RIGSREVISIONEN

Memorandum to the Public Accounts Committee on the European Parliament's discharge resolution regarding the 2010 EU accounts

August 2012

The European Parliament's discharge resolution regarding the 2010 EU accounts

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Translation

I. Introduction

1. As a follow-up to my memorandum to the Public Accounts Committee issued in December 2011 on the Annual Report for 2010 of the European Court of Auditors ("the Court"), I will in this memorandum, like in previous years, inform the Public Accounts Committee about the European Parliament's ("the Parliament") discharge resolution. In the memorandum I have highlighted the sections of the Parliament's discharge resolution that I find particularly relevant.

2. Initially I will present the main conclusions of the Parliament's discharge resolution and its observations regarding the reliability of the accounts and the legality of the underlying transactions. I will then describe four priority actions to which the Parliament has devoted special interest. I will also brief the Public Accounts Committee about the Parliament's comments on the significance of the financial crisis for the European Community and its call for increaseed focus on results. Finally, and before I provide my own comments on the discharge resolution, I will inform the Committee of the latest developments concerning the cooperation on audit of European Union ("EU") funds.

3. On 10 May 2012, the Parliament decided to approve the closing of the accounts regarding the implementation of the EU's general budget for 2010. By this approval the Parliament granted discharge to the European Commission ("the Commission") and other institutions, agencies, etc., but decided to postpone approval for the budgets of the Council, the European Food Safety Authority, the European Environment Agency and the European Medicines Agency. The Parliament's discharge resolution includes the Parliament's observations.

4. Prior to this, at its meeting on 21 February 2012, the Council had adopted a positive recommendation regarding discharge to the Commission. Great Britain, the Netherlands and Sweden, however, voted against granting discharge to the Commission on account of the lack of progress in the management of EU funds. In doing so the three countries stepped up the criticism of the Commission's management that they raised last year, when they abstained from voting on the Council decision for discharge.

Discharge closes the accounts

The Commission presents accounts for the bulk of the Community's funds. The accounts of the other institutions form part of the overall accounts. The accounts are audited by the Court. Subject to recommendation by the Council, the Parliament may then grant discharge to the Commission and thereby approve the closing of the accounts. The Parliament is also granting discharge to the individual institutions, like for example the Council, the Court and the Court of Justice.

II. The Parliament’s main conclusions concerning the discharge resolution

5. In its discharge resolution, the Parliament initially states that the EU Member States are faced with a severe budgetary and financial crisis and that it is therefore vitally important that the EU is a leading example for good public management. For the very same reason, the Parliament therefore finds it particularly regrettable that the Court for the seventeenth consecutive year has not been able to issue a positive declaration of assurance on the budget, and that more than 90 per cent of all errors are identified at the level of Member States’ authorities and the level of final beneficiaries.

6. The Parliament emphasises however that it is necessary to differentiate between national authorities with well-functioning administrative systems (monitoring and control systems) and national authorities with only partially effective administrative systems. This differentiation is necessary in order to avoid additional burdens being imposed on all Member States to remedy deficiencies identified in some Member States.

7. According to the Parliament the inadequate progress in the management of the EU funds could be due to the Commission’s insufficient efforts in identifying publicly the Member States, regions and programmes that are underperforming in managing EU funds. This year, as in past years, the Parliament also emphasises the necessity to introduce mandatory national management declarations in order to increase the sense of accountability of certain national authorities for the management of EU funds.

8. The Parliament highlights four priority actions and invites the Commission to present action plans for:

- monitoring of Financial Engineering Instruments;
- strengthening the Commission’s accountability for the management of EU funds;
- reconsidering the increased use of pre-financing;
- creation of an effective sanctioning mechanism in the area of Cohesion policy.

I shall comment further on the Parliament’s observations in respect to these four areas in section IV of the memorandum. The Parliament’s discharge resolution includes, in addition to the above-mentioned priority actions, also observations regarding the management of the various EU policy areas.

III. The Parliament’s observations on the reliability of the accounts and the legality of the underlying transactions

9. The Parliament notes that the 2010 annual accounts of the EU, according to the Court, are in all material respects reliable. The Parliament also notes with satisfaction that revenue and commitments underlying the 2010 accounts are in all material respects legal and regular. The Parliament regrets deeply, however, that underlying payments remain materially affected by error.

10. Table 1 provides an overview of the Court's assessment of the reliability of the management of the bulk of the EU expenditure and revenue in 2010, including error rates for the respective policy areas.

Table 1. The Court's audit findings

Distribution of EU expenditure and revenue in 2010	Error rate	EUR billions	Functionality of supervisor and control systems	Conclusion
Agriculture and natural resources	2.3%	56.0	Partially effective	Materially affected by error
Cohesion, energy and transport	7.7%	37.6	Partially effective	
External aid, development and enlargement	1.7%	6.5	Partially effective	Overall not materially affected by error, but interim and final payments are materially affected by error
Research and other internal policies	1.4%	9.0	Partially effective	
Administration and other expenditure	0.4%	9.2	Effective	No significant level of error
Income	0.0%	127.8	Effective	

Source: Annual Report of the Court for 2010.

Table 1 shows that the monitoring and control systems in all areas of expenditure, with the exception of "Administration and other expenditure" are considered only partially effective, like in previous years. It also appears from the table that the largest policy groups "Agriculture and natural resources" and "Cohesion, energy and transport" were materially affected by error with error rates of 2.3% and 7.7%, respectively. The level of error in the remaining policy groups was below 2%.

11. The Parliament regrets that payments in the EU accounts are overall materially affected by error and the monitoring and control systems only partially effective, which has resulted in an adverse opinion of the Court. The Parliament is particularly concerned that the total error rate has increased from 3.3% in 2009 to 3.7% in 2010, which indicates that the positive trend of recent years has been reversed. According to the Parliament the negative trend is primarily attributable to the increase in error rates in "Cohesion, energy and transport".

IV. Priority actions

12. As mentioned in the introduction, the Parliament invites the Commission to present action plans for four priority actions.

Monitoring of Financial Engineering Instruments (FEIs)

13. FEIs are funds providing financial support to small and medium-sized enterprises, urban development and energy efficiency in the form of equity, loans or guarantees. The Parliament is concerned about the increased use of FEIs and in particular the lack of information on the implementation of FEIs. The Parliament refers to the Commission's own assessment of the FEIs as being high risk and regrets the lack of formal reporting requirements in respect of the use of FEIs.

14. The Parliament therefore invites the Commission to consider monitoring the use of FEIs a *priority action*. The Parliament wants the Commission to evaluate the experiences with FEIs, prepare risk assessments, gather information from the Member States on the use of FEIs and report annually to the Parliament on its findings.

Strengthening the Commission’s accountability for the management of EU funds
15. As mentioned, the Parliament regrets deeply that the management of EU funds remains so materially affected by error. In this year’s discharge resolution, the Parliament stresses that the Commission holds the primary financial responsibility for the management of the EU funds despite the fact that approximately 80% of EU’s budget is implemented under shared management with the Member States. The Commission should therefore assume greater responsibility for managerial weaknesses and irregularities that may be identified at Member State level.

16. The Parliament also notes a number of critical observations made by the Court in respect to the annual activity reports that are provided by the various departments and services of the Commission. The Parliament therefore invites the Commission to consider it a *priority action* to strengthen its accountability for improving the management of EU funds. Among the actions proposed by the Parliament are:

- making public the Member States’ annual summaries of audits and controls performed;
- delivering a political declaration in which the Commission accepts its final and overall responsibility for the implementation of the EU budget;
- adding the responsible Commissioners’ signature to the annual activity reports that are provided by the EU departments and services.

17. Parallel with its emphasis on the Commission’s accountability, the Parliament stresses the importance of the role played by the Member States in the implementation of the EU budget. The Parliaments deeply regrets that the two policy areas “Cohesion, energy and transport” and “Agriculture and natural resources”, which are both implemented under shared management by the Commission and the Member States, are prone to the highest error rates. In this context, the Parliament welcomes the fact that the Commission has analysed the errors reported by the Court for the financial years 2006-2009, and highlighted the Member States and regions in which the majority of errors have been identified. The Parliament calls on the Commission to systematically and consistently identify and make public information on problem and risk areas.

18. The Parliament recalls its repeated invitations to the Commission to present a proposal for introduction of mandatory national management declarations that should be issued in compliance with international auditing standards and should include full information on the Member States’ use of EU funds.

Reconsidering the increased use of pre-financings
19. The Parliament notes that pre-financings are considered necessary in order for beneficiaries to start the agreed action. Yet, at the same time the Parliament notes that the Commission, according to the observations of the Court, has increased the use of pre-financing considerably the last five years and the Parliament is concerned about the lack of clearing of these pre-financings. The Parliament is of the opinion that the Commission takes on an increased financial risk by paying high volumes of pre-financings, because the final acceptance of the cost declared by the beneficiary is postponed to a later date. This increases the risk of error and the risk of the beneficiaries becoming insolvent in the interim.

20. Therefore the Parliament invites the Commission to make it a *priority area* to reconsider the increased use of pre-financings. In this context, the Commission should inform the Parliament of the reasons for the increased use of pre-financings. In order to safeguard the EU’s financial interests, the Commission should also determine a level of pre-financings in the various programmes while ensuring that the beneficiaries will be able to start their projects.

Creation of an effective sanctioning mechanism in the area of Cohesion policy
21. The Parliament regrets the increase in the error rate to 7.7% in the policy area ”Cohesion, energy and transport” and is deeply concerned about the fact that some of the errors identified in 58% of the transactions that were affected by error could have been detected and corrected. The Parliament deplores that failure to comply with the rules of public procurement accounts for a large proportion of the errors year after year, which may put the functioning of the internal market at stake.

22. The Parliament does not consider the current sanctioning mechanism in the Cohesion policy area effective. The effect of the sanctions on the Member States is limited and therefore providing little incentive to prevent errors.

23. The Parliament therefore invites the Commission to consider it a *priority action* to support the Parliament’s efforts to create an effective sanctioning mechanism in the Cohesion policy area. The sanctioning mechanism should oblige Member States to recover ineligible expenditure from final beneficiaries and ensure that the full range of sanctions is available for all funds with minimal scope for discretion and that the Commission is allowed greater authority to impose penalties on Members States or regions that have repeatedly failed to observe the rules.

V. EU and the financial crisis

24. The Parliament is concerned about the continuing financial and budgetary crisis in the Member States and sees different types of risks for the EU budget; financial risks in relation to loans granted to Member States and financial risks in relation to the fact that a large proportion of the EU’s revenue is derived from the national budgets of the Member States. Member States that are particularly severely affected by the financial crisis will find it increasingly difficult to contribute to the EU budget.

25. In this context the Parliament deplores the fact that the Court did not to the extent appropriate address these challenges in its Annual Report for 2010, and calls on the Court to focus more on the significance of the financial crisis for the EU budget and to monitor and report on the financial control mechanisms implemented by the EU including in particular the European Financial Stability Mechanism (EFSM).

26. The Parliament criticises the fact that the European Financial Stability Facility (EFSF) is neither subject to democratic control by the Parliament nor to audit by the Court, and strongly criticises the fact that the EFSF has not even any provision on external public audit.

27. The Parliament also criticises that the European Stability Mechanism (ESM) has been established by the Member States outside the institutional framework of the EU and thereby outside the effective democratic control of the Parliament, like the EFSF. At the same time the Parliament stresses that it shares the concern of the auditor generals in the EU Contact Committee that the ESM Treaty lacks sufficient provisions for ensuring effective external audit; the Parliament refers directly to the resolution of the EU Contact Committee of 14 October 2011 concerning external audit of the ESM and the statement from the same day on the impact of the European Semester and the recent developments in the EU’s economic governance. The Public Accounts Committee was informed of the resolution and statement of the EU Contact Committee in my memorandum on the Court’s Annual Report for 2010.

28. On the basis of the above, the Parliament invites the Council and the Member States to establish appropriate arrangements for public external audit, accountability, transparency and the reliability of data and statistics, and to ensure that the Parliament is involved at an equal basis with the Council in the political control with the ESM.

EU’s new financial crisis initiatives

EFSM
The EFSM was created in May 2010 in response to the debt crisis in Greece. It is a temporary funding programme which allows the Commission to borrow up to a total of EURO 60 billion in the financial markets on behalf of the 27 Member States under an explicit EU budget guarantee. These loans are then disbursed to Member States in financial difficulties. The individual Member States do not service the loans directly, but through their contribution to the EU budget.

EFSF
The EFSF was created by the euro-area Member States in response to the debt crisis in Greece. The EFSF has a lending capacity of EURO 440 billion and provides financial assistance to heavily indebted members of the eurozone. The EFSF has its headquarters in Luxembourg. The Facility was established on the basis of a framework agreement between the euro-area Member States which expires in June 2013.

ESM
In July 2011 the euro-area countries signed the treaty that established the ESM. The ESM has assumed the tasks of the EFSF and EFSM in July 2012 and has a lending volume of EURO 500 billion. Financial assistance from the ESM to a eurozone country will be provided if the support is considered indispensable to safeguard the stability of the eurozone and will be conditional upon the implementation of a strict macroeconomic adjustment programme.

VI. Greater focus on results

29. The Parliament welcomes the Court's greater focus on the Commission's performance, which constitutes a separate chapter in the Court's Annual Report for 2010. In this chapter the Court analyses the Commission's self-assessment of performance. According to the Parliament, the observations made by the Court indicate that the Commission's reporting on its performance is inadequate.

30. The Parliament is of the opinion that performance is as important as legality and regularity, and therefore invites the Court to elaborate further on performance in future annual reports. The Parliament also invites the Commission and Member States to define performance indicators in areas of shared management and to ensure that the Member States' reporting of achieved results is mandatory, complete, accurate and public.

VII. Progress of the cooperation on the audit of EU funds

31. In my memorandum to the Public Accounts Committee on the Court's Annual Report for 2010, I summarized the decisions made at the EU Contact Committee meeting on 14 October 2011 where the following activities were initiated by the Committee:

- Ensure effective external public auditing of the ESM headed by the German Supreme Audit Institution. The outcome of this work cannot be fully assessed before the rules governing the ESM have been laid down, but the position of the Supreme Audit Institutions on this issue has been well received by the Council and the Parliament.
- Undertake a pilot study to identify possible public audit deficits in the EU and Member States chaired by the Supreme Audit Institution of the Netherlands. The results of this study will be presented at the forthcoming EU Contact Committee meeting on 18-19 October 2012.
- Establish a task force to explore the possibilities for cooperation between Supreme Audit Institutions, Eurostat and national statistical institutions to improve the quality of the data that are reported to Eurostat. This task force is chaired by the Supreme Audit Institutions of Denmark and Poland.

32. In its capacity as co-chairman of the statistical task force of the EU, Rigsrevisionen hosted a meeting on 21-22 June 2012 in Copenhagen with representatives of 16 Supreme Audit Institutions, the Court, Eurostat (EU's statistical office) and Statistics Denmark who discussed how the cooperation between these institutions could be further strengthened. Eurostat invited the Supreme Audit Institutions to play an active role in the efforts to assure the quality of the source data that are received by the national statistical institutions for processing and reporting of national statistics to Eurostat and others. Some of the Supreme Audit Institutions were sceptical of the viability of this proposal for various reasons including restrictions in audit mandates, competences and resources.

33. The task force will produce a resolution that will be presented for adoption at the EU Contact Committee meeting in October 2012. On this occasion the Supreme Audit Institutions of the EU will get an opportunity to consider a number of concrete proposals aiming to strengthen the cooperation between Supreme Audit Institutions, Eurostat and the national statistical institutions.

34. Rigsrevisionen has also contributed to highlighting the audit of agricultural funds in the EU; on 2-3 February 2012 Rigsrevisionen hosted a methodology seminar on the audit of EU agricultural subsidies. Representatives of 18 Supreme Audit Institutions, the Court and the Commission participated in the seminar and shared knowledge and experiences on risk assessments and audit strategies in relation to the audit of EU agricultural funds. Another topic of the seminar was the latest developments in the management and governance of EU funds, and the EU national declarations/EU audit opinions that are issued in Great Britain, Sweden, the Netherlands and Denmark.

VIII. Conclusion

35. The Parliament has decided to grant discharge to the Commission regarding the EU 2010 accounts. I have noted that Great Britain, the Netherlands and Sweden have again this year not been able to vote in favour of the Council's recommendation to grant discharge on account of the continuing high error rates that are affecting large parts of the EU policy areas.

36. It is regrettable that the overall error rate has increased from 3.3% in 2009 to 3.7% in 2010 primarily because the number of errors identified in the Cohesion area has increased. Taking into consideration the statistical uncertainty that always accompanies calculations of this nature, it is not a steep increase, but it is unfortunate that recent years' positive trend in the error rates has now been reversed.

37. I agree with the Parliament's assessment of the necessity to focus efforts in the Member States, regions and programmes that are prone to the highest error rates, to ensure that additional control systems and the related administrative burdens are imposed selectively. I also concur with the Parliament's assessment that it may have a preventive effect if the Commission and the Court more consistently make public information on problem and risk areas.

38. I have also noted the Parliament's invitation to strengthen the Commission's and the Member States' political accountability for the management of the EU funds.

39. I welcome the Parliament's recognition of the resolution and statement of the EU Contact Committee concerning the importance of ensuring external public audit of the new financial crisis initiatives in the EU, and the Parliament's decision to adopt and reflect this view in the discharge resolution.

40. In my opinion it is of critical importance that the Supreme Audit Institutions in the EU and the Court help the EU Member States in overcoming the crisis. Ensuring adequate public audit of the EU crisis initiatives and contributing to improved quality of EU statistics are just minor contributions. Each individual Supreme Audit Institution can through its audit contribute to enhancing the effect of the national crisis initiatives and contribute to improving the administration of the limited public funds.

41. Rigsrevisionen has carried out several studies that have revolved around the financial crisis and has published the results of these studies in report no. 14/2008 on *The Danish Financial Supervisory Agency's activities in relation to Roskilde Bank A/S,* report no. 1/2011 on *The issue of an individual government guarantee to Amagerbanken A/S* and report no. 12/2011 on *The Financial Stability Company A/S.*

42. The financial crisis has also increased the need for improved financial management in the public sector along with enhanced prioritisation and control of public expenditure. The focus on improving public sector financial management will have a bearing on the audit of the state accounts in the coming years, and this is reflected in Rigsrevisionen's strategy for the period 2012-2015 which includes the following elements; in 2012 Rigsrevisionen will develop a standard for auditing financial management and ensure that 75% of the preliminary studies that precede the major studies are about either efficiency, effectiveness, economy or financial management. Rigsrevisionen will also, through participation in relevant fora and elaboration of cross-departmental studies, ensure knowledge sharing across government.

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