COMMISSION OF THE EUROPEAN COMMUNITIES

COM(87) 430 final
Brussels, 4 August 1987

COMMISSION COMMUNICATION ON BUDGETARY DISCIPLINE

COMMISSION COMMUNICATION ON BUDGETARY DISCIPLINE

1. GENERAL INTRODUCTION

In February the Commission put forward a number of proposals concerning the future financing of the Community. The new budget discipline guidelines occupy an important place here, notably because of the unsatisfactory results achieved on the basis of the December 1984 decisions. The Brussels European Council examined all these proposals and included the following points in its conclusions:

- the Community's financial equilibrium, must be achieved on the one hand by providing it with appropriate resources and on the other hand by subjecting the use of these resources to effective and binding budgetary discipline;

- the new budgetary discipline will have to be stricter than the present arrangements and will have to be applied to all the Community's expenditure, i.e. both to payment appropriations and to commitment appropriations;

- as regards non-compulsory expenditure, the rules of budgetary discipline will have to comply with Article 203(9) of the Treaty;

- EAGGF Guarantee expenditure must not progress at a rate exceeding that of the own resources base, i.e. GNP;

- budgetary discipline will have to produce a better balance between the various categories of expenditure in the Community budget;

- to achieve the objectives of budgetary discipline, budget management rules must be strengthened, in particular through a reform of the Financial Regulation.

In accordance with the proposals adopted in February and the conclusions of the Brussels European Council, this communication to the Council is intended to:

- explain the various aspects of budgetary discipline contained in COM(87)100 and COM(87)101; some of these aspects are also contained in the draft decision on new own resources;

- explain in more detail how some of the constituent parts of budgetary discipline will work;

- present in a single document all the components of the new budgetary discipline arrangements formally contained in various proposals which the Commission has already sent or will be sending to the Council.

The Commission considers that all the provisions on budgetary discipline should be contained in the following instruments:

- the decision on new own resources;
- guidelines for a Council decision on budgetary discipline in respect of agriculture (and other compulsory expenditure) and the principles of an Interinstitutional Agreement which will define the role of each institution in the implementation of budgetary discipline in respect of non-compulsory expenditure (drafts annexed);
- the proposal for the revision of the Financial Regulation;
- the rules for implementing the agricultural stabilizers in each market organization.

The medium-term financial perspective presented in COM(87)100 and COM(87)101 provides an overview of the operation of the budgetary discipline measures proposed by the Commission. It indicates how this budgetary discipline should be applied up to 1992 by determining the growth path for the various categories of expenditure during the reference period.

The present paper discusses the following aspects:

- the general principles of budgetary discipline;
- budgetary discipline in respect of agriculture;
- budgetary discipline in respect of non-compulsory expenditure;
- the Interinstitutional Agreement.

2. GENERAL PRINCIPLES

The Commission proposes that the resources available to the Community in 1992 should be subject to an overall ceiling of 1.4% of its GNP.

This should enable the Community to operate the common policies, notably those provided for by the recent reform of the Treaty following the entry into force of the Single Act, put it into a sounder position and give it budgetary security for a sufficiently lengthy period.

In return for this new margin of resources, the Community must impose tighter budgetary discipline. Observance of budgetary discipline will be guaranteed by a smooth growth path for the Community budget in terms of GNP, as set out in the multiannual financial perspective.

These guarantees will be of two kinds.

2.1 For payment appropriations the decision on new own resources will determine for each year up to 1992 an annual ceiling for the own resources which may be called in.

These ceilings will be slightly higher than the multiannual financial forecasts in order to give the Community a small safety margin which it can draw upon if need be. The ceilings are as follows:

1988	1989	1990	1991	1992
1.20	1.22	1.24	1.27	1.30

The ceiling for 1992 (1.30% of GNP) is lower than the overall own resources ceiling (1.40% of GNP) so that the Community will not find itself once again in the position it has been in throughout the eighties whenever a decision has had to be taken to allow it new own resources.

2.2 For commitment appropriations the European Council, like the Commission, has requested that they too should be subject to strict limits. Commitments reflect the Community's legal and financial obligations. In the case of differentiated appropriations, which relate to operations covering a number of years (structural Funds and research programmes, for instance), the commitment appropriations express the amounts required to attain the objectives of Community policies.

The limits on commitment appropriations will be set as follows:

- the own resources decision will stipulate that commitment appropriations for 1992 will have to be below the ceiling of 1.40% of GNP;

- the own resources decision will also stipulate that a strict relationship must be maintained between commitment appropriations and payment appropriations and the increase in commitment appropriations must be regular up to the ceiling set for 1992.

The annual allocations of commitment appropriations are specified in the multiannual forecasts and are determined each year by the budgetary authority in accordance with the rules laid down in the own resources decision. This procedure will reconcile the requirements of budgetary discipline with a certain degree of flexibility for the gradual preparation and application of the common policies.

2.3 Apart from establishing the overall ceiling on resources available to the Community, budgetary discipline will have to help strike a better balance between the different categories of expenditure. This balance is already present in the Commission's options as set out in the multiannual perspective. It involves an increasingly large proportion of the budget being devoted to expenditure designed to achieve greater economic and social cohesion and to expenditure on new policies.

This means that specific mechanisms will be needed to maintain budgetary discipline in respect of agriculture and non-compulsory expenditure.

*

*   *

3. BUDGETARY DISCIPLINE IN RESPECT OF AGRICULTURE

At its meeting on 29 and 30 June 1987 the European Council confirmed the basic principles of budgetary discipline applicable to EAGGF Guarantee expenditure listed in COM(87)100 and COM(87)101. Budgetary discipline would then operate as follows in respect of agriculture:

3.1 Basic principles and general objectives

- Annual expenditure on the management of the agricultural markets must not increase faster than the own resources base.

- The new agricultural guideline - as defined by the multiannual financial perspective - and hence the appropriations allocated to EAGGF Guarantee must be respected as part of budgetary discipline in the agricultural sector.

- The planned budgetary discipline arrangements must not, in the event of the overall allocation being exceeded, adversely affect the development of the policies provided for by the Single Act.

- To achieve these objectives the following measures will be taken:

  - introduction of stabilizers for all market organizations;
  - new financing arrangements proposed in connection with the revision of the Financial Regulation and changeover from advances to reimbursements;
  - monetary reserve and arrangements to allow for exceptional circumstances.

3.2 Practical details of application

A. Definitions

- The definition of EAGGF Guarantee expenditure to be used for the application of budgetary discipline is that appearing in the conclusions of the Council of 4 December 1984 (expenditure chargeable to Titles 1 and 2 of Part B of Section III of the budget, less the total amounts corresponding to the disposal of ACP sugar, food aid refunds and payments made by producers in respect of sugar and isoglucose levies).

. The expenditure of the reference year used as a basis for calculating the annual allocations is real requirements for 1987.

. The rate of increase to be applied to this base every year is the rate of increase in the own resources base, i.e. Community GNP.

. The annual allocation for agricultural expenditure as defined above must cover costs connected with the disposal and depreciation of existing agricultural stocks and any stocks built up in future years despite the new line of the CAP.

B. Application of budgetary discipline in respect of agriculture

The annual allocation defined above will have to be respected every year. This will require a careful check on EAGGF Guarantee expenditure chapter by chapter, a task which will be made easier by the introduction of agricultural stabilizers in each of the market organizations.

Under the Commission's broader management powers, it will take the following action to ensure that expenditure does not exceed the appropriations allocated to each of the chapters:

- For each chapter the expenditure path will be compared each month with the average for the previous three years (early warning system). Operation of this early warning system (chapter by chapter) will be helped by the strict management of reimbursements. This management system will no longer work in overall terms, as was the case with the system of advances, since in future reimbursements will depend on the availability of appropriations for each heading.

- The Commission will inform the budgetary authority of any significant or potentially significant upward divergence and then take appropriate action, including the triggering of stabilizers, to keep expenditure within the limit of the appropriation allocated to the chapter in question.

- If the allocations cannot be respected through the use of stabilizers in the financial year in which they are triggered, the Commission will propose transfers from other EAGGF Guarantee chapters which are expected to have surplus appropriations for the current year.

- If these two mechanisms cannot keep expenditure within the total allocation for EAGGF Guarantee, in the current financial year, the Commission will propose a supplementary and amending budget subject to the arrangements specified at C below, the annual ceilings on own resources and the Community's other policies.

Three conditions must be met if this new budgetary discipline in respect of agriculture is to operate (see 3.3 below):

6

- the Commission's management powers must be increased;
- the Council must be given binding deadlines for taking decisions;
- the agricultural regulations and Financial Regulation must be suitably amended.

C. Compliance with the annual allocation on a three-year basis

(a) Cases where the annual allocation is under-utilized

Any part of an allocation not used for the year in which it is available may be considered as a margin which can be drawn on in subsequent financial years under the budgetary procedure.

(b) Cases where the annual allocation is exceeded

If the overrun leads to the adoption of a supplementary budget in the course of the financial year, the additional amounts provided must be offset by an equivalent volume of savings over the next two years. Most of these savings must be made in the year following the overrun.

D. Monetary reserve

The reference framework ("guidline") for budgetary discipline in respect of agriculture in the multiannual perspective makes no allowance for the exchange rate structure which, experience has shown, seriously affects agricultural expenditures, sometimes favourably, sometimes adversely.

External monetary movements will therefore have to be dealt with by means of the following special mechanism:

- a dollar/ECU reference parity is established by the Council acting on a proposal from the Commission;
- before the end of October each year, the Commission presents, in the light of the reports on the execution of the budget, an analysis of the differences in relation to the dollar/ECU reference parity together with an assessment of the implications in budgetary terms;
- in the event of savings produced by a favourable movement in the ECU/dollar rate, a monetary reserve will be set up by reducing the agricultural allocations in the current year's budget;
- in the event of an adverse movement in the dollar/ECU rate, the Commission will propose, on the basis of its assessment, that appropriate measures be taken: mobilization of the monetary reserve already built up; drawings on the "book" reserve generated by under-utilization by reference to

7

the guideline in an earlier financial year; application of additional agricultural stabilizers; presentation of a supplementary budget.

E. Exceptional circumstances

The measures proposed above should, together, serve to contain agricultural expenditure in accordance with the principles of budgetary discipline.

However, it is impossible to rule out entirely the possibility of something occurring that will have a major impact on the world markets or the Community markets.

The budgetary effects of such occurrences must be cancelled out over a three-year period.

However, if the full amount of any overspending cannot be recovered, the Commission and the Council will assess the situation and decide how to deal with overruns caused by exceptional circumstances which have not been offset by savings within the period.

3.3 Agricultural stabilizers

The mechanism of the stabilizers must be such as to ensure that the budgetary allocations are respected in each EAGGF Guarantee chapter. They must therefore be provided for each market organization and it must be possible to bring them into operation rapidly when necessary. With expenditure being booked heading by heading, any risk of overruns will be quickly spotted, since reimbursement will depend on the availability of appropriations for each heading.

At all events, the Commission will have to be given more extensive management powers to keep the necessary tight rein on the market organizations. The proposals contained in the review of action taken to control the agricultural markets and the outlook for the common agricultural policy will allow the Commission and in some cases the Council to adopt the necessary measures (operation of stabilizers, stopgap measures) by emergency procedure whenever there is a risk of the budget allocations being exceeded.

Some stabilizers already exist although they do, of course, differ according to product and the type of market support. Products subject to intervention arrangements do not require the same stabilizing instruments as those subject to a system of direct aid. Similarly, a sector subject to production quota arrangements has less need for additional budgetary stabilizers since the quotas established correspond to the market balance. Finally, multiannual production sometimes requires different mechanisms.

So far, production quotas apply to sugar and milk, production guarantee thresholds to oilseeds and cotton, processing guarantee thresholds to some fruit and vegetables, intervention thresholds to fresh tomatoes, butter and milk powder and direct financial coresponsibility measures to sugar, milk and cereals.

Where the use of stabilizers requires amendments to the rules in order to contain expenditure, it will be necessary:

- in some cases to adjust the respective powers of the Council and the Commission to allow quick action and sufficient flexibility of management;

- to grant the Commission power to adopt stopgap measures.

The Commission's communication on the common agricultural policy contains practical proposals for introducing new stabilizing measures in each sector in line with the above objectives.

4. OTHER COMPULSORY EXPENDITURE

Of the other compulsory expenditure, EAGGF Guidance expenditure is subject to the principles of discipline applicable to the structural Funds.

The bulk of the remaining non-agricultural compulsory expenditure is on the common external policy. It represents the commitments which the Community wishes to enter into in respect of certain areas or certain countries outside the Community.

This expenditure is mainly the budgetary expression of these commitments, it will, of course, have to take account of the constraints governing the management of public finance and develop in line with the medium-term financial perspective.

5. BUDGETARY DISCIPLINE IN RESPECT OF NON-COMPULSORY EXPENDITURE

The main objective of budgetary discipline in respect of non-compulsory expenditure, as defined in COM(87)100 and COM(87)101, is to enable the political decisions and guidelines, enshrined in particular in the Single Act, to be put into effect with the same strictness as now applies in the Member States.

The medium-term financial perspective should therefore be given a more central role to ensure that the best possible balance can be struck between the various categories of expenditure, in line with the conclusions of the Brussels European Council.

If required by circumstances or political options, the safety margin could be used for non-compulsory expenditure in the same way as for other expenditure.

5.1 Discipline in respect of non-compulsory expenditure and the five-year perspective

The growth in appropriations for non-compulsory expenditure between 1988 and 1992 will be defined by the multiannual financial perspective. These financial forecasts lay down a controlled increase in non-compulsory expenditure which should lead by 1992 to an overall volume of commitment appropriations for the entire Community budget slightly below 1.4% of GNP. This will require compatible and controlled growth of commitment and payment appropriations.

The perspective will incorporate realistic growth forecasts for the major areas of non-compulsory expenditure - broken down wherever possible by major objectives - with due allowance for the framework decisions to be adopted by the Council on increasing the allocation for the structural Funds and on the overall appropriation for the research programme and other multiannual operations.

It should thus reflect the political agreement reached on the financial aspects of achieving the objectives of the Single Act between now and 1992.

Each year the financial perspective will be submitted for approval to the Council and Parliament not later than 15 February. Should the two arms of the budgetary authority fail to reach agreement by 15 April, the Commission may use its proposal as the reference framework for budgetary discipline.

The annual budgetary estimates must be drawn up in accordance with these forecasts.

Each year's preliminary draft budget presented by the Commission will reflect - in terms of commitment appropriations - the growth path for non-compulsory expenditure laid down in the financial perspective. The payment appropriations will be determined according to the schedules for payments.

It will be for the two arms of the budgetary authority to take a decision on the overall allocation for non-compulsory expenditure and to negotiate during the annual budgetary procedure on the relative size of the increases in appropriations within the allocations by major area contained in the multiannual perspective.

5.2 <u>Determination of the rate of increase for non-compulsory expenditure</u>

The rate of increase for non-compulsory expenditure will be determined in compliance with Article 203(9) of the Treaty and within this multiannual framework.

At the beginning of the budgetary procedure the Commission will propose a growth rate for non-compulsory expenditure which includes provision for progress in applying the policies agreed upon in the Single Act which have been the subject of a Council decision.

5.3 <u>Improved management of non-compulsory expenditure and budgetary discipline</u>

As far as the Commission is concerned, the starting point for tightening budgetary discipline in respect of non-compulsory expenditure is improved management, designed to achieve:

- a reduction in the over-allocations in many budget headings, resulting from overestimates of spending capacity,
- stricter compliance with the principle of budget annuality, leading also to an improvement in budget transparency,

- better monitoring of budget execution as regards both annual growth rates and compliance with schedules,

- a better match between budget spending and the aims being pursued.

This can only be achieved by the combined efforts of all those involved in the budgetary decision-making procedure, i.e.:

- the Commission
- the two arms of the budgetary authority and
- the national authorities.

In more concrete terms, stricter management will be possible only if the Council adopts the Commission's proposals on:

- the Financial Regulation and
- the reform of the structural Funds.

6. THE INTERINSTITUTIONAL AGREEMENT

The tighter budgetary discipline proposed by the Commission will only be effective if there is a broad consensus among the institutions. This means that the disputes of past years will have to be eliminated from the budget procedure, and an atmosphere of trust established between the Council, Parliament and the Commission.

The Commission suggests that the rules of budgetary discipline in respect of non-compulsory expenditure, as provided for in section 5 above, should be laid down in an interinstitutional Agreement. The content of such an agreement is outlined in the annex.

The discussions between Parliament, the Council and the Commission might result in this Agreement being extended to other matters, notably as regards the orderly growth of the main areas of budget expenditure and the establishment of desirable limits for them, each year, at the start of the budgetary procedure.

7. COMMISSION REPORT FOR 1991

By the end of 1991 the Commission will present a report on the operation of the own resources system and the conditions of budgetary discipline linked with it.

ANNEX

GUIDELINES FOR A DECISION OF THE EUROPEAN COUNCIL ON BUDGETARY DISCIPLINE AND PROPOSED PRINCIPLES FOR AN INTER-INSTITUTIONAL AGREEMENT

A. GUIDELINES FOR A DECISION OF THE EUROPEAN COUNCIL

GENERAL PRINCIPLES

1. Budgetary discipline shall apply to all Community expenditure, in terms of both commitment appropriations and payment appropriations. It shall be binding on all the institutions involved in its application.

2. The Decision on the system of the Communities' own resources shall lay down an overall own resources ceiling for 1992 and intermediate ceilings for the years from 1988 to 1992. It shall also lay down a ceiling for commitment appropriations in 1992 and determine an orderly progression for them, maintaining a strict relationship between commitment appropriations and payment appropriations.

   The Community budgets adopted for 1988 to 1992 shall keep within those ceilings.

3. Each year the budgetary authority, acting on a proposal from the Commission, shall adopt a five-year financial perspective drawn up in line with the principles set out at 2 above, which shall serve as a reference framework within which the budget for each financial year shall be established in both commitment appropriations and payment appropriations.

AGRICULTURAL EXPENDITURE

1. The annual growth rate of EAGGF Guarantee expenditure shall not exceed that of the own resources base, i.e. Community GNP.

2. The expenditure to which Article 4 applies shall be the expenditure chargeable to Section III, Part B, Titles 1 and 2 (EAGGF Guarantee) of the budget, less amounts corresponding to the disposal of ACP sugar, food aid refunds, sugar and isoglucose levy payments by producers, and any other revenue raised from the agricultural sector in the future.

   For the financial years 1988-92 this expenditure shall also include:

   - costs connected with the disposal and depreciation of existing agricultural stocks with a view to restoring a healthy situation by the end of 1992;

   - annual depreciation costs for newly formed stocks.

3. The reference basis for the definition of the annual allocations for EAGGF Guarantee expenditure shall be established by reference to real requirements for 1987.

4. To ensure that the agricultural reference framework is respected, stabilization mechanisms shall be introduced in each of the common market organizations.

   Details of the conditions which will trigger these mechanisms shall be laid down in the specific agricultural regulations for each sector.

5. The Commission shall draw up its price proposals within the limits laid down by the agricultural reference framework.

   If the Commission considers that the outcome of the Council's discussions on these price proposals is likely to exceed the costs put forward in its original proposal, the final decision shall be referred to a special meeting of the Council attended by the the Ministers of Finance and the Ministers of Agriculture, which shall have the sole power to adopt a decision.

6. The agricultural allocation shall be respected each year.

   However, if the allocation is exceeded in the course of a financial year, the overrun shall be offset by equivalent savings over the following two years. As much as possible of these savings shall be made in the year following the overrun.
   If an annual allocation is not fully used, the margin available may be drawn on in a subsequent financial year.

   The development of policies linked with the Single Act must not be jeopardized by any overrun on the total allocation for agriculture.

7. An ECU/dollar reference parity shall be established by the Council acting on a proposal from the Commission; the budgetary consequences of any divergence from this reference parity shall be dealt with by the following special mechanism:

   - in the event of savings, a monetary reserve shall be set up which may be drawn upon in subsequent financial years.

   - in the event of an adverse movement in the ECU/dollar rate, the Commission shall propose appropriate measures: e.g. drawing upon the monetary reserve set up, the application of additional budgetary stabilizers, the presentation of a supplementary budget, etc.

8. Other occurrences may affect world markets or Community markets.

The budgetary effects of such exceptional circumstances shall be cancelled out within the three-year period. If any overruns have not been offset by the end of this period, the Commission and the Council shall assess the situation and decide how to deal with such overruns.

OTHER COMPULSORY EXPENDITURE

The Council shall adopt a reference framework for non-agricultural compulsory expenditure (commitment appropriations and payment appropriations) to ensure that its growth to meet the Community's legal obligations is compatible with the medium-term financial perspective adopted for expenditure as a whole.

* *

*

On the basis of these guidelines, the European Council requests the Council, after consulting Parliament, to adopt a formal decision.

B. PROPOSED PRINCIPLES FOR AN INTER-INSTITUTIONAL AGREEMENT

1. The growth of non-compulsory expenditure shall be defined in the five-year financial perspective in the light of the framework decisions on the structural Funds, research, and other multiannual operations.

   The Community's financial objective for 1992 in respect of the policies provided for under the Single European Act shall be achieved within this framework.

2. Before 15 February each year the Commission shall present a proposal relating to the five-year financial perspective.

   The perspective shall describe the growth, year by year, of the budget and its principal components, in terms of both commitment appropriations and payment appropriations.

3. The budgetary authority shall give its decision on the perspective before 15 April.

   In the absence of agreement between the two arms of the budgetary authority, the Commission may consider that its proposal shall constitute the reference framework for drawing up the preliminary draft budget.

4. On the basis of the multiannual financial perspective the Commission shall propose a rate of increase for non-compulsory expenditure in the next financial year.

   This rate shall be adopted by the Council and the European Parliament at the start of the budgetary procedure, pursuant to Article 203(9) of the Treaty.

16

6. The Joint Declaration of 30 June 1982 shall be amended, in particular as regards the classification of expenditure and the treatment of one-off operations.

7. Before the end of 1991 the Commission shall present a report on the operation of this joint decision and on any amendments which may be necessary in the light of experience.

17