2014 discharge: EU general budget, European Commission and executive agencies

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PURPOSE: presentation of the Annual report of the Court of Auditors on the implementation of the budget concerning the financial year 2014.

CONTENT: the Court of Auditors published its 38th annual report on the implementation of the general budget of the Union for the year 2014.

This report follows a two-part structure:

- the first part contains the statement of assurance and a summary of the results of the audit on the reliability of accounts and on the regularity of transactions;
- the second part presents the findings on budgetary and financial management.

The statement of assurance (DAS) concerning the reliability of the EU's annual accounts and the legality and regularity of transactions is the central element of this report.

DAS: expenditure recorded in 2014 under the multi-annual financial framework headings 1 to 4, covering operational spending, is materially affected by error. The estimated level of error, which measures the level of irregularity in transactions, for payments in 2014 is **4.4%.** It remains persistently above the materiality threshold of 2%. The Court noted that the EU accounts for 2014 were correctly prepared in accordance with international standards and present a true and fair view. It was, once again, able to give a clean opinion on their reliability. However, it gave an **adverse opinion on the regularity of payments**.

It concluded that revenue underlying the accounts for the year ended 31 December 2014 is legal and regular in all material respects.

Overall results of the DAS:

The EU accounts for 2014 were correctly prepared in accordance with international standards and present a true and fair view. We were therefore able, once again, to give a clean opinion on their reliability. However, we gave an adverse opinion on the regularity of payments.

Payment issues: the estimated level of error, which measures the level of irregularity, for 2014 payments is 4.4 %, close to that of 2013 (4.5 %) and persistently above the materiality threshold of 2 %. The Court found the same estimated level of error (4.6 %), under shared management with the Member States and for expenditure managed directly by the Commission. The highest levels of error were found in spending under:

- economic, social and territorial cohesion (5.7 %);
- competitiveness for growth and jobs (5.6 %).

The Court stressed that there is a clear relationship between expenditure types and levels of error. The estimated level of error for cost reimbursement schemes (5.5 %), where the EU reimburses eligible costs for eligible activities on the basis of cost declarations made by beneficiaries, is double that for entitlement programmes (2.7 %), where payments are made on meeting conditions rather than reimbursing costs.

Corrective measures: corrective action by authorities in the Member States and by the Commission had a positive impact on the estimated level of error. Without this action, the overall estimated level of error would have been 5.5 %. There is further scope for the Commission to improve its assessment of risk and the impact of corrective actions. The Court noted that if the Commission, authorities in the Member States or independent auditors had made use of all information available to them, they could have prevented, or detected and corrected a significant proportion of the errors before these were made.

RAL: amounts of RAL to be paid in the current and future years remain at a very high level. It is essential for the Commission to take measures to deal with this persistent problem. For some Member States the backlog of unused funds represents a significant share of overall government spending.

Europe 2020: the Court noted that the periods of the 10-year Europe 2020 strategy and the EU's 7-year budgetary cycles (2007-2013 and 2014-2020) are not aligned. Member States give inadequate attention to Europe 2020 achievements in partnership agreements and programmes. Both issues limit the Commission' s ability to monitor and report on performance and the contribution of the EU budget to Europe 2020.

Mid-term review of the MFF: the upcoming mid-term review of the 2014-2020 multiannual financial framework is a key point in the management of EU spending. It is important that the Commission analyses the areas of persistently high levels of error as soon as possible and assesses opportunities for reducing this while strengthening the focus on performance in spending

Other characteristics of the Court's audit report: in the 2013 and 2012 annual reports, the Court reported an estimated level of error of 4.7% and 4.8% respectively for the EU budget as a whole. The comparable estimated levels of error for 2013 and 2012, presented in the 2014 annual report are 0.2 and 0.3 percentage points lower because we have updated the way we quantify serious infringements of public procurement rules.

Overall, the Court noted that **reimbursement spending was most affected by error**. The correct calculation of payments to recipients of funding often depends on information provided by the recipients themselves. This is especially significant in the area of reimbursement activities. EU spending by programme expenditure type includes the following errors:

- for reimbursement expenditure, the estimated level of error is 5.5% (2013: 5.6%). Typical errors in this area include ineligible costs contained in the cost claims, ineligible projects, activities and beneficiaries, and serious infringement of public procurement rules;
- for entitlement programmes, the estimated level of error is 2.7% (2013: 3%), with typical errors including **over-declarations by farmers of agricultural areas** and administrative errors affecting payments to farmers.

Furthermore, the report noted that there is scope for further improvement in the Commission's assessment of risk and impact of corrective actions.

The Court insisted on:

- the need for EU money to be spent in line with the principles of sound financial management: economy, efficiency and effectiveness;
- the aim to implement programmes by applying a performance culture and by focusing on the optimal use of resources.

The Commission is called upon to make appropriate proposals to the legislator to:

- better align the EU strategy and the MFF (this would help to ensure that adequate and effective monitoring and reporting arrangements are in place for future EU strategies);

- propose to the legislator that the performance framework is based, as far as possible, on common result indicators.

Analysis of budgetary implementation by groups of expenditure and recommendations from the Court:

- **Competitiveness for growth and jobs (€13 billion)**: in this area, almost 90% of spending is in the form of grants to private and public beneficiaries. In the area of research and innovation, the report found the same type and range of errors that we were detected throughout the course of the audit of FP7: incorrectly calculated personnel costs; other ineligible direct costs such as unsubstantiated costs for travel or equipment; as well as ineligible indirect costs based on erroneous overhead rates or including costs categories not linked to the project. The Commission is called upon, along with national authorities and independent auditors, to use all the relevant information available to prevent, or detect and correct errors before reimbursement.
- **Economic, social and territorial cohesion (€55.7 billion)**: this spending area comprises two parts: regional and urban policy which accounts for 80%; and employment and social affairs which covers the remaining 20%. The main source of error for the spending on economic, social and territorial cohesion as a whole continues to be **infringement of public procurement rules**, accounting for nearly half of the estimated level of error. This is followed by the inclusion of ineligible expenditure in the beneficiaries' cost declarations, infringement of state aid rules and the selection of ineligible projects. The impact of errors varies between these two spending areas. Cases of serious failure to comply with public procurement rules that were identified include, for example, unjustified direct award of contracts, additional works or services, unlawful exclusion of bidders, as well as cases of conflict of interest and discriminatory selection criteria. In particular, checks on state aid done by audit authorities were inadequate for nearly a third of the examined operational programmes. This is why the Court recommended the Commission to further strengthen the control system for audit authorities, ensuring adequate checks of compliance with state aid and public procurement rules. Managing authorities and intermediate bodies in Member States should intensify their efforts to address weaknesses in 'first level checks'. Member States should extend the use of the simplified cost options for projects exceeding €50 000.
- **Natural resources (€57.5 billion)**: this spending area covers the common agricultural policy (CAP), common fisheries policy (CFP) and environmental measures. As regards agriculture, many of the errors identified are the result of inaccurate or ineligible claims by beneficiaries, with the most frequent being the over-declaration of agricultural land surface or ineligible parcels of land. Having a reliable and up-to-date Land Parcel Identification System database (LPIS) can help to reduce such errors. For rural development, environment, climate action and fisheries, the main reasons for errors in this spending area were ineligibility of the beneficiary, activity, project and/or expenditure, or non-compliance with agri-environment commitments to use agricultural production methods compatible with protection of the environment, landscape and natural resources. The Council recommended that for EAGF, Member States should make further efforts to include reliable and updated information in their LPIS database and to use all the information available to avoid payments for ineligible land.
- **Global Europe (€7.4 billion)**: this spending area covers expenditure in the fields of foreign policy, support to EU candidate and potential candidate countries, as well as development assistance and humanitarian aid to developing and neighbouring countries (with the exception of the European Development Funds). Expenditure is dispersed throughout more than 150 countries, using a broad range of cooperation instruments and delivery methods. Spending is implemented directly by Commission directorates-general, either from their headquarters in Brussels, by EU delegations in recipient countries, or jointly with international organisation. The majority of errors identified from audits involve ineligible expenditure claimed by final beneficiaries, particularly expenditure incurred outside the eligibility period, inclusion of ineligible taxes, non-compliance with the rule of origin, and indirect costs wrongly charged as direct costs. Other errors found related to the acceptance and clearance of payment by the Commission for services, works or supplies that had

not yet been incurred by the beneficiary. The Commission was recommended to set up and implement internal control procedures to ensure that pre-financing payments are cleared on the basis of **actual incurred expenditure**.

- **Administration (€8.8 billion)**: this heading covers the expenditure of EU institutions and other bodies. It also includes payments to the European Schools. Spending on human resources (salaries, allowances and pensions) accounts for about 60 % of the total. Expenditure on buildings, equipment, energy, communications and information technology accounts for the remainder. Overall, the examination of systems did not reveal any significant weaknesses. However, the European Parliament is called upon to reinforce the controls concerning the reimbursement of costs by European political parties to their affiliated organisations as well as for public procurement by the political parties.