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III

(Preparatory acts)

COURT OF AUDITORS

OPINION No 6/2010

(pursuant to Article 322 TFEU)

on a proposal for a regulation of the European Parliament and of the Council on the Financial Regulation applicable to the general budget of the European Union

(2010/C 334/01)

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THE COURT OF AUDITORS OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 322 thereof, in conjunction with the Treaty establishing the European Atomic Energy Community, and in particular Article 106a thereof,

Having regard to the proposal for a Regulation⁽¹⁾ of the European Parliament and of the Council on the Financial Regulation applicable to the general budget of the European Union⁽²⁾ (hereinafter 'the Financial Regulation'),

Having regard to the Council's request for an opinion on the abovementioned draft received at the Court on 3 September 2010 and Parliament's request of 23 June 2010,

HAS ADOPTED THE FOLLOWING OPINION:

Summary

- I. Improving the financial management of the European Union and the arrangements for holding the Commission to account for its management of funds is an important task. Regulation can play a role in this — and the proposed amendments include changes that will assist managers to make sensible decisions: some proposed changes involve significant simplification of procedures. But regulation alone is not enough: the key improvements will be made through the actions of managers in the Commission, the other institutions, and the Member States.
- II. The Commission has described this proposal as going beyond the normal scope of triennial revision. But in practice, the changes proposed are less ambitious than portrayed. For example (paragraph 42), the explanatory memorandum talks of switching the regime of grants from one based on inputs to one based on outputs. In practice, while there are some innovations such as provision for the award of prizes, the proposals fall short of this aspiration.
- III. The Commission's proposal on external assigned revenue is soundly based, but it appears unnecessary to maintain a category of internally assigned revenue (paragraphs 6 to 9).
- IV. The Commission makes proposals on a tolerable risk of error. The Court notes that considerable uncertainty surrounds the definition and application of the concept of tolerable risk; and that the Commission proposal appears to use the concept of tolerable risk solely as a basis for judging what level of irregular payment of funds should be regarded as acceptable *ex post*. The Court suggests that the Parliament and Council consider whether the Financial Regulations should require the Commission to improve its screening of spending proposals at the time they are put forward, and to improve its diagnosis of the causes of error. The Financial Regulation should not seek to restrict the responsibility of the Court to decide on an appropriate level of materiality (paragraphs 10 to 23).
- V. The Commission's proposal on management modes involves a significant requirement for a management declaration on the use of all funds whose management is shared with Member States. However the proposals raise issues of cost, practicality and responsibility which require careful consideration (paragraphs 24 to 36).
- VI. The Court recommends that the Implementing Regulation should take account of earlier comments by the Court in respect of fiduciary accounts (paragraphs 38 to 41).
- VII. The inclusion in the Financial Regulation of a specific legal basis for the use of financial instruments is appropriate. However, the Court notes that the proposed addition to the Financial Regulation does not tackle the issue of ownership. It is not clear whether the Commission expects to record all financial instruments in the balance sheet of the European Union (paragraphs 43 to 47).
- VIII. Substantial parts of the proposals on external audit would constrain the ability of the Court to carry out its Treaty responsibilities effectively. The Court therefore recommends the Parliament and Council to reject the greater part of these proposals (paragraphs 48 to 69).
- IX. The Commission proposes the creation of European trust funds. The Court draws the attention of the Parliament and Council to issues of administration, accountability and audit raised by this proposal (paragraphs 70 to 78).
- X. The provision on the 'light model Financial Regulation' for the proposed special public-private partnership bodies does not explicitly require consultation of the Court. The Court considers that it is important that this document should in no way restrict the capacity of the Court to audit the use of EU funds (paragraphs 79 to 81).

⁽¹⁾ COM(2010) 260 final of 28 May 2010.

⁽²⁾ OJ L 248, 16.9.2002, p. 1.

- XI. The Court recommends further strengthening of the provision on prefinancing, together with management action to reduce an excessive build-up of uncleared items (paragraphs 86 to 89).
- XII. The proposals involve some simplification to the arrangements for preparing and presenting the accounts. The Court recommends that in addition the Commission's commitment to preparing financial statements in accordance with the internationally accepted standards be restated and clarified (paragraphs 90 to 93).
- XIII. The Court recommends clarification of the Commission's proposal for the audit of the agencies in order to maximise the contribution which this proposal might make to overall assurance on the legality and regularity of expenditure (paragraphs 94 to 99).
- XIV. The Court suggests a review of reporting requirements (paragraphs 101 to 102).
- XV. Taken as a whole, the proposals contained in the recast of the Financial Regulation will provide opportunities for the Commission to improve transparency and financial management. Simplification of sectoral legislation remains however an important route to a significant improvement in performance.

Introduction

1. The Commission's proposal (COM(2010) 260 final) contains a large number of detailed proposed changes to the articles of the Financial Regulation. The explanatory memorandum to that proposal summarises the intention and nature of changes to groups of articles. The Court's opinion so far as possible follows the structure of the Commission's explanatory memorandum.

2. This opinion makes reference where necessary to the Commission's text (SEC(2010) 639/2) indicating possible changes to its Regulation implementing the Financial Regulation. It does not attempt to comment on that text as a whole.

3. Improving the financial management of the European Union and the arrangements for holding the Commission to account for its management of funds is an important task. Changes to the Financial Regulation can play a role in this — and the proposed amendments include many desirable changes that will take this process further. But, as the Court has pointed out elsewhere ⁽¹⁾, improving the quality of EU spending requires

⁽¹⁾ See Opinion No 1/2010 – Improving the financial management of the European Union budget: risks and challenges (<http://eca.europa.eu/portal/page/portal/publications/auditreportsandopinions/opinions>). The Court recalls that in this opinion it suggested that the concept of 'European added value' should be articulated in a suitable political declaration or in EU legislation in order to provide guidance to the EU's political authorities to be used when choosing expenditure priorities. The Financial Regulation could constitute such a legislative vehicle.

simplification of, and other improvements to, sectoral legislation together with other steps to support, encourage and require sound action by managers in the Commission, the other institutions, and the Member States. Complex legislation is unlikely to produce the improved performance sought by all EU stakeholders.

4. In a few cases the paragraphs below make detailed suggestions for changes to the Commission's proposals. These are set out in the Annex.

Budgetary principles (Articles 3 to 30)

5. The Commission proposes a number of changes to Title II of the Financial Regulation, dealing with budgetary principles. The Court notes that these changes (notably, steps to simplify provisions on the recovery of interest) are generally intended to simplify and facilitate the operation of the budget while respecting the budgetary principles: with two exceptions (treatment of assigned revenue and tolerable risk of error) it has no detailed comments.

Assigned revenue (Articles 10 and 18)

The Commission's proposal

6. The existing Financial Regulation lists (in Article 18) several types of 'assigned revenue', which are to be used to finance specific items of expenditure. Article 10 of the existing text provides that any such revenue not used should automatically be carried over. The Commission proposes:

— in Article 18 to draw a distinction between 'external assigned revenue' (from Member States, third countries, etc.) and 'internal assigned revenue' from certain categories of transaction (proceeds from the sale of vehicles, equipment, insurance payments, etc.),

— in Article 10 to provide that external assigned revenue will be carried over until fully spent, while internal assigned revenue will be carried over for 1 year.

Analysis

7. The Commission's proposal is reasonable in respect of external assigned revenue. Governments and others who have contributed to, for example, research or aid programmes wish to be able to identify that their funds have been used for the purposes intended.

8. However it appears unnecessary to maintain a category of internal assigned revenue. Internally-generated receipts can be dealt with through the normal budgetary process.

Recommendation

9. The Court recommends the Parliament and Council to adopt the Commission's proposal in respect of external assigned revenue only.

Tolerable risk of error (Article 28b)

The Commission's proposal

10. Article 28b of the Commission's proposal would oblige (and not merely permit) the legislative authority to decide on a level of tolerable risk of error 'at an appropriate aggregation of the budget'. This decision is to be 'taken into account' in the annual discharge procedure. The level of tolerable risk is to be based on an analysis of the costs and benefits of controls. Member States, entities and persons managing EU funds will be required to report to the Commission on the cost of checking EU expenditure borne by them.

11. Recital 27 adds further details:

- tolerable risk will change the way authorising officers will assess risk (thus changing the way they prepare annual activity reports),
- the discharge authorities will take their decision on the basis of tolerable risk,
- the legislative authority should determine tolerable risk 'per policy area', a term normally taken to mean the more than 30 policy areas into which the Commission's section of the budget is divided.

Analysis

12. The Court sets out below observations relating to the purposes, definition, estimation and application of a tolerable level of risk, and to the responsibilities of institutions.

Purpose

13. The Court has previously pointed out (Opinion No 1/2010) that an analysis of the costs and benefits of expenditure programmes and of the likely risks of error could inform examination of the regulatory regime and management structure of the programmes concerned. In other words, the Commission should look at the weaknesses in present systems and analyse the costs and benefits of various possible changes.

Where it is impractical to obtain a high level of compliance with scheme rules, a number of options would appear to be possible. These could include simplifying the scheme rules, redesigning the programme, tightening controls, tolerating a higher level of non-compliance or, if necessary, terminating the activity.

14. The Commission's proposal for Article 28b by contrast seems to use the concept of tolerable risk solely as a basis for deciding what level of irregular use of funds should be regarded as acceptable *ex post*. It does not for example require the Commission to estimate the cost of administrative and control systems, the likely rate of non-compliance, and set out the options for simplification considered when putting forward any new expenditure schemes (for example when considering Union spending programmes from 2014 onwards).

15. At present the Financial Regulation is silent on the Commission's responsibilities when preparing new spending proposals (other than Article 49, covering the need for a basic act). It is for consideration whether the Financial Regulation should require the Commission to estimate likely levels of non-compliance, to undertake an impact assessment, and to assess likely overhead and control costs before putting forward new spending proposals.

Definition and estimation

16. Although the 'level of tolerable risk' is to be defined by the legislative authority in numerical terms, the parameters involved have not been clearly defined. As mentioned above, the units of spending to be covered are, confusingly, defined in more detail in the draft recital than in the draft article. Equally significantly, the draft text does not make it clear whether the risk of error is to be considered in relation to the amount of expenditure claimed as correctly executed by final beneficiaries (a valid measure) or to the volume of disbursement by the Commission (including advance payments, which are of limited relevance in showing whether expenditure has been legal and regular in areas such as shared management or research).

17. It is not clear from the proposal for Article 28b whether 'costs of controls' should be taken to include the costs borne by beneficiaries. It can be argued that they should do so if a level of tolerable risk is to be set by comparing marginal costs and benefits of additional controls, as the Commission envisages in its communications. Nor does the text make explicit that the costs borne by the Commission will be taken into account.

Measuring the level of tolerable risk

18. If the legislative authority were to accept elements of the Commission's proposals, detailed consideration would be needed of how to measure whether the risk of error had indeed been restricted to a tolerable level.

Roles and responsibilities

19. As the Court indicated in its comments on the Commission's 2008 communication 'Towards a common understanding of the concept of tolerable risk of error' (COM(2008) 866), the concept of a tolerable level of error, or risk of error, raises issues which it is for Parliament and Council to debate and decide, both as legislator and in the context of the discharge procedure. The Commission's proposal thus appropriately reflects the distribution of responsibilities among institutions.

20. The definition of the level of materiality, by contrast, is a matter for decision by the external auditor. The Court of Auditors is obliged to define a 'materiality threshold' in accordance with international standards on auditing.

21. These standards require the external auditor to:

- (a) use professional judgement when determining the level of materiality at the planning stage;
- (b) consider not just the aggregate error present but also the nature of the error when deciding whether or not the audit opinion should be modified.

22. The Court notes that if the European Parliament and Council wished to define thresholds for the tolerable risk of error they could do so in 'soft law', for example guidelines, rather than legislation.

Recommendation

23. The Court recommends the European Parliament and the Council to consider the Commission's proposal taking account of the considerations set out above. The conditions under which the discharge authorities grant discharge are a matter for the discharge authorities. The Court however points out that considerable uncertainty surrounds the definition and application of the concept of tolerable risk. The Court suggests that the Parliament and Council consider whether the Financial Regulations should require the Commission to improve its screening of spending proposals at the time they

are put forward, and to improve its diagnosis of the causes of error. The Financial Regulation should not seek to restrict the responsibility of the Court to decide on an appropriate level of materiality.

Methods of implementation and obligations of the Member States (Articles 53 and 53a)**The Commission's proposal**

24. The Commission proposes to reduce the current number of management modes defined in the Financial Regulation to two: direct and indirect. All expenditure whose management is shared with the Member States would be subject to administrative arrangements modelled upon the current arrangements for agriculture.

25. Bodies entrusted by Member States with the responsibility for managing expenditure would be required to ensure that it was subject to an independent external audit and to produce a 'management declaration of assurance' covering the completeness and accuracy of the accounts, the operation of control systems and the regularity of expenditure managed. This declaration, accompanied by the opinion of an independent auditor, would be provided by 1 February (with a synthesis report required by 15 February where more than one body is responsible for making expenditure).

Analysis

26. A standard requirement for a timely declaration from management should usefully improve the timeliness and coherence of financial and management reporting.

27. However the Commission's proposals would not simplify the administrative arrangements. They prompt a number of questions, including:

- the cost of the arrangements required under the legislation,
- how easily the financial systems for agriculture (the model for the proposed Article 53a) can be applied to other expenditure streams,
- whether the proposal is compatible with the Commission's declared objective of moving to a performance-based system of reimbursement, and
- how the Commission would make use of the information generated by the proposed arrangements.

In addition the overall benefit of the proposal has not been spelled out (see paragraphs 35 and 36).

Responsibilities of the Commission and Member States

28. The changes proposed to the Financial Regulation include deletion of the previous definition of the role of the Member States as undertaking 'implementation tasks'. It is essential that the responsibilities of the Commission be clearly set out in relation to shared management⁽¹⁾. This should include fixing deadlines for the activities described in Article 53a(b), and requiring the Commission to adopt a decision recognising the final amount of chargeable expenditure for the financial year.

Applying elsewhere the administrative arrangements for agriculture

29. Agricultural expenditure from the EU budget has over the years tended to be affected by a lower level of error than some other areas of operational expenditure. However differences between agricultural spending and other areas are striking. Beneficiaries of common agricultural policy expenditure typically carry out the required activity, and national authorities perform checks, before payment is made; around 70 % of expenditure is calculated not on the basis of cost reimbursement but on the basis of objective criteria e.g. land eligible for Single Payment Scheme payments.

30. For expenditure in such areas as the Structural Funds, Education and Culture and Justice and Home Affairs, recipients of subsidy are diverse and receive EU contributions to on-going activities which are co-financed from other sources. Payments are made in advance of costs being incurred, and claims are accepted on the basis of declarations that eligible costs have been incurred.

31. Thus the accounting system of the body managing payment will not provide a direct record of the entitlement to payment, but an indirect record of declarations made by other bodies. In addition, the nature of checks on (for example) an infrastructure scheme, a venture capital scheme, and a training scheme may be diverse in timing and in nature.

32. Thus, replicating the administrative arrangements surrounding agricultural payments will not necessarily be easy. Nor can it be assumed that the change proposed will automatically transfer to other parts of the budget the apparent strengths of the current system for dealing with agricultural spending.

⁽¹⁾ Preambular paragraph 39 appears to indicate that there will be no *ex ante* assessment of whether Member States' controls provide a satisfactory level of protection for the financial interests of the Union, though there is a suggestion in Article 53a that the Commission may have an accreditation role.

Cost of the proposals

33. There is no indication of the likely cost of creating the structures outlined in Article 53a. The inclusion of an impact assessment for the proposals would have helped in assessing such costs.

Compatibility with a performance-based system of reimbursement

34. The proposals made in this Article appear to represent a major investment in obtaining more accurate information on reimbursable costs incurred by beneficiaries. While this is desirable if systems of payment are to stay as they are, the introductory memorandum to the Financial Regulation proclaimed a shift towards a 'performance-based system, based on the definition of agreed indicators and objectives'. A different administrative framework might be appropriate if such a system were introduced.

How will the Commission use the information?

35. The Commission's proposal bears a significant resemblance to the ideas set out in the Court's Opinion No 2/2004 on the 'single audit' model (and a proposal for a Community Internal Control Framework). Both include a system of coordinated checks on spending throughout the budget, forming a pyramid, supporting overall assurance at the level of the Commission. While the proposals made in the draft Financial Regulation might contribute to such a 'pyramid of assurance', the Commission's proposal does not show how it will use this information to reach a conclusion that the accounts are accurate, and that all expenditure streams are free from material error.

Recommendation

36. The Court recommends the Parliament and Council to consider the Commission's proposals in the light of the comments set out above. It notes in particular that the proposals conflate issues of institutional architecture and issues of assurance in respect of the reliability of accounting information, the legality and regularity of expenditure, and the risk profile for spending streams. It would, for example, be possible to obtain a management declaration for each expenditure stream without insisting that they each have the same organisational arrangements.

Payments, recovery action and procurement

37. The Court has no comment on the proposals in the draft Financial Regulation.

Fiduciary accounts (Article 61(4))

The Commission's proposal

38. The Commission proposes that fiduciary accounts (under the responsibility of the authorising officer in charge of the implementation of the programme or action in agreement with the accounting officer of the Commission) may be opened in the name of the Commission and on its behalf. These accounts will be managed by an entity listed in Article 53(1) point (2)(c) and (d), including financial institutions entrusted with the implementation of financial instruments, the European Investment Bank (EIB) and European Investment Fund (EIF).

Analysis

39. The Court has previously audited the management of fiduciary accounts by the Commission (e.g. Special Report No 5/2009). The Court concluded, among other things, that no clear rules for setting up fiduciary accounts were established.

40. Fiduciary accounts have already been used by the Commission for many years, when implementing such programmes and actions as venture capital operations or guarantees for SMEs. This new provision would provide the legal basis for opening new fiduciary accounts. It does not require the authorising officer in charge of implementation of the programme or action to obtain agreement from the accounting officer of the Commission for existing fiduciary accounts, nor to establish rules for their use and monitoring.

Recommendation

41. The Court suggests that the Commission take account of the comments made in paragraphs 30 to 32 of the Court's Special Report No 5/2009 when finalising the text of the implementing rules.

Grants and prizes (Articles 108 to 120a)

42. The Commission makes numerous proposals for adapting the system for reimbursing costs (allowing for further use of lump sums, standard unit costs, etc.). However the proposals to amend the Financial Regulation do little to explain how moves will be made to a performance-based system. There is therefore a gap between the aspiration of the explanatory memorandum (which states that an objective is to 'shift the regime of grants from a real-cost based management (inputs) towards a performance-based scheme (outputs), in order to better target policy objectives and achieve significant simplifi-

cation of procedural and documentary requirements for the benefit of beneficiaries, and facilitate the use of lump sums') and the reality of the proposed changes. The proposals for prizes may signal a move away from cost-reimbursement. If the Commission wishes to make significant progress towards a performance-based system of reimbursement it needs to address the point in the implementing rules and/or sectoral legislation.

Financial instruments (Articles 120b and 120c)

The Commission proposal

43. This new Title provides a legislative framework for the use of financial instruments. Under its provisions the Commission may implement financial instruments in the direct management mode or in the indirect management mode, by entrusting tasks to the EIB, EIF or other financial institutions. Previously financial instruments were dealt with as exceptions to the standard arrangements for grants.

Analysis

44. The inclusion in the Financial Regulation of a specific legal basis for the use of financial instruments is appropriate for the reasons explained by the Commission. However, the Court notes that the new guidance provided by the proposed addition to the Financial Regulation does not tackle the issue of ownership: it is not clear whether the Commission expects to record all financial instruments in the balance sheet of the European Union, as it should do according to internationally recognised accounting standards⁽¹⁾ (see also paragraphs 46 and 92).

45. The Court has previously audited the management of the different financial instruments by the Commission and the EIB, EIF and other financial intermediaries (e.g. Special Report No 1/2009, 2008 Annual Report). The Court concluded, among other things, that in some cases the monitoring of the use of the financial instruments by the Commission or by financial intermediaries entrusted with their management was not adequate.

46. The Commission intends to expand its use of financial instruments. It will therefore need to monitor their use and to invest in training staff in managing the associated risks⁽²⁾. It will also need to ensure that staff are aware of the need for transparency (including disclosure in accordance with internationally accepted accounting standards).

⁽¹⁾ Some of the financial instruments mentioned in the Commission's technical fiche on this aspect of its proposals are not in the balance sheet at present.

⁽²⁾ The Court notes that agencies have also used financial instruments.

Recommendation

47. The Court recommends the European Parliament and the Council to seek further clarification from the Commission in respect of the ownership of financial instruments, and how it expects financial instruments to be accounted for and reported in the financial statements of the EU. Furthermore, the Court recommends that the Commission include within the implementing rules appropriate policies for monitoring the use of the financial instruments, including those implemented under indirect management. It should also reinforce the capacity of the Commission's staff to operate relatively complex financial instruments.

External audit (Articles 129, 140, and 143 to 144a)

48. The Commission makes a number of proposals relevant to the Court's Annual Report (Articles 129, 143 and 144a) and special reports (Article 144). The Commission (the Court's principal auditee) did not consult the Court (the Commission's external auditor) before proposing these changes to the arrangements for the Court's audits.

The annual report

The Commission's proposal

49. The Commission proposes (in addition to some reordering of Article 143):

- earlier deadlines for the transmission of any observations likely to appear in the annual report, i.e. draft chapters of the annual report. Instead of 30 June, as at present, the date for transmission would be 15 June for transmission to the Commission and 1 June for transmission to other institutions and bodies (Article 143(1)),

- earlier deadlines for comments on the provisional accounts of institutions other than the Commission, and of other bodies (Article 129(1)),

- a statement that the Court's observations are subject to a contradictory procedure (Article 143(1) and (2)),

- a rewording of the arrangements for publication of the institutions' replies (Article 143(4)),

- a recasting of the arrangements whereby the Commission seeks the views of each Member State on observations by

the Court relevant to it (Article 143(6)), including a longer time for Member States to reply,

- a new provision requiring the Court to transmit statements of preliminary findings relevant to the Annual Report by 1 June of the year after that to which they refer, and giving the institution, body or Member State concerned 2 ½ months to inform the Court of any comments which it wishes to make on statements of preliminary findings (Article 144a).

Analysis

50. The Court has no comments on the changes proposed to Article 143(4) or (6).

51. The proposal to insert a reference to the contradictory procedure in Article 143(1) and (2) is redundant.

52. The Court regards the proposed timetable changes to Article 143(1) as inappropriate. Formally, they would significantly reduce the time available to the Court to prepare its observations. The Court notes moreover that the Commission has not proposed to bring forward the date at which it is required to present the provisional (Article 128) and final accounts (Article 129).

53. The proposed timetable is particularly striking in respect of the annual activity reports of the Commission's Directors-General and the 'synthesis report' which brings them together. The Court comments on these documents in its annual reports. Article 60(8) of the Financial Regulation provides that these will be made available on 15 June. The Court would thus be required to transmit its draft report on the same day that the Commission is required to transmit its synthesis report on the operation of the internal control system.

54. The Court recognises the desirability of making any material available to the Commission and others in good time and in practice does so in advance of the deadlines for formal transmission set out in the Financial Regulation wherever possible. It suggests that it would be best to leave existing formal deadlines unchanged and to continue to rely on cooperation.

55. If the Parliament and Council take the view instead that certain deadlines should be brought forward, the Court considers that the same approach will be necessary in respect of deadlines for the Commission.

56. In this case, it would in particular be desirable to reconsider the deadline for receipt of the replies from the Commission and other institutions to the Court's draft Annual Report (observations). This is set at 15 October in Article 143(1). If institutions only made their final translated replies available as late as this, it would become impossible to publish the Annual Report on time. To meet the current timetable for presentation of the Annual Report to the budgetary authority at the beginning of November, the Court must receive fully translated replies no later than 30 September.

57. The proposed new Article 144a also needs to be considered in the light of the constraints upon drawing up the Court's annual report.

58. The Court is required to report on all of the expenditure for a financial year. It cannot complete its programme of audit visits until the Commission has recorded all expenditure⁽¹⁾. In these circumstances, it is inevitable that communication of audit results will impose stress upon all parties. Cooperation, communication and discussion are necessary to address this.

59. There are usually three occasions on which the auditee has a chance to respond to the Court's findings:

- (a) during audit visits (after which many beneficiaries/Member States decide to provide additional documentation);
- (b) through the statement of preliminary findings (sent following the audit visit, and receipt of any additional information);
- (c) following transmission of the draft report ('observations') to the Commission. At present all draft reports involve a face-to-face meeting with the Commission to discuss their draft reply.

60. The statement of preliminary findings is a part of the Court's internal procedures rather than a document adopted by the Court or a Chamber⁽²⁾. The Court therefore takes the view that it is inappropriate in principle to insert in the Financial Regulation a provision such as Article 144a.

⁽¹⁾ It is still the case that payments are concentrated at year end. In 2009, for example, the Commission recorded 33 % of European Social Fund expenditure in December.

⁽²⁾ Present arrangements reflect discussions in the context of the Contact Committee, which is composed of the heads of the European Union Supreme Audit Institutions including the Court's President (in line with the Treaty requirement for the Court and the national audit bodies to 'cooperate in a spirit of trust while maintaining their independence'). The Court seeks a reply within four weeks, or, wherever possible within a longer period, for its observations relating to the DAS. The Court would be prepared to commit itself to transmit statements of preliminary findings relating to the Annual Report by the date of 1 June set out in the proposed Article 144a.

61. Moreover there are significant practical objections to the Commission's proposal.

- There are likely to be some occasions in which later corroboration of findings is desirable (for example, when information is received late from a beneficiary).
- The period of 2 ½ months provided for in Article 144a(2) for replies to the statements of preliminary findings (which could go up to mid-August) is impractically long and, as noted in paragraph 59, does not correspond to the current arrangements. It could render impossible the production of the Annual Report by 15 November, as required by the Financial Regulation.
- It is also inconsistent with either the present Article 143(2) or the proposed Article 143(1). The Court's draft observations (to be sent in June) should reflect discussion of statements of preliminary findings (which pursuant to the proposed Article 144a could continue until the middle of August).

62. If the use of statements of preliminary findings is to be regulated, the priority would be to place a legal obligation on the Commission to reply, with a maximum deadline of six weeks.

Recommendation

63. The Court recommends the Parliament and Council:

- not to make the changes proposed to Article 143(1),
- not to insert into the Financial Regulation the proposed new text of Article 143(2),
- not to insert into the Financial Regulation the proposed new Article 144a.

Special reports

The Commission's proposal

64. The Commission proposes:

- to insert a reference to the contradictory procedure in Article 144,
- to make some drafting changes to the text of Article 144(1),
- to insert a new paragraph to regulate the way in which the Court presents its special reports.

Analysis

65. As in the case of the annual report, the Court considers the reference to the contradictory procedure redundant.

66. The second of the supposedly clarifying changes is obscure. The intention is presumably that the Court should adopt the definitive version of the special report within 1 month of receiving the replies concerned. The Court's practice is in any case to adopt special reports immediately after it has received the final version of the replies of the institution concerned. The Court considers that this revision of the Financial Regulation provides a good opportunity to remove this redundant subparagraph from Article 144.

67. The proposed new final subparagraph of Article 144(1) would unhelpfully constrain the Court's ability to produce special reports in a way which maximises their value to readers. The Court is continually revising the way in which reports are presented and already gives more prominence to replies from the auditee than most supreme audit institutions. The Court understands that most national audit bodies invite the comments of the auditee on their draft reports, and then summarise their comments within the text of the report. If changes are to be made, the Court would prefer this model of presentation.

Recommendation

68. The Court recommends the Parliament and Council not to accept the changes to Article 144 discussed above; and to consider the deletion of Article 144(1), third subparagraph.

Further issues on external audit

69. The third sentence in Article 140(2) of the current Financial Regulation diverges from the text of the Treaty in three respects: the words 'in conjunction' replace 'in liaison' from the Treaty; the Financial Regulation talks of 'audit institutions' rather than 'audit bodies' and 'national departments' are described as 'responsible' rather than 'competent'. The Court recommends that this section be aligned with the terminology of the Treaty.

European trust funds (Article 164)

The Commission's proposal

70. The draft Financial Regulation includes a new Article 164, providing a basis for the possible creation of European trust funds. These would follow the model of the trust fund operations of the World Bank and United Nations. They would allow the Commission to manage funds from other

donors (as well as from the EU budget) in a common pool. The Commission proposes to hold these funds in a specific bank account, and to charge a management fee of 7 %.

Analysis

71. The decision whether the Commission should begin to manage trust funds is a policy matter on which the Court does not seek to take position. The Court however draws the attention of the Parliament and Council to issues of administration, cost, accountability and audit raised by this proposal.

Administrative issues

72. While a specific bank account may be appropriate for receiving contributions, and holding them until they are required, other arrangements are necessary in order to put donations to use. A trust fund aimed at responding to the earthquake in Haiti, for example, would incur local currency expenses in Haiti, purchase supplies and services in a variety of currencies around the Caribbean region, and obtain goods and logistical services from within and around the EU. This would require trust funds transactions to be handled by a variety of bank accounts, and to be dealt with by a variety of delegations and staff members.

73. Trust fund accounting would therefore be a complex activity, intimately integrated with other accounting activities. This complexity is not recognised in the Commission's draft text on 'specific bank accounts'.

Cost

74. The draft Financial Regulation would allow the Commission to charge a management fee of 7 % of contributions for administering a trust fund. The Court understands that this figure (which is also used under the EC/UN Financial and Administrative Framework Agreement) reflects the limit to administration overheads allowed in other areas of the budget, rather than an evaluation of the likely additional costs of running a trust fund.

75. A feature of the proposal is that the Commission, which would be a donor itself, would be able to charge the administration fee for managing its own contribution to the fund. The explanatory fiche describes the specific bank account as 'outside the budget', suggesting that the Commission expects to treat transfers to the trust fund as budgetary expenditure. It is not clear that it is legitimate for the Commission to charge an administrative fee for managing its own funds, nor is it clear whether the 7 % management fee represents a justified appraisal of the likely costs involved.

Accountability and audit arrangements

76. The draft Implementing Rules (Article 231a) state that the trust fund is to be consolidated into the Commission's annual accounts and that an annual account is to be presented to the budgetary authority in the context of the discharge process. Each individual trust fund is to be subject to at least three audits: that of the Internal Audit Service, that of the Court, and that of an 'independent external auditor'.

77. These arrangements can be compared with those of established managers of trust funds. These typically involve preparation of a consolidated statement of trust funds, covered by a single audit. This consolidation reduces significantly the cost of audit. In the case of the World Bank, donors who wish for extra assurance on individual trust funds arrange for an audit to be performed by the external auditor of the managing body, but must pay a fee to the auditor to cover the extra cost of this audit.

Recommendation

78. The Court recommends the Parliament and Council to give due weight to the considerations set out above when considering this Commission's proposal, and to consider how, if the proposal to create European trust funds is supported, robust but cost-effective arrangements can be devised.

Model Financial Regulation for public-private partnerships (Article 185a)

The Commission's proposal

79. The draft Financial Regulation includes a new Article 185a, providing a basis to introduce explicitly the concept of public-private partnerships (PPP) and to entrust a special public-private partnership body with their implementation. The Commission proposal provides for the adoption by the Commission of a light model Financial Regulation, which would lay down a set of principles necessary to ensure sound financial management. These principles, inspired in particular by the new Article 53b of the draft Financial Regulation, would be included in the financial rules to be adopted by the bodies having a legal personality set up by a basic act and entrusted with the implementation of a PPP pursuant to Article 53(1) point (2)(e).

Analysis

80. In essence public-private partnerships are a form of long term, high value and often complex legal arrangement. The Commission's technical fiche states that partners do not consider the provisions of the current Financial Regulations suitable. On this basis (and after further analysis), the

Commission considered that for implementation of a PPP an additional option of entrusting it to a special public-private partnership body should be added to the current options.

81. The decision whether to entrust a special public-private partnership body with the implementation of a PPP is a policy matter on which the Court does not seek to take position. The provisions on the 'light model Financial Regulation' for the special bodies make no provision for consultation of the Court. The Court considers that it is important that this document should in no way restrict the capacity of the Court to audit the use of EU funds.

Recommendations

82. The Court recommends that the words 'and after consulting the Court of Auditors' be added to the second sentence of this Article.

Financing the purchase of buildings (Article 179(3)(b))

83. The Court has no comment on this proposal.

Final provisions

84. The Court has no comment on the procedural suggestion made by the Commission.

Issues not given prominence in the Commission's explanatory memorandum

85. The Court wishes to draw the attention of the Parliament and Council to four matters not brought to their attention in the Commission's explanatory memorandum: the clearing of prefinancing payments (Article 81), the responsibilities of the accounting officer (Article 123), the audit of agencies (Article 185(4)) and the proliferation of reporting obligations across the Financial Regulation.

Clearance of prefinancing (Article 81)

The Commission's proposal

86. Very high levels of uncleared prefinancing have occurred in recent years in some parts of the budget. The Commission's proposal responds to this problem.

Analysis

87. The Commission proposes, inter alia, the addition of a new paragraph 4 to Article 81 which would require the responsible authorising officer to clear prefinancing 'regularly', but with no mention of the frequency of clearing. It is not clear whether the change proposed will achieve the objective set.

Recommendation

88. The Court recommends the European Parliament and the Council to consider strengthening this provision, for example by referring to the desirability of avoiding an excessive build-up of uncleared items, and/or allowing only a single prefinancing payment.

89. The Court points out that it should be possible for the Commission to tackle the problem of high levels of uncleared prefinancing before changes are made to the Financial Regulation. The Court suggests the Commission adopt a target for reducing the level of uncleared prefinancing, and monitor progress via annual activity reports.

Presentation of the accounts and accounting (Title VII)

The Commission's proposal

90. The Commission's proposals simplify and reduce the text on the presentation of the accounts. Some changes are made to the date for presentation of different sets of financial information.

Analysis

91. The Court welcomes the simplification of the existing text of this title. However, the Court takes the view that it would be useful to take this opportunity to make explicit the responsibility of the Commission's accounting officer in respect of the Commission's accounts to ensure that the accounts are properly prepared. The intention would not be to bring about any change of substance: in practice the accounts are prepared in all material respects in accordance with International Public Sector Accounting Standards. But there is scope for greater clarity.

92. The Court suggests a modification to Article 123 to state that the accounts are to be drawn up in accordance with 'the internationally accepted accounting standards for the public sector' (borrowing words from Article 133) but allowing the accounting officer a true and fair view override. Thus the accounting officer would be allowed to adopt a treatment different from that required by the standards only where that was necessary to show a true and fair view. S/he would then be required to explain that this had been done, and show (in the notes to the accounts) how the financial statements would have been different if the standards had been followed.

Recommendation

93. The Court recommends the Parliament and Council, when considering the Commission's proposals for this part of

the Financial Regulation, to consider the insertion of a clarification on the lines suggested above.

Financial regulations of agencies and other bodies set up under the Treaty (Article 185(4))

The Commission's proposal

94. The Commission has proposed a new Article 185(4), dealing with the audit of EU agencies. It provides that the Court's specific annual reports on the agencies shall draw upon work done by private sector auditors, which would be appointed by each agency. There is some ambiguity about the exact intention of the proposal: the first sentence refers to the legality and regularity of revenue and expenditure, the second to the accounts.

Analysis

95. The Commission's proposal has the potential to provide a basis for an improved audit framework for the agencies. Private sector auditors are used to forming an opinion on the reliability of accounts. The Court shares the Commission's view that it should be able to rely on the work of an independent, properly appointed, private sector auditor in respect of its opinion in relation to the reliability of an agency's accounts.

96. Matters are somewhat more complicated in relation to legality and regularity, where the requirements set out in EU law are further removed from the conventional audit work of private sector auditors. In the Court's view the most appropriate course would be to require a designated private sector auditor to undertake 'agreed-upon procedures' in respect of procurement and recruitment issues, whereby the private sector auditor would select an 'agreed-upon' sample of procurement and recruitment processes and subject that sample to an 'agreed-upon' set of tests. The Court would then form its own opinion, based on the results of the testing, on the issue of the legality and regularity of the agency's accounts.

97. The Court therefore suggests that it should be involved in the selection of the private sector auditors, should have ownership of the audit working papers and be in the ultimate position to dispense with the services of a private sector auditor should the Court believe this to be necessary. As the audit opinion is the Court's opinion and would remain so, the Court should have complete control of any outsourced audit field work.

98. A proposal revised on these lines would permit the Court to continue to fulfil its mandate in a cost-effective way in the context of a growing number of agencies and bodies.

Recommendation

99. The Court recommends the adoption of the Commission's proposal subject to the following changes.

- (a) Court approval should be a prerequisite to the appointment by an agency of a private sector auditor. The Court must be satisfied that a proper tendering process has taken place, that the audit firm chosen is sufficiently competent and independent and that the audit fee proposed is reasonable. The Court would stipulate that a standard contract be in place containing the clauses relating to agreed-upon procedures on the legality and regularity of expenditure.
- (b) The Court should not be obliged to rely completely on the work of others. The Court must have the ability to conduct any audit procedures deemed necessary to form its opinion. Furthermore, the phrase 'shall rely' should be modified to become 'may rely' so that the Court is not stripped, by the Financial Regulation, of its discretion. The legal thrust of the phrase must allow the Court to rely on the work of others without forcing it to do so.
- (c) The mission of the private sector auditor should include providing the Court with the external auditor's opinion on reliability and to undertake a set of agreed-upon procedures

in respect of legality and regularity. It is proposed that the text be modified slightly to reflect such proposed mission.

100. In addition to these points, the Court proposes a small addition to Article 185(1) to ensure that the Court continues to be consulted before the adoption of a model Financial Regulation for agencies and other bodies.

Reporting requirements

101. The Financial Regulation provides for a number of reports by the Commission. The annual financial statements and the reports on implementation of the budget flow (Article 121) from international standards. The Financial Regulation imposes other reporting requirements, such as the authorising officer's annual activity report (Article 60(7)) and the report on budgetary and financial management (Article 122). The Treaty now also requires an annual evaluation report on the Union finances (Article 318 TFEU).

102. Without calling into question the value of any of these reports, the Court suggests that the European Parliament and the Council might wish to ask the Commission to consider whether there is scope for simplifying and consolidating reports, taking account of the needs of users.

This opinion was adopted by the Court of Auditors in Luxembourg at its meeting of 21 October 2010.

For the Court of Auditors
Vitor Manuel da SILVA CALDEIRA
President

ANNEX

Commission's modified text	Court's suggestion
<p style="text-align: center;"><i>Article 10</i></p> <p style="text-align: center;">Carry over rules for assigned revenue</p> <p>Revenue not used and appropriations available at 31 December arising from the assigned revenue referred to in Article 18 shall be carried over as follows:</p> <ul style="list-style-type: none"> — external assigned revenue shall be carried over automatically and must be fully used until all the operations relating to the programme or action to which they are assigned have been carried out. External assigned revenue received during the last year of the programme or action may be used in the first year of the succeeding programme or action, — internal assigned revenue shall be carried over for one year only, unless specified otherwise in the basic act applicable, or in duly justified exceptional circumstances. The corresponding appropriations available must be used first. 	<p style="text-align: center;"><i>Article 10</i></p> <p style="text-align: center;">Carry over rules for assigned revenue</p> <p>Revenue not used and appropriations available at 31 December arising from the assigned revenue referred to in Article 18 shall be carried over as follows:</p> <ul style="list-style-type: none"> — external assigned revenue shall be carried over automatically and must be fully used until all the operations relating to the programme or action to which they are assigned have been carried out. External assigned revenue received during the last year of the programme or action may be used in the first year of the succeeding programme or action. — internal assigned revenue shall be carried over for one year only, unless specified otherwise in the basic act applicable, or in duly justified exceptional circumstances. The corresponding appropriations available must be used first.
<p style="text-align: center;"><i>Article 81</i></p> <p style="text-align: center;">Types of payments</p> <p>[...]</p> <p>4. Prefinancing payments shall be cleared regularly by the responsible authorising officer. To this effect appropriate provisions shall be included in the contracts, grant decisions and agreements as well as the delegation agreements entrusting implementation tasks to the entities and persons referred to in points (a) to (h) of point (2) of the first paragraph of Article 53.</p>	<p style="text-align: center;"><i>Article 81</i></p> <p style="text-align: center;">Types of payments</p> <p>[...]</p> <p>4. Prefinancing payments shall be cleared regularly <u>in a manner and with a frequency sufficient to avoid excessive amounts of uncleared prefinancing</u> by the responsible authorising officer. To this effect appropriate provisions shall be included in the contracts, grant decisions and agreements as well as the delegation agreements entrusting implementation tasks to the entities and persons referred to in points (a) to (h) of point (2) of the first paragraph of Article 53.</p>
<p style="text-align: center;"><i>Article 123</i></p> <p style="text-align: center;">Rules governing the accounts</p> <p>The financial statements referred to in Article 121 shall comply with the Union accounting rules as adopted by the Accounting Officer of the Commission and shall present a true and fair view of the assets and liabilities, charges, income and cash flow.</p> <p>The budgetary accounts referred to in Article 121 shall comply with the budgetary principles laid out in this Regulation. They shall present a true and fair view of the budgetary revenue and expenditure operations.</p>	<p style="text-align: center;"><i>Article 123</i></p> <p style="text-align: center;">Rules governing the accounts</p> <p><u>The Accounting Officer of the Commission shall adopt rules to give effect to internationally accepted accounting standards for the public sector. The Accounting Officer may diverge from these if he considers this necessary to give a true and fair view of the assets and liabilities, charges, income and cash flow. Where the Accounting Officer of the Commission diverges from the standards he shall disclose this, and quantify the impact in the notes to the financial statements.</u></p> <p>The financial statements referred to in Article 121 shall comply with the Union accounting rules as adopted by the Accounting Officer of the Commission and shall present a true and fair view of the assets and liabilities, charges, income and cash flow.</p> <p>The budgetary accounts referred to in Article 121 shall comply with the budgetary principles laid out in this Regulation. They shall present a true and fair view of the budgetary revenue and expenditure operations.</p>

Commission's modified text	Court's suggestion
<p style="text-align: center;"><i>Article 143</i></p> <p style="text-align: center;">Annual Report of the Court of Auditors</p> <p>1. The Court of Auditors shall transmit to the Commission by 15 June and to other institutions and bodies referred to in Article 121 by 1st of June at the latest, any observations which are, in its opinion, such that they should appear in the annual report. These observations must remain confidential and are subject to a contradictory procedure. Each institution shall address its reply to the Court of Auditors by 15 October at the latest. The replies of institutions other than the Commission shall be sent to the Commission at the same time.</p> <p>2. After completion of the contradictory procedure, each institution or body concerned shall address its reply to the Court of Auditors by 15 October at the latest. The replies of institutions other than the Commission and of the bodies shall be sent to the Commission at the same time.</p>	<p style="text-align: center;"><i>Article 143</i></p> <p style="text-align: center;">Annual Report of the Court of Auditors</p> <p>1. The Court of Auditors shall transmit to the Commission by 15 June and to other the institutions and bodies referred to in Article 121 concerned, by 1st of 30 June at the latest, any observations which are, in its opinion, such that they should appear in the Annual Report. These observations must remain confidential and are subject to a contradictory procedure. Each institution shall address its reply to the Court of Auditors by 15 October 30 September at the latest. The replies of institutions other than the Commission shall be sent to the Commission at the same time.</p> <p>2. After completion of the contradictory procedure, each institution or body concerned shall address its reply to the Court of Auditors by 15 October at the latest. The replies of institutions other than the Commission and of the bodies shall be sent to the Commission at the same time.</p>
<p style="text-align: center;"><i>Article 144</i></p> <p style="text-align: center;">Special Reports of the Court of Auditors</p> <p>1. The Court of Auditors shall transmit to the institution or the body concerned any observations which are, in its opinion, such that they should appear in a special report. These observations must remain confidential and are subject to a contradictory procedure.</p> <p>The institution or the body concerned shall have two-and-a half months within which to inform the Court of Auditors of any replies it wishes to make on the observations in question.</p> <p>The Court of Auditors shall adopt the definitive version of the special report in question the following month upon the receipt of the replies made by the institution or the body concerned.</p> <p>The special reports, together with the replies of the institutions or bodies concerned, shall be transmitted without delay to the European Parliament and the Council, each of which shall decide, where appropriate in conjunction with the Commission, what action is to be taken in response.</p> <p>The Court of Auditors shall take all necessary steps to ensure that the replies of each institution or body concerned to its observations are published immediately next to or after each observation to which they relate.</p>	<p style="text-align: center;"><i>Article 144</i></p> <p style="text-align: center;">Special Reports of the Court of Auditors</p> <p>1. The Court of Auditors shall transmit to the institution or the body concerned any observations which are, in its opinion, such that they should appear in a special report. These observations must remain confidential and are subject to a contradictory procedure.</p> <p>The institution or the body concerned shall 2 ½ months within which to inform the Court of Auditors of any replies it wishes to make on the observations in question.</p> <p>The Court of Auditors shall adopt the definitive version of the special report in question the following month upon the receipt of the replies made by the institution or the body concerned.</p> <p>The special reports, together with the replies of the institutions or bodies concerned, shall be transmitted without delay to the European Parliament and the Council, each of which shall decide, where appropriate in conjunction with the Commission, what action is to be taken in response.</p> <p>The Court of Auditors shall take all necessary steps to ensure that the replies of each institution or body concerned to its observations are published immediately next to or after each observation to which they relate <u>together with the report.</u></p>
<p style="text-align: center;"><i>Article 185</i></p> <p style="text-align: center;">Framework Financial Regulation for agencies and bodies set up under the Treaty on the functioning of the European and the Treaty establishing the European Atomic Energy Community</p> <p>1. In accordance with Article 290 of the Treaty on the Functioning of the European Union, the Commission shall adopt a framework Financial Regulation for bodies set up under this Treaty and the Treaty establishing the European Atomic Energy Community which have legal personality and receive contributions charged to the Union budget.</p> <p>[...]</p>	<p style="text-align: center;"><i>Article 185</i></p> <p style="text-align: center;">Framework Financial Regulation for agencies and bodies set up under the Treaty on the functioning of the European and the Treaty establishing the European Atomic Energy Community</p> <p>1. In accordance with Article 290 of the Treaty on the Functioning of the European Union <u>and after consulting the Court of Auditors,</u> the Commission shall adopt a framework Financial Regulation for bodies set up under this Treaty and the Treaty establishing the European Atomic Energy Community which have legal personality and receive contributions charged to the Union budget.</p> <p>[...]</p>

Commission's modified text	Court's suggestion
<p>4. Unless otherwise provided in the basic act creating a body referred to in paragraph 1, the Court of Auditors shall examine the legality and regularity of the revenue and expenditure of this body before its accounts are consolidated with the Commission's accounts. This examination shall rely on the audit report established by an independent external auditor designated by the body and whose mission is to verify the conformity of the body's accounts with Article 123 of this Regulation.</p>	<p>4. Unless otherwise provided in the basic act creating a body referred to in paragraph 1, the Court of Auditors shall examine the legality and regularity of the revenue and expenditure of this body before its accounts are consolidated with the Commission's accounts. This examination shall rely on the audit report established by an independent external auditor designated by the body and whose mission is to verify the conformity of the body's accounts with Article 123 of this Regulation.</p> <p>4. <u>The bodies referred to in paragraph 1 shall each appoint by contract, following receipt of approval of the Court of Auditors, an independent auditor whose mission is to verify the conformity of the body's accounts with Article 123 of this Regulation and to undertake an analysis, under the direction of the Court of Auditors, of the legality and regularity of the revenue and expenditure of this body. The Court of Auditors shall examine the report prepared by any such independent auditor and, together with carrying out any other procedures it deems necessary, may rely on the independent auditor's report when forming its opinion.</u></p>
<p style="text-align: center;"><i>Article 185a</i></p> <p>Model Financial Regulation for public private partnership bodies</p> <p>The bodies having legal personality set up by a basic act and entrusted with the implementation of a public-private partnership pursuant to Article 53(1) point (2) (e) shall adopt their financial rules.</p> <p>These rules shall include a set of principles necessary to ensure sound financial management of Union funds, inspired by Article 53b of the present Regulation and which shall be laid down in a light model Financial Regulation, to be adopted by the Commission, in accordance with Article 290 of the Treaty on the Functioning of the European Union.</p> <p>The Provisions of Articles 183aa, 183ab and 183ac shall apply <i>mutatis mutandis</i> to this Article.</p>	<p style="text-align: center;"><i>Article 185a</i></p> <p>Model Financial Regulation for public private partnership bodies</p> <p>The bodies having legal personality set up by a basic act and entrusted with the implementation of a public-private partnership pursuant to Article 53(1) point (2)(e) shall adopt their financial rules.</p> <p>These rules shall include a set of principles necessary to ensure sound financial management of Union funds, inspired by Article 53b of the present Regulation and which shall be laid down in a light model Financial Regulation, to be adopted by the Commission, in accordance with Article 290 of the Treaty on the Functioning of the European Union <u>after consulting the Court of Auditors.</u></p> <p>The Provisions of Articles 183aa, 183ab and 183ac shall apply <i>mutatis mutandis</i> to this Article.</p>

CORRIGENDA**Corrigendum to Annual Report of the Court of Auditors on the implementation of the budget concerning the financial year 2009, together with the institutions' replies**

(Official Journal of the European Union C 303 of 9 November 2010)

(2010/C 334/02)

On pages 158 and 159, Annex 6.4 is replaced by the following table:

FOLLOW-UP OF PREVIOUS OBSERVATIONS FOR EXTERNAL AID, DEVELOPMENT AND ENLARGEMENT

Court observation	Action taken	Court analysis	Commission reply
External relations and development			
1. <i>Monitoring of, and support to, organisations in charge of the implementation of EU-funded projects</i>			
<p>Regarding <i>ex ante</i> checks, weaknesses were noted including insufficient monitoring of, and support to, organisations in charge of the implementation of EU-funded projects.</p> <p>(2008 Annual Report, paragraphs 8.22 and 8.35)</p>	<p>Preparation of a Financial Management Toolkit for implementing organisations.</p>	<p>See report on the EDFs, Annex 4, row 2.</p>	<p>EuropeAid's Financial Management Toolkit for implementing organisations will be finalised and made available during 2010.</p>
2. <i>Budget support payments</i>			
<p>Regarding <i>ex ante</i> checks, weaknesses were noted in the case of budget support payments in the processes for verifying the fulfilment of the payment conditions.</p> <p>(2008 Annual Report, paragraph 8.22)</p>	<p>Widespread awareness throughout the Commission's services of the need to ensure a more structured and formal approach when assessing budget support payments including the strengthening of the role of verification by finance and contracts staff in the payment approval process.</p>	<p>See report on the EDFs, Annex 4, row 9.</p>	<p>EuropeAid will address this issue in the revision of the Budget Support Guidelines and the review of the peer review process for action proposals (Quality Support Group), planned for 2011.</p>
3. <i>System of external audits</i>			
<p>In respect of the use of external audits, one of the most important components of EuropeAid's internal control framework, the Court noted improvement in the processes. However, it concludes that these controls remain partially effective overall.</p> <p>(2008 Annual Report, paragraphs 8.23 and 8.24)</p>	<p>Reforms introduced since 2007 to the audit methodology in place complemented by a substantial revision of the annual audit plan methodology.</p>	<p>See report on the EDFs, Annex 4, row 3.</p>	<p>The Commission agrees that substantial improvements have been achieved in the audit planning process.</p>
4. <i>Risk management process</i>			
<p>The risk management process was found to be partially effective.</p> <p>(2008 Annual Report, paragraph 8.23)</p>	<p>Continuing efforts to raise awareness of the risk management process.</p>	<p>The risk management process was assessed as being overall effective.</p>	<p>EuropeAid's risk management methodology was completely revised in 2009 and compulsory awareness-raising training sessions were run for all units.</p>

Court observation	Action taken	Court analysis	Commission reply
5. <i>Ex post controls</i>			
<p>Important shortcomings were identified in respect of the <i>ex post</i> controls component of the DG RELEX's supervisory and control systems for ensuring the regularity of transactions.</p> <p>(2008 Annual Report, paragraph 8.25)</p>	<p>Close monitoring of the implementation of the <i>ex post</i> controls annual plans.</p>	<p>Notwithstanding the efforts and the progress made so far there are still important weaknesses to overcome.</p>	<p>DG RELEX is taking measures to address all recommendations received regarding <i>ex post</i> controls.</p>
Enlargement			
6. <i>IAC</i>			
<p>It was noted that the multiannual programme of the IAC was not sufficiently developed.</p> <p>(2008 Annual Report, paragraph 8.27)</p>	<p>IAC in 2009 developed a multiannual programme of its activities.</p>	<p>The Court considers this observation duly addressed by DG ELARG.</p>	
7. <i>Ex post controls of centrally managed projects</i>			
<p>It was noted that DG ELARG did not have a specific strategy for the <i>ex post</i> controls of centrally managed projects.</p> <p>(2008 Annual Report, paragraph 8.27)</p>	<p>During 2009 DG ELARG developed the strategy for the <i>ex post</i> control of centrally managed projects.</p>	<p>The Court welcomes the initiative of DG ELARG, but the new strategy will be put in practice only in 2010 and still needs to prove its effectiveness.</p>	<p>The implementation of the new strategy is currently showing its first positive results.</p>
8. <i>Potential irregularities in the management of Phare funds by two agencies in Bulgaria</i>			
<p>It was noted that fundamental weaknesses remained concerning potential irregularities in the management of Phare funds by two agencies in Bulgaria.</p> <p>(2008 Annual Report, paragraph 8.28)</p>	<p>During 2009 and following corrective actions from the Bulgarian authorities, DG ELARG lifted the suspension of payments to Bulgaria.</p>	<p>DG ELARG still needs to devote a special attention to the follow-up of the implementation of the post-accession funds in Bulgaria.</p>	<p>The implementation of the post-accession funds in Bulgaria will continue to receive the special attention needed until all programmes are closed.</p>
Humanitarian aid			
9. <i>IAC</i>			
<p>In 2008 the IAC did not operate yet in its full capacity due to the transferral of activities from EuropeAid's IAC.</p> <p>(2008 Annual Report, paragraph 8.29)</p>	<p>During 2009 IAC was properly staffed and implementing a full year working programme.</p>	<p>DG ECHO's IAC is functioning properly and providing assurance to DG ECHO's Director-General.'</p>	

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