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THE EUROPEAN UNION**

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NOTE

from :	General Secretariat of the Council
to :	Permanent Representatives Committee
No. prev. doc.:	9626/1/11 REV 1 FIN 286 CODEC 730 + ADD 1
No. Cion prop.:	5129/11 FIN 5 CODEC 21 - COM(2010) 815 final
Subject :	Proposal for a Regulation of the European Parliament and of the Council on the financial rules applicable to the annual budget of the Union (first reading)

1. On 6 January 2011, the Commission submitted to the Council a proposal for a Regulation of the European Parliament and of the Council on the financial rules applicable to the annual budget of the Union, based on Article 322 TFEU (ordinary legislative procedure)¹.
2. Following the examination of the Commission proposal by the Budget Committee at several meetings from February until May 2011, the Permanent Representatives Committee held, on 25 May 2011, an orientation debate on some outstanding issues² and, on the basis of the text recorded in document 9626/1/11 REV 1 ADD 1, entrusted the Presidency with a mandate to establish contacts with the European Parliament.

¹ The Court of Auditors delivered its opinions on 21 October 2010 and 25 January 2011 (Docs. 6552/11 FIN 82 CODEC 229 and 6553/11 FIN 83 CODEC 230).

² These related to: shared management (Article 56), financial instruments (Articles 130 and 131), EU Trust Funds for external actions (Article 178) and expenditure related to building projects (Article 195). Additionally, the Commission had specific concerns, particularly on the provisions related to Commission transfers (Article 23).

3. On 26 October 2011, the European Parliament voted 281 amendments to the Commission proposal but did not adopt a legislative resolution, thus leaving open the possibility for a single reading agreement.
4. Since then, several informal trilogues have taken place, during which a provisional agreement could be reached on a very large part of the text, as recorded in the Addendum.
5. However, as the political trilogue held on 9 May 2012 confirmed, some important divergences remain between the European Parliament, the Council and the Commission. These relate to the provisions on:
 - (a) discharge (*Articles 156, 157, 158*);
 - (b) powers and duties of the internal auditor (transmission of audit reports) (*Article 93(4)*);
 - (c) MFF-related issues (*Articles 9 and 9a: Cancellation and carry-over of unused appropriations; Articles 15 and 15a: Balance from financial year, Reserve for payments and commitments; Article 49: Compliance of Union acts with the budget*);
 - (d) EDF-related issues (*Article 4(2)(b) and Article 46(1)(ea)*);
 - (e) rules applicable in case of late adoption of the budget (*Article 13*);
 - (f) assigned revenue – treatment of other fines and out of court settlements (*Article 18(2)(ea)*);
 - (g) transfers (*Articles 23(3)*);
 - (h) publication of budgets, accounts and reports (*Article 30(2)*) and obligations of the Member States stemming from the adoption of the budget (*Article 37*);
 - (i) shared management with Member States (*Article 56, in connection with Articles 57 (indirect management) and 77 (Rules on recovery)*);
 - (j) VAT as an eligible cost (*Article 117a(3)(c)*);
 - (k) financial instruments – earmarking of reflows (*Article 131(5) and Article 18(3)(h)*);
 - (l) EU multi-donor trust funds for external actions (*Article 178*);
 - (m) expenditure related to building projects (loans and assigned revenue) (*Article 195(8), Article 18(3)(f) and Article 14*);
 - (n) delegated act (*Articles 199, 202, 203 and 204*).

6. These outstanding issues are on the agenda of the next political trilogue scheduled on 1 June 2012.
7. After the political trilogue of 9 May 2012, a draft Presidency proposal was submitted to the Budget Committee. This proposal, while maintaining the same position as in the previous negotiation mandate on issues listed under (a), (c), (d) and (h) of point 5 above, aimed at creating the necessary margin of manoeuvre to tackle the other issues.
8. Following its examination by the Budget Committee on 21 and 22 May 2012, the draft Presidency proposal obtained a general support, with the exception of the following main provisions, on which delegations maintained concerns and/or reservations:
 - shared management with Member States (*Article 56, in connection with Articles 57 (indirect management) and 77 (Rules on recovery)*);
 - VAT as an eligible cost (*Article 117a(3)(c)*);
 - financial instruments – earmarking of reflows (*Article 131(5) and Article 18(3)(h)*);
 - EU multi-donor trust funds for external actions (*Article 178*);
 - expenditure related to building projects (loans) (*Article 195(8)*).
9. With a view to address some of the concerns expressed, some modifications have been introduced in the text of the Presidency proposal recorded in the Addendum for some of the articles mentioned under point 8.

The Commission statements on the following issues have also been integrated into the Presidency proposal (see Annex 1):

- the enhancing of efforts to combat the illegal traffic in tobacco products (*Article 18(2)(ea)*);
- confidentiality of audit reports (*Article 93(4)*);
- eligibility of non recoverable VAT (*Article 117a(3)(c)*); and
- the comitology for EU trust funds (*Article 178(8)*).

10. Furthermore, the Commission submitted additional draft statements on "issues relating to the MFF Regulation and the IIA for the years post-2014" (Articles 4(2)(b), 9, 9a, 15, 15a and 46(1)(ea)) and on "the alignment of the Financial Regulation to the judgment of the Court of Justice regarding the adoption and the publication of the budgets and to the MFF Regulation and the IIA for the years post-2014" (Articles 30(2) and 37(1)) (see Annex 2).

11. This note and its Addendum are submitted to the Permanent Representatives Committee as a basis for an orientation debate on the issues mentioned under point 8 above, with the aim of updating as a whole the Presidency's mandate to continue and conclude negotiations with the European Parliament.

COMMISSION STATEMENTS INTEGRATED INTO THE PRESIDENCY PROPOSAL

1. On the enhancing of efforts to combat the illegal traffic in tobacco products
(Article 18(2)(ea))

"The Decision 878/2007/EC¹ extending the Hercule I programme in the field of the protection of financial interests over the period 2007 to 2013 placed specific emphasis on the fight against cigarette smuggling and counterfeiting in order to honour the intentions expressed by the EU and the Member States notably in the Anti-Contraband and Anti-Counterfeiting Agreement with Philip Morris International signed in 2004, to intensify efforts to curb the introduction, sale and distribution of Contraband Cigarettes and Counterfeit Cigarettes. As a consequence, the financial envelope for Hercule I was increased considerably within the programme Hercule II. Between 2007 and 2010, three similar agreements were concluded with Japan Tobacco International, British American Tobacco and Imperial Tobacco Limited². The four tobacco manufacturers will pay a collective total of USD 2.15 billion over 20 years, of which 10% are entered into the EU budget. The rest is forwarded to Member States.

¹ OJ L 143, 30.04.2004, p. 9.

² Japan Tobacco International (JTI) Cooperation Agreement (2007), Cooperation agreement with British American Tobacco (BAT) 2010 and Cooperation agreement with Imperial Tobacco Limited (ITL) 2010; http://ec.europa.eu/anti_fraud/investigations/eu-revenue/cigarette_smuggling_en.htm.

In December 2011, the Commission presented the proposal for the Hercule III programme to promote activities in the field of the protection of the European Union's financial interests¹. This proposal takes into consideration the work of a "Task Group Cigarettes" (composed of specialist services in Member States dealing in particular with the agreements with the tobacco manufacturers) and the proposed Regulation formally acknowledges in its Article 2 the contribution of Hercule III programme to "developing the activities at Union level and the Member States to counter fraud, corruption and any other illegal activities affecting the financial interests of the Union, including the fight against cigarette smuggling and counterfeiting". In the light of this role of Hercule III which will allow the EU and the Member States to continue implementing the agreements with the tobacco manufacturers, the Commission proposes to keep the overall budgetary envelope for Hercule III stable (after inflation) at EUR 110 millions for 2014 to 2020.

The Commission will continue in the future proposing appropriate financial means necessary to fight cigarette smuggling and counterfeiting by the EU, in addition to efforts undertaken by the Member States."

2. **On confidentiality of audit reports (Article 93(4))**

"The Commission recalls that reports referred to in Article 93(4), third subparagraph of the Financial Regulation which are made available to the European Parliament at its request shall be treated confidentially in accordance with Annex II (Forwarding of confidential information to Parliament) of the Framework Agreement on relations between the European Parliament and the European Commission²."

3. **On eligibility of non recoverable VAT (Article 117a(3)(c))**

"The Commission confirms that, as indicated in Article 115(2)(e), provisions of Title VI - including Article 117a(3)(c) on eligibility of non recoverable VAT - do not apply to expenditure implemented under shared management within the meaning of Articles 55(1)(b) and 56".

¹ COM(2011) 914 final.

² OJ L 304, 20.11.2010, p. 47.

4. **On the comitology for EU trust funds (Article 178(8))**

"The Commission confirms that draft decisions to create, extend and liquidate EU trust funds will be submitted to the examination procedure in accordance with the provisions of the relevant basic acts."

ADDITIONAL DRAFT STATEMENTS PROPOSED BY THE COMMISSION

1. Draft joint statement on issues relating to the MFF Regulation and the IIA for the years post-2014 (Articles 9 and 9a, 15 and 15a, Articles 4(2)(b) and 46(1)(ea))

"The European Parliament, the Council and the Commission agree that the provisions relating to the following issues will be discussed in the context of the negotiations on the MFF Regulation and the IIA for the years post-2014:

- the carry-over rules for the Emergency Aid Reserve and for projects financed under the Connecting Europe Facility,
- the carry-over of unused appropriations and of the budgetary balance as well as the related proposal to enter these in a reserve for payments and commitments,
- the possible inclusion of the EDF in the EU budget."

6. Draft Commission statement on the alignment of the Financial Regulation to the judgment of the Court of Justice regarding the adoption and the publication of the budgets and to the MFF Regulation and the IIA for the years post-2014 (Articles 30(2) and 37(1))

"The Commission undertakes to propose a revision of the Financial Regulation, should it prove necessary, to align it to:

- the judgement of the Court of Justice on the adoption and publication of the budgets,
- the MFF Regulation and the IIA for the years post-2014."