

I

(Resolutions, recommendations, guidelines and opinions)

OPINIONS

COURT OF AUDITORS

OPINION No 1/2007

on the draft Commission Regulation (EC, Euratom) amending Regulation (EC, Euratom) No 2342/2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities

(submitted pursuant to Article 248(4), second subparagraph, EC Treaty)

(2007/C 46/01)

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THE EUROPEAN COURT OF AUDITORS,

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, notably Article 160 C, paragraph 4, and Article 183 thereof,

Having regard to the Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities ⁽¹⁾, and in particular Article 183 thereof,

Having regard to the modified proposal for amending Council Regulation (EC, Euratom) No 1605/2002 approved by the Commission on 18 May 2006 ⁽²⁾,

Having regard to the Court's Opinion No 4/2006 ⁽³⁾ on this proposal,

Having regard to the Council Regulation (EC, Euratom) No 1995/2006 of 13 December 2006 amending Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities ⁽⁴⁾,

Having regard to the Court's Opinion No 2/2004 on the 'single audit' model (and a proposal for a Community internal control framework) ⁽⁵⁾,

Having regard to the Court's Opinion No 1/2006 on the proposal for a regulation of the European Parliament and of the Council laying down the rules for the participation of undertakings, research centres and universities in actions under the Seventh Framework Programme and for the dissemination of research results (2007 to 2013) ⁽⁶⁾,

Having regard to Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities ⁽⁷⁾, as last amended by Commission Regulation (EC, Euratom) No 1248/2006 of 7 August 2006 ⁽⁸⁾ (hereafter the 'implementing rules'),

Having regard to the draft Commission Regulation amending Commission Regulation (EC, Euratom) No 2342/2002 ⁽⁹⁾,

Having regard to the Commission's request for an opinion on the latter addressed to the Court dated 4 July 2006,

HAS ADOPTED THE FOLLOWING OPINION:

Introduction

1. The proposal updates the implementing rules of the current Financial Regulation to take into account the changes made to the Financial Regulation. Both the new Financial Regulation and the new implementing rules are intended to enter into force in 2007, for application to the new generation of spending programmes.

2. The Court has assessed the Commission's proposal against the following principles:

- consistency with the Financial Regulation;
- compliance with the principles of sound financial management;
- simplification of administrative procedures without compromising the protection of financial interests.

3. The Court considers that in most cases the proposed amendments meet these conditions. However, the Court has concerns about a number of issues where:

- the new or amended Financial Regulation requirements are insufficiently developed;
- the amendments go against the principles of simplification and/or protection of financial interests; or
- there is a contradiction with the requirements of the Financial Regulation.

Financial Regulation requirements insufficiently developed

4. The implementing rules are intended as an indispensable accompaniment to the Financial Regulation, setting out the detailed and more technical rules which are essential for applying the Financial Regulation. As such, they should cover all Financial Regulation requirements which may otherwise be susceptible to inappropriate or inconsistent application. The Court identified the following areas where it considers that this was not the case.

⁽¹⁾ OJ L 248, 16.9.2002 (corrected by OJ L 25, 30.1.2003, p. 43).

⁽²⁾ Commission document COM(2006) 213 final.

⁽³⁾ OJ C 273, 9.11.2006, p. 2.

⁽⁴⁾ OJ L 390, 30.12.2006.

⁽⁵⁾ OJ C 107, 30.4.2004.

⁽⁶⁾ OJ C 203, 25.8.2006.

⁽⁷⁾ OJ L 357, 31.12.2002.

⁽⁸⁾ OJ L 227, 19.8.2006, p. 3.

⁽⁹⁾ Commission document SEC(2006) 866 final.

5. **Article 23a** sets out a definition of the characteristics of effective and efficient internal control. The Court welcomes this initiative but considers the reference to 'best international practices' is insufficient, given that formally established best practices do not exist for some of the key issues, such as the verification of the legality and regularity of underlying transactions. The Court recommends that the implementing regulations include the main principles of effective control as set out in the Court's Opinion No 2/2004, notably common principles and standards of control, the basic components of systems and control procedures, the definition of responsibilities and procedures for ensuring the quality of each control level as well as the overall supervision of systems.

6. **Articles 35.4** and **43.6(a)** refer respectively to 'internationally accepted standards' and 'international standards' on procurement procedures. As such standards do not formally exist, this formulation could cause uncertainty and inconsistency. The Court therefore recommends that the principal standards — additional to those set out in **Article 43.6(a)** — intended by the reference are stipulated in the implementing regulations.

7. **Article 42b** recognises that the Commission has no responsibilities regarding the efficiency of internal control procedures where the costs of controls are not charged to the Community budget. However, the basic elements for an efficient system outlined in **Article 23a.2** are also relevant to effectiveness, and the Commission does have responsibilities in the latter regard. The Court therefore recommends that a clear distinction is made between the Member States' and Commission's responsibilities as established by the Treaty.

8. **Article 43.4(g)** requires that agreements concluded with international organisations include 'the detailed arrangements for Commission scrutiny'. They should also cover the right of access of the Court of Auditors to sufficient information to allow it to rely on the audit of the organisation, or where necessary to audit the activity directly, in accordance with international auditing standards.

9. **Article 43.6(b)** stipulates that grants must involve cofinancing. To ensure consistency, the Article should make reference to the derogations from the principle of cofinancing as set out in **Article 253**.

Non-respect of the principles of simplification and/or protection of financial interests

10. **Article 60.7 of the Financial Regulation** sets out the obligation for authorising officers by delegation to provide an annual activity report. The implementing rules do not provide sufficient guidance. For example: the summary of the annual activity reports is only required for the Commission, whereas this may also be appropriate for those other institutions that prepare more than one annual activity report (such as Parliament and Council); no deadline for the production of the reports is

given, although the Commission summary has to be prepared by 15 June of year $n + 1$; the addressees of the reports are not specified; nor are the requirements for their publication. Furthermore, there are other annual reporting requirements, such as the report on compliance with time limits as set required by **Article 106.6** and the reporting requirements of **Articles 54** and **87.5** which could be included in the annual activity report. This is currently specified for the Commission only. In the Court's opinion the resulting multitude of annual activity and other reports with different form, content, timing and publication goes against the principle of simplification.

11. To ensure consistency and simplification, the Court recommends that the implementing rules should set out the content and publication requirements of annual activity reports for application by all institutions alike, incorporating the annual reporting requirements cited in the previous paragraph.

12. **Article 117.1 fourth indent** states 'In sectors subject to a rapid price and technological evolution framework contracts without reopening of competition shall contain a stipulation on a mid-term review. If the conditions initially laid down are no longer geared to the price or technological evolution, the contracting authority may not use the concerned framework contract and shall take appropriate measures to terminate it'. This provision should only apply to framework contracts whose specific contracts are awarded without reopening of competition. The framework contract should also specify what happens with ongoing specific contracts in the case of its termination. This provision risks being the source of litigation because of the vagueness of its terms. Therefore, instead of providing for a mid-term review, the implementing rules should insist on the fact that the length of framework contracts should be adapted to suit areas subject to rapid technological or economic change and include a clause for revision of prices. Additionally, contracts involving several economic operators should provide that the specific contracts be awarded with the reopening of competition.

13. **Article 118.4 second indent (ii)** is superfluous as **Article 158a** requires a standstill period of ten days to be observed with effect from the day following the publication of the contract award notice in the *Official Journal of the European Union*.

14. **Article 130.4(c)**, which proposes a change to the model contract as regards the law to be applied, is superfluous because the contracting parties will be automatically bound by the treaties and applicable decisions and regulations, without this needing to be specified. Furthermore, since this change is only applicable for the Commission, the other institutions are no longer required to indicate the applicable law in their contracts. The Court therefore recommends that the existing text of the Article is maintained.

15. **Article 93.2(b) of the Financial Regulation** requires subcontractors to comply with the same criteria as main contractors as regards exclusion from participation in procurement procedures. However, **Article 130.5** provides insufficient protection of the financial interests of the Communities. Firstly, the candidate or tenderer is only required to submit information on the 'financial and operational capacities' of subcontractors, rather than on the 'financial, economic, technical and professional capacity' required under **Article 135.2** for assessing the contractor or tenderer. Secondly, the information to be provided under **Article 130.5** does not include the information required to assess whether or not the subcontractors would be excluded from participating in the tender under **Article 93.1 of the Financial Regulation**. In the absence of sufficient information there is a risk that a candidate who would be excluded from direct participation would be accepted through indirect means as a subcontractor.

16. **Article 145 and 146** set out the obligations in respect of interinstitutional procurement procedures. As currently drafted, each participating institution would be required to establish committees for opening and for evaluating offers, representing an unnecessary duplication of tasks. The Court recommends that the contracting authority responsible for the interinstitutional procurement procedure should be given the power to nominate single interinstitutional opening and evaluation committees.

17. **Article 158a.1** states that requests or comments from unsuccessful or aggrieved tenderers or candidates 'must be received during the 10 calendar days following the notification of the rejection or award decisions (...)'. This will be 10 days following the receipt of the notification by the tenderer, which therefore may not coincide with the ten day standstill period before which a contract can be signed which runs 'from the day after the simultaneous dispatch of the award decision (...)'. The Court recommends that the two requirements be harmonised to ensure transparency and avoid legal uncertainty.

18. **Article 169a** sets out a number of measures the Commission should take to provide information and advice to applicants for grants. Some of them, such as monitoring the 'size and readability of the application forms' and the organisation of seminars for applicants could be the source of appeals for failed applicants, potentially complicating management and causing delays in the process. The Court recommends that such details are set out in the operational instructions only.

19. **Article 172a** sets out eligibility criteria. Those in paragraph 1 contain repetition, such as (a) with (c) and (d) with (e). Those in paragraph 2 constitute unnecessary detail as, being non-binding, they will be set out in the basic act. The Court recommends rationalising and simplifying the requirements along the lines set out in the attached annex.

Contradiction with the requirements of the Financial Regulation

20. **Article 3.2** sets out thresholds for recovery of interest on prefinancing for external actions ⁽¹⁾ (250 000 euro) and humanitarian aid (750 000 euro) at much higher amounts than the general rule (50 000 euro). In the case of amounts under these thresholds the potential exists for significant interest income, contrary to the non-profit principle set out in **Article 109.2 of the Financial Regulation**. In order to respect this principle, while avoiding complex interest recovery processes, the Court recommends that all interest on prefinancing amounts held should be assigned by the beneficiary to the programme or action concerned.

21. **Article 35.6** states that the 'independent external audit' should be carried out by 'an audit service functionally independent of the entity' being audited. The use of the term 'functional' could be interpreted as allowing internal audit services to perform such audits, which would be contrary to the Financial Regulation principle that the auditor should be external. Furthermore, the Court suggests the implementing rules should make reference to the norms the auditor is expected to follow — such as international auditing standards — and specifically provide for access by the Commission and the Court to the auditor's working papers.

22. **Article 43.2 (d)** defines the European Investment Bank and the European Investment Fund as international organisations under Article 53 of the Financial Regulation. However, this contradicts **Article 54.2(b) of the Financial Regulation** in which these organisations are referred to as 'specialised Community bodies' and which should be the basis for all delegated powers.

23. **Article 118.4 third indent** covers the situation where framework contracts are below the thresholds laid down by **Article 158** for publishing, whereas the specific contracts based thereon exceed those limits. However, in order to comply with **Article 90 of the Financial Regulation** — and to help prevent inappropriate use of the framework contract — the contracting authority must have estimated the value of the contracts expected to be signed under the framework contract before the latter is concluded. As such, the proposed rules are in contradiction with the Financial Regulation, or, as a minimum, superfluous.

⁽¹⁾ The draft regulation continues to use the headings of the 2000-2006 financial perspectives, whereas these have been superseded by new headings in the 2007-2013 financial framework.

24. **Article 125c** allows institutions to decide that 'procedural rules applicable to the contracting authority from a Member State shall apply provided that they can be considered as equivalent to those of the institution'. This is in contradiction with **Article 91 of the Financial Regulation** which makes no provision for the use of procedures other than those set out in the Financial Regulation. Furthermore, the proposed article does not sufficiently develop the rules to implement **Article 91 of the Financial Regulation**: 'the procurement procedure may be carried out jointly by the institution and this contracting authority, as specified in the implementing rules'. For example, it does not define who should make the final award decision or which legal system would prevail in the event of litigation.

25. **Article 160e.1** states that the 'annual work programme shall determine whether grants shall be only covered by a decision or also by a written agreement.' The use of the word 'also' appears to be in contradiction with **Article 108 of the Financial Regulation** where it is stated that grants 'shall be covered either

by a written agreement or by a Commission decision notified to the successful applicant.' The Court recommends that this ambiguity be removed.

26. Revised **Article 122 of the Financial Regulation** states that the report on budgetary and financial management should include information on the rate of implementation of appropriations and summary information on transfers. However, **Article 185** of the implementing rules does not define the information to be provided, but sets out other requirements — the achievement of objectives and events with an influence on activities. The Court recommends the implementing rules cover all aspects of reporting.

27. In addition to the above points, the changes made to the proposed **Financial Regulation Articles 28a, 30a, 33, 72, 73a, 96** and **166.3(a)** must be reflected in the corresponding implementing rule **Articles 23a, 23b, 78, 84, 85b, 134b** and **233a.1(i)**.

This Opinion was adopted by the Court of Auditors in Luxembourg at its meeting of 25 January 2007.

For the Court of Auditors
Hubert WEBER
President

ANNEX

Proposed eligibility criteria for Article 172a

Eligible costs are costs actually incurred and paid by the beneficiary of a grant which meet the following conditions:

- (a) were incurred during the duration of the action or work programme, with the exception of costs related to the preparation of final reports and provision of audit certificates, when provided for in the basic act;
- (b) were incurred for the purpose of achieving the objectives of the action or the work programme which is the subject of the grant;
- (c) are identifiable and verifiable, in particular being recorded in the accounting records of the beneficiary and determined according to the applicable accounting standards of the country where the beneficiary is established and determined according to the usual cost accounting practices of the beneficiary;
- (d) comply with the requirements of applicable tax and social legislation;
- (e) are reasonable, justified and comply with the requirements of sound financial management, in particular regarding economy and efficiency;
- (f) exclude costs that do not meet the conditions referred to in points (a) to (e), including recoverable indirect taxes, duties, interest paid, provisions for future losses or charges, exchange losses, costs incurred for other Community projects and excessive or reckless expenditure.

The costs declared as cofinancing in kind by beneficiaries or third parties should comply with the provisions of this Article.

A general budget setting out estimated eligible costs is submitted with the proposal and, subject to verification by the Commission, is included in the grant agreement or decision.'
