

A NEW FRAMEWORK FOR EU ADMINISTRATION: THE FINANCIAL REGULATION 2002

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I

INTRODUCTION

This Article, a discussion of the administration of the European Union budget, including direct and shared management, and of the recently enacted new Financial Regulation, has three related objectives, which will be explored in the course of the ensuing analysis. The first is to point to the increasing constitutionalization of Community administration. The term constitutionalization has a plethora of meanings. Its use here signifies, in formal terms, that the principles governing European Community (“Community”) administration have now been enshrined in a norm, the new Financial Regulation, which is of constitutional importance. The term constitutionalization signifies, in substantive terms, the emergence of overarching principles that frame the entirety of Community administration.

The second is to convey an understanding of Community administration. Much has been written on topics such as comitology. There is, however, a paucity of material on the different ways in which the Community administers its policies. The divide between direct and shared administration is imperfectly understood. This is especially important given the numerous legislative and non-legislative initiatives that are fundamentally reshaping this terrain.

The third objective is to examine the role of law in Community administration. Judicial review is but part of this story. It is not the whole story, and it is certainly not even the first chapter in what is a much richer and more interesting tale. It will be seen that law, both hard and soft, plays a plethora of roles in this area. Law, in the form of general Community legislation, establishes the overarching principles to govern Community administration, as exemplified by the new Financial Regulation. Law, in the form of specific Community legislation, encapsulates choices that can markedly affect success or failure, as exemplified by the Common Agricultural Policy. Law will be used to legitimate new institutions for policy delivery, such as executive agencies. Law, in the form of judicial review, has a Janus-like focus: the Community courts will control abuse of administrative power, and they can also use judicial review to read Community legislation in the manner that best conforms to the

Community interest. We must also be mindful of the limits of law. The bypassing of formal legal norms by key players, and the legal response, is a fascinating part of the story.

II

THE EMERGENCE OF A CONSTITUTIONAL FRAMEWORK FOR ADMINISTRATION

The recognition that Community policies are administered in different ways is not new. The work of the Committee of Independent Experts nonetheless constituted a major step toward clarifying Community administration. The Committee was established to investigate claims of mismanagement and fraud in Community administration. Its First Report¹ precipitated the downfall of the Santer Commission. In its Second Report the Committee distinguished between direct and shared management. Direct management covers those Community programs administered by the Commission itself, either “in house” or by contract. The Committee’s Report had a marked impact on the Commission’s thinking. The White Paper on *Reforming the Commission* (“White Paper”)² drew heavily on the Committee’s analysis of direct and shared administration. Shared management” covers “those Community programs where the Commission and the Member States have distinct, legislated administrative tasks that are interdependent and where both the Commission and Member States need to discharge their respective tasks for the Community policy to be implemented successfully.”³ The Common Agricultural Policy (“CAP”) and the Structural Funds are the principal instances of shared management.

The new Financial Regulation embodies the functional distinction between direct and shared management. The previous Financial Regulation was enacted in 1977 and amended on many occasions.⁴ The new Financial Regulation⁵ now provides a legal framework for the structure of Community administration.

The detailed provisions of the new Regulation concerning direct and shared management will be considered below. The present discussion will focus on the structural aspects of the Regulation. These are dealt with in Title IV, Implementation of the Budget, Chapter 2 of which is concerned with Methods of Implementation. Article 53(1) of the Financial Regulation provides that the Commission shall implement the

1. Committee of Independent Experts, First Report on Allegations Regarding Fraud, Mismanagement and Nepotism in the European Commission (15 March 1999) [hereinafter First CIE].

2. *Reforming the Commission*, COM (00)200 [hereinafter White Paper].

3. Committee of Independent Experts, Second Report on Reform of the Commission: Analysis of Current Practice and Proposals for Tackling Mismanagement, Irregularities and Fraud, Vol. I, para. 2.3.27-2.3.31 (1999) [hereinafter Second CIE].

4. Financial Regulation of 21 December 1977 Applicable to the General Budget of the European Communities, 1977 O.J. (L 356) 1 [hereinafter Financial Regulation of 1977].

5. Council Regulation 1605/2002 on the Financial Regulation Applicable to the General Budget of the European Communities, 2002 O.J. (L 248) 1 [hereinafter Financial Regulation]. For background, see Proposal for a Council Regulation on the Financial Regulation Applicable to the General Budget of the EC, COM(00)461 final [hereinafter Proposal for a Council Regulation]; Amended Proposal for a Council Regulation on the Financial Regulation Applicable to the General Budget of the EC, COM (01)691.

budget in one of three ways: through centralized, shared, and decentralized⁶ management. These methods of implementation must be considered separately.

Centralized management covers those instances in which the Commission implements the budget directly or indirectly through its departments.⁷ In centralized management, the Commission is not allowed to entrust its executive powers to third parties when they involve a large measure of discretion implying political choices. The implementing tasks delegated must be clearly defined and fully supervised.⁸ There will clearly be problems in deciding whether the task allocated to third parties is *ultra vires*, in the sense that it involves “a large measure of discretion implying political choices” within the meaning of Article 54(1).

Within these limits, the Commission can entrust tasks to the new breed of executive agencies, or Community bodies that can receive grants.⁹ It can also, within the limits of Article 54(1), entrust tasks to national public-sector bodies, or bodies governed by private law with a public service mission guaranteed by the State.¹⁰ These national bodies can only be entrusted with budget implementation if the basic act concerning the program provides for the possibility of delegation and lays down the criteria for the selection of such bodies. It is also a condition that the delegation to national bodies comply with the requirements of sound financial management and be non-discriminatory.

The delegation of executive tasks to these bodies must be transparent, and the procurement procedure must be non-discriminatory and prevent any conflict of interest. There must be an effective internal control system for management operations, proper accounting arrangements, and an external audit.¹¹ The Commission is not allowed to entrust implementation of funds from the budget, in particular payment and recovery, to external private-sector bodies, other than those which have a public service mission guaranteed by the State.¹² The Commission is, however, empowered to entrust such private-sector entities with tasks involving technical expertise and administrative, preparatory, or ancillary tasks involving neither the exercise of public authority nor the use of discretionary judgment.¹³

When aspects of the budget are implemented by shared management, tasks are entrusted to the Member States in accordance with specific provisions of the new Financial Regulation concerning the European Agricultural Guidance and Guarantee Fund (“EAGGF”), Guarantee Section, and the Structural Funds.¹⁴

6. Decentralized management, or management undertaken jointly with an international organization, will be further defined in this Article but not discussed in depth.

7. Financial Regulation, *supra* note 5, art. 53(2). The principles concerning indirect centralized implementation are set out in Article 54.

8. *Id.* at art. 54(1).

9. *Id.* at art. 54(2)(a-b).

10. *Id.* at art. 54(2)(c).

11. *Id.* at art. 56(1).

12. *Id.* at art. 57(1).

13. *Id.* at art. 57(2).

14. *Id.* at arts. 149-60.

Decentralized management covers those instances in which funds are intended for third country beneficiaries. These funds can be disbursed directly by the Commission or by the authorities of the beneficiary state.¹⁵ In the latter instance the rules of the new Financial Regulation concerning separation of function between authorizing and accounting officers, internal and external audit, and procurement procedures are applicable. These will be considered in detail below.¹⁶ It is in this area that management may be undertaken jointly with an international organization.

The following discussion will consider direct management and will then analyze shared management within the Common Agricultural Policy.

III

DIRECT/CENTRALIZED MANAGEMENT

A. The Rationale for Direct/Centralized Management

The traditional pattern of Community administration has been shared: the Commission works directly with national bureaucracies to implement the CAP and the Structural Funds.

The Commission has, however, increasingly undertaken administration directly, without a systematic relationship with national administrations. This was in part because the Commission was given wider responsibilities, and the enabling provisions in various legislative acts did not establish any general pattern of shared management. The shift also took place in part because the subject matter did not necessarily lend itself to shared management and in part because the Commission felt that certain policies were best implemented through non-governmental organs. The appropriations for directly managed operations are approximately one sixth of the Community budget, in the order of 14 billion Euros per year. Initiatives in relation to tourism, cooperation with non-member countries of the southern Mediterranean (the MED programs), emergency aid, vocational training (the Leonardo da Vinci program), nuclear safety policy, as well as aid to former Soviet bloc countries (TACIS and PHARE), have been managed directly by the Commission. There are an increasing number of programs that are managed in this way.

B. Delivery of Direct/Centralized Management and Contracting Out

Direct management captures the idea that the Commission will implement a program without formal, systematic cooperation with national bureaucracies. It does not mean that the Commission carries out the entirety of the activity itself "in house." The Commission commonly contracts-out part of the work, as exemplified by the programs considered above. The historical motivations for contracting-out were eclectic. In some areas, such as nuclear safety, expertise was the key factor. In others, such as the MED programs, there was a desire to involve civil society in service delivery. The

15. *Id.* at arts. 163-71.

16. *See* discussion *infra* Part IV.B.

rationale for contracting-out in the context of humanitarian assistance was that specialist aid organizations would be better placed to deliver the aid than the Commission. Shortage of staff within the Commission was another reason for contracting-out.

C. Direct/Centralized Management, the Fall of the Santer Commission, and Internal Reform

For considerable time there was concern within the European Community about fraud and mismanagement. This culminated in the Committee of Independent Experts, convened by the European Parliament and the Commission, with a mandate to detect and deal with fraud, mismanagement, and nepotism. The Committee produced its first report in March 1999.¹⁷ The Report spoke of the mismatch between the objectives assigned to the Commission and the way in which it fulfilled them.¹⁸ It led to the resignation of the Santer Commission.

It is only by reading the report in its entirety however that one can understand the nature of the problem. The difficulties encountered were those inherent in contract relationships in which a public arm of government is a party.¹⁹ The line between policy formation and policy implementation became blurred. It was difficult to ensure that the private contractor did not breach its contract with or defraud the Commission. The Commission's mismanagement resided principally in its failure to detect these problems and to address them. The Commission's control and audit procedures were not able to rectify the problems in good time.

Romano Prodi, the new Commission President, sought to restore faith in the institution. He introduced a new Code of Conduct for Commissioners.²⁰ This was followed by the creation, in September 1999, of the Task Force for Administrative Reform ("TFRA"), for which Neil Kinnock was given responsibility. The TFRA produced a White Paper,²¹ which was heavily influenced by the Second Report of the Committee of Independent Experts.²²

This Second Report dealt, *inter alia*, with the different ways in which Community services are delivered. In relation to direct management, the Committee accepted that the Commission would have to contract-out tasks.²³ It was equally firm in its belief that the existing arrangements were imperfect. The Committee proposed a new type of executive agency.²⁴

17. First CIE, *supra* note 1.

18. *Id.* at para. 9.4.5.

19. Paul Craig, *The Fall and Renewal of the Commission: Accountability, Contract and Administrative Organisation*, 6 Eur. L.J. 98 (2000).

20. Romano Prodi, President of European Commission, The Formation of the Commission, July 12, 1999 (unpublished commission document, on file with author); *see also* Romano Prodi, President of European Commission, Operation of the Commission, 12 July 1999 (unpublished Commission document, on file with author).

21. White Paper, *supra* note 2.

22. Second CIE, *supra* note 3.

23. *Id.* at Vol. I, para. 2.3.1; *see also* paras. 2.0.1 and 2.3.8.

24. *Id.* at Vol. I, paras. 2.3.27-2.3.31.

The Commission's White Paper acknowledged the contributions made by the Reports of the Committee of Independent Experts.²⁵ The general theme of the White Paper was the need for the Commission to concentrate on core functions such as policy conception. Delegation to other bodies would enable the Commission to concentrate on its core activities.²⁶ Externalization was only to be used when it was the most efficient option and would not be pursued at the expense of accountability. Therefore, externalization should not be used for the administration of ill-defined activities, nor when real discretionary power was involved.²⁷ The White Paper also suggested a new type of implementing body²⁸ and made important recommendations about staffing and financial control.

IV

DIRECT/CENTRALIZED MANAGEMENT AND LAW

A. Direct/Centralized Management and Externalization: Four Choices

The new Financial Regulation provides a four-part framework for those activities directly managed by the Commission: 1) such programs can be directly managed within the Commission; 2) management tasks can be undertaken by executive agencies; 3) some tasks can be delegated to networks of national agencies; and 4) certain activities can be contracted-out.

These modes of direct management inter-relate. Thus, even when the Commission decides to use an executive agency, important aspects of the program will still be overseen by the Commission since the management tasks that can be delegated to such agencies are limited. Moreover, the contracting-out of certain tasks can be used in conjunction with any of the other modes of direct management. Thus it is possible for an executive agency to contract-out certain of its assigned tasks.

B. Management by the Commission: Recasting Responsibility for Projects

Public lawyers will be aware of the importance of proper control systems when dealing with contracting-out and externalization. Such systems are a necessary, albeit not sufficient, element in the accountability of public administration. This is reinforced by the findings of the Committee of Independent Experts. They revealed that many of the problems with direct management were integrally linked to deficiencies to financial controls. The basic provision was the Financial Regulation of 1977.²⁹ It was amended many times, but certain fundamentals remained largely unchanged. Two were especially significant.

First, the authorization of expenditure and the collection of revenue were both in the hands of the Financial Controller of each Community institution. The Financial

25. White Paper, *supra* note 2, Part I, p. 2.

26. *Id.*, Part I, p. 6.

27. *Id.* at Part I, p. 7.

28. *Id.* at Part I, p. 7.

29. Financial Regulation of 1977, *supra* note 4.

Controller would give the “visa” authorizing the expenditure and would collect revenues.³⁰ Secondly, the authorizing officer and the accounting officer had separate functions. The former entered into the financial commitments, subject to the grant of a “visa” by the Financial Controller, and the latter actually carried out the relevant operation.

The Committee of Independent Experts was critical of this regime.³¹ The Financial Controller’s responsibility for *ex ante* control and *ex post* audit could lead to a conflict of interest. The centralization of *ex ante* control in the Financial Controller through the visa system was ineffective. Control of expenditure should be decentralized to the Directorates-General (“DG”). The responsibility for authorization of expenditure should be linked to responsibility for the carrying out of the operation.³² Responsibility should, in this sense, be repatriated through decentralization.

These ideas were taken up directly into the White Paper on *Reforming the Commission*. The aim was to create “an administrative culture that encourages officials to take responsibility for activities over which they have control—and gives them control over the activities for which they are responsible.”³³ The system of *ex ante* visas proved inadequate to assess the legitimacy of financial operations³⁴ and led to a culture that denuded officials of responsibility.

The new Financial Regulation gives legal force to these ideas.³⁵ The duties of the authorizing officer and the accounting officer are separate.³⁶ The latter is responsible for payments, collection of revenue, and keeping the accounts.³⁷ However, the authorizing officer is central to the whole scheme. Each institution “performs” the duties of authorizing officer.³⁸ It lays down rules for the delegation of these duties to staff of an appropriate level, specifies the scope of the powers delegated and the possibility for sub-delegation.³⁹ The authorizing officer to whom power has been delegated makes the budget and legal commitments, validates expenditure, and authorizes payments.⁴⁰ The authorizing officer to whom power has been delegated must establish the organizational structure and internal management and control procedures suited to the performance of his or her duties. Before an operation is authorized, members of staff other than the person who initiated the operation must verify the operational and financial aspects.⁴¹

30. *Id.* at art. 24.

31. Second CIE, *supra* note 3, paras. 4.6-4.7.2.

32. *Id.* at para. 4.7.

33. White Paper, *supra* note 2, Part I, p. 19.

34. *Id.* at p. 21.

35. Financial Regulation, *supra* note 5.

36. *Id.* at art. 58.

37. *Id.* at art. 61.

38. *Id.* at art. 59(1).

39. *Id.* at art. 59(2).

40. *Id.* at art. 60(2).

41. *Id.* at art. 60(4).

The provisions on expenditure reinforce the centrality of the authorizing officer. Every item of expenditure must be committed, validated, authorized, and paid.⁴² The budget commitment consists of making the appropriation necessary to cover a legal commitment. The legal commitment is the act whereby the authorizing officer enters an obligation to third parties that results in expenditure being charged to the budget. The same authorizing officer undertakes the budget and legal commitment,⁴³ and the former must precede the latter.⁴⁴ It is for the authorizing officer when adopting a budget commitment, to ensure, *inter alia*, that the appropriations are available, that the expenditure conforms to the relevant legal provisions, and that the principles of sound financial management are complied with.⁴⁵ The authorizing officer is responsible for validation of expenditure, the creditor's entitlement to payment and the conditions on which it is due.⁴⁶ The onus is also on the authorizing officer to authorize the expenditure through the issuance of a payment order for expenditure that has been validated.⁴⁷ These rules are designed to "give authorizing officers the entire responsibility for the internal controls in their departments and for the financial decisions they take in the exercise of their functions."⁴⁸ There are rules as to the liability of authorizing and accounting officers.⁴⁹

The internal auditor is also central to the reform package. The idea was strongly advocated by the Committee of Independent Experts⁵⁰ and endorsed by the Commission White Paper.⁵¹ The central idea was to establish an Internal Audit Service, whose auditors would advise the institutions about proper budgetary procedures and the quality of their management and control systems. They are intended to help, *inter alia*, authorizing officers by providing a check on the overall systems adopted. The new Financial Regulation made provision for internal auditors,⁵² and the Internal Audit Service has published a Charter to describe its role.⁵³

C. Management by Executive Agencies: Policy and Implementation, Power and Responsibility

The origins of executive agencies are to be found in the Committee of Independent Experts' Second Report. The Committee noted that technical assistance offices were nothing more than contractors who undertook work for the Commission.⁵⁴ The weak controls over such firms led to the problems highlighted in the Committee's

42. *Id.* at art. 75.

43. *Id.* at art. 76(1), subject to limited exceptions.

44. *Id.* at art. 77(1).

45. *Id.* at art. 78.

46. *Id.* at art. 79.

47. *Id.* at art. 80.

48. Proposal for a Council Regulation, *supra* note 5, Explanatory Memorandum, p. 17.

49. *Id.* at arts. 64-67.

50. Second CIE, *supra* note 3, para. 4.13.

51. White Paper, *supra* note 2, Part I, p. 22.

52. Financial Regulation, *supra* note 5, arts. 85-86.

53. Charter of the Internal Audit Service of the European Commission SEC(00)1801/2.

54. Second CIE, *supra* note 3, para. 2.3.4.

First Report. The creation of implementing agencies was seen as a way of alleviating these problems.⁵⁵ The new Financial Regulation makes provision for such executive agencies.⁵⁶ There is now a framework Regulation dealing specifically with these agencies (“Regulation on Executive Agencies”).⁵⁷

It is important to read this Regulation within the broader context of the other institutional reforms. The objective is to foster flexible, accountable, and efficient management of tasks assigned to the Commission. Policy decisions remain with the Commission, and implementation is assigned to the agency.⁵⁸ The conjunction of power and responsibility, a principal theme of the new Financial Regulation, is carried over to this new regime, since the agency director is cast as the authorizing officer. This is apparent from the Regulation on Executive Agencies.

It is fitting to begin with the rules relating to the establishment and winding-up of executive agencies. An executive agency is a legal entity that manages a Community program and is created in accordance with the Regulation.⁵⁹ The Commission may decide after a cost-benefit analysis to set up such an agency.⁶⁰ The cost-benefit analysis takes into account a variety of factors: the justification for outsourcing, the costs of coordination and checks, the impact on human resources, efficiency and flexibility in the implementation of outsourced tasks, possible financial savings, simplification of the procedures used, proximity of the outsourced activities to final beneficiaries, the need to maintain an adequate level of know-how in the Commission, and the visibility of the Community as promoter of the Community program. A particular agency is not necessarily permanent. The Commission determines the lifetime of the agency, which can be extended within limits.⁶¹ When the services of the agency are not required, it may be wound up.⁶² The creation of a particular agency requires approval under the comitology regulatory procedure,⁶³ and a new comitology committee is established.⁶⁴

In terms of legal status, executive agencies are Community bodies with a public service role. They are legal entities with the capacity to hold property and to be a party to legal proceedings.⁶⁵ The agencies are located in the same place as the Commission and its departments.⁶⁶

55. *Id.* at para. 2.3.27.

56. Financial Regulation, *supra* note 5, arts. 54(2)(a), 55.

57. Council Regulation 58/2003 on Laying Down the Statute for Executive Agencies to be Entrusted with Certain Tasks in the Management of Community Programmes, recitals 5-6, art. 2, 2003 O.J. (L 11) 1 [hereinafter Regulation on Executive Agencies]. For background, see Amended Proposal for a Council Regulation laying down the Statute for Executive Agencies to be Entrusted with Certain Tasks in the Management of Community Programmes, COM(01)808 final, replacing the earlier version COM(00)788 final.

58. Executive Agencies, *supra* note 57, recitals 5-6.

59. *Id.* at art. 2. “Community program” covers any activity, set of activities or other initiative which the relevant basic instrument or budgetary authorization requires the Commission to implement for the benefit of one or more categories of specific beneficiaries, by committing expenditure. *Id.* at art. 2(b).

60. *Id.* at art. 3(1).

61. *Id.* at arts. 3(1)-(2).

62. *Id.* at art. 3(2).

63. *Id.* at arts. 3(3), 24(2).

64. *Id.* at art. 24(1).

65. *Id.* at art. 4.

66. *Id.* at art. 5.

The staffing arrangements are a blend of the old and the new. The operational head of the agency is the director, who must be a Community official within the staff regulations. The Commission makes the appointments which are for four years renewable.⁶⁷ The director is responsible for the agency's tasks and draws up an annual work program.⁶⁸ The director is assisted by a Steering Committee of five members, who do not have to be Community officials. They are appointed by the Commission for at least two years renewable.⁶⁹ The Committee is to meet at least four times a year. Its main tasks are to adopt the agency's annual work program presented by the director, to adopt the agency's budget, and to report annually to the Commission on the agency's activities.⁷⁰ The agency staff are comprised of Community officials, seconded to the agency, and non-Community officials recruited on renewable contracts.⁷¹ This is designed to provide flexibility, facilitating employment of those needed for particular tasks, without the need to incorporate them into the hierarchy of Community officials.

The Regulation on Executive Agencies also contains important provisions specifying the agency's tasks. The Commission can entrust the agency with any tasks required to implement a Community program, with the exception of "tasks requiring discretionary powers in translating political choices into action."⁷² The intent is clear. Policy choices remain for the Commission; implementation is for the agency. This is confirmed by the examples of tasks that can be assigned to executive agencies.⁷³ These are to be defined more fully in the instrument creating a particular executive agency.⁷⁴ The tasks include management of projects within a program by adopting relevant decisions using powers delegated to the agency by the Commission; adopting the instruments of budget implementation for revenue, expenditure, and the award of contracts on the basis of powers delegated by the Commission; and gathering and analyzing data for the implementation of the program.

While the intent is clear, the actual wording in Article 6 to delimit the agency's power may be problematic. This wording is similar to that found in Article 54(1) of the new Financial Regulation, which precludes delegation of executive powers to executive agencies involving a "large measure of discretion implying political choices."⁷⁵ There are, however, crucial differences between the two formulations. Article 54(1) of the Financial Regulation prevents delegation of discretionary political choices. Article 6(1) of the Regulation on Executive Agencies precludes delegation of tasks requiring discretionary power in translating political choices into action. On this formulation the executive agency is not only prevented from making the initial political choices, but also from exercising discretionary power when translating those

67. *Id.* at art. 10.

68. *Id.* at art. 11.

69. *Id.* at art. 8.

70. *Id.* at art. 9.

71. *Id.* at art. 18.

72. *Id.* at art. 6(1).

73. *Id.* at arts. 6(2)(a)-(c).

74. *Id.* at art. 6(3).

75. Financial Regulation, *supra* note 5, art. 54(1).

choices into action. If taken literally, this will severely limit the tasks that can be given to agencies, since such discretion may exist in relation to the specific functions listed in Article 6(2)(a)-(c). This conclusion might be avoided by reading the phrase “discretionary powers” more narrowly. On this view, the mere existence of choices as to how to manage a project or award a contract, for example, would not be regarded as the exercise of “discretionary powers,” and hence would not be caught by the limit in Article 6(1).

The financial arrangements for the new agencies are important, but space precludes a detailed analysis of this issue. Suffice it to say that the principles of the new Financial Regulation concerning financial transparency, internal and external audit, and the like are carried over into the scheme for executive agencies.⁷⁶ This is especially true regarding the fusion of financial power and responsibility. The director is the authorizing officer for budgetary matters within the agency⁷⁷ and therefore has the general responsibilities laid down in the new Financial Regulation. The director is required to draw up the provisional statement of revenue and expenditure, and, in his capacity as authorizing officer, he is to execute the agency’s administrative budget.⁷⁸

The new Regulation also specifies rules on agency liability in damages. The law applicable to the contract governs contractual liability.⁷⁹ Article 288(2) concerning non-contractual liability has been extended to the executive agency.⁸⁰ This follows the legal technique used in relation to “older” agencies such as the European Environment Agency.⁸¹

The provisions on review of legality have been more controversial. The initial draft Regulation stipulated that the legality of the acts of an executive agency could be reviewed under Article 230 on the same conditions as the acts of the Commission itself.⁸² It is questionable whether Article 230 could have been used to challenge the legality of actions of executive agencies, since these actions are not included in the list of reviewable acts under Article 230(1). The better view is nonetheless that such agency decisions could, as a matter of principle, be reviewed under Article 230. The Court of Justice has read Article 230 broadly so as to facilitate review of the European Parliament (“EP”)⁸³ and Court of Auditors,⁸⁴ holding that the rule of law demanded that their actions be susceptible to legal control. Moreover, Community legislation has provided for challenges to the legality of decisions made by bodies such as the Office for Harmonization in the Internal Market (“OHIM”). The OHIM is the defendant in the legality challenge.⁸⁵ The EP nonetheless argued that the executive agency was

76. Executive Agencies, *supra* note 57, arts. 12-16, 20; Financial Regulation, *supra* note 5, arts. 55-56.

77. Executive Agencies, *supra* note 57, arts. 11(3), 16(2).

78. *Id.* at arts. 11(4), 14(1), 16(2).

79. *Id.* at art. 21(1).

80. *Id.* at art. 21(2).

81. Council Regulation 1210/90 on the Establishment of the European Environment Agency, art. 18, 1990 O.J. (L 120) 1.

82. COM (00)788 final, art. 21.

83. Case 249/83, Parti Ecologiste—‘Les Verts’ v. European Parliament, 1986 E.C.R. 1339.

84. Case 193-4/87, Maurissen v. Commission, 1989 E.C.R. 1045.

85. Council Regulation 40/94 on the Community Trade Mark, art. 63, 1994 O.J. (L11) 1.

the Commission's responsibility, that the Commission should be legally responsible under Article 230, and that it should "monitor" the legality of the agency's action.⁸⁶ The Commission counter-argued that the executive agency had its own legal personality, and that therefore the Commission should not be liable for the legality of its actions.

The final version of the Regulation is a compromise between these two views: the initial legal responsibility lies with the agency, and the legality of its acts can be reviewed by the Commission, with a further review of the Commission by the Court of Justice under Article 230 if the Commission rejects the appeal.

Article 22(1) of the Regulation provides for a novel form of internal review of agency decisions by the Commission. An act of an executive agency that injures a third party can be referred to the Commission by any person directly and individually concerned, or by a Member State, for a review of its legality. Such actions must be brought within one month of the day on which the applicant learned of the act challenged. After hearing arguments, the Commission must make a decision within two months. If it does not do so, it means that the action has been implicitly rejected. The Commission is also able, of its own volition, to review an act of the executive agency.⁸⁷ The Commission can, pursuant to such internal review, suspend implementation of the measure or prescribe interim measures; it can, in its final decision, uphold the measure or decide that the agency must modify it in whole or in part. The executive agency is bound to act as soon as possible on Commission decisions taken under Article 22.

This regime for internal monitoring by the Commission is complemented by recourse to Article 230. Thus, Article 22(5) states that an action for annulment of the Commission's explicit or implicit decision to reject an administrative appeal may be brought before the Court of Justice in accordance with Article 230.

The rules on the legality of agency acts raise a number of technical legal issues. The grounds for review are not spelled out, although the implicit assumption is that they will be those used under Article 230. It seems moreover that any act of the executive agency that injures a third party can be reviewed, irrespective of whether it is binding, although the requirement that the act should cause injury may impose an indirect qualification in this respect. There also seems to be an asymmetry as to recourse to the Court of Justice. Article 22(5) is framed in terms of an annulment action whenever the Commission rejects the administrative appeal. Therefore, the executive agency itself has no such recourse when the Commission upholds the appeal.

The rules on the legality of agency acts also raise important issues of principle. Article 22 has introduced a novel form of internal review of the legality of executive agency action by the Commission. The procedure in such cases will require careful thought. Executive agencies are accorded only limited implementing powers. Policy formation remains the prerogative of the Commission. This raises two important

86. Report of the European Parliament on the Proposal for a Council Regulation laying down the Statute for Executive Agencies, A5-0216/2001, amendment 12.

87. Executive Agencies, *supra* note 57, art. 22(2).

points of principle. On the one hand, it is important who hears such cases within the Commission. It is not clear whether they will be heard by the Directorates-General (“DG”) to which the executive agency is attached, and, if so, who within the DG will hold the hearing. If the cases come to the same DG that established the agency, there is a danger of a conflict of interest. It is not easy to keep policy formation and implementation distinct. If an action challenging implementation implicates policy, there could be real objections to the Commission sitting as a “judge.” On the other hand, an issue of principle arises from the executive agency’s apparent lack of recourse to the Court of Justice when the Commission upholds the appeal. This may be especially problematic if the internal hearing is by the same DG as set up the agency. The executive agency may feel that the Commission is using its internal power of review to impose a view concerning detailed matters of implementation that is legitimately within the agency’s sphere.

The rules on the legality of executive agency acts also prompt thought about broader issues of “legal design.” These rules require us to reflect on the optimal structuring of legal liability. It is important at the outset to clear the “legal ground.” The mere fact that a body has separate legal personality, so that it can hold property and bring actions in its own name, does not *a priori* preclude making another body liable for its actions. The principled argument for holding the Commission responsible for the executive agency is that the program has been assigned to the Commission itself. The Commission may choose to deliver this program “in house” or through an executive agency. That choice should not affect legal liability, which should remain with the Commission.

The argument to the contrary is that holding the executive agency directly responsible promotes accountability and transparency. Executive agencies are lawful. They have been properly created pursuant to Article 308 of the Treaty, and their powers do not infringe the *Meroni* principle.⁸⁸ They are Community bodies and have legal personality. Placing liability directly on the executive agencies best serves the broader objectives of the administrative reforms considered above. It reinforces the conjunction of power and responsibility that is central to the new Financial Regulation. This is the approach adopted in relation to damages liability. The rules on review for legality represent a compromise: the initial and primary responsibility lies with the executive agency, which is subject to review by the Commission, with further review of the Commission’s decision by the Court of Justice.

D. Networks of National Agencies

The Commission’s White Paper clarified that externalization could be pursued through devolution of tasks to certain national public bodies.⁸⁹ This was confirmed by the new Financial Regulation.⁹⁰ Centralized management of Community activities can be undertaken by, *inter alia*, national public sector bodies, or bodies with a public ser-

88. Case 9/56, *Meroni v. High Authority*, 1958 E.C.R. 133.

89. White Paper, *supra* note 2, Vol. I, p. 10.

90. Proposal for a Council Regulation, *supra* note 5, Explanatory Memorandum, p. 19.

vice mission guaranteed by the state.⁹¹ The constraints and conditions described above⁹² apply to these bodies, just as much as when externalization is pursued through executive agencies.

A Communication devoted to the topic clarified the Commission's thinking about the use of such bodies.⁹³ The idea is to devolve executive responsibilities to national bodies, which are either public or have a public service mission guaranteed by the state. These bodies are collectively referred to as "national agencies," and this status can be conferred on existing or new entities. The agencies then act as partners in the implementation of Community policies, but the Commission retains overall responsibility for service delivery.⁹⁴ The intention is to devolve detailed implementation to national agencies, so that they have no margin of discretion on Community policy. The implementing tasks entrusted to such agencies will "in no way alter any choices taken by the Commission involving political judgment."⁹⁵ The scale of delegation to national agencies is therefore conceived to be less than to the new breed of executive agencies. This is because the Commission will retain a degree of control over executive agencies "going well beyond what it can exercise over" national agencies.⁹⁶ The Commission makes clear that use of national agencies is to be distinguished from shared administration, which the states themselves have responsibility for budget operations.⁹⁷

The Commission perceives a number of advantages to using national agencies.⁹⁸ National agencies facilitate proximity to the beneficiaries of the policy, as in the case of education and training. They foster efficiency through their specialization in a particular policy areas. National agencies can offer greater flexibility than executive agencies, since it is easier to adapt to local circumstance. The Commission has established criteria for when networks of national agencies will be appropriate.⁹⁹

The Commission is also mindful of the need for precautions when using this strategy.¹⁰⁰ Certain precautions will be necessary to avoid cumbersome procedures, ensure the visibility of the European dimension to the programs, secure the overall coherence of the program, and maintain a clear distinction between intermediaries and beneficiaries of the policies.

The Commission is against a general framework regulation for management by networks of national agencies.¹⁰¹ This is because it would be difficult to draft such a measure that could cover all possible scenarios while providing sufficiently detailed

91. Financial Regulation, *supra* note 5, art. 54(2)(c).

92. See discussion *supra*, Part IV.C

93. Communication from the Commission, Management of Community Programs by Networks of National Agencies, COM(01)648 final [hereinafter National Agencies].

94. *Id.* at para. 3.1.

95. *Id.* at para. 5.2.

96. *Id.* at paras. 5.2., 7.

97. *Id.* at para. 3.2.

98. *Id.* at para. 4.1.

99. *Id.* at para. 5.1.

100. *Id.* at para. 4.2.

101. *Id.* at para. 5.3.

common rules. The preferred approach is to provide for management by national agencies within the specific regulation governing a particular program. There will then be a Commission decision laying down the responsibilities of the Commission and the Member States in relation to the national agencies. This will be supplemented by operating agreements between the Commission and national agencies specifying the duties and powers of the latter. There will also be an agreement on decentralized measures that deals with the management of funds transferred to national agencies.

Controls operate *ex ante* and *ex post*. The former includes the Commission decision specifying the responsibilities of the Commission and Member States in respect of national agencies, the terms of the operating agreement, and of the agreement on decentralized measures. There will be internal audits to consider management and control systems within the national agencies. The latter encompasses external audits to ensure that expenditure is consistent with the legal provisions and spot checks through field visits.

E. Contract Award, Contract Specification, and the Allocation of Contractual Risk

Contracts are used to secure the delivery of many of the programs directly administered by the Commission. Problems surrounding such contracts played a large part in the fall of the Santer Commission, and the Court of Auditors has revealed difficulties in other areas.¹⁰² It is therefore unsurprising that subsequent reforms have been directed towards these contractual relationships. The type of activities that can be given to another body, the bodies that can perform these tasks, the award of the contract, and the content thereof must be considered separately.

The new Financial Regulation contains rules as to the type of activities that can be entrusted to another body. The implementing tasks must be clearly defined and supervised, and the Commission is not allowed to entrust its executive powers to third parties when “they involve a large measure of discretion implying political choices.”¹⁰³ Public lawyers will be familiar with the difficulties of divining such expressions, and there could be a legal challenge to externalization for violation of this criterion. Much will depend on how intensively the Community courts decide to review such matters.

The new Financial Regulation contains rules as to the types of bodies to whom such tasks can be assigned. Within the limits specified in the previous paragraph, the Commission can entrust tasks of public authority and budget implementation to the new breed of executive agencies (Community bodies that can receive grants) and national public-sector bodies (bodies with a public service mission guaranteed by the State).¹⁰⁴ The Commission is not allowed to entrust implementation of funds from the budget, in particular payment and recovery, to external private sector bodies, other

102. See, e.g., Court of Auditors, Special Report 16/2000 on Tendering Procedures for Service Contracts under the Phare and Tacis Programs, 2000 O.J. (C 350) 1; Court of Auditors, Special Report 12/2000 on the Management by the Commission of European Union Support for the Development of Human Rights and Democracy in Third Countries, 2000 O.J. (C 230) 1.

103. Financial Regulation, *supra* note 5, art. 54(1).

104. *Id.* at art. 54(2).

than those that have a public service mission guaranteed by the State.¹⁰⁵ The Commission is, however, empowered to entrust private sector entities with tasks involving technical expertise and administrative, preparatory, or ancillary tasks involving neither the exercise of public authority nor the use of discretionary judgment.¹⁰⁶ The dividing line between technical expertise or administrative tasks and the exercise of public authority or discretionary judgment will be difficult to maintain.

In relation to the award of contracts, the basic strategy of the new Financial Regulation is to apply the directives on public procurement to contracts awarded by the Community institutions.¹⁰⁷ The institutions are obligated to put such contracts out to tender, using the open, restricted, or negotiated procedures, or for there to be a contest.¹⁰⁸ There are safeguards against fraud by contractors. Thus, firms are excluded from the tendering process if they are bankrupt or guilty of grave professional misconduct.¹⁰⁹ A contract cannot be awarded to a firm that has a conflict of interest, nor to one that has been guilty of misrepresentation.¹¹⁰ The contracting authority is empowered to exclude such firms from contracts financed by the budget for up to five years.¹¹¹ The centrality of the authorizing officer to the new Financial Regulation is evident here, since this officer decides to whom the contract is to be awarded.¹¹²

The specification of the contract terms is equally important to avoid the mistakes of the past. Fraud and financial irregularities perpetrated by contractors will be prevented in part by the provisions concerning the exclusion of certain firms from the tendering process. This can, however, be only part of the overall strategy. It is also important to ensure the effective discharge of Community policies by those to whom tasks have been contracted-out. The specification of the contract terms is all-important. Contracts are bargains that allocate risks. The Committee of Independent Experts was critical of Commission practice in this respect. It found instances in which the contractor's task was poorly defined, there was insufficient monitoring of contractual performance, and the Community pre-financed the project by paying a large amount of the contract price "up front."¹¹³ There is an integral connection between the specification of the contract terms and the contractual objective. If the objective is set at too high a level of generality, it will be difficult to devise concrete contractual terms that can operate as a meaningful constraint on the other contracting party.

F. Reflections on Direct Management and Law

The shockwaves from the fall of the Santer Commission generated the Commission's radical re-thinking of the delivery of programs for which it has direct manage-

105. *Id.* at art. 57(1).

106. *Id.* at art. 57(2).

107. Financial Regulation, *supra* note 5, arts. 104-06.

108. *Id.* at arts. 90-91.

109. *Id.* at art. 93.

110. *Id.* at art. 94.

111. *Id.* at art. 96.

112. *Id.* at art. 100.

113. Second CIE, *supra* note 3, paras. 2.2.4-2.2.14.

ment responsibility. The Commission might well have retreated into a defensive shell after the Report of the Committee of Independent Experts. It did not do so. It embraced the majority of the Committee's suggestions. Any assessment of the emerging order must take account of the legislative and non-legislative initiatives. Three more general observations on the new administrative order are warranted.

First, the Commission's overall strategy is based on the conjunction of power and responsibility, which are integrally linked, legally and financially, with the authorizing officer being the key figure in this regard. The divide between policy and implementation is equally central:¹¹⁴ policy remains the preserve of the Commission, with implementation devolved to executive agencies, networks of national agencies, or managed through contractings subject to Commission oversight. It can be accepted that the divide between policy and implementation is difficult to preserve. This does not mean that the overall strategy is misguided. It is inevitable, for the reasons considered above and below, that the Commission will have to externalize the administration of some programs. Given that this is so, it is right that the central policy choices should be made by the Commission, which is given the primary responsibility for implementing a program. It is right that this basic precept should be enshrined in the new administrative order, even if in some instances an executive agency might "cross the line" and make some limited discretionary policy choices.

Second, just as ensuring the effective delivery of policy is an endemic problem within national polities, so it is too when programs are administered at Community level. The Commission cannot administer all policies "in house." It has neither the expertise nor the personnel to do so. Moreover, if implementation were always undertaken "in house," it would divert the Commission from policy formation. The Commission must therefore externalize the administration of some programs for which it has direct management responsibility. This cannot be avoided. Nor will one technique of externalization serve for the plethora of differing programs that the Community manages. In some cases the best technique will be to maintain control within the Commission but to contract for detailed implementation. In other cases executive agencies will be the most appropriate institutional form, and they may use contracts to facilitate fulfillment of their tasks. In yet other instances existing national agencies will be the most fitting medium, and these agencies may use contracts to fulfill their remit.

Third, there are several layers to the legal realization of these administrative reforms. This is not excessive legalism. The differing legal norms legitimate the new structures through the provision of overarching principles applicable to all forms of administration combined with detailed rules relevant to particular institutional forms. The new Financial Regulation is at the apex. It is of constitutional significance. It contains the budgetary principles, orders the different forms of Community admini-

114. There are clear analogies to reforms of the administrative landscape within national polities, such as the UK, with the shift to core departments, and Next Steps Agencies. *See* *Improving Management in Government: The Next Steps* (Her Majesty's Stationery Office, U.K., 1988); Diana Goldsworthy, *SETTING UP NEXT STEPS: A SHORT ACCOUNT OF THE ORIGINS, LAUNCH, AND IMPLEMENTATION OF THE NEXT STEPS PROJECT IN THE BRITISH CIVIL SERVICE* (Her Majesty's Stationery Office, 1991).

stration, establishes principles governing the allocation and exercise of administrative power, and allocates financial power and responsibility. The next level down is the Regulation on Executive Agencies, which draws on the principles in the new Financial Regulation. No such general regulation is contemplated for networks of national agencies. The use of such networks will nonetheless be legitimated through Community legislation in the specific areas in which they are used. There is a further legal level, concerned with the detailed operation of an executive agency, or network of national agencies. Specific Community legislation, combined with operating agreements, defines the tasks of such bodies in particular areas.

V

SHARED MANAGEMENT

We have already seen that the new Financial Regulation contains provisions dealing with shared management as well as direct/centralized management.¹¹⁵ It is nonetheless important to press further in order to understand the difficulties posed by this mode of administration and the role of law within this area. Analysis of shared management is especially important given that a number of these problems are not addressed by the new Financial Regulation. These problems will be explored in the context of the Common Agricultural Policy, which is one of the main areas in which shared administration operates.

A. The Common Agricultural Policy: Treaty Foundations

The Treaty foundations for the CAP have not altered in substance since the inception of the Community in Articles 32-38 (previously Articles 38-46). The objectives of the CAP are laid down in Article 33(1). They are:

- a) to increase agricultural productivity by promoting technical progress and by ensuring the rational development of agricultural production and the optimum utilization of the factors of production, in particular labor;
- b) thus to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture;
- c) to stabilize markets;
- d) to assure the availability of supplies;
- e) to ensure that supplies reach consumers at reasonable prices.

It is clear that these objectives are set out at a high level of generality and that they can conflict *inter se*. Decisionmaking in this area has therefore always necessitated a balancing operation of the factors listed in Article 33(1).

The Treaty does, however, provide further guidance, both positive and negative, as to the attainment of the objectives listed in Article 33(1). In positive terms, Article 34(2) stipulates that the common organization of agricultural markets may, *inter alia*, be directed towards price regulation, production and marketing aids, and storage ar-

115. Financial Regulation, *supra* note 5, arts. 149-60.

rangements to stabilize imports and exports. In negative terms, Article 34(2) provides that there shall be no discrimination between producers or consumers within the Community.

B. Implementation: From Price Support Toward Income Support

The detailed story of the CAP has been told elsewhere.¹¹⁶ It is however necessary to understand the outline of this story in order to comprehend the regime of shared management.

The principal focus of CAP policy has been on price support. A rationale for the European Community has always been that goods should be able to move unhindered by trade barriers, subsidies and other burdens. This regime has not applied to agricultural produce. The Council established common prices for most agricultural goods. There is a target price, the price that it is hoped farmers will be able to obtain on the open market; there is an intervention price, the price at which the Commission will buy up produce from the market; and a threshold price, the price to which imports are raised when world prices are less than those prevailing in the Community.

The price support system has proven very costly for the Community, consuming the largest share of the Community's budget. Community prices have, on the whole, been higher than those obtainable on the open markets. This has encouraged production and generated surplus goods. These then have to be stored at a further significant cost. If they were exported, further cost was incurred, since the CAP regime provided "restitution" to exporters to ensure that they suffered no loss on such transactions.

The Community adopted a variety of measures to ameliorate the consequences of the CAP price support regime. Quotas and the like were introduced to reduce the impact of the system. The degree of price support for particular agricultural goods was reduced. Farmers were encouraged to set aside certain farmland and hence reduce production. There was a realization that the existing regime could not continue in the wake of enlargement. Many of the applicant countries were heavily dependent on agriculture, and therefore the financial burden on the Community would increase. Incentives for CAP reform also came from external sources. The Community was under pressure from the United States and other countries to reform its protectionist agricultural policies. These pressures became particularly forceful during the Uruguay Round of the GATT negotiations in the early 1990s. The Agriculture Commissioner, MacSharry, put together a package of reforms that that were accepted after much hard bargaining within the Community and with the United States. The CAP reforms in

116. See, e.g., *id.* at chap. 7; J.A. USHER, *LEGAL ASPECTS OF AGRICULTURE IN THE EUROPEAN COMMUNITY* (Oxford University Press, 1988); FRANCIS SNYDER, *NEW DIRECTIONS IN EUROPEAN COMMUNITY LAW*, Chaps. 4-5 (Weidenfeld, 1990); WYN GRANT, *THE COMMON AGRICULTURAL POLICY* (MacMillan, 1997); ROSEMARY FENNELL, *THE COMMON AGRICULTURAL POLICY: CONTINUITY AND CHANGE* (Clarendon Press, 1997); NEILL NUGENT, *THE GOVERNMENT AND POLITICS OF THE EUROPEAN UNION*, chap. 15 (MacMillan, 4th ed., 1999); JOSEPH MCMAHON, *LAW OF THE COMMON AGRICULTURAL POLICY* (Longman, 2000); STEPHEN GEORGE & IAN BACHE, *POLITICS IN THE EUROPEAN UNION*, chap. 24 (Oxford University Press, 2001); E. Rieger, *The Common Agricultural Policy, Politics against Markets*, in *POLICY-MAKING IN THE EUROPEAN UNION* (H. Wallace & W. Wallace eds., 4th ed., 2000)..

1991-93 were of longer term significance, since it was acknowledged that support for farmers could be disaggregated from production.

This was the beginning of the shift from price support to income support. Fischler, the Agriculture Commissioner in the Santer Commission, continued this trend. Support for farmers began to be seen separately from support for production. This theme was developed in the Commission's *Agenda 2000* document.¹¹⁷ The Commission proposed large reductions in support prices, coupled with direct compensation to farmers. These proposals were, however, watered down in the Council meeting of the Agriculture Ministers in March 1999, as a result of French opposition. Further opposition from President Chirac in the Berlin European Council led to a greater dilution of the original proposals. The Commission nonetheless sought to make the "best" of the outcome of the Berlin European Council, emphasizing those aspects that fitted with its *Agenda 2000* initiative. More detailed plans have also been forthcoming to deal with enlargement. The decoupling of support from production is central to this strategy.¹¹⁸ It has not been easy to secure agreement on such changes. However, the impending pressures of enlargement, and the EU's negotiating position with the WTO, were the principal factors leading to an agreement in June 2003, the foundation of which is the disaggregation of financial support from production.

It is clear that the CAP has been "not only a tool for the technical arrangement for the management of agricultural markets, but also a tool of commercial and humanitarian policy."¹¹⁹ It has as a consequence been directly concerned with the distribution of income.

C. The Framework of Shared Management

The administration of the CAP is "shared" in the sense that the various forms of price support payments are administered jointly by the Commission and the Member States.¹²⁰ This is done through the European Agricultural Guidance and Guarantee Fund ("EAGGF"). The Guidance section deals with Community expenditure relating to agricultural structures, and the Guarantee section covers payments relating directly to the regulation of agricultural markets, refunds on exports and intervention payments. The latter is of principal concern here.

The main enabling provision for many years was Regulation 729/70.¹²¹ The Member States designated institutions within their countries to make the payments covered by the Guarantee section,¹²² and the Commission would make the funds available to the Member States for disbursement by those bodies.¹²³ The Member States

117. Commission, *Agenda 2000: For a Stronger and Wider Union*, COM(97)2000.

118. Commission Press Release (Agriculture Directorate-General), *Enlargement and Agriculture: An Integration Strategy for the EU's Member States* (February 8, 2002), available at <http://www.evropska-unie.cz/eng/article.asp?id=1134>.

119. Rieger, *supra* note 116, at 186.

120. Second CIE, *supra* note 3, para. 3.6.3.

121. Council Regulation 729/70 on the Financing of the Common Agricultural Policy, 1970 O.J. (L 94) 13.

122. *Id.* at art. 4(1).

123. *Id.* at art. 4(2). There is evidence of shift to pre-financing by Member States. See *Financial Regulation*, *supra* note 5, arts. 151-52.

were under an obligation to take the necessary measures to satisfy themselves that the transactions financed by the Fund were actually carried out correctly, to prevent and deal with irregularities, and to recover sums lost as a result of irregularities or negligence.¹²⁴ However, in the absence of total recovery, the financial consequences of irregularities or negligence were borne by the Community with the exception of the consequences of irregularities or negligence attributable to administrative bodies of the Member States.¹²⁵ The Member States and the Commission had the power to carry out inspections to ensure the probity of the transactions financed by the Fund.¹²⁶

In addition to the provisions of Regulation 729/70, protection of the Community Budget was to be secured, *inter alia*, through the system of clearance of accounts. This was particularly important since the Commission made payments to national bodies on a monthly basis and sought to recover thereafter sums that should not have been paid. Prior to 1995 the Commission was required to clear the EAGGF Guarantee accounts by December 31st of the year following the financial year concerned, that is, by 31 December of year $n + 1$. The Member States were meant to submit accounts of their paying agencies by March 31 of the year $n + 1$. The Commission then examined the accounts. The accounts were rarely closed on time, however, and it became common for them to be finalized a year late. The Commission could order a correction in relation to a particular irregularity. It could also order flat rate corrections when it discovered a systemic weakness in the procedures of a paying agency from which it could be concluded that irregular payments had been made.

Three major changes to Regulation 729/70 were made in 1995. First, it was stipulated that paying agencies had to be *accredited* by the Member States. Only such agencies could make payments.¹²⁷ When more than one agency was accredited, the Member State had to specify a coordinating body responsible for promoting the harmonized application of Community rules.¹²⁸ Second, the accounts of the paying agencies had to be *certified* by a body that was operationally independent of the paying agency.¹²⁹ Third, the timetables and procedures for *accounting* and *compliance* were separated within the system for clearance of accounts.¹³⁰ These changes were incorporated in Regulation 1258/99.¹³¹

124. Regulation 729/70, *supra* note 121, art. 8(1).

125. *Id.* at art. 8(2).

126. *Id.* at art. 9.

127. Commission Regulation 1663/95 Laying Down Detailed Rules for the Application of Council Regulation 729/70 Regarding the Clearance of Accounts of the EAGGF Guarantee Section, 1995 O.J. (L 158/6), art. 1.

128. Council Regulation 1287/95 Amending Regulation 729/70 on the Financing of the Common Agricultural Policy, 1995 O.J. (L 125/1), art. 1.

129. Regulation 1663/95, *supra* note 127, art. 3.

130. Regulation 1287/95, *supra* note 128, art. 1.

131. Council Regulation 1258/99 on the Financing of the Common Agricultural Policy, 1999 O.J. (L 160/103). *See also* Proposal for a Council Regulation Amending Regulation 1258/99, COM(00)494 final.

VI

SHARED MANAGEMENT, THE CAP, AND LAW

A. The Role of Law within Shared Management

It is interesting to reflect on the role of law within the pattern of shared management that characterizes the CAP. Unsurprisingly, there are a number of dimensions to this inquiry.

It is fitting to begin by considering legislative objectives. It is clear that there is tension between the collective interests of the Member States in the Council and the interests of individual Member States as recipients of CAP funds. The framers of legislation will approach their task with certain aims. The Member States in their collective capacity have an interest in the allocation of the Community budget and in the proper use of funds within that allocation. This objective conflicts with the accountability of individual Member States for the correct disbursement of CAP funds. Individual states have sought to minimize their liability for incorrect CAP allocations. This is reflected in the content of the legislation and the way it is applied.

This leads naturally to the design and content of legislation. Legislation will contain procedural and substantive conditions for eligibility to funds. It will specify liability if things go wrong. These matters are crucial to the way shared management operates. Law creates incentives or disincentives to certain types of action. The framing of the relevant legal provisions is of central importance to the success of the overall scheme.

The importance of legislative design can be seen from three examples, the first of which concerns the complex system of export refunds intended to bridge the gap between Community prices and those on the world market. The provisions differentiate payments according to product type and export destination. The system has been difficult to police and highly susceptible to fraud. It requires careful verification that the goods are of a kind for which the refund is claimed and that they are destined for one particular country and not for another where the prices are higher, and hence for which only a lower refund would be payable.¹³²

A second example relates to the 1995 legislative reforms that introduced the ideas of accreditation and certification of accounts. The Commission argued that it should be responsible for the accreditation of paying agencies and for the approval of the national certifying bodies, but these suggestions were rejected by the Council. The Member States are empowered to accredit agencies¹³³ and to specify the certifying bodies.¹³⁴ This has been problematic, with bodies being accredited that did not fulfill the relevant criteria.

The third example of the importance of legislative design is provided by Article 8 of Regulation 729/70.¹³⁵ Member States have an obligation to prevent irregularities

132. Second CIE, *supra* note 3, paras. 3.13.2-3.13.5.

133. Regulation 1258/99, *supra* note 131, art. 4.

134. Regulation 1663/95, *supra* note 127, art. 3.

135. *Supra* note 121. The provision has remained unchanged in Regulation 1258/99, *supra* note 131.

and to recover sums lost as a result of irregularities or negligence. However, in the absence of total recovery, the financial consequences of irregularities or negligence are borne by the Community, with the exception of losses attributable to irregularities or negligence by administrative bodies of the Member States. This creates, as the Committee of Independent Experts noted, a particular pattern of incentives:

It is difficult to believe that the administrative authorities . . . in the Member States are always inclined to highlight for the Commission instances of irregularity or negligence on their part which would result in them bearing the resulting financial consequences. It is also difficult to believe that they are never negligent. In other words the arrangements which this basic Regulation established and which still pertain do not provide the immediate disbursers of 48% (at one time as high as 70%) of the Community's budget, the EAGGF paying agencies in the Member States, with any immediate incentive for rigor and tight control of what is in effect someone else's, that is, the Community's, money.¹³⁶

Formal law, howsoever framed, can only do so much. The history of shared management in this area provides ample testimony to the way in which formal legal norms were undermined in the operation of the CAP. We have already noted the differing incentives of the Member States collectively and those of individual member States as recipients of CAP funds. Member States have bypassed formal law when it suited their interests.

This can be exemplified by the accreditation of paying agencies. Article 4 of Regulation 729/70¹³⁷ was clear: Member States were obliged to submit to the Commission details of the paying agencies, and the accounting conditions for payment. However, prior to 1996 there were "hundreds of unnotified small *de facto* agencies making EAGGF Guarantee payments in the Member States without any structured procedures for checking on their activities or accounts."¹³⁸ This illegality was practised by the Member States and tolerated by the Commission. In this context, "shared administration amounted to not much more than shared acceptance that the Regulation could be flouted."¹³⁹ This point can also be exemplified by the system for clearance of accounts. The time scale for this procedure was rarely adhered to, in part because the Member States were late in submitting the accounts of paying agencies.

The interplay between formal legal norms and practical reality is evident in the response to the preceding problems. The law attempted to catch and address the problems caused by shared management. There have been many changes in the CAP regulations. The major changes have been motivated by the need to address shortcomings of the previous legal structure. Thus the 1995 Regulations¹⁴⁰ were designed to deal with the weaknesses of the previous legal regime. The accreditation requirements, the stipulation that there must be a coordinating body when there was more than one paying agency, the certification of accounts, and the divide between accounting and compliance were all directed towards this end.

136. Second CIE, *supra* note 3, para. 3.7.5.

137. *Supra* note 121.

138. Second CIE, *supra* note 3, para. 3.9.6.

139. *Id.* at para. 3.9.6.

140. *Supra* notes 127-130.

It is also necessary to consider the effectiveness of law reform. The provision of revised legal norms may be a necessary condition for the improvement of the CAP regime. It is not, however, sufficient. The effectiveness of these new norms must be evaluated. The Court of Auditors looked at these issues twice. It concluded that the revised regime was certainly better than before, but that the new system still had deficiencies. Both reports revealed weaknesses in the accreditation system. The 1995 reforms gave power of accreditation to the Member States. The Court of Auditors found major shortcomings in many paying agencies that ought to have led the Member States to withdraw accreditation.¹⁴¹ It also found that the certifying bodies were not always operationally independent of the paying agencies.¹⁴² Its later Report found that there had been improvements, but that there were still causes for concern. There were still too many paying agencies, some of which failed to meet the criteria for accreditation, but the Member States had not generally withdrawn their accreditation.¹⁴³ The independence of certifying bodies had been resolved, but there were shortcomings in the conduct of audits.¹⁴⁴ The Committee of Independent Experts expressed itself more forcefully. It concluded that the "leeway which the Commission has allowed the Member States on accreditation and certification amounts to a lax implementation of the Regulation."¹⁴⁵

The legal regime for the CAP has also been markedly affected by the Conciliation Procedure. There will inevitably be differences of opinion between the Member States and Commission that arise in the clearance procedure. The Commission can exclude expenditure by paying agencies whenever it is not in compliance with Community rules.¹⁴⁶ Before such a decision is finalized, the Member State can invoke the Conciliation Procedure, which was introduced in 1994.¹⁴⁷ The original idea, as advanced by the Belle Group, was for a mandatory mechanism that would facilitate settlement out of court and hence reduce the number of cases brought by Member States under Article 230.

What emerged was rather different. The Conciliation Body¹⁴⁸ is instructed to try to reconcile the divergent positions of the Commission and the Member States.¹⁴⁹ This is not binding on the Commission, however, nor does it preclude a Member State

141. Court of Auditors, Special Report 21/98 Concerning the Accreditation and Certification Procedures as Applied to the 1996 Clearance of Accounts for EAGGF-Guarantee Expenditure, 1998 O.J. (C 389) 1, para. 2.11.

142. *Id.* at para. 3.2.

143. Court of Auditors, Special Report 22/2000 On Evaluation of the Reformed Clearance of Accounts Procedure, 2000 O.J. (C 69/1), paras. 13-23.

144. *Id.* at paras. 31-47.

145. Second CIE, *supra* note 3, para. 3.9.10.

146. Regulation 1258/99, *supra* note 131, art. 7(4).

147. Commission Decision 94/442 Setting Up a Conciliation Procedure in the Context of the Clearance of Accounts of the EAGGF Guarantee Section 1994 O.J. (L 182) 45.

148. It is composed of five members appointed by the Commission after consulting the EAGGF Committee. The members must be highly qualified in EAGGF Guarantee Section matters or in the practice of financial audit. Commission Decision 94/442, *supra* note 147, art. 3, as amended by Commission Decision 2000/649 2000 O.J. (L 272) 41.

149. *Id.* at art. 1(1)(b).

from using Article 230.¹⁵⁰ Conciliation is in many respects a sensible idea. The effect of the Conciliation Body has, however, been mixed. The number of cases in which it secures agreement is relatively low,¹⁵¹ and there has not been a marked drop in the cases submitted to the Court of Justice.¹⁵² In more general terms, the Committee of Independent Experts described conciliation as a “win-win” procedure for the Member States, enabling them to delay recovery of undue payments, while reserving the right to challenge the Commission’s final decision before the Court.¹⁵³

The discussion of law in CAP shared management would be incomplete if it did not take account of the role of the Court of Justice. There has been a steady stream of cases in which Member States have challenged Commission decisions concerning recovery of payments unduly made by national paying agencies. These have been brought under Article 230. The general reaction of Community lawyers is for the eyes to glaze over concerning annulment actions in relation to EAGGF funding. The Court’s contribution to the “law” that governs the CAP regime is nonetheless important. It has interpreted the legislation in a teleological manner, with important consequences for the allocation of financial responsibilities between the Community and the Member States.

The Court of Justice has allocated the risk of incorrect interpretation of the Community rules to the Member States. The Member States argued that the implication of Article 8(2)¹⁵⁴ of Regulation 729/70 was that losses flowing from an incorrect, but *bona fide*, application of a Community rule by a national authority should be borne by the Community, unless there was negligence at the national level. The Court disagreed. It held that the text of Article 8(2), viewed in the light of the preparatory documents and the language versions, contained “too many contradictory and ambiguous elements to provide an answer to the question at issue.”¹⁵⁵ The Court decided the case on the basis of Articles 2 and 3 of the same Regulation, from which it concluded that only sums paid in accordance with the relevant rules, correctly interpreted, could be charged to the EAGGF. It was for the Member States to bear the burden of other sums paid.¹⁵⁶ The Court of Justice reasoned that otherwise states might give a broad interpretation to the relevant rules, thereby benefiting their traders as compared to those in other states.

The Court also made it easier for the Commission to impose financial corrections on the Member States in the clearance procedure. Most actions for judicial review involve a challenge to the legality of flat rate corrections. These are made by the Commission when it discovers a systemic weakness in the procedures of a paying agency and concludes that a series of irregular payments have been made. Flat rate correc-

150. *Id.* at art. 1(2).

151. Court of Auditors, Special Report 22/2000, *supra* note 143, paras. 65-68.

152. *Id.* at para. 72.

153. Second CIE, *supra* note 3, para. 3.11.1.

154. Regulation 729/70, *supra* note 121.

155. Case 11/76, *Netherlands v. Commission*, 1979 E.C.R. 245, para. 6.

156. *Id.* at para. 8.

tions can be 2%, 5% or 10% of the value of the moneys disbursed, depending upon the seriousness of the deficiency and the degree of probable loss to Community funds.

The Court enunciated the following principles when dealing with these cases. It is for the Member State, in accordance with Article 8(1),¹⁵⁷ to ensure the correct implementation of the CAP, prevent irregularities, and recover sums lost due to irregularity or fraud. This is seen as an application of the general duty of cooperation found in Article 10 of the Treaty.¹⁵⁸ It is for the Commission to prove an infringement of the CAP rules and give reasons explaining the defect in the national procedures.¹⁵⁹ However, the Commission is not required to demonstrate exhaustively that the checks carried out by national authorities are inadequate, or that there are irregularities in the figures submitted by them, but to adduce evidence of “serious and reasonable doubt on its part regarding those checks or figures.”¹⁶⁰ The rationale for this “mitigation of the burden of proof” is that the Member State is best placed to verify the data required for the clearance of the EAGGF accounts. Therefore, the State must adduce evidence to show that it has carried out the necessary checks or that its figures are accurate, and that the Commission’s assertions are inaccurate.¹⁶¹

This judicial reasoning is of real importance for the operation of the clearance procedure. It legitimates the system of flat rate corrections without which the compliance aspect of clearance would be unworkable. It goes a considerable way to negate the damaging force of Article 8(2), under which the financial consequences of irregularities or negligence are borne by the Community unless attributable to irregularities or negligence by the national agencies. The Commission will carry out inspections of national procedures and conclude that there is a serious and reasonable doubt as to their soundness or as to the correctness of the national figures. The “mitigation” of the burden of proof means that the Member State must adduce evidence to dispel those doubts. It is, in this sense, much easier to attribute the irregularities to the Member States, denying them the safe haven of Article 8(2).

B. The Role of Law within Shared Management: Conclusions

Two related conclusions can be drawn concerning the role of law in the administration of the CAP.

First, sharing the administration of a complex activity is difficult. This is a trite statement, but an important one nonetheless. It was both natural and inevitable that the administration of the CAP should be shared between the Commission and national bureaucracies. The interplay between Member States and the Community in the design of the CAP, and the rules for its administration, was never going to be straight-

157. Reg. 1258/99, *supra* note 131.

158. Case C-235/97, *France v. Commission*, 1998 E.C.R. I-7555, para. 45; Case C-278/98, *Netherlands v. Commission*, 2001 E.C.R. I-1501, para. 92.

159. Case C-253/97, *Italy v. Commission*, 1999 E.C.R. I-7529, para. 6; Case C-278/98 *Netherlands v. Commission*, *supra* note 158, para. 39.

160. Case C-54/95, *Germany v. Commission*, 1999 E.C.R. I-35, para. 35; Case C-278/98 *Netherlands v. Commission*, *supra* note 158, para. 40.

161. Case C-278/98, *Netherlands v. Commission*, *supra* note 158, para. 41.

forward. The complexity of the legislative norms, combined with the divide between the collective and individual interests of Member States, produced a regime the administration of which is inherently difficult. Moves towards the simplification of the CAP legislation are to be welcomed in this respect.¹⁶²

Secondly, we should be careful about the ascription of blame when things go wrong. The tendency has to been to lay the fault at the door of the Community, and more especially the Commission. This suits the Member States and anti-European commentators. The Commission has of course been at fault by, for example, tolerating departures from existing rules and by allocating insufficient personnel to the EAGGF section. To suggest that the entire malaise of the CAP can be laid at its door, or that of the Community, is a gross oversimplification. The Community is not some reified entity that desired the CAP in its present format. The existing regime is largely the result of Member State preferences expressed in the Treaty provisions and in the CAP legislation.¹⁶³

VII

CONCLUSION

The reforms to Community administration undertaken since the fall of the Santer Commission are to be welcomed. The new Financial Regulation contains a framework of principles for the management of Community policies of a kind that have not existed hitherto. These principles are important for both direct and shared management. The creation of the new breed of executive agencies should also foster accountability in the area of direct management. It should nonetheless be recognized that law, in the form of specific Community legislation, encapsulates choices that will affect the success or failure of the particular regime, and this remains so notwithstanding the reforms discussed above. The difficulties encountered over the years with the Common Agricultural Policy provide a fitting example. For Community administration to be accountable, efficient, and legitimate, we must pay attention to both the overarching principles contained in the new Financial Regulation and also to the rules that govern particular areas of Community policy.

162. Commission Report on Simplification of Agricultural Legislation, COM(01)48 final.

163. Rieger, *supra* note 116, at 180.