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REPORT FROM THE COMMISSION
TO THE COUNCIL AND THE EUROPEAN PARLIAMENT

Assessment at 31 December 2003 of the Commission’s 2001 Action Plan
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INTRODUCTION

During the last discharge procedure both the Council and the European Parliament asked the Commission to take action pursuant to the recommendations made by the Court of Auditors and showed their interest in a follow-up of the commitments entered into by the Commission.

In this context, the Commission established an action Plan for 2001 containing all the answers to these recommendations of the Court of Auditors in its annual Report 2001.

More than one year after its presentation the Commission considers it useful to draw a first assessment of the implementation of this 2001 action Plan, and its achievements.

The Action Plan for 2001 comprised 94 recommendations resulting from the annual Report of the Court of Auditors, some of which can comprise several aspects or concrete measures to be carried out.

54 recommendations out of 94 are closed (57%), i.e. will no longer be the subject of an additional action on the part of the Commission and 40 are still being addressed.

Among the 54 closed recommendations several cases can be distinguished. For approximately 44% of the cases (24), the Commission considered that either it was not necessary to take new measures, or it had fully respected the regulation in force. For the 55% remaining (30 recommendations), the Commission considers that it took measures responding to the criticisms and to the suggestions of the Court.

The implementation of the latter actions covers the majority of the sectors of the financial perspectives and, except the measures connected with specific cases, can be gathered in two categories:

(i) Modification or adoption of regulatory texts: It is in particular the case for the Research policy with the adoption of the 6th Framework programme which comprises provisions answering directly recommendations concerning the sanctions which can be imposed on contractors, the definition of standard contracts and the procedure for recovery. It must be noted however that the Council did not agree to all the Commission proposals (in particular concerning the eligible costs), thus preventing it from completing all the initiatives taken to respond to the criticisms of the Court of Auditors.

For the common agricultural policy, a similarly considerable number of recommendations could be taken into account under the reform of the common agricultural policy decided in June 2003. Beyond these major regulatory proposals, the Commission also revised other regulatory provisions, for example as regards administrative cooperation for the VAT resource.

(ii) Adaptation and improvement of the internal systems of management, of control and of supervision, and launching audits: In several cases, the Commission re-examined its procedures or developed new tools to respond to the criticisms which were addressed to it. Thus for example it took specific measures to harmonise the presentation of the annual Reports of the Directors-General, and to improve the operation of certain computer systems (database CATS in the agricultural field, database TEN-T for the internal policies). Similarly, reorganisation measures were decided, such as those concerning the implementation of the SAPARD programme or the financing of the ACP Secretariat.
At the end of this first assessment of the implementation of the 2001 action Plan, 42 recommendations are still in the process of implementation. The fact that these recommendations are not closed does not mean that the Commission has not already started to react. Indeed, certain recommendations of the Court of Auditors require a multiannual action on the part of the Commission. It is the case for example of the modernisation of the accounting system of the Commission and the closing of programmes involving the Structural Funds. This is why the report, that the Commission will present soon, present for each of the 40 still open recommendations a progress report stressing what has already been carried out and the complementary measures still to be implemented.
Assessment at 31 December 2003 of the Commission’s Action Plan in response to the recommendations made by the Court of Auditors in its annual report for 2001
1. The introductory sections of the Etats financiers (Volume II, Tome 1 and Volume IV) contain a table of prime importance entitled 'Budget outturn'. This table omits a lot of interesting data, whereas other data such as the balance for the financial year, are pointlessly duplicated elsewhere.

The 'revenue' part of the Financial Statements (implementation of the budget, Volume II, Part 1) should also be made clearer, as regards structure and content. In particular the detailed budgetary headings should be observed, the headings should be indexed, the terminology in the regulations should be used, the figures for forecast and actual revenue should be presented in parallel and, more generally, there should be harmonisation of the various parts of the revenue and expenditure account and the general budget.

(1.17./1.18)

**Commission's response:**

The Commission is taking the recommended action.

In Volume I for 2002, the Commission substantially improved the presentation of the implementation of revenue and expenditure and the link with the outturn table. The revenue table now includes data relating to implementation for the year n-1 (in a separate table) and implementation rates compared with the budget.

It intends to continue to work towards greater transparency in the sense desired by the Court.

2. The Court takes the view that the actual data for the VAT and GNP bases used to calculate the balances and the adjustments of the balances are now entered in the revenue and expenditure account, just like the forecast data concerning these items. However, the calculation operations concerning the burdens on the Member States in respect of these resources should also be set out.

The Court claims that a special table should be drawn up for the UK correction (Chapters 15 and 35) and the essential information given concerning the basic data and the calculation operations on which the overall amount of the UK correction and its financing are based (paragraphs.1.19/1.20)

**Commission's response:**

The recommended action has been taken.

From the accounting report 2002 on, a detail of the calculated VAT and GNI balance is indicated for each Member State and for each financial year for which corrections take place.

Tables with the basic data for the calculations of the amounts of the UK corrections budgeted in the year in question are included in the revenue and expenditure accounts as from the accounts relating to the year 2002.
3. Every year the Commission prepares a working document which explains in some detail the calculation and financing of the definitive correction concerning year n-4. This explanatory document does not form part of the budgetary procedure for fixing the amount of the UK correction and its financing, but is only provided to the Council for information purposes, after the adoption of the Supplementary and Amending Budget. In 2001 this document was presented to the Council on 5 September, after the adoption of SAB No 3/2002. Considering the relevance of the document mentioned before, it would be appropriate to make it available to the two arms of the budgetary authority in due time.

Taking into account the limitation to the scope of the audit, the Court obtained a reasonable assurance that the VAT and GNP resources were correctly assessed and collected. However, the Commission should put forward proposals for the simplification of the final calculation of the financing of the United Kingdom correction. (paragraphs. 1.38/1.39/1.40)

**Commission’s response:**

The Commission is taking the recommended action.

The original idea behind the working document was to give a detailed explanation of the final calculation, using the correction of one year as an example. Furthermore, in the past it has not always been possible to submit this document in advance of the adoption of the relevant amending budget.

In order to use DG Budget's resources in the most efficient way it has been decided not to produce the document as long as the calculation method does not change. The next working document will therefore concern the definitive calculation of the 2001 correction, which is the first to be calculated according to the new Own Resources Decision (2000/597/EC, Euratom) and its annexed “Calculation Method”. The next working document will consequently be submitted in 2005, when the result of the definitive calculation of the 2001 correction will be budgeted.

All basic data for the definitive calculation of the rebate is presented in the explanatory memorandum of the relevant preliminary draft amending budget. The Commission is examining the possibility of including further details.

The new Own Resources Decision and its accompanying working document on the calculation of the UK correction (‘the calculation method’) does give some scope for simplifying the budgeting of the result of the final calculation of the UK correction. This in turn could simplify the final calculation of the financing of the correction. The Commission intends to pursue this opportunity for the year 2001 calculation, to be budgeted in 2005.

4. The Financial Regulation stipulates that the budgetary nomenclature in the context of the budgetary procedure must be set out in titles, chapters and articles. The form of classification used, which must accommodate the very disparate characteristics of the different types of revenue, is uneven. The Court takes the view that the extreme concentration in Title 1 (98.3% in 2001) should be avoided by separating the traditional own resources from the VAT and GNP resources and the correction for the United Kingdom. The surplus available from the previous financial year (Chapter
30) should come under a separate title as it has nothing in common with the balances, corrections and refunds concerning the VAT and GNP resources and the UK correction included under the same title. (Chapters 31, 32, 33 and 35 paragraph 1.21)

**Commission's response:**

*The recommended action has been taken.*

A detailed review of the budgetary nomenclature for revenue took place during the year 2003. A lot of amendments have been proposed for title 4, 5 and 6 of the revenue side. These amendments will in principle be incorporated in the DAB 2005.

5. For a number of warehouses examined, the frequency of physical controls carried out did not reach the levels prescribed by national guidance. The Court takes the view that Member States could improve the national instructions in respect of the control system for customs warehouses so that type, scope and frequency of controls are clearly set out. Instructions should also indicate at which level of the customs service decisions about the control modalities should be taken. Finally Member States should ensure that scheduled controls are carried out. (paragraphs 1.32/1.36)

**Commission's response:**

*The Commission is taking the recommended action.*

Under the Customs 2002 programme a document was entitled 'inventory on control areas'. The document provides customs administrations with an exhaustive list of control areas and sub areas as well as common definitions of control methods.

The Court's observations on warehousing have been followed-up with Member States with a view to identifying any non-conformances with Community regulations and ensuring these are remedied.

The Commission recognises that the picture in relation to controls is uneven. Within the Customs 2007 programme, project groups of customs experts and Commission representatives are working on the use of a common risk management model, standard formats for exchange of control information and selection of risk categories (paragraphs 1.30/1.31/1.35/1.36).

6. In 2001, as in previous years, problems were found with the maintenance of the B accounts in several Member States. In Germany, it is not at present possible to confirm the B account balance, because the database does not allow a breakdown into single entries. The management of the B accounts in Italy is not yet uniform and calculation errors can occur at local and regional level without being detected by controls. Errors in entries in the B accounts were also found in Belgium and France, and inspection reports by the Commission referred to B account errors in Ireland, Sweden and Finland. These errors, though minor in terms of the amounts, reflect a weakness in the accounting for own resources under the Community transit system. (paragraph 1.27)
Commission's response:

The Commission is taking the recommended action.

The Commission is pursuing modifications to Regulation 1150/2000 to improve the structure of the system and has continued to pay close attention to the subject during its own inspections in Member States. Action is ongoing to ensure Member States remedy any systematic structural deficiencies found. Where appropriate recovery orders have been issued.

7. The Court considers that the following measures could be taken in order to increase the effectiveness of administrative cooperation between Member States and the Commission:

a) the SCAC and SCAF committees, could, under the guidance of the Commission, develop best practice in respect of the development of an anti-fraud strategy;

b) exchange of information between Member States could be facilitated by the further development of the VIES to combat fraud, of bi- or multilateral agreements as well as by the introduction of corrective actions in cases where Member States do not provide timely information;

c) special control units to tackle specific VAT fraud cases could be set up to give Member States better opportunities to fight fraud on the condition that these units are integrated in, or work closely with, the CLOs and with the assistance of OLAF;

d) the scope of the information exchange mentioned in Articles 11 and 12 of Council Regulation (EC) No 218/92 should be clarified and made more explicit; information exchanges between Member States could be made more efficient by harmonising the competences and capabilities of CLOs in Member States (paragraph 1.54)

Commission's response:

The recommended action has been taken.

a) The Commission has, together with the Member States, carried out an in-depth examination of VAT fraud in intra-community trade and has identified the various measures that have been taken at national level and which have given the best results in the fight against "missing trader fraud". These "best practices" are based on an enhanced and quicker use of mutual assistance and on an adaptation of national control systems in order to disrupt "missing trader fraud".

b) On 7 October 2003 the Council has adopted Regulation (EC) N° 1798/2003 on administrative cooperation in the field of VAT. This Regulation intensifies the international exchange of information outside the VIES system to strengthen the fight against VAT fraud.

In addition, in its Communication to the Council and the European Parliament on the review and update of VAT strategy priorities (COM/2003/614), the Commission undertook to replace the existing VIES with a higher-powered and more flexible system. The Commission will commence a feasibility study with the intention of creating a new VIES within the lifetime of the Fiscalis programme 2003-2007.
c) The Commission endorses this recommendation. The need for special control units to tackle specific VAT fraud has been addressed in several Commission working papers and reports. In the meantime a majority of Member States has set up anti-fraud units specialised in VAT fraud.

d) Articles 11 and 12 of Council Regulation 218/92/EEC have been repealed by Article 35 of Council Regulation (EC) Nº 1798/2003 on administrative cooperation in the field of VAT. On the one hand, the information which the Member States are obliged to provide to the Commission for the purposes of evaluating administrative cooperation is now described at greater length and the exact detail of the data to be sent is to be decided by the comitology procedure. On the other hand, the new Regulation provides for a clear legal base for Member States to forward to the Commission information on specific cases on a voluntary basis.

In addition, Regulation (EC) Nº 1798/2003 provides now for a legal framework to devolve administrative cooperation in order to ease the burden on the CLO's.

Working closely with the Member States, the Commission will continue in the SCAC and under the Fiscalis programme to work intensively on the issue of VAT fraud. It will shortly be submitting a new report to the Council and the European Parliament on the use of the administrative cooperation arrangements in the fight against VAT fraud.

As far as OLAF’s operational competence in the field of VAT is concerned, the Commission included in both its action plan for 2001 2003 on protecting the Communities' financial interests and the fight against fraud and its work programme 2001 a proposal for a European Parliament and Council Regulation establishing a system for cooperation between the Member States' authorities and the Commission with a view to protecting the financial interests of the Communities against illegal activities, including VAT related activities and money laundering.

The Commission services are preparing a separate proposal under Article 280 of the EC Treaty, laying down specific provisions which confer a role on the Commission in coordinating administrative cooperation (paragraph 1.53).

8. The monthly amounts of agricultural duties made available by France averaged 4.7 million euro from January to April 2001. In May 2001 they increased sharply to 10.3 million euro and remained thereafter at the higher level. For the whole of 2001 this represented an increase over 2000 of 74%, contrary to the general trend of import duties. (paragraph 1.7)

Commission's response:

The recommended action has been taken.

This point was examined during a TOR inspection in 2003 and it was found that there were no financial consequences. This was because the total amount of own resources had been properly made available although, prior to May 2001, the proportion relating to agricultural duties had been understated.
As part of the Annual Report concerning the financial year 1999, the Court recommended that a method of comparing tax sources with statistical sources, tested by both France and Italy, be extended to other Member States and used as a possible means of combating fraud. In its reply the Commission committed itself to discussing this method with the Member States.

In its recommendation on the discharge to be given to the Commission in respect of the implementation of the general budget for the European Communities for the financial year 1999, the Council welcomes with interest the Court's recommendation and suggests that this matter should be examined by the Advisory Committee on Own Resources. Although the Commission has taken adequate steps in carrying out this commitment, the Member States have been unable to come to an agreement. The Court again recommends that the Commission should continue its efforts in this very important area. (paragraphs 1.42/1.43/1.44)

**Commission's response:**

*The recommended action has been taken.*

*This item was discussed at both meetings of the Advisory Committee on Own Resources (ACOR) held in 2001. The conclusion, shared by Italy and France, was that, regrettably, statistical information about theoretical VAT receipts requires such extensive disaggregation to be useful in targeting tax controls that other risk indicators are more readily accessible, more reliable and easier to use. In addition, Member States concluded that ACOR was not the most suitable forum for any further development. However, the findings remain available for use wherever Member States consider that they may prove useful input for their risk analysis systems. Furthermore, the Commission systematically raises this matter on VAT own resources' control missions, in order to ensure that national authorities give full consideration to the implications of discrepancies between theoretical and actual VAT.*
10. In the context of the appraisal of the legality and regularity of the underlying transactions, the Court has audited a sample of 156 transactions. It compared its results with inspections carried out under IACS.

The Court considers that the reporting of IACS inspection results needs to be improved and, in particular, to distinguish between the results of risk-based and random checks. (paragraph 2.44)

Commission's response:
The recommended action has been taken.

Three IACS experts groups were organised during 2003 to discuss, among other things, the matters raised by the Court. On the 16 December 2003 the EAGGF Committee voted several significant amendments to Regulation 2419/2001 that will further enhance the reliability and transparency of annual statistics from 2004 onwards.

In addition to these regulatory changes, additional efforts were undertaken to ensure more clear and uniform statistical reporting and more prompt collection of statistics for claim years 2001 and 2002.

Any failures to comply will as usual be considered in the context of the clearance of accounts, as failure to provide proper and correct statistics is viewed as an indicator of administrative weakness to the Fund that could imply financial risk to the Fund.

As for arable aid schemes, The Member States are required to send a report that shall among other things give the result of the checks carried out. For this purpose the Commission requires from the Member States to report separately the results of cases selected on a risk and random basis with effect from 2000 on the basis of a questionnaire which the Commission services have created. As for animal premium schemes, Member States are not required to report their inspection results in the way proposed by the Court, however the breakdown between random and risk-based checks has indeed been examined regularly, as appropriate in the context of audits of agricultural expenditure conducted by the Commission services; the aim being to ensure that the selection of farmers for on-the-spot checks is representative as provided by Regulation No 3887/92. Furthermore, IACS legislation has been strengthened in this respect by Article 19(1) of Regulation no 2419/2001, applicable as from 1 January 2002, which provides that Member States “shall select randomly between 20% and 25% of the minimum number of farmers to be subject to on-the-spot checks.” This regulatory requirement will adequately ensure the properly based audit conclusions implied by the Court’s remark (paragraph 2.44.)

11. The Commission has a database containing all the information on EAGGF-Guarantee payments that have been made in the 15 Member States in the course of the previous financial year. The Court has established that most of the data have
many shortcomings. The Commission should take the necessary steps to make the CATS database more reliable and useful. (paragraph 2.47)

**Commission's response:**

*The recommended action has been taken.*

*Strict quality controls (e.g. on the use of code lists) have been built in the programme used by the Member States for sending the computer data to the Commission from the financial year 2002 onwards. Furthermore, specific control programmes are available to the EAGGF-Guarantee auditors for in-depth checking of the computer data related to their audits.*

12. Certifying bodies: some of these bodies were appointed late. Some paying agencies do not meet the accreditation criteria. The Commission should take measures allowing to improve this situation. (paragraphs 2.53.-2.55)

**Commission's response:**

*The recommended action has been taken.*

*The Commission recommended in several occasion that the certifying bodies should be appointed earlier in the year and will continue to undertake all possible and reasonable efforts to ensure that this is done. During the certification experts’ meeting held on 18/12/2003 all the delegation were asked to confirm, and actually they did, that for 2003 this recommendation had been followed up. It is worthwhile to recall that in any case in which the certifying body’s work should be considered insufficient, for a reason or another, appropriate action, including disjunction of the paying agency’s accounts, will be considered. It will also closely monitor the procedure for accrediting new paying agencies.*

13. The Court reiterates that the Commission should take action to ensure that corrections are applied for system weaknesses which pose a financial risk for EAGGF. (paragraph 2.71)

**Commission's response:**

*The recommended action has been taken.*

*Previous financial corrections applied for supplementary levy referred to two elements: the amount of levy uncollected and the calculated interest for late payment of that levy. Recent Judgements of the European Court of Justice state that the Member States cannot be required to pay over levies which they have not yet collected (particularly where levies have been challenged in the national courts) - that, if certain monies remain unpaid or are paid late, this is not in itself a violation of the Member States' obligations.*

*The Commissions draws attention to the fact that the reason why large amounts of levy have been uncollected is essentially due to legal action being brought before the national courts by producers who refuse to pay the levy.*
Furthermore, it should be recalled that the Commission has adopted a new Regulation implementing the quota regime (R. 1392/2001) which considerably reinforces the sanctions applicable in case of irregularity or fraud, so meeting the recommendation made by the Court of Auditors.

14. In its follow-up to its observations in the 1997 annual report, the Court notes that the aid for durum wheat greatly exceeds the amount needed to achieve the goal of maintaining producers' incomes. A reform of the CMO would have allowed substantial budgetary savings. The Court considers that its previous recommendations are still relevant. (paragraphs 2.87.-2.89)

Commission's response:

The recommended action has been taken.

With the reform of the CAP, decided by the Council in June 2003, the specific durum aid will be incorporated in the Single Farm Payment (SFP) form 2005 onwards (Council Regulation 1782/2003). In line with the Court of Auditors' analysis of the durum wheat sector and the evaluation by independent experts, the Council decided to limit the impact of additional payment on the calculation of the Single Farm Payment to 291 €/ha for 2005 and to 285 €/ha from 2006 onwards. The aid scheme in non-traditional areas will be abolished altogether from 2006 onwards.

In order to increase the production of high quality durum a specific aid of 40 €/ha is introduced for the production of some varieties with better quality criteria. This aid is valid for traditional areas within the limit of a maximum guaranteed area.

15. There have been shortcomings in the implementation of the CMO's objectives, some of which have not been achieved, and some of the measures taken have had unforeseen and undesired results. In its special report, the Court sets out a number of recommendations for defining the CMO's objectives better and tightening up the controls. As the Commission has committed itself to conducting its first major evaluation around 2004, it should ensure that it keeps to this timetable and that, in particular, it includes an evaluation of the synergies developed by the various types of support for the banana sector. (paragraphs 2.115. to 2.117)

Commission's response:

The Commission is taking the recommended action.

The level of detail in the definition and quantification of objectives is similar to the other market organisations and will be reviewed in depth when the market organisation is evaluated under Article 32 of Regulation (EEC) No 404/93.

Evaluation of the market organisation for bananas is being carried out in 2004. A tender for an evaluation study was launched in 2003 with a contract to be established by April 2004. Results are expected for the end of 2004.

Moreover, a tariff-only system will be introduced on 1 January 2006 at the latest (Article 16(1) of Regulation (EEC) No 404/93, as amended by Regulation (EC) No 216/2001).
More specifically, the Member States' customs procedures on imports have yet to be improved and the Commission will continue to insist that the Member States find a permanent solution to the problem (paragraphs 2.115. to 2.117.).

16. The Court recommends that the Commission should reassess the support given to products which may be grown instead of oilseeds. (paragraph 2.123)

**Commission's response:**

*The recommended action has been taken.*

*With the reform of the CAP, decided by the Council in June 2003, oilseeds as other arable crops will be covered by the Single Farm Payment (SFP) from 2005 onwards (Council Regulation 1782/2003).*

17. The Court has detected a number of weaknesses in the implementation of the aid, but has above all tried to gauge the actual influence which the premium has had on farming methods. The Court considers that the impact is limited. It therefore recommends that the efficiency of the aid should be assessed. (paragraph 2.127)

**Commission's response:**

*The Commission is taking the recommended action.*

*The Commission evaluation plan for the year 2004 schedules the evaluation of the CMO for beef and veal from mid 2004 to end 2006. The work in 2004 will essentially be the preparatory internal work. The extensification payment introduced by Agenda 2000 will be part of this evaluation, although this measure will not be maintained. With the reform of the CAP, decided by the Council in June 2003, the extensification premium will be covered by the Single Farm Payment (SFP) from 2005 onwards (Council Regulation 1782/2003).*

*Concerning weaknesses in the implementation of the extensification payment scheme, deficiencies in several Member States have been found for which financial corrections have been proposed in the context of the Commission’s clearance of accounts procedure.*

18. The Commission should reperform and verify a selection of IACS inspections on an annual and representative basis. (paragraph 2.44)

**Commission's response:**

*The Commission will not be taking the recommended action.*

*The Commission considers that IACS allows to limit to a large extent the incidence of errors. Furthermore, the Commission is continuously improving the control system by amending the relevant regulations and by initiating their full implementation and development in Member States. It is the case for example for the implementation of the bovine identification system or the introduction at the latest by 1 January 2005 of a geographical identification system (paragraph 2.44).*
The reperformance of controls has been a routine part of almost all IACS-related missions for many years, and indeed continues to be an essential component of any on-the-spot audit by the Commission services. This is fully reported in the Commission's audit reports.
19. Despite the introduction, in cooperation with the Member States, of a system for forecasting payment requests, the estimates of the necessary payment appropriations needed are still not very reliable. Moreover, in cases where the available information is such as to modify these estimates no account is taken of it for the purpose of updating budget forecasts (amending letter, supplementary and amending budget). Under these circumstances, as in the case of commitment appropriations, budgetary estimates of payment appropriations continue to be unrelated to the process for adopting interventions and to the progress of the interventions themselves. (paragraph 3.14)

**Commission's response:**

The Commission is taking the recommended action.

It is no easy task to predict the budget implementation of payment appropriations.

In its annual publication "Analysis of the budgetary implementation of the Structural Funds", the Commission has extensively analysed the forecasting performance of Member States, and will continue to do so. On aggregate, the sizeable forecasting errors have been associated with a tendency for very substantial over-estimation of payments by Member State.

The Commission has taken several measures aimed at simplifying Member States' forecasting task, using the information collected in a survey it made to the Member States. The forms to be transmitted to the Commission have been clarified and simplified. The communication channels have been rationalised and there is now a single preferential contact point for the forecasts. Annual reminder letters are now sent not only to the Permanent Representations of the Member States but also to the managing authorities of all the programmes (which should allow a better and quicker dissemination of the information and also reduces Member States' administrative burden with the forecasts). Further reminder letters are now systematically sent to the Member States that have not sent their forecasts in due time. The Commission now sends the results of the forecasting exercise to the Budgetary Authority identifying each Member State individually. It also publishes an exhaustive analysis, by Member State, of historical forecasting performance to create peer pressure. Thus, within the limits allowed by the current legal framework, the Commission has taken big steps aiming at improving the forecasts. For all these measures to lead to better forecasts, however, Member States will need to improve their own procedures.

So far the forecasting ability of Member States has not improved though. The forecasting error for the 2000-2006 programmes was 46% in 2002. The error increased slightly in 2003.

Given the poor predictive ability of Member States forecasts, the last Commission budgets have been rather based on its own estimations. This has allowed an improvement of the execution rate of payment appropriations. In 2002, again for the 2000-2006 programmes, the execution rate of the payment appropriations was
Based on preliminary figures for the 2003 execution, this has improved to 97% in 2003.

The Commission hopes that its efforts to improve the forecasting performance of Member States will bear fruit in the medium term, allowing it to factor such information in the budgeting exercise.

For what concerns commitment appropriations, the situation is completely different. Budgets have been based on the most recent programming available and have been executed at rates very close to 100%.

The low rate of payments in 2000 and 2001 for assistance measures covered by the 2000-06 period is due mainly to their late start.

In the Communication from the Commission to the Council and the European Parliament - Evolution of budget execution of the Structural Funds, in particular outstanding commitments (COM(2002) 328 final of 20.9.2002), the Commission has already examined in detail the differences between Member States' forecasts and the outturn and set out payment prospects for the period leading up to 2010.

The Commission has discontinued (in its revenue and expenditure account) the 'lessons to be learnt' sections, which were a feature of the previous financial year. This is despite the fact that the structural shortcomings observed in recent years would have required much more detailed analysis with a view to suggesting at the right time improvements to be made in the future to the financial and budgetary frameworks (i.e. the financial perspective and the procedures for drawing up estimates of appropriations) as well as the programming and management provisions contained in the regulations governing the structural measures. It would also have been beneficial for the Commission to consider its own responsibility as regards delays in the programming procedure, shortcomings in the estimates of appropriations and the increase in transactions at the end of the financial year.

(Paragraphs 3.18/3.19)

**Commission's response:**

The Commission is taking the recommended action.

As far as the Structural Funds are concerned, the Commission indicates in its Preliminary Draft Budgets the methodology followed to construct the budget appropriations it proposes. The Commission also analyses extensively Member States' payments forecasting performance in its annual publication "Analysis of the budgetary implementation of the Structural Funds", which also analyses the yearly time pattern of transactions. The Commission will continue to do so in the future.

As regards the discontinuation of the 'lesson to be learnt' sections, the Commission takes the view that there is no loss of information because detailed analyses are always given in the revenue and expenditure accounts.

One of the main objectives of the new legislative framework was to speed up and simplify programming procedures. However, the proper programming work, which took place in several successive stages, proved to be especially cumbersome and
difficult to manage. It was typified by a lack of clarity in the division of responsibilities between the Commission and the Member States and by the absence of a precise pre-established programming framework. Long negotiations between the Member States and the Commission proved to be necessary but in spite of that the operational framework for the intervention was still not completely defined. This situation is explained in general by persistent uncertainty about the responsibilities of the Commission and the Member States and by legislation which is still complex in terms of the programming, management and booking of expenditure. The establishment of the areas eligible for Objective 2 interventions is a specific example of difficulties in getting the programming phase off the ground. The Court therefore recommends that the necessary measures should be taken so as to prepare in due course an appropriate framework for future programmes, in particular in the context of the future enlargement. *(paragraphs 3.30, 3.33 and 3.41)*

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A package of measures to simplify the management of current programmes was approved by the Commission in April 2003 (“Communication on the simplification, clarification, coordination and flexible management of structural policies” – C(2003) 1255). These measures were possible without amending the legislation. They cover the coordination of audit work, flexibility in the reimbursement of expenditure by the Commission and in the application of the “n + 2” decommitment rule, streamlining of the mid-term review process including allocation of the performance reserve, and simplification of procedures for amending programmes, for meetings, indicators and reporting requirements. The measures involving routine management were put into effect immediately; the remainder are being implemented in accordance with the timetable. In the financial control area specific measures included publication of an updated Structural Funds audit manual in December 2003 (for the European Social Fund a supplementary audit manual was also issued), guidance (included in the audit manuals) on sample checks, and clarification of the requirements for retaining documents as part of the audit trail (Regulation (EC) No 2355/2002, amending Regulation 438/2001). The Commission also discussed with Member States the conclusion of “contracts of confidence”, which will allow the Commission to reduce its own audit activity in the Member State. With several Member States negotiations on contracts of confidence have begun.

The Commission expects the simplification measures to help speed up implementation of the current programmes. In this connection it is worth noting the increase in payments of Structural Funds for the 2000-06 period in 2003.

For the new Member States the Commission in 2003 completed the negotiation of the main documents for their 2004-2006 programmes (CSFs and Objective 1 SPDs). This should allow formal approval of programmes immediately after accession in May 2004 and an early start to implementation.

In preparation for the new Structural Fund period starting in 2007, the second progress report, following on from the Second Report on Economic and Social Cohesion of 2002, was published in January 2003 and a seminar with Member States was held in March. The 3rd Report on Economic and Social Cohesion,
which will set out the broad lines of the Commission’s proposals for the future period, will be published in February 2004, followed in May by a “Cohesion Forum”. The Commission intends to finalise its proposals for the regulations governing the new period in 2004 with the aim of having the legislative framework in place by the end of 2005.

22. In addition to these problems with programming procedures, the legislation governing expenditure proved to be complex, and uncertainty persisted as regards the interpretation of a number of basic questions such as the eligibility of certain items of expenditure, the rates at which revenue-yielding investments were jointly financed or the definition of the final beneficiary. (3.32)

Commission’s response:

The Commission is taking the recommended action.

Regulation (EC) No 1685/2000 on the eligibility of expenditure for co-financing by the Structural Funds was amended by Regulation 1145/2003 to clarify certain points such as bank charges in INTERREG programmes and the status of payments into venture capital funds as expenditure actually paid out. No change was made to the position of advances of funds to beneficiaries, after the Member States had rejected the proposal to consider such advances as eligible expenditure in the discussion of the simplification package (the adoption of Regulation 1145/2003 was challenged in the Court of Justice on procedural grounds and the Commission will withdraw and reissue it in early 2004). In addition to the guidance note on the consideration of revenue in infrastructure projects, the Commission in December 2002 updated the Guide to cost-benefit analysis in ERDF, Cohesion Fund and ISPA projects. It has held several meetings with national authorities to improve the methodology of cost/benefit analyses. The Guide sets out the principles to be applied in the financial analyses that serve as a basis for determining the co-financing rate, including revenue, residual value and discount rates. In April 2003 the Commission wrote to the Member States to remind them of these principles and setting certain parameters for the calculation of the co-financing rates.

23. The dividing up of the management of structural measures amongst various Commission departments meant that it was still difficult to arrive at an understanding of the overall situation. Moreover, the common database for the Structural Funds, which is intended to make electronic exchanges of information possible, was not operational when the programmes were being negotiated. At the end of 2001 some information in particular concerning the IFOP, was still missing. (paragraph 3.37)

Commission’s response:

The Commission is taking the recommended action.

DG FISH entered the initial financial allocations for FIFG in 2000-06 on to the common SFC database in July/August 2002 and has since updated this information. However, it does not use the system for processing payment claims. The SFC already produces certain types of report and performs analyses such as for “n + 2”, but is being improved and developed so that it can offer further functions. Links to important documents are being created and the possibility of
electronic signature provided. A Structural Funds portal in which the SFC would have an important role is also being developed. In 2004 the Commission will define the necessary links between the SFC and the architecture of its new general accounting system.

24. The checks which the Member States are required to perform before the completion of each form of intervention from the period 1994-1999 are an essential component in the reliability of their systems and the regularity of requests for payments. Despite some improvements which are intended to bring about uniform application of the rules, the control systems still do not ensure that the checks on which final declarations of expenditure rely are rigorous and reliable enough. In 2001 the Commission finally closed 53 1994-1996 Objective 2 interventions (16 ERDF and 37 ESF). At the end of 2001 there were still 53 interventions open, representing 575 million euro of commitments outstanding (including 44 ERDF for a total of 540 million euro and nine ESF for a total of 35 million euro). The closure procedures applied to 1994-1996 Objective 2 measures and Cohesion Fund projects are substantially identical to those for the preceding period. In view of the closures that will occur from 2002 onwards the Commission should therefore reinforce its initiatives, including improving the coordination of the work of the departments that are responsible for the different structural measures (paragraphs 3.62 and 3.81).

**Commission’s response:**

*The Commission is taking the recommended action.*

In 2003 the Commission closed the bulk of the 1994-96 Objective 2 programmes remaining open at the end of 2001. By the end of 2003 only eight such programmes remained open for either ERDF or ESF, five for ERDF and three for ESF, representing €70 million of commitments (€66 million ERDF, € 4.7 million ESF). For most of the other programmes from the 1994-99 period the Member States only sent the documents required for closure just before the deadline of end-March 2003. By the end of 2003 the Structural Fund departments had completed their scrutiny of these documents and the closure process with final payment and the decommitment of unclaimed expenditure for programmes representing 41% of the commitments outstanding at the end of 2002. The procedures applied were common to all the four funds and conducted rigorously using checklists. Any unclear issues were resolved in consultation between the four departments. In roughly two-thirds of programmes clarifications of matters in the closure declarations concerning the audit work done before the winding up of programmes or the reasons for qualifications of the statements were requested. There was close coordination between the Structural Fund departments and OLAF to ensure that all reported cases of irregularity had been cleared. In addition, the departments carried out a substantial number of on-the-spot audits of programmes already closed. Where these audits have detected deficiencies in the audit work or the closure declarations themselves were qualified to indicate a risk of irregularity in the expenditure declared which cannot be resolved, the Commission will apply financial corrections. These may be at flat rates on a basis agreed by all funds. The Structural Fund departments will continue the closure work and the audits of closed 1994-99 programmes in 2004. Reference is made to the Commission’s replies to points 5.20-5.21 and 5.54 of the Court of Auditors’ 2002 report (OJ C 286, 28.11.2003, p. 1).
25. The procedures for examining final payment requests still took the form of interdepartmental consultations, and respective responsibilities had not been amended since the previous period. The follow-up of such audit observations continued to rely on various databases that had been set up without any coordination as the unified database announced by the Commission could not be operational before 2002. (paragraph 3.48)

Commission's response:

The Commission is taking the recommended action.

For the closure of programmes from the 1994-99 period all the Structural Fund departments have applied common rigorous procedures. The full entry into production of the audit management tool SYSAUDIT, which among other things will monitor effective follow-up, was delayed. It is being brought into use in the first part of 2004. In the meantime other Structural Fund departments used other systems to follow up audit findings; for instance, DG EMPL is following up all its recommendations on the systems for 2000-06 programmes with its computerised audit follow-up system GESAUDIT, which it developed in 2002.

26. The regulatory management and control arrangements for the 2000-2006 period have been strengthened. However, their implementation is already marred by delay, the structures are not yet all operational and independent auditing of the operations effected has not begun. The Court detected in interim payments the presence of ineligible expenditure of the same types as for previous periods, which suggests that some of those involved are not sufficiently conversant with the rules applicable. In order to satisfy itself that the management and control systems meet the standards imposed by the regulations, the Commission is required to examine the functioning of the systems at regular intervals. For that, on-site visits are necessary. However, a small number of visits were made in 2001 by DG REGIO and PECHE, one was made by DG EMPLOI and DG AGRI made none at all. As a result, the Commission did not have adequate assurance in regarding the reliability of these systems. In some Member States weaknesses, such as the absence of checks on paid invoices or equivalent documents, are present in the procedures for verifying the reality and eligibility of expenditure. As a consequence expenditure declarations are drawn up without any check on whether the expenditure was actually incurred. The Commission should therefore try to complete its checks in the Member States as soon as possible and should ensure that the control standards and rules of eligibility, as well as the sanctions to be imposed for non-compliance, are circulated and understood at every level. (paragraphs. 3.66, 3.67 and 3.82)

Commission's response:

The Commission is taking the recommended action.

The Structural Fund departments are continuing their on-the-spot audits of the management and control systems which Member States have set up for 2000-06 programmes. The number of such audits by Fund undertaken up to the end of 2003 was as follows:

- ERDF : 37
For 2004 DG REGIO is planning a further 15 audits of systems for the current programmes, while DG EMPL plans 40. DG FISH will complete its audit of all FIFG programmes by March 2004. DG AGRI will have audited programmes representing 41% of EAGGF Guidance expenditure by February 2004. DG REGIO carried out 10 audits of the systems required for Cohesion Fund projects under Regulation 1386/2002 in 2003 and has a further five such audits on its audit programme for 2004.

27. In the case of a sample of innovative and preparatory local employment projects which were directly funded by the Commission, the Commission's financial management procedures had not been sufficiently stringent in some cases. In addition, value for money on such projects was not assured due to a degree of overlap between the different innovative measures and the authorisation of such projects. (paragraph 3.118)

Commission's response:

The Commission is taking the recommended action.

Great efforts were made to rationalise the available Community support for local employment initiatives directly financed by the Commission. This is why new projects have not been financed under budget line B5-503 since 2003, to avoid overlap between action under Article 6 and preparatory measures for local employment financed in 2001 and 2002 from this line.

The Commission's work in this area in 2003 has primarily focused on the exchange and dissemination of good practices, the development of methodological and other tools to assist all those involved and evaluation by subject and by programme of action supported by the Commission to date. The Commission has also actively encouraged the Member States to develop the regional and local dimension of their employment policies in the framework of the European Strategy for Employment.

With regard to innovative actions co-financed under Article 6 of the ESF, targeted calls for proposals have been launched and a rigorous system of selection and management of projects has been put in place. Financial management of projects has also been improved and controls - including on-the-spot controls - have been stepped up within the limits of available resources.

28. The Court notes that, in general, the Commission's follow-up to the observations made in the 1999 and following Statements of Assurance has been more diligent than for previous DASs. Nevertheless, although the Court's observations often reveal management and inspection shortcomings which are common to many programmes, the Commission rarely extends its investigations beyond the necessarily limited samples examined by the Court. Particularly with regard to closed interventions, the Commission should evaluate the impact of errors on the entire intervention
concerned rather than confine itself to recovering undue financing in respect only of individual cases which have not been contested. (paragraph 3.104)

**Commission's response:**

**The Commission is taking the recommended action.**

_When errors detected by the Court of Auditors clearly point to the existence of a systemic problem the Commission extends the follow-up action beyond the cases where the error has been found. Examples include public procurement in Spain, where in 2003 DG REGIO extended its enquiry to other cases and is proposing an across-the-board flat-rate correction to compensate for breaches of these rules in 1994-99 programmes, and an ESF case in France. As a result of an audit carried out by the Court in Paris in 1998 on the Chambre des métiers d'Ile de France, for a specific project, with detailed additional checks being carried out later by the Commission at the French Ministry for Crafts and SMEs, a net financial correction of € 22 million was decided in 2002 for the 1994 French Objective 3 SPD for the whole of the measure in question (Decision C(2002)44 of 21.03.2002)._
29. For the TEN-T programme, the Commission should strengthen the legal and control framework (for instance requiring offer letters between Member States and final beneficiaries and developing and implementing clearer rules with regard to the eligibility of costs). The evaluation of proposals should be improved by using more intensively external experts and should be properly documented. Administrative procedures and IT-systems should be modified taking into account the specific requirements of the TEN-T programme. Completed TEN-T actions should be regularly audited (paragraph 4.74)

**Commission's response:**

The Commission is taking the recommended action.

The Commission has introduced in 2003 a new version of the Commission decision that has strengthened the role of the Members States (control, appraisal, monitoring, evaluation...) and has defined the responsibilities of each partner involved in the using of this financial contribution. In 2004 the Commission Decision will be revised again to include more precise conditions related to obligations of the Member States. The Commission now formally addresses the Decision to the final beneficiary as well as to Member States and defines more clearly their respective roles.

The clarity of the definition of works and studies has been improved. The Commission has introduced the use of a standardised cost statement in the new version of the 2003 Commission Decision, as well as within the 2003 review of the TEN-T procedures, which has resulted in a TEN-T handbook which will be used at the beginning of 2004. More precise rules regarding publicity obligations will be developed using existing Structural Funds practice as a guideline.

The Commission reflects on the use of external experts in the evaluation of the projects.

30. The Commission is encouraged to protect the Community's financial interests by imposing the sanctions provided for in Council Regulation No 2988/95. In addition to the recovery of the wrongly obtained advantage, these sanctions should be visible and provide for proportionate administrative measures and penalties in order to be both effective and dissuasive. These sanctions could be defined in model contracts or introduced by means of a specific sectoral rule. (paragraph 4.51)

**Commission's response:**

The recommended action has been taken.

The FP6 contracts include penalties in the form of "liquidated damages" (see below), the possibility of audits and controls, by the Court of Auditors and others, and specific provisions as regards the recovery of amounts wrongly paid.

**Liquidated damages**
Without prejudice to any other measures provided for in this contract, the contractors agree that the Community, with the aim of protecting its financial interests, is entitled to claim liquidated damages from a contractor who is found to have overstated expenditure and who has consequently received an unjustified financial contribution from the Community. Liquidated damages are due in addition to the recovery of the unjustified financial contribution from the contractor.

1. Any amount of liquidated damages shall be proportionate to the overstated expenditure and unjustified portion of the Community contribution. The following formula shall be used to calculate any possible liquidated damages:

\[
\text{Liquidated damages} = \text{unjustified financial contribution} \times \left( \frac{\text{overstated expenditure}}{\text{total claimed}} \right)
\]

The calculation of any liquidated damages shall only take into consideration the period relating to the contractor's claim for the Community contribution for that period. It shall not be calculated in relation to the entire Community contribution.

2. The Commission shall inform the contractor which it considers liable to pay liquidated damages in writing of its claim by way of a registered letter with acknowledgement of receipt. The contractor shall have a period of 30 days to answer the Community's claim.

3. The procedure for repayment of unjustified financial contribution and for payment of liquidated damages will be determined in accordance with the provisions of Article II.31.

4. The Commission shall be entitled to compensation in respect of any overstated expenditures which come to light after the contract has been completed, in accordance with the provisions of paragraphs 1 to 6.

5. These provisions shall be without prejudice to any administrative or financial sanctions that the Commission may impose on any defaulting contractor in accordance with the Financial Regulation or to any other civil remedy to which the Community or any other contractor may be entitled. Furthermore, these provisions shall not preclude any criminal proceedings which may be initiated by the Member States' authorities.

6. Further, as established by the Financial Regulation, any contractor declared to be in grave breach of its contractual obligations shall be liable to financial penalties of between 2% and 10% of the value of the Community financial contribution received by that contractor. The rate may be increased to between 4% and 20% in the event of a repeated breach in the five years following the first breach.

31. It is recommended to complement the regular on-the-spot checks, performed by the officials in charge of monitoring TEN-T actions, by ex-post financial and technical audits. (paragraph 4.33)
**Commission's response:**

The Commission is taking the recommended action.

In conformity with the Court’s recommendation DG TREN’s central financial audit cell has audited a sample of TEN-T actions in 2003. These audits will continue in 2004. Thanks to increased human resources in the financial audit cell and a new framework contract being concluded with an external audit firm, the number of audits will be further increased.

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32. Model contracts for indirect RTD actions should provide for participants bearing unlimited joint and several liability for the use made of the Community financial contribution (with the exception of participants such as public universities). (paragraph 4.50)

**Commission's response:**

The recommended action has been taken.

The FP6 standard contract includes the principle of joint and several liability for contractors who are not public entities, international organisations or organisations whose participation is guaranteed by a Member State or associated country. This liability applies to all projects except Marie Curie contracts, specific action for SMEs and certain specific and duly substantiated support actions.

**Financial collective responsibility**

1. Should the contract be terminated or the participation of a contractor be terminated in accordance with Article II.16, and any contractor does not honour the reimbursement of the amount due by that contractor, the consortium will reimburse the amount due to the Commission.

   The amount due to the Commission may not exceed the value of the contribution due to the consortium in accordance with Article 5.

2. The amount to be recovered shall be allocated between the remaining contractors other than those referred to in paragraph 3 in accordance with their pro rata share in the overall project.

   This allocation shall be based on the relative weight of all those contractors not excluded by paragraph 3, taking into account their share of the provisional costs as indicated in Annex I when pre-financing is to be recovered and their share of accepted certified costs when payment is to be recovered.

   Any amount claimed from a contractor shall not exceed the contribution it is entitled to receive according to applicable reimbursement rates. The amount a contractor is entitled to receive is based on its provisional costs as indicated in Annex I when pre-financing is to be recovered and is based on its certified costs accepted by the Commission when a settled payment is to be recovered.

3. Paragraphs 1 and 2 do not apply where the defaulting contractor is a public body, an international organisation or a contractor whose participation to the indirect action is guaranteed by a Member State or an Associated State.
4. The consortium is not collectively responsible for:

a) any amount owed by a defaulting contractor for any breach discovered after the final implementation date;

b) liquidated damages due by a contractor in accordance with Article II.30;

c) sanctions referred to in Article II.30 imposed on a defaulting contractor.

33. The efforts to recover overpaid Community funds from beneficiaries need to be intensified, specifically with regard to DGs RTD, INFSO and TREN (paragraph 4.76)

Commission's response:

The recommended action has been taken.

Article 73 of the new Financial Regulation introduced the mechanism of offsetting which facilitates the recovery of overpayment. Moreover, the reporting procedures on the state of play of recovery have been reinforced on Commission level. These procedures have been implemented in the various Directorates-General in accordance with their organisation.

As far as DG INFSO is concerned, a specific tool facilitating the implementation of audit results has been developed.

At DG TREN the follow-up procedure of the recovery of the overpaid funds has been strengthened and the audit follow-up is now a performance indicator monitored regularly.

In February 2003, DG RTD set up a help desk on recovery orders in the central financial unit.

The main tasks assigned to this help desk are:

- the animation of a network of liaison officers for recovery orders,

- creating guidelines on recovery orders and up dating them, (http://intranet-rtd/services/f_procedures-ordres-recouvrements_fr.shtml)

- providing a coaching service, which is complementary to the training sessions organised by DG Budget,

- reporting on recovery orders but also on potentially abnormal RAL in order to tackle possible delays in establishing recovery orders (including targeted exercises).

- DG RTD produces a monthly financial scoreboard available on the DG’s Intranet site, and it includes recovery orders pending (http://intranet-rtd/politique/ics12_fr.shtml).

On the preventive approach, it can be mentioned that, in addition to existing measures, such as verification of contractors’ legal and financial situation and use
of financial guarantees when necessary, FP6 has introduced the following measures:

- the collective responsibility of contractors,
- audit certificate,
- new scheme for pre-financing (advance payments adapted to actual costs periodically during the duration of the project).

34. In its Special Report No 2/2002 (Socrates and Youth for Europe) the Court made a number of recommendations for improving the management of these programmes which should be taken into consideration. These include the replacement of the TAO with a Community agency, clearly defining the relationship between the Commission and national authorities, improving control and monitoring at all levels and providing effective and timely evaluations. (paragraph 4.77)

Commission's response:

The Commission is taking the recommended action.

The Commission confirms that it plans to replace the temporary TAO which has been helping it to manage the Socrates II and Youth for Europe programmes by a Community agency: it is expected that it will adopt the decision creating the agency in 2004 and that it should become operational in 2005. The agency will be responsible for managing certain centralised aspects of the programmes in the field of education and culture.

The Commission confirms that the entry into force of the new Socrates II and Youth for Europe programmes has been the impetus for more use to be made of networks of national agencies for managing decentralised aspects of these programmes; in particular, these improvements include clarification of the respective responsibilities of the Commission and the Member States in the operation of the agencies (resources to be placed at the disposal of agencies, tasks to be accomplished by agencies).

The Commission is striving to improve control and monitoring of the implementation of programmes in the field of education and culture (particularly Socrates II and Youth for Europe). In particular, at the end of 2001, it published an invitation to tender for assistance by audit firms to enable it to increase its control activities: the number of agreements audited therefore rose from 50 in 2002 to nearly 200 in 2003.


35. The Commission should aim for a homogeneous implementation of the TEN-T programme applying the same provisions to all beneficiaries in all Member States. The legal framework of the TEN-T programme should be strengthened in order to improve the protection of the Community's financial interests. Where contracts are not concluded with final beneficiaries, offer letters could be implemented by
Member States based on a framework set by the Commission. These offer letters, requiring a written acceptance by the beneficiary, should define the terms and conditions of the grant thus enhancing the awareness of beneficiaries to the specific requirements to be met when implementing the action. \(\text{paragraph 4.31}\)

**Commission's response:**

*The Commission is taking the recommended action.*

Since 2002, the Commission notifies the Commission Decision directly to the Member State and to the beneficiary. For a homogeneous implementation of the programme, the 2003 decisions regroup in only one comprehensive document "the role and the responsibilities of the Member States and the final beneficiaries" (annex I for the technical part and annexe II for the modalities of execution). In the context of the strengthening of the role of the Member States, and to avoid a risk of "dilution" of responsibilities through different sub-agreements, a separate contract (to which the Member States are not parties,) or offer letters should not be considered necessary.

The notification of the decisions to the Member States and the final beneficiaries stipulates their respective obligations and rights. Within this contractual legal framework, the new 2003 Commission Decision also states that any substantial modification, reduction, suspension, cancellation of the Commission Decision, must be notified to the final beneficiaries and the Member States prior to taking place. A handbook has been elaborated which will contribute to clarify the legal framework of the TEN-T programme and the obligations of the Member States and the final beneficiaries.

36. DG TREN should rigorously apply eligibility criteria for proposals (in particular with regard to the reception dates); strengthen the evaluation process by widening the use of external experts, and properly document all controls operated. \(\text{paragraph 4.35}\)

**Commission's response:**

*The Commission is taking the recommended action.*

The integration of the specific TEN-T procedures in the official Manual of procedures has clarified the requirements concerning the documentation of evaluation and decision process.

Since 2003, the Commission operates with a call for proposals with binding deadlines. The Commission reflects on the use of external experts in the evaluation of the projects.

37. A migration from the current databases to the central DG TREN IT-system should be done as quickly as possible, taking into account the specific requirements of TEN-T. In the meantime, solutions should be sought on how to cope with key functions with regard to proposal, contract and/or project management which are as yet missing or incomplete in the current IT systems \(\text{paragraph 4.36}\)
**Commission's response:**

The recommended action has been taken.

The integration of TEN-T into the central DG TREN-T project management system is achieved.

38. In order to comply with the Commission's Internal Control Standards, DG TREN is also invited to apply the procedures approved by its Director-General, modified where necessary to reflect the actual procedures in place for managing the TEN-T programme. Operational procedures should then be kept up-to-date (paragraph 4.34)

**Commission's response:**

The recommended action has been taken.

The specific procedures for TEN-T have been incorporated into the Manual of Procedures and have been applied in 2003. Regular updates are made.

39. In order to reduce the risk of non-eligible expenditure being unintentionally and intentionally declared by final beneficiaries and to allow for a more accurate and effective financial management of indirect RTD actions by the Commission services, it is recommended to fundamentally simplify the cost reimbursement system in the forthcoming 6th Framework Programme (2002 to 2006). The three main types of cost systems (AC, FC, and FF) should be replaced by a single system and the ten cost categories should be reduced to three (i.e. personnel, co-ordination costs and specific costs) with a much wider use of flat rates (paragraph 4.47)

**Commission's response:**

The recommended action has been taken.

The action has been completed. As the proposal from the Court of Auditors was not approved by the Council and the European Parliament, that recommendation was not acted upon. However, many other simplifications have been incorporated into the FP6 standard contract, including the elimination of cost categories, the use of participants’ accounting systems, the certification of costs by external auditors and simplification and consistency in cost models and their application.
These trends (the cumulative value of outstanding commitments dating back five years or more increased from 933.9 million euro at the end of 1998 to 1589.6 million euro at the end of 2001) underline the need for constant monitoring of the OCs in order to contain them. It is important that the Commission equip itself with the means to obtain reliable and complete accounting and management information to facilitate the management of the measures financed. This information should make it possible to carry out in-depth analyses of the development of the OCs and the nature of the payments made (advances or others) in order to compare the rate of disbursement of the aid with the progress of implementation on the ground. (paragraph 5.10)

**Commission's response:**

*The Commission is taking the recommended action.*

AIDCO has consistently pursued during 2002 and 2003 the systematic review of old and dormant commitments, adding each year a new budget year to the review exercise (the latest being budget year 1997, added in 2003 to the review process). The monitoring system of the review results (Excel tables on AIDCO Intranet), put in place in 2000, has been kept running and the tables periodically updated. In 2003 steps were taken in order to fully integrate this monitoring and reporting system on old and dormant commitments into the CRIS database, which is the general management tool for external aid. This will inter alia also facilitate reporting on old or dormant commitments by delegations. The necessary analysis and programming was undertaken and the new facility is now being subject to tests, in order to become operational in the first half of 2004.

With the full operation of CRIS as from beginning 2003, a single database recording financial and contractual information on projects became available, and it was thus possible to launch in 2003 a more targeted internal review exercise. This was specifically targeted at under-performing commitments (even if not formally neither dormant nor old), with low contracted amounts and/or slow disbursement pace and/or low disbursement ratio. The commitments identified were reviewed at the highest level of management and corrective action decided, ranging from speeding up measures, or scaling down of activities, or closure of programmes.

As regards analysis on the basis of the nature of payments made, the compliance of the accounting system with new provisions in article 81 of the new FR in force from 2003 onwards will allow in the future to incorporate the uncleared pre-financing criteria as a risk criteria in a automated and systematic way.

As regards monitoring of progress of implementation on the ground, CRIS has already a module which allows the regular monitoring of projects. This module will in 2004 be expanded to also cover sectoral programs and budget support operations. Furthermore the Commission will in 2004 introduce a new module for the management of the project pipeline and financial planning and forecasting. The module will allow the registration of key milestones and a comparison between forecasts and actual implementation.
41. The Commission should deal with this matter quickly in order to ensure that systematic audit programmes are established, including by clearly stipulating the responsibilities required within the Commission, so that the conclusions of audit reports are acted upon. (paragraph 5.21)

**Commission's response:**

The Commission is taking the recommended action.

In December 2002, EuropeAid has adopted an audit programme for the financial year 2003 on audits carried out under the direct supervision of headquarters and delegations. This audit programme has been closely monitored during its execution. The second programme relating to the financial year 2004 was adopted in December 2003 on the basis of a risk assessment.

The follow-up of audit reports is clearly defined to be the responsibility of the authorizing officers and authorizing officers by subdelegation.

Since the reform, DG RELEX has set up an annual internal audit programme which focused, among other things, on the audit of the whole external service during the first half of 2002. In the framework of the monitoring of the administrative reform and, in particular, of internal control standard No 21, all audit reports are catalogued and observations and recommendations are followed up in an appropriate manner through action plans.

42. The Court recommends that:

- the Commission takes further steps to ensure that organisations responsible for handling EU funds strengthen their internal control systems, in particular to ensure the adequacy of supporting documentation and their tendering procedures. The Commission should lay down more specifically the minimum standards which are required;

- the Commission takes the steps necessary to ensure that sufficient reviews and audits are carried out by it, or on its behalf, to enable it to judge whether the internal control procedures applied by its implementing partners are adequate, and takes corrective action if necessary. (paragraph 5.50)

**Commission's response:**

The recommended action has been taken.

In the area of humanitarian aid, the organisations handling the EU funds, have signed a Framework Partnership Agreement, that has been arrived at after consulting all relevant stakeholders. This sets out the minimum standards, in particular in respect of supporting documentation and tendering, which the organisations have to comply with. In the light of the reform and in compliance with the new financial regulations and implementing rules, a new Framework Partnership Agreement has been approved in 2003 and is now being applied. In respect of tendering, the new Framework Partnership and in particular its annex V, adopted by the college on 28 October 2003 on the basis of article 238.2 of the implementing rules for the Financial Regulation, reinforces the obligation of
humanitarian organisations of establishing standard procedures on procurement and guidelines for drafting tender documents. These procedures comply with the best international practice. The Commission will exercise its powers of control, on documents and on the spot, in order to verify the conformity of the humanitarian organisation's procedures on procurement and its implementation (point 1.3.4, Annex V of the Framework Partnership Agreement).

Echo operates an extensive number of reviews and controls: both at the stage of the appraisal of each operation by it's Technical Assistants, the appraisal by the operational and financial desks as well by the subdelegated authorising officer and the liquidation by the finance unit. ECHO officials have carried out and managed a substantial number of audits over the last years. In June 2002 following a major call for tenders ECHO contracted an external audit company to undertake audits, which substantially increased the audits carried out in 2002 and 2003. Hence, 96 audits at the headquarters of ECHO's partners were completed in 2003 with another 44 audits in an advanced on-going state and 16 field audits were completed with another 13 on-going. The audits cover checks on internal controls and systems put in place by ECHO partners and substantiate the documentation supporting costs claimed from ECHO. By this means all partners are expected to be audited every 2 years. Furthermore, the human resources devoted to auditing have tripled.

43. Whereas the monitoring system can now identify projects' weaknesses, additional work needs to be carried out to be able to analyse their underlying causes. Furthermore the quality, performance and methodology of the monitoring system should be regularly evaluated by the Commission (paragraph 5.77)

Commission's response:

The recommended action has been taken.

1. The results oriented monitoring system (ROM) gives, in real time, an independent overview over projects’ progress and likely success. Underlying causes for success or failure are analysed in depth through evaluations. The two tools (evaluation and monitoring) are distinct, but complement and reinforce each other.

2. The Commission has put in place a coordination function whose tasks include quality control and development of methodology. As planned, works have started to assess the utility of the system (questionnaires to users).

44. The Court recommends that:- the added value of the European Union's interventions in comparison to the World Bank and the International Monetary Fund should be more clearly established;

consideration should be given to creating a more harmonised approach between MFA and SAF, so that countries in similar situations are dealt with in a similar manner;

- the Commission's decision making for the various phases of the management of macro-economic assistance should be more transparent, and in particular the Commission should document its justification for waiving conditions;
- the Commission's monitoring of the quality of financial management in beneficiary countries should be considerably improved and involve all relevant Directorates General;

- more priority should be given to carrying out evaluations (paragraph 5.85)

**Commission's response:**

The recommended action has been taken.

- A systematic effort is made to ensure adequate complementarity with BWI programmes; in this context regular consultations of BWI by ECFIN and AIDCO are organised;

- DG ECFIN is implementing systematic ex-ante evaluation for each MFA operation to assess the residual financial needs of the beneficiary countries. Complementarity aspects with BWI programmes now become systematically part of this ex-ante evaluation analysis.

- Within the limits resulting from the specificity of the various instruments and the different legal bases, the Commission agrees with the need for developing more harmonised approaches between MFA and SAF. In this regard a manual defining harmonised guidelines for budget assistance to third countries is being prepared;

- In the context of an ad hoc inter-service group, ways to enhance co-operation between DGs directly concerned are being looked into;

- The Commission now ensures, in all cases, that reasons for granting waivers are adequately documented; (mission reports in the beneficiary country, analysis of the conditionalities included in the MoU, results of the consultation of the EFC);

- A first draft of the Vademecum on MFA including a description of the financial circuit in DG ECFIN and the others services of the Commission is available and will be finalised shortly.

- A four year framework contract to assist in the implementation of operational assessments aiming at checking the soundness of financial circuits and controls pertaining to MFA in beneficiary countries was awarded to Deloitte in December 2003. Operational missions will start shortly;

- Correction of the weaknesses detected in these operational assessments could be included as conditions or monitoring items in the different MoUs;

- The results of the operational assessments will also be communicated to RELEX and AIDCO;

- Provisions on fraud prevention are now included in each proposal of the Commission for Council decision;

- Each MoU granting MFA now contains an audit and recovery clause;
• The results of these exercises will also be discussed in due course with BWI in the context of programmes addressing weaknesses in financial management in the recipient countries.

• A greater focus on evaluation is already a part of the general reform. Evaluations of selected MFA programmes are planned to take place from 2003 onwards, and all SAFs approved since 2000 include financial provision for a final independent evaluation (paragraph 5.85);

• Following a call for tender launched in 2003, an ex-post evaluation will start with respect to MFA for Armenia in the first quarter of 2004 with the assistance of a specialised firm;

• A call for tender will be launched in 2004 for selecting a consultant who will be required to carry out ex-post evaluations for other MFA programmes in the context of a three year framework contract;

• The final reports of these evaluations will also be communicated to RELEX and AIDCO.

Delegations should be allowed sufficient time for giving their opinion on proposals made by NGOs. The Commission should also examine alternative procedures to shorten the time between the NGO's submission of proposals and the signing of the contracts. (paragraph 5.78)

**Commission's response:**

*The Commission is taking the recommended action.*

The Commission welcomes the Court's comments on the actions taken. The consultation process will involve delegations, and sufficient time will be allowed for them to comment (paragraph 5.78).

The Commission should consider having a greater part of the assessment work carried out by the Delegations on the basis of clear instructions and guidance from the central services, subject to subsequent monitoring. (paragraph 5.75)

**Commission's response:**

*The Commission is taking the recommended action.*

The existing procedures foresee an active involvement of delegations in the assessment of proposals, and the Commission will ensure that proposals are received in due time for them to be assessed.

An information and management system containing data on experts and contractors should be developed (paragraph 5.67). (paragraph 5.67)

**Commission's response:**

*The Commission is taking the recommended action.*
Data on contractors and individual experts are already recorded in a CRIS special file called "Opérateurs". AIDCO intends to continue to register contractors and individual experts in this file, because information on companies or individuals is often needed even if a contract should not be signed (i.e. companies which apply to a call for tender). In order to comply with the modernization of the Commission accounting system, the EuropeAid local information system (CRIS) will use an interface to transfer data from "Opérateurs" to ICON-DB. It is obvious that EuropeAid intends to adapt its local systems to the requirement of the ABAC project.
Enlargement

48. When the Commission monitors compliance with the conditions for decentralised management, it should ensure that the shortcomings identified by the Court are sufficiently covered. The Commission should also review that the items mentioned in its own audit reports are rectified (paragraph 6.31)

Commission's response:

The recommended action has been taken.

The recommended action has been taken. After publication of the 2001 annual report of the Court of Auditors, the Commission emphasised to the applicant countries that the Court’s recommendations had to be implemented. Moreover, a programme of systematic compliance audits was launched in September 2003. This covers both the recommendations of the Court and those made previously by the Commission.

The Commission responded also to the shortcomings identified by the court with a series of actions aimed to facilitate program implementation and to give guidance and to assist the staff in the Candidate countries (i.e. modification of COM REG 2759/99 concerning the scope of the training measure, help in the preparation of the Monitoring Committees, invitation to bring forward any suggestion to ease the implementation of the Sapard Programme, response to numerous requests from parties interested in any aspects of SAPARD, advice on financial management...).

The competence of the staff assigned to managing the Sapard programme is also evaluated during both ex-ante and ex-post audit missions, through interviews, training of staff, collection of CVs and job descriptions.
49. The way in which the satellite bodies' financial statements are presented should be harmonised. The presentation should also take account of the special nature of the satellite bodies in order to highlight their economic outturn more. (paragraph 7.26)

Commission's response:

The Commission is taking the recommended action.

The Financial Regulation applicable from 1 January 2003 has extended the scope of consolidation to include "bodies set up by the Communities and having a legal personality which actually receive grants charged to the budget" and stipulates that they must apply the same accounting rules as the institutions so that their accounts can be consolidated with those of the Commission for the 2005 financial year at the latest in accordance with the transitory provisions of the regulation. To that end, the Commission's accounting officer will adopt the accounting rules and methods and the harmonised accounting plan to be followed by all the institutions, agencies and satellite bodies. Harmonisation of the way in which financial statements are presented will thus be achieved.

As part of this process, there has been a two day meeting held in Brussels in October 2002 between the Commission and representatives of the bodies explaining the modernisation of the accounting system project followed up by a second meeting in Lisbon in Spring 2003 outlining the advantages of the accounting reform. The most recent meeting, which provided an update to these bodies on the status of the project, was held in December 2003. These meetings allow the bodies to put forward their needs and issues with regard to the requirements of the Financial Regulation.

Additionally, these bodies have a direct input to the modernisation project by having two representatives on the Accounting Standards Committee.

50. The efforts already made to achieve greater uniformity in the presentation of the Schools' accounts should be continued with a view to making their consolidation less difficult. The Schools' accounting plan fails to provide for any fixed-assets accounts and the property which is supposed to be entered on the inventory is not recorded in the general accounts: the fixed assets are not entered in the individual balance sheets of the Schools or of the Office of the Representative of the Board of Governors. In its report concerning the 2000 financial year, shortcomings in the inventory-keeping were highlighted. (paragraph 7.34)

Commission's response:

The Commission is taking the recommended action.

Following the Court's observations, progress has been made in the harmonisation of the presentation of the schools' accounts. Nevertheless, greater care will be taken in the classification of assets in the budget and ex-budget accounts on the balance sheet.
Also as a result of the Court's observations, the Office asked the schools to take fixed assets into account in their balance sheets. In principle this recommendation has been taken up by all the schools.

At the various meetings of the Boards of Governors, the Commission always asks about the situation as regards the inventory and encourages the schools to take action. In fact, most of the European Schools are now complying with the Court’s wishes, and the Commission will continue to encourage them to do so.
Since there are no precise targets to be achieved, it is particularly important that reports on the implementation of the facility and on employment and job creation are reliable, that the relevant figures are accurate and that the facility is coherent with others managed by the EIF and running parallel to it.

The information on commitments and draw-downs made by the EIF for investments in venture-capital funds is available for the full year 'n' during the first quarter of the following year ('n+1). On the other hand, information on employment from SMEs concerning year 'n' is transmitted to the Commission through the venture-capital funds and the EIF in the third quarter. The Commission considers that it is reasonable to keep the existing deadlines, rather than to oblige SMEs to either change their financial reporting cycle or send a report in two parts. The Court notes that the budgetary authority is not informed about the development of the scheme before budgetary decisions are made in year 'n+1'. (paragraphs 8.14/8.15)

**Commission's response:**

*The recommended action has been taken.*

Like the Court, the Commission and EIF attach great importance to the reliability of figures provided regarding the implementation of the facility. Figures regarding commitments, contract signature, draw downs and repayments are verified by the EIF and monitored by the Commission.

The Commission considers that the collection and analysis of statistical data including employment is best addressed in the context of evaluation. In accordance with the Council Decision, an ex post evaluation has been carried out.

To further speed up reporting of statistical data, the Commission services have taken the following measures:

Regarding ETF Start-up, from 2002 onwards, EIF will provide information on employment as at 30 June of year “n”. This requirement will be percolated down to newly approved venture-capital funds in a side-letter.

Regarding the SME Guarantee Facility (loan guarantees), information on the number of employees and expected number of employees in one and two years, will be provided by EIF at 31 October of year “n”, based on data as at 30 June of year “n”, as reported by intermediaries at the time of inclusion.

Until the new fiduciary and management agreement entered into force the EIF provided information on commitments and draw downs twice a year. Under the new framework agreement the information will be provided four times a year (paragraphs 8.14/8.15).

Regarding reporting by the Commission to European Parliament, it should be noted that since the last quarter of 2001 and during the full commitment period, the Commission services provide quarterly reports to the Rapporteur of European Parliament. These reports are provided in addition to the reports to the budgetary
The responsible Commission services consider that with these actions, the Court’s recommendations have been addressed.

52. The Court is aware of the difficulties inherent in the implementation of the schemes audited. The Court recognises that a fair balance has to be struck between potentially profitable uses for the funds and requirements owing to the character of these funds as public money intended to be used for public interest objectives. Nevertheless, the Court recalls that difficulties remain in establishing the ETF Start-up and to a lesser extent establishing the SME Guarantee facility equitably throughout the Community.

In accordance with the above the Court recommends that the Commission and the EIF should study the way to find remedies for the weakness observed by the Court in the speed and the extension of the schemes’ implementation. (paragraphs 8.31/8.32)

Commission’s response:

The recommended action has been taken.

The SME Guarantee Facility has established itself as an effective instrument reaching a sizeable population of SMEs active in a wide range of different activities.

The differences in the take up of the Facilities were identified by the Commission at an early stage and largely taken into account in defining the framework for implementation of the MAP (Multi annual programme for enterprise and entrepreneurship). The new MAP proposes modifications and extensions of the ETF Start up Facility and the SME Guarantee Facility and introduces a new action, the Seed Capital Action. All three actions are to be managed by the EIF and aim to address recognised market failures in order to improve SMEs' access to finance (paragraphs 8.30/8.31).

Based on the experience gained under the Growth and Employment Initiative, it was recognised that it would be more appropriate for the EIF to seek a balanced global geographical distribution for all the financial instruments managed by the EIF in the context of MAP.

The contract with EIF was updated accordingly and geographical distribution guidelines have been included in the restated fiduciary and management agreement. These guidelines set out that EIF will seek to achieve a global geographic distribution among Member States of the amounts available under the financial instruments financed by the Community budget (ETF Start-up Facility, SME Guarantee Facility and Seed Capital Action), taking into account, in no specific order of priority, the following 4 criteria:

– the aim to achieve a balanced global country coverage for the three financial instruments taken together;

– the aim to allow each Member State to benefit from at least one financial instrument;
– the minimum size necessary for a specific operation to be viable;
– the characteristics of the different markets.
For several years the Commission has been developing a new accounting framework which complies with the principles of accruals-based accounting. Nevertheless, the new Financial Regulation states that the reformed accounting system will only gradually be brought in and that it will not be fully operational until the financial year 2005. A draft action plan was submitted in June 2001. By the end of May 2002, no start had been made on implementing this action plan, which has remained at the draft stage. The deadline for adopting the new Financial Regulation is not justification for these delays in implementation. In short, the provisions of the Financial Regulation will not be sufficient, in themselves, to make up for the present shortcomings in the accounting system and a good many practical measures need to be taken (paragraph 9.8)

Commission's response:

The Commission is taking the recommended action.

In its Communication of 17 December 2002 the Commission adopted an action plan for the modernisation of the European Communities’ accounting system. This plan is designed as a follow-up to the provisions of the Financial Regulation adopted in June 2002. It states that the reformed accounting system is to be completely in accordance with accrual-based accounting principles and will be applied gradually and, will only be fully effective in the 2005 financial year. To meet this goal there are two key areas: the adoption of a new accounting framework and the development of the information systems required for its implementation.

Work on the project began in 2003 with the allocation of specific resources, including staff and external consultants to the task. Two committees have been set up under this plan during the first quarter of 2003 (a project oversight board and an advisory committee for accounting standards). The Accounting Standard Committee meets each month and to date 18 standards have been presented to and discussed by this committee.

The preparation of the Accounting Manual is in progress and planned to be completed in 2004.

The Commission will continue to regularly inform the Discharge Authority and the European Court of Auditors of the progress made in this exercise as was done in 2003 when the Commissioner in charge of the Budget presented an update to the COCOBU in July.

As at 31 December 2001, the total shown in the balance sheet under sundry debtors for the amounts held by financial intermediaries (980 million euro, including 73 million euro of interest) comes from a non-accounting record. The procedure that is followed does not enable the Commission to demonstrate the justification for the sums thus entered in the accounts. Consequently, the declarations by the Directors-General of the Enlargement DG and the EuropeAid Cooperation Office include reservations concerning the reliability of the estimates in their fields which amount to 685 million euro. (paragraph 9.25)
Commission's response:

The Commission is taking the recommended action.

As the Court has pointed out previously, non accounting records are inherent to the Commission's current accounting system and are necessary for drawing up the annual accounts.

From the changeover to accrual accounting onwards, the use of non-accounting records will be minimal as the New Financial Regulation requires that prefinancing payments be identified.

It is also noted that the financial statements received from the national authorities are certified by them, and are accompanied by extracts from the bank accounts.

In the framework of the modernisation project for the accounting systems, an accounting standard for prefinancing payments has been prepared. The improvements to the IT systems will allow for the correct bookkeeping and clearing of the prefinancing payments. Prefinancing amounts will be able to be followed up in the central accounting system in 2005.

A provision of 564 million euro for risks and liabilities was entered in the consolidated balance sheet as at 31 December 2001 to cover the cost of dismantling the JRC's installations, the activities of which have ceased (374 million euro) or are still in progress (190 million euro). Apart from the fact that the cost of deploying the JRC's own staff (estimated at between 75 and 100 million euro) was not included in this provision, the amount of the provision is the result of an internal evaluation by the JRC. Until the technical evaluation on which it is based has been the subject of an independent examination involving consultation of the parties involved, its probative value will remain limited. (paragraph 9.31)

Commission's response:

The recommended action has been taken.

The external evaluation announced in 2001 has taken place and the recommendations of the experts introduced in a project of communication to the Parliament and the Council on the Decommissioning and Waste Management Program (launched in Inter-Services Consultation the 19 December 2003).

The value of the provision recommended for 2002 was 1,114.392 Mio€ and takes into account the staff expenditure necessary for this activity.

Commitments against differentiated appropriations still outstanding at 31 December 2001 totalled 86 760 million euro. Of these, commitments still outstanding for more than two years accounted for 28 840 million euro, of which 9,790 million euro had not been the subject of any payment during the last two years. Of the latter amount, the Court considers that some 1 318.2 million euro (13%) no longer represent an obligation to make payments (paragraph 9.32)
The Commission is taking the recommended action.

During the period mentioned by the Court, the Commission paid some 147 million against these outstanding commitments; a further 745 million in commitments were examined, but the Commission departments considered that they should remain open for various reasons: contract still valid, awaiting final report, legal dispute ongoing, etc. At the end of April 2002, the Commission had reviewed one quarter of all the commitments to be examined. The rate of examination was accelerated by the end of 2002. The Action Plan aims at examining all potentially abnormal RAL by the end of 2003 and the results will be reported to the Budgetary Authority in May 2004.

The total of the consolidated balance sheet for the financial year 2001 shows an increase of 76% compared with the total for the previous financial year. This increase is mainly due to a change in the accounting policy applied by the Commission in respect of pension rights. This change in method comes in the wake of an observation by the Court, asking for the annual liability representing the rights acquired during the financial year to be deducted from the economic result. However, the Commission does not record this expenditure, as it has entered the total amount of the potential debt for pensions in the financial statements for a single financial year and, in compensation, has entered revenue for the same amount, thus neutralising the impact on the economic result. In so doing, it is not complying with the Court's request. At the time, moreover, the Commission considered that a thorough accounting analysis was required. The Court is consequently of the opinion that it would be useful for the Commission to continue its analysis of the way in which the pensions scheme is treated in the accounts, bearing in mind the Community context.

The Commission is taking the recommended action.

For several years now, the Commission has been supplying detailed information on pension rights in the annex to the annual accounts (in the off balance sheet commitments). A major step forward was made in the 2001 accounts, when the provisions for pension rights were entered for the first time as liabilities in the accounts.

A new accounting standard for pensions is currently being prepared as part of the modernisation of the accounting systems project. This will be discussed by the Accounting Standards Committee. The Commission feels that it would be more appropriate to deal with this issue in the accounts when the standard has been adopted to avoid making numerous changes in the meantime.

The calculation of pension rights, the Commission employs an expert to carry out a full actuarial study every five years. Besides this five-yearly analysis, the figures are adjusted every year, using the method suggested by the expert, on the basis of changes in interest rates.
Following independent expert advice received the Commission is awaiting the results of the latest valuation (early 2004) to verify if the simplified approach used in calculating the changes in the provision is appropriate.

The first draft of the new accounting standard for pensions has been presented to the Accounting Standards Committee.

The interest yielded by the advances and payments on account is not always notified to the Commission by the financial intermediaries. Where it is notified, it is not always recorded as budgetary revenue. At 31 December 2001, interest on the funds held by the financial intermediaries known at central level (see paragraph 9.25) amounted to 73 million euro, of which only 28 million euro were recorded as budgetary revenue. When the sums received in this way are allocated to measures or programmes, they are not automatically recorded as budgetary expenditure. It follows from this that the accounts do not reflect the whole of the Community contribution (paragraph 9.27).

Commission's response:

The Commission is taking the recommended action.

The Commission will ensure that such interest is entered in the accounts on a regular basis and will regularise the past situation.

The new Financial Regulation requires that estimates of amounts receivable be drawn up when prefinancing payments are made and that interest yielded by funds which remain the property of the European Communities be entered in the budget as miscellaneous revenue.

Furthermore, the implementing rules for the Financial Regulation, applicable since 1 January 2003, specify exactly the scope of the pre-financing amounts that remain the property of the Communities.

Additionally an accounting standard concerning prefinancing has been prepared and discussed by the Accounting Standards Committee.

The declarations of the Directors-General and the Commission's summary report are spontaneous expressions of opinion which the external auditor (the Court) cannot disregard in the context of its Statement of Assurance. However, the dates set by the Commission for submitting these declarations are incompatible with the timetable for the Annual Report laid down by the Financial Regulation. The reports of the Directors-General are the basis for the Summary report which the Commission sends to the European Parliament, the Council and the Court (see paragraphs 9.9-9.100) at the end of July, despite the fact that, according to Article 88(1) of the Financial Regulation, the Court is required to send the observations likely to be included in its Annual Report to the Commission by 15 July at the latest.

This timetable therefore does not enable the Court to make a detailed examination under proper conditions of the declarations and reports submitted both by the authorising officers and by the Commission itself. The deadline set by the Charter for authorising officers by delegation for the submission of annual reports (15 March) would be much more suitable. The alterations to the timetable provided for by the
new Financial Regulation make it even more necessary for the Commission to review the deadlines for the submission of the declarations and annual reports by its departments (paragraph 9.54, paragraph 9.55)

**Commission's response:**

The recommended action has been taken.

On 21 January 2003, the Commission adopted the ABM communication (COM(2003) 28), which also covers the preparation of the Annual Report and provides the services with new guidelines on the declaration of the authorising officer by delegation (AOD) and, the concept of reservation, the hand-over between Directors-General and the question of the cross-delegations.

However, some elements have evolved following notably the New Financial regulation (NFR) and the 2002 Synthesis (COM (2003) 391). Due to this, the "Circular on the annual activity reports for year 2003" (SEC (2003) 1469) pays special attention to the CALENDAR which has been adjusted to meet the new constraints set in the NFR.

Following art 60.7 of the NFR, the Commission shall no later than 15 June each year send to the budgetary authority a summary of the annual reports for the previous year prepared by the AODs. To be able to prepare the mentioned summary, the individual annual activity reports approved by the AODs will be communicated to the Secretariat General and the responsible Commissioner, with copy to DG ADMIN, DG BUDG and the Internal Audit Service, by not later than Wednesday 31 March 2004.

The deadline for Action 96 of the White Paper on more effective management of the recovery of unduly paid funds (see paragraph 9.26) was set for July 2000. In December 2000 the Commission adopted a communication laying down the principles for a reform of its procedures and an action plan for this purpose consisting of operational decentralisation and greater support for its Legal Service. In the wake of administrative difficulties, the deadline was deferred until 30 June 2002 (paragraph 9.67)

**Commission's response:**

The Commission is taking the recommended action.

With a view to a more effective management of the recoveries, the Commission has adopted two communications aiming to implement action 96 of the White Paper. The first communication has been adopted on 3 December 2000 and redefines the roles of the actors (authorising officer, accounting officer, legal service and Olaf) and the second communication, adopted on 3 December 2002 (COM(2002) 671 final) has taken stock of the improvements put in place in the field of the regulatory framework, the organisational structure and the IT System.

**Regulatory Framework:**

- Guidelines on the application of the principle of proportionality to the waiving of debts recovery of 21 November 2001;
- Financial Regulation applicable to the general budget of the European Communities of 25 June 2002;

- Commission Regulation of 23 December 2002 laying down detailed rules for the implementation of the Financial Regulation applicable to the general budget of the European Communities;

- Internal Procedure provisions of 17 December 2002 for the recovery of entitlements arising from direct management and the recovery of fines, lump sums and penalty payments under the Treaties.

The new framework has introduced two important tools for the recovery: a systematic offsetting of debts and claims and a broad application of Article 256 of the EC Treaty ("titre exécutoire").

**Organisational improvements:**

- DG Budget has reinforced the number of staff directly allocated to recovery and created a separate unit within directorate C (Unit C5). The necessary organisational framework has been put in place for the systematic claiming of late-payment interest. With regard to offsetting, a new sector dealing exclusively with the technical process has been set up within unit C3.

- OLAF has created a new unit (A5) dealing with the financial and recovery aspects of its audits.

- The Legal Service has set up a new sector dealing with enforcement proceedings at a central level.

**IT Systems:**

- Some major improvements of the existing informatics tools, notably with regard to more reliable reports on outstanding recovery orders, have been realised.

- As from the budget year 2003, the necessary modifications to the IT System for the decentralisation of debit note processing have been implemented. Debit notes are now printed, signed and sent to debtors by the authorising officers according to the Financial Regulation.

- A new computerized system of dunning is to be implemented as part of the modernisation of the accountancy of the Commission.

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61. ECIP (European Community Investment Partners) is a financial instrument created during the 1980s to support joint ventures founded by companies established within the Community and companies in developing countries (ACP, Latin America and Asia). The Court considers that the Commission's accounts do not give a true picture of this instrument's situation for the following reasons (paragraph 9.20)

**Commission's response:**

The Commission is taking the recommended action.
The Commission has made progress in the field of accounting and reporting, although some problems are still to be ironed out.

Between 1988 and 1999, the Commission granted within the framework of ECIP, 1365 interest-free advances under conditions for an amount of 139.3 M€. During the same period, the Commission contributed to the investment funds of financial institutions. The regulation ECIP stipulated that, except in exceptional situations, these financial institutions had to use these funds to intervene directly and in their own name in the capital of companies of the ALA/MED/SA area. These amounted to more than 150 operations and almost €33 M. In both cases, these amounts were carried on the balance sheet of the Commission.

However, for these two cases, the Commission has continued a detailed examination of the contracts in order to establish if these actions have to be maintained under these headings of the balance sheet or have they, on the contrary, to be shown under the prefinancing heading of the accounts, to foresee in compliance with the modernisation of the accounting system and the scheduled calendar.

With regard to the general situation of the interest-free advances (under condition), the files of 665 actions having benefited from a total of €71.5M of advances, were examined by a steering committee. Following this examination, it was decided that: (1) €49.6M of advances for 624, actions the conditions for a regularisation in payment were met. The remainder should be refunded. In 2004, the Commission departments will give priority to the administrative and financial closure of these 624 files. The remaining files (almost 700) will be examined as from 2005.

The programme cannot be definitively wound up until the last joint venture has been completed.

62. In 2000 the Commission opened three bank accounts with the Central Bank of Jordan. These accounts were intended to meet the needs of three MEDA programmes. The funds paid into these accounts were regarded as expenditure by the authorising department concerned at the Commission. On 31 December 2001, the deposits on these accounts totalled 639 927 euro. Apart from the fact that these amounts had been classed, in advance, as the equivalent of budgetary expenditure, they were not shown under disposable assets on the Commission's balance sheet as the accounting officer was not aware the accounts had been opened. Such practices are contrary to the most elementary principles of internal control and the Commission should forbid them from being used by its authorising officers by subdelegation (paragraph 9.29)
Commission's response:

The recommended action has been taken.

With regard to the three bank accounts mentioned by the CoA, they were closed in 2002 and the "Third Party" references blocked in SINCOM2. A circular note dated 15 January 2002 was sent to all Directorate-generals reminding them of the rules for the opening of bank accounts. The replies from banks to the letters sent at the end of each year asking for information on Commission bank accounts are compared carefully with the Commission records in order to detect any anomalies.
European Development Fund (EDF)

63. The Court has repeatedly called on the Commission to present the EDF accounts in a form that is more consistent with accounting principles. The Commission included a consolidated balance sheet for the sixth, seventh and eighth EDFs in the EDF balance sheet for 2001. However, the presentation of the consolidated balance sheet and the balance sheets of the various EDFs was not sufficiently harmonised and the information value of the accounts was still inadequate (see paragraphs 19 to 21). The Court considers that further improvements should be made in the presentation of the EDF accounts. Moreover, the accounts should be published in the Official Journal, which would comply better with Community practice as regards financial information (paragraph 5)

Commission's response:

The Commission is taking the recommended action.

Significant efforts were made to make improvements in the presentation of the consolidated Balance Sheet for 2002. It considers that the presentation is now clearer and as such, provides more useful information. Nevertheless the Commission recognises that further improvements can, and should be made.

In particular, the Commission intends to consult the Court of Auditors on the presentation of future sets of accounts, in accordance with the provisions of Article 103 of the Financial Regulation of the 9th EDF. Any feedback received in the course of this exercise will be incorporated into the published accounts, where it is feasible to do so.

In accordance with the provisions of the same Article (103) of the 9th EDF Financial Regulation, the EDF accounts will in future be published in the Official Journal, thus complying with the Court of Auditors recommendation. Such publication will take place before 30 November 2004 in respect of the 2003 Financial Statements.

64. In support of the EDF financial statements for the financial year 2001, the Commission also provided an analysis of their financial management. This document is more detailed than the one for the financial year 2000 whose inadequacies the Court had pointed out in its previous Annual Report. However, there is still room for improvement, in particular with regard to the explanation of the slow implementation of the EDFs. The Commission should therefore show and comment on the cumulated implementation rates of the various EDFs. It should also analyse thoroughly the causes of under-implementation instead of mentioning them briefly whilst announcing the improvements that it expects to achieve via decentralisation (paragraph 6)

Commission's response:

The Commission is taking the recommended action.

The Commission prepared a separate Report on the financial management of the EDF in respect of the Financial Year 2002. This Report was appended to the
Financial Statements and communicated to the Council, Parliament and the Court of Auditors.

The 2002 Report contains some analysis on the factors affecting the accumulated implementation rate of the different EDFs, the Court's comments were noted and this ‘implementation’ analysis has been and continues to be improved in subsequent reporting periods. This process has been substantially aided by the establishment of annual regional seminars covering all ACP delegations in which each partner country’s implementation and financial performance is analysed.

65. In order to avoid the implementation delays that affected the previous EDFs, the Commission has started adapting certain accompanying texts that would be necessary for the implementation of the agreement when it enters into force. One of these regards the rules for contracts. It has still not presented the proposal for a Financial Regulation and could therefore put the legislative authority in the difficult position of having to adopt this text as soon as possible before the entry into force of the Cotonou agreement. Generally, the Commission should look into the possibility of setting up a legislative support framework so as to avoid transition problems when it introduces new EDFs.

The Court recognises that development aid policy involves constraints that are likely to make implementation slow. It therefore asks the Commission to show more realism in establishing its forecasts so as not to give rise to unjustified expectations. At the same time, it asks the Commission to give more emphasis to reforms aimed at limiting this slowness, so that the eighth and the ninth EDFs do not suffer from the same excessive implementation delays found for the previous EDFs. (paragraphs 16 and 17)

Commission's response:

The Commission is taking the recommended action.

The Commission presented a proposal on 11 June 2002 for the new (9th) EDF Financial Regulation. This came into force on the 2nd April 2003, the same date as the entry into force of the Cotonou Agreement as requested by the Court of Auditors. In addition the Commission presented a proposal in October 2003 for the budgetisation of the EDF which would entirely remove delays caused to EDF transition problems for the future.

The Commission has taken concrete steps to introduce new IT based forecasting tools under the auspices of the Common Relex Information System which is planned for full implementation in 2004. This action has been supported by substantial structural change and new procedures in relation to planning and financial forecasting responsibilities by ACP delegations. The subsequent forecasts for 2002 and 2003 have been proved to be highly accurate.

The Commission has given significant priority in the Reforms announced in May 2000 to the acceleration of implementation. In particular, the devolution process - which should be completed for all ACP countries in 2004 – should have a significant impact on the rapidity and quality of payments. In addition, given that implementation of programmable aid will always be influenced by the capacities of
Precise guidelines should be drawn up and they should be applied in a uniform way. They should be based on the best practice observed in the many audits already carried out. In particular, the terms of reference of the audit contracts should include:

- details of the checks to be carried out on the various types of expenditure, including the search for infringements of tender rules, over-invoicing and purchases at higher than market prices;

- the establishment of the main cases of ineligibility for EDF financing;

- rules for the presentation of the summary audit reports, envisaging the quantification of the coverage of the audit and the cases of ineligibility found as well as a detailed account of the expenditure audited, together with an indication of whether the expenditure has been accepted or rejected or is doubtful.

Therefore, the current audit mechanism does not yet make it possible to ensure that Community financing is verified in an appropriate and uniform way. The Commission should improve its system by specifying the nature of the audit work to be carried out and the structure and contents of the audit reports more clearly in the financing agreements and the terms of reference. It should improve their actual implementation and its analysis and monitoring of the necessary corrective action. (paragraph 26, paragraph 30)

**Commission's response:**

The Commission is taking the recommended action.

The Commission continues its efforts for the creation and the improvement of its audit systems and significant progress has been made particularly as far as the provision of standard documentation is concerned relating to the preparation, execution and reporting on audits carried out under the direct supervision of headquarters and delegations.

Most of these audits are carried out by external audit firms under two operational framework contracts that are operational since 2002 and 2003 respectively. This documentation is available on dedicated WebPages on the EuropeAid Intranet and should be considered as being part of the methodological framework for audits. The development of such a methodological framework is an ongoing task.

As the majority of audits are mandatory by financial agreements or contracts, carried out on request of the beneficiary, standardisation and improvement can be achieved by including or modifying audit related dispositions in those legal documents. For certain contract types these rules have been improved in 2002.

Whilst as from 2003 audits carried out under the direct supervision of headquarters and delegations are registered in CRIS AUDIT, this system is not yet available to accommodate data on audits on request of beneficiaries (so called certification-audits). This function will become operational during the current exercise.
In December 2001 a budget of 9 million euro for the 2002-2004 period was allocated to ad hoc projects (meetings, seminars, workshops and studies) involving expenditure that is, by its nature, difficult to distinguish from the expenditure relating to the ACP Secretariat's normal operations.

The Court recommends that the Commission prevent this budget being used to finance activities that are covered by the flat-rate operating subsidy paid to the ACP Secretariat. In addition, the Court recommends that the Commission reduce, as far as possible, the advances earmarked for these ad hoc projects, so that the Secretariat is not provided with funds in excess of its requirements. The reduction in its cash resources should encourage the ACP Secretariat to practise more rigorous management (paragraph 46/47)

**Commission's response:**

*The recommended action has been taken.*

1) All the Ad Hoc Projects implemented by the ACP Secretariat have been gathered under a single Financing Agreement and a yearly programming of the activities is ensured by means of regular work programmes; technical and financial reporting of the yearly activities are requested in order to allow financing of subsequent work programmes;

2) All costs related to the statutory activities of the ACP Secretariat (i.e. participation to missions of the ACP Secretariat's staff, etc.) are duly financed within the Financing Agreement for the Functioning of the ACP Secretariat. No such costs are budgeted or incurred under the FA for the Ad Hoc Projects;

3) The percentage of the first advance payments of both the Ad Hoc Projects and the Functioning of the ACP Secretariat have been reduced from 80% to no more than 50%;
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68. At the end of the financial year, dormant commitments had been cancelled to the tune of 58 million euro. These cancellations regarded rehabilitation aid and social measures (23.2 million and 15.5 million euro respectively), interest rebates (10.3 million euro) and research (9.1 million euro). It should be noted that, in 2001, the Commission cancelled amounts that it should have cancelled during previous financial years. In view of the liquidation of the ECSC on 23 July 2002, the Court suggests that the Commission should carry out a special examination of all the commitments that are still open and cancel those that it can assume will not to be used in the future (paragraph 13)

Commission's response:

The Commission is taking the recommended action.

The Commission shares the Court's concern regarding cancellations of dormant commitments and regularly examines commitments that are still open with a view to cancelling them where necessary, as shown by the relatively high level of cancellations in 2001. Since the expiry of the Treaty in 2002 the balance of outstanding commitments has continued to drop.

Caution is nevertheless required since cancellations cannot be reversed. As regards interest rebates, a minimum level of appropriations needs to be maintained in case a sub borrower were to supply additional documentation proving entitlement to the late payment of a rebate.

69. The Commission (DG Personnel and Administration) is required to draw up an annual report concerning the situation of loans to officials, which amounted to 34.8 million euro at the end of 2001. Until 1987, this report was forwarded to the Council. Since then, it has only been sent to the various Commission departments. The most recent report available relates to the period 1994 to 1995. In reply to the Court's report concerning the financial year 2001, the Commission committed itself to drawing up the missing reports by the end of 2001. It did not comply with this commitment. (paragraph 14)

Commission's response:

The recommended action has been taken.

An internal auditor was appointed in February 2002 who analysed the files of 1996 to 2002. The final audit report was submitted to the Commission by the end of 2002 and approved by Commission Decision E/396/2003 of 24 March 2003.

70. Up until July 1999, the Commission's departments used a certain database for the management of loans to officials. Following various problems, it exported the data to another database without validating them. The Commission only started the task of validating the data for the financial years after 1999 at the beginning of February 2002. Furthermore, there is a gap of two to three months between DG ADMIN's data (the personnel and administration Directorate-General) and the data held by DG ECFIN (the economic and financial affairs Directorate-General), which is
responsible for drawing up the ECSC's monthly and annual balance sheets. The Court notes with concern the weaknesses found in the management of these loans and recommends that urgent steps should be taken to restore sound management. (paragraph 15)

**Commission's response:**

The recommended action has been taken.

On 1 January 2003, the management of construction loans to officials was transferred to PMO.