Brussels, 21 March 2017

European Parliament Workshop

European Court of Auditors' opinion on the revision of Financial Regulation

EUROPEAN COURT OF AUDITORS

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Three key points

- One stop reporting accountability

- Moving from cost conditionality to performance conditionality

- Streamlining budgetary arrangements

(1) One stop reporting accountability

Objective:

- Bring Commission reporting truly into the modern age with a one stop shop for Commission accountability

The Commission proposal:

- is reporting really "integrated"?
  …or publishing existing reports at the same time?

(1) One stop reporting accountability

Our proposal (paragraphs 7-11)

Produce a single accountability report incorporating:

- a President's report;
- activities during the year;
- non-financial performance,
- operational and strategic risks;
- governance statement;
- report of the Audit Committee;
- financial statements discussion and analysis;
- the consolidated accounts;
- a mid- and long-term fiscal sustainability statement; and
- budgetary implementation reports

Present in due time for audit of the accounts and consistency checks on other information

Integrated Financial Reporting Package – positive move, but not enough

(2) Moving from cost conditionality to performance conditionality (77-84)

- Performance based payments
- Checks and controls focused on outputs
- Commission-wide simplified forms of grants

We support the move to make the payments based on conditions fulfilled or results achieved the preferred option across the EU budget

(2) Moving from cost conditionality to performance conditionality (28-34)

- Abandoning the principle of no profit

  We do not see the need for this requirement

- Recognition of volunteers work as eligible costs for co-financing

  Could increase risk of ineligible spending

- Exemptions from the principle of non-cumulative award and no double funding

  Exemptions should be restricted to principle of non-cumulative award

(3) Streamlining the budget (51-63)

- Holding funds in reserve
  - 'flexibility cushion' for certain external aid instruments

    Creating one additional reserve and one more exception to the annuality principle
  - 'negative reserve'

    No strong justification for its increase

- Transfers from shared management to Union level

  Could effectively represent a transfer of appropriations

(3) Streamlining the budget (57-76)

- Budgetary carry overs (57-60)

  Complicated and lengthy procedure which could be simplified significantly

- Assigned revenue (69-76)

  "Internal assigned revenue" should be accounted for as general revenue

Other points: new instruments

- Financial interventions (paragraphs 42-50)
  - Single regulatory framework
  - Common provisioning fund
  - Performance based fees
  - Ex-ante evaluations required for financial operations
  - Single report on all financial operations

- Combinations of instruments

- Trust funds extension to internal policies (64-68)

Closing point: Help the auditors help you!

- Respect our independence (16-17,106-108)
- Cross reliance on audit (100-105)
- Streamline the audit of EU agencies and public-private partnerships (23-27)

Closing point: Help the auditors help you!

Save our special reports (18-22)

Table 2

Role/composition of Audit Progress Committee and selected audit committees compared to best practices recommended by Good Governance in the Public Sector Framework

Best practices recommended by Good Governance in the Public Sector Framework	Commission's Audit Progress Committee[2]	Role of selected audit committees[1]			
		World Food Programme Audit Committee	European Investment Bank Audit Committee	World Bank Group Audit Committee	United Nations Independent Advisory Committee
Provide assurance on risk management arrangements	x	√	√	√	√
Provide assurance on internal control arrangements	x	√	√	√	√
Provide assurance on arrangements for reporting on financial and non-financial performance	x	√	√	√	√
Oversee internal audit	√	√	√	√	√
Reinforce effectiveness of external audit	x	√	√	√	x
Majority of independent members	x	√	√	√	√

1 *Sources:* World Food Programme: Terms of reference for the Audit Committee of the World Food Programme (November 2011), European Investment Bank: Audit Committee Charter (June 2007), World Bank Group: World Bank Resolution Standing Committees (2009), Annex A Terms of Reference of the Audit Committee, United Nations: Terms of reference for the Independent Audit Advisory Committee and strengthening the Office of Internal Oversight Services (June 2007).

2 *Source:* ECA. The APC Charter also refers to external audit (see paragraph 30).

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As stated in the Commission communication on the APC Charter, 'audit committees play an increasingly important role in delivering the transparency and accountability citizens and other stakeholders rightly demand of public bodies'[48]. The APC is currently the 'audit committee' of the Commission. We examined the APC against the criteria of best practice (***Box 8***), and international bodies selected as benchmarks (***Table 2***). Notably, all members of audit committees in these international bodies are independent. In the case of Commission, seven out of nine members of the APC are internal.

48 C(2015) 3014 final 'Charter of the Audit Progress Committee of the European Commission', p. 2.

Aligning internal controls and financial reporting with international standards

The Commission chose the COSO framework as the basis for its internal control standards …

Box 9

Internal control

'Internal control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance of achieving objectives relating to operating, reporting and compliance'[49].

49 Definition of COSO, Committee of Sponsoring Organisations of the Treadway Commission, 2013 COSO Internal Control – Integrated Framework. © Committee of Sponsoring Organisations of the Treadway Commission (COSO). All rights reserved. Used with permission.

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The Commission modified its internal control (see ***Box 9***) arrangements as part of the Prodi reform (see ***Figure 1*** and ***Box 3***). The new arrangements represented a significant departure from the previous system based on the centralised approval (visa) of the financial controller. The Commission based the control arrangements on the COSO 1992 framework (see ***Box 10***) and introduced the COSO definition of internal control into the Financial Regulation[50].

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In 2001 the Commission introduced 24 control standards complemented by a set of baseline requirements defining the specific practical actions which should underlie each department's internal control system. It required DGs to assess and report on their level of compliance with the baseline requirements each year. These reports rely on internal reviews, management self-assessments and relevant audits performed by the IAS and the ECA. We reported on progress in implementing these standards in our annual reports from 2002 to 2008.

50 Article 32.2 of Regulation (EU, Euratom) No 966/2012.

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Closing point: Help the auditors help you!

Save our special reports

THE COURT'S OBSERVATIONS	THE COMMISSION'S REPLIES
2.40. The Commission made a high level of commitments in 2015, in part on appropriations brought forward from 2014. Outstanding commitments returned to previous levels (paragraphs 2.5 to 2.9). Amounts to be funded from future budgets rose to 339 billion euro. The Commission has not produced a cash flow forecast covering the next seven to ten years (paragraph 2.10). Such a forecast would enable stakeholders to anticipate future payment requirements and budgetary priorities and constructively plan ahead.	**2.40.** *The MFF is the tool ensuring medium- to long-term stability and predictability of future payment requirements and budgetary priorities.* *Therefore long-term forecasts can only be established taking into consideration existing financial frameworks. The payment implications of future financial frameworks which have not yet been agreed cannot be predicted with precision.* *The forecast for the post-2020 period will be presented in 2017 (as foreseen in point 9 of the Inter-institutional Agreement on budgetary discipline, on cooperation in budgetary matters and on sound financial management) and it will be an integral part of the Commission proposals for the post-2020 MFF (to be presented before 1 January 2018 based on Article 25 of the MFF Regulation).* *The Commission already committed itself to presenting a medium-term payment forecast (in the framework of the Mid-term review of the financial framework) which will analyse the sustainability of the payment ceilings and evolution of RAL and de-commitments until 2020.*
2.41. Cost claims submitted for cohesion during 2015 fell. This led to a reduction in cost claims awaiting reimbursement, but did not reduce the level of payments made (see paragraphs 2.14 and 2.15).	
2.42. Continuing lengthy delays between initial commitments and final clearings of expenditure means that patterns of spending are slow to respond to changing budgetary priorities and increases the risk that documentation is unavailable at closure (see paragraphs 2.16 and 2.17.	**2.42.** *The delay between commitments and payments are just reflecting the duration of ongoing projects. Some projects are large infrastructure projects in the Union or projects in rather difficult third countries and an average delay of 2,4 years should not be seen as particularly abnormal. The legal framework obliges the beneficiaries to keep the relevant documentation for a certain period after the closure.*
2.43. Outstanding commitments (together with outstanding pre-financing) in ESI Funds of the 2007-2013 MFF for some Member States remain high and frequently exceed 15 % of general government expenditure (paragraphs 2.19 to 2.21).	
2.44. Increasing amounts are held in financial instruments under indirect management, for such the EIB Group remains the preferred financial institution for the management (paragraph 2.23).	
2.45. Unused amounts of the financial instruments under shared management remain high and are concentrated in some Member States (paragraph 2.31).	**2.45.** *See reply to paragraph 2.31.*

THE COURT'S OBSERVATIONS	THE COMMISSION'S REPLIES
2.46. Establishment of EFSI affected the launch of the CEF programme. Although it affects the assumptions the Commission made in its ex-ante assessment of the use of financial instruments under CEF, this was not re-evaluated. EFSI will also impact upon the use made of some other financial instruments (see paragraphs 2.32 to 2.38).	**2.46.** *The adoption of EFSI did not affect the overall objectives of CEF, but created an additional mechanism for the EU financial assistance, i.a. to infrastructural projects, in particular via debt finance. To take into account the launch of EFSI, the CEF DI Steering Committee in its first meeting defined the main principles for providing CEF and EFSI support, with a view to enhance their complementarity. Moreover, an addendum to the CEF* ex ante *assessment is under preparation to reflect (i) the latest analysis on the potential to launch a CEF Equity Instrument in the CEF sectors, and (ii) the market developments post-EFSI launch. This addendum is to be understood as complementing the previous* ex ante *assessment, and not as a revision. The coherence of CEF debt instrument with other EU initiatives, including EFSI, will be assessed in the mid-term review of the CEF.*
Recommendations	
2.47. We recommend that:	
— **Recommendation 1**: the Commission should act to reduce outstanding commitments by, for example, quicker decommitment, where appropriate, faster closure of the 2007-2013 programmes, where appropriate, wider use of net correction in cohesion, reducing cash held by fiduciaries and the compilation of payment plans and forecasts in those areas where outstanding commitments and other obligations are significant (see paragraphs 2.5 to 2.9, 2.19 and 2.28);	*The Commission accepts the recommendation.* *Any measures taken by the Commission vis-à-vis the Member States, including efforts to reduce outstanding commitments and make wider use of net corrections in cohesion must obviously comply with the regulatory framework*
— **Recommendation 2**: the Commission should prepare and publish an annually updated cash flow forecast, spanning a seven to ten year time horizon, covering budgetary ceilings, payment needs, capacity constraints and potential decommitments (paragraph 2.10);	*The Commission accepts the recommendation.* *The forecast for the post-2020 period will be presented in 2017 (as foreseen in point 9 of the Inter-institutional Agreement on budgetary discipline, on cooperation in budgetary matters and on sound financial management) and it will be an integral part of the Commission proposals for the post-2020 MFF (to be presented before 1 January 2018 based on Article 25 of the MFF Regulation).* *In addition the Commission will present a mid-term payment forecast assessing the sustainability of the current payment ceilings until the end of the current MFF in the framework of the Mid-term review of the MFF.*

Thank you for your attention!

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