Budgetary principles

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Community budgetary law obeys general principles which are largely based on those that apply in national budgetary law. They are enshrined in the Treaty establishing the European Community (EC) and are developed, adapted and, in some cases, relaxed in Council Regulation No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities. The principles in question are those of unity, universality, annuality and specification — seen as the four main traditional budgetary principles — plus the principles of equilibrium, unit of account, budget accuracy, sound financial management and transparency.

The principles of unity and budget accuracy

The principles of unity and budget accuracy mean that, for every financial year, all revenue and expenditure of the Communities, together with that of the Union — where expenditure is chargeable to the budget — must be entered in a **single document**: the **budget**. More particularly, the principle of budget accuracy enshrined in Council Regulation No 1605/2002 requires that all Community revenue and expenditure must be booked to a budget heading and that no expenditure may be incurred in excess of the authorised appropriations. These principles allow effective monitoring of the conditions in which Community resources are used (see Article 268 of the EC Treaty and Articles 4 and 5 of Council Regulation No 1605/2002).

Although the Treaty establishing the European Economic Community (EEC) of 25 March 1957 lays down the principle of unity (Article 199), there has not always been a single budget (*the general Community budget*). In the early years of European integration, there were five different budgets: the *general* budget of the *EEC*, the *operating* and *research and investment* budgets of the European Atomic Energy Community (*EAEC*), and the *administrative* and *operating* budgets of the European Coal and Steel Community (*ECSC*). Major progress towards a single budget was made with the Treaty of 8 April 1965 establishing a Single Council and a Single Commission of the European Communities and with the first Treaty of 22 April 1970 amending certain budgetary provisions of earlier treaties which allowed the number of different budgets to be reduced, first to three, then to two. On 23 July 2002, following the expiry of the ECSC Treaty, the ECSC operating budget disappeared, and the corresponding operations were incorporated into the only remaining budget, the general Community budget.

In addition, there are also cases where the principle of unity is **stretched**. Some of the Union's financial activities are not entered in the general budget. This is true of *certain operating expenditure* committed in connection with the *common foreign and security policy* (CFSP) and as part of *police and judicial cooperation in criminal matters* (PJCC). While administrative expenditure incurred in these areas is entered in the general budget, operating expenditure is charged to the European Communities budget, except for expenditure relating to operations with military implications or in the defence field and instances where the Council has unanimously decided otherwise (Articles 28 and 41 of the Treaty on European Union (EU) and Article 4(2) of Council Regulation No 1605/2002). Nor are *borrowing and lending operations* included in the budget, but the guarantee for borrowing and lending operations entered into by the Communities (EC and EAEC) is entered in the general budget. Similarly, revenue and expenditure of the *European Development Fund* (EDF) — the financial instrument for Community cooperation with the African, Caribbean and Pacific States — are implemented outside the budget. The financial activities of the *European Investment Bank* (EIB) are not included in the budget because of its legal personality and financial independence. Lastly, some of the Community's decentralised bodies (*European agencies*) have their own budgets, but these budgets are not, strictly speaking, an exception to the unity rule in that their resources come from a subsidy entered in the general Community budget.

The principle of universality

The principle of universality means that *the total revenue in the budget must cover the total expenditure*. In other words, the revenue in the budget constitutes a common fund which is used to finance all expenditure without distinction. This principle encompasses two important budget rules (Article 17 of Council Regulation No 1605/2002). The first is that budget revenue must not be assigned to specific expenditure, known as the **non-assignment rule**. The second is that there cannot be any adjustment of revenue and expenditure against each other: they must both be entered in full in the budget without being set off against each other. This is the **gross budget principle**.

The **non-assignment rule**, already enshrined in the Decision of 21 April 1970 establishing the Communities' own resources (Article 5), nevertheless allows exceptions, for example financial contributions from the Member States to finance certain research programmes, or contributions to certain Community programmes from applicant countries (Article 18 of Council Regulation No 1605/2002). Furthermore, the ECSC operating budget — which has disappeared since the ECSC Treaty expired — from the very outset allowed levies to be assigned to expenditure.

The **gross budget principle** also allows a few exceptions, but these are mainly technical and are designed to simplify procedures (Article 20 of Council Regulation No 1605/2002).

The principle of annuality

The principle of annuality, which is designed to make it easier for the budgetary authority (Parliament and Council) to monitor the executive body's activities, requires all budgetary operations to be attached to one financial year. This means that the Community's revenue and expenditure are *estimated* for each financial year, and the *implementation* of expenditure is authorised for one financial year, which coincides with the *calendar year*, starting on 1 January and ending on 31 December (Articles 268, 271 and 272 of the EC Treaty and Articles 4(1) and 6 of Council Regulation No 1605/2002).

However, like national budgetary law, many of the operations financed from the Community budget and adopted during a given calendar year are actually carried out over a number of years (research programmes, structural measures, etc.). In order to reconcile the principle of annuality with the multiannual nature of certain operations, the budget includes **differentiated appropriations —** as compared with non-differentiated appropriations **—** which are divided into **commitment appropriations** and **payment appropriations** (Article 7 of Council Regulation No 1605/2002). **Non-differentiated appropriations** are those where commitments and payments are the same. In practice, they include administrative expenditure, repayments to Member States, EAGGF expenditure (European Agricultural Guidance and Guarantee Fund, Guarantee Section), and guarantees for loans, all categories of expenditure for which there is, by their very nature, no time-lag between the legal commitment of the expenditure and its payment. The expenditure is, therefore, approved and effected within a single financial year. **Differentiated appropriations**, on the other hand, are those where commitments and payments are separated in order to take account of the unavoidable time-lag in carrying out the operations (structural measures, internal policies and external measures, in the main). Differentiated appropriations are broken down into commitment appropriations and payment appropriations (Article 176(1) of the EAEC Treaty, given more general application by Article 7 of Council Regulation No 1605/2002). **Commitment appropriations** cover the total cost of the legal commitments entered into in one calendar year in respect of measures which are to be carried out over more than one financial year. **Payment appropriations** are the appropriations required to cover expenditure arising from commitments entered into in the current financial year and/or earlier financial years.

In order to take account of certain budgetary constraints and to enable the budget to be managed more flexibly, the system of **carry-over of appropriations** (Article 271 of the EC Treaty and Article 9 of Council Regulation No 1605/2002) allows for certain adjustments to be made to the principle of annuality. With regard to *differentiated appropriations*, appropriations which have not been used at the end of the financial year for which they were entered are generally cancelled, but they may, exceptionally, be carried over to the budget for the following financial year in accordance with the rules laid down in the Financial Regulation. For *non-differentiated appropriations*, appropriations corresponding to obligations duly contracted at the end of the financial year are carried over automatically to the following financial year only (Article 9 of Council Regulation No 1605/2002). As for revenue, any surplus remaining from the total expenditure effected in a financial year is carried over to the following financial year (Article 10 of Council Regulation No 1605/2002).

The principle of specification

Under the principle of specification, *each appropriation must have a particular intended use and be earmarked for a specific purpose* in order to prevent any confusion between the various appropriations either when they are authorised or when they are implemented. The budgetary authority (Parliament and Council) may therefore be certain that the expenditure that it has authorised is implemented for the purpose for which it was intended. The same principle also applies to revenue and requires the various sources of revenue paid into the Community budget to be identified precisely (third and fourth paragraphs of Article 271 of the EC Treaty and Article 21 of Council Regulation No 1605/2002).

The principle of specification requires a **budgetary nomenclature** covering all Community revenue and expenditure. The budget is, therefore, structured in two ways. The first, horizontal structure separates the *general statement of revenue and expenditure* from the *sections*, which are themselves divided into statements of revenue and expenditure for each institution or body created by the Treaty. The second, vertical structure is broken down by the type or purpose of the appropriations into *sections*, *titles*, *chapters*, *articles* and *items* (Article 21 of Council Regulation No 1605/2002). The specification rule means that expenditure must be itemised for each chapter, and it is in the *chapters* that the benefits of the principle of specification may be seen (third paragraph of Article 271 of the EC Treaty and Article 21 of Council Regulation No 1605/2002).

In order to correct inaccuracies in the budget estimates and to optimise the management of appropriations authorised for a financial year, it is often necessary to apply the technique of **transfer of appropriations**. This technique, which is seen as a relaxation of the principle of specification, involves transferring appropriations from one budget line to another — transferring them from title to title, chapter to chapter and article to article. The Financial Regulation sets out the conditions for the making of such transfers of appropriations. An institution may make transfers as of right (as is the case with the Commission), or the budgetary authority may need to be informed of them in advance or to take a decision on them (Article 274 of the EC Treaty and Articles 22–24 of Council Regulation No 1605/2002).

The inclusion of **reserves** in the budget is a departure from the principle of specification in that they are not earmarked for a particular purpose. Reserves are used because the procedure for initiating a measure may sometimes not have been defined in full at the time when the budget is adopted, or else the appropriations authorised may need to be increased during a financial year in order to deal with unforeseen circumstances. The Financial Regulation provides for three types of reserves: *provisions*, *a negative reserve*, and *a reserve for emergency aid for third countries and a reserve relating to Community loans and loan guarantees to third countries* (Articles 43–45 of Council Regulation No 1605/2002). However, these reserves may be used only following a transfer procedure, so the principle of specification comes back into play then.

The principle of equilibrium

The principle of equilibrium means that the budget must include the *same amount of revenue and expenditure*. The total amount of Community expenditure is, therefore, capped by the limit of its own resources. This principle is peculiar to the Community budget, because, unlike the situation in the Member States, if the Community does not have sufficient resources, it may not borrow to cover its expenditure (Article 268 of the EC Treaty, Article 14 of Council Regulation No 1605/2002 and successive decisions on own resources). It reflects the Member States' concern to keep the Community budget under control in order to avoid having to make up any shortfall later.

However, sometimes the budget estimates, which are adopted at the same time as the budget, do not correspond to the budget actually implemented, and a surplus is left over. This surplus, which is the direct result of the principle of equilibrium and is the difference between the revenue collected and the expenditure effected, cannot be placed in a reserve and must therefore be entered in the budget for the following financial year by means of an *amending budget*. Where the balance is positive (surplus), it is entered on the revenue side. Conversely, where it is negative (deficit), it is entered on the expenditure side, though this hypothetical case is exceptional (Article 15 of Council Regulation No 1605/2002).

The situation of having a surplus is quite usual in the Community budget, and so a **negative reserve** mechanism has been introduced. Even if this mechanism is, in principle, a breach of the equilibrium rule, it nevertheless indirectly helps to keep the budget in balance. It consists of financing new expenditure by assuming that savings will be made during a financial year, even though the items likely to generate these savings cannot be identified when the budget is adopted (Article 44 of Council Regulation No 1605/2002). This reserve, represented by a negative amount entered in the budget, should be filled during the year by transfers from budget lines where a surplus has appeared.

For the ECSC operating budget, which disappeared when the ECSC Treaty expired on 23 July 2002, the equilibrium rule was watered down and applied over a number of years, thereby allowing for annual imbalances.

The principle of unit of account

According to this principle, the Communities' general budget is to be expressed in *units of account* (Article 277 of the EC Treaty, Article 181 of the ECSC Treaty and Article 16 of Council Regulation No 1605/2002).

From the time when it was established in 1952, the ECSC budget was expressed in *units of account* that were separate from each of the Member States' currencies (Article 2 of ECSC Decision No 3-52 of 23 December 1952). The unit of account used was that of the European Payments Union, the **American dollar**. The Treaties of 25 March 1957 establishing the EEC and the EAEC also provided for the Communities' budget to be expressed in units of account that were separate from each of the national currencies (Article 207 of the EC Treaty and Article 181 of the EAEC Treaty). From 1958 to 1960, however, pending the implementation of the provisions of the Treaties, the EEC and EAEC budgets were drawn up in **Belgian francs**. The ECSC budget, on the other hand, was drawn up from 1958 in a '**gold parity**' unit of account defined by a fixed weight of gold, in accordance with the Bretton Woods Agreements. From 1961, this 'gold parity' unit was extended to the EEC and the EAEC. In 1978, in the hope of greater monetary stability, the 'gold parity' unit was replaced by a unit of account based on a basket of European currencies. This **European Unit of Account** (**EUA**) corresponded to a weighted average of the values of the Member States' currencies (see Article 10 of the Financial Regulation of 21 December 1977). In 1981, the **ecu** became the unit of account for the Community budget (see Article 10 of the Financial Regulation of 21 December 1977, as amended by the Financial Regulation of 16 December 1980). Like the EUA, the ecu was based on a basket of European currencies, but, unlike the EUA, its composition could be regularly revised. Since 1999, with the establishment of Economic and Monetary Union, the **euro** has been the single currency and has been adopted as the unit of account for the Communities' general budget. The euro is the unit of account for the establishment and implementation of the Community budget and for the presentation of the accounts (Article 16 of Council Regulation No 1605/2002).

The principle of sound financial management and transparency

The **principle of sound financial management** enshrined in Council Regulation No 1605/2002 requires budget appropriations to be used in accordance with the principles of *economy*, *efficiency* and *effectiveness*. The principle of *economy* requires that the resources used by the institution for the pursuit of its activities should be made available in due time, in appropriate quantity and quality and at the best price. The principle of *efficiency* is concerned with the optimum relationship between resources employed and results achieved. The principle of *effectiveness* is concerned with attaining the specific objectives set and achieving the intended results. The application of the principle of sound financial management is based on the definition of *specific objectives* that are measurable, achievable, relevant and timed for all sectors of activity. The attainment of these objectives is monitored by performance indicators in order to move from resource-led management to result-led management (Article 27 of Council Regulation No 1605/2002, and see also Article 274 of the EC Treaty). Any proposal submitted to the legislative authority which may have an impact on the budget must be accompanied by a financial statement and an *ex ante* evaluation (Article 28 of Council Regulation No 1605/2002, and see also Article 274 of the EC Treaty).

The **principle of transparency** enshrined in Council Regulation No 1605/2002 must be respected at every stage of the budgetary cycle, from its *establishment* and *implementation* to the *presentation of accounts*. One effect of this principle is that the budget, the amending budgets, the consolidated financial statements and the financial management reports drawn up by each institution are all published in the *Official Journal of the European Union* (Article 29 of Council Regulation No 1605/2002).