

**OPINION No 4/2006**  
**on the draft Council Regulation amending Regulation (EC, Euratom) No 1605/2002**  
**of 25 June 2002 on the Financial Regulation applicable to the general budget**  
**of the European Communities**

*(pursuant to Article 248(4), second subparagraph, EC)*

(2006/C 273/02)

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## THE COURT OF AUDITORS OF THE EUROPEAN COMMUNITIES

Having regard to the Treaty establishing the European Community and, in particular Articles 248(4) and 279 thereof,

Having regard to the Treaty establishing the European Atomic Energy Community and, in particular Articles 160C(4) and 183 thereof,

Having regard to Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities <sup>(1)</sup> and, in particular Article 184 thereof, which provides for a review of the Regulation every three years,

Having regard to the Court's Opinion No 10/2005 <sup>(2)</sup> on the draft Council Regulation amending the latter <sup>(3)</sup>,

Having regard to the Court's Opinion No 2/2004 on the 'single audit' model (and a proposal for a Community internal control framework) <sup>(4)</sup>,

Having regard to the Court's Opinion No 2/2002 on an amended proposal for a Council Regulation on the Financial Regulation applicable to the general budget of the European Communities <sup>(5)</sup>,

Having regard to a modified Proposal for a Council Regulation amending Regulation (EC, Euratom) No 1605/2002 <sup>(6)</sup>,

Having regard to the Council's request for an opinion on this proposal, which was submitted to the Court of Auditors on 26 June 2006,

HAS ADOPTED THE FOLLOWING OPINION:

**INTRODUCTION**

1. The Commission presented its first proposal to amend the current Financial Regulation in May 2005. As a result of the inter-institutional consultations, it has now decided to present a revised proposal which takes account, *inter-alia*, of the following:

- to strike a better balance between the protection of the financial interests and the proportionality of administrative costs and user-friendly procedures,
- to reinforce the budgetary principles by limiting the exceptions allowed, introducing the principles of effective and efficient control and that of proportionality; and developing further the principle of transparency by providing for information on beneficiaries of Community funds,
- the role and responsibilities of the Commission's Accounting Officer has been clarified,
- public procurement procedures have been brought more into line with the provisions of the Community Directive <sup>(7)</sup>,
- inter-institutional cooperation, notably in the area of public procurement procedures, has been further developed,
- further provisions have been introduced for external aid.

<sup>(1)</sup> OJ L 248, 16.9.2002. Corrigendum published in OJ L 25, 30.1.2003.

<sup>(2)</sup> OJ C 13, 18.1.2006.

<sup>(3)</sup> COM(2005) 181 final of 3 May 2005.

<sup>(4)</sup> OJ C 107, 30.4.2004.

<sup>(5)</sup> OJ C 92, 17.4.2002.

<sup>(6)</sup> COM(2006) 213 final of 18 May 2006.

<sup>(7)</sup> Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 (OJ L 134, 30.4.2004).

2. The Court considers that the amendments introduced will result, by and large, in an improved overall financial control environment. Nevertheless, further clarifications are necessary and certain incoherencies and inconsistencies remain, namely as regards:

- the exceptions to the budgetary principles,
- the new principle of effective and efficient internal control,
- the methods of implementation of the budget and their compliance with the provisions of the Financial Regulation,
- the accountability of the financial actors — authorising officer, accounting officer — and of the Commission,
- the exceptions and conditions for signing contracts awarded by the Community Institutions on their own account,
- certain provisions regarding grants for communication activities, multiple grants and the renewal of operating grants,
- the provisions proposed in the framework of external actions concerning amounts payable from imprest accounts for crisis management and humanitarian aid, and deadlines for contracts and payments,
- the contents of the report on budgetary and financial management,
- the timetable for the presentation and audit of the Community accounts.

These are dealt with in the following paragraphs.

#### **EXCEPTIONS TO BUDGETARY PRINCIPLES**

3. While the Court welcomes the introduction of the new budgetary principle of efficient and effective internal control <sup>(1)</sup>, and that of proportionality <sup>(2)</sup> and the development of the concept of transparency <sup>(3)</sup>, certain amendments introduced have the effect of diminishing the Budgetary Authorities' control over budgetary management. In particular, certain exceptions remain, as indicated in the Court's previous opinion <sup>(4)</sup>. Furthermore, new exceptions have been introduced, such as the possibility foreseen in the proposed Article 158 to make transfers from title to title of budgetary resources for technical assistance in the area of Structural Funds without any limit.

4. On the other hand, the proposals offer few possibilities to the institutions, other than the Commission, for the simplification of budgetary procedures for justified budgetary modifications, thereby depriving those institutions of the necessary flexibility as regards staff management.

#### **PRINCIPLE OF EFFECTIVE AND EFFICIENT INTERNAL CONTROL**

5. While the Court supports the new budgetary principle of effective and efficient internal control introduced in the proposed Article 30a, further development of this principle is necessary to ensure its effective implementation in line with the principles proposed in the Court's Opinion No 2/2004 on the 'single audit' model (and a proposal for a Community internal control framework). In particular:

- it will be necessary to define the common characteristics of the internal control systems for the different budgetary areas and to take appropriate action to monitor the costs of controls and to evaluate the benefits they bring,

<sup>(1)</sup> See proposed Articles 3, 30a, 53b, 54, 56 and 60.

<sup>(2)</sup> See proposed Articles 3 and 28(a).

<sup>(3)</sup> See proposed Articles 53b(2)(d), 53c(3), 53d(3) and 56(1)(f).

<sup>(4)</sup> Opinion No 10/2005, paragraphs 19, 20, 22 and 24.

- it is essential that the Commission develops a logical framework using common principles and standards, as well as adequate supervision, to be applied at all levels of administration in the institutions and the Member States alike, in order to ensure the integration and coordination of controls,
- notwithstanding that it is a fundamental concept underpinning an integrated internal control framework, there is no indication as to how, by whom or when the definition of 'tolerable level of risk' is to be established. Moreover, the relationship between the tolerable level of risk and the cost/benefit balance of controls has not been established.

6. Overall, the role of the Commission in the context of an integrated internal control framework has not been clarified. Yet the success of the concept is critically dependent on the Commission playing a central role in the development, monitoring and supervision of such a framework. In this regard, it is noteworthy that the supervisory role of the Commission is only envisaged where it delegates managerial responsibility, when implementing the budget on a centralised basis, by indirect centralised management and in the case of decentralised management (see proposed Articles 54 and 56).

#### **METHODS OF IMPLEMENTATION OF THE BUDGET: COMPLIANCE WITH PROVISIONS OF THE FINANCIAL REGULATION**

7. The modifications proposed are designed to introduce improved codification and systemisation of the obligations arising from the different implementation methods and, as such, are welcomed by the Court.

8. However, where the Commission implements the budget by indirect centralised management (proposed Article 56), it shall no longer seek to obtain evidence that the entities to which it entrusts the implementation do so in accordance with the principles of sound financial management. This is in conflict with the provisions of Article 27 of the Financial Regulation which stipulates that budget appropriations shall be used in accordance with the principle of sound financial management.

9. In the case of indirect centralised management the revised proposal also stipulates that the Commission may accept from the entities to which it entrusts the implementation that the audit, accounting and procurement systems '*are equivalent to its own, with due account for internationally accepted standards*'. Thus, the entities to which the Commission entrusts implementation of the budget in such instances, are not bound by the provisions of the Financial Regulation. Furthermore, given that there are no internationally accepted standards for procurement systems nor for compliance audit, the stipulation to take due account of internationally accepted standards is meaningless. The same applies to a similar reference to internationally accepted standards under paragraph 2 of the proposed article dealing with procurement procedures of the beneficiary partner country in the case of pooling of funds arrangements. As a result, in those areas where the budget can be implemented by centralised and indirect centralised management (such as the RTD framework programmes or activities in the area of education and training), different principles, standards and rules may apply to essentially the same type of Community funding (see Court Opinion No 1/2006 <sup>(1)</sup>, paragraph 17).

#### **ACCOUNTABILITY OF FINANCIAL ACTORS**

##### ***Authorising officer***

10. The new proposal for Article 60 of the Financial Regulation provides that the authorising officer by delegation '*shall report to his institution on the performance of his duties in the form of an annual activity report, together with financial and management information and any reservation in relation thereto*'. Any such reservation would not be consistent with the declaration provided for in the same proposed article according to which the authorising officer shall certify that '*the information contained in the report presents a true and fair view*'. While the Court agrees that the Annual Activity Reports and Declarations of the Directors General as Authorising Officers reinforce transparency and management accountability, it considers that any reservations should relate to the Declaration and be confined to clearly defined areas of revenue or expenditure as is the current practice (see Court's proposal in the Annex).

<sup>(1)</sup> OJ C 203, 25.8.2006.

11. As far as the synthesis report is concerned, as the said proposal only provides for a summary of the Annual Reports of the Authorising Officers to be presented to the budgetary authority, the Commission as a college does not assume its responsibility as provided for in Article 274 of the Treaty. Furthermore, the proposal provides for this summary to be sent to the budgetary authority no later than 15 June each year which is too late for the report to be taken into account by the Court in its Annual Report (see further observations at paragraph 23).

### **Accounting officer**

12. The amended proposal for Article 61 clarifies the role and responsibilities of the accounting officer. It also provides that, before the adoption of the accounts by the institution, the accounting officer shall sign them off, certifying that they present a '*reasonable true and fair view*' (emphasis added) of the financial situation of the institution. The term '*true and fair view*' is a comprehensive concept and its qualification by the term '*reasonable*' unnecessarily dilutes the concept so that it loses its meaning. It would be more meaningful for the accounting officer to certify that he/she has reasonable assurance that the accounts present a true and fair view of the financial situation of the institution.

### **CONDITIONS FOR SIGNING CONTRACTS AWARDED BY THE COMMUNITY INSTITUTIONS ON THEIR OWN ACCOUNT**

13. The proposed revision of Article 105, paragraph 2, introduces the possibility for exceptions and conditions to be specified in the Implementing Rules. This provision fails to take account of the primacy of the Financial Regulation which is the sole instrument which may provide for exceptions from the general rules and provisions expounded therein.

### **GRANTS AND SUBVENTIONS**

14. A new provision is introduced in Article 108, paragraph 4, whereby '*each institution may award grants for communication activities where, for duly justified reasons, the use of public procurement procedures is not appropriate*'. The Court considers that this exception is not justified as the circumstances in which public procurement procedures or grant procedures are to be used are already clearly set out in Titles V and VI respectively of the Financial Regulation.

15. The Court supports the principle proposed in Article 111, whereby the applicant shall immediately inform the authorising officers of any multiple applications and multiple grants relating to the same action or to the same work programme. The Court underlines, however, that this principle will be difficult to monitor in practice, notably in the case of multi-partner actions (such as in the ERTD framework programmes) where it is normal practice for consortia of beneficiaries to apply for Community financial support.

16. According to the proposed Article 108a, grants may take the form of: reimbursement of eligible costs actually incurred, lump sums, flat-rate financing or a combination of these forms. For operating grants, the proposed Article 113(2) provides that, when renewed, they shall be gradually decreased. However, the same article proposes that this principle shall not apply in the case of grants taking the form of lump sums and flat-rate financing. Since these forms of grants should be established on the basis of the best available estimates of the costs to be financed, and should be reviewed periodically to ensure compliance with the principles applicable to grants (Article 181 of the current implementing rules), the said exception is not justified.

### **EXTERNAL ACTIONS**

17. The new proposal in Article 63 provides for imprest accounts to be used without any limitation on the amount for payments in the field of crisis management and humanitarian aid. This absence of limitation is against the principle of imprest accounts and the protection of the financial interests of the Union. The Court considers that, while flexibility for these specific operations needs to be taken into account, at least the limits of the amounts decided for such actions should be respected.

18. The proposed amendment to Article 166 extends by one year the possibility for financing agreements to be concluded with beneficiary third countries. Furthermore, it provides for the individual contracts, grant decisions and agreements which implement such financing agreements, to be concluded or adopted no later than three years following the date of conclusion of the financing agreement. However, in the case of long-term and multi-phase infrastructure and rural development projects, the Commission may exceptionally fix an extension of this deadline of up to five years in the financing decision on the project concerned. These deadlines are set to take account of the difficulties in finalising such projects and are welcomed by the Court.

19. The article also provides for automatic decommitment of unused commitments at the end of the fourth year following the year in which the commitment was made ( $n + 4$ ). This is longer than the  $n + 3$  rule which is generally applicable to the budget. In the opinion of the Court the longer deadline allowed is not justified for instruments whose aim is to prepare acceding and candidate countries for accession to the Union, notably in the framework of structural operations where a stricter rule ( $n + 2$ ) applies.

#### REPORT ON BUDGETARY AND FINANCIAL MANAGEMENT

20. Article 122, first paragraph provides that the accounts of the institutions and bodies referred to in Article 121 shall be accompanied by a report on budgetary and financial management during the year. The revised Commission proposal stipulates that that report 'shall give an account, inter-alia, of the rate of implementation of the appropriations together with summary information on the transfers of appropriations among the various budget items.' The budget is presented to, and approved by, the budgetary authorities on the basis of ABB/ABM principles. On this basis, the Commission must attach to the preliminary draft budget activity statements stipulating, *inter alia*, objectives to be achieved and performance indicators set (proposed Article 33(2)). In the Court's opinion it would be appropriate that the report on budgetary and financial management provide details of what has actually been achieved relative to those objectives as illustrated by the indicators.

#### TIMETABLE FOR THE PRESENTATION AND AUDIT OF THE ACCOUNTS

21. The revision of the Financial Regulation in 2003 introduced a new timetable which advanced by one month the dates established for the presentation and audit of the Community accounts. The Court in its Opinion No 2/2002 (see paragraphs 9 to 14) noted, *inter alia*, that, while it supported the accelerated timetable for producing the Annual Report, achieving this would require a consistent approach throughout the Financial Regulation and, as this was not the case, the procedure and timetable proposed, particularly for the Court's Annual Report, were unworkable.

22. The revised timetable entered into force in 2005. This has also coincided with the introduction of the accruals-based accounting system.

23. The experience to date has demonstrated that significant difficulties arise from the revised timetable with the result that the Court's audit is subject to severe constraints:

- the provisional accounts submitted to the Court by 31 March have been subject to significant modifications up to the submission of final accounts on 31 July; this situation is aggravated by the fact that the accounting records are decentralised with the result that the Commission's Accounting Officer can only introduce the necessary amendments to the accounts at a very late stage, leaving too little time for the Court to complete its audit work,
- the summary Activity Report of the Authorising Officers is only finalised on 15 June — the date by which the Court must make its preliminary observations; accordingly, the Court has no opportunity to take into account before finalising its preliminary observations, a document which the Budgetary Authority considers as a key element of the Commission's improved internal control framework,
- as pointed out by the Court in Opinion No 2/2002, this situation adversely affects, not only the Court, but also the Member States as there is inadequate time for the latter's replies to be taken into account before the Court finalises its Annual Report.

24. In the Court's experience, the minimum period necessary for it to carry out its audit after the publication of the provisional accounts is 12 working weeks, and a further three working weeks after the publication of the final accounts in order to finalise the audit. Therefore, in order to allow sufficient time for the Court to complete its annual work, particularly on the accounts and other aspects of the Statement of Assurance, it is necessary either to advance the timetable for the submission of final accounts to the Court to 30 June, or to change the dates for the Court's presentation of its preliminary observations to 15 July and the production of the Annual Report to 30 November, as in the past.

This Opinion was adopted by the Court of Auditors in Luxembourg at its meeting of 14 September 2006.

*For the Court of Auditors*  
Hubert WEBER  
*President*

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ANNEX

**Article 60, paragraph 7**

Commission's original proposal	Commission's revised proposal	Court's proposal
The authorising officer by delegation shall report to his/her institution on the performance of his/her duties in the form of an annual activity report together with financial and management information, and a declaration of assurance certifying that the information contained in his report presents a true and fair view.	The authorising officer by delegation shall report to his/her institution on the performance of his/her duties in the form of an annual activity report together with financial and management information, and <u>any reservations in relation thereto, and accompanied by</u> a declaration of assurance certifying that the information contained in his report presents a true and fair view.	The authorising officer by delegation shall report to his/her institution on the performance of his/her duties in the form of an annual activity report together with financial and management information, and a declaration of assurance certifying that the information contained in his report presents a true and fair view <u>except as otherwise specified in any reservations related to defined areas of revenue or expenditure.</u>