

A Step Forward in ESA Budgeting

Extract from the Financial Regulations -
ESA/C/CLXXXIX/Rules (Final)

Chapter II - Planning and Budgets
Article 4 - Preparation of Budgets

4/4 The in-year flexibility limits shall be established as follows:

- the overall annual limit is defined as a percentage of the total amount of Member States' contributions to the adopted budgets. This limit shall not exceed 25%.
- the upper and lower limits of each budget, expressed in millions of euro, shall be based on an analysis of the main programmatic assumptions on which the draft budget has been prepared.

Article 5 - Adoption of Budgets and Flexibility Limits

5/4 Once the budgets of the Agency have been adopted by the relevant governing bodies, Council shall approve the in-year flexibility limits upon the recommendation by the Administrative and Finance Committee.

Article 6 - Execution of Budgets

6/2 The Director General shall be authorised to effect transfers of payment appropriations between adopted budgets up to the in-year flexibility limits approved by Council.

6/4 A report on budget execution, highlighting in particular the implementation of the in-year flexibility, shall be submitted to each Administrative and Finance Committee meeting for information.





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The new FINPOL ('Financial Policy') system in use since 1 January 2006 is helping ESA to adapt itself at a time when most countries face restrictions in their national budgets and their contributions need to be justified and used as efficiently as possible. The various flexibility systems put in place beginning in 1998 produced important improvements in the yearly consumption of ESA budgets, but they had drawbacks. FINPOL is a simpler, more transparent system, providing greater flexibility for programme managers and Member States.

Introduction

ESA programmes are legally independent from each other. Each has its own separate declaration, contributions scale and programme envelope that provide the legal basis for the yearly budgets. Practically, this means that ESA has one budget per programme – and that means more than 60 budgets must be managed in parallel.

In the past, programme managers had to include margins when planning their yearly budgets in order to cope with most of the risks inherent to any programme. But this approach created artificially high budgets with a high risk of under-consumption at the end of the year because, statistically, not all the risks for each programme materialised in the same year. This situation was unsatisfactory.

To handle that problem, while recognising that a programme must absorb risks, the Accompaniment Fund was set up in 1998, followed by the Budget Management System (BMS). They led to an important reduction in under-consumption, while introducing flexibility into the Agency's budget management.

The BMS had some drawbacks, however. Its two-level approach was complicated, thus preventing transparency. Not all the budgets were included; mandatory activities and technology programmes were excluded. To improve the system, the FINPOL reform was introduced in 2006.

Basics of the FINPOL Flexibility Mechanism

The main changes from the former Budget Management System are:

- it allows simple transfers of income and allocation between programmes, resulting in transparent management and easy reporting;
- it involves all budgets financed by contributions;
- it is closely linked to long-term planning;
- it uses the new corporate control procedures.

This combination is expected to bring major improvements for the in-year and multi-year management of ESA's budgets and programmes because, through it, the Director General can manage the yearly budgets at a corporate (Agency) level. It also ensures that resources are used by the programmes that need them, when they need them and within the approved limits.

Of course, budgetary flexibility must be limited to current activities and programmes – it is not a tool to finance new activities. It must also respect the commitments made by the Member States and prevent any transfer from one state to another at the end of the programme. Flexibility should also protect the cost-at-completion of a programme and not allow any unauthorised increase.

The degree of flexibility has set limits. Each programme is constrained by

upper and lower margins that reflect the programmatic 'reality' (based on the assessment of programmatic risks and/or uncertainties); the total flexibility allowed during a given year cannot exceed 25% of the contributions.

Flexibility Framework

The flexibility mechanism is in place to manage the programmes and optimise the use of resources. However, it does not change any former commitment made by the Member States to ESA programmes, as reflected in the programme declarations. This implies constraints on the flexibility.

Guaranteeing commitments

Whatever the transfers of contributions and allocations between programmes, transfers in the other direction have to be made before the end of the programme so that the total contributions of each Member State to each programme are constant and correspond to their original commitment.

Cost-at-Completion (CAC)

Flexibility is designed to support the management of the programmes through upward or downward adjustments of their budgets during a given year. The difference is recovered during the following years before the completion of the programme. There should be no increase in CAC as a result of using the flexibility measure.

Activities covered

Flexibility covers only the activities planned in the normal course of the programme as defined in the declaration, or problems deriving from it. At no time will it be used to finance new activities in a programme or the start of a new programme.

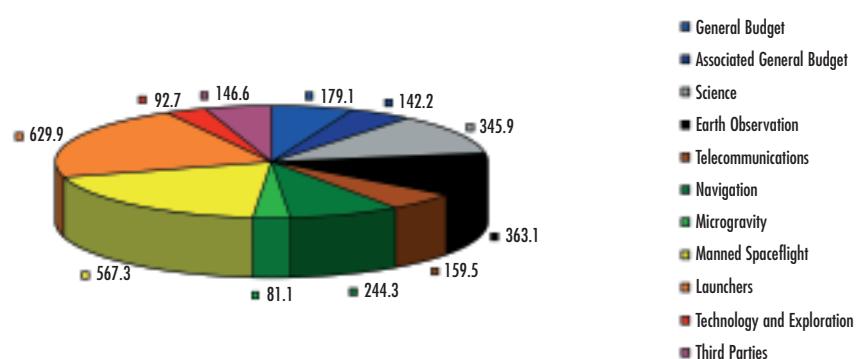
The Flexibility Process

The basic feature of flexibility is to move allocations from one budget to another during the year, depending on the real needs of the programmes, so that the best use is made of the contributions from the Member States, while respecting the commitments of the Member States in each programme. Practically, this means that when a programme receives or gives income and allocation during the course of a year, its future planning is adjusted to maintain a constant CAC.

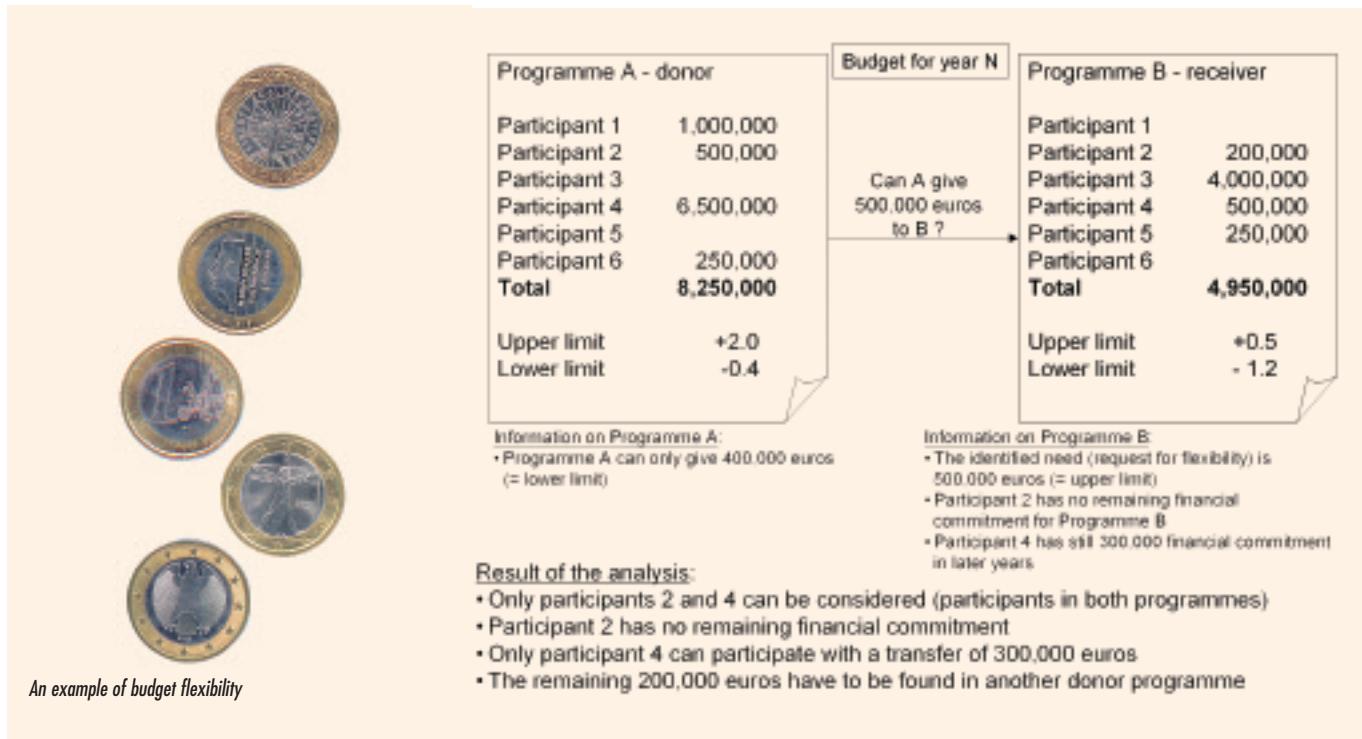
The main steps of the process are described below.

Establishing budgets and margins

At the time of budget preparation for year N+1 (during the spring of year N), the programme managers update their planning, and the data are integrated into the new long-term plan, prepared in parallel. The first year of this new plan is the basis for the next year's budgets. The level of Member States' contributions is first checked at that time, ensuring at the Agency level that the



The ESA budget by programme for 2005 (in € million)



planned contributions reasonably fit the needs of the programmes.

At the same time as fixing the appropriate budget level for each programme (corresponding to the normal course of development), an assessment of the risks and uncertainties associated with the activities planned for year N+1 is performed. This identifies the upper and lower margins, which could potentially modify the initial level of the budget.

The identified margins are submitted to the ESA Council at the time of budget approval. In addition, the overall flexibility limit is set, at no more than 25% of the budgeted contributions.

Execution of the budgets

During the course of the year, the planning and actual consumption of payment appropriations are closely monitored to anticipate the need for flexibility measures (increasing or decreasing a budget).

When an increase via the flexibility is requested, it is necessary to identify one or several 'donor' programmes, i.e. programmes that are anticipating under-

consumption in their budgets. However, this is not enough to allow the transfer of allocations because the flexibility applies to the individual contributions per Member State and not to the allocations as such. Flexibility is not only about transferring allocations, but transferring allocations from one or more countries to the same countries with the same amounts, between programmes. So when donors are identified, the viability of transferring allocations while respecting the contributions of the Member States has to be investigated and confirmed.

Elements for processing a request

The receiver and donor programmes will not have the same size of contributions. An analysis is necessary to ensure that a transfer of contributions is possible. For example:

- an amount can be transferred only if the country is a participant in both programmes (donor and receiver). So even if potential donor programmes have been identified for the right amount, it does not mean that their

structure of contributions is compatible with the receiver;

– the remaining obligations for a Member State must be considered. The amounts that have still to be paid by the state before the end of the programme must be equal or higher in the receiver programme than the amount to be transferred;

– in some cases, Member States wish to limit the flexibility on their contributions. This might occur when contributions are paid from different national sources – flexibility could create internal difficulties;

– flexibility measures should not create imbalances in the structure of contributions. This avoids having some countries with highly unbalanced contributions scales for a given year when compared to the scale in the declaration, unless the Member State agrees or wishes so.

Reporting to the Member States

A report on budget execution, highlighting how much flexibility has been given each year, is submitted to each Administrative and Finance Committee

meeting for information. It allows Member States to follow the use of flexibility during the year, with information on receiver and donor programmes and the evolution of their contribution per programme (the overall figure for the year being constant).

Processing a Request

A request from a programme to Corporate Planning & Controlling is processed as follows:

- the request is analysed to confirm the need and that there is a margin available for flexibility;
- the potential donor(s) are identified (the Directorate requesting the increase provides this information, if possible);
- the contribution structure and availabilities are analysed, of both the

receiver and the donor(s) to validate the possibility of flexibility and to identify the detailed transfers to be implemented;

- a go/no-go decision is taken on the feasibility, with the arbitration of the Director General and the Directors if priorities have to be defined;
- the transfer is executed, and the income and expenditure budgets are updated.

Specific Exclusions

The monies to be considered for flexibility are those from contributions of the ESA Member States. All other income is excluded, in particular the amounts financed by the European Union or third parties.

In addition, the Member States can indicate specific exclusions, mainly when

contributions are from specific national sources (for example, when another Ministry or organisation funds programmes in specific domains).

Conclusions

FINPOL allows the Director General to adjust, in a very simple and transparent way, each individual annual budget to the real needs of a programme as it evolves during the year, within limits agreed by the Council and without putting an additional burden on the Member States while, at the same time, guaranteeing that the overall commitment of each state to each programme is respected. It can only serve to improve the efficiency of running the Agency and its programmes.

