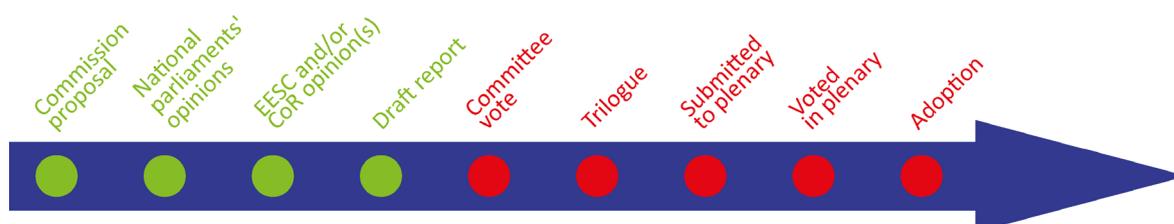


# Protecting the EU budget against generalised rule of law deficiencies

## OVERVIEW

On 3 May 2018 the Commission put forward a proposal for a regulation on the protection of the Union's budget in the event of generalised deficiencies as regards the rule of law in a Member State. The proposal addresses, from a budgetary perspective, generalised deficiencies as regards the rule of law, including threats to the independence of the judiciary, arbitrary or unlawful decisions by public authorities, limited availability and effectiveness of legal remedies, failure to implement judgments, or limitations on the effective investigation, prosecution or sanctions for breaches of law. The proposal provides for the possibility for the Commission to make proposals to the Council on sanctions measures with regard to EU funding. These include suspension of payments, suspension, reduction or even termination of legal commitments (to pay), suspension of programmes, and the transfer of money to other programmes. Such a proposal would be deemed to have been adopted if the Council failed to reject it by a qualified majority. On 17 August 2018, the European Court of Auditors (ECA) delivered its opinion on the proposal and on 3 October 2018, Parliament's co-rapporteurs presented their draft report on the proposal. While sharing the broad objectives put forward by the Commission, they have proposed a number of amendments.

<b>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</b>		
<i>Committees responsible:</i>	Budgets (BUDG) and Budgetary Control (CONT) (jointly under Rule 55)	COM(2018) 324 2.5.2018
<i>Rapporteurs:</i>	Petri Sarvamaa (EPP, Finland) and Eider Gardiazabal Rubial (S&D, Spain)	2018/0136(COD)
<i>Shadow rapporteurs:</i>	Esteban González Pons (EPP), Inés Ayala Sender (S&D), Ali Nedzhmi (ALDE), Anneli Jäätteenmäki (ALDE), Dennis De Jong (GUE/NGL), Younous Omarjee (GUE/NGL), Sven Giegold (Greens/EFA), Jávör Benedek (Greens/EFA), Marco Valli (EFDD)	Ordinary legislative procedure (COD) (Parliament and Council on equal footing – formerly 'co-decision')
<i>Next steps expected:</i>	Vote on report in committee	



## Introduction

### The EU as a community of law

The European Union is a [community of law](#) and the rule of law is one of the fundamental values of the Union (Article 2 of the Treaty on European Union (TEU)) that must be respected by all Member States. National courts and administrative bodies are at the same time the Union's courts and administrative bodies, as they apply and interpret EU law on a daily basis. Hence the importance of all the Member States respecting the rule of law. The rule of law encompasses such aspects as judicial independence, the principle of legality (all government action must be in accordance with the law), respect for EU law (which enjoys supremacy over national law) and respect for the national constitution. Systemic violation of the rule of law by a Member State puts the effective application of EU law in peril, not only in that Member State, but across the Union. This is because the judicial systems of the Member States are closely interconnected, and their collaboration is based on mutual trust and the free movement of judgments. The destruction of an independent judiciary in one Member State has, therefore, effects for all other Member States, as they should normally treat judgments in civil, commercial or criminal matters, emanating from that Member State, as equivalent to their domestic judgments.

### The importance of an independent judiciary for budgetary affairs

As the Commission points out in the explanatory memorandum to its [proposal](#), the EU budget's potential can only be fully unleashed in a favourable regulatory and administrative environment. This includes respect for the rule of law, which in the Commission's words 'is a prerequisite for confidence that EU spending in Member States is sufficiently protected'. The Commission considers that there is a close link 'between the respect for the rule of law and mutual trust and financial solidarity amongst Member States'. Therefore, in order to protect EU financial interests from the risk of financial loss caused by generalised rule of law deficiencies, there is a need to introduce 'the possibility to adopt appropriate measures in such cases'.

## Context

### Rule of law situation in Poland

On 20 December 2017, the Commission triggered the procedure provided for by Article 7(1) TEU for the first time, submitting a [reasoned proposal](#) for a decision of the Council on the determination of a clear risk of a serious breach of the rule of law by Poland ([2017/0360 \(NLE\)](#)), simultaneously issuing detailed [recommendations](#) (for details of the legal framework of the procedure see the 'Existing situation' section below). The triggering of the procedure was preceded by three detailed recommendations adopted by the Commission under its [Rule of Law Framework \(2016/1374, 2016/146 and 2017/1520\)](#), concerning issues such as the President's refusal to swear in properly elected Constitutional Court judges, government's refusal to publish and to abide by certain Constitutional Court judgments from 2015 to 2016, the irregular appointment of the Constitutional Court president, the subjection of judges to disciplinary measures inflicted by Minister of Justice appointees, the appointment of court presidents by the Minister of Justice, the termination of the term in office of the constitutionally established National Council of the Judiciary and the replacement of members elected by judges with members elected from among judges by the parliament, the lowering of the pensionable age of judges at the Supreme Court and its packing with new appointees. The European Parliament backed the Commission's move in a [resolution](#) of 1 March 2018, having already expressed criticism of the situation in Poland in its resolutions of [November 2017](#), [September 2016](#) and [April 2016](#). Council [discussed](#) the situation in Poland in April 2018, and held a [hearing](#) on the issue in June 2018.

## Rule of law situation in Hungary

On 12 September 2018, the European Parliament adopted a resolution calling on the Council to determine the existence of a clear risk of a serious breach by Hungary of the values on which the Union is founded (procedure [2017/2131\(INL\)](#)). This resolution was preceded by numerous others adopted between March 2011 and May 2017. Annexed to the resolution is a proposal for a Council decision containing a detailed account of the situation in Hungary. The Council has yet to decide when the proposal will be discussed. The Parliament's proposal focuses, inter alia, on: constitutional changes affecting the competences and the election of judges of the constitutional court; excessive use of direct democracy instruments by the Hungarian government; electoral reforms, mainly focusing on the delimitation of constituencies; constitutional and legal reforms endangering the independence of the judiciary (e.g. the establishment of new rules relating to the retirement of judges); the shortcomings of national rules dealing with conflicts of interest by the members of the national parliament; Hungary's poor record in relation to government effectiveness and corruption; the current framework relating to secret surveillance for national security purposes; the changes introduced to media legislation hindering freedom of expression and information; legal changes affecting foreign universities and academic freedoms; legal reforms tackling freedom of religion and dramatically reducing the number of legally recognised churches; a political discourse stigmatising NGOs and legal changes adversely affecting their activities; deficiencies concerning the protection of women's and LGBTI people's rights; widespread discrimination suffered by the Roma population and the rise of xenophobia and racism; general disrespect for the fundamental rights of migrants and asylum seekers; and Hungary's poor record in relation to socio-economic rights.

## Existing situation

### Rule of law procedures in the Treaties

#### The evolution of Article 7 TEU

A procedure for sanctions of Member States in cases of systemic rule of law breaches was first introduced by the Treaty of Amsterdam into what was originally [Article F\(1\) TEU](#). The Treaty of Nice added to it a preventive mechanism, creating the two-tier procedure that was taken over by the Treaty of Lisbon. The Court of Justice of the EU (CJEU) enjoys only limited jurisdiction in relation to both mechanisms, as decisions adopted under either of the two procedures can only be submitted to its scrutiny under a request made by the Member State concerned in relation to the procedural – but not the substantive – requirements laid down in Article 7 TEU ([Article 269 TFEU](#)).

#### The preventive mechanism

The preventive mechanism may be activated when there is a 'clear risk of a serious breach' of EU values by a Member State ([Article 7\(1\) TEU](#)). The procedure can be triggered by one third of the Member States, the Parliament or the Commission submitting a reasoned proposal to the Council. After hearing the concerned Member State, the Council may adopt a decision determining whether there is a clear risk of a serious breach of EU values. The Council may also issue recommendations following the same procedure. The Council decides by a qualified majority of four fifths of its members – not including Member State concerned ([Article 354 \(1\) TFEU](#)) – after receiving Parliament's consent, which requires a qualified majority of two-thirds of votes cast, representing an absolute majority of all Members ([Article 354 \(4\) TFEU](#)).

#### The sanctions mechanism

The sanctions mechanism – which can be activated without any previous application of the preventive mechanism – is divided into two distinct phases. The first phase can be triggered by one third of the Member States or by the Commission, but not by the Parliament ([Article 7\(2\) TFEU](#)). After inviting the Member State concerned to submit its observations, the European Council may decide

if there is a 'serious and persistent breach' of EU values by a Member State. The European Council decides by unanimity, without the vote of the Member State concerned, but the Treaties are silent on the voting rights of other Member States subjected to the same procedure, allowing them to vote until a sanctions decision against them is formally adopted ([Article 354 \(1\) TFEU](#)). Abstentions do not prevent unanimity from being reached in the European Council. Parliament's consent is necessary with the same majority as for the preventive mechanism. The adoption of a decision by the European Council opens up the second phase of the procedure ([Article 7\(3\) TEU](#)), in which the Member State concerned may be sanctioned with the suspension of certain membership rights, including its voting rights in the Council. In this phase, the Council is the only institution to intervene, deciding by a qualified majority, without the vote of the Member State concerned ([Article 354, in conjunction with Article 238 \(3\) \(b\) TFEU](#)). If the situation in the Member State changes, the Council may decide by a qualified majority to change or revoke its previous decision ([Article 7 \(4\) TEU](#)).

## *Ex ante* conditionalities – some examples

In addition to the rule of law mechanisms provided for by Article 7 TEU, the existing regulations concerning the specific EU funds also contain rules; these are known as 'conditionalities', since they set out the conditions that must be fulfilled for payments to be made (*ex ante* conditionalities) and the conditions that, if not fulfilled may lead to a halt in payments (interim and *ex post* conditionalities). However, rule of law deficiencies are not addressed explicitly, hence the need for the proposed legislation.

### Regulation 1303/2013

Article 19 of [Regulation 1303/2013](#) (laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund, and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund) sets out *ex ante* conditionalities with regard to the funds covered by the regulation. Member States are obliged to assess in accordance with their institutional and legal framework and in the context of the preparation of the programmes and, where appropriate, the Partnership Agreement, whether the *ex ante* conditionalities laid down in the respective fund-specific rules and the general *ex ante* conditionalities set out in an annex to the regulation are fulfilled. According to Article 19(5), the Commission may decide, when adopting a programme, to suspend all or part of interim payments to the relevant priority of that programme pending the completion of actions referred to in paragraph 2 when necessary to avoid significant prejudice to the effectiveness and efficiency of the achievement of the specific objectives of the priority concerned. Failure to complete actions to fulfil an applicable *ex ante* conditionality which has not been fulfilled at the date of submission of the partnership agreement and the respective programmes, by the deadline set out in paragraph 2, shall constitute grounds for suspending interim payments by the Commission to the priorities of the programme concerned that are affected. In both cases, the scope of suspension must be proportionate, taking into account the actions to be taken and the funds at risk.

Article 23 of the Regulation also contains an important conditionality known as the macroeconomic conditionality, which links cohesion fund spending with the European Semester.

### Regulation 515/2014

[Regulation \(EU\) No 515/2014](#) of 16 April 2014 establishing, as part of the Internal Security Fund, the instrument for financial support for external borders mentions in its recitals that 'in order to achieve freedom and justice, security should always be pursued in accordance with the principles of the Treaties, the *rule of law* and the Union's fundamental rights obligations' (recital 5), and that 'respect for fundamental freedoms and human rights and the rule of law, a strong focus on the global perspective and the link with external security, and consistency and coherence with the Union foreign policy objectives, as laid down in Article 21 of the Treaty on European Union (TEU), should

be key principles guiding the implementation of the Internal Security Strategy' (recital 6). However, the regulation does not provide any concrete mechanisms for cases of rule of law deficiencies in the Member States.

## Parliament's starting position

The Parliament has always supported the rule of law as a fundamental value of the European project. For instance in a [2014 resolution](#) it reiterated its call for a new human rights monitoring mechanism in individual Member States, and in June 2015 urged the Commission to propose an EU mechanism on democracy, the rule of law and fundamental rights, as a tool for compliance with the Charter of Fundamental Rights and Treaties. In December 2014, the Council established an annual dialogue among all Member States to promote and safeguard the rule of law in the Treaties' framework, with two dialogues taking place under the Luxembourg and the Dutch Presidencies. Parliament welcomed this process but expressed doubts about its effectiveness, criticising that it was neither informed of, nor involved in, the political dialogue. In September 2015, Parliament urged the Commission to implement and improve the rule of law framework through clear application criteria and by ensuring the automatic triggering of the Article 7 procedure if the framework failed to resolve the situation.

On 25 October 2016, Parliament adopted an [own-initiative legislative resolution](#) addressing recommendations to the Commission on the establishment of an EU mechanism on democracy, the rule of law and fundamental rights. It invited the Commission to submit, by September 2017, on the basis of Article 295 TFEU, a proposal for the conclusion of a Union pact for democracy, the rule of law and fundamental rights in the form of an interinstitutional agreement. This resolution was accompanied by a [European added value assessment](#) that suggested the existence of a gap between the proclamation of rights and values and actual compliance by EU institutions and Member States, leading to significant economic, social and political costs, recommending the conclusion of an interinstitutional agreement to strengthen the EU legal and policy framework, estimating that the costs of the arrangement would be relatively low and that a pact would foster mutual trust, attract more investment and result in higher welfare standards.

Parliament has also held debates and adopted resolutions concerning the rule of law in individual Member States. For instance, it adopted, on 15 November 2017, a [Resolution on the situation of the rule of law and democracy in Poland](#) [2017/2931(RSP)] and on 1 March 2018 a [Resolution on the Commission's decision to activate Article 7\(1\) TEU as regards the situation in Poland](#), 2018/2541(RSP). Parliament itself activated the procedure of Article 7 against Hungary (see section 'Context' above).

## Preparation of the proposal

The proposal was tabled in response to a rule of law situation in certain Member States that was evolving in a dynamic and adverse way, and therefore was not preceded by any stakeholder consultations, green papers or impact assessments.

## The changes the proposal would bring

On 3 May 2018 the Commission put forward the proposal for a regulation on the protection of the Union's budget in cases of generalised deficiencies as regards the rule of law in the Member States. The proposal is based on Article 322(1)(a) of the Treaty on the Functioning of the European Union and Article 106a of the Treaty establishing the European Atomic Energy Community. It is consistent with the principles of subsidiarity and proportionality. The proposal envisages measures proportionate to the generalised deficiencies as regards the rule of law, including the suspension or reduction of funding under existing commitments, and a prohibition on concluding new commitments with specific categories of recipients. Proportionality would be ensured in particular by taking into account the seriousness of the situation, the time that had elapsed since the relevant

conduct, its duration and its recurrence, the intention and the degree of collaboration of the Member State in putting an end to the violation of the rule of law and the effects of that deficiency on the respective Union funds.

The proposal lays down the following as generalised deficiencies as regards the rule of law:

- endangering the independence of judiciary;
- failing to prevent, correct and sanction arbitrary or unlawful decisions by public authorities, including by law enforcement authorities, withholding financial and human resources affecting their proper functioning or failing to ensure the absence of conflicts of interests;
- limiting the availability and effectiveness of legal remedies, including through restrictive procedural rules, lack of implementation of judgments, or limiting the effective investigation, prosecution or sanctions for breaches of law.

If the Commission found generalised deficiencies in one of the Member States as regards the rule of law as described above, it could:

- suspend payments or the implementation of the legal commitment or terminate the legal commitment;
- issue a prohibition on entering into new legal commitments;
- suspend the approval of one or more programmes or amend such programmes;
- suspend commitments;
- reduce commitments, including through financial corrections or transfers to other spending programmes;
- reduce pre-financing;
- interrupt payment deadlines;
- suspend payments.

The proposed procedure for introducing protective measures would involve, as a first step, investigation by the Commission (involving for instance questions to the Member State). Once the Commission considered that the generalised deficiency as regarded the rule of law to be established, it would submit a proposal for an implementing act on the appropriate measures to the Council. The implementing act would be considered to be adopted unless the Council decided, by a qualified majority, to reject the Commission proposal within one month of its adoption by the Commission. The Council, acting by a qualified majority, could also amend the Commission proposal and adopt the amended text as a Council decision.

## Advisory committees

### European Economic and Social Committee

On 18 September the European Economic and Social Committee (EESC) adopted its [opinion](#) on the multiannual financial framework (MFF) package for the years 2021 to 2027 (rapporteur: Javier Doz Orrit, Workers – Group II, Spain). The EESC supports the Commission's proposal to make the receipt of EU funds by the Member States conditional upon respect for the principle of the rule of law. The Committee also considers that this conditionality could be extended to the other principles linked to the rule of law contained in the EU Treaties and asks the Commission and the Parliament to study this possibility.

### Committee of the Regions

On 9 October 2018 the Committee of the Regions (CoR) adopted its [opinion](#) on the MFF package for the years 2021 to 2027 (rapporteur: Nikola Dobroslavić, EPP, Croatia). The Committee takes the view that respecting the rule of law is a necessary condition for sound financial management and efficient use of the EU budget and welcomes the Commission's efforts to put in place effective mechanisms to ensure respect for the rule of law, legal certainty in all Member States and effective measures

against fraud and corruption. Concerning the Court of Auditor's opinion on the proposal (see below), the CoR agrees with the Court that the proposed mechanism for ensuring compliance with the rule of law goes further than the procedure under Article 7 TEU and can be implemented more quickly. It also agrees with that the Commission's current legislative proposal would allow too much discretion in relation to the initiation of procedures, and calls on the Commission to set clear criteria to determine what constitutes a generalised deficiency, as regards the rule of law, that puts sound financial management at risk. It also sees a stronger role for the European Court of Auditors in implementing the proposed procedure, in conformity with Article 287 TEU.

Concerning the text of the proposal, the CoR puts forward a number of significant amendments. The Committee would exclude all directly elected local or regional authorities' administrative bodies and entities from the application of the regulation. In the CoR's view, a suspension of the approval of one or more programmes or of an amendment thereof would have no direct punishing financial effects on a Member State concerned, therefore the option for the Commission to make such a suspension would be deleted from the regulation. The Committee considers that the Commission should assess the possible budgetary implications of a reduction in EU funding for the national and subnational budgets of the Member State concerned with due regard to the principles of proportionality and non-discrimination. Once measures are imposed, in the CoR's view their lifting ought to be accompanied by solid, impartial and timely evidence in order to proceed with the implementation of programmes concerned without any unnecessary delays. An opinion from the Court of Auditors could be sought for that purpose.

## National parliaments

The proposal was transmitted to national parliaments on 7 May 2018, and the deadline for submitting reasoned opinions (Article 6 of the Protocol on the principles of subsidiarity and proportionality) expired on 2 July 2018 (after 8 weeks). No national parliament submitted a reasoned opinion questioning the conformity of the proposal with the principle of subsidiarity. Following scrutiny procedures, detailed contributions were submitted by the German Bundesrat, the Portuguese parliament and the Czech Senate.

### German Bundesrat

The Bundesrat [takes the view](#) that the Commission is correct in asserting that the rule of law is an indispensable prerequisite for sound financial management and effective EU funding. However, concerning the proposal itself the Bundesrat points out that 'the TEU and the TFEU lay down clear procedures for ascertaining breaches of EU law and for sanctioning them — including cutting EU resources'. Furthermore, the German upper house considers that 'the criteria for the proposed sanctions are not fixed in part and that the list of them is not exhaustive. It also points out that the suspension of programme approval proposed as a sanction may lead to considerable delays in implementation and may continue to have an effect even after the alleged breach has already been stopped, which is why the Bundesrat is in favour of these sanctions being reconsidered'.

### Czech Senate

The Czech Senate [is of the opinion](#) that 'an effective democratic state governed by rule of law based on the respect for fundamental rights of the individual is a necessary precondition for the functioning of Europe based on the values of democracy, law and freedom' and welcomed the proposal. However, the Senate disagreed with the sanctions mechanism in the proposal, 'in particular that the Commission's proposal shall be deemed to have been adopted by the Council, unless it decides, by qualified majority, to reject the proposal, for which, furthermore, the Council has an inadequately short period of one month'.

## Stakeholders

### Academics

Maria José Rangel de Mesquita (Professor of Law at the University of Lisbon) [takes the view](#) that the proposal is inspired by existing conditionalities in the current 2014 to 2020 MFF, especially those linking the effectiveness of European structural and investment (ESI) funds to sound economic governance, as provided in Regulation 1303/2013. In de Mesquita's view, 'the Commission intends to replicate the regime of measures linking effectiveness of ESI funds to sound economic governance within the domain of ensuring effectiveness regarding the respect of EU values and the [rule of law]'. She points out, however, that in contrast to Regulation 1303/2013, the new proposal 'does not establish a formal link with the infringement procedure of Article 7 TEU ..., neither with its declarative phase ... nor, at least, with the preventive phase ...'. This leads de Mesquita to the critical conclusion that 'the newly proposed mechanism by-passes the Article 7 procedure'. She also harbours doubts as to the conformity of the procedure with primary law. She points out that 'the "reinversed" decision-making procedure ... apparently reinverses the normal rule of voting by qualified majority and the case is not expressly foreseen in the Council's Rules of Procedure, in which a simplified written procedure (called "silent procedure") can be applied exceptionally, according to which the relevant text shall be deemed to be adopted at the end of a period laid down by the Presidency, except where a member of the Council objects'. Finally, she points out that the proposed sanctions mechanism may 'have an undesirable effect on EU actors other than Member State and also on the internal market that may be both disproportionate and ineffective as a form of deterrence regarding the legal sphere of the involved Member State considering the nature of the alleged infringement'.

Iain Begg (professorial research fellow at the European Institute, co-director of the Dahrendorf Forum, London School of Economics and Political Science) [considers](#) that 'the attempt to link EU expenditure with adherence to the rule of law, while reflecting a moral position, is fraught with dangers. Defining the circumstances in which EU money will be withheld – in other words, financial sanctions – will be tricky enough, but implementation will be harder still'. He warns that 'when pushed, Member States not only resent the implied intrusion in their autonomy, but also struggle to enforce the conditions', adding that one should consider also 'issues of fairness ... particularly where the delinquent authority (for example, a government failing to abide by macroeconomic conditions or rule of law provisions) is different from the one penalised (a regional government)'.

Dencho Georgiev (Guest Professor at the Vrije Universiteit Brussel) [argues](#) that 'reform of EU finances should ensure that solidarity and progressivity in the EU become a matter of the rule of law and not of governance through conditionalities and sanctions'. In his view, if the Member States 'want to bring more rule of law in the Union's finances, they should introduce into its budget and its policies more rules and principles based on objective criteria and leave fewer possibilities for arbitrary political decisions by the executive bodies ...'. Georgiev is critical of the proposal, arguing that it 'would enhance the already immense power of direct governance of the Commission to unprecedented levels, both with respect to the domestic constitutional laws of the Member States and to international law', adding that because 'the proposal ... is not about placing power under superior rules, principles or values, it can hardly be claimed that it is about protecting the rule of law in the EU'. He concludes by warning that adopting the proposal would mean that the 'EU would be taking a step further away from democracy and a step closer to what can be described as an empire'.

### Think-tanks

#### Spinelli Group

The Spinelli Group, in its [manifesto](#) on the future of Europe unveiled in September 2018, expressed the view that the European Parliament 'must acquire full powers of co-decision with the Council over all financial decisions ...'. Although the manifesto does not address the proposal directly, it can

be inferred that the group would like see stronger involvement of Parliament in the sanctions procedure.

## Friedrich Ebert Stiftung

The Friedrich Ebert Stiftung published a [position paper](#) by Dr László Andor (Corvinus University in Budapest) who warns that 'if the current budget debate leads to a significant reduction of transfers by downgrading the cohesion funding instruments, the single market may also disintegrate. The EU should not resolve one problem by creating or aggravating others ...'. Dr Andor believes that it 'seems like eternity to establish that this or that country is actually violating the values and democratic standards of the EU'. He also remarks that 'the past decade has shown that while the EU has successfully enforced the Maastricht criteria, it has failed to do so with regard to the Copenhagen criteria; apparently the EU considers the first more important than the second.'

## Europeum

A commentator from Czech think-tank Europeum [points out that](#) the proposal would give the Commission the power to 'assess, for instance, whether prosecution, audit offices or the judiciary are independent enough to conduct unbiased investigation of potential frauds'. In contrast, in his view, the proposal 'is not constructed to punish Member States for promoting policies that diverge from "the European mainstream" ... but rather countries whose political system cannot guarantee solid systems of checks and balances, and fundamental rule of law'. He is critical of the procedural side, arguing that the Commission proposal 'results in reduced clarity – is the Commission as an expert institution responsible for the decision, or the Council as purely political body? In this respect, the upcoming MFF negotiations should resolve the ambiguity and opt for only one source of legitimacy'.

## Legislative process

### Opinion of the European Court of Auditors

On 17 August 2018, the European Court of Auditors (ECA) delivered its [opinion](#) on the proposal. The ECA welcomed the aim of the Commission's legislative initiative to protect the Union budget against generalised deficiencies as regards the rule of law in a Member State that affect or risk affecting the sound financial management or the protection of EU financial interests, and agreed with the Commission that unlawful and arbitrary decisions by public authorities responsible for managing funds and for judicial review could harm EU financial interests. However, at the same time ECA noted that the regulation would give the Commission a very broad margin of discretion in the procedure. ECA also pointed to the lack of rules on specific stakeholder consultation and an impact assessment. ECA recommended that clear and specific criteria for defining what constitutes a generalised deficiency as regards the rule of law should be set out in the regulation and pointed to the need to protect the legitimate interests of the EU fund beneficiaries who would be affected.

### Draft report by the Parliament's co-rapporteurs

On 3 October 2018, the co-rapporteurs from the Committees on Budgets (BUDG) and on Budgetary Control (CONT) presented their [draft report](#) on the proposal. The co-rapporteurs, while sharing the broad objectives put forward by the Commission, have proposed a number of amendments.

According to the draft report, the concept of the rule of law should be understood as having regard to the fundamental values enshrined in Article 2 TEU and to the Copenhagen criteria, which include the stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities, a functioning market economy and the capacity to cope with competition and market forces, and the ability to take on the obligations of Union membership.

The co-rapporteurs consider that when assessing the existence of a generalised deficiency and in order to ensure the proportionality of the measures being adopted, it is necessary that the

Commission take into account all relevant information, including information coming from Parliament and from bodies such as the Venice Commission of the Council of Europe.

In the co-rapporteurs' view, the Commission should first assess the potential impact of the proposed measures on final beneficiaries and should then actively monitor whether the legal entitlements of the final beneficiaries are respected.

The draft report insists on putting Parliament on an equal footing with the Council when it comes to adopting or lifting measures: the Commission would adopt a decision on the appropriate measures by its own implementing act, and simultaneously submit to the Parliament and the Council a proposal to transfer to a budgetary reserve an amount equivalent to the value of the measures adopted. That decision would only enter into force if the Parliament and the Council failed to reject it within one month.

Finally, the co-rapporteurs propose a number of amendments: to specify more precisely what constitutes endangering the independence of the judiciary; to improve the certainty of the procedure by including indicative deadlines for the Commission to react to information received from Member States; and to ensure that if measures being imposed are not lifted after two years, the suspended funds are not lost but are entered in the Union Reserve for Commitments provided for in the 2021-2027 MFF Regulation.

## Debate in the joint committee

On 10 October 2018, a debate was held on the proposal within a joint CONT and BUDG committee meeting. Considering the rule of law crisis in certain Member States, some Members deplored the lack of reaction from the Council and therefore welcomed the Commission's proposal, which tackled the crucial issue directly. It was pointed out that implementing this instrument to ensure respect for the rule of law created a very powerful tool that could be used in a discretionary manner. The need for clear and transparent criteria was therefore great in order to ensure that it would be used properly and without any abuse. Another issue raised in the meeting was the need to protect the beneficiaries of the fund. It was underlined that the aim of the mechanism was not to punish the beneficiaries of the funds since they were not the ones responsible for its misappropriation. The aim was to punish governments that refused to use the European funds as they were intended. Another point that was often debated was the one of the nature of this mechanism, and therefore the legal basis for it. For some Members, the proposal was more of a sanctions mechanism, especially since the Commission had included corruption and fraud within the scope of the tool, rather than limiting it to breaches of the rule of law. Others criticised this extension to corruption and fraud, stating that the Union already had ways to combat that. As some Members underlined, this tool could only be used as a last resort measure against a general breach of the rule of law. It was only after all dialogue had failed that this mechanism could be triggered to protect the integrity of the EU funds. It was pointed out that the tool should be used with caution, as used unwisely it could result in a backlash of anti-European sentiments. Finally, some Members highlighted the need to involve Parliament in the procedure.

## Council

On 31 October 2018, *Agence Europe* [reported](#) that the Council Legal Service had prepared a legal opinion on the proposal. This opinion had not however at the time of writing been made available ([or even mentioned](#)) in the Council Register of Documents. According to the press information available, the Council Legal Service experts:

- 'doubt the Treaty articles used as the legal basis for the legislative proposal, but they did not say that "it was impossible to make this proposal" linking European funds and the rule of law',

- consider Article 322 TFEU as 'the appropriate basis', but point out that 'difficulties exist with Article 7 of the Treaty', which may lead to a situation in which 'the two procedures may overlap',
- consider that 'reference to the rule of law in Article 3 of the proposal as a condition for triggering the proposed mechanism is neither necessary nor sufficient to establish a link with the proper implementation of the EU budget, which is essential for genuine conditionality of expenditure'.

## EP SUPPORTING ANALYSIS

Mańko R., [The EU as a community of law: Overview of the role of law in the Union](#), EPRS, European Parliament, 2017.

Poptcheva E.-M., [Understanding the EU Rule of Law mechanisms](#), EPRS, European Parliament, 2016.

## OTHER SOURCES

[Protection of the Union's budget in case of generalised deficiencies as regards the rule of law in the Member States](#), European Parliament, Legislative Observatory (OEIL).

[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](#), European Commission, COM(2018)324.

[Opinion No 1/2018 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](#), European Court of Auditors, May 2018.

[Draft Report on the 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](#), European Parliament Committees on Budgets and on Budgetary Control, 3 October 2018.

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