



Memorandum to the Danish
Public Accounts Committee on
the European Court of Auditors'
Annual Report for 2008

December
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The European Court of Auditors' Annual Report for 2008

8 December 2009

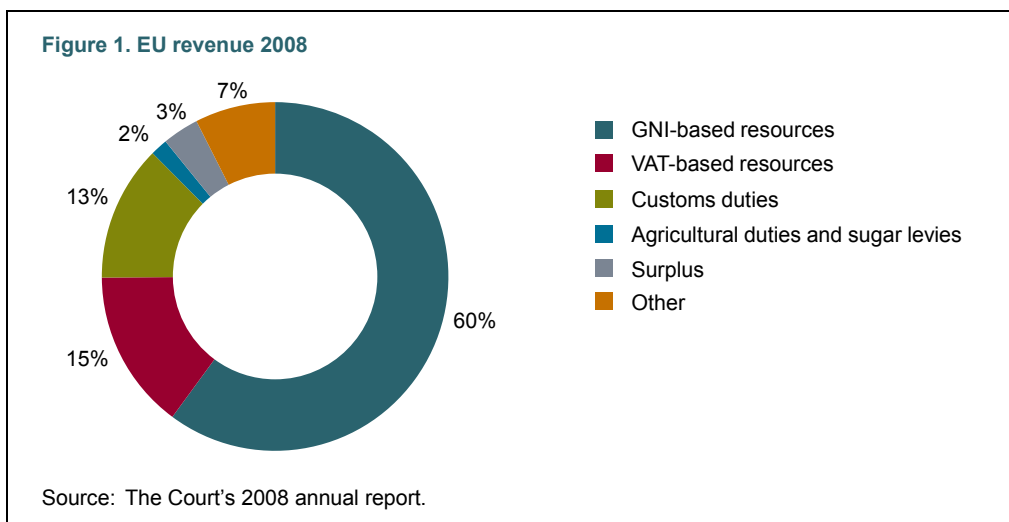
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Translation

I. Introduction and EU revenue and expenditure in 2008

1. On 10 November 2009, the European Court of Auditors ('the Court') presented its annual report and statement of assurance for the financial year 2008. In this memorandum I will inform the Public Accounts Committee of selected parts of the Court's annual report, including the statement of assurance and the most important conclusions. The memorandum begins with a brief outline of EU revenue and expenditure for 2008 to provide the basis for my subsequent briefing on the outcome of the Court's audit.

EU revenue 2008

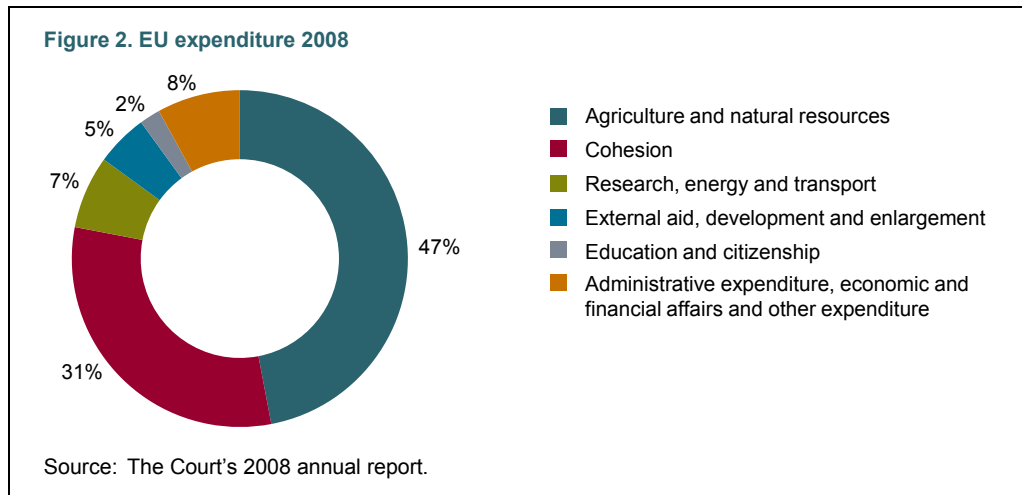
2. In 2008, EU revenue totalled approx. EUR 122 billion, equal to approx. DKK 906 billion. The revenue broken down by source is set out in figure 1.



According to figure 1, the bulk (60%) of the EU revenue is GNI-based resources calculated as a fixed percentage of gross national income (GNI), while the second and third largest sources of revenue are VAT (15%) and customs duties (13%).

EU expenditure 2008

3. In 2008, EU expenditure totalled approx. EUR 117 billion, equal to approx. DKK 868 billion. Expenditure broken down by area of expenditure is set out in figure 2.



According to figure 2, the largest expenditure areas are “Agriculture and natural resources” (47%) and “Cohesion” (31%). “Agriculture and natural resources” mainly represents common agricultural policy (CAP) expenditure and rural development aid. “Cohesion” represents the EU’s structural policies (the Regional Development Fund, the Social Fund, etc.).

“Agriculture and natural resources” and “Cohesion” account for about 80% of EU expenditure. The management of these areas is shared by the Commission and individual Member States (shared management). This means that the Commission has overall responsibility for the correct implementation of the budget, whereas the Member States select and check eligible projects and pay funds to the final beneficiaries.

4. In 2008, Denmark received a total of approx. DKK 9.5 billion from the EU and contributed approx. DKK 18.3 billion. In addition to this, private beneficiaries in Denmark received direct contributions from the Commission. For a detailed review of the management of EU funds in Denmark, I refer to report no. 18/2008 on the audit of EU funds in Denmark in 2008 considered by the Public Accounts Committee at its meeting on 25 November 2009.

5. Denmark is not mentioned in the Court’s 2008 annual report, except in a number of general tables on EU expenditure and revenue and one table showing that Denmark is the only EU-15 country for which the Commission made no reservations regarding VAT payments. A detailed account of the Court’s audit in Denmark in 2008 is included in the report on the audit of EU funds in Denmark in 2008.

II. The Court’s 2008 annual report and statement of assurance

The Court’s audit approach

6. On 10 November 2009, the Court presented its annual report and statement of assurance for the financial year 2008 to the European Parliament (‘the Parliament’) and the Council. The Court’s 2008 annual report presents the results of the Court’s financial audit, whereas the results of its performance audits are published in separate reports issued in the course of the year. Since the publication of the most recent annual report, the Court has issued 19 reports on the results of its performance audits.

7. The Court’s annual report forms part of the Parliament’s discharge procedure, which is a political assessment and approval of the management of the EU budget by the Commission and other EU institutions. This year, the Court issued its 32nd annual report, which has included a statement of assurance (DAS from the French *Déclaration d’Assurance*) since 1994.

The DAS includes the Court's overall opinion on EU revenue and expenditure, i.e. whether revenue and expenditure:

- have been properly recorded in the Commission's accounts (reliability of the accounts)
- have been paid into or out of the Commission's accounts in a lawful and formally correct manner (legality and regularity of the underlying transactions).

8. The Court applies the so-called DAS approach in its audits. The key element is an assurance model indicating the level of assurance that can be achieved from the following two principal sources:

- *Systems-based auditing* of the supervisory and control systems applied by the Commission, Member States and Third Countries to examine whether they function as intended and prevent, identify and correct errors in connection with the collection and disbursement of EU funds.
- *Substantive auditing* of payments made to and by the Commission which the Court selects through a random representative sample of transactions. Transactions to be checked are selected by the Court's special sampling method – the so-called monetary unit sampling that identifies and checks individual payments down to the level of the final beneficiary, often through on-the-spot audit visits.

Moreover, in its audits, the Court may supplement these sources with annual activity reports and declarations by the Commission's Directors-General and the work of other auditors.

The Court's 2008 statement of assurance

9. Based on the audit of the EU's 2008 accounts, the key elements of the Court's statement of assurance are:

Reliability of the accounts:

- The EU's 2008 annual accounts are in all material respects presented fairly, and for the second consecutive year, the Court has issued an unqualified statement of assurance on the reliability of the accounts.

Legality and regularity of the underlying transactions:

- Generally, the level of errors has been reduced. The areas "Revenue", "Administrative expenditure" and "Education and citizenship" are free from material errors. The error rate for "Agriculture and natural resources", the largest policy area, is now so low that for the first time it has been given a positive opinion, although the opinion was qualified for the sub-area "Rural development". Overall, policy areas that are free from material errors account for approx. 47% of payments made in 2008.
- However, the Court finds that the remaining approx. 53% of the EU expenditure is affected by material error, and the Court's opinion is therefore adverse for large parts of the expenditure areas "Cohesion", "Research, energy and transport" and "External aid, development and enlargement".
- The Court repeats that complicated and unclear legal requirements and eligibility rules significantly impact the error rate. Accordingly, the Court finds that rules should be simplified, but in a manner that does not lead to less focused programmes with the increased risk of erroneous payments.
- Again this year, the Court has noted improvements in the Commission's supervisory and control systems, but repeats previous years' recommendations for further system improvements.

Table 1 shows the distribution of the bulk of EU expenditure and revenue for 2008 and the Court's assessment of the legality and regularity of the underlying transactions.

Table 1. The Court's assessment of the legality and regularity of the underlying transactions in 2008

Distribution of EU expenditure and revenue in 2008	EUR billion	Functioning of supervisory and control systems	Error rate
Agriculture and natural resources	55.0	Partially effective	Below 2%
Cohesion	36.6	Partially effective	Over 5 %
Research, energy and transport	7.5	Partially effective	Between 2% and 5%
External aid, development and enlargement	6.2	Partially effective	Between 2% and 5%
Education and citizenship	1.7	Partially effective	Below 2%
Economic and financial affairs	0.5	Partially effective	Between 2% and 5%
Administrative and other expenditure	8.5	Effective	Below 2%
Revenue	121.6	Effective	Below 2%

Source: The Court's 2008 annual report.

10. Table 1 shows that "Agriculture and natural resources" is the largest policy area in the EU (EUR 55 billion in 2008) and that this year, for the first time, it was given a positive opinion, although the opinion was qualified for the sub-area "Rural development". Despite a fall in the level of errors, rural development aid remains affected by a high error rate. In the Court's 2007 annual report, it was the high level of errors affecting rural development aid that gave rise to an adverse opinion for this policy area as a whole.

According to the Court, this year's improvements are due to the implemented simplification of the rules and the decoupling of aid from production so that most aid is now calculated on the basis of land in good agricultural and environmental condition.

11. "Cohesion" is the second-largest policy area (EUR 36.6 billion in 2008), and the Court's audit has repeatedly documented very high error levels in this area. This is also the case this year, with the Court estimating for the second consecutive year that at least 11% of total reimbursements to Member States ought not to have been made. In particular, the high error rate reflects that projects and programmes failed to fulfil the financing and procurement conditions and that many non-eligible expenses have been reimbursed.

The Court recommends that the Commission focus on the Member State elements and programmes with the highest error rate and that it strengthen its efforts to recover erroneous payments to beneficiaries.

12. I have noted that for the second consecutive year, the Court has issued an unqualified statement of assurance on the reliability of the accounts. Last year was the first time ever that the Court issued an unqualified statement of assurance and it is gratifying to see that this development has continued. It is also gratifying to see that the error rate for "Agriculture and natural resources" has been reduced and that for the first time this policy area has received a positive, qualified opinion. However, the Court has identified material errors in the underlying transactions for more than half the expenditure. Thus, for the 15th year in a row, the Court issued adverse opinions on several areas of the EU accounts.

III. Cooperation on audit of EU funds

Rigsrevisionen's EU report and the EU summary included in the state accounts

13. As a new feature, Rigsrevisionen this year issued a report on the audit of EU funds. The report includes the opinion on the audit of EU funds that Rigsrevisionen has prepared since 2005 and which, until this year, formed part of the report on the audit of the state accounts. The opinion and the report are issued partly to clarify Rigsrevisionen's overall assessment of the EU area in Denmark, partly to contribute to enhancing cooperation on the audit of EU funds. The report will be translated into English and submitted to all supreme audit institutions in the EU, the Court, the Commission and the Parliament.

On the basis of discussions with Rigsrevisionen, the Danish Ministry of Finance has for the first time included a summary of Denmark's contributions to and receipts from the EU in the state accounts for 2008. The summary has provided Rigsrevisionen with a better basis for auditing and giving an opinion on EU funds. Rigsrevisionen has audited the summary and identified certain allocation errors. In the Ministry of Finance, efforts are under way to consolidate the summary. Moreover, the Ministry of Finance and Rigsrevisionen are discussing ways of developing the summary so that in future, it will provide more information and be more useful for auditors and other interested parties.

Cooperation on audit of EU funds

14. Rigsrevisionen's formal cooperation with other SAIs in the EU and the Court takes place within the framework of the Contact Committee where the heads of the EU SAIs (including the President of the Court) meet once a year. The Contact Committee has set up a number of working groups on specific topics relating to the audit of EU funds across Member States.

Among the working groups Rigsrevisionen participates in is the working group on "National SAI Reports on EU Financial Management", whose main purpose is to exchange experience on EU audits and provide assistance to SAIs wishing to develop EU audit reports. At the most recent meeting in Budapest in June 2009, Rigsrevisionen presented its work on developing the new EU report and its most recent experience from auditing EU funds in Denmark.

Dialogue with the Court

15. As mentioned in the May 2009 memorandum on discharge to the Parliament, Rigsrevisionen has been discussing options with the Court for strengthening bilateral cooperation on the audit of EU funds in Denmark. However, these discussions have not yet produced any concrete results. To date, the Court has insisted on basing audit cooperation on the Court's audit approach, described above in paragraph 8, which differs materially from that applied by Rigsrevisionen.

16. Rigsrevisionen plans and performs the audit of EU funds on the basis of the same considerations concerning materiality and risk as apply to the audit of state funds. Rigsrevisionen applies international auditing standards and good auditing practice as well as risk- and systems-based auditing of management and control systems in the administration supplemented by sample substantive auditing. The Court, on the other hand, places great emphasis on substantive auditing of the final beneficiaries in order to calculate the error rates that form the basis of the Court's statements of assurance regarding policy areas examined. Unlike the Court, Rigsrevisionen neither applies monetary unit sampling nor calculates error rates for areas examined.

17. I welcome stronger cooperation with the Court, and Rigsrevisionen is prepared to go to great lengths to facilitate this. However, such cooperation must be based on mutual respect for each other's mandates, audit approach and the auditing already performed today.

IV. Conclusion

18. The Court's 2008 annual report shows that recent years' positive trend in EU fund management has continued. For the second consecutive year, the Court has issued an unqualified statement of assurance on the reliability of the EU accounts, and error levels for the underlying transactions have fallen again this year. I note in particular that for the first time the policy area "Agriculture and natural resources" was given a positive, qualified opinion.

However, the error rate is still too high in several policy areas, notably including "Cohesion". Overall, the Court has again this year given adverse opinions on more than half the EU expenditure for 2008.

19. This year, Rigsrevisionen for the first time issued a report on the audit of EU funds in Denmark to clarify its assessment of the EU area in Denmark and promote cooperation on the audit of EU funds. The report is intended to give the Public Accounts Committee and the public a better overview of EU fund management and auditing in Denmark. The report is also meant to provide a good basis for the exchange of experience and stronger cooperation in the audit of EU funds between Rigsrevisionen, the Court and the other SAs in the EU.

20. Rigsrevisionen and the Court are discussing the cooperation on the audit of EU funds, but have not yet reached any concrete results due to material differences in audit approach. I welcome a strengthened cooperation between the Court and Rigsrevisionen, but such cooperation must be based on mutual respect for each other's audit approach, methods and a willingness to compromise.

I will keep the Public Accounts Committee informed about developments in the cooperation on the audit of EU funds and will report on any progress in my memorandum on the Parliament's discharge procedure, which I expect to issue in spring 2010.

Henrik Otbo