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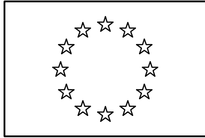

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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

on the functioning of the Interinstitutional Agreement on budgetary discipline and sound financial management

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1. INTRODUCTION

The Interinstitutional Agreement on budgetary discipline and sound financial management (IIA) is a political agreement between the European Parliament, the Council and the Commission. It contains many provisions and principles that have proven to be helpful and even necessary to ensure budgetary discipline and smooth budgetary procedures. The IIA affects numerous aspects of the planning, preparation, execution and control of the budget.

The current IIA was adopted on 17 May 2006[1] on the basis of the agreement reached at the Brussels European Council on 15-16 December 2005 and subsequent changes later agreed with the European Parliament. It represents the most recent milestone in a long history — more than 50 years — of budgetary debates between the European institutions. Since 1988, four successive IIAs have been concluded: the *Delors I* (1988-1992) and *Delors II* (1993-1999) packages, *Agenda 2000* (2000-2006) and the current 2007-2013 package. Together, they have ensured that the EU budget has been adopted smoothly and on time over the last 20 years.

This report presents a thorough examination of the functioning of the current IIA in line with Declaration 1 to the IIA, which states that in relation to Point 7 of the Interinstitutional Agreement, the Commission will prepare a report on the functioning of the Interinstitutional Agreement 'accompanied, if necessary, by relevant proposals'.

The analysis below follows broadly the structure of the IIA. It focuses first on the procedures implementing the Multiannual Financial Framework (MFF), in particular the adjustments and revisions, and on flexibility (margins and instruments of flexibility). It then assesses provisions related to the institutional collaboration during the budgetary procedure. Finally, issues related to the sound financial management of EU funds (Statements of Assurance, financial programming and the new financial instruments) are examined.

The report does not claim to be exhaustive. A number of important issues related to interinstitutional collaboration are not examined here. And many important aspects of the budget reform are left to the 'full, wide-ranging review' of the EU budget pursuant to Declaration 3 to the IIA.

Equally, the Treaty of Lisbon introduces or gives new emphasis to many policy areas that may in the longer term require corresponding budgetary changes. But this will first

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[1] Interinstitutional Agreement (IIA) of 17 May 2006 between the European Parliament, the Council and the Commission on budgetary discipline and sound financial management (OJ C 139, 14.6.2006).

require the preparation of new legal acts and a careful assessment of their potential financial impact.

Finally, it must be noted that the Commission has tabled proposals for a Regulation laying down the Multiannual Financial Framework pursuant to article 312(2) of the Treaty on the Functioning of the European Union[2]. The Multiannual Financial Framework regulation together with the proposed new Interinstitutional Agreement on cooperation in budgetary matters[3] and some provisions of the Financial Regulation[4] will together replace the IIA.

2. ANALYSIS OF IMPLEMENTATION PROCEDURES RELATED TO THE MFF

The MFF, together with the other provisions in the IIA, has ensured

- budgetary discipline: the annual budgetary procedure must respect the MFF ceilings;
- a smooth budgetary procedure and effective cooperation between institutions thanks to the various rules of procedure agreed upon in the IIA. It is important to stress that since 1988 all budgets have been adopted on time;
- more predictability regarding the evolution of EU expenditure.

Acknowledgement of the usefulness of the MFF is reflected in the insertion of article 312(1) in the Treaty on the Functioning of the European Union stating that ‘the annual budget of the Union shall comply with the multiannual financial framework’.

2.1. Procedures for adjusting the Multiannual Financial Framework

2.1.1. Yearly technical adjustment

Point 16 of the IIA provides for a yearly technical adjustment ahead of the budgetary procedure for year n+1. This involves in particular a revaluation, at year n+1 prices, of the ceilings and of the overall figures for appropriations for commitments and appropriations for payments[5].

For this purpose, a fixed deflator of 2 % a year is used and not the price deflator of GDP as was partially the case for previous MFFs. This offers a clear advantage in terms of transparency as the ceilings are known in real as well as in nominal terms for the entire duration of the financial framework. This in turn facilitates long-term financial planning and gives more certainty to all stakeholders involved in the budgetary procedure.

The advantages of the current system would appear to outweigh the inevitable positive or negative difference between ceilings and overall figures for appropriations obtained using the fixed deflator and figures that would be obtained using the observed price deflator of GDP. In 2007, the ceilings would have been 1.7% higher using the observed price deflator. In 2008, this difference disappeared. In 2009, a divergence appeared as a consequence of the economic recession: the deflator index using the fixed deflator was at

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2 COM(2010) 72.
3 COM(2010) 73.
4 COM(2010) 71.
5 The same provisions maintained in the draft MFF Regulation (Article 4).

110.4 (base year 2004 = 100) while the deflator index using the observed price deflator of GDP was at 106.7.

	2007	2008	2009
(a) Fixed deflator used for technical adjustments	2.0 %	2.0 %	2.0%
(b) Cumulated index using the 2 % deflator (2004=100)	106.1	108.2	110.4
(c) Price deflator of GDP (ECFIN Autumn 2009 forecast)	2.9 %	0.4 %	-1.3%
(d) Cumulated index using effective deflator (2004=100)	107.8	108.2	106.7
(e) Cumulated divergence (d)-(b)	1.7	0.0	-3.7

2.1.2. Adjustment of cohesion policy allocations

Point 17 of the IIA provides for a technical adjustment for the year 2011 if it is established that any Member State's cumulated GDP for the years 2007-2009 has diverged by more than +/- 5 % from the cumulated GDP estimated when drawing up the IIA. In that case, the Commission will adjust the amounts allocated from funds supporting cohesion to the Member States concerned for that period.

The assessment of the GDP divergence and the corresponding adjustment was made by the Commission as part of the technical adjustment for the year 2011 presented in April 2010[6].

2.1.3. Adjustment of the global payment ceiling

Pursuant to Point 18 of the IIA, the Commission checks every year the global ceiling for appropriations for payments, which was established when the financial framework was drawn up, in the light of implementation, to ensure an orderly progression in relation to the appropriations for commitments[7].

During the first years of the programming period, the actual level of payment appropriations has been significantly lower than the ceilings, which could possibly lead to a catch-up phenomenon with higher than foreseen payment levels in years to come. Nevertheless, based on the current assessment regarding levels of payment appropriations until 2013, it is premature to adjust the existing ceiling of payments.

The Commission will continue to monitor carefully the evolution of the situation and keep fine-tuning its estimates of payments for structural operations and for all other headings.

Regarding payment appropriations after 2013, the Commission will update the forecasts in 2010, in accordance with the terms of Point 19 of the IIA in the form of a new "Fiche" 11 as presented on 28 April 2004.

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6 COM(2010) 160.

7 The same provisions maintained in the draft MFF Regulation (Article 6).

2.1.4. *Adjustment for implementation of structural funds, cohesion funds, rural development and the European Fund for Fisheries (EFF)*

Under Point 48 of the IIA, in the event of adoption after 1 January 2007 of new rules or programmes governing the Structural Funds, the Cohesion Fund, Rural Development and the European Fund for Fisheries (EFF), the two arms of the budgetary authority undertake to authorise, on a proposal from the Commission, the transfer to subsequent years, in excess of the corresponding ceilings on expenditure, of allocations not used in 2007.

Appropriations for commitments totalling EUR 2 034 million were not implemented in 2007 and were not carried forward to 2008. This corresponds to the 2007 allocations for 45 Operational Programmes that could not be adopted in 2007, mainly due to delays in their submission to the Commission. The reprogramming for heading 1b and heading 2 was implemented as follows by Decision 2008/371[8] of the European Parliament and of the Council of 29 April 2008:

(in current prices, in EUR million)

	2008	2009	2010	2011	2012	2013
Heading 1b	378	0	0	24	24	0
Heading 2	394	387	387	147	147	147

Better preparation by the Commission meant that this amount was much lower than the EUR 6 152.3 million reprogrammed in 2001[9].

Key messages on the procedures for adjusting the MFF

The procedures for adjusting the MFF appear to function. The advantages of using a fixed deflator (Point 16) outweigh the limited average difference with the observed price deflator of GDP. Adjustment of the global payment ceiling (Point 18) has so far not been necessary, but continued careful monitoring is appropriate. Finally, the adjustment for implementation (Point 48) went smoothly and the amounts concerned were far lower than in 2001.

2.2. Flexibility in the Multiannual Financial Framework

2.2.1. *Analysis of margins*

Heading 1a covers priorities of immediate relevance for the renewed Lisbon agenda for growth and jobs. This heading gathers the largest number of different EU policies and is regularly under pressure due to the evolving context of global challenges.

The financing of the Galileo programme, of the European Institute of Innovation and Technology and of the energy-related projects under the European Economic Recovery Plan have required repeated revisions of the ceilings (see Chapter 2.3.1.). Appropriations for more recent decisions or proposals, such as the continuation of funding for the

[8] OJ L 128, 16.5.2008, p. 8.

[9] See Decision 2001/692/EC of the European Parliament and of the Council of 3 May 2001 adopted pursuant to paragraph 17 of the IIA of 6 May 1999.

decommissioning of the Kozloduy (Bulgaria) nuclear power plant, the setting up of new financial supervisory authorities, the European Microfinance Facility and the launching of the operational phase of the European Earth Observation Programme (GMES) have already been included in the updated financial programming on the basis of the proposal by the Commission. The available margins and possibilities to respond to future eventualities have been reduced accordingly, leaving only an estimated margin of EUR 50.1 million in 2011, EUR 34.6 million for 2012 and EUR 47.8 million for 2013.

New additional needs are expected to come up over the next three years, for instance in relation to ITER.

The estimated additional commitment appropriations for ITER to be provided by the EU budget under the present MFF might be well above one billion euro. The need for payments appropriations remains to be assessed in the light of the schedule currently under discussion, but payments are expected to occur mainly after 2013.

The issue of margins is not as relevant for **heading 1b** as, under Point 13 of the IIA, the institutions are not obliged to maintain any margin under this heading, i.e. this ceiling is a target for expenditure.

The situation of **heading 2** is quite different. At the European Council in Brussels in October 2002 EU leaders agreed the ceilings for CAP first pillar spending at the 2006 level with an annual increase of 1% in current prices from 2007 and up to the year 2013. The subsequent 2003 CAP reform introduced a financial discipline mechanism to ensure that the amounts for the financing of the CAP are not exceeded in any year. In practice this situation has not arisen, and during the budget years 2007 to 2009 the budget execution has left substantial margins under the ceiling of heading 2. These margins have therefore been a source of flexibility: whereby increases in other headings have been offset by decreases in heading 2, allowing the overall MFF to remain unchanged.

However, these margins will diminish over coming years in particular in view of the continued phasing-in of direct aids in new Member States. Currently a margin of EUR 456 million remains in the 2010 budget, which may become available towards the end of the year. Barring very favourable market conditions, it is unlikely that for 2011-2013 budgetary availabilities will be found within the sub-ceiling for the first pillar of the CAP, particularly not up-front in view of the obligation to maintain a margin of at least EUR 300 million to avoid application of the financial discipline mechanism.

Regarding **headings 3**, the evolution of expenditure has been managed within the existing ceilings with no major problems from 2007 to 2009. For sub-heading 3a *Freedom, Security and Justice* that has been possible thanks to the relatively steep expenditure profile of the ceiling, which increases by 2.5 times between 2007 and 2013. On the other hand, the situation is tighter in sub-heading 3b *Citizenship* given the relatively stable ceiling which translates into very tight margins till the end of the period.

Recurring international crises and emergencies regularly confront **heading 4** with insufficient margins and flexibility issues. Problems in this area are particularly acute because of the volatile nature of external events, for example sudden conflicts and natural disasters, such as the recent earthquakes in Haiti, Chile or Turkey. Even though it has so far been possible to accommodate the additional needs through recourse to various flexibility instruments in the course of the annual budget procedure, the protracted negotiations on the food facility, for instance, have clearly shown the limits of the IIA's flexibility mechanisms. Furthermore, the current strict separation of internal and external

expenditure, which was highlighted when the budgetary authority rejected the Commission proposal to make available part of the financing for the so-called *Food Facility* within the margin available under heading 2, appears to limit the Union's capacity to react timely to global challenges.

In the remaining years of the present MFF the margins programmed for heading 4 are very limited. After taking into consideration the financing of banana accompanying measures to ACP countries following a trade agreement in the framework of the WTO trade negotiations, the expected margins amount to EUR 70.3 million for 2011, EUR 132.3 million for 2012 and EUR 134.6 million for 2013.

In the area of climate change, the EU budget is expected to contribute EUR 150 million over 2010-2012 to the fast-start international funding set out as part of the Copenhagen Accord. In addition to EUR 50 million already included in the 2010 budget, EUR 50 million will be expected for each year 2011 and 2012. However a new dimension could be opened if from 2013 funding for an ambitious climate agreement would be provided from the EU budget as proposed by the Commission in September 2009[10].

Over the period 2007-2009, expenditure under **heading 5** evolved in line with expenditure ceilings. As part of the package agreed to finance the European Economic Recovery Plan (see section 2.3.1 below), the expenditure ceiling was reduced by EUR 126.5 million in 2010 (and by EUR 173.5 million in 2009). The situation in heading 5 is becoming much tighter in 2010 and till the end of the period because of two main reasons: the impact of the entry into force of the Lisbon Treaty, and the impact of the annual salary adjustment for staff higher than originally estimated. On the one hand, several institutions have requested additional appropriations in relation to the entry into force of the Lisbon Treaty thus eroding the available margin. Moreover, it cannot be excluded that the creation of the European External Action Service (EEAS) may require additional spending. On the other hand, if the Council's decision to limit the annual salary adjustment for staff to only half the proposed increase was to be reversed by the Court of Justice ruling (following the Commission's appeal), there would be an additional one-off increase in expenditure (with retroactive effect) and an increase in the expenditure base to which future salary adjustments will have to apply. All in all, the ceilings of heading 5 are going to become a much tighter constraint on expenditure than observed till now. Nevertheless, there is still a limited margin as the Commission sticks to its strict policy of no new human resources (except for enlargement) and is facing the new tasks deriving from Lisbon Treaty and other new priorities by redeployement only.

2.2.2. Instruments of flexibility

The IIA contains provisions regarding a number of instruments of flexibility: the Emergency Aid Reserve (EAR), the European Union Solidarity Fund (EUSF), the European Globalisation Adjustment Fund (EGF) and the Flexibility Instrument. The amounts for the EU Solidarity Fund are only entered in the budget when the Fund is mobilised while the amounts corresponding to the Emergency Aid Reserve and the European Globalisation Fund are already entered in the budget from the beginning of the

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[10] Commission Communication to the EP, the Council, the ECOSOC and the CoR - Stepping up international climate finance: A European blueprint for the Copenhagen deal - COM(2009) 475, 10.9.2009.

year, albeit in a reserve. The Flexibility Instrument is of a different nature: it is never entered in the budget as such but it allows expenditure to be budgeted above the ceiling of the corresponding heading of the multiannual financial framework.

There are also slight differences in the procedures for mobilising these instruments:

- The mobilisation of the **Emergency Aid Reserve** requires a transfer and a trilogue procedure, 'if necessary in simplified form'. The commitment appropriations mobilised recently are EUR 49 million in 2007, EUR 479 million in 2008[11] and EUR 188 million in 2009.

- Mobilising the **EU Solidarity Fund** requires a proposal to deploy the instrument, the use of the 'appropriate budgetary instrument', which de facto is an amending budget, and the initiation of a trilogue procedure, 'if necessary in simplified form'. Although the EUSF may be mobilised for up to EUR 1 billion in a given year, the highest mobilisation was in the first year, 2002, and was for EUR 728 million. In all other years the annual mobilisation levels have been between EUR 22 million and EUR 615 million. Similarly, there has never been a problem in respecting the rule that 25 % of the total amount should remain unused by 1 October.

- The **European Globalisation Adjustment Fund** is mobilised through a proposal to deploy the instrument and a transfer. The total amounts mobilised were EUR 18.6 million in 2007, EUR 49 million in 2008 and EUR 54 million in 2009. Use of a transfer for the EGF should mean a speedier process. However, the necessity to accompany this with a mobilisation decision slows the procedure down. It is only when the mobilisation decision is finally adopted that the transfer can actually be made in the accounting system, although it has already been endorsed by the budgetary authority. With the experience gained over the last three years the practical modalities of the procedure have been adjusted[12] but it could be simplified further.

- The mobilisation of the **Flexibility Instrument** is accompanied by a proposal for a decision of the European Parliament and the Council. In practice this may accompany the Commission's [Preliminary] Draft Budget or a Commission proposal for a [Preliminary] Draft Amending Budget or an Amending Letter. The proposal may also be prepared following a political agreement at conciliation to mobilise the Instrument. In accordance with the provisions of the IIA, amounts mobilised are first taken from the oldest open tranche. The key difference between the present text and that included in the IIA of 6 May 1999 is the deletion of the following text 'The flexibility instrument should not, as a rule, be used to cover the same needs two years running'. This stipulation no longer applies, which is a valuable development as experience has shown (e.g. in Kosovo or Palestine) that some crises may require repeated recourse to the Flexibility Instrument. At the same time, there is an inherent contradiction — and inevitable trade-offs — when a financial instrument which has been conceived to respond to short-term crises also has to play a role to solve lasting or recurring crises.

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[11] Taking into account the one-off increase of EUR 240 million decided in the framework of the agreement reached during conciliation on 21 November 2008 for the financing of the Food Facility.

[12] As suggested by the European Parliament, the Commission now submits EGF individual applications to the budgetary authority, rather than in batches.

The common strand for the first three instruments is the trilogue procedure "if necessary in simplified form". What this ‘simplified form’ entails has never been clarified. The pragmatic solution, frequently followed, is that no trilogue takes place, unless a regular budgetary trilogue is on the horizon. The draft Interinstitutional Agreement on cooperation in budgetary matters incorporates the current practice and it stipulates that the trilogue is called only if there is a disagreement between the institutions regarding the mobilisation of the instruments.

The main reason for mobilising the Flexibility Instrument over the period 2000-2009 has been to meet the needs of heading 4, where the margins have proved too tight to deal with unforeseen events. Once the political decision to mobilise is taken, the procedure has advanced quite smoothly. The main issue here is therefore not one of procedures, but one of available means compared to a vast array of needs responding to important European priorities. Even though the IIA foresees that unused amount can be carried over up to n+2, the amount currently available in 2010 is limited to EUR 115 million due to the recurrent use of the Flexibility Instrument.

2.2.3. Possibility to diverge by 5 % from legislative act

Point 37 of the IIA defines the circumstances under which the amounts set out in the [Preliminary] Draft Budget can depart by more than 5 % from the reference amounts laid down in the legislative act, while it leaves to the Commission and to the budgetary authority a certain degree of discretion for deviations within the 5 % limit[13].

This has resulted in the adoption of a set of common rules to be applied to budgeting and programming by the Commission: as a general rule, modifications are systematically offset in following years of the programming period in order to continue respecting the overall financial allocations of the corresponding legislative act.

Exceptions to this general rule can be considered if the Commission finds substantial arguments for diverging from the financial allocation, which will be explained in the financial programming documents transmitted to the budgetary authority. Whereas the general rule of compensation is applied to Commission proposals, it is not applied in cases where the Council or European Parliament amends the [Preliminary] Draft Budget proposal with additional appropriations.

Key messages on flexibility in the MFF

Margins under all ceilings of the MFF are becoming very tight. The margins under heading 2 are expected to shrink significantly in coming years. At the same time remaining margins and possibilities for redeployment within headings 1a, 3b and 4 offer only limited scope at best to respond to future eventualities. Overall, the remaining margin for manoeuvre within *the MFF for years to come is severely limited. The various instruments (Points 25 to 28) which provide flexibility* outside *the MFF have been used with varying degrees of intensity. Furthermore, regarding the Flexibility Instrument, the main issue is one of available means compared to a vast array of needs responding to important European priorities. Besides, the rules framing the possibility for amounts in the [Preliminary] Draft Budget to depart from reference amounts (Point 37) are clear and function well.*

[13] The same provisions maintained in the draft new IIA (Point 15).

2.3. Revisions of the Multiannual Financial Framework

2.3.1. Analysis of the recent revisions of the MFF and amendments to the IIA

Except for the first financial perspectives (1988-1992), only little use was made before 2007 of the possibility to revise the multiannual financial framework (MFF). The 1993-1999 framework was revised only once and the 2000-2006 framework not at all, apart from the adjustments related to enlargements. By contrast, exceptional developments have already triggered two revisions of the 2007-2013 financial framework, as well as one other amendment of the IIA:

- In the first half of 2007, the negotiations with the private partners on the financing of the European Global Navigation Satellite System (GNSS) programmes EGNOS and **GALILEO** failed. In order to secure the implementation of this strategically important project, as well as the financing of the European Institute of Technology (EIT), the budgetary authority decided on 18 December 2007 to revise the financial framework. The increase in the ceilings for heading 1a for the years 2008 to 2013 by a total amount of EUR 1.6 billion in current prices was offset by an equivalent reduction of the ceiling for heading 2 for the year 2007[14.] Additionally, EUR 600 million was made available by re-allocating funds from other programmes and budget lines within heading 1a, and EUR 200 million by mobilising the Flexibility Instrument. In total, an amount of EUR 2.4 billion of EU financing was added to the amount provided for in May 2006 when the financial framework was agreed.

- In order to provide a rapid response to soaring food prices in developing countries a EUR 1 billion **Food Facility** was set up in late 2008. The solution agreed by the three institutions for financing this facility required an amendment of the IIA in order to exceptionally increase the Emergency Aid Reserve (EAR) provided for in Point 25 of the IIA by an amount of EUR 240 million in 2008[15]. This allowed the EAR to make EUR 340 million available to the food facility. The remaining amount was provided by the Flexibility Instrument (EUR 420 million for 2009) and through redeployment from other programmes within heading 4 (EUR 240 million in 2009 and 2010).

- On 2 April 2009 agreement was reached on the financing of a EUR 5 billion package for energy and rural development proposed by the Commission in the framework of its **European Economic Recovery Plan** (EERP) of 26 November 2008. The agreement involved an immediate revision of the financial framework[16], by which the 2009 ceiling for commitment appropriations under heading 1a was increased by an amount of EUR 2.0 billion, fully offset by a decrease of the 2009 ceiling for commitment appropriations under heading 2. Additionally, EUR 600 million was made available within the margin of heading 2 in 2009 for rural development in the form of broadband infrastructure and measures related to the 'new challenges' identified under the Common Agricultural Policy's 'health check'. As a second step, at the November 2009 conciliation meeting additional EUR 1980 million was made available for energy projects under heading 1a. This implied a further revision of the

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14 OJ L 6, 10.1.2008, p. 7.
15 OJ C 326, 20.12.2008, p. 3.
16 OJ L 132, 29.5.2009, p. 8.

financial framework[17] with a raising of the 2010 ceiling for commitment appropriations under heading 1a fully compensated by a decrease of the 2009 and 2010 ceilings of other headings (mainly heading 2). Furthermore, additional EUR 420 million was made available for broadband and 'new challenges' within the 2010 margin of heading 2.

The above-mentioned revisions of the 2007-2013 MFF aimed to increase the ceilings for commitment appropriations under heading 1a. The time needed for an agreement (starting from the initial Commission proposal) tended to increase: three months were needed for the first revision (Galileo and EIT) of the 2007-2013 MFF. Five months were needed for the agreement on the EERP package, excluding the time needed for effectively implementing the budgetary 'compensation mechanism' it provides for.

The Council only accepted the principle of a revision to the extent that the raising of the ceilings under heading 1a could be fully offset by the lowering of the ceilings for another heading so as to leave the 'overall ceiling' (i.e. the total amounts expressed in current prices for commitment appropriations as well as for payment appropriations for all headings and years) of the 2007-2013 MFF unchanged. For financing the EUR 5 billion EERP package, a compensation mechanism potentially stretching over two or even three budgetary procedures was preferred to a one-off revision of the MFF as proposed by the Commission. In practice, this limited the flexibility allowed for by the IIA.

Full offsetting of the increase of the ceilings under heading 1a by the lowering of the ceilings for heading 2 was only possible because of exceptionally large margins left under that particular heading in the years 2007 to 2009. This was due to the combined effect of very favourable market conditions in the agricultural sector, high levels of assigned revenue and the gradual phasing-in of direct aids in the new Member States.

Overall, experience shows that agreement for a revision takes time and that recent revisions have been greatly facilitated by existing margins. However, such a favourable environment for revisions is unlikely to be found in the foreseeable future, thus calling into question the capacity of the Union to react swiftly and effectively to future changes.

2.3.2. *Procedures applicable to revisions*

Point 22 of the IIA, which lays down the voting rules for revision of the MFF, sets the threshold for switching from a qualified majority vote in Council to a unanimous decision at 0.03 % of the EU GNI. This is to be interpreted as relating to each of the years concerned by the revision, e.g. for 2009 the threshold was set at 0.03 % of the EU GNI of 2009 or EUR 3.6 billion[18]. Even though consensual decision-making has generally been sought, the possibility to have a qualified majority vote in Council was crucial in terms of obtaining a timely agreement on the revision.

Point 22 of the IIA further provides that, 'as a general rule', any revision of the MFF must be presented and adopted before the start of the budgetary procedure for the year or the first of the years concerned. The words 'as a general rule' were interpreted as allowing for some flexibility in terms of the timing of the relevant Commission proposal within the budgetary year concerned.

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[17] OJ L 347, 24.12.2009, p. 26.

[18] The GNI to be used for setting the threshold is the one used for the latest technical adjustment of the financial framework and it is the GNI used for the purposes of the Own Resources Decision.

There was, however, no agreement between the institutions on whether the increase of a ceiling for the present or future years can be 'offset' (within the meaning of Point 23, second paragraph, of the IIA) by lowering a ceiling for a year for which the budgetary exercise is closed. As a result, this option was foreclosed[19].

Key messages on revisions of the MFF

In the first three years of the 2007-2013 MFF, the financial framework and the IIA have already been amended on three different occasions to accommodate new initiatives with substantial financing needs: the financing of Galileo and the EIT, the increase of the Emergency Aid Reserve to finance part of the Food Facility, and the European Economic Recovery Plan. The related adjustments to the current Financial Framework and the IIA totalled EUR 8.4 billion. While the institutions agreed on the procedures and instruments to deal with the financial impact of these unforeseen situations (Points 21 to 23), in each instance their use led to prolonged and very difficult political negotiations. Success was ultimately possible because the increases in the ceiling for heading 1a were offset by decreases of the other ceilings, in particular of heading 2, where large margins were available. Recourse to this option will be much more difficult in the second half of the Financial Framework at a time when further adjustments may be necessary.

3. INTERINSTITUTIONAL COLLABORATION

Points 31, 32 and 33 and Annex II of the IIA set out the provisions relating to the improvement of interinstitutional collaboration during the budgetary procedure. These provisions have proved extremely useful as a framework for the annual budget procedure.

3.1. Interinstitutional collaboration and the budget procedure

As the Lisbon Treaty significantly changes the budgetary procedure, the provisions on the interinstitutional cooperation adjusted to the new procedure are included in the Annex of the new Interinstitutional Agreement on cooperation in budgetary matters. This new annex keeps some of the well-established practices of the previous agreement but most of the provisions had to be adjusted. Amongst the provisions that would remain, albeit adjusted in the new framework, appropriate attention should be granted to the following:

– Point 33 refers to the so-called 'letter of executability', in which the Commission comments on the European Parliament's first reading amendments. The IIA specifies that "the two arms of the budgetary authority will take those comments into account in the context of the conciliation procedure." It would be useful to see greater use made of these provisions by the budgetary authority and this would certainly help to improve budgetary implementation. Under the new procedure, the format and the content of the Commission comments will have to be adjusted to take into account both the Council's position and the European Parliaments' amendments.

– Under the provisions of Part D of Annex II, both arms of the budgetary authority will inform the Commission by mid-June of their intentions in regard to pilot

[19] The same provisions are included in the draft MFF Regulation (Article 8).

projects/preparatory actions, with a view to holding a first discussion at the conciliation meeting of the Council's first reading. During the 2009 procedure, important progress was made in this regard, when the European Parliament presented its initial proposals in due time. All parties agreed that this had greatly improved the process, and hopefully such an approach can be built on in the future.

3.2. Classification of expenditure

Since the Council had the final say on compulsory expenditure, and the European Parliament had the final say on non-compulsory expenditure, the potential for disputes had been significant.

However, with the introduction of interinstitutional agreements, and an agreed breakdown between the two categories, this type of dispute had largely disappeared. The Lisbon Treaty takes this a stage further by abolishing the distinction altogether.

3.3. Maximum rate of increase

Article 272(9) of the Treaty, which is repealed by the Lisbon Treaty, required the Commission to declare each year the 'maximum rate of increase' of non-compulsory expenditure in the budget of the following year and to communicate this rate before 1 May to all the institutions of the Community. This maximum rate, which was based on the average growth of GDP, central government expenditure and cost of living in the Member States, was established at 4.6 % for the 2010 budget[20], 5.0 % for the 2009 budget and 4.7 % for the 2008 budget.

Since the European Parliament, the Council and the Commission have agreed to respect the ceilings of the MFF, this maximum rate was *de facto* purely indicative.

3.4. Fisheries agreements and CFSP

The provisions relating to the fisheries agreements are set out in Point 41 and Annex IV of the IIA. The Commission undertakes to keep the European Parliament regularly informed of developments, and each quarter the Commission presents detailed information about the implementation of agreements in force and financial forecasts for the remainder of the year[21].

This process seems to be working well in practice. It is not necessary to modify it.

The provisions relating to the Common Foreign and Security Policy (CFSP) are set out in Points 42 and 43. The good practice of joint meetings between the Council and the European Parliament (AFET and COBU committees), held under Point 43 at least five times a year, has proved to be a useful tool not only for the dialogue on political issues concerning the CFSP, but also for regular updates on budgetary issues[22].

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20 SEC(2009) 583, 30.4.2009.

21 The same provisions are included in the draft new IIA (Point 17).

22 Provisions included both in the draft MFF Regulation (Art. 12) and the draft new IIA (Point 18 and 19).

Key messages on the interinstitutional collaboration provisions

The IIA has been a useful tool to facilitate interinstitutional collaboration. The principles and procedures for cooperation set out in Annex II of the IIA have contributed to smoother negotiation procedures. Based on this positive experience, these principles should obviously be revised to take into consideration the new procedure and competences deriving from the Lisbon Treaty. The arrangement whereby the Commission provides Parliament with quarterly information about the implementation of fisheries agreements in force and financial forecasts for the remainder of the year (Point 41) seems to be working well in practice. Similarly, regular joint meetings between the Council and the European Parliament on the CFSP (Point 43) have proved a useful tool. At the same time, greater use of provisions regarding the so-called 'letter of executability' and comments made by the Commission in the new context of the conciliation procedure (Point 33) would certainly help improve budgetary implementation. Important progress was made during the 2009 procedure on information regarding pilot projects/preparatory actions (Annex II) and hopefully such an approach can be built on in the future.

4. SOUND FINANCIAL MANAGEMENT OF EU FUNDS

4.1. Statements of Assurance

To implement Point 44 of the Interinstitutional Agreement, the Financial Regulation and the Implementing Rules were flanked by provisions to strengthen internal control in the area of shared management whereby the relevant audit authorities in Member States were to produce an assessment of the compliance of management and control systems with Community regulations through an annual summary at the appropriate national level of the available audits and declarations[23].

The Commission issued guidance to Member States on the preparation of the statements of assurance and annual summaries on 2007, and revised these in the light of experience for the 2008 and 2009 rounds to reinforce the value-added elements. While in agriculture the sectoral legislation contains a legal requirement for the provision of annual statements of assurance, this is not the case in cohesion policy. As a result the Commission can currently only recommend that Member States supplement their summaries in this field with a declaration of assurance: seven Member States provided such statements in their annual summaries due on 15 February 2009. For these summaries, all Member States respected the obligation and eventually submitted summaries which complied with the minimum requirements. For the first time annual summaries were also received in the area of justice, freedom and security.

The responsible departments provide an assessment of the quality of annual summaries and of their contribution to assurance in their annual activity reports. The Commission will continue to work with Member States to maximise the added value of annual summaries and to obtain an increased assurance on their management and control systems.

[23] Articles 53b(3) of the Financial Regulation and 42a of the Implementing Rules.

In its annual report on the year 2008, the Court of Auditors observed that some Member States had submitted elements or analyses which added value to the annual summaries, by seeking to identify and comment on systemic deficiencies or cross-cutting issues. Noting the encouragement in successive Discharge Resolutions, the Commission intends, in its proposal for the triennial revision of the Financial Regulation, to reinforce the provisions on annual summaries to add value in terms of assurance, notably through the incorporation of declarations of assurance and audit opinions.

Parallel to the work on annual summaries, the Commission supports the voluntary initiatives taken by some Member States to provide national management declarations covering EU funds.

4.2. Financial programming

In accordance with Point 46 of the IIA, the Commission submits the financial programming to the budgetary authority twice a year — once in May/June as part of the [Preliminary] Draft Budget, and once in December/January after the adoption of the budget.[24] The financial programming sent each January is a technical update to the results of the budgetary procedure and to the evolution of various legislative procedures.

In presenting the financial programming, the provisions of Point 37 of the IIA are taken into consideration (see above).

The financial programming provides an orientation for future years, remains indicative in nature and, as such, does not prejudge any decision the Commission or the budgetary authority might take in future annual budgetary procedures.

In line with requests from the two arms of the budgetary authority, the format of the financial programming document has been revised in 2009 to highlight more clearly the changes since the last financial programming.

Point 46 of the IIA also states that "on the basis of the data supplied by the Commission, stocktaking should be carried out at each trilogue". In practice this is not the case, unless one of the institutions specifically requests that the item be added to a trilogue agenda. This flexible approach is valuable and this provision shall not be reproduced in the new IIA.

4.3. Agencies and European Schools

Point 47 of the IIA regarding agencies foresees a procedure for the two arms of the budgetary authority to arrive at a timely agreement on the financing of a new agency, as proposed by the Commission. The three Institutions have clarified the practical application of point 47 in a joint declaration in November 2009, by applying three procedural steps to arrive at agreement. Accordingly, the Commission has proposed to include the text of the joint declaration in the Interinstitutional Agreement on cooperation in budgetary matters[25].

4.4. New financial instruments

In accordance with Point 49, when presenting the [Preliminary] Draft Budget, the Commission is requested to report to the budgetary authority on the activities financed by

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[24] The same provisions are included in the draft new IIA (Point 20).

[25] Point 21 of the draft new IIA.

the EIB, EIF and EBRD to support investment in research and development, TENs, and SMEs. There are no particular problems to address here, and no need for change[26].

Key messages on the sound financial management provisions

A positive overall assessment can be made of provisions in the IIA regarding the sound financial management of EU funds. The new format of the financial programming (Point 46) appears to be a valuable tool for supporting political decisions. Reports by the Commission to the budgetary authority on the activities financed by the EIB, EIF and EBRD to support investment in research and development, TENs, and SMEs (Point 49) have been running smoothly. The reinforcement of the annual summaries will be proposed in the triennial revision of the Financial Regulation. In the meantime efforts must be made to add value to the annual summaries and to support those Member States choosing to produce voluntary national declarations. Lastly, a more systematic procedure for the implementation of Point 47 regarding agencies has been agreed.

5. CONCLUSIONS

The Interinstitutional Agreement has proved invaluable in facilitating budgetary discipline and ensuring a smooth budgetary procedure. Overall, the track record of this instrument and, in particular, of the Multiannual Financial Framework (MFF) can be regarded as quite positive.

At the same time, this report has highlighted that adjustments to the current MFF and the IIA totalling a gross amount of EUR 8.4 billion have already been required in the first half of this MFF, and that the remaining margin for manoeuvre is now severely limited. This raises questions as to whether the Union will be adequately equipped for new challenges and rapidly evolving circumstances in the second half of this MFF. Concerns along these lines have already been expressed by the European Parliament in its Report on the Mid-Term Review of the 2007-2013 Financial Framework[27]. Furthermore, the Europe 2020 strategy makes it clear that more can and must be done to deliver smart, sustainable and inclusive growth and to create new jobs.

Under **heading 1A**, a number of issues are emerging, for which the exact additional financial needs still have to be determined (for example on ITER). Given the extremely limited margin, the potential amounts at stake decisively exceed amounts anticipated to remain unspent/uncommited under the current ceiling of heading 1A and there is no budgetary room for new initiatives.

Regarding **heading 4**, the current foreseeable margins are very limited and may not be sufficient to deal with future demands. In particular, the consequences of recurring international crises and the potentially important impact of the 2013 climate change financing needs to be considered carefully.

Depending on the size of additional requirements in headings 1A and 4 and the nature (one-off vs. permanent) of additional needs, a number of options could be envisaged:

– Redeployment within the heading concerned for limited amounts;

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[26] The same provisions included in the draft new IIA (Point 22).

[27] P6_TA(2009)0174, 25.3.2009.

- Mobilisation of the Flexibility instrument could play a role;
- Revision of the ceiling of the heading concerned may need to be necessary if the amounts required are substantial and permanent, which could be the case for either ITER or climate change financing in 2013. Such a revision could either take the form of a compensation mechanism offsetting the increase in one heading by the decrease in another or, if necessary, a net increase of the overall ceiling of the 2007-2013 MFF.

Other financing possibilities outside the scope of the IIA such as EIB loans or intergovernmental financing could be examined as well.

In view of the very limited margins, it is clear that more flexibility will be needed to cope with the potential budgetary impact of new developments. On the basis of the above-mentioned options, the Commission will make proposals as soon as the budgetary impact of the pending issues mentioned in this report has been sufficiently clarified.