

Policy Brief

The EU's new rule of law mechanism

How it works and why the 'deal' did not weaken it

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#RuleOfLaw
#EuropeanCommission
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After Hungary and Poland almost derailed the EU budgetary negotiations over rule of law conditionality, the EU found itself in a weeks-long game of chicken before the drama finally culminated in the European Council conclusions of December 2020. The conclusions were widely criticised for postponing the enforcement of the rule of law mechanism and for upsetting the EU's institutional balance. In this Policy Brief, Thu Nguyen explains how the rule of law mechanism works and takes a more balanced approach: The rule of law mechanism was not weakened by the conclusions, nor did the European Council encroach upon the Commission's prerogatives in a meaningful way.

Introduction¹

Rule of law conditionality was one of the [stickiest issues](#) surrounding the negotiations on the European Union's long-term budget, the multiannual financial framework (MFF), and the recovery fund. After Poland and Hungary vetoed the budgetary package in protest against the adoption of the rule of law mechanism, the EU found itself in a nerve-wrecking [game of chicken](#) for a few weeks. The drama finally culminated in a deal between Hungary, Poland, and the German presidency shortly before the European Council summit of 10/11 December. The deal was subsequently confirmed by all 27 EU governments in the form of European Council [conclusions](#). The Commission confirmed the part of the conclusions that refer to its role in a [statement](#).

The conclusions were widely criticised both for postponing the enforcement of the rule of law mechanism and for upsetting the EU's institutional balance. This policy brief takes a more balanced approach: The rule of law mechanism was not weakened by the deal, nor did the European Council [encroach](#) upon the Commission's prerogatives in a meaningful way. More generally, the deal must

¹ I would like to thank Matteo Bonelli for his input and comments on this paper.

be assessed against the backdrop of the budgetary negotiations in which it was concluded. It is not perfect. But in the end, it did succeed in meeting an urgent requirement: Clearing the way for adopting an historic recovery fund and budget worth €1.8 trillion as well as a novel mechanism linking EU funds to the respect for the rule of law.

The Council formally adopted the regulation on the mechanism on 14 December 2020 with only Hungary and Poland objecting. The European Parliament adopted it on 16 December.

The rule of law mechanism: How does it work?

The rule of law mechanism allows for financial sanctions in cases where breaches of rule of law in an EU member state have a sufficiently close connection to the EU budget. The [final version](#) of the regulation laying down the mechanism is the result of a compromise between many different positions, following a long and cumbersome negotiation process.

Scope

Two conditions must be fulfilled for the EU to sanction member states: (1) Breaches of the rule of law in a member state, **and** (2) these breaches must affect or seriously risk affecting sound financial management of the EU budget or protection of the Union's financial interests in a sufficiently direct way.

The regulation lists those areas where breaches of the principle of the rule of law can impair the functioning of institutions or procedures related to the use of EU funds in such a way that sanctions can be triggered. They are the following:

- a. the proper functioning of the authorities implementing the Union budget;
- b. the proper functioning of the authorities carrying out financial control, monitoring and audit, and the proper functioning of effective and transparent financial management and accountability systems;
- c. the proper functioning of investigation and public prosecution services in relation to the investigation and prosecution of fraud;
- d. effective judicial review by independent courts of actions or omissions by the authorities referred to above;
- e. prevention and sanctioning of fraud and imposition of effective and deterrent penalties on recipients by national courts or by administrative authorities;
- f. the recovery of any unduly paid funds;
- g. effective and timely cooperation with OLAF and EPPO in their investigations or prosecutions;
- h. other situations or conduct of authorities that are relevant to the sound financial management of the Union budget or the protection of the financial interests of the Union.

If one of the above is impaired, the Commission can start the procedure that can in the end lead to sanctions

Sanctions

The sanctions available under the regulation range, inter alia, from the suspension of payments via eschewing new commitments to non-disbursements of loans. Budgetary commitments are legal commitments by the EU to cover subsequent expenses. A suspension of commitments would mean that member states cannot budget for new projects with EU funds. Payments are pay-outs of the budgetary commitments entered into. A suspension of payments would mean

that member states are not reimbursed with EU funds for projects already in train. Any measure adopted must be proportionate, meaning it must reflect the extent to which the breach of the rule of law impacts on the Union budget. This includes the nature, duration, gravity and scope of the breach. Beyond that, the Commission is relatively free to choose the preferred sanction. In any event, member states remain obliged to ensure that the final recipients or beneficiaries are not affected by the measure.

Procedure

If the Commission has reasonable grounds to believe that the conditions for sanctions are fulfilled, it notifies the member state in question and explains its misgivings. The member state responds and proposes measures to remedy the Commission's concern within a time period specified by the Commission of at least one month and a maximum of three months. The Commission then decides within one month whether to propose sanctions to the Council. If it so decides, the member state again has one month to submit new observations, in particular regarding the sanctions' proportionality. The Commission in turn has a month to submit a proposal for an implementing decision to the Council. The Council must then adopt its own final decision (it can adopt, amend, or reject the proposal) within another month by qualified majority unless the emergency brake is triggered (see immediately below).

Emergency brake

The regulation also contains a so-called emergency brake. A member state unhappy with the Commission's assessment can refer the matter to the European Council for discussion. The suspension of funds can thereby be delayed by up to three months, albeit not stopped as the European Council does not have to reach a consensus on the matter.

Summary

The rule of law mechanism will add a useful new tool to the EU's toolbox to deter countries from embarking on certain breaches of the rule of law that can be connected fairly directly to the EU budget. If a member state undertakes such a breach in future, the Commission will be able to dangle the threat of a suspension of funds in front of the member state to force it to back down. The Commission will likely do so only in situations where it can reasonably expect to win any escalation of the dispute, i.e. where it knows a majority of member states back it. It is decidedly not a tool to undo all previous rule of law breaches as this would mean establishing a link to the EU budget in each and every case. Therefore, it is important not to raise expectations too high.

The European Council conclusions: What do they mean for the mechanism?

The [December European Council conclusions](#) have first of all no legal force. The European Council is not a legislative body; from a *legal* point of view what matters is the text of the regulation as adopted now by the co-legislators. But the conclusions bind the member states and the Commission *politically* to some extent – with the caveat that European Council conclusions have previously been disregarded as circumstances change. And in this case, it is clear to everyone that these conclusions were adopted for the sole purpose of helping member states save face while accepting defeat, under very particular circumstances.

Still, it is useful to analyse whether the conclusions change anything substantially. By and large the conclusions merely confirm the written text of the regulation. The references to the principles of objectivity, non-discrimination and equal treatment; to the mechanism's subsidiarity character; and to the proportionality of the measures are all contained within the final, unchanged regulation. Equally, the reference to a link between rule of law breaches and the Union budget, including the statement that a "mere finding that a breach of the rule of law has taken place does

not suffice to trigger the mechanism”, is simply a reiteration of the regulation’s text. In fact, the regulation’s own [legal basis](#) requires it to demand such a link.

In a few points, however, the conclusions do go beyond the regulation’s text. The most controversial point is that it states the Commission’s intention not to propose sanctions under the regulation until the Court of Justice of the European Union (CJEU) has delivered a judgment. More precisely, it states that the Commission will develop guidelines on how to apply the regulation; these will not be finalised until after the Court has ruled on an action for annulment that will likely be brought to the Court by Hungary and Poland. Only then will the Commission propose measures. This paragraph was widely criticised for postponing any enforcement of the regulation, but the key question is how a Commission proposal for measures would indeed be delayed in practice.

Article 263 TFEU gives member states the right to challenge the legality of legislative acts before the CJEU and to ask for their annulment within two months of publication of the contested measure. This means that, assuming the rule of law conditionality regulation is published on 1 January 2021, Hungary and Poland will have until 1 March 2021 to file an action for annulment. The average duration of a direct action before the Court was [19.1 months](#) in 2019. The President of the Court can also decide to deal with the case in an [expedited procedure](#). The average duration of direct actions in expedited procedures was [10.3 months](#). This in turn means that, depending on the type of procedure, we could expect a CJEU ruling on the matter somewhere between January 2022 and October 2023 – even though the average implies that the ruling could come well before the end of 2021. The European Parliament has already [announced](#) that it would ask the Court to decide on the matter in an expedited procedure.

In addition, it must be borne in mind that preparations for building a case against a member state that has breached the rule of law take time and is then followed by a lengthy back-and-forth process as outlined above, before any sanctions can be proposed. It is delusional to believe that the Commission would have immediately moved to sanction countries after the regulation’s entry into force in the absence of the European Council conclusions.

Furthermore, as explained above, the mechanism should mostly be seen as a deterrent for very specific steps member states are taking or are planning to take. Nothing will stop the Commission as of 1 January 2021 from making it known publicly that it will examine the implications of a proposed policy for the use of EU funds. Everyone will understand what that means. For a deterrent to be credible, member states only need to believe that the Commission would eventually be ready and willing to propose sanctions – even an 18-month delay would not remove that credibility as long as a political majority for sanctions is clearly there.

Many observers have criticised the conclusions for allegedly calling on the Commission to delay sanctions until the CJEU has ruled: The argument goes that this is supposed to violate the principle of institutional balance by, first, according a suspensory effect to an action of annulment and, second, by having the European Council issue instructions to the Commission on how to apply the regulation. Both arguments are formally correct: Actions before the Court legally do not have suspensory effect and only the Court itself can order the suspension of the application of a contested measure under article 278 TFEU. And the Commission acts independently as the Guardian of the Treaties under article 17 TEU and as such cannot be instructed by the European Council – but it should also be noted that the conclusions do not contain any direct instructions to the Commission but merely state the Commission’s intentions.

Concerning the institutional balance, this section of the European Council conclusions does look politically problematic. It can be read as the European Council telling the Commission how to apply a regulation, which is not its job under the Treaties, and the European Parliament is right in its [resolution](#), adopted alongside the regulation, to call on the Commission to be independent in its application of the mechanism. Yet, this does not change the fact that European Council conclusions are not legally binding on the Commission. The European Council cannot order the Commission to do anything.

As the Guardian of the Treaties, the Commission has a high margin of discretion on how it uses its powers. It can, for example, not be forced to take action against member states for infringing the EU Treaties. If the Commission therefore were to decide of its own accord to refrain from proposing measures before a certain date – let's say before the CJEU has ruled – because it knows it would not get the necessary support in the Council before then, this decision would fall within its rights. Thus, we can criticise the delay of sanctions for many reasons, not least *political* reasons, but not *legally* for reasons of encroachment by the European Council on the Commission's powers through a political, non-binding declaration.

Moreover, another question in this context is what the regulation is designed to achieve. If its aim is merely to sanction member states ex post for breaching the rule of law, a delayed suspension of funds is indeed a regrettable development as has been pointed out by many commentators. If its aim is, however, to prevent member states from breaching the rule of law through the credible *threat* of sanctions, any delay in proposing these would affect the regulation's effectiveness far less. We now have a mechanism with much more credible deterrent effects than under the procedure available under article 7 TEU. Even if sanctions become possible only after one or two years, which seems likely, that is in the long run a big step. Something that was previously impossible becomes possible, and the EU's rule of law toolbox becomes much stronger.

Conclusion: Not a perfect but a necessary compromise

The deal that the German Council presidency brokered with Hungary and Poland is far from perfect. On the contrary, it is rather dubious from a political and institutional standpoint. Nor is the final version of the regulation on rule of law conditionality a perfect compromise. And yet, all in all, this is a good deal: We have a MFF 2021-2027. We have a budget 2021. We have a historic recovery fund, which is sorely needed by the EU member states facing not only a second (or third) wave of the pandemic but also a second wave of economic downturn while still recovering from the first. And we have, for the first time in history, a mechanism that allows the EU to financially sanction member states that breach the rule of law. Its application may be delayed for a few months by the deal that has been struck. But, from a long-term perspective, this is a laudable achievement, and having the Court's seal of approval for the mechanism could well enhance its legitimacy once in use.

At the same time, one must see the mechanism for what it is: a good and solid addition to the toolbox the EU has at its disposal to protect the rule of law in the member states. But it is not a miracle solution for all of the EU's problems; much will still depend on the Commission's and member states' willingness to use it. In light of this, the question must be asked, also of arch-critics of the deal, what a better alternative would have been – because it would certainly not have been sacrificing an historic and sorely needed €1.8 trillion budget package.

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