Agenda for change: the future of EU development policy

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Budget support is an important instrument in EU's comprehensive development policy towards partner countries. It involves policy dialogue, financial transfers to the national treasury account of the partner country, performance assessment and capacity building, based on partnership and mutual accountability. It should not be seen as an end in itself, but as a means of delivering better aid and achieving sustainable development objectives

In this Communication, the Commission sets out a **new policy on budget support and puts forward policy proposals for an EU coordinated approach**. It aims to adapt budget support policy to the changing political and policy environment, including the Treaty of Lisbon, and to make EU budget support a more effective instrument. Member States may also consider these as recommendations as regards to their bilateral budget support, in order to achieve a coordinated approach by the EU as a whole.

Following a Communication on budget support in 2000, the Commission pioneered a results- oriented approach based on outcome indicators. It remains committed to **results-based budget support operations** and intends to further strengthen the assessment of progress and monitoring of outcomes, including by using process and output indicators,

Budget support will be provided as a driver for change to address **five key development challenges and objectives:**

1. **Promoting human rights and democratic values**: when providing EU general budget support, the Commission aims at fostering domestic accountability and strengthening national control mechanisms as a basis for improving governance and adherence to fundamental values. In cases where the partner country's commitment to fundamental values shows a significant deteriorating trend an adequate and coordinated response strategy at EU and Member States level needs to be defined and implemented. Unless there is a clear cut-situation where EU financial interests and reputation need to be protected, in which case general budget support can be suspended immediately, the response to deterioration should be progressive and proportionate. Where appropriate, measures to limit the impact on poor people should be designed jointly by the EU and Member States, in cooperation with other non-EU donors. This could include making adjustments to the size of any fixed tranche and/or reallocating funds to sector programmes, channelling funds to target groups via non-governmental organisations or reinforcing other aid modalities such as projects. In order to better reflect these fundamental changes, EU general budget support should be referred to in future as **"Good Governance and Development Contracts".**
2. **Improving financial management, macroeconomic stability, inclusive growth and the fight against corruption and fraud:** budget support, in particular "Good Governance and Development Contracts", should be used to **strengthen core government systems, such as public finance management and public administration**. As part of its objective to improve core government systems, particularly procurement, budget support will contribute to the fight against corruption and crimes involving fraud. Partner countries should be committed to inform the Commission, and in general all partners, when allegations of possible fraud or corruption are brought to the attention of the national authorities.
3. **Promoting sector reforms and improving sector service delivery:** when promoting service delivery or reforms in a specific sector on the basis of a partner government's sector strategy, the provision of sector budget support can be decisive in enhancing the government's capacity to

perform its functions and deliver sector objectives. The Commission intends to make more use of sector budget support to address sector constraints, promote reforms and improve service delivery to populations. In order to better reflect these fundamental changes, EU sector budget support should be referred to in future as **"Sector Reform Contracts".**

4. **State building in fragile states and addressing the specific development challenges of small island development states (SIDS) and overseas countries and territories (OCTs):** situations of fragility call for action to help partner countries ensure vital state functions. **The decision to provide EU budget support should be taken on a case-by-case basis** and supported by an assessment of the expected benefits and potential risks. The Commission will ensure that these decisions take into account the overall political and security situation, the financial risks, and the potential cost of non-intervention. The dynamics of change should be assessed on the basis of a **joint analysis by the EU and Member States** wherever possible. This should serve as the basis for coordination with the main development partners. A gradual and sequenced approach to EU budget support should be privileged, to best adapt to specific circumstances and to manage the risk. This should be referred to in future as **"State Building Contracts"** to better reflect these elements.
5. **Improving domestic revenue mobilisation and reducing dependency on aid:** in programming EU budget support, in particular the Good Governance and Development Contracts, **the Commission intends to give stronger emphasis to domestic revenue mobilisation, including from natural resources**. In resource-rich countries, the EU should reinforce support for comprehensive reform programmes promoting enhanced natural resource governance, transparency and accountability. In addition, **fair and transparent tax systems** are central to fostering citizenship and state-building.

EU Coordinated Approach: the EU should work with Member States in particular towards **a "single EU Good Governance and Development Contract".** Acting together would increase leverage on political and policy dialogue, as well as the impact of EU and Member States' bilateral budget support on partner countries' development. The Communication sets out the **key principles of coordination**, which include systematic information exchange while retaining the notion of sovereign decision-making.

Budget support eligibility criteria: the Commission will continue to apply the existing three eligibility criteria while reinforcing the following dimensions of each:

- **Stable macro-economic framework:** the Commission will pay particular attention to whether fiscal policy and targets are consistent with macroeconomic stability and managed according to sound rules. The assessment will be in line with the EU policy on tax and development.

- **National/sector policies and reforms**: this should focus on sustainable growth and poverty reduction in line with the policy proposed in the Communication "EU Development policy – An agenda for change: increasing the impact of EU Development Policy"

- **Public financial management**: before launching a budget support programme, the Commission will assess the institutional, legislative and regulatory framework and the performance of the public financial management (PFM) system in the partner country in order to identify a baseline upon which the dynamic approach will be based and the key reforms will be addressed during implementation by policy dialogue, capacity building and disbursement conditions. The Commission will pay particular attention to the fight against corruption and will promote a stronger use of anti-corruption provisions.

The Commission will also introduce a **new eligibility criterion**:

- **Transparency and oversight of the budget:** public availability of budgetary information is essential for promoting greater scrutiny of the budget. Based on the most relevant budget

information, the Commission will define an "entry point" to assess this eligibility criterion. Countries will have to show that they either provide the relevant information to the public or are making progress in a short period to do so. This may also imply an assessment of the statistical system and in particular of the quality of budget data. Moreover, the Commission will apply a dynamic approach by focusing on the implementation of a credible reform aimed at gradually achieving full disclosure of budgetary information. The Commission will also take into account the specific features of Fragile States and SIDS/OCTs in applying this criterion.

Managing risk: the Commission will strengthen its risk management framework for EU budget support in line with the Court of Auditors' recommendations. This will include closely monitoring progress in the fight against corruption and fraud with a view to ensuring sustainable development benefits. Commission services and where appropriate the EEAS will develop an improved risk management framework adapted to the specific risk profile of budget support, covering political governance, macroeconomic stability, development risk, public financial management, corruption and fraud. This framework will be an important complementary tool in programming, designing and implementing programmes and to inform policy dialogue.

The Commission will refrain from establishing global targets for EU budget support to third countries. It considers that the appropriate mix between the different aid modalities is best decided as part of a portfolio approach that comprises several aid modalities in response to a partner country's specificities and agreed development objectives.