliation Committee, which shall be composed of Members of the Council or their representatives and an equal number of representatives of the European Parliament, shall have the task of reaching agreement on the budget. If, within 21 days of its being convened, the Conciliation Committee reaches agreement on the whole budget, the budget thus agreed shall stand as finally adopted.
7. If, within 21 days of its being convened, the Conciliation Committee fails to reach agreement, the budget lines on which there is no agreement shall be determined at the lower of the level then proposed by either the Council or the European Parliament, or at the level included in the previous year's budget, if higher, and the budget thus agreed or determined shall stand as finally adopted.
8. When the procedure provided for in this Article has been completed, the President of the European Parliament shall declare that the budget has been finally adopted.
9. Each institution shall exercise the powers conferred upon it by this Article with due regard for the provisions of the Treaty and for acts adopted in accordance therewith. It shall ensure that the necessary appropriations are available in order to allow the Union to fulfil its legal obligations to third parties.

Article [E] – implementation

1. The Commission shall implement the budget, in accordance with the Law adopted

pursuant to Article [I], on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management. Member States shall co-operate with the Commission to ensure that the appropriations are used in accordance with the principles of sound financial management.

2. The Law shall lay down detailed rules for each institution concerning its part in effecting its own expenditure.

Article [F] – financial statements and performance reports

1. The Union's institutions and bodies shall draw up annual financial accounts and a related performance report on the results and effectiveness of the operations and policies which are charged from their respective parts of the Budget.
2. The Commission shall compile and submit annually to the Council and to the European Parliament the consolidated accounts of the preceding financial year giving a true and fair view of the execution of the Budget, of the revenue, expenditure, assets and liabilities of the Union, and a related consolidated performance report on the results and effectiveness of the Union's operations, policies, and use of financial and other Union resources.

Article [G] – discharge

1. The European Parliament, acting on a recommendation from the Council which shall act by a qualified majority, 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 consolidated accounts and performance report referred to in Article [F], 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 [248(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, the results and effectiveness of the Union's operations and policies, and the related use of Union resources, including 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 implementation of the budget, 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 documents 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.

Article [H] – unit of account

I. The budget shall be drawn up in euros.

II.

Article [II] – Financial Law

1. The Council, acting unanimously on a proposal from the Commission and after consulting the European Parliament and obtaining the opinion of the Court of Auditors, shall adopt a Law

- a) specifying in particular the detailed procedures to be adopted in connection with the Financial Perspective, for establishing and implementing the budget, and for presenting and auditing accounts and performance reports¹
- b) laying down rules concerning the responsibility of authorising officers, the accounting officer and the internal auditor.

From 1 January 2007, the Council shall act by a qualified majority on a proposal from the Commission and after consulting the European Parliament and obtaining the opinion of the Court of Auditors.

2. The Council, acting unanimously on a proposal from the Commission and after consulting the European Parliament and obtaining the opinion of 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 [J] - Fraud

- 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.
- 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 this Constitution, the Member States shall co-ordinate 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

¹ Regulations will amount to a revised Financial Regulation consolidating the current provisions, amended in light of new budgetary procedures, provisions for revising the FP within limits and subject to conditions set by the European Council at the time of its adoption, procedure for making technical adjustments to the FP, procedure for drawing on reserves, procedure for incorporation and status of financial provisions in legislative acts, status of expenditure for which the Treaty or legislation give third parties a legal claim against the Budget, and detailed requirements for annual consolidated EU Accounts and Performance Reports.

co-operation between the competent authorities.

4. The Council, acting in accordance with the legislative procedure, after consulting the Court of Auditors, shall adopt the necessary measures in the field 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. These measures shall not concern the application of national criminal law or the national administration of justice.
5. The Commission, in co-operation with the Member States, shall each year submit to the European Parliament and to the Council a report on the measures taken for the implementation of the Article.