



HOUSE OF LORDS

European Union Committee

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20th Report of Session 2008–09

# The EC Budget 2010

Report with Evidence

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The European Union Committee of the House of Lords considers EU documents and other matters relating to the EU in advance of decisions being taken on them in Brussels. It does this in order to influence the Government's position in negotiations, and to hold them to account for their actions at EU level.

The Government are required to deposit EU documents in Parliament, and to produce within two weeks an Explanatory Memorandum setting out the implications for the UK. The Committee examines these documents, and 'holds under scrutiny' any about which it has concerns, entering into correspondence with the relevant Minister until satisfied. Letters must be answered within two weeks. Under the 'scrutiny reserve resolution', the Government may not agree in the EU Council of Ministers to any proposal still held under scrutiny; reasons must be given for any breach.

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The Members of the Sub-Committee which conducted this inquiry are listed in Appendix 1.

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NOTE: References in the text of the report are as follows:  
(Q) refers to a question in oral evidence  
(p) refers to a page of written evidence

## **SUMMARY**

This report informs the House about the Commission's proposals for the 2010 General Budget of the European Communities. The report summarises the significant proposed changes to funding under each of the budget headings. We have been aided in this by oral evidence from the Economic Secretary to HM Treasury (Ian Pearson MP) and a written Explanatory Memorandum from HM Treasury.

This is the fourth budget to be drawn up under the current Financial Perspective, the agreement which sets spending ceilings over a seven year period. The Commission has stated that the budget aims to aid economic recovery. However, the EU's relatively small budget limits its potential to contribute to stimulus efforts, and the system of multi-year ceilings, though useful for discipline and stability, inevitably reduces flexibility. In the report, we also express concerns over the size of the margin—the difference between the Financial Perspective ceiling and proposed spending levels—under Heading 1a (competitiveness and growth), which is not currently big enough to accommodate spending as part of the European Economy Recovery Plan and other unforeseen expenditures.

We have also briefly considered the large proportion of the budget which is spent on agriculture. We conclude that it is disappointing in the context of the financial crisis that this proportion remains so large. We do however welcome the efforts of the Government to reallocate unspent funds under Heading 2 (natural resources) to Heading 1a (growth and employment).

We have also briefly considered the forthcoming budget review, which is due to be published before the end of 2009. We look forward to scrutinising this document on its publication.

# The EC Budget 2010

## THE 2010 PRELIMINARY DRAFT BUDGET

1. The Committee has scrutinised the EC Budget annually since 2004 on the basis of oral evidence provided by the Government before the First Reading of the Preliminary Budget in the European Council. The Committee decided in the last Parliament that taking evidence from the Government at an early stage in the budgetary process was the most effective way in which we could fulfil our parliamentary obligation to scrutinise proposed EU legislation and so ensure greater accountability and transparency.<sup>1</sup>
2. HM Treasury provided an Explanatory Memorandum on the Preliminary Draft Budget (PDB) on 11 June; on the basis of this document we took oral evidence from the Economic Secretary to the Treasury, Ian Pearson MP, on 30 June. Both the Explanatory Memorandum and the transcript of oral evidence are printed with this report. As this report was published after the First Reading of the Preliminary Budget on 10 July, we expressed our views to the Minister in a letter of 8 July, which is published in Appendix 2 of this report.
3. The annual EC Budget is largely determined by the previously agreed Financial Perspective. Despite this, scrutiny of the annual EC Budget plays an important part in making the budgetary process in the EU more transparent. Accordingly, the aim of the Committee's annual report on the Budget is to inform the House of the issues relating to the Budget and to scrutinise the Government's position on the Commission's Preliminary Draft Budget. Scrutiny of the Government's position is particularly important given that the UK is a net contributor to the EC Budget. We will continue to consider the Budget until it is adopted and also any Preliminary Draft Amending Budget presented by the Commission.
4. This report was prepared by Sub-Committee A, whose Members are listed in Appendix 1. A guide to the annual European budget procedure and a glossary are presented in Appendix 3 and 5 respectively. **We make this report to the House for information.**
5. Spending in the annual EC Budget is divided into eight categories under six Headings, which are pre-determined by the multi-annual Financial Perspective:
  - (1) Sustainable growth:
    - (a) Competitiveness for growth and employment;
    - (b) Cohesion for growth and employment;
  - (2) Preservation and management of natural resources;
  - (3) Citizenship, freedom, security and justice:
    - (a) Freedom, security and justice;
    - (b) Citizenship;

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<sup>1</sup> European Union Committee, 1st Report (2002–03): *Review of Scrutiny of European Legislation* (HL 15).

- (4) The EU as a global player;
- (5) Administration; and
- (6) Compensation.

No funding has been allocated to Heading 6 in the 2010 EC Budget.

- 6. The current Financial Perspective runs from 2007 to 2013, making the 2010 Budget the fourth under the current Perspective. This agreement between the European Council, the Commission and the European Parliament provides the financial framework for the EC for seven years, setting a ceiling for total EC expenditure over the seven years and annual ceilings for each expenditure Heading. Total EC expenditure is defined in terms of a percentage of EU Gross National Income (GNI).

### **BOX 1**

#### **Commitment and Payment appropriations**

The Preliminary Draft Budget makes a distinction between commitment and payment appropriations.

*Commitment appropriations* are the total cost of legal obligations which can be entered into during the current year, for activities which will lead to payments in the current and future years.

*Payment appropriations* are actual transfers of cash from the Community Budget to creditors during the current year, resulting from commitments made in the current or previous years.

#### **Total appropriations**

- 7. The PDB proposes commitment appropriations in 2010 of €138,564 million or 1.18% of EU GNI, an overall increase of 1.5% compared to 2009. For the entire budget there is a margin of €1,754 million below the Financial Perspective ceiling for 2010. The PDB allocates total payment appropriations of €122,322 million, an increase of 5.3% compared to 2009. This leaves a margin of €12,162 million below the Financial Perspective ceiling. A full table of commitment appropriations and payments can be found in Table 1. The Minister told us that this increase was in line with that outlined in the Financial Perspective for 2010 (Q 21).
- 8. In his Explanatory Memorandum, the Minister argued that the PDB had insufficient margins to accommodate the commitments already agreed as part of the European Economic Recovery Plan (see below), but not allocated funding within the Budget. Foreseen external action requirements in Palestine and Kosovo, and further unforeseen requirements will also need to be incorporated within the margin (p 5). The Minister told us that the Government would argue for increased margins across all Headings, but with particular focus on Headings 1a, 3 and 4. He said that the ability to finance the Economic Recovery Plan using the budget margins has shown their importance, but he noted that there were disagreements between Member States over how big these margins needed to be (QQ 31–32). He explained that the margins enabled a disciplined approach to the budget, so that unexpected events can be dealt with, without needing revision of Financial Perspective ceilings (Q 8).

9. **We agree that a sufficient margin under Heading 1a must be maintained under the Financial Perspective ceiling to ensure that unforeseen commitments and the European Economic Recovery Plan can be accommodated. We agree with the Government that the margin allowed by the Preliminary Draft Budget is likely to be insufficient.** To increase the margin, appropriations have to be reduced under Headings 1a, given that the ceiling is fixed. Where relevant we comment below on commitments and appropriations that should be reduced to allow for an increased margin.

### **The European Economic Recovery Plan**

10. The Minister explained in the Explanatory Memorandum that in March 2009 additional funding of €5,000 million outside the 2009 Budget was agreed to fund broadband and energy efficiency infrastructure projects as part of the European Economic Recovery Plan (EERP). Of this, €2,600 million was committed from the 2009 Budget and €2,400 million will be committed from the 2010 Budget, allocated from the Heading margins. The 2009 Budget has been updated to include these commitment appropriations and payments, whereas the 2010 PDB does not yet include these appropriations (p 1). Comparisons between 2009 and 2010 figures are therefore not always accurate. We refer to this in the report where appropriate.
11. The Minister told us that the €2,600 million allocated to EERP projects in the 2009 Budget was partly funded using excess funds for agricultural projects under Heading 2 (QQ 8–9). Of the €5,000 million total, €1,020 million will go toward broadband infrastructure and CAP health check projects and €3,980 million towards energy infrastructure projects. The financing for the €1,020 million allocation will come exclusively from Heading 2, €600 million of which will be covered by the existing 2009 Heading 2 margin. Financing for the energy projects in 2009 will come from an increase to the Heading 1a margin of €2,000 million offset by a corresponding decrease in the Heading 2 margin. Excess funding originally allocated for agriculture projects is therefore being used to fund the EERP.
12. The Commission describe the 2010 Budget as an “instrument of economic recovery.” The Minister emphasised increased spending under Heading 1a and the provision of extra funding for core tools to aid recovery (such as the European Globalisation Adjustment Fund as well as EERP projects) as examples of how the PDB fulfils this claim (Q 4). He welcomed the increases in these areas and said that he was “confident that this can play a part” in stimulating the economy (Q 7). In particular he praised the energy projects which form part of the EERP, such as development of carbon capture and storage, which he believed should remain a key priority at both Member State and EU level (Q 21). He acknowledged that many of these projects would only have a significant impact in the long term, but argued that the Recovery Plan should contain a mix of short-term stimuli and longer-term projects that will benefit the EU after the recession. He said that the EERP should have policies “that provide real assistance, support jobs and employment now” whilst ensuring that there is a longer-term “forward facing agenda”. He concluded that “essentially that means spending less on the Common Agricultural Policy and more on competitiveness, growth and jobs” (Q 14).

13. The Minister argued that it was correct to fund the EERP through the existing budget margins, as this allowed the use of funds from Heading 2, under which funds for the Common Agricultural Policy are allocated. He described agricultural spending as poor value-for-money for the EU taxpayer (Q 12). He said that spending under Heading 2 distorted markets and did not support a prosperous EU and argued that the Budget “could do more” to aid economic recovery by further reducing spending under this Heading and increasing spending under Heading 1 (Q 3). He described it as “curiously bizarre” that the EU is still spending a significant proportion of the Budget on agriculture when Europe is focused on climate change and the economic crisis (Q 19).
14. He argued that in some respects the operating mechanisms of the Budget forced the use of margins to fund the EERP as there is no provision within the Budget to react to unexpected events (Q 10). He agreed that seven-year budgeting through the multi-annual Financial Perspective makes it harder for the Budget to be adjusted to respond to a crisis and admitted “privately I might have some sympathy” for a zero-based budgeting system.<sup>2</sup> He commented that the Financial Perspective remains a key tool for budgetary discipline, but added that the system does need a “fundamental review”. He said that “until we reshape and modernise the EU Budget overall I think its ability to effectively support a prosperous EU is limited”. However, he did note that the Budget was just one of many tools the EU had to respond to the economic crisis along with coordination of Member State action (QQ 3–4). We discuss this further in the section on the Budget Review below.
15. The economic crisis has created a need to focus the budget on aiding economic recovery, which the Commission has recognised. **We support the Commission’s attempts to focus the Preliminary Draft Budget on economic recovery. However, the EU’s relatively small budget limits its potential to contribute to stimulus efforts, and the system of multi-year ceilings, though useful for discipline and stability, inevitably reduces flexibility.<sup>3</sup> In the light of the recession the distribution of the Budget in favour of agriculture is deeply frustrating.**

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<sup>2</sup> This budgeting system reviews all departmental spending annually, and all expenditure must be approved, rather than only approving increases to spending.

<sup>3</sup> The Committee commented on the length of the multi-annual financial programmes in its Report *Future Financing of the European Union* (European Union Committee, 6th Report (2004-05) HL 62).

































