2004 discharge: EC general budget, section III, Commission and ECSC in liquidation

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COMMISSION FOLLOW-UP REPORT ON THE 2003 DISCHARGE : MEMBER STATES' REPLIES TO THE COURT OF AUDITORS' 2003 ANNUAL REPORT

Preliminary remark: this synthesis report from the Commission concerning the Member States' replies to the Court of Auditors' 2003 Annual Report should have been transmitted to the Court of Auditors, the Council and the European Parliament before 15 February. Due to the late receipt of some replies, as well as the time needed for translation of the replies and of the report itself, this deadline was not met.

Member States' views on a Community internal control framework: theCourt of Auditors published its CICF opinion in April 2004 where it set out some general principles for a Community internal control framework. As Member States are involved in shared management of around 80% of EU funds, the Commission considered that an appropriate follow-up to the Court's opinion should be based on input from the Member States as well. The Commission therefore invited Member States to answer two general questions relating to issues raised in the Court's opinion.

Question no. 1: in the areas of shared management, the Court is proposing that a chain of tasks and responsibilities be developed, stretching from the immediate managers of the funds (primary controls to the Commission (supervisory controls) via a central Member State control function. This model presupposes that each level can rely and use (i.e. has access to) the results of the other control bodies. Do you support this chain-based model in general and would you support the development of such a chain-based model in the areas where it does not already exist? What can be done in practice to improve the co-ordination of controls?

19 Member States have replied. None reject the idea of a Community internal control framework but several Member States made the following comments:

- Responsibilities of all involved should be clearly defined. The Commission shall remain responsible for the implementation of the EU budget;
- Several Member States stress that an internal control framework already exists to some extent;
- Common standards for financial control and internal audit must exist at all levels for the control chain. Such standards should be developed in full cooperation between the Commission and Member States. They should be based on already existing international standards;
- Costs and benefits must be reasonably balanced. Any changes to the Community internal control framework should make the system simpler and not increase the administrative burden. One Member State proposes that the EU budget should bear the costs of Member State controls. Another argues that support for audit and control activities within Structural Funds and the Cohesion Fund should continue to be financed under technical assistance measures. One Member State notes that accurate estimates of the costs of controls by national authorities are difficult to obtain because of the complex range of control activities for a given type of expenditure;
- Several Member States say that differences in national administrative cultures and practices must be taken into account;
- Some Member States indicate that reporting documents should be harmonized and pooled while others find that reports of national bodies cannot be considered the property of the Union. In a few cases, Member States foresee legal complications if such reports should be directly accessible to other control levels;

- Some Member States point out that imprecise legislation and lack of guidelines cause irregularities;
- Lastly, some Member States argue that a change in the role of Member States in the internal control framework should be counterbalanced by a different approach in the audit and control activities of the Court of Auditors and the Commission, such as by reducing control activities in Member States in general and focusing on systems audits instead of doing on-the-spot controls.

Question no. 2: until 2001, the Court of Auditors based its statements of assurance on the errors found in a limited sample of payments charged to a year's EU budget. The Court is now moving towards basing its statement of assurance on its assessment of the supervisory and control systems put into place to manage the risk of irregularity in claims, rather than on individual errors found during its audits.

How can Member States best provide evidence that supervisory and control systems are in place which keep the risk of irregularity in EU funds to within reasonable limits?

19 Member States have replied. Very few Member States have presented ideas on how the Member States at an operational level should provide evidence that the risk of irregularity in EU funds is within reasonable limits. One proposes that each Member State should have a central coordination body carrying out effective and constant supervision. Another proposes to introduce a principle of one audit authority for each Member State . And a third proposes that each Member States should provide the Commission with an annual report and a declaration, based on the same model as is used by the Commission internally.

Member States' views on specific observations made by the Court of Auditors : 22 Member States have replied to the Court's specific observations. Almost all provide feedback on a majority of the specific observations where a reply is expected. In more than one in four cases, Member States indicate that they either disagree with the observations of the Court or they consider the issue still open for discussion. Disagreements between the Court and the Member States do vary in nature, but among the recurring issues are:

- the eligibility of expenditure;
- the structure of checks (i.e. sampling methods, risk analysis and extrapolation);
- the estimated effect on the Community budget when taking into account that corrections have been made or will be made in later payments.

Several Member States point out that the Court has not taken their replies into account in the 2003 Annual Report. Some point out, that the Court's observations are based on findings in individual

transactions and do not necessarily indicate systematic irregularities within e.g. a Structural Funds programme. One stresses that the current procedure makes it impossible for Member States to profit from the exercise. Instead, the Court should present a qualitative examination of the systems it has examined as such input would be of more value to the Member States. Another proposes that the Court includes a brief summary of specific recommendations for clearly identified Commission follow-up actions, together with deadlines. This would reinforce the multi-annual aspect of the Commission's work and provide a baseline for subsequent reports.

DAS ERRORS : the Court of Auditors bases its statement of assurance on four elements: an examination of the way in which the supervisory systems and controls set up in both the Community institutions and in the Member States and third countries work; an examination of samples of transactions for each major area by carrying out checks down to the final beneficiary level;an analysis of the annual activity reports and declarations of the Directors-General and of the procedures applied in drawing them up; where necessary, an examination of the work of other auditors who are independent of Community management procedures.

The Court identifies errors which are either attributed to the Commission itself or to the Member States. Errors are classified as either substantive or formal, with substantive errors having direct financial consequences and formal errors not.

About one third of the errors identified by the Court in 2003 were classified as substantive. Of these, almost one in three were cases with an error rate (i.e. the amount in error as a share of the total amount involved in the transaction) less than 2%. In the cases with error rates higher than 2%, more than 2/3 were attributed to areas of shared management. On the basis of the replies received, it is not possible to present a global estimate of how many errors the Member States accept or contest. However, the Commission follows up on all error findings made by the Court of Auditors in cooperation with the Member States concerned. If the Court's observations are confirmed, the necessary financial corrections and recoveries are made. Based on the results so far achieved in the follow-up, the Commission's analysis of the errors indicates that about half of the substantive errors with an error rate higher than 2% can be accepted. For the remaining half, the errors are either rejected or it is not yet possible to accept/reject the error because the cases have not been closed yet.

In the vast majority of the cases with accepted errors, the Commission/Member States agree with the Court of Auditors on the amount which is considered to be in error. However, it should be noted that the amount in error (as a share of the total transaction amount) is usually in the lower range; thus, in more than 60% of the cases, the amount in error is less than 10% of the total transaction amount.

Conclusion : theCommission welcomes the Member States' replies which in many cases are full and comprehensive. The 2003 exercise has provided the Commission with valuable information on Member States' preliminary reactions to the Court of Auditors' CICF opinion. The Commission will continue to make further efforts along with the Court of Auditors to ensure that Member States can more easily identify and thereby comment on DAS errors. It will also continue to make efforts to ensure that Member States' replies to the Court's observations are taken into account in the Court's annual report and in the discharge process but must acknowledge that this is often difficult due to the timing of the procedure.