EUROPEAN UNION

Committee of the Regions

Implications of the annual EU budget for local and regional authorities

This file note was written by the Centre for European Policy Studies - CEPS (Author: Jorge Núñez Ferrer).
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Executive summary

This report analyses the relevance for local and regional authorities (LRAs) and thus for the Committee of the Regions (CoR) of: a) the budget lines of the 2014 draft budget in preparation; b) the annual budget adoption and subsequent amendments based on the experience of the 2011, 2012 and 2013 budgets; and c) the 2014-2020 Multiannual Financial Framework (MFF), in particular the interplay with the annual budgets and the impact of the RAL (*reste à liquider* or outstanding commitments) of the 2007-2013 period.

Relevance to LRAs of budgetary headings: The main budget line of relevance is for the Structural Funds. Based on a sample analysis, the **main beneficiaries of the European Regional Development Fund (ERDF) are LRAs**. In a sample analysis of ERDF funds in a convergence region, 45% of the beneficiaries were municipalities. For the European Social Fund (ESF), the largest share is not for LRAs, even if those are still important beneficiaries. For funds under central management, the report notes **the rising importance of the Horizon 2020 programme**. Due to the shift in focus on demonstration and deployment, regional and municipal authorities will become central players in the planning and implementation process and also in the pre-commercial deployment process, which will also involve the Structural Funds. **The mechanisms are not yet decided and the CoR should be closely involved in designing them.** The same applies for key instruments focusing on LRAs, the LIFE+ programme and the continuation of the existing ELENA-style initiatives.

On the annual budget procedures: There has been a tendency for the Council to severely cut the proposed appropriations for payments, leading to acrimonious negotiations over amendments to the draft budget, reallocations of unused margins and the rollover of uncovered payment appropriations to the next budget year. For LRAs and the CoR, the main aspects are the following:

- **The RAL is accumulating to reach an historical high** (expected to be €230-250 billion at the end of 2013). This is equivalent to approximately 50% of the annual budgets from 2014 to 2016. **This volume of RAL could cause rising pressures, particularly in 2016** when payment requests from 2014 commitments arrive.
- **In 2016, a review of the budget is going to be undertaken that could strongly impact budget lines where the absorption is weak**. Given the expected late start of the programming period, and the experience of past programming periods, this review is of crucial importance for the CoR, as LRAs may see regional funding cut due to weak absorption.

- **The increased flexibility between headings for the 2014 and 2020 MFF may negatively affect LRAs.** The CoR should attentively follow decisions in this area, given the expected difficulties and delays that the LRAs may face in implementing programmes. Budget lines with low absorption rates may be cut in favour of others.

Introduction

Following the request by the CoR, this report has the following objectives:

a) To identify the lines in the EU budget of main relevance to local and regional authorities (LRAs) and offer a rationale for local authorities to intervene in the annual budgetary procedures.
b) To analyse the annual budgets for 2011, 2012 and 2013 in terms of what was proposed and the final adopted outcomes, with a view to indicating the relevance for LRAs of the annual budgetary decisions and suggesting which budget lines the CoR should focus on in the process.
c) To analyse the repercussions of a recurring high RAL (*reste à liquider*/ outstanding commitments) on LRAs, based on the experience in 2012-2013 and the expected RAL in the 2014-2020 MFF (Multiannual Financial Framework).

1 Headings in which LRAs are main beneficiaries

There are a number of headings that benefit or potentially could benefit the LRAs, in addition to the ones under shared management of the Structural Funds. The most important in funding terms is Heading 1b of the multiannual budget.

This section analyses the 2014 draft budget, heading by heading, based on their relevance to LRAs. Some important changes will affect the way LRAs can benefit from funding, as more funding will be allocated to financial instruments to leverage European Investment Bank (EIB) and private debt funding, which LRAs can use to finance important local infrastructure. This means that some small headings have a high financial impact. Their training components can also help LRAs improve their planning and implementation practices.

The 2014 draft budget is presented in Table 1. Of the six main headings, only Headings 1 and 2 are relevant for this study. There are important changes in the future budget structure affecting the size and type of support that LRAs can expect. First there is an observable shift from regional policy funding (under shared management) to the centrally managed competitiveness funding in Heading 1a. This is followed by the drive from the European Commission to require more integrated programmes at regional level, reinforcing links between the regional programmes under shared management and centrally planned instruments, in particular Horizon 2020. This might not only be limited to actions linked to the smart specialisation strategies, but may even be part of specific R&D calls under the industrial leadership policy of Horizon 2020.

Table 1: 2014 draft budget, commitment appropriations for 2014 (€ million)

HEADING	
1. Smart and inclusive growth	***63 973***
– *1a Competitiveness for growth and jobs*	*16 390*
– *1b Economic, social and territorial cohesion*	*47 583*
2. Sustainable growth: natural resources	***59 303***
– of which: European Agricultural Guarantee Fund	44 130
3. Security and citizenship	**2 179**
4. Global Europe	**8 335**
5. Administration	**8 721**
6. Compensation	**29**
Total commitment appropriations	**142 540**
Total payment appropriations	**135 866**

Source: European Commission, Statement of estimates of the European Commission for the financial year 2014 (Preparation of the 2014 Draft Budget), SEC(2013)370 – June 2013.

According to present transparency rules on EU funding, information has to be provided on the amounts, intervention type and name of the final beneficiary of funds. The Commission publishes a list of all beneficiaries of funding for instruments under central management and presents links to the data in the Member States.[1]

This report performs only partial sample analysis on the distribution of the funds by type of beneficiary, identifying where regional and local authorities benefit most from the funds. However, several barriers to such an analysis exist. For the funds under central management (i.e. managed by the Commission), there are over 55 000 beneficiaries listed in the database for 2012 alone. These are not separated into types of beneficiaries, making searches according to the type of beneficiary difficult, e.g. municipality, regional authority, private entity, etc. Searches can be performed by action type and then beneficiaries can be checked one by one. However, the nature of the beneficiary is not always clear from the name alone, and the names are in the original language, making such research even more difficult.

In the case of funding under shared management, each Member State provides information on beneficiaries to which the Commission provides links. The presentation of the data, however, is not standardised. Some information is presented in datasets that allow for manipulation and easy searches whereas other data are provided on web pages or in PDF format. The data are in the official language of the country (and some names may be in the local or regional language). As is the case for the centrally managed funds information, there is generally no indication on the type of beneficiary, which makes it difficult to identify LRAs.

[1] http://ec.europa.eu/contracts_grants/beneficiaries_en.htm

1.1 Heading 1A. Competitiveness for growth and jobs

Heading 1 is divided into two main subheadings: competitiveness for growth and jobs (Heading 1a) and economic, social and territorial cohesion (Heading 1b). Heading 1a is composed of centrally managed instruments targeting transnational needs and excellence in research. It also finances centrally managed programmes for small- and medium-sized enterprises (SMEs).

Table 2: Heading 1a Competitiveness for growth and jobs (€ million)

	Commitment appropriations	Payment appropriations
Large infrastructure projects	2 629,4	1 987,1
Nuclear safety and decommissioning	130,4	180
Common Strategic Framework Research and Innovation	9 113,7	6 328,5
– ***Horizon 2020***	*8 826,5*	*6 077,1*
– **Euratom**	287,2	251,4
COSME	243,8	236,7
Erasmus for all	1 418,3	1 219,4
Social Change and Innovation	119,4	109,6
Customs, Fiscalis and Anti-Fraud	118,3	86
Connecting Europe Facility	1 966,2	885,9
EERP Energy projects under the economic recovery programme		100
Other actions and programmes + Commission specific competences	291,5	309
Pilot projects preparatory actions	pm	19,3
Decentralised agencies	233,2	233,4
Total	16 264,2	11 694,9
Ceiling	16 390	
Margin	125,8	

Source: European Commission, Statement of estimates of the European Commission for the financial year 2014 (Preparation of the 2014 Draft Budget), SEC(2013)370 – June 2013.

LRAs are rarely direct beneficiaries of the programmes, but the Horizon 2020 heading is set to involve the LRAs intensively in the future. Horizon 2020 is shifting away from the present focus of the 7th Framework Programme on basic research to give more weight to industrial policy. This will result in more funding for pilot projects in the area of innovative infrastructure, in particular for energy, transport or water management. These demonstration projects will require the full participation of LRAs and their readiness to adapt procedures to the needs of the infrastructure. The funds allocated to the Industrial Leadership sub-heading are presented below (Table 3). A considerable amount of this important funding can (and often will) involve LRAs, as many demonstration

and deployment activities require their active involvement. LRAs can in some cases be partial beneficiaries of the funds.

Table 3: Heading 2020 sub-heading Industrial Leadership, € million

	Commitment appropriations	Payment appropriations
– **Industrial Leadership**	1 936	468,1
– ***Leadership in enabling and industrial technologies***	*1 485*	*135,3*
– ***Access to risk finance***	*384,8*	*326,8*
– **Innovation in SMEs**	66,2	6

Source: European Commission, Statement of estimates of the European Commission for the financial year 2014 (Preparation of the 2014 Draft Budget), SEC(2013)370 – June 2013.

In addition, the Europe 2020 Innovation Union flagship initiative[2] calls for better coordination of funds, linking Horizon 2020 to Cohesion Policy, i.e. mainly the Structural Funds. This starts of course with reinforcing the funding from the Structural Funds with the aim of developing the innovative capacity of the regions, but it goes further. The Structural Funds are seen as a mechanism to assist the rollout of innovations that have been financed by Horizon 2020. This means that the Commission seeks to find solutions to link the investments in innovative infrastructure from Horizon 2020 to other local/regional investments in infrastructure as a deployment instrument.

This coordination between Horizon 2020 and the Structural Funds is somewhat obscure and has not yet been defined by the Commission. However, for the Smart Cities European Innovation Partnership,[3] for example, serious internal discussions are under way and workshops and consultations will most likely be undertaken.[4] This means that large programmes under Horizon 2020, supported by the EIB risk-sharing and debt facilities backed by the EU budget[5] can be expected, involving the LRAs. The link to other Structural Fund instruments for deployment means a strong involvement of regional and local authorities. Regions and municipalities able to set up strong private-public partnerships with academia and businesses can expect direct and considerable benefits from Horizon 2020. The Commission will draft the details for the first calls over the coming months.

The CoR should be involved in the discussions on the practical procedures that the European Commission will prepare for the calls and actively assist in finding

[2] Communication from the Commission, Europe 2020 Flagship initiative – Innovation Union, SEC(2010) 1161.
[3] Communication from the Commission, Smart Cities and Communities European Innovation Partnership, Brussels, 10.7.2012, C(2012) 4701 final.
[4] Based on discussions by the author with officers responsible for the European Innovation Partnership.
[5] Risk-Sharing Finance Facility (RSFF) for the demonstration and pilot phase guaranteed by the 'Access to risk finance' support in Table 3.

workable methods for combining funds that are different in nature in terms of procedures and management. This is complex as shown in a recent Court of Auditors report for Horizon 2020. The report highlights the disparate procedures within the different Horizon 2020 projects, as they are often managed by different DGs (e.g. transport by DG MOVE, energy by DG ENER, etc.).[6]

In addition to the industrial policy actions under Horizon 2020, another action presently covered by the Competitiveness and Innovation Programme (CIP) relevant to LRAs is the ELENA programme under the Intelligent Energy Europe programme (IEE). ELENA offers funds to public bodies to develop energy investment programmes. The IEE will soon no longer exist in it is present form and it appears that its eco-innovation programmes will be shifted to the Horizon 2020 societal challenges heading 'Secure, clean and efficient energy'. It is still unclear how and in what form ELENA will continue, as it is not really an innovation programme. While the ELENA-style programmes are expected to continue and even expand, it is not possible at this stage to have a clear picture as regards under which heading these will be financed, although there is an expectation that this will be from the 'Social Change and Innovation' sub-heading.[7]

Operations under Heading 1a cannot be clearly divided into figures of funds being channelled through or benefiting LRAs. While these may be involved to a variable extent, most funds are not targeting LRAs. The present Intelligent Energy Europe programme is an exception. Roughly a third of the funds under the IEE (€730 million for the 2007-2013 period) were dedicated to actions of public authorities, all levels combined. Within the programme, ELENA is clearly an instrument benefiting local authorities and managed by them, as well as other public bodies operating locally. Under the ELENA facility, €28 million has been invested, which triggered around €1.5 billion of total investment, which would mean a leverage factor for current projects of 54. Some 18 projects with €34 million in ELENA funding are in the pipeline, amounting to investment of €2.2 billion.[8] This is why, despite the small budgetary allocation to ELENA, the impact on LRAs is substantial.

[6] Even within FP7 there have not been consolidated procedures inside the Commission (see the Court of Auditors 7 June 2013 report "Has the Commission ensured efficient implementation of the Seventh Framework Programme for Research?", Special Report 2/2013).

[7] Answers to a request by the author for clarification to the European Commission and EIB indicate that this has not yet been cleared.

[8] K. Medarova, A. Volkery, R. Sauter, I. Skinner, S. Withana and J. Núñez Ferrer (2013), "Study on the optimal use of EU grants and financial instruments in the next Multiannual Financial Framework to address the climate objective", report for DG CLIMA.

1.2 Heading 1b. Economic, social and territorial cohesion

This heading is of course of great relevance for local authorities and takes over the present 'Cohesion for Growth and Employment' heading. The components are nearly identical. Most of the budget is dedicated to the Structural Funds under shared management, which means they are generally managed by regional authorities. The exception is the nationally managed Cohesion Fund. It will be left to Member States to decide if the management of the new budget lines 'Youth Unemployment Initiative' and 'European Aid for the Most Deprived' will be conducted at national or at regional level.

Table 4: 2014 draft budget, Heading 1b. Economic, social and territorial cohesion (€ million)

	Commitment Appropriations	Payment Appropriations
Investment for growth and jobs	*44 531,6*	*48 828,5*
– ***Regional convergence (less developed regions)***	*23 332,0*	*29 802,0*
– ***Transition regions***	*4 719,9*	*288,0*
– ***Competitiveness (more developed regions)***	*7 348,2*	*7 615,0*
– ***Outermost and sparsely populated regions***	*209,1*	*13,0*
– **Cohesion fund**	8 922,4	11 110,5
o **Of which part dedicated to Connecting Europe Facility (CEF)**	983,0	p.m.
European territorial cooperation	*674,9*	*1 369,0*
Technical assistance and innovative actions	*184,9*	*133,4*
Youth Employment initiative (specific top-up allocation)	1 804,1	450,0
European Aid to the Most Deprived (FEAD)	365,1	306,0
Pilot projects and preparatory actions	p.m.	6,8
Total	47 560,6	51 093,7
Ceiling	47 583,0	

Source: European Commission, Statement of estimates of the European Commission for the financial year 2014 (Preparation of the 2014 Draft Budget), SEC(2013)370 – June 2013.

Decisions on how the Structural Funds are managed and at what level the managing authorities operate are in the hands of the individual countries. Exceptionally, the 5% of the ERDF funds (minimum level) allocated to urban development may be managed by beneficiary cities directly. How the funding will be distributed regionally is based on the agreed formulas and ultimately set

by the Partnership Agreements between the European Commission and the regions.

It is not easy to report how much of the Structural Funds in the present period of the MFF directly benefited LRAs. It would require a detailed analysis of numerous national reports. Declarations offered by the Member States are generally presented at regional level. With over 270 regions in the European Union, an overall picture would require a comprehensive review of the data. Drawing on the data for one convergence region in Italy and convergence and competitiveness regions in Wales, it is possible to offer in the subsection below a small illustration of the balance of fund distribution amongst different kinds of beneficiaries.

1.2.1 Distribution of ERDF and ESF funds Campania and Wales

The distribution of funds in the regions is illustrated in Figure 1.[9] The final beneficiaries of the European Regional Development Fund's support for the Campania Operation Programme (2007-2013) are mainly public authorities and public entities. Interestingly, municipalities have been the beneficiaries of 45% of the committed funds, regional authorities 29% and the rest, 26%, mostly public organisations (tourist boards, water management companies, etc.).[10]

Of the ESF funds, only 41% were allocated to LRAs as beneficiaries, even if most of the remaining funds were channelled to public or semi-public entities (e.g. schools, employment agencies, etc.). Of these, 20% were destined for municipalities.

An interesting region to consider is Wales in the UK, which is divided into four regions, two of them under the convergence objective and two under the competitiveness objective. The municipalities benefit little compared with the case of Campania, with the regional authorities being the main beneficiaries. For the ESF, most funds are attributed to regional authorities.[11]

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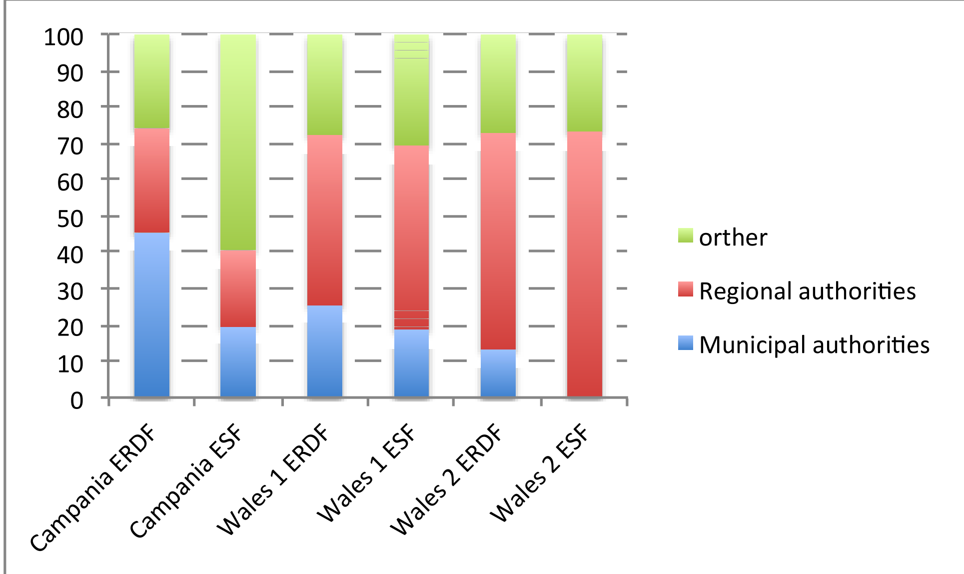
[9] By municipal and regional authorities this report understands the offices under the direct control of municipal authorities, not agencies or bodies such as municipal schools.
[10] Data sources: ERDF Campania portal (http://porfesr.regione.campania.it/it/beneficiari/elenco-beneficiari) and ESF Campania portal (http://www.fse.regione.campania.it/index.cfm?m=1&s=8&i=23).
[11] Data source: Welsh European Funding portal (http://wefo.wales.gov.uk).

Figure 1: ERDF and ESF funds Campania and Wales, 2007-2013 approved projects



Notes: Convergence regions: Campania and Wales 1; Competitiveness region: Wales 2

1.3 Heading 2. Sustainable growth: natural resources

Heading 2 is primarily composed of direct payments to farmers. Local authorities can benefit from the rural development policy to a very limited extent, but are a main target for the environmental LIFE+ programme. The LIFE+ programme will also increase in relevance now that agreement has been reached on its role in assisting local authorities in implementing climate actions and obtaining access to the necessary funds.

1.3.1 Rural development

The draft budget for 2014 does not present any detailed information on the rural development funding, except that commitment appropriations will be €13 991 million. For local authorities, the funds directed to and managed by them will depend on decisions at national level. However, municipalities are not the main targets of the policy and most of the budget (approximately 80%) is distributed to farms, food industries and other agriculture-related organisations. Some funding has been earmarked to upgrade municipal infrastructure in rural areas and for vocational training programmes managed by local services, but the funds are low in proportion to the programme. The Member States provide a breakdown by beneficiary, but in separate national websites and in their national language(s). Beneficiaries are presented by organisation name and not grouped by kind of entity, private, public, national, regional or local. Hence, any analysis at EU level is difficult to perform.

Looking at the programming summary by the Commission,[12] the magnitude of funding for the local authorities for the period 2007-2012 can be inferred by the percentage of the funds distributed by action. One can see, for example, that 3% of the funds were allocated fully for municipalities in the action for village renewal and development. Some other funds, such as basic services for the economy and population (3%) or LEADER+ (for local development 3%) can also benefit municipal authorities.

1.3.2 Heading 2. LIFE+ programme

The general objective of LIFE+ is to contribute to the implementation, updating and development of EU environmental policy and legislation and, in particular, to support the implementation of the 6th European Action Plan. Financial support under this LIFE+ should contribute to the development, implementation, monitoring and evaluation of environmental policy and legislation, as well as its communication and dissemination.
For the period 2014-2020, LIFE+ will be reinforced, although well below actual needs, but it will also develop financial instruments to increase the leveraging of funding, although these have not yet been defined. Most likely, these instruments will emulate the ELENA and JESSICA programmes but focusing on adaptation measures. The adaptation strategy of the EU mentions LIFE+ as a central financial tool for LRAs. The total budget is €2.143 billion for the whole funding period 2007-2013. For 2014-2020, funding has increased to €3 billion, divided into a sub-programme on climate action (~€800 million) and a sub-programme on the environment (~€2 200 million).

Table 5: Heading 2. LIFE + subheading

	Commitment appropriations	Payment appropriations
Environment and Climate action LIFE+	404,6	263
–Environmental policy at Union and international level	303,4	243,9
–Climate Action at EU and international level	*101,3*	*19,1*
–Decentralised agencies	41,7	41,7
TOTAL	446,3	304,7

Source: European Commission, Statement of estimates of the European Commission for the financial year 2014 (Preparation of the 2014 Draft Budget), SEC(2013)370 – June 2013.

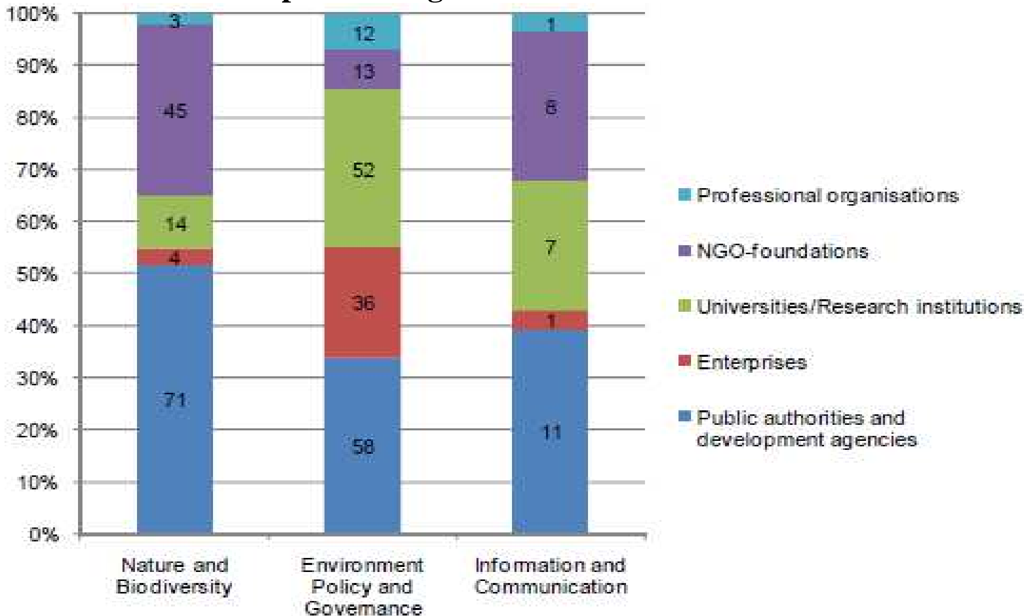
A wide range of stakeholders have benefited from LIFE+ in this programming period. Figure 7 below shows the main beneficiaries per action grant strand for 2007-2008, with approximately 40% of the appropriations going to public

[12] Source: European Commission (2013) Rural Development in the European Union - Statistical and economic information – 2012.

authorities. It is an important instrument for LRAs to comply with EU environmental and climate-related legislation and objectives.

To have a better picture of the type of public authorities that are beneficiaries of LIFE+, data for 2012 show that less than 20% are regional or local authorities. Those LRAs are divided evenly between regional authorities and municipalities. If adaptation measures for cities are going to be financed by LIFE+, the share of municipalities will most likely increase considerably. As the design of the adaptation financing for cities has not yet been decided, it is not possible to know to what extent LRAs will be direct beneficiaries of LIFE+ in the next MFF.

Figure 2: Main beneficiaries per action grant strand for 2007-2008



Source: Commission Staff working paper, Impact assessment accompanying the document on the Proposal for a Regulation on the establishment of a Programme for the Environment and Climate Action (LIFE), SEC (2011) 1541 Final.

2 The draft annual budgets, adopted budgets and the draft amending budgets

The annual budgetary procedure can be divided into three parts. The first is the European Commission's draft budget that has to be drawn up before 1 September. This is generally already presented in May/June. This budget is then scrutinised by the European Council, which adopts a position and sends it to the Parliament. Should the Parliament not adopt the Council's position, a conciliation committee is called upon to find agreement. Failure to agree requires the Commission to draft a new proposal, and the process is repeated.

Once an agreement for the annual budget has been found, there is the possibility for the Commission to propose amending budgets during implementation in response to unforeseen, exceptional or unavoidable circumstances. The amended budget will have to undergo the same process as the draft budget.

Until the 2008 crisis, annual budgets were not an issue of great controversy due to the existence of multiannual programmes. The MFF established the commitment and payment appropriations and budgetary decisions were kept close to the agreed levels. Since 2010, however, there has been a proliferation of amending budgets during the implementation year. For 2013 there are already five, which is close to one amendment per month, although 2010 saw ten of those, likely due to the redistribution of funding needed to finance the recovery package, as well as other actions to react to the worsening situations in many EU regions.

In analysing the draft amending budgets in 2011, 2012 and 2013, amendments[13] have often focused on reallocating funding or solving an excessively low payment appropriation level compared to outstanding commitments (RAL – *reste à liquider*) to be honoured in the same year. Looking back at the Commission's proposed budgets for 2011 and 2012 and the ones adopted, we see that payment appropriations have been systematically reduced by the Council, only to result subsequently in draft amending budgets to cover the shortage.

The discrepancy of actual payment requests in relation to the agreed appropriations for payments in 2012 and 2013 resulted in considerably higher payment requests (even compared to the original Commission proposal). This reflects more likely a politicisation of the annual budget due to the austerity measures rather than mistakes or disagreements on the accuracy of estimations

[13] Data from the European Commission (http://ec.europa.eu/budget/biblio/documents/index_en.cfm).

in the calculations of the RAL, either to make the EU budget appear lower or to impose pressure on the Commission to reallocate unused funding or cut expenditure where possible.

2.1 Changes between the European Commission's proposals in the annual budgets and final results for the budgetary years 2011, 2012 and 2013

This paper compares the first draft budget presented by the European Commission in the spring for the next financial year with the final budget figures recorded for the year in the next draft budget published. Draft amending budgets have been scrutinised to detect important changes.

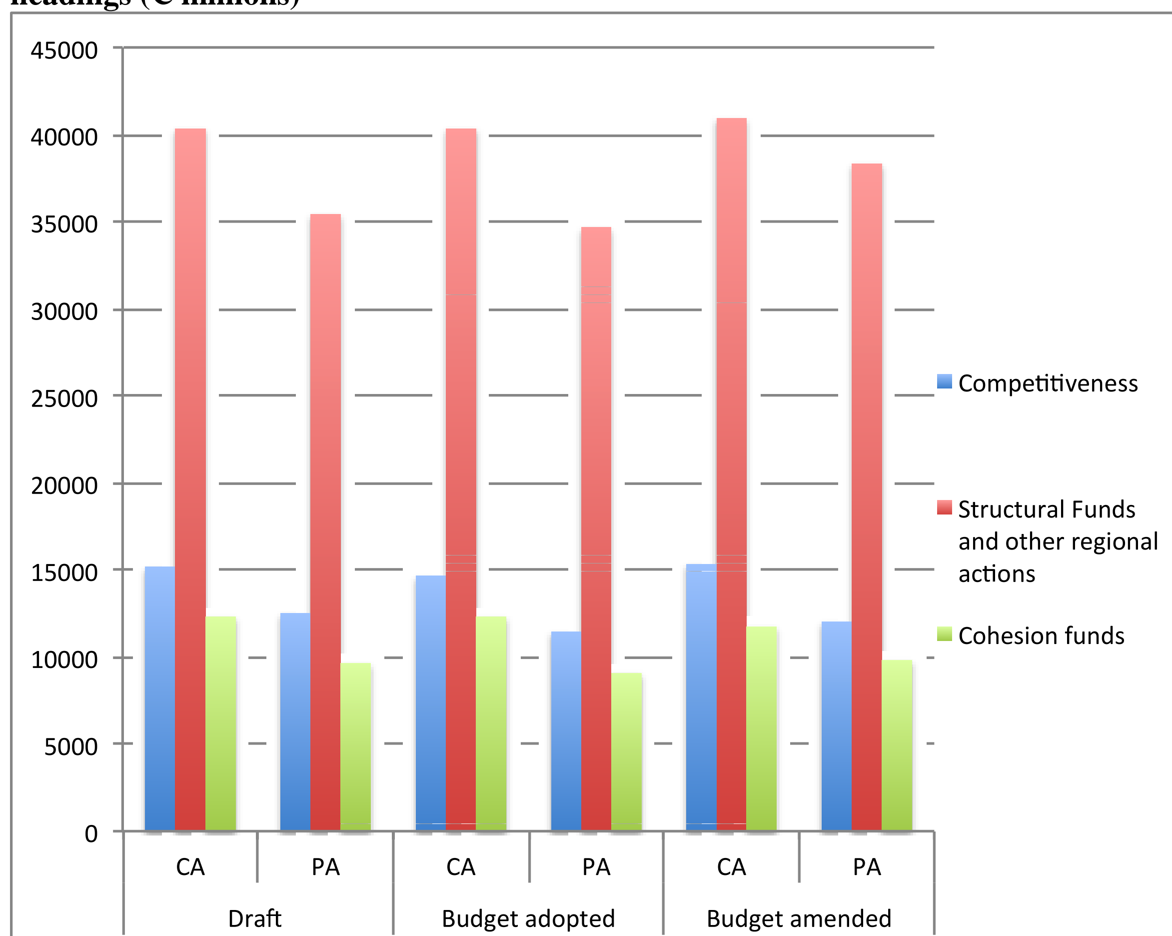
2.1.1 Changes between the draft budget and the final budget

The first interesting finding to emerge from the analysis of the budget lines is that a transfer of commitment and payment appropriations has taken place between the Natural resources heading to Headings 1a and 1b (compared to the original MFF). This is due to the impact of the CAP Health Check adopted in 2008 in reducing direct payments.

In the annual budgets, the Council and the Parliament have preserved most of the appropriations for commitments as in the MFF. Paradoxically, however, the *payment appropriations* have been systematically reduced. This pattern of unchanged or increased commitments and falling payments is repeated yearly, when comparing the annual budgets proposed by the Commission and the adopted budgets. Payment appropriations have systematically been underestimated leading to successive amendments, as commitments need eventually to be honoured.

It is also a common feature of the multiannual programmes that payment requests for the MFF accumulate from the third year of the programming period and particularly in the last quarter of each year. This is due to the programming cycle, which led to large payment claims at the end of 2011 (over €15 billion), rolling into 2012 (€10.5 billion). This was repeated in 2012 with €11.2 billion rolling over into 2013.

Figure 3: Comparison of draft budget 2012, adopted and amended, Sustainable growth headings (€ millions)



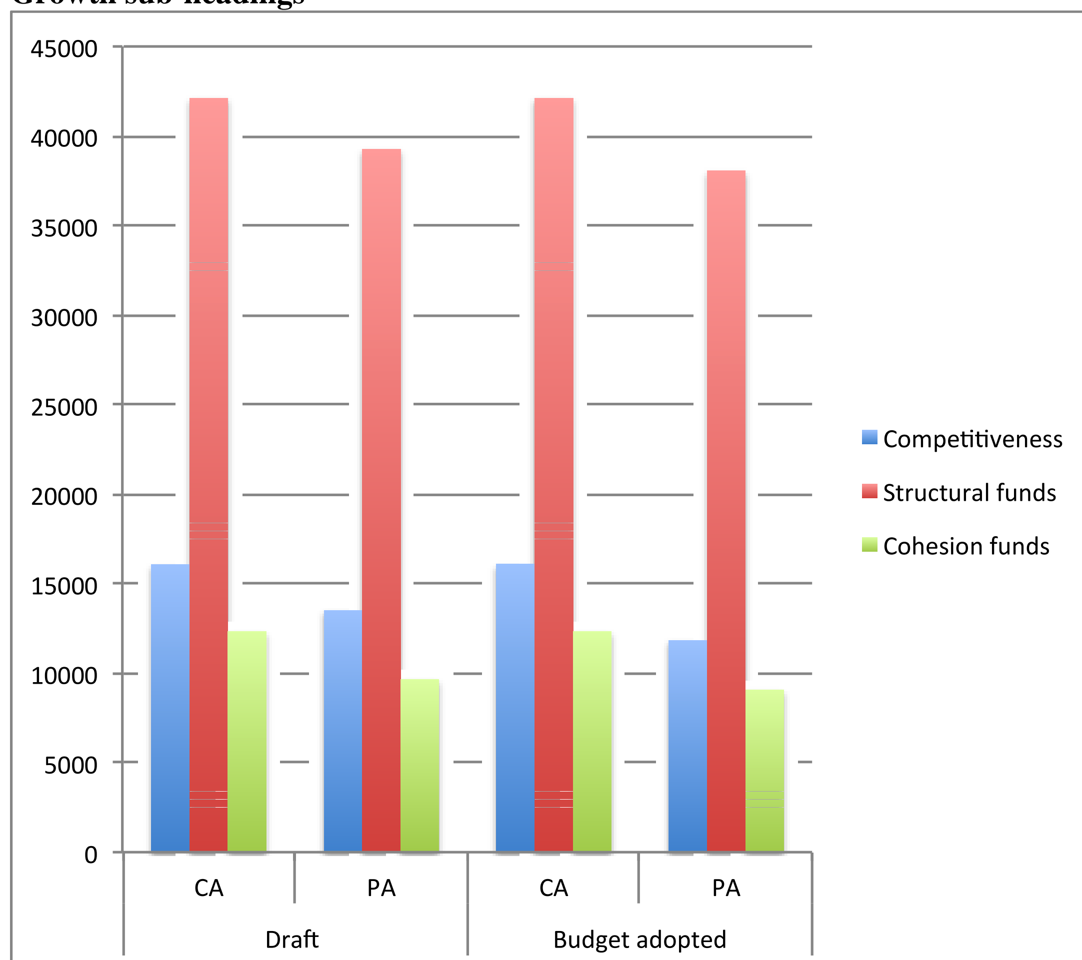
CA = Commitment appropriations; PA = Payment appropriations

Figure 8 above shows the differences between the Commission's draft budget, the adopted budget and the actual budget after six amendments during 2012. The lack of a sufficiently high allocation to appropriations for payments led to a substantial amendment of the budget in 2012. For regional policy alone, the changes in the payment appropriations exceeded €5 billion.

The lesson was not learned for 2013. In the drive towards austerity, the payment appropriations were cut back by the Council for the year 2013, making the adopted budget look cheaper (Figure 9), but leading again to a shortfall of necessary payment resources to cover commitments. Practicing this deception in the final years of a multiannual programme is unwise, as this is the period when commitments tend to accumulate for payment. Payments submitted in 2012 that rolled over to 2013 were of a magnitude of €11.2 billion.[14]

[14] European Parliament (2012), Working document on outstanding commitments (RAL) and the payments issue, Committee on Budgets, rapporteurs F. Balzani, J. La Via and J. Mulder.

Figure 4: Comparison draft budget 2013 and the adopted budget, selected Sustainable Growth sub-headings



CA = Commitment appropriations; PA = Payment appropriations

The under-provision of an appropriate level of payment appropriations is quite visible in the case of the Structural Funds. The Commission proposal of €39.4 in payment appropriations was reduced and the adopted budget totalled €37.4 billion. Today it is clear that even the Commission's estimate was too conservative and the estimated required payment appropriations have already exceeded €42 billion.

An agreement was reached in a second amendment in March, but fell short by €3.9 billion of the requested €11.2 billion. However, with the adoption of the 2014-2020 MFF, Member States pledged that they would cover all outstanding commitments and would avoid a rollover of unpaid payment appropriations to 2014. However, the ECOFIN Council of 9 July 2013 only approved €7.3 billion to cover additional appropriations, keeping the expected shortfall of €3.9 billion open.[15] It should be noted, however, that the Danish, Finnish, Dutch, Swedish and UK delegations voted against this increase.

[15] Council of the European Union, Press release of the 3252nd Council meeting, Economic and Financial affairs.

The ‘austerity drive’ in the annual EU budget process has led to a clearly dysfunctional outcome. The payment appropriations are knowingly under-budgeted by design from the start. The pressure to cut annual budgets is to a large extent a political exercise, because there is very little room for cuts in the EU budget, as most of the budget is a multiannual investment tool allocated to Member States, and payments are *binding* commitments. Any meaningful reductions in payments for the future can only be undertaken by reducing the commitment appropriations, which then lead to lower payments in later years. Commitment appropriations have, however, hardly been reduced.

It is important to point out that in this second half of the MFF, the need to cover the payment commitments has even been partially mitigated by the lower direct payments of the CAP as well as some ‘decommitments’.[16] In fact, payments are in line with the agreed MFF ceilings. If payment appropriations are systematically and unreasonably low when adopted, it leads to a forceful reallocation of funding during the year and this is not in line with the letter of the treaty and the IIA (Inter-Institutional Agreement) on reallocations, which allows this option only for unforeseen and exceptional cases. The impacts were indeed foreseen and expected.

One should also mention that the EU budget should never ‘default’ on payments, not only because of the legal obligations and internal political difficulties, but because of the potential repercussions. The European Union is increasing its reliance on capital markets to finance a number of operations. The EU borrows for its macro-financial assistance mechanisms guaranteed by the EU budget (the Balance of Payments assistance, European Financial Stability Mechanism and the Macro Financial Assistance),[17] and the EIB is backed by Member States and the EU budget. The EU budget’s AAA rating, and thus the EU’s capacity to borrow for its operations, depends on the trust borrowers place in the commitment of Member States to meet common financial challenges. Any serious undermining of the EU budget may have unintended consequences in the international financial market’s trust in the EU institutions, which may lead to higher borrowing rates. For the moment, the European Commission’s borrowing operations on behalf of the Member States are not of such a large magnitude to be affected by EU budget disputes, but the EU financial instruments are gaining in size and complexity and an erosion of confidence in the EU institutions could have serious consequences. The fact that a non-negligible number of Member States are voting against the EU fulfilling its *binding* budgetary obligations can be considered a rising threat to the EU’s credit rating and its operations.

[16] Commitments not realised under the N+2 and N+3 rules.

[17] A. Giovannini, A. Casale, J. Núñez Ferrer, P. Ivan, D. Gros and F. Peirce (2012), “The implications for the EU and national budgets of the use of EU instruments for macro-financial stability”, Report for the European Parliament, Directorate General for Internal Policies, PE 453.237, Brussels 18/06/2012.

3 LRAs and the 2014-2020 budget

The EU MFF 2014-2020 has recently been approved (27 June) and the first 'preparatory' annual draft budget for 2014 was released in parallel, but much of the accompanying regulations have not yet been finalised. Programming can only be concluded once all regulations for implementation of the funds are adopted. A number of important aspects are also not resolved, in particular the size and scope of financial instruments and the exact rules governing the funds and the possibility to 'blend' them for projects. Without clarity in those areas, the Partnership Contracts, the integrated territorial investment (ITI) plans as well as the smart specialisation strategies cannot be completed.

There is most likely going to be a considerable delay in the programming. This would not be the first time (it happened in the implementation of the last two MFFs), but will most probably be the most severe and complex case, due to the more demanding programming rules. There is a certain expectation that the start of the programming period will be near the end of 2014 with an accumulation of commitments occurring shortly after adoption of the programmes. This will nevertheless result in a risk that regions fail to commit much of the funds in time, requiring a redistribution of uncommitted funds to subsequent years. This will mean a very complex budgetary negotiation for 2015 and possibly necessitate a difficult adjustment of the MFF.

In addition, one can foresee a growing problem with the RAL. In 2014, 2015 and 2016, the EU budget will pay the lion's share of the programmes closing from the 2007-2014 programming period, while the 2014-2020 commitment appropriations will require increasing payments from the year 2016 onwards. The rules for the MFF approved for the 2014-2020 period indicate that some serious RAL problems may appear from 2016 onwards, which may trigger the need for funding reallocation and even a cut in the yearly planned payment appropriations (that in turn will increase the RAL at the end of the year).

The RAL legacy of this MFF for the next MFF is large. It is expected to reach €230-250 billion by the end of 2013, of which €70 billion is expected to be paid out in 2013. This means a residual of €160 to €180 billion would have to be paid out in 2015 and 2016. This is equivalent to approximately one half of the EU budget in 2016, kicking in simultaneously with the payment claims accumulating from 2014. The Council has partially understood the risks of RAL disputes under strict ceilings and has agreed for the 2014-2020 MFF that payment appropriations will be adapted freely to needs (as long as the MFF ceilings are not breached).[18] From 2018 onwards, however, the increases of

[18] The elements of the agreement can be found in http://europa.eu/rapid/press-release_MEMO-13-625_en.htm.

payment appropriations will be limited to €7 billion in 2018, €9 billion in 2019 and €10 billion in 2020. Any amount exceeding these limits will have to be recovered from the original payment ceiling through a reallocation of unused margins and cuts. This is risky for LRAs, as those are the years where the payments from the programmes accumulate.

The year 2016 will be especially risky for LRAs, as this is the year when the payments from the programmes started in the second and third years of the MFF will accumulate, combined with the final payments of the RAL of the present MFF. In addition, it coincides with a budgetary mid-term review that the Commission has been formally requested to carry out, including the drafting of legislative proposals for reform. The CoR will have to be careful, as such a review may lead to effective cuts in the budget if the payment appropriations are expected to grow beyond the permitted amounts. The biggest risk is that with a late programming start, a considerable number of regions may still encounter absorption capacity problems in 2016. This has been a common feature at the beginning of the multiannual programmes and may lead to a permanent reallocation of the unused margins away from the regions in the budget review.

4 Recommendations for the CoR

The Committee of the Regions has limited direct influence in the annual budget negotiations, as well as on the Multiannual Financial Framework. However, local and regional authorities are the quintessential partners in budget implementation and constitute the level of government that is closest to the citizens. The complex processes involved in setting and implementing the EU budget are of significant importance to the CoR for the following reasons:

- The European Commission has not yet fully designed the implementation rules for a number of funding lines, some of which have repercussions on LRAs. There is a strong opportunity to contribute to the design of the mechanisms, in particular:
  - The growing interlinkage between headings such as Horizon 2020 and the Structural Funds for large industrial demonstration and deployment projects, in which LRAs are heavily involved.
  - The use of financial instruments, such as LIFE+ for adaptation, or ELENA for energy efficiency.

- The CoR should carefully analyse the impact that a slow programming start and absorption of funds may have on the mid-term review of the MFF planned for 2016. Low absorption and an accumulation of the RAL could endanger the funding allocated to the Structural Funds. The motivation and thus the objective of the mid-term review may be very different from the one performed under the present MFF. It could be used to reduce or reallocate funding that is not absorbed – actions that could affect LRAs. With the slow start of this programming period, it is likely that the RAL and absorption difficulties will be considerable in 2016.

- For the next MFF, it was agreed that the flexibility between headings will be enhanced. Local authorities may be the main affected parties from any increase in flexibility for the reasons highlighted above. The CoR needs to develop the capacity to monitor the implementation of the EU budget and be able to react in a timely fashion to funding reallocation decisions to avoid the situation whereby important headings are reduced during programming on the basis of common initial absorption problems.

- The image of the EU budget is deteriorating at national level. A number of Member State governments are using the annual budget to lobby for funding cuts and reallocations. The Structural Funds are one of the most vulnerable funding instruments. LRAs and CoR representatives should be more active in conveying a clearer picture of the benefits for citizens of

EU funds in their region, as well in urging central government to take a more responsible approach to the EU budget. The present view of the budget as a mere cost to Member States by central governments can be detrimental to beneficiaries at lower levels of government.