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REPORT FROM THE COMMISSION

Member States' Replies to the Court of Auditors' 2009 Annual Report

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REPORT FROM THE COMMISSION

Member States' Replies to the Court of Auditors' 2009 Annual Report

1. SCOPE OF THE REPORT

The European Union's external auditor, the European Court of Auditors (the Court), under the terms of the Treaty¹ provides a statement of assurance (the DAS) in its Annual Report. The DAS concerns the reliability of accounts and the legality and regularity of the underlying transactions and is provided to the European Parliament and the Council.

The Financial Regulation states that as soon as the Court has transmitted the Annual Report, the Commission shall inform the Member States concerned immediately of the details of that report which relate to management of the funds for which they are responsible, under the rules applicable. Member States should reply to the Commission within sixty days and the Commission transmits a summary of the replies to the Court of Auditors, the European Parliament and the Council before 28 February²

Following publication on 9 November 2010, the Commission duly informed Member States of details of the report. This information was presented in the form of a letter and three annexes: Annex I was a questionnaire on the paragraphs in the report referring to the individual Member States; Annex II was a questionnaire on the audit findings which refer to the individual Member State and Annex III was a questionnaire on general findings related to Shared Management for DAS 2009.

This report is an analysis of the Member States' replies and is accompanied by a Staff Working Document (SWD) which is a summary of the findings and the replies to Annex I and Annex III.

2. DAS 2009 FINDINGS

2.1 The Court's audit methodology

The Court's audit approach and the methodology used for regularity of transactions, is based on testing transactions and assessments of the effectiveness of supervisory and control systems. This is supplemented by an analysis of management representations and evidence provided by other auditors.

With regard to transactions, the Court selects a representative statistical sample for each policy group and then carries out a detailed examination of that sample. In order to further evaluate its audit work, the Court classifies errors as quantifiable and non-quantifiable. Only quantifiable errors contribute to the error rate. Table 1 at the end

¹ Article 248 of the EC Treaty (Article 287 of the Lisbon Treaty)

² OJ L 390, 30/12/2006 -Financial Regulation Article 143.6

of this report, provides a detailed breakdown of all quantifiable and non quantifiable errors extrapolated by the Court and used in its audit work.

Errors are further categorised by nature- in particular eligibility (payment does not meet eligibility rules), occurrence (reimbursement of a cost which is not proven to have been incurred) and accuracy (payment incorrectly calculated). The Court also examines the frequency of errors by presenting the proportion of transactions in any one sample which is affected by errors- both quantifiable and non quantifiable. This frequency of errors provides an indication of how widespread errors are likely to be within a policy group³.

The Court also determines the most likely error rate by estimating the overall financial impact of quantifiable errors. The most likely error rate is classified in three ranges-below 2%,-between 2%-5%,-above 5%.

Finally the Court also assesses the supervisory and control systems by examining their effectiveness in ensuring regularity.

2.2 The Court's Annual Report- a new presentation

In terms of presentation, the structure of the Annual Report for 2009 changed. The Court merged the observations relating to internal control systems, the management representations and budget implementation into the DAS Chapter and the policy group chapters. The DAS chapter included an annex on the Court's audit approach and methodology. As a result of this new presentation of information, the number of chapters was reduced from eleven to nine and the policy group chapter numbers were altered.

2.3 Clean Accounts and a continuing reduction in the most likely error rate for payments

The Court's 2009 DAS findings stated that the accounts of the European Union give a fair presentation- or true and fair view- of the financial position and the results of operations and cash flows. In addition, the Court acknowledged that the Commission had improved the detailed information disclosed about recoveries of irregularly paid amounts and other corrections in the notes to the final accounts.

As far as legality and regularity of transactions were concerned, in 2009 the Court found that payments for Revenue were free from material error and the supervisory and control systems were effective. Commitments were also free from material error. However, with the exception of two areas of expenditure-Administrative expenditure and Economic and financial affairs- payments from the budget continued to be materially affected by error.

Regarding the supervisory and control systems, the Court stated that for all policy groups, with the exception of Revenue and Administrative expenditure, all systems were partially effective.

³ ECA Annual Report 2009 Annex 1.1

For the policy group Agriculture and Natural Resources, the most likely error rate has increased in comparison to 2008. The estimate of the most likely error rate for the chapter was between 2%-5% and accuracy errors were the most common type of quantifiable error found by the Court. As regards the supervisory and control systems, IACS⁴, the main system to ensure regularity of transactions, although well designed, was found to be adversely affected by the degree of accuracy of the data entered and the quality of the cross checks carried out in its databases.

With reference to the Cohesion chapter, the Court highlighted a significant decrease in the most likely error rate which was estimated at above 5%. Errors of eligibility were the most common type of quantifiable error. For systems relating to the 2007-2013 implementation period, the Court found weaknesses with regard to verifications carried out by Management Authorities/and or systems audited by the Audit Authorities. Systems for reporting of corrections to the Commission for the 2000-2006 period were also partially unsatisfactory. The Court therefore assessed the supervisory and control systems as partially effective.

The table below is a summarized version of the information on the Court's findings per policy group.⁵

Specific assessments	Revenue or operational expenditure (million euro)	Functioning of supervisory and control systems	Error rate range
Revenue	117,285	Effective	Less than 2 % (below materiality threshold)
Agriculture and natural resources	56,318	Partially effective ⁽⁴⁾	Between 2 % and 5 % ⁽⁴⁾
Cohesion	35,467	Partially effective ⁽⁴⁾⁽¹⁾	Greater than 5 % ⁽²⁾
Research, energy and transport	7,966	Partially effective ⁽⁴⁾	Between 2 % and 5 % ⁽⁴⁾
External aid, development and enlargement	6,596	Partially effective ⁽⁴⁾	Between 2 % and 5 % ⁽⁴⁾
Education and citizenship	2,153	Partially effective ⁽⁴⁾⁽³⁾	Between 2 % and 5 % ⁽⁴⁾
Economic and financial affairs	732	Partially effective ⁽⁴⁾	Less than 2 % (below materiality threshold)
Administrative and other expenditure	9,129	Effective	Less than 2 % (below materiality threshold)

The above table summarises the overall assessment of supervisory and control systems, as outlined in the relevant chapters, and gives the broad results of the Court's substantive testing. The table highlights the key elements but cannot present all of the relevant detail (in particular concerning weaknesses of supervisory and control systems and types of error) for which it is necessary to refer to the body of the report, within the context of the methodology underlying the Court's audit approach (see [Annex 1.1](#), paragraphs 3 to 18).

- (1) The majority of the work on systems relates to the new period and consisted of examining the compliance of the systems with regulatory requirements and resulted in an assessment as "partially compliant" (see paragraph 4.36).
- (2) Interim and final payments reimbursing certified expenditure amounting to 23 081 million euro (see paragraph 4.15).
- (3) The assessment of the supervisory and control systems is based on the examination of the Commission's system for closures of programmes and projects (see paragraph 7.19).
- (4) Systems are classified as 'partially effective' where some control arrangements have been judged to work adequately whilst others have not. Consequently, taken as a whole, they might not succeed in restricting errors in the underlying transactions to an acceptable level.
- (5) The Court decided to present the error rates (see [Annex 1.1](#), paragraphs 8 to 12) in three intervals. These error rate ranges cannot be interpreted as a confidence interval (in a statistical sense).

⁴ Integrated Administrative and Control System

⁵ Extracted from ECA Annual Report- Table 1.2 p22- Summary of 2009 findings on the regularity of transactions

3. ACTION TAKEN BY THE MEMBER STATES

As mentioned in the introduction, in addition to the letter, the Commission duly provided each Member State with three annexes-Annex 1 was a questionnaire on the paragraphs in the report referring to the individual Member States; Annex II was a questionnaire on audit findings which refer to the individual Member State and Annex III was a questionnaire on general findings related to Shared Management for DAS 2009. For Annex I and II, the Member States were asked, where necessary, to provide details of actions taken to rectify the errors as well as the timing, content and expected outcome.

In the case of Annex I, replies provided by the Member States were generally extensive⁶. Although the Court highlighted paragraphs related to all policy areas, Member States' replies focused mostly on the Court's paragraphs related to the policy areas Revenue, Agriculture and Natural Resources and Cohesion.

For example, in the policy area Revenue, the Court reported on the Greek government deficit and debt statistics and called into question the quality of the Greek macroeconomic statistics, including the national accounts⁷. The Greek response underlined that effective action had been taken and stated:

*"As far as improvements to the quality of national accounts is concerned, the update to the joint statistics action plan agreed by the Steering Group in October 2010 focuses on specific actions to be taken in 2011 designed to improve the quality of sectoral accounts, household savings accounts, quarterly accounts, volume and price measurements and a revision of the national accounts."*⁸

Also highlighted in the policy group Agriculture and Natural Resources was the Court's audit work on the effectiveness of systems and the fact that the 2009 Annual Activity Report (AAR) of the Director General for Agriculture and Rural Development contained a reservation in respect of the expenditure under the IACS in Bulgaria and Romania⁹. Both countries replied clearly that firm action had been taken and was ongoing. Bulgaria stated that:

*"As regards direct payment expenditure, a consolidated action plan to improve the functioning of the IACS was approved in 2009 and Bulgaria has since then been working to implement the recommendations and measures laid down in the plan. Detailed accounts of the progress made implementing the consolidated plan are submitted to the Commission every three months."*¹⁰

:

According to Romania, "the Director of the Agency took a keen interest in the 2010 financial year in ensuring that effective remedial measures were taken, which would result in the improvement of IACS."

⁶ See attached Staff Working Document (SWD)

⁷ ECA report-paragraph 2.27

⁸ SWD p15

⁹ ECA report-paragraph 3.68

¹⁰ SWD-p50-51

With regard to the reservations expressed by the Certifying Body in the Report for 2009, APIA¹¹ has made efforts and has achieved significant progress in implementing the measures set out in the IACS Action Plan and the recommendations of the Certifying Body".¹²

With regard to Annex II, a questionnaire on the audit findings which refers to the individual Member State, the majority of Member States provided detailed replies. These findings were mostly related to the policy area Agriculture and Natural Resources and Cohesion and had been previously provided by the Court to the Member State in the form of Statements of Preliminary Findings (SPFs). SPFs are findings arising from the audit work of the Court and are sent to the auditee. Information provided by the Member States in their replies can therefore be considered as a follow up to all actions already undertaken after receipt of the initial SPF.

In total 24 Member States were audited for DAS 2009. Member States with a large number of findings (more than 10 findings) included France, Germany, Greece and Spain. Those with less than 5 findings included Denmark and the Netherlands. Generally, quantifiable errors were accepted by Member States and the necessary corrective action was reported to have been taken.

In over 50% of cases where replies to the findings were provided Member States reported that action had already been taken and was either completed or ongoing. In the case of Portugal for example, comprehensive replies to all findings were provided. Most of the findings were serious quantifiable errors and in all cases payment adjustments or corrections were reported as having been duly made.

In most cases where no action was taken, justifications and supporting documentation were provided. This was the case for Spain which took action for approximately 50% of its findings which were mostly for Agriculture and natural resources. For 18 findings no action was taken, due partly to outstanding information being requested from the Commission or a disagreement with regard to the nature or seriousness of the findings. Supporting documents were also included with the replies. This was also the case for Cyprus which provided replies to all the Court's findings, 14 in total, all related to systems audits in the Agriculture and natural resources chapter. For 11 findings, action was taken and in the 3 cases where Cyprus disagreed with the findings, justification was provided.

4. MEMBER STATES' REPLIES TO THE QUESTIONNAIRE CONCERNING THE COURT'S 2009 ANNUAL REPORT

4.1 Supreme Audit Institutions (SAIs)

The information provided by Member States with regard to the Court's findings is further supplemented by their replies to a questionnaire on the main issues for DAS 2009.

¹¹ Agentia de Plati si Interventie Pentru Agricultura
¹² SWD-p51-52

As was the case for the report in 2008, for the 2009 report, questions were addressed to the SAIs. The first question concerned the single audit principle as defined by the Court of Auditors in its single audit opinion 2/2004 and whether SAIs found this a useful tool. Approximately half the SAIs of the Member States highlighted the fact that the single audit principle had potential benefits. The SAI in Latvia stated that the single audit principle could be "*deemed an efficient tool for managing EU funds, as it could enhance the quality of audit activities without undermining the independence of the audit bodies concerned*". The French SAI cited several reasons in support of the principle, including harmonising and lowering the costs of controls, as well as providing the auditing authority with a more comprehensive view of the audit results.¹³

The Finnish SAI pointed out that their interpretation of the international auditing standards differs from the European Court of Auditors' practices and that consequently, the SAIs could not directly apply the results of each other's audits; Adjustments would therefore be required.¹⁴

Some SAIs, were concerned that the single audit principle could compromise the independence of the institutions. This concern with independence was illustrated clearly by the Belgian SAI (FR division) which made a formal statement that it would not provide a reply to any of the questions posed to the SAIs directly. The reasons given were that it had an independent position as the national external control body and the fact that all SAIs were mandated to act as observers in the context of an audit carried out by the Court. In general, Member States SAIs also advised caution and noted that assurance was required at each level of the pyramid in order to ensure that the principle worked.

The SAIs were also surveyed on the materiality threshold which they applied. The majority of the institutions claimed to use a threshold between 0.5% and 2% with possible variations. Germany highlighted the fact that the Federal SAI was unable to provide information on the extent to or the levels at which the materiality threshold was applied by the various Courts of Auditors in each *Lander*.¹⁵

The third question for the SAIs concerned the use of the EC reports on payments which have been made available to the Member States since 2006. Overall, SAIs found that the information and data provided by the Commission in these reports were useful in the context of their audit work.

4.2 Agriculture and Natural Resources

The questionnaire also included a question on simplification in the area of rural development. More than half the Member States stated that not only were they favourable to the idea of simplification but that they had introduced simplification initiatives, such as clarifying and harmonising national rules and procedures or reducing beneficiaries' information obligations. Many of these initiatives were currently underway. France for example, underlined the actions taken by

¹³ SWD-p73

¹⁴ SWD-p69

¹⁵ SWD-p75

MAAPRAT¹⁶ to simplify rural development rules with particular emphasis on online declaration¹⁷. Lithuania underlined that *"in order to simplify the administrative and award procedure for support under the 2007-13 Lithuanian Rural Development Programme amendments were made to general legislation"*.¹⁸

Slovenia made reference to complicated reporting systems which since 2010 it has been simplifying and also the *"(over-strict) system of infringements and sanctions"*, which it had been upgrading in order to ensure that *"possible infringements are defined more clearly, while sanctions are more effective, dissuasive and in proportion to the gravity of the infringements."*

Member States also underscored their cooperation with each other and ongoing dialogue with the Commission in defining and implementing simplification. Spain highlighted its interregional dialogues as well as its participation *"in meetings or forums at European level related to simplifying the CAP"*.¹⁹

4.3 Cohesion

In the Cohesion chapter, three issues were raised: eligibility criteria, procurement and effective management verifications. Firstly, with regard to stricter eligibility criteria, Member States underlined the fact that there were two levels of consideration- EU/national level and programme level. Some Member States suggested that stricter rules were necessary and required from a legal view point. France and Finland both drew attention to the fact that Article 56 of Council Regulation n° 1083/2006 on the 2007-2013²⁰ programmes stipulates that the rules on the eligibility of expenditure must be laid down at national level. Finland therefore noted that *"the Regulation itself requires national eligibility rules to be more detailed than those laid down at Community level. Member States thus do not merely have the possibility of imposing eligibility requirements but are under an obligation to enact more specific requirements than those laid down by the Regulation at Community level"*.²¹

However, some Member States indicated that EU level eligibility rules were not specific enough for the needs of the programmes and that greater emphasis should be placed on programme specific rules. Poland summed up the issue by stating that there is *"the need to adapt general provisions of Community law to the specific characteristics of the Operating Programme. It was therefore necessary to make them more specific so that they were not misinterpreted by the beneficiary."*²²

Secondly, on the subject of procurement, the Member States were nearly all in favour of more training for national and regional authority staff as well as beneficiaries by the Commission and many Member States underlined the complex nature of the

¹⁶ Ministère de l'Agriculture de l'Alimentation, de la Pêche, de la Ruralité et de l'Aménagement du Territoire

¹⁷ No paper documents; 100% electronic process of the application by the farmers.

¹⁸ SWD-p81

¹⁹ SWD-p94

²⁰ Article 56.4. The rules on the eligibility of expenditure shall be laid down at national level subject to the exceptions provided for in the specific Regulations for each Fund. They shall cover the entirety of the expenditure declared under the operational programme.

²¹ SWD-p71

²² SWD-p88

rules. A significant number of Member States also considered that clearer guidelines from the Commission were necessary. Table 1 below summarizes the questions and responses provided by Member States on the procurement rules.

a) more training for national/regional authority staff by the Commission?	YES	20	74%
	NO	5	19%
	Other answer	2	7%
b) Should training include national/regional authority staff and beneficiaries?	YES	21	78%
	NO	5	19%
	Other answer	1	4%
c) Should clearer guidelines be provided to Member States by the Commission?	YES	22	81%
	NO	4	15%
	Other answer	1	4%
d) Should more guidelines be provided to Member States by the Commission?	YES	12	44%
	NO	11	41%
	Other answer	4	15%

Finally, with regard to more effective management verifications, approximately half of the Member States agreed that more precise eligibility rules were required at EU and national level. Member States, who disagreed with this idea, stated that it was generally because it was not an optimal solution. The UK stated that: *"the Commission have already significantly strengthened their supervisory role in shared management of the Cohesions funds. Any further increase in their control eats away at Member States' competence"*. Malta noted that *"more precise rules might compromise the element of flexibility and simplification which are necessary in the management of the Funds"*.

Table 2 below is a summary of the questions on verifications at managing authority level and the replies by the Member States.

(a) more precise eligibility rules at EU and national level	YES	14	52%
	NO	10	37%
	Other answer	3	11%
(b) less rigid eligibility rules at EU and national level	YES	9	33%
	NO	12	44%
	Other answer	6	22%
(c) more guidance to beneficiaries	YES	15	56%
	NO	7	26%
	Other answer	5	19%
(d) additional staff resources at national level	YES	11	41%
	NO	8	30%
	Other answer	8	30%
e) revised internal guidelines for managing verifications	YES	12	44%
	NO	9	33%
	Other answer	6	22%

5. CONCLUSION

The results of the Court's 2009 Annual Report illustrate the continuing improvement of the performances of all actors involved in the management of the EU funds. The fact that for the budget as a whole the Court's estimate of error has fallen over recent years, that for the third year in a row, a "clean opinion" on the accounts has been given and that the error rate in Cohesion has fallen significantly, are all worth noting. However, it is clear that there is a need for further sustained improvement, in particular, for the European funds under shared management between the Commission and the Member States.

Member States replies remarked positively on the improvements noted by the Court and, particularly, the significant decrease in the most likely error rate in the policy area Cohesion. However, Member States signalled that even closer cooperation with the Commission is desirable. For instance, in the complex field of procurement, guidance and support in the form of training programmes and targeted guidelines have been highlighted as key issues which need to be continually addressed.

The Commission remains firmly committed to improving EU financial management. The current Commission proposal for a recast Financial Regulation deals with the issues highlighted by both the Court and the Member States in their replies to the Court's findings. This is particularly relevant as regards the Commission proposals to lay down the control and audit obligations of the Member States in the Financial Regulation²³ and to further simplify and rationalise the rules applicable to the EU funds and programmes. Together these two commitments are regarded as an important route to the significant improvement in the quality of spending. At the same time, the Commission remains acutely attentive to the fact that simplification of programme structures and management systems at beneficiary level should not undermine assurance provided by a high effectiveness of controls.

The Commission is focused on sustaining the positive trend in the evolution of sound financial management. It is therefore of particular importance that the Commission and the Member States cooperate even more closely to address the findings highlighted by the Court.

²³ Also stated in the Lisbon Treaty – Article 317

Table I

Member State	ACCURACY				ELEGIBILITY				OCCURRENCE				OTHER COMPLIANCE ISSUES				T. AGRI	T. COH	T. REV
	AGRI	COH	REV	Total	AGRI	COH	REV	Total	AGRI	COH	REV	Total	AGRI	COH	REV	Total			
Austria	3	0	0	3	0	0	0	0	0	0	0	0	1	0	0	1	4	0	0
Belgium	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Bulgaria	0	0	0	0	2	0	0	2	0	0	0	0	0	0	0	0	2	0	0
Czech Rep	4	1	0	5	0	0	0	0	0	0	0	0	0	0	0	0	4	1	0
Cyprus	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Denmark	1	0	0	1	0	1	0	1	0	0	0	0	0	0	0	0	1	1	0
Estonia	0	0	0	0	0	1	0	1	0	0	0	0	0	5	0	5	0	6	0
Finland	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
France	6	1	0	7	0	2	0	2	0	0	0	0	1	5	0	6	7	8	0
Germany	4	0	0	4	1	1	0	2	0	0	1	1	1	15	0	16	6	16	1
Greece	3	0	0	3	1	1	0	2	0	0	0	0	7	1	0	8	11	2	0
Hungary	1	0	0	1	0	2	0	2	0	0	0	0	1	4	0	5	2	6	0
Ireland	1	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0
Italy	1	0	1	2	2	0	0	2	0	0	0	0	5	0	0	5	8	0	1
Latvia	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Lithuania	0	0	0	0	0	0	0	0	0	0	0	0	0	4	0	4	0	4	0
Luxembourg	1	0	0	1	0	1	0	1	0	0	0	0	0	5	0	5	1	6	0
Malta	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Netherlands	1	0	0	1	0	0	0	0	0	0	0	0	1	0	0	1	2	0	0
Poland	0	1	0	1	0	0	0	0	0	0	0	0	0	2	0	2	0	3	0
Portugal	1	2	0	3	0	5	0	5	0	0	0	0	1	0	0	1	2	7	0
Romania	0	0	0	0	0	0	0	0	1	0	0	1	8	0	0	8	9	0	0
Slovakia	1	0	0	1	0	0	0	0	0	0	0	0	1	4	0	5	2	4	0
Slovenia	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Spain	1	0	0	1	0	9	0	9	0	0	0	0	1	3	0	4	2	12	0
Sweden	0	2	0	2	0	1	0	1	0	0	0	0	0	1	0	1	0	4	0
UK	6	0	0	6	2	0	0	2	0	0	0	0	2	0	0	2	10	0	0
TOTAL				43				32				2				79			

