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# THE COUNCIL AND THE EUROPEAN COMMISSION ON BUDGETARY DISCIPLINE AND IMPROVEMENT OF THE BUDGETARY PROCEDURE FOR 2007-2013

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## ESSENCE AND SCOPE OF THE IIA

The IIA on budgetary discipline and improvement of the budgetary procedure (COM (2006) 36 final) is a document, reached as a result of the negotiations between the European Parliament, the Council and the European Commission (the Commission). The aim of the IIA is to provide a set of agreed rules concerning the multi-annual FF (Financial Framework) and the sequence of operations in the annual budgetary procedure.

The IIA is a tool to frame the annual budgetary practice within an agreed multi-annual FF. Its renewal updates and simplifies the existing agreements and joint declarations on budgetary matters. The agreement aims at finding the balance between budgetary discipline and efficient resource allocation.

The purposes of the IIA concluded between the European Parliament, the Council and the Commission (the institutions) are:

- to implement budgetary discipline and to improve the functioning of the annual budgetary procedure; and
- to initiate co-operation between the institutions on budgetary matters.

Budgetary discipline covers all expenditure. It is binding on all institutions involved in its implementation for as long as the IIA is in force. The IIA does not alter the budgetary powers of the various institutions, as laid down in the Treaties—the Council will act by a qualified majority and the European Parliament by a majority of its members and three fifths of the votes cast.<sup>1</sup>

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<sup>1</sup> In compliance with the voting rules laid down in the fifth subparagraph of Article 272(9) of the Treaty establishing the European Community (the 'EC Treaty').

**Box 1 Structure and contents of the IIA**

IIA on budgetary discipline and improvement of the budgetary procedure

**PART I—FF 2007-2013: DEFINITION AND IMPLEMENTING PROVISIONS**

- A. Contents and scope of the FF
- B. Annual adjustments of the FF
- C. Review of the FF
- D. Revision of the FF
- E. Consequences of the absence of a joint decision on the adjustment or revision of the FF
- F. Emergency Aid Reserve
- G. EU Solidarity Fund
- H. Instrument of Flexibility
- I. European Globalisation Adjustment Fund
- J. Adjustment of the FF to cater for enlargement
- K. Duration of the FF and consequences of the absence of a FF

**PART II—IMPROVEMENT OF INTERINSTITUTIONAL COLLABORATION DURING THE BUDGETARY PROCEDURE**

- A. The inter-institutional collaboration procedure
- B. Establishment of the budget
- C. Classification of expenditure
- D. Maximum rate of increase of non-compulsory expenditure in the absence of a FF
- E. Incorporation of financial provisions in legislative acts
- F. Expenditure relating to fisheries agreements
- G. Financing of the common foreign and security policy (CFSP)

ANNEX I : FF 2007-2013

ANNEX II: INTERINSTITUTIONAL COLLABORATION IN THE BUDGETARY SECTOR

ANNEX III: CLASSIFICATION OF EXPENDITURE

ANNEX IV: FINANCING OF EXPENDITURE DERIVING FROM FISHERIES AGREEMENTS

DECLARATION on the adjustment of Structural Funds, Rural Development and the European Fund for Fisheries in the light of the circumstances of their implementation

Any amendment of the IIA requires the consent of the institutions which are party to it. Changes to the multi-annual FF must be made in accordance with the procedures in the IIA. The IIA has two parts and four annexes (Box 1):

- Part I contains a definition and implementing provisions for the multi-annual FF<sup>2</sup> 2007 to 2013 and applies for the duration of that FF,
- Part II relates to the improvement of inter-institutional collaboration during the budgetary procedure.

The IIA enters into force on 1. January 2007. It replaces with effect from the same date:

- the IIA 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)<sup>3</sup>,
- the IIA of 7 November 2002 between the European Parliament, the Council and the Commission on the financing of the EU Solidarity Fund.

The 2007 to 2013 FF (set out in Annex I) is an integral part of the IIA. It is the reference framework for inter-institutional budgetary discipline. The FF ensures that, in the medium term, EU expenditure, broken down by broad categories, develops in the limits of own resources.

Simultaneously with a proposal for a new FF<sup>4</sup>, the Commission will present a report on the application of the IIA, accompanied where necessary by amendments.

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<sup>2</sup> The multi-annual financial framework is also referred to as 'the financial framework (FF)' in the agreement.

<sup>3</sup> OJ C 172, 18.6.1999, p. 1. This IIA replaces and declares obsolete the following instruments:

- the 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);
- the IIA of 29 October 1993 between the European Parliament, the Council and the Commission on budgetary discipline and improvement of the budgetary procedure (OJ C 331, 7.12.1993, p. 1);
- the Declaration by the European Parliament, the Council and the Commission of 6 March 1995 on the incorporation of financial provisions into legislative acts (OJ C 102, 4.4.1996, p. 4);
- the Joint Declaration of 12 December 1996 concerning the improvement of information to the budgetary authority on fisheries agreements (OJ C 20, 20.1.1997, p. 109);
- the IIA between the European Parliament, the Council and the European Commission of 16 July 1997 on provisions regarding financing of the common foreign and security policy (OJ C 286, 22.9.1997, p. 80);
- the IIA of 13 October 1998 between the European Parliament, the Council and the Commission on legal bases and implementation of the budget (OJ C 344, 12.11.1998, p. 1).

<sup>4</sup> presented pursuant to point 31 of the IIA.

## **HISTORICAL BACKGROUND PRECEDING THE ADOPTION OF THE IIA FOR THE PERIOD 2007-2013**

Agenda 2000 and the Inter-institutional agreement of 1999 managed to fulfill its main purposes concerning financial discipline, the gradual growth of expenditure and inter-institutional collaboration in the budgetary procedure. The Budget of the EU has been adopted on time each year, and the two budgetary authorities have jointly adjusted the financial framework 2000-2006 to cater for the enlargement of the Union with ten new members.

On 14 July 2004 the Commission presented a proposal for the renewal of the Inter-institutional Agreement (IIA) on budgetary discipline and improvement of the budgetary procedure for the period 2007-2013 (COM(2004)498).

On 8 June 2005 the European Parliament adopted a resolution on Policy Challenges and Budgetary Means of the Enlarged Union 2007-2013 (P6\_TA(2005)0224), followed by a resolution on the IIA on budgetary discipline and improvement of the budgetary procedure adopted on 1 December 2005 (P6\_PROV(2005)0453).

On 15-16 December 2005, the European Council reached a political agreement on the Financial Perspective 2007-2013 (Document 15915/05, CADREFIN 268). On 18 January 2006 the European parliament adopted a resolution on the European Council's position on the Financial Perspective and the renewal of the IIA 2007-2013 (PE 368.274, B6-0049/2006).

## **MAIN FEATURES OF THE IIA FOR THE PERIOD 2007-2013**

In the IIA for the above period the basic features of the financial framework are left unchanged, namely:

- for each year of the 2007-2013 period expenditure is classified in broad categories called headings;
- maximum amounts (called ceilings) are established in the FF for appropriations for commitments and payments for each heading. Expenditure levels are based on the assumption that Bulgaria and Romania join the EU on 1 January 2007, if their accession takes place later, the expenditure ceilings will be revised accordingly;
- overall annual amounts are expressed both for commitment appropriations and payment appropriations;

**Box 2 The EU Solidarity Fund (EUSF)**

The EUSF allows rapid financial assistance in the event of major disasters occurring in the EU or a candidate country. There is a ceiling on the annual amount available for the Solidarity Fund of € 1 billion. On 1 October each year, at least one-quarter of the annual amount will remain available in order to cover needs arising until the end of the year. The portion of the annual amount not entered in the budget may not be rolled over in the following years.

In case the financial resources in the Fund in the year of disaster are not sufficient to cover the amount of assistance deemed necessary by the budgetary authority, the Commission may propose to finance the difference from the following year's Fund. The annual amount of the Fund in each year may not exceed € 1 billion under any circumstance.

When the conditions for mobilising the EUSF are met, the Commission shall propose to deploy it. Where there is scope for reallocating appropriations under the heading requiring additional expenditure, the Commission shall take this into account when making the proposal in accordance with the Financial Regulation in force, by the appropriate budgetary instrument. The decision to deploy the Solidarity Instrument is taken jointly by the two budgetary authorities.

The corresponding commitment appropriations shall be entered in the budget over and above the relevant headings in the FF as laid down in Annex I of the IIA.

Parallel with its proposal for a decision to deploy the EUSF, the Commission must initiate a triologue procedure, if necessary in a simplified form, to secure the agreement of the two budget authorities on the need to use the fund and on the amount required.

The IIA of 7.11.2002 on the EUSF is outside the FF for 2000-2006 but has the same features in terms of maximum annual amount (€1 billion), triologue procedure, joint adoption by the budget authority after a Commission proposal, no possibility for carry-overs for non-budgetised portions of the Fund.

- the annual ceiling for payment appropriations must respect the own resources ceiling currently established at 1.24% of the EU gross national income (GNI).

In the perspective of future institutional developments, the present IIA proposes to replace the term 'financial perspective' with 'multi-annual FF' or 'FF'.

It also proposes to insert a new provision in 2008 or 2009 by which the Commission will present to the European Parliament and Council a wide-ranging review on all aspects of EU spending and resources.

The IIA renews the IIA of 6 May 1999, comprising, at the same time, the experience acquired during its implementation. It consolidates all the joint declarations and IIAs concluded on budgetary matters since 1982. It simplifies the financial framework in three aspects wherever justified and possible:

- a) The IIA incorporates the separate supplementary IIA of 7 November 2002 on the creation of the EU Solidarity Fund (EUSF). The fund maintains the current rules for its mobilisation (Box 2) and when it is mobilised, corresponding expenditure is entered in the budget over and above the relevant headings of the FF.

### **Box 3 The Instrument of Flexibility**

The Instrument of Flexibility finances clearly identified expenditure of one-year or multi-annual character, which can not be financed within the limits of ceilings for other headings for a given year and up to the amount indicated. It has an annual ceiling of € 700 million euro.

The Commission makes a proposal for the instrument to be used after it has examined all possibilities for re-allocating appropriations under the heading requiring additional expenditure.

The proposal is presented, for any financial year, during the budgetary procedure. The Commission proposal is included in the preliminary draft budget or accompanied, in accordance with the Financial Regulation, by the appropriate budgetary instrument.

The decision to deploy the instrument of flexibility is taken jointly by the two budgetary authorities. Agreement will be reached by the conciliation procedure according to Part II of the IIA.

So, the existing flexibility instrument is reinstated and the reallocation flexibility removed. The annual amount of the flexibility instrument is increased to € 700 million and its scope broadened to cover also needs extending beyond one year. These changes ensure sufficient flexibility within lower ceilings for commitments.

- b) Simplification of the method for technical adjustment extends the predetermined 2% annual inflation rate used for structural funds and agriculture to the rest of expenditure.
- c) The provisioning of the guarantee fund for loans to third countries is rationalised so that there is no longer need for a 'reserve' to this end. The related (reduced) expenditure becomes part of the instruments available for the EU external policy.

Flexibility of the multi-annual FF is essential for financial discipline. If properly designed, it enhances effective resources allocation while allowing spendings for unforeseen needs or new priorities. Several parameters influence the flexibility of the FF:

- the length of the period covered by the financial perspective;
- the number of expenditure headings and the margins available within each expenditure ceiling;

#### **Box 4 The Emergency Aid reserve**

The emergency aid reserve is included in Heading 4 'the EU as a global partner' of the FF. The reserve enters in the general budget of the EU as a provision. The purpose of the reserve is to provide a rapid response to specific aid requirements of non-member countries after unforeseen events take place after the budget is established—mainly for humanitarian operations and civil crisis management. Its annual amount is fixed at € 221 million for the duration of the FF.

When the Commission considers to call on the reserve, it presents the two budget authorities a proposal for a transfer from this reserve to the corresponding budgetary lines. Any Commission proposal for a transfer to draw on the reserve for emergency aid must be preceded by an examination of the scope for reallocating appropriations.

At the same time as it presents its proposal for a transfer, the Commission must initiate a dialogue procedure, if necessary in a simplified form, to secure the agreement of the two budgetary authorities on the need to use the reserve and on the amount required. The transfers are made in accordance with Article 26 of the Financial Regulation (OJ L 248, 16.9.2002, p. 1).

The reserve for guaranteeing loans to non-member countries is deleted in the IIA 2007-13. The emergency aid reserve remains the only reserve, its scope is enlarged to civil crisis management and its amount is adjusted in 2004 prices. If necessary, supplementary needs for this reserve can be covered by transfers from other operational budget lines or by an amending budget to use the available margin.

- the margin below the own resources ceiling; the share of EU spending pre-determined by ‘amounts of reference’ in co-decided legislation;
- pre-allocated multi-annual programs;
- the general attitude towards using the revision procedure.

The degree of flexibility has evolved over time with the changing mix of those parameters. *Agenda 2000* has succeeded to answer unforeseen budget challenges at the price of greater complexity and lower transparency, without necessarily improving effective resource allocation. For instance, the instrument of flexibility and the EUSF had to be created outside the financial perspective to respond to unforeseen needs.

#### **Box 5 The European Globalisation Adjustment Fund**

The EGAF is intended to 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.

The Fund can not exceed a maximum annual amount of € 500 million which can be drawn from any margin existing under the global expenditure ceiling of the previous year, and/or from commitment appropriations de-committed during the previous two years.

When conditions exist for mobilising the EGAF, the Commission will propose to deploy it. The decision to deploy the EGAF will be taken jointly by the two budgetary authorities.

At the same time as it presents its proposal for a decision to deploy the Fund, the Commission must initiate a triologue procedure, if necessary in a simplified form, to secure the agreement of the two arms of budgetary authority on the need to use the Fund and the amount required.

The corresponding commitment appropriations shall be entered in the budget under the relevant heading, if necessary over and above the relevant amount as laid down in Annex I.



On 15-16 December 2005, the European Council reached a political agreement on expenditure ceilings that are significantly lower than those proposed by the Commission. Tighter expenditure ceilings entail more rigidity in the FF and risks in the EU ability to address future challenges, they hinder rather than encourage effective resource allocation. This is why the Commission proposed *three measures* to balance between budgetary discipline and efficient resources allocation:

- (1) The revision of the multi-annual FF remains the main instrument of response to significant and permanent changes in the EU policies in a fast developing context.
- (2) Three flexibility instruments can be mobilised in the 2007-2013 FF to facilitate the deployment or redeployment of financial resources within the expenditure ceilings. These are:
  - (a) The Emergency Aid reserve in Heading 4 that will respond to emergency situations in third countries. Its amount and mobilisation procedure remain unchanged.
  - (b) A new European Globalisation Adjustment Fund (EGAF) will provide additional support for workers who suffer the consequences of major structural changes in world trade patterns and will assist them with their reintegration into the labor market.
  - (c) The possibility for the budgetary authority to depart up to 10% from the so-called 'reference amounts' of multi-annual programmes adopted under the co-decision procedure (except for cohesion programmes). This possibility is based on a proposal of the European Commission in the framework of the annual budgetary procedure.
- (3) Two other instruments can be mobilised above the agreed expenditure ceilings within certain limits. They can be used in the framework of the annual budget procedure under the relevant provisions defined in the IIA. These are:
  - (a) the EU Solidarity Fund;
  - (b) the Flexibility Instrument.

The experience with the 2000-2006 financial perspective has shown that there is no longer a need to maintain the agricultural guideline in Council Regulation (EC) No 2040/2000 on budgetary discipline, since agricultural expenditure is already constrained by ceilings agreed till 2013. The other provisions on budget discipline in agriculture are found in the new Regulation (Articles 18-20) on the financing of

the common agricultural policy. The shift from market intervention towards direct payments to farmers and rural development measures makes agriculture expenditure more predictable.

The monetary reserve exists no longer and the Commission has proposed a new mechanism for the provisioning of the fund to guarantee loans to non-Member countries. According to the European Commission Council Regulation (EC) No 2040/2000 should be repealed and it will propose separately the appropriate legal act in due time.

## **INTER-INSTITUTIONAL COLLABORATION IN THE BUDGETARY PROCEDURE**

Provisions included in Part II of the IIA aim at improving the annual budgetary procedure. They result from budgetary practice and previous agreements and declarations. They are related with the new financial regulation (OJ L 248, 16.9.2002). The annexes I to IV form an integral part of the present proposed agreement. There are several steps in inter-institutional collaboration.

### **Step one**

After the technical adjustment of the FF for the forthcoming year, taking into account the Annual Policy Strategy presented by the Commission and prior to its decision on the preliminary draft budget, a dialogue meeting will be convened to discuss the budget priorities for the year. Account will be taken also of the institutions' powers and the needs for the next year and for the following years of the FF. Account will be taken also of the new elements of the FF that are likely to have a significant and lasting financial impact on the budget.

### **Step two**

As regards compulsory expenditure, the Commission, presenting its preliminary draft budget, identifies:

- (a) appropriations connected with new or planned legislation;
- (b) appropriations arising from the application of legislation existing when the previous budget was adopted.

The Commission will make a careful estimate of the financial implications of the Community's obligations. If necessary it will update its estimates in the course

of the budgetary procedure. It will supply the budgetary authority with all the duly justified reasons it may require.

The Commission may update ad hoc the estimate of agricultural expenditure in the preliminary draft budget or correct the amounts and their breakdown between the appropriations for international fisheries agreements and those entered in reserve. For this purpose an ad hoc letter of amendment must be sent to the budgetary authorities before the end of October. If it is presented to the Council less than a month before the European Parliament's first reading, the Council will, as a rule, consider the ad hoc letter of amendment when giving the draft budget its second reading.

As a consequence, before the Council's second reading of the budget, the two budgetary authorities will try to meet the conditions necessary for the letter of amendment to be adopted on a single reading by each of the institutions concerned.

### **Step three**

1. A conciliation procedure is set up for all expenditure.
2. The purpose of the conciliation procedure is to:
  - (a) continue discussions on the general trend of expenditure and, in this framework, on the broad lines of the budget for the coming year in the light of the Commission's preliminary draft budget;
  - (b) secure agreement between the two budgetary authorities on:
    - the appropriations referred to in step 2(a) and (b), including those proposed in the ad hoc letter of amendment referred to in point 2,
    - the amounts to be entered in the budget for noncompulsory expenditure,
    - and, particularly, matters for which reference to this procedure is made in the IIA.
3. The procedure begins with a trialogue meeting convened in time to allow the institutions to seek agreement by not later than the date set by the Council for establishing its draft budget.

There will be conciliation on the results of this trialogue between the Council and a European Parliament delegation, with the Commission also taking part. Unless decided otherwise during the trialogue, the conciliation meeting will be held at the traditional meeting between the same participants on the date set by the Council for establishing the draft budget.

4. If necessary, a new triilogue meeting could be held before the European Parliament's first reading on written proposal by the Commission or written request by either the chairman of the European Parliament's Budgets Committee or the President of the Council (Budgets). The decision whether to hold this triilogue will be agreed between the institutions after the adoption of the Council draft budget and prior to the vote of the amendments on the first reading by the European Parliament Budgets Committee.
5. The institutions continue the conciliation after the first reading of the budget by each budgetary authority to secure agreement on compulsory and noncompulsory expenditure and, in particular, to discuss the ad hoc letter of amendment referred to in point 2.

A triilogue meeting will be held for this purpose after the European Parliament's first reading. The results of the triilogue will be discussed at a second conciliation meeting to be held the day of the Council's second reading. If necessary, the institutions will continue their discussions on non-compulsory expenditure after the Council's second reading.

6. At these triilogue meetings, the institutions' delegations are to be led by the President of the Council (Budgets), the Chairman of the European Parliament's Committee on Budgets and the Member of the Commission with responsibility for the budget.
7. Each arm of the budgetary authority takes steps to ensure that the results secured in the conciliation process are respected throughout the budgetary procedure.

#### **Step four**

In order for the Commission to be able to assess in due time the implementability of the amendments envisaged by the budget authority, like creating new Preparatory Actions and Pilot Projects or prolonging existing ones, both arms of the budgetary authority must inform the Commission by mid June of their intentions, so that a first discussion may take place at the conciliation meeting of the Council's first reading. The three institutions agree to limit the total amount of appropriations:

- for pilot schemes to € 38 million in any budget year;
- for new preparatory actions to € 36 million in any budget year;
- actually committed for preparatory actions to € 90 million.

**Box 6 Compulsory and non-compulsory expenditure****CLASSIFICATION OF EXPENDITURE****HEADING 1 Sustainable growth**

1A Competitiveness for growth and employment Noncompulsory expenditure (NCE)

1B Cohesion for growth and employment NCE

**HEADING 2 Preservation and management of natural resources NCE**

Except: Expenditure of the common agricultural policy concerning market measures and direct aids, including market measures for fisheries and fisheries agreements—

Compulsory expenditure (CE) (CE)

**HEADING 3 Citizenship, freedom, security and justice NCE**

3A Freedom, Security and Justice NCE

3B Citizenship NCE

**HEADING 4 The EU as a global partner NCE**

Except: Expenditure resulting from international agreements which the EU concluded with third parties CE

Contributions to international organisations or institutions CE

Contributions provisioning the loan guarantee fund CE

**HEADING 5 Administration NCE**

Except: Pensions and severance grants CE

Allowances and miscellaneous contributions on termination of service CE

Legal expenses CE

Damages CE

**HEADING 6 Compensations CE****STRUCTURE AND CLASSIFICATION OF EXPENDITURE**

Annex III of the IIA classifies compulsory and non-compulsory expenditure by heading. The two budget authorities classify the new budget items within the annual conciliation procedure.

**FINANCIAL PROVISIONS IN LEGISLATIVE INSTRUMENTS**

The principle set out in the Joint Declaration of 6 March 1995 and incorporated in point 33 of the IIA of 6 May 1999, according to which the institutions comply with the reference amounts adopted in the legislative co-decision procedure in the budget procedure, is maintained. The co-decision procedure, however, has

been regularly extended since 1995 and the strict provisions on reference amounts impose increasing constraints for budgetary policy. The Commission proposes that the budgetary authority and the Commission be able to depart from these amounts by a limited margin (10%) in the course of the annual budgetary procedure.

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