FINANCE DEPARTMENT

Alicante, 22 October 2020

Bi-annual report on the Office's financial situation (2018 – 2019)

Abstract

This report analyses the financial situation of the European Union Intellectual Property Office (hereinafter, "the Office") on a bi-annual basis. In this regard, it describes the legal requirement stemming from Article 172(9) of the Regulation (EU) 2017/1001 of the European Parliament and of the Council of 14 June 2017 on the European Union trade mark, the financial situation for the 2018 and 2019 financial years, the financial operations performed under Article 152(5) and (6) and Article 172(5) and (7).

Disclaimer

The information contained in this document is extracted from the Office´s annual accounts for the financial years 2018 and 2019. This report has not been adopted nor endorsed by the Office´s governing bodies.

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EXECUTIVE SUMMARY

This report has been drawn up by the Office pursuant to Article 172(9) of Regulation (EU) 2017/1001 of the European Parliament and of the Council of 14 June 2017 on the European Union trade mark [(1)] (hereafter EUTMR). It describes the Office´s financial situation for the period 2018 and 2019 and, in particular, the financial operations performed under Article 152(5) and (6) and Article 172(5) and (7), as follows:

- **European Cooperation:** financial support to promote convergence and tools in order to ensure effective participation of the national and regional IP offices of the Member States up to 15% of the yearly revenue of the Office;

- **Enforcement**: financial support to awareness raising and fighting against counterfeiting, focussing on establishing standards and practices as well as organising education and training activities within the European Cooperation context and within the 15% threshold;

- **Offsetting**: financial support to offset costs incurred by the national and regional IP offices of the Member States and by other authorities nominated by Member States based on the specific tasks which they carry out as functional parts of the EU trade mark system.

  The total amount for offsetting is 5% of the Office's yearly revenue. The distribution amongst Member States is based on a distribution key determined by the Management Board.

  Offsetting can only take place if no budgetary deficit is incurred in accordance with Article 104(5) and (6) of the Office's Financial Regulation.

The Office attaches great importance to the reporting obligations as a regular means of evaluating the health of its overall solid financial situation. Once again, the Office's annual accounts underline the solid financial situation for the years 2018 and 2019. In 2019, revenues reached EUR 257.8 million and expenditure EUR 254.4 million whereby the Office's productivity indicators show that unit costs evolve positively. The Office manages an overall volume of treasury of EUR 513.4 million, part of which is due to the reserve fund required by Article 172(10) of the EUTMR and which amounted to EUR 238.6 million by the end of 2019.

Expenditure related to European Cooperation in line with Article 152(5) and (6) reached EUR 32.5 million in 2019 (EUR 29.9 million in 2018) respecting the upper limit of 15% of the budgeted revenue for these years.

Following the budgetary result according to Article 104(5) of the Office's Financial Regulation, the offsetting of costs to the Member States was triggered for 2018 and 2019 for EUR 12.0 million and 12.7 million respectively.

In 2019, the Office Management Board approved a new Strategic Plan (SP2025) [(2)] which

[(1)] OJ L 154, 16.6.2017, p. 1–99.
[(2)] Decision No MBBC-19-18.

builds upon its predecessors by continuing to solidify the value of the European Union Intellectual Property Network for the benefit of users with the following vision: “IP value for business and citizens in Europe”.

Moreover, in view of the discussions concerning the new Multiannual Financial Framework (MFF) for 2021-2027, the Office has launched again a reflection on how its accumulated surplus could be used to support initiatives of common interest with the Union needs and priorities in the area of IP.

Besides, the European Court of Auditors (ECA) recently invited the Office to identify a more productive use for its accumulated surplus. In this context, the Office decided to fuel discussions with the European Commission on mechanisms allowing the possible use of the Office’s surplus in a productive manner.

In this context, as from 2020, the agreements with the European Commission regarding EU-funded projects are being treated as ‘separate budget items’ within the meaning of Article 10(4) of the Office’s Financial Regulation.

In addition, starting with 2021 budget, the Office’s financing to the European School of Alicante, under a renewed agreement concluded in accordance with Article 7 of the Office’s Financial Regulation, is also proposed to be treated separately.

In 2021, the Office plans to also use part of its surplus to co-finance at 99% and implement a EUR 20 million SME IP action under a contribution agreement within the COSME programme in the context of the post COVID-19 recovery plan of the Commission.

Through these various initiatives, the Office continues to seek to unlock funds by mobilising its accumulated financial surplus in support of EU policies in the field of IP.

With respect to the future, the financial outlook confirms the sustainability of the Office´s resources. After a sudden decrease of incoming applications in the first weeks of the COVID-19 crisis, an important recovery is noted since then, resulting in a total revenue probably slightly above budget in 2020 and a continued increase in the region of 4-5% in consecutive years.

As the growth in expenditure is more moderate, the unit costs will continue their favourable evolution, indicating increase levels of efficiency resulting among others from the Office´s investments in Strategic Plan projects.

1. INTRODUCTION

According to the EUTMR, and in particular to Article 172(9), the Office shall prepare on a biannual basis a report for the European Parliament, the Council and the Commission "on its financial situation, including on the financial operations performed under Article 152(5) and (6) and Article 172(5) and (7), as follows:

- **European Cooperation.** The Office provides financial support to projects that promote convergence and tools in order to ensure the effective participation of the central industrial property offices of the Member States and the Benelux Office for Intellectual Property. These projects must not exceed the total limit of 15% of the yearly revenue of the Office. This support can be done by means of grants or in-kind contributions (Article 152(5) EUTMR).

- **Enforcement**. The Office provides financial support to cover projects that contribute to awareness raising and fighting against counterfeiting, focussing on the implementation of established standards and practices as well as at organising education and training activities (Article 152(6) EUTMR).

- **Offsetting**. The Office shall, under certain circumstances, offset costs incurred by the central industrial property offices of the Member States, by the Benelux Office for Intellectual Property and by any other relevant authority to be nominated by a Member State as the result of the specific tasks which they carry out as functional parts of the EU trade mark system (offsetting). The total amount corresponds to 5% of the yearly revenue and the distribution amongst Member States must be based on a distribution key determined by the Management Board on the basis of fair, equitable and relevant indicators. (Article 172(5) EUTMR).

  On a proposal from the Office and after having consulted the Budget Committee, the Management Board may increase the percentage to a maximum of 10% of the yearly revenue, provided that there is a sufficient budgetary surplus available (Article 172(7) EUTMR).

Therefore, the report reviews the information of the Office's financial situation for 2018 and 2019, covering its revenues, expenditure, treasury and reserve fund, followed by a detailed presentation of the EU cooperation activities and the offsetting of costs to Member States. Additional information regarding the activities and finances of the Office, in particular the Annual Report and the Annual Accounts, can be found on the Office´s website[3].

[3] Links to the Annual Reports and to the Annual Accounts

2. FINANCIAL SITUATION 2018 – 2019

The main source of information about the financial situation of the Office are the Annual Accounts. Due to the fact that the above mentioned articles of the EUTMR have to be read in conjunction with the Office's Financial Regulation, and in particular Articles 6 and 104, the relevant part of the Annual Accounts for the purpose of this report are the chapters 3 and 4, that is the Report on Budget Implementation and the Report on Budgetary and Financial Management.

Additional information on the financial situation of the Office can also be found in the Office´s Annual Report, in particular its appendix on resources management and assurance [(4)].

The legal reform of the Office's founding regulation which entered into force on 23 March 2016 introduced a new legal reporting obligation consisting in the bi-annual report. A first report of this kind was issued in 2018 covering the financial years 2016 and 2017. This report covers the period 2018 and 2019.

2.1 THE OFFICE'S BUDGET REVENUE

The Office's revenue is composed of its own revenue coming essentially from European Union trade mark (EUTM) and Registered Community design (RCD) fees. Other revenue concerns miscellaneous services and administrative fees for insufficient funds for current accounts. Another source of revenue concerns interest income.

Assigned revenue relates to funds received from the European Commission for the implementation of technical cooperation projects in the area of industrial property (external assigned revenue) in compliance with the corresponding contribution agreements signed between the Office and the European Commission and to a small part to recoveries of amounts initially paid from the Office's budget (internal assigned revenue). These amounts are treated as assigned revenue according to Article 20 and 21 of the Office´s Financial Regulation [(5)].

(EUR) *31-Dec-19*

REVENUE		
	2019	2018
OWN REVENUE	**254,602,712.18**	**239,456,849.39**
Revenue from fees	254,527,768.50	239,210,946.75
Other revenue	74,943.68	245,902.64
INTEREST	**29,398.71**	**16,085.05**
ASSIGNED REVENUE	**3,147,600.35**	**5,411,077.68**
EU-funded projects	2,532,290.09	3,272,419.75
Other assigned revenue	615,310.26	2,138,657.93
TOTAL	**257,779,711.24**	**244,884,012.12**

(4) 2019 Annual Report, Appendix C. Management of Resources and Declaration of Assurance, pp C.1-18.
(5) For the purpose of Article 104(5) of the Office´s Financial Regulation, only own revenue and interest income have to be taken into account, but not the assigned revenue.

2.1.1 OWN REVENUE

Compared to the execution of the year 2018, the number of EUTM applications received in 2019 reached 160 377, which represents a growth of 5.2% [(6)], broken down in 3.5% growth of direct applications and 13.5% growth of international applications under the Madrid Protocol.

Regarding RCD filings, 111 598 have been received in 2019, that is 3.5% above the 2018 filings ([7]), broken down in 3.8% of direct filings and 3.0% of international filings.

In 2019, the Office accrued [(8)] 155 377 EUTM applications and 108 467 design fees compared with 148 424 EUTM applications and 106 170 design fees in 2018. The Office receives revenue not only from fees relating to the registration of trade marks and designs, but also from fees for post-registration procedures, such as renewals, recordals and inspections. EUTM and design fees recorded as revenue increased by 6.4% in 2019 and 3.1% in 2018, compared with 2018 and 2017 respectively.

The distribution of revenue from EUTMs and RCDs is relatively stable. In 2019, the EUTM share of the total fees revenue stood at 88.3% compared with 88.2% in 2018 and 88.3 % in the two preceding years.

In 2019, 64.8 % of EUTM filings came from EU Member States and 35.2 % from non-EU countries, which represents a similar distribution as in 2018.

Basic fees, fees for additional classes, international application fees and renewal fees made up 96.2% of all EUTM fees received in 2019, the same percentage as in 2018.

2.1.2 INTEREST

The Office's policy is to benefit from interest generated mainly by short-term deposits and current accounts. As in former years, and given the situation of the financial markets, security aspects had clear priority over yield in 2019 and 2018.

The amount of EUR 29 399 is budgetary revenue. Given the Office's focus on security and the current level of the European Central Banks deposit rate, negative interests have to be paid for the funds held with Central Banks and to a lower extent also with commercial banks. For more information, see also the chapter on treasury.

2.2 THE OFFICE'S BUDGET EXPENDITURE

The Office's expenditure is composed of the following elements [(9)]:

- Title 1 – Staff expenditure (salaries and social security expenses, professional travel expenses, welfare, medical service, etc.);

[(6)] Trade mark filings in 2018 reached 152 494, 4.1% above the previous year.
[(7)] Design filings in 2018 reached 107 618, 2.1% below the previous year.
[(8)] This means that the fee payment has been received and the filing fee has been verified and included in the accounts.
[(9)] For the purpose of Article 104(5) of the Office´s Financial Regulation, only expenditure related to titles 1, 2 and 3 has to be taken into account, but not the assigned revenue (EU funded projects, other assigned revenue), nor the offsetting to Member States.

- Title 2 – Buildings and equipment (all expenses related to the Office's premises, IT infrastructure and programming, technical and workplace-related equipment, telecommunications, administrative translations, consultancy, etc.);
- Title 3 – Expenditure related to the registration of trade marks and designs, as well as cooperation with National and Regional IP Offices and support for the Observatory;
- Title 4 – EU funded projects: expenditure related to the implementation of technical cooperation projects in the area of industrial property in line with the corresponding contribution agreements signed with the European Commission. These funds are treated as external assigned revenue (see also comments made under the chapter revenue).
- Title 5 – Offsetting to Member States: Expenditure covering costs incurred by the Member States IP offices as foreseen in Article 172(5) of the EUTMR.

The following table and the subsequent analysis are made by using a presentation by nature of the Office's expenditure, in line with the presentation of the Annual Accounts.

(EUR) *31-Dec-19*

EXPENDITURE		
	2019	2018
STAFF EXPENDITURE (TITLE 1)	**123,041,652.46**	**114,054,773.64**
Expenditure paid during the financial year	122,429,744.30	113,482,672.79
Carryover of expenditure	611,908.16	572,100.85
OPERATING EXPENDITURE (TITLE 2)	**63,483,677.08**	**65,571,683.00**
Expenditure paid during the financial year	53,634,460.06	55,586,150.77
Carryover of expenditure	9,849,217.02	9,985,532.23
SPECIFIC EXPENDITURE (TITLE 3)	**52,410,228.71**	**53,350,685.73**
Expenditure paid during the financial year	42,044,634.13	42,551,825.50
Carryover of expenditure	10,365,594.58	10,798,860.23
OFFSETTING TO MEMBER STATES (TITLE 5)	**0.00**	**0.00**
Expenditure paid during the financial year	0.00	0.00
Carryover of expenditure	0.00	0.00
EU-FUNDED PROJECTS (TITLE 4)	**14,808,153.61**	**16,641,354.84**
Expenditure paid during the financial year	3,857,605.30	4,365,491.32
Carryover of expenditure	10,950,548.31	12,275,863.52
OTHER ASSIGNED REVENUE	**615,310.26**	**2,138,657.93**
Expenditure paid during the financial year	0.00	0.00
Carryover of expenditure	615,310.26	2,138,657.93
TOTAL	**254,359,022.12**	**251,757,155.14**

The expenditure in title 1 increased by 7.9% in 2019 and 9.0% in 2018 as compared to the respective previous year. The main reason for this is the increase in remuneration of staff in both years as explained hereafter and the increase of the Office's contribution to the European School in 2018.

The increase in remuneration of staff is the consequence of an increase of the average staff cost (indexation, steps, increase of weighting factor) and the staff level (of any type) by 3.7% in 2019 and 6.2% in 2018 compared to the respective previous year as can be seen in the following table. This increase has also to be seen in the light of the evolution of trade mark and design filings as shown in chapter 2.1.1.

Nº of staff in place

Year	Officials	Temporary agents	Contract agents	Agency staff (*)	Seconded national experts	Trainees	Special advisors	Total at year-end
2019	559	270	199	21	65	98	4	**1,216**
	1,028							
2018	556	241	201	23	52	96	4	**1,173**
	998							

The expenditure in title 2 decreased in 2019 by 3.2% as compared to the year 2018 and continued a downward trend started in 2017 with a decrease of 13% as compared the previous year. The main reason for decrease in expenditure are linked to the implementation of the SP2020 projects, whose appropriations are concentrated mainly in this title, as investments are progressively reducing while the projects are implemented

The expenditure in title 3 has decreased by 1.8% in 2019 as compared to 2018 when it was at the same level as in 2017 as a consequence of reductions regarding expenditure related to the Observatory, IP translations, communication and promotion, partially compensated by an increase in EU Cooperation activities.

Expenditure in title 4 is related to EU funded projects. These are technical cooperation projects with third countries in the area of industrial property funded by the European Commission and where the Office performs all budget implementation tasks. The degree of expenditure depends on the project plans agreed upon through contribution agreements with the European Commission.

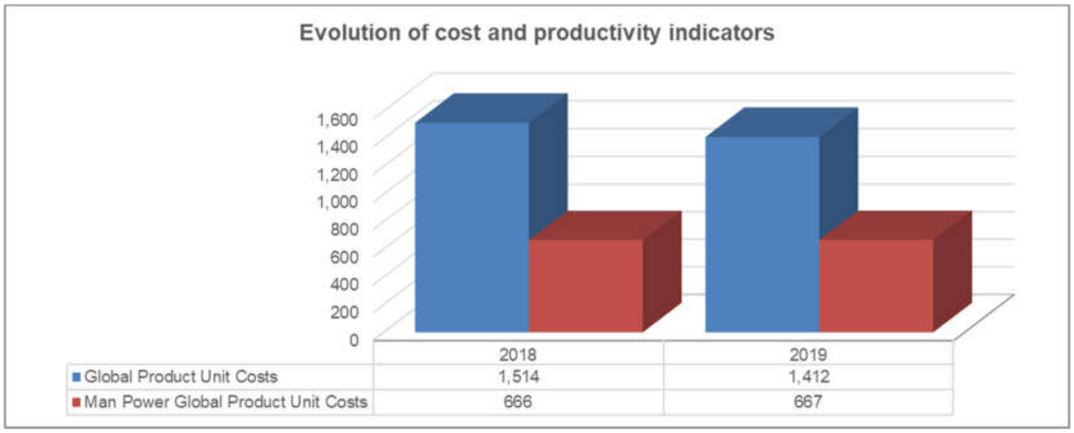
From 2020 onwards, this title will include all the Office´s contributions to EU policies in the area of IP which are to be treated separate budget items' within the meaning of Article 10(4) of the Office's Financial Regulation. This includes not only the Office´s contribution to EU-Funded projects but also, as of 2021, the Office´s financing of the European School of Alicante and the Office´s contribution to a EUR 20 million SME IP action within the COSME programme in the context of the post COVID-19 recovery plan of the Commission, all performed under agreements concluded with the European Commission in accordance with Article 7 of the Office´s Financial Regulation. Hence, the combination of Article 7 and Article 10(4) of the Office´s Financial Regulation allows the Office to use part of its financial reserves in support of EU policies.

The Office also has an Activity Based Budget (ABB) to plan and monitor the use of resources and allow for performance based decision making. The budget structure by nature (title, chapter, article and budget line) is therefore complemented with a hierarchic dimension based on lines of action (SP2020) or strategic drivers (SP2025), cost headings and activities/projects.

In this context and with a view to have an objective measure of Office's global performance over time, showing the evolution of cost and productivity, two indicators are used [10]:

- The Global Product Unit Cost;
- The Manpower Global Product Unit Cost.

[10] The Global Product Unit Cost represents the cost of a generic product and is the result of dividing the expenditure by the number of generic products. The number of generic product can be defined as the weighted average (by revenue) of the volume of individual products. The Manpower Global Product Unit Cost which is calculated in the same way as the previous but using only staff costs.



Both indicators show a favourable evolution of the Office´s efficiency.

2.3 THE OFFICE’S RESERVE FUND

2.3.1 THE CHARACTERISTICS OF THE RESERVE FUND

Since the entry into force of the EUTMR and according to Article 172(10), the Office’s reserve fund must cover the equivalent of the sum of the appropriations of titles 1, 2 and 3 of the budget of the corresponding year.

The mechanism for fund allocations and withdrawals is decided by the Office’s Budget Committee within the budgetary procedure and is based on the following elements:

- The reserve fund aims to ensure the continuity of the Office’s operations and the execution of its tasks, covering one year of its operational expenditure. The Office’s tasks are defined by Article 151 EUTMR.
- Paragraph 1 of Article 100 of the Office´s Financial Regulation clarifies that the volume of the reserve fund, and therefore its allocations or reductions, depends on the estimated budget appropriations envisaged for titles 1, 2 and 3 of the Office’s Budget.
- Pursuant to Article 101, the required level of the reserve fund does not include an amount for the offsetting of costs borne by Member States in accordance with Article 172(5) EUTMR (i.e. the 5%) and Article 172(7) EUTMR (i.e. the possibility to increase the amount to 10%). In other words, the offsetting does not constitute operational expenditure in the sense of Article 172(10) EUTMR and should not be taken into account when determining the necessary level of the reserve fund.

Allocations to or withdrawals from the reserve fund have to be included in the budget proposal for year N. The amount of allocation or withdrawal has to correspond to the difference between the existing reserve fund in year N-1 and the sum of titles 1, 2 and 3 of the budget proposal for year N:

- Allocation to the reserve fund is needed when the sum of titles 1, 2 and 3 of the budget proposal for year N is higher than the reserve fund for year N-1.
- Withdrawal from the reserve fund is needed when the sum of titles 1, 2 and 3 of the budget proposal for year N is lower than the reserve fund for year N-1.

2.3.2 THE BUDGETARY TREATMENT OF THE RESERVE FUND

An allocation to the reserve fund must be entered in the expenditure part of the budget (within title 10) as it represents an additional charge to the budget. Similarly, a withdrawal from the reserve fund must be entered in the income part (within title 3) as it represents an additional resource for the budget.

The amount to be allocated to or withdrawn from the reserve fund will be included in the budget.

- Allocations to the reserve fund are included in chapter 102 (Allocation to reserve fund) within title 10 on the expenditure side of the budget;
- Withdrawals from the reserve fund are included in title 3 on the income side of the budget (Balance from the previous year and Withdrawals from the reserve fund).

2.3.3 THE EVOLUTION OF THE RESERVE FUND

In compliance with the legal requirements and considering the existing level of the reserve fund at the end of previous year, the evolution of the reserve fund is as follows:

(EUR)

	2019	*2018*
Reserve fund as per 31/12 of the previous year	242,939,606.33	249,111,642.99
Allocation to the reserve fund corresponding to the year		
Withdrawal from the reserve fund corresponding to the year	-4,292,408.74	-6,172,036.66
Reserve fund as per 31/12 of the year	**238,647,197.59**	**242,939,606.33**

2.4 THE OFFICE'S TREASURY

Apart from seeking compliance with the Office´s Financial Regulation, in particular the principle of sound financial management, treasury should be managed respecting three main guiding principles:

- **Liquidity**: funds need to be available for budget execution and to achieve the Office's strategic goals;
- **Security**: risks in relation to the management of the Office's funds should be mitigated;
- **Yield**: yields should reflect the best market conditions available, while maintaining a high degree of security, as this is more important than the yield.

The cash and bank balances of the Office on 31 December were as follows:

(EUR)	2019	2018
Short-term deposits	0.00	1,000,000.00
Current accounts	500,759,170.19	479,521,468.14
EU-funded projects	12,611,375.38	12,271,106.99
Petty cash	90.76	205.38
TOTAL	**513,370,636.33**	**492,792,780.51**

It is worth noting that, as part of the total treasury, the Office is required to keep, among other elements, the amounts corresponding to the reserve fund (EUR 238.6 million), customers balances (EUR 32.2 million), budget commitments carried over to the following financial year in order to face the payment obligations towards third parties (EUR 20.8 million), the pre-financing received from the European Commission regarding the EU-funded projects (EUR 12.6 million) as well as funds reserved for future offsetting payments (EUR 24.7 million) generated in 2018 and 2019 and 3 months of expenditure as operational treasury for payments (approximately EUR 60 million).

In compliance with the treasury guidelines updated in November 2019, the Office had its treasury distributed between three commercial banks that complied with the minimum rating A- from the three credit agencies Fitch, Standard & Poor's and Moody's ([11]) and three central banks.

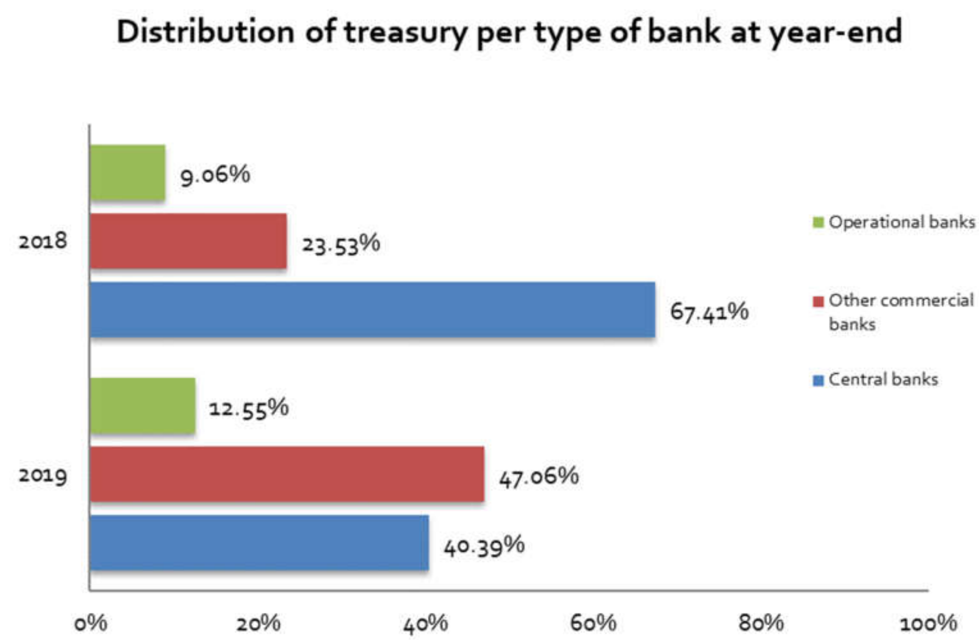
Further operational funds for carrying out daily transactions regarding incoming and outgoing payments necessary for the normal functioning of the Office are held with operational banks that comply with a minimum rating of –BBB in accordance with the above mentioned treasury guidelines.

The balances regarding the accounts of the EU funded projects correspond to the funds received from the European Commission for the execution of the EU funded projects. These funds are also held with operational banks.

2.4.1 DIVERSIFICATION OF RISK – DISTRIBUTION OF FUNDS BY CATEGORY OF BANKS

The distribution of the Office's treasury by category of banks on 31 December was as follows:

([11]) These rating requirements are aligned with the European Commission practice.



Central banks and commercial banks are used for keeping 'peaks' of treasury, that is to say, the part of treasury that is not immediately needed to cover the Office's operational needs. Operational banks are used for daily business activities (incoming payments from users and outgoing payments to suppliers and staff).

Given the Office's focus on security, approximately two thirds of the funds were held with central banks in 2018, which entailed also the paying of negative interests to these banks as a consequence of the European Central Bank's level of the deposit rate which stood at -0.4% until September 2019 when it was decreased to – 0.5%. As a consequence of this, and based on the updated treasury guidelines, funds were moved from central banks to commercial banks with a view to reduce the impact of additional negative interests.

3. THE EXPENDITURE RELATED TO ARTICLE 152(5) AND (6) EUTMR

The expenditure related to the financial support given in compliance with Article 152 is shown from an Activity Based Budgeting (ABB) point of view and also by nature.

The reason for using such an ABB approach is that when looking at the expenditure any type expenditure related to an activity is included, without distinction of whether it comes from title 1, 2 or 3 of the budget. This facilitates more transparency of the costs of the different cooperation programmes.

3.1 THE 15% UPPER LIMIT OF FUNDING BASED ON THE BUDGET

In Article 152(5) EUTMR it is stated that “The Office shall provide financial support to the projects referred to in paragraph 2”. That financial support may take the form of grants and in-kind contributions. The total amount of funding shall not exceed 15% of the yearly revenue of the Office. The beneficiaries of grants shall be the central industrial property offices of the Member States and the Benelux Office for Intellectual Property.

The concept of “yearly revenue of the Office” is clearly defined in the Article 6 of the Office´s Financial Regulation which in its paragraph 4 refers to the estimated revenue for the year.

The reference in Article 152 to “the total amount of funding ...” has firstly to be read as the total amount estimated in the approved budget for year N for projects under EU Cooperation. Therefore it follows that the 15% upper limit of funding has to be complied with at the moment of drafting and approving the budget.

3.2 EU COOPERATION

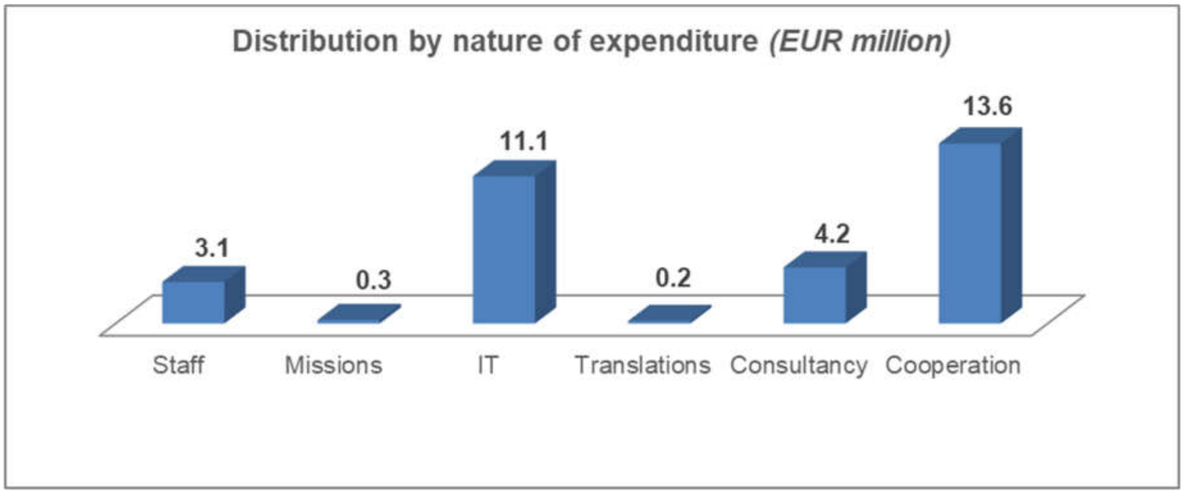
The following table shows the evolution of expenditure related to EU cooperation according to Article 152(5) and (6) from an ABB point of view:

EU COOPERATION	2019	2018
ECP1 - Consolidating and Completing the CF Landscape	3,219,747.24	3,492,728.76
ECP2 - Major Improvements to Existing CF Tools	3,262,134.17	4,047,707.49
ECP3 - New Tools	2,013,850.71	1,749,488.51
ECP4 - Shared Services and Practices	3,001,855.42	2,811,404.65
ECP5 - Supporting the Network	21,012,484.90	17,827,855.89
TOTAL	**32,510,072.44**	**29,929,185.30**

The level of effective expenditure on EU cooperation is below the limit of 15% of the yearly budgeted revenue of the Office, as laid down in Article 152(5) EUTMR.

	2019	2018
Total budgeted revenue	251,750,320.00	243,755,328.50
15% upper limit	37,762,548.00	36,563,299.28
Total budget execution	***32,510,072.44***	***29,929,185.30***

Looking at the expenditure by nature, the two main expenditure items per nature are cooperation and IT, followed by consultancy and staff expenditure.



4. OFFSETTING OF COSTS TO THE MEMBER STATES

4.1 OFFSETTING MECHANISM

Pursuant to Article 172(5) EUTMR, the Office's Management Board, on a proposal by the Office and after having consulted the Office's Budget Committee, will determine a distribution key on the basis of the following four indicators:

(a) the annual number of EU trade mark applications originating from applicants in each Member State;
(b) the annual number of national trade mark applications in each Member State;
(c) the annual number of oppositions and applications for a declaration of invalidity submitted by proprietors of EU trade marks in each Member State;
(d) the annual number of cases brought before the EU trade mark courts designated by each Member State in accordance with Article 123 EUTMR.

The distribution key was adopted by the Management Board on 15 November 2016 ([12]). Member States must submit to the Office, by 31 March of each year, statistical data corroborating the figures corresponding to each of these four indicators for the preceding year, which will then be included in the proposal to be made by the Office to the Management Board. Finally, it is provided that, on grounds of equity, the costs incurred by the authorities in each Member State will be deemed to correspond to at least 2% of the total offsetting.

The timing for the fixing of the amounts to be paid for a given year and their actual payment by the Office is established by Article 172 EUTMR and Article 104(8) of the Office´s Financial Regulation. In accordance with these provisions the compensation for year N is calculated and paid as follows:

(1) The first step in the process is to determine whether any compensation is to be paid for year N, that is to say whether no budgetary deficit occurs in year N (Article 172(6) EUTMR). On the basis of the Annual Accounts ([13]), it can be determined (first provisionally, and then finally) whether any budgetary deficit or surplus has occurred in year N, in accordance with the provisions of Article 104(5) and (6) of the Office´s Financial Regulation.

(2) Pursuant to Article 172(5) EUTMR, second subparagraph, the central industrial property offices of the Member States must submit to the Office by 31 March of year N+1 statistical data demonstrating the figures referred to in points (a) to (d) of the first subparagraph for year N. The purpose of this submission is to substantiate the costs referred to in Article 172(4) EUTMR. When doing so, Member States must inform the Office of the nomination of any other relevant authorities whose costs would be eligible under paragraph 4 in view of the specific tasks that they carry out as functional parts of the EU trade mark system.

(3) If there were a budget deficit, as defined in the previous paragraph, the exercise described in Article 172(4) to (7) EUTMR for year N would end at this point since the

([12]) Decision No MB-16-36.
([13]) Pursuant to Articles 106 and 107 of the Office´s Financial Regulation, the provisional accounts of year N have to be send to the Budget Committee by 31 March of year N+1 and the final accounts no later than 1 July of year N+1.

obligation by the Office to offset costs would not apply. Therefore, the Office would not need to submit any proposal to the Management Board for the distribution of an offsetting amount for that year. If there were no budget deficit, the Office would proceed to the next step.

(4) Once the final accounts for year N are available, no later than 1 July of year N+1, the Office prepares its draft proposal for the distribution among the Member States of the overall amount, corresponding to 5 % of its yearly revenue, by applying to the statistical data for year N submitted by the Member States () the distribution key previously determined by the Management Board (Article 172(5) EUTMR).

In the event of a budgetary surplus above 5% of its yearly revenue (as defined in Article 104(6), the Office may also decide to include in its proposal an increase in the overall amount to be distributed. Such proposal may consist of a percentage increase of up to a maximum of 10%.

(5) The Office subsequently presents its proposal regarding the payment of the offsetting at the Management Board meeting that will take place in November of the year N+1. Should the proposal be approved by the Management Board, it will be included in the budget for year N+2, to be approved by the Budget Committee after the meeting of the Management Board. The decision of the Management Board will constitute a financing decision within the meaning of Article 72(1) Office´s Financial Regulation.

(6) The budgetary appropriation of the compensation amounts corresponding to year N to each of the Member States will therefore be included in the budget of year N+2 under title 5 (Offsetting to Member States). The actual validation of expenditure and authorisation of payment by the Office's authorising officer related to such appropriation can be implemented as from January of year N+2, as provided for under Article 104(8) of the Office´s Financial Regulation. To that end, the authorising officer will act in accordance with Article 45 of the Office´s Financial Regulation.

4.2 THE OFFSETTING AMOUNT

According to Article 172(5) EUTMR, the overall offsetting of the costs identified in paragraph 4 shall correspond to 5 % of the yearly revenue of the Office. The Office's Financial Regulation establishes in its Article 6(5) that for the purpose of the offsetting the yearly revenue shall be the revenue collected under points (a) and (b) of paragraph 3 of that same article.

Therefore, the revenue to be considered relates to:
(a) revenue consisting of all fees and charges and any other revenue which the Office is authorised to collect by virtue of the tasks entrusted to it;
(b) revenue consisting of any other type of income, such as interest, revenue from exchange rate fluctuations or extraordinary income.

The following table shows how the amounts for the offsetting have been calculated.

(EUR)

	2019	2018
Own revenue	254,602,712.18	239,456,849.39
Interests	29,398.71	16,085.05
Any other type of income	0.00	0.00
Total yearly revenue in accordance with Art. 6 (5) of the EUIPO Financial Regulation	**254,632,110.89**	**239,472,934.44**
5% of the yearly revenue in accordance with Art. 172 (5) EUTMR	**12,731,605.54**	**11,973,646.72**

4.3 BUDGETARY RESULT ACCORDING TO ARTICLE 104(5) OF THE OFFICE´S FINANCIAL REGULATION

According to Article 172(6) EUTMR, the Office shall offset the costs referred to in paragraph 4 of the same article and incurred in a given year. This shall only apply to the extent that no budgetary deficit occurs in that year.

In order to define such a budgetary deficit, the Office´s Financial Regulation sets out in its Article 104(5) and (6) the following definition:

For the purposes of Article 172(6) of the EUTMR, a budgetary deficit shall be the negative result consisting in the difference between:

- the yearly revenue, as defined in Article 6(5), plus any unused appropriations carried over from the previous financial year,
  and
- the total of the budget execution of titles 1, 2 and 3 of that financial year, comprising the payments and the appropriations carried over against that financial year's budget,

less any eventual allocations to or plus any withdrawals from the reserve fund,
less the amount that would correspond to the offsetting foreseen in article 172(5) of the constituent act,
and excluding the positive/negative balance from the previous financial year.

The following table shows in detail the calculation related to the potential activation of the offsetting mechanism.

(EUR)

	2019	2018
Own revenue EUIPO Financial Regulation Art. 6 (1) a	254,602,712.18	239,456,849.39
Interests EUIPO Financial Regulation Art. 6 (1) b	29,398.71	16,085.05
Exchange rate differences EUIPO Financial Regulation Art. 6 (1) b	-115,819.05	-82,188.61
Carryover not used from previous year related to title 1, 2 and 3	5,665,775.69	4,068,266.80
(A) Total yearly revenue according to Article 104 (5) and (6) of the EUIPO Financial Regulation	**260,182,067.53**	**243,459,012.63**
Staff expenditure (title 1)	-123,041,652.46	-114,054,773.64
Operating expenditure (title 2)	-63,483,677.08	-65,571,683.00
Specific expenditure (title 3)	-52,410,228.71	-53,350,685.73
(B) Total budget execution (title 1- 3)	**-238,935,558.25**	**-232,977,142.37**
(C) Difference (A) - (B)	**21,246,509.28**	**10,481,870.26**
(D) Less allocation to reserve fund	0.00	0.00
(E) Plus withdrawal from reserve fund	4,292,408.74	6,172,036.66
(F) Less expenditure relating to the offsetting based on Art. 172 (5) EUTMR	-12,731,605.54	-11,973,646.72
(G) Budgetary result according to Article 104 (5) and (6) of the EUIPO Financial Regulation (C) - (D) + (E) - (F)	**12,807,312.48**	**4,680,260.20**

The above table shows that the offsetting mechanism was triggered for the financial years 2018 and 2019 for EUR 12.0 million and 12.7 million respectively.

It is also worth mentioning that the planned level of expenditure has a twofold impact in terms of mobilisation of appropriations: on the one hand, on the expenditure side of the budget, and, on the other, on the allocation to the reserve fund. Although an excessive mobilisation of funds on the expenditure side of the budget is overridden by the budget execution, this is not the case for the allocation to the reserve fund. This is the reason why the relevance of the Office's budget's accuracy (where necessary through an amendment, timed as to preserve the forecasting nature of a budget) increases, following the provisions in the Office's founding and financial Regulations specifying the mechanisms of the offsetting. In this context, the budget execution level reached 100.1% in 2019 and 96% in 2018, showing the good results of the Office´s efforts to precisely plan and estimate expenditure.

5. ANNEX

This annex includes extracts of the legal basis mentioned in the report.

5.1 ARTICLE 152 EUTMR – EU COOPERATION TO PROMOTE CONVERGENCE OF PRACTICES AND TOOLS

(1) The Office and the central industrial property offices of the Member States and the Benelux Office for Intellectual Property shall cooperate with each other to promote convergence of practices and tools in the field of trade marks and designs.

Without prejudice to paragraph 3, this cooperation shall in particular cover the following areas of activity:
(a) the development of common examination standards;
(b) the creation of common or connected databases and portals for Union-wide consultation, search and classification purposes;
(c) the continuous provision and exchange of data and information, including for the purposes of feeding of the databases and portals referred to in point (b);
(d) the establishment of common standards and practices, with a view to ensuring interoperability between procedures and systems throughout the Union and enhancing their consistency, efficiency and effectiveness;
(e) the sharing of information on industrial property rights and procedures, including mutual support to helpdesks and information centres;
(f) the exchange of technical expertise and assistance in relation to the areas referred to in points (a) to (e).

(2) On the basis of a proposal by the Executive Director, the Management Board shall define and coordinate projects of interest to the Union and the Member States with regard to the areas referred to in paragraphs 1 and 6, and shall invite the central industrial property offices of the Member States and the Benelux Office for Intellectual Property to participate in those projects.

The project definition shall contain the specific obligations and responsibilities of each participating industrial property office of the Member States, the Benelux Office for Intellectual Property and the Office. The Office shall consult with user representatives in particular in the phases of definition of the projects and evaluation of their results.

(3) The central industrial property offices of the Member States and the Benelux Office for Intellectual Property may opt out of, restrict or temporarily suspend their cooperation in the projects referred to in the first subparagraph of paragraph 2.

When making use of the possibilities provided for in the first subparagraph, the central industrial property offices of the Member States and the Benelux Office for Intellectual Property shall provide the Office with a written statement explaining the reasons for their decision.

(4) Once having committed to participate in certain projects, the central industrial property offices of the Member States and the Benelux Office for Intellectual Property shall, without prejudice to paragraph 3, participate effectively in the projects referred to in paragraph 2

with a view to ensuring that they are developed, function, are interoperable and kept up to date.

(5) The Office shall provide financial support to the projects referred to in paragraph 2 to the extent that is necessary in order to ensure, for the purposes of paragraph 4, the effective participation of the central industrial property offices of the Member States and the Benelux Office for Intellectual Property in those projects. That financial support may take the form of grants and in-kind contributions. The total amount of funding shall not exceed 15 % of the yearly revenue of the Office. The beneficiaries of grants shall be the central industrial property offices of the Member States and the Benelux Office for Intellectual Property. Grants may be awarded without calls for proposals in accordance with the financial rules applicable to the Office and with the principles of grant procedures contained in Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council and in Commission Delegated Regulation (EU) No 1268/2012 ([14]).

(6) The Office and the relevant competent authorities of the Member States shall cooperate with each other on a voluntary basis to promote the raising of awareness concerning the trade mark system and the fight against counterfeiting. Such cooperation shall include projects aiming, in particular, at the implementation of established standards and practices as well as at organising education and training activities. The financial support for those projects shall be part of the total amount of funding referred to in paragraph 5. Paragraphs 2 to 5 shall apply mutatis mutandis.

5.2 ARTICLE 172 EUTMR – BUDGET

(1) Estimates of all the Office's revenue and expenditure shall be prepared for each financial year and shall be shown in the Office's budget. Each financial year shall correspond to the calendar year.

(2) The revenue and expenditure shown in the budget shall be in balance.

(3) Revenue shall comprise, without prejudice to other types of income, total fees payable under Annex I to this Regulation, total fees as provided for in Regulation (EC) No 6/2002, total fees payable, under the Madrid Protocol, for an international registration designating the Union, and other payments made to Contracting Parties to the Madrid Protocol, total fees payable, under the Geneva Act referred to in Article 106c of Regulation (EC) No 6/2002, for an international registration designating the Union and other payments made to Contracting Parties to the Geneva Act, and, to the extent necessary, a subsidy entered against a specific heading of the Commission section of the general budget of the Union.

(4) Every year the Office shall offset the costs incurred by the central industrial property offices of the Member States, by the Benelux Office for Intellectual Property and by any other relevant authority to be nominated by a Member State, as the result of the specific tasks which they carry out as functional parts of the EU trade mark system in the context

([14]) The regulations to which the legal text refers to have been repealed and replaced by Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union , amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Regulation (EU, Euratom) No 966/2012; OJ L 193, 30.7.2018, p. 1–222.

of the following services and procedures:

(a) opposition and invalidity proceedings before the central industrial property offices of the Member States and the Benelux Office for Intellectual Property involving EU trade marks;
(b) provision of information on the functioning of the EU trade mark system through helpdesks and information centres;
(c) enforcement of EU trade marks, including action taken pursuant to Article 9(4).

(5) The overall offsetting of the costs identified in paragraph 4 shall correspond to 5% of the yearly revenue of the Office. Without prejudice to the third subparagraph of this paragraph, on a proposal by the Office and after having consulted the Budget Committee, the Management Board shall determine the distribution key on the basis of the following fair, equitable and relevant indicators:

(a) the annual number of EU trade mark applications originating from applicants in each Member State;
(b) the annual number of national trade mark applications in each Member State;
(c) the annual number of oppositions and applications for a declaration of invalidity submitted by proprietors of EU trade marks in each Member State;
(d) the annual number of cases brought before the EU trade mark courts designated by each Member State in accordance with Article 123.

For the purpose of substantiating the costs referred to in paragraph 4, Member States shall submit to the Office by 31 March of each year, statistical data demonstrating the figures referred to in points (a) to (d) of the first subparagraph of this paragraph for the preceding year, which shall be included in the proposal to be made to the Management Board.

On grounds of equity, the costs incurred by the bodies referred to in paragraph 4 in each Member State shall be deemed to correspond to at least 2 % of the total offsetting provided for under this paragraph.

(6) The obligation by the Office to offset the costs referred to in paragraph 4 and incurred in a given year shall only apply to the extent that no budgetary deficit occurs in that year.

(7) In the event of a budgetary surplus, and without prejudice to paragraph 10, on a proposal by the Office and after having consulted the Budget Committee, the Management Board may increase the percentage laid down in paragraph 5 to a maximum of 10 % of the yearly revenue of the Office.

(8) Without prejudice to paragraphs 4 to 7 and paragraph 10 of this Article and to Articles 151 and 152, where a substantive surplus is generated over five consecutive years, the Budget Committee, upon a proposal from the Office and in accordance with the annual work programme and multiannual strategic programme referred to in Article 153(1)(a) and (b), shall decide by a two-thirds majority on the transfer to the budget of the Union of a surplus generated from 23 March 2016.

(9) The Office shall prepare on a biannual basis a report for the European Parliament, the Council and the Commission on its financial situation, including on the financial

operations performed under Article 152(5) and (6), and paragraphs 5 and 7 of this Article. On the basis of that report, the Commission shall review the financial situation of the Office.

(10) The Office shall provide for a reserve fund covering one year of its operational expenditure to ensure the continuity of its operations and the execution of its tasks.

5.3 ARTICLE 104 (5), (6), (7) AND (8) OF THE OFFICE´S FINANCIAL REGULATION

Paragraph 5

For the purposes of Article 172(6) of the constituent act, a budgetary deficit shall be the negative result consisting in the difference between:

- the yearly revenue, as defined in Article 6(5), plus any unused appropriations carried over from the previous financial year,
  and
- the total of the budget execution of titles 1, 2 and 3 of that financial year, comprising the payments and the appropriations carried over against that financial year's budget, less any eventual allocations to or plus any withdrawals from the reserve fund,
  less the amount that would correspond to the offsetting foreseen in article 172(5) of the constituent act,
  and excluding the positive/negative balance from the previous financial year.

Paragraph 6

For the purposes of Article 172(7) of the constituent act, a budgetary surplus shall be the positive result consisting in the difference between:

- the yearly revenue, as defined in Article 6(5), plus any unused appropriations carried over from the previous financial year,
  and
- the total of the budget execution of titles 1, 2 and 3 of that financial year, comprising the payments and the appropriations carried over against that financial year's budget, less any eventual allocations to or plus any withdrawals from the reserve fund,
  less the amount corresponding to the offsetting foreseen in article 172(5) of the constituent act,
  and excluding the positive/negative balance from the previous financial year.

Paragraph 7

For the purposes of the substantive surplus generated during five consecutive years provided for in Article 172(8) of the constituent act, a budgetary surplus shall be the positive result in each year consisting in the difference between:

- the yearly revenue, as defined in the Article 6(5), plus any unused appropriations carried over from the previous financial year,
  and
- the total of the budget execution of titles 1, 2 and 3 of that financial year, comprising the payments and the appropriations carried over against that financial year's budget, less any eventual allocations to or plus any withdrawals from the reserve fund,
  less the amount corresponding to the offsetting foreseen in articles 172(5) and (7) of

the constituent act,
and excluding the positive/negative balance from the previous financial year.

Paragraph 8

Where applicable, the offsetting foreseen in Article 172(5) of the constituent act corresponding to a specific financial year N will be distributed to the Member States in year N+2, i.e. in the budgetary exercise following the closure of the accounts of that financial year.