



EUROPEAN
COURT
OF AUDITORS

Opinion No 1/2018

(pursuant to Article 322(1)(a) TFEU)

Concerning the proposal of 2 May 2018 for a regulation of the European Parliament and of the Council on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States

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THE COURT OF AUDITORS OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union (TFEU), and in particular Article 322(1)(a) thereof, together with the Treaty establishing the European Atomic Energy Community, and in particular Article 106a thereof,

Having regard to the Commission's proposal for a regulation of the European Parliament and of the Council on the protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States ("the Proposal")¹,

Having regard to the Commission's request for an opinion on the above-mentioned Proposal of 3 May 2018, received by the Court on 14 May 2018,

HAS ADOPTED THE FOLLOWING OPINION:

INTRODUCTION***Background***

1. The Commission's 2014 communication 'A new EU Framework to strengthen the Rule of Law'² set out a new framework to ensure effective and coherent protection of the rule of law in all Member States. This framework provided a structure within which to address and resolve a systemic threat to the rule of law, seeking to avert future threats to the rule of law in Member States before the conditions for activating the mechanisms in Article 7 of the Treaty on European Union (TEU) were met. The framework was intended to be complementary to the Article 7 TEU mechanisms and does not prejudice the use of infringement procedures under Article 258 of the Treaty on the Functioning of the European Union (TFEU).

¹ COM(2018) 324 final of 2 May 2018.

² COM(2014) 158 final of 11 March 2014.

2. The Commission's 2018 communication 'A new, modern Multiannual Financial Framework for a European Union that delivers efficiently on its priorities post-2020'³ explains that 'The Union is a community of law and its values constitute the very basis of its existence. They permeate its entire legal and institutional structure and all its policies and programmes. Respect for these values must therefore be ensured throughout all Union policies. This includes the EU budget, where respect for fundamental values is an essential precondition for sound financial management and effective EU funding. Respect for the rule of law is important for European citizens, as well as for business initiatives, innovation and investment. The European economy flourishes most where the legal and institutional framework adheres fully to the common values of the Union.'

3. On 14 March 2018, the European Parliament called 'on the Commission to propose a mechanism whereby Member States that do not respect the values enshrined in Article 2 TEU can be subject to financial consequences', warning, however, 'that final beneficiaries of the Union budget can in no way be affected by breaches of rules for which they are not responsible'. It declared that it was 'convinced, therefore, that the Union budget [was] not the right instrument for addressing the failure to observe Article 2 TEU, and that any possible financial consequence should be borne by the Member State independently of budget implementation'⁴.

4. According to the Commission, 'there is currently no mechanism in place to protect EU tax payers' money in case of deficiencies regarding the rule of law in a Member State'⁵. The current rules oblige Member States to demonstrate that their management and control systems and procedures for implementing EU funds sufficiently protect the Union's financial

³ COM(2018) 98 final of 14 February 2018.

⁴ European Parliament resolution of 14 March 2018 on the next MFF: Preparing the Parliament's position on the MFF post-2020 (2017/2052(INI)).

⁵ See Commission leaflet 'EU budget for the future – sound financial management and the rule of law', https://ec.europa.eu/commission/news/eu-budget-future-2018-may-02_en.

interests⁶, failing which the Commission takes corrective action (for example suspending payments or applying financial corrections). If the Commission identifies infringements of EU law, it may launch an infringement procedure against a Member State based on Article 258 TFEU. Furthermore, if a Member State does not respect the fundamental values referred to in Article 2 TEU, including the rule of law, the Commission may trigger the mechanism in Article 7 TEU, which may ultimately lead to the suspension of certain rights (including voting rights in the Council; see paragraph 15).

The Commission's Proposal

5. In view of the overall aim of the Proposal to contribute to the proper implementation of the EU budget, the Commission has chosen Article 322(1)(a) of the Treaty on the Functioning of the EU (TFEU), which is the same legal basis as for the Financial Regulation. The Proposal is a self-standing regulation within the regulatory package for the Multiannual Financial Framework 2021-2027.

6. More specifically, the Commission's Proposal aims at establishing 'the rules necessary for the protection of the Union's budget in the case of generalised deficiencies as regards the rule of law in Member States', which affects or risks affecting the principles of sound financial management or protection of the financial interests of the Union. It therefore gives the Commission the right to initiate the procedure before such risks have materialised. By increasing the protection against possible practices or omissions of national authorities, which go against the rule of law, the Proposal is intended to have a positive impact on the sound financial management of the EU budget.

7. The Proposal provides for the Commission, after having taken into account information and observations received from the Member State concerned, to submit a proposal to the

⁶ According to Article 59 (2) of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council (Financial Regulation) (OJ L 298, 26.10.2012, p. 1), 'when executing tasks relating to the implementation of the budget, Member States shall take all the necessary measures, including legislative, regulatory and administrative measures, to protect the Union's financial interests, ..[..].'

Council for an implementing act on appropriate measures (depending on the nature, gravity and scope of the generalised deficiency as regards the rule of law). This proposal shall be deemed to have been adopted by the Council, unless it decides, by qualified majority to reject or to amend the Commission's proposal within one month. Appropriate measures can take the form of suspension, reduction or restriction of a Member State's access to the EU funding, whether in full or in part.

8. The Proposal obliges the Commission to assess the situation where the Member State concerned has submitted evidence that shows that the generalised deficiencies established have been remedied or have ceased to exist in full or in part, and, if the assessment is positive, to submit to the Council a proposal for a decision lifting those measures in full or in part. Without such a decision by year n+2, suspended commitments of year n would be definitively lost for the Member State concerned.

GENERAL REMARKS

Overall aim to protect the Union budget

9. We welcome the aim of the Commission's legislative initiative to protect the Union budget against generalised deficiencies as regards the rule of law (see **Box 1**) in a Member State, which affect or risk affecting the sound financial management or the protection of the financial interests of the Union.

Box 1 - Rule of Law in the Union

The case law of the Court of Justice and of the European Court of Human Rights, as well as documents drawn up by the Council of Europe, building notably on the expertise of the Venice Commission, provide guidance on the core meaning of the rule of law as a common value of the EU in accordance with Article 2 TEU.

Those principles laid down include: legality, which implies a transparent, accountable, democratic and pluralistic process for enacting laws; legal certainty; prohibition of arbitrariness of the executive powers; independent and impartial courts; effective judicial review including respect for fundamental rights; and equality before the law.

10. We note that the Commission bases the proposed mechanism on the necessity to respect the rule of law as a precondition for ensuring compliance with the principles of sound financial management of EU funds. We agree with the Commission's view that unlawful and arbitrary decisions by public authorities responsible for managing funds and for judicial review could harm the financial interest of the Union.

11. As the supreme audit institution of the Union, we recognize that the confidence of all EU citizens and national authorities in the functioning of the rule of law is particularly vital for the further development of the EU into "an area of freedom, security and justice without internal frontiers"⁷. We also acknowledge that the independence and impartiality of the judiciary are essential to ensure the sound financial management and the protection of the EU budget, particularly with regard to the judicial enforcement of legal claims, the fight against fraud and other legitimate interests of the EU.

New mechanism with much discretionary power for the Commission

12. We note that the proposed mechanism is more specific in objective, scope, and range of measures which can be taken than the Article 7 TEU mechanisms, and faster to apply. The draft regulation assigns the Commission more discretionary power in the process than the current rules to counter any breach against one of the fundamental values set out in Article 2 TEU.

13. The Commission would start the procedure if it finds it has 'reasonable grounds' to believe that the conditions in Article 3 of the Proposal had been met. In doing so, it may take into account all relevant information mentioned in Recital 12 of the Proposal, including decisions handed down by the Court of Justice of the EU, reports from the Court of Auditors and conclusions and recommendations from relevant international organisations (see paragraph 19). The criteria for launching the procedure and for the qualitative assessment are however not clearly defined (see paragraphs 20-23).

⁷ Articles 3(2) TEU and 67 TFEU; COM(2014) 158 final as of 11 March 2014.

14. In reaction to the Commission's finding, the Member State concerned should provide all required information and may submit its observations, which the Commission should take into account. The Commission would decide which measure was appropriate in each individual case. The Proposal states that the Commission would do so in line with the principle of proportionality and evaluate each case on its own merits (seriousness, time, duration, recurrence, intention of the said conduct and degree of the cooperation and effects of that deficiency on the respective EU funds). The criteria for the choice and extent of measures are also not clearly defined (see paragraph 20).

15. Article 7 TEU requires a four-fifth majority of the Council to establish a clear risk of a serious breach of the values referred to in Article 2. Furthermore, it requires unanimity of the European Council - based on a Commission proposal and after consent of the European Parliament - to determine the existence of a serious and persistent breach by a Member State of the values referred to in Article 2. After determination of such existence, the Council acting by qualified majority can suspend certain membership rights of the Member State concerned, including voting rights in the Council. In this proposed mechanism, however, the Commission's proposal is deemed accepted unless rejected or modified by the Council. Blocking the Commission's proposal would require a qualified majority of the Council within one month ('reversed qualified majority voting'). The European Parliament would only be informed of any proposed or adopted measures.

16. The lack of criteria for important milestone decisions in implementing the proposed regulation and the adoption of the Commission's proposal under the reversed qualified majority voting by the Council contributes to the discretionary power provided to the Commission in the Proposal.

No specific stakeholder consultation done

17. Article 11 (3) TEU requires the Commission to 'carry out broad consultations with parties concerned in order to ensure that the Union's actions are coherent and transparent'. More specifically, Article 2 of Protocol No. 2 on the application of the principles of subsidiarity and proportionality annexed to the Treaty stipulates that 'before proposing

legislative acts, the Commission shall consult widely'. While we note that the subject matter has been widely debated including at the European Parliament and the Council, we consider it would have been essential for the Commission to undertake a specific stakeholder consultation before publishing the Proposal.

No impact assessment done

18. According to the Interinstitutional Agreement on Better Law-Making, the Commission should carry out impact assessments of any of its legislative and non-legislative initiatives, delegated acts and implementing measures which are expected to have a significant economic, environmental or social impact. Despite the potential impact on final beneficiaries (see paragraph 26) and the fact that parts of the Union budget are likely to be left outside the mechanism (see paragraph 28), we note that no impact assessment was undertaken. The Commission considers that rules adopted under Article 322 TFEU provide the general framework for implementing spending programmes, which implies that there are no direct economic, environmental or social impacts that could be usefully analysed. We are, however, of the view that carrying out an impact assessment before publishing the Proposal would have allowed for a better informed decision-making by the legislative bodies.

SPECIFIC REMARKS

Sources of guidance and criteria are not clearly specified

19. The Proposal does not clearly specify which available sources of guidance the Commission should use for making its qualitative assessment to identify a generalised deficiency as regards the rule of law, which puts sound financial management at risk. It only states that the Commission may base its assessment on information from all available sources. In our view, clearer specification could improve the transparency, traceability and auditability of the proposed mechanism as well as legal certainty and non-arbitrariness of the executive powers proposed to be conferred to the Commission. **Box 2** shows some possible guidance sources.

Box 2 - Examples of possible guidance sources

The Commission could find sources of guidance from chapter 23 (judiciary and fundamental rights) and chapter 24 (justice, freedom and security) applicable to EU accession negotiations, as well as the Cooperation and Verification Mechanism (CVM) on Bulgaria and Romania, which was deployed to address shortcomings in the fields of judicial reform, corruption or organised crime. Other examples of possible relevant sources or guidance are the Venice Commission's Rule of Law Checklist, the Council of Europe Recommendation CM/Rec (2010)12 'Judges: independence, efficiency and responsibilities', the Venice Commission Report on the Independence of the Judicial System Part I: the Independence of Judges (CDL-AD(2010)004), and the Venice Commission Report on Part II: the Prosecution Service (CDL-AD(2010)040).

20. Article 4(3) of the Proposal provides that the measures taken should be proportionate to the nature, gravity and scope of the generalised deficiency. Proportionality should be ensured by taking into account the seriousness of the situation, its duration, its recurrence, the intention and the degree of cooperation of the Member State and the effects of the generalised deficiency on the respective EU funds.

21. The proposed measures should also, 'insofar as possible, target the Union actions affected or potentially affected by that deficiency'. However, no precise criteria are set for important milestone decisions, such as the initiation of the procedure or determining the choice and extent of measures, which does not ensure a consistent application of the provisions.

22. According to the Commission, further detailing the criteria is not necessary and would be counterproductive, as the generalised deficiencies as regards the rule of law need to be established on the basis of a qualitative assessment, which does not allow for the use of quantitative criteria. Any quantitative approach would weaken the mechanism substantially due to the risk that not all possible cases are covered. Moreover, it argues that the burden of proof for its qualitative assessment, which is subject to judicial review, is with the Commission and the Council.

23. In the context of our audits of the excessive deficit procedure and the macroeconomic imbalance procedure⁸, we noted the existence of clear criteria, which allowed us to conclude that weaknesses in the consistent and transparent application of the two procedures existed. With this background, we consider there is a need for developing criteria that allow for a critical appreciation of the consistency in applying the provisions with a view to ensure equal treatment of Member States in case of generalised deficiencies as regards the rule of law, which puts sound financial management at risk.

Recommendation 1

We recommend that the legislative bodies set clear and specific criteria for defining what constitutes a generalised deficiency as regards the rule of law, which puts sound financial management at risk, and for determining the extent of measures, either in the proposed regulation or in possible implementing rules. When setting the criteria, the sources of guidance, which the Commission used in the context of EU accession negotiations, as well as in the Cooperation and Verification Mechanism to track the progress of a Member State could be taken into consideration.

No deadlines for the Commission

24. Despite fixing no deadlines for the Commission, the draft regulation sets strict deadlines by which the Member State concerned must reply to the Commission's notification (within a time limit not less than one month), and by which the Council must reject a proposed decision by qualified majority (within one month). We note that the Treaty does not prescribe any deadlines for the mechanism of Article 7 TEU or the infringement procedure of Article 258 TFEU. The Commission informed us that it has in any event the obligation to act within a reasonable timeframe⁹.

⁸ Special Report No 10/2016 'Further improvements needed to ensure effective implementation of the excessive deficit procedure' and Special Report No 3/2018 'Audit of the Macroeconomic Imbalance Procedure (MIP)'.

⁹ See Joined Cases C-74/00 P and C-75/00 P Falck SpA and Acciaierie di Bolzano SpA v Commission of the European Communities, EU:C:2002:524, par. 139-141

Recommendation 2

We recommend that the legislative bodies specify the basis for setting time limits by which the Member State concerned has to provide the required information as well as introducing similar deadlines for the Commission whenever appropriate, for example as regards the lifting of measures in case the underlying generalised deficiencies have ceased to exist.

No clear obligation for the Commission to assess possibility to lift measures at its own initiative

25. According to Art. 6 (2) of the Proposal, the Commission has the obligation to carry out an assessment with regard to the lifting of measures following a request made by the Member State concerned. We note, however, that the Proposal does not contain a provision which requires the Commission to carry out an assessment in the absence of such a request at its own initiative, if there are grounds justifying it. The Commission has informed us that it would still do so.

No requirement for the Commission to assess the potential impact on final beneficiaries and the national budget

26. Appropriate measures may be adopted under the direct, indirect and shared management modes, the consequences of which, according to the Proposal's explanatory memorandum, 'should fall on those responsible for identified shortcomings'. Unless provided otherwise in the Council decision, the imposition of the measures should not affect the obligation of government entities or Member States to implement the programme or fund affected by the measure and the obligation to make payments to final beneficiaries¹⁰.

<http://curia.europa.eu/juris/document/document.jsf?text=&docid=47692&pageIndex=0&doclang=FR&mode=lst&dir=&occ=first&part=1&cid=263967>.

¹⁰ This reflects point 119 of the European Parliament resolution of 14 March 2018, 'The next MFF: Preparing the Parliament's position on the MFF post-2020', which mentions that 'final beneficiaries of the Union budget can in no way be affected by breaches of rules for which they are not responsible'.

We note that the Proposal does not contain a provision on how this would be ensured. In practice, this would require the Member State concerned to step in and pay or otherwise ensure the financing of the projects or programmes.

27. In this context, we note that payments of national and EU funds may be conditional on the availability of budgetary funding, as revealed during our audits¹¹. The Commission has informed us that it has proposed rules¹² for the next MFF which would impose a series of obligations on national authorities to ensure payments to the beneficiaries in full and on time. We note, however, that the proposed common provisions regulation also contains a clause, which makes the obligation of the national authority to ensure payment to the beneficiary subject to the availability of funding¹³.

28. The aim of the draft regulation is to protect the Union's budget in its entirety. While doing so, it however seeks to ensure that any repercussions of the measures taken fall on the government entities responsible for the identified generalised deficiencies, and not on non-governmental final beneficiaries¹⁴ (such as Erasmus students, researchers or civil society organisations) or other Member States (e.g. through European Territorial Cooperation Programmes). With this aim in mind, the Proposal foresees that for direct and indirect management, measures can only be applied if a government entity is the beneficiary. Consequently, if the beneficiary is a non-government entity, the EU funding which goes to

¹¹ During our audits in the field of shared management, we found contracts concluded between national authorities and final beneficiaries, which contained conditional clauses linking payments to availability of budgetary funding.

¹² Proposal for a Regulation of the European Parliament and of the Council on the financing, management and monitoring of the common agricultural policy (COM(2018)393 final) and the Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument (COM(2018)375 final).

¹³ See Article 68 (1) b) of the proposal for the common provisions regulation.

¹⁴ Depending on the regulation on which basis EU funding is provided, final beneficiaries are also referred to as final recipients.

such an entity is left outside the measures the Commission would propose. Without an impact assessment which could have clarified how much of the Union budget would necessarily remain outside the protection of this proposed mechanism, it is difficult to establish the potential magnitude of this.

Recommendation 3

We recommend that the legislative bodies request the Commission to assess in detail in its proposal to the Council how the legitimate interests of final beneficiaries will be safeguarded. For all measures under Article 4(1) of the Proposal (such as the reduction of commitments or the suspension of commitments or payments), the rights of the final beneficiaries should be safeguarded.

29. In cases where national funds are used to substitute the suspended or reduced EU funds, these funds would have to come from the national budget of the Member State concerned. This leads to budgetary implications for the Member State¹⁵, particularly in case of large-scale suspensions or reductions.

Recommendation 4

We recommend that the legislative bodies request the Commission, before deciding on which appropriate measures to propose, assess the possible budgetary implications of a reduction in the EU funding for the national budget of the Member State concerned with due regard to the principles of proportionality and non-discrimination.

Cooperation with European Public Prosecutor's Office not applicable to all Member States

30. A generalised deficiency as regards the rule of law in a Member State can relate to the effective and timely cooperation with the European Anti-Fraud Office and with the European Public Prosecutor's Office. We draw attention to the fact that not all Member States are part of the European Public Prosecutor's Office cooperation, making the provisions relating to the

¹⁵ In its resolution of 14 March 2018, the European Parliament has stated that the 'Union budget is not the right instrument for addressing the failure to observe Article 2 TEU, and that any possible financial consequence should be borne by the Member State independently of budget implementation'.

European Public Prosecutor's Office, after its establishment, only applicable to the participating Member States.

Recommendation 5

We recommend that the legislative bodies clarify that the provisions relating to the European Public Prosecutor's Office can, after its establishment, only be applicable to the participating Member States.

This Opinion was adopted by the Court of Auditors in Luxembourg at its meeting of 12 July 2018.

For the Court of Auditors



Klaus-Heiner LEHNE

President