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NW	Wide
NP	<i>National platform</i>
NW	<i>Network</i>

Hearing on the Financial Regulation at the European Parliament

“ CUTTING RED TAPE: HAS THE REFORM HAD EFFECTS IN DIMINISHING THE ADMINISTRATIVE BURDEN ON NGOS WORKING IN DEVELOPMENT POLICY”?

26 June 2008

Alexandra Mège,
CONCORD Funding Development Relief (FDR) working group

CONCORD'S RECOMMENDATIONS:

On the Financial Regulation and its implementing rules:

- Regroup the amendments to the Financial Regulation and its implementing rules every 3 years so as to ensure a stable contractual environment;
- Revise the Financial Regulation and its Implementing rules to ensure a proportionate control of grant beneficiaries;
- Ensure the eligibility of VAT when it can not be re-claimed regardless of the concerned instruments;
- Authorise the use of actual exchange rates.

On the EuropeAid practical Guide and its annexes:

- Develop a common manual for all users of the practical guide, both for EC Delegations and grant beneficiaries;
- Establish an arbitration mechanism in case of disagreements that can not be solved at Delegations level;
- Go-on and increase regular training provided on the practical guide and its annexes at delegation level and for grant beneficiaries.

CONCORD is the European confederation of relief and development NGOs. Its national associations and international networks represent over 1 600 NGOs which are supported by millions of citizens across Europe. CONCORD leads reflection and political actions and regularly engages in dialogue with the European institutions and other civil society organisations. CONCORD is part of the 'Global Call to Action against Poverty'.

Let me start my presentation to this hearing by introducing myself. My name is Alexandra Mège. I am working for the Handicap International network (present in several European Union's members) and today I will speak on behalf of CONCORD, the European platform of development NGOs. CONCORD actually represents more than 1600 development and humanitarian NGOs throughout the European Union. The total turnover of funding within the CONCORD network amounts to approximately 7 billion of euros per year and there are around 25 million private donors supporting the work of the CONCORD community¹. Within CONCORD, we have set up different working groups, one of them entitled Funding Development Relief (FDR) to which I belong. Within the FDR subgroup we have set up a specific team dealing more precisely with Financial Regulation and EuropeAid's practical guide and its annexes that notably include the grant standard contract.

To address the issue at stake today – ***“has the reform of the financial Regulation had effects in diminishing the administrative burden on NGOs working in development policy”***, I will start with a few preliminary remarks on the principles of the Financial Regulation and how these need to be taken into account in effective implementation of development policy. I will then go on to address on the one hand improvements and problems that are actually linked to the Financial Regulation itself and on the other hand the issue of the varied interpretations of the EuropeAid practical guide and its annexes by the different stakeholders.

1. The Financial Regulation and effective development policy

First of all it should be noted that NGOs appreciate the need for a comprehensive Financial Regulation that ensures financial accountability and best practice. We seek to deliver good quality programmes that respect financial regulations and are accountable to European tax payers, as well as the beneficiary communities we endeavour ourselves to serve.

However, it also needs to be noted that NGOs still identify administrative burden as one of the key barriers to accessing development aid. We are well aware that the control environment has been reinforced throughout the years following the fall of the Santer Commission but a better balance should be sought between operationality and accountability. Furthermore, a review of the financial regulation should not (and does not need to) increase the administrative burden on NGOs, nor does increased administrative burden necessarily lead to increased efficiency, impact or financial rigour. Too much control may even have adverse effects in discouraging smaller and /or less experienced NGOs to apply for EC funding, hence discouraging creativity and renewal within the NGO's world.

Any review and possible changes of the Financial Regulation should be evaluated against the principles of: **economy, efficiency and effectiveness**. We also affirm that *all* the principles are *equally* important and require equal weight. CONCORD together with other NGO platforms produced in 2005 a deep analysis of the 2003 Financial Regulation, which remains valid on some issues and which was pointing out in particular the need to ensure a balance between these 3 principles of economy, efficiency and effectiveness (this is the report entitled “Striking a Balance - Efficiency, Effectiveness and Accountability – The impact of the EU Financial Regulation on the relationship between the European Commission and NGOs”²).

¹ Source: 2005 CONCORD survey "Insights into the objectives, structures, funding and capacities of CONCORD's wide membership

² Report by F.M. Partners Limited on behalf of Open Society Institute Brussels, CONCORD, the platform of European Social NGOs, SOLIDAR and the European Women's lobby, April 2005.

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2. Remarks on the Financial Regulation and its implementing rules

a. Important improvements for NGOs

Some improvements were brought by the 2007 revision of the Financial Regulation. Let me mention 3 important examples from an NGO's perspective :

- **First: the explicit eligibility of sub grants to third parties** (within the limit of 100.000 euros per action and maximum 10.000 euros per organization)

Financial Regulation n°1995/2006:

Article 120

(...)

2. Where implementation of the action requires financial support to be given to third parties, the beneficiary of a Community grant may give such financial support provided that the following conditions are met:

(a) the financial support is not the primary aim of the action;

(b) the conditions for the giving of such support are strictly defined in the grant decision or agreement between the beneficiary and the Commission, with no margin for discretion;

(c) the amounts concerned are small.

For the purpose of point (c), the maximum amount of financial support that can be paid to a third party by a beneficiary shall be determined in the implementing rules.

Implementing rules n°478/2007:

Article 184 a

Financial support to third parties

1. Provided the objectives or results to be obtained are sufficiently detailed in the conditions referred to in Article 120(2)(b) of the Financial Regulation, the margin of discretion may be considered to be exhausted if the grant decision or agreement also specifies:

(a) the minimum and maximum amounts of financial support that can be paid to a third party and criteria for determining the exact amount;

(b) the different types of activity that may receive such financial support, on the basis of a fixed list.

2. For the purpose of Article 120(2)(c) of the Financial Regulation, the maximum amount of financial support that may be paid to third parties by a beneficiary shall be EUR 100 000, with a maximum of EUR 10 000 per each third party.'

- **Secondly: higher thresholds for procurement** (single quote up to 10.000 euros and negotiated procedure of 3 quotations up to 60.000 euros)

Implementing rules n°478/2007:

In Article 241(1), the second subparagraph is replaced by the following:

'Contracts with a value of less than or equal to EUR 10 000 may be awarded on the basis of a single tender.'

(...)

Article 243(1) is amended as follows:

(a) point (b), 'EUR 30 000' is replaced by 'EUR 60 000'.

(b) point (c) is replaced by the following:

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'(c) for contracts with a value of less than EUR 60 000: competitive negotiated procedure within the meaning of paragraph 2.'

(c) the second subparagraph is replaced by the following:

'Contracts with a value of less than or equal to EUR 10 000 may be awarded on the basis of a single tender.'

(...)

In Article 245(1), the second subparagraph is replaced by the following:

'Contracts with a value of less than or equal to EUR 10 000 may be awarded on the basis of a single tender.'

- **Thirdly: the possibility for grant beneficiaries to keep the amount of interests accrued on EC pre-financing:**
 - o For projects in non crisis situations :
 - For an EC pre-financing below 250.000 euros, the organisation can keep the interest earned;
 - For an EC pre-financing between 250.000 euros and 750.000 euros, the organisation has to pay back the EC the interests earned only at the end of the action;
 - For an EC pre-financing above 750.000 euros, the organisation has to pay back the EC the interests earned after each fiscal year.
 - o For projects within crisis situations:
 - for an EC pre-financing below 750.000 euros, the interests can be used by the organisation (with the exclusion of projects implemented within ENPI).
- In all cases, it includes interests received by implementing partners, if applicable.

Financial Regulation n°1995/2006:

Article 5a

1. Interest generated by pre-financing payments shall be assigned to the programme or the action concerned and deducted from the payment of the balance of the amounts due to the beneficiary. The Regulation laying down the rules for implementing this Regulation, hereinafter "the implementing rules", shall specify the cases in which the authorising officer responsible shall, by way of exception, recover annually such interest. That interest shall be entered in the budget as miscellaneous revenue.

2. Interest shall not be due to the Communities in the following cases:

(a) pre-financing which does not represent a significant amount, as determined in the implementing rules; (...)

Implementing rules n°478/2007:

Article 3

2. (...) However, for external actions pre-financing shall be regarded as representing a significant amount if the amount is higher than EUR 250 000. For crisis management aid and humanitarian aid operations, prefinancing shall be regarded as representing a significant amount if it exceeds per agreement EUR 750 000 at the end of each financial year and is for projects of a duration of more than 12 months.

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b. Issues still to be tackled

That being said, some issues do add a lot of administrative and technical burden to the daily work of NGOs. And the European Parliament has the leverage and ultimately the power to address them in a future revision of the Financial Regulation and its implementing rules.

Beyond the 3 points that I am going to outline, allow me first to emphasize that the **first and foremost need of all stakeholders is a reasonably stable contractual environment**. It is indeed extremely difficult for operators to implement their mandate in an ever-changing Financial Regulation and its relating implementing rules. Actually, according to our understanding the FR's implementing rules were amended already 3 times since 2003 (on 20 July 2005, 7 August 2006 and 23 April 2007), and that means that all the relating guide and procedures that EuropeAid refers to also had to be adapted accordingly.

And as far as NGOs are concerned, we have had to adapt ourselves to 4 versions of the grant standard contract over the last 2 years (February 2006, August 2006, May 2007, revision in December 2007) and a fifth version is again expected in 2008.

All these different versions contain different rules and provisions. For NGOs at large, but especially for small and medium ones, it is almost impossible to catch up and being updated on the different applicable rules. Honestly, this is also very problematic and cumbersome for EC Delegations themselves who tend to get confused on the applicable provisions for each grant agreements and to request elements that were not in force at the time of signing the grant.

Whilst we appreciate the need for flexibility and adaptation of the rules and procedures, especially where it takes into account feedbacks from stakeholders, our mandate also requires a sufficiently stable contractual environment to operate effectively. It is our belief that this requirement applies to all contractors implementing projects benefiting from EC funding.

Regarding the 3 issues that should be improved, we would like to mention:

- **the whole control process,**
- **the VAT issue,**
- **exchange rates.**

- Control process (audit, list of expenditures and reporting per currency)

Since 2003, we have noticed a significant administrative burden linked to control issues. This takes the form of **ex post control** with external audit requirements, which are more and more constraining to reflect the amendments brought to article 180 of the implementing rules. But since 2006 it also includes more and more **ex ante control** with the obligation to annex a list of all expenditures detailing each expense incurred for the period covered by the report. It means that, in addition to the financial report, we need to provide for each single expenditure : the wording of the expenditure, the amount, the concerned budget heading as well as the reference of the supporting document. And as we need to have cross-references to the financial report provided, it forces us to go through a significantly time consuming administrative work to extract and organise all the datas from our accountancy books.

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In addition, we have the obligation, from 2006, to provide our financial report in the different currencies used within the granted project. When considering activities in developing countries, you could sometime have to deal with up to 4 or more currencies involved. I believe you will agree that this constraint represents for us a tremendous work.

So even if the list of expenditures and the obligation to report by currency did not derive directly from the Financial Regulation and its implementing rules, we really request the European institutions to **take into account the principle of proportionality as mentioned in the Financial Regulation when considering all these control issues, and also in any future revision of article 180 of the implementing rules for audit requirements.**

- ***Eligibility of VAT costs***

We believe that the Financial Regulation should make the cost of VAT eligible whenever it can not be reclaimed, and this regardless of provisions from other Regulations. We actually face this problem with the Regulation of the DCI Instrument, which does not authorise the eligibility of VAT in any case.

Article 25.2 of the DCI Regulation: *“Community assistance shall not be used for paying taxes, duties or charges in beneficiary countries.”*

We have just discovered this issue during a meeting last April with EuropeAid, and I must say that this particular point is really going to create problems. There will be many cases where NGOs will be refused tax exemption in developing countries, therefore leading to the question of “who is going to pay for these taxes if the Regulation does not permit it”? Ultimately it will have to be supported by grant beneficiaries, a situation which is hardly understandable and acceptable. Since we understand that it is more a political issue than a technical one, I urge you to take into consideration this problem with the view to adapt the DCI regulation and the Financial Regulation accordingly.

Implementing rules n°478/2007:

Article 172a:

Without prejudice to paragraph 1 and to the basic act, the following costs may be considered as eligible by the authorising officer responsible: (...) value added tax paid, and which cannot be refunded to the beneficiary according to the applicable national legislation; (...)

- ***Possibility to use actual exchange rates of the grant beneficiary:***

The Financial Regulation and its implementing rules should allow grant beneficiaries to use actual exchange rates. First it would avoid NGOs to bear the financial risk associated to exchange rate variations and it will enable reconciliation between financial reports provided to the EC and the accountancy of the grant beneficiaries.

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RECOMMENDATIONS:

- **Regroup the amendments to the Financial Regulation and its implementing rules every 3 years so as to ensure a stable contractual environment;**
- **Revise the Financial Regulation and its Implementing rules to ensure a proportionate control of grant beneficiaries;**
- **Ensure the eligibility of VAT when it can not be re-claimed regardless of the concerned instruments**
- **Authorise the use of actual exchange rates.**

3. Interpretation issues on the EuropeAid Practical Guide and its annexes

Finally I would like to say a few words on the EuropeAid Practical guide and its annexes. In their daily work, development NGOs refer mainly to the EuropeAid practical guide instead of the Financial Regulations or its implementing rules. The EuropeAid Practical Guide is actually the explanation and interpretation of the Financial Regulation, Implementing rules and of other relevant legal basis for the activities and projects implemented or supported by EuropeAid funding. The core Practical Guide essentially deals (except for some instructions related to amendments to contracts) with the award phase of contracts. There is no practical guide on agreed upon guidelines regarding the execution phase of contracts, which is often the critical part.

The main difficulties that development NGOs encounter lie with **interpretation issues of the applicable rules**. Even if the deconcentration of the grant management to EC Delegations in the field has enabled some improvements - in particular an increase in understanding and rapidity of responses from the Delegation staff - it has also increased the divergence of interpretation of the same rules between the different services of EuropeAid and the EC Delegations. Ultimately, grant beneficiaries bear the increased administrative burden and financial risks associated with these variable interpretations.

I would like to underline the very good collaboration CONCORD has with unit G7 of DG EuropeAid (Financial and contractual matters and legal affairs). Based on the results of our discussions, CONCORD FDR sub group has been able to draft a reader on how to interpret the different applicable provisions to grants.

That being said, we recommend that European Commission:

- **Develop a common manual for all users of the practical guide, both for EC Delegations and grant beneficiaries.** CONCORD has been able so far to elaborate its own reader with the recognition of DG EuropeAid but we believe it would be much more efficient if such a manual would directly be issued by the relevant European Commission' services. Written guidance from the EC would allow a standardization of approach across Delegations, enable faster decision-making and ultimately more timely project implementation. CONCORD would certainly be willing to provide a constructive input to this work.

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Alternatively, CONCORD would suggest that the reader be endorsed by the Director General of EuropeAid and annexed to the core text of the Practical Guide as common guidance for all users.

- We recommend the European Commission to establish an arbitration mechanism in case of disagreements that can not be solved at Delegations level. The current system to refer to geographic directions of EuropeAid has proved to be inefficient. The establishment of clear lines of authority for arbitrations of disagreements, in particular over interpretation of rules is of paramount importance in our opinion.

- We do recommend to the EC to sustain and reinforce regular training provided on the practical guide and its annexes, both for Delegation personnel and grant beneficiaries.

To conclude, I would like to re-iterate CONCORD's willingness and commitment to continue to develop a real and fruitful partnership with the different EC Services dealing with external actions and in particular with EuropeAid. I thank you very much for your attention.

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