



REPLIES OF THE EUROPEAN COMMISSION

TO THE EUROPEAN COURT OF AUDITORS' SPECIAL REPORT

Verification of gross national income for financing the EU budget: risks in data compilation well covered overall, but scope for increased prioritisation of actions

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This document presents the replies of the European Commission to observations of a Special Report of the European Court of Auditors, in line with Article 259 of the [Financial Regulation](#) and to be published together with the Special Report.

EXECUTIVE SUMMARY (I-IX)

Commission replies:

I. The Gross National Income (GNI) data and the sources and methods used by the Member States to calculate them are verified by Eurostat in multiannual cycles and on annual basis as well. The objective is to ensure that the GNI data are reliable, exhaustive and comparable across Member States. The last completed verification cycle, that is subject to this ECA's audit, took place in the years 2016-2019. The verification is based on a model established by the Commission (Eurostat) in close cooperation with experts from Member States' national statistical institutes (NSIs). Eurostat is assisted in its verification by the GNI Expert Group (GNIG), which brings together Eurostat and NSIs experts. The whole verification process is subject to peer review by the GNIG members. Every year GNIG issues an opinion on the appropriateness of the GNI data, which are then used by DG Budget for the purpose of the Member States' contributions to the EU budget under the GNI own resource.

III. Eurostat's verification cycle comprises a thorough analysis of the Member States' GNI Inventories of sources and methods and detailed analysis of the GNI data reported by Member States, possibly leading to action points or reservations to ensure comparability, reliability and exhaustiveness of those data. The results from this verification work are taken into account for budgetary purposes. While Eurostat has, together with Member States, already reduced the length of the GNI verification cycle, this work necessitates sufficient time in order not to compromise its scope and quality.

VI. The Commission welcomes the ECA's conclusions that the verification process was effective. The identified high-risk issues were targeted through the cross-country comparisons and through placing of transversal reservations. Eurostat carried out all 16 cross-country comparisons in a timely manner during the 2016-2019 cycle, and the Commission considers this as a major achievement. The five transversal reservations were set at the end of the cycle, at the same time as the transaction-specific reservations. Given the above, it is the Commission's view that the high-risk issues identified during the 2016-2019 GNI verification cycle were overall targeted in a timely manner.

VII. The work on high-risk transversal issues reflected the results of the relevant prioritisation exercise carried out by Eurostat. As a result, two issues with lower potential impact were dropped and the scope of the analysis was narrowed for another three issues. The remaining issues were assessed as deserving the same high level of scrutiny. The results and consequences of the prioritisation exercise were reported to and approved by the GNI Committee.

The Commission considers that all the initiatives reported by the ECA in the paragraph 69, together with the work undertaken by the Member States within the GNI reservation on globalisation, ensured adequate response to this issue.

VIII. Eurostat welcomes the ECA's acknowledgement of the timely completion of the GNI verification cycle and of the provision of timely information to the Member States on the adjustments to their contributions resulting from that verification. The scope of Eurostat's checks was determined by the GNI verification model designed in a close cooperation with, and approved by, the GNI Committee. In the 2016-2019 GNI cycle, there was a need for enhanced scrutiny due to the implementation of the new national accounting standard, ESA 2010.

With regard to the reservations being in place after the completion of the verification cycle, the Commission notes that this is a normal feature of the GNI verification process.

The Commission acknowledges that application of the materiality threshold in the GNI verification has its limitations, as in many cases the potential impact of the identified deficiencies on GNI is not known at the time of their identification.

IX. The Commission accepts all the recommendations except for the sub-recommendation 2b which it partially accepts.

INTRODUCTION (Paragraphs 1-26)

No Commission replies.

AUDIT SCOPE AND APPROACH (Paragraphs 27-35)

No Commission replies.

OBSERVATIONS (Paragraphs 36-104)

Commission replies:

39. The Commission welcomes the ECA's recognition of the GNI risk assessment model and of its role in the adequate identification of all high-risk issues. It should be noted that apart from consequences for direct verification, assigning Member States to three risk categories within the risk assessment model had further consequences for structuring the GNI verification cycle. These included the order/prioritisation of the verification of the individual countries, its scope, as well as minimum number of GNI information visits per country.

44. Eurostat used information gathered through its initial verifications to reassess the risk level and estimate the potential impact of the 18 transversal issues identified in 2016. The Commission considers the re-assessment of risk level carried out in 2017 as an important evidence of prioritisation, following which the less risky transversal issues were given less attention in the subsequent verification. The remaining issues were assessed as deserving each the same high level of scrutiny, which in the Commission's view positively contributed to the assurance of the appropriateness of the GNI data for own resource purposes.

45. An important consequence of the prioritisation exercise of the high-risk transversal issues was also the confirmation that a big majority of the issues initially identified for cross-country comparisons should indeed be followed up through detailed checks across countries. Eurostat timely completed all cross-country comparisons during the cycle, which led to subsequent improvements in these areas through action points and/or reservations solved by the Member States.

Common reply to 46 and 47: The Commission notes that the ECA's analysis of the action points "A" only took into account the impact from the action points satisfactorily addressed by Member States. It did not take into account the impact of reservations that were placed when the action points had not been satisfactorily addressed, as this information was not available at the time of the audit. It is plausible to assume that impacts from the respective reservations will be higher than for the action points.

The Commission notes that the selected Member States account for one quarter of the action points resulting from cross-country comparisons.

48. Following the 2017 prioritisation exercise for transversal issues, the whole risk assessment was subject to another review in 2018, in line with the approach agreed in the GNI Committee. For each Member State the scores for individual criteria, where appropriate, were updated as new information became available. This update did not result in any need for changes to the list of transversal issues or their further prioritisation.

50. With respect to the planning and prioritisation of checks, the risk level determines the start of verification (and the order of checks by the individual country officers). In addition, it was planned from the outset that consecutive rounds of visits to countries (where appropriate) may be carried out until December 2019 (document GNIC/332 "Verifying GNI for own resource purposes – outline of the control approach"), which may influence the timing of the placement of action points for countries that are subjects to several visits.

51. The Commission notes that this analysis is based on the time of placing action points and does not take into account the preceding steps, like filling of the GNI Inventory Assessment Questionnaire, formulation of the questions and initial assessment of the replies from the Member States, organisation of the information visits etc. Those other steps may further evidence the prioritisation of the checks for high-risk countries by Eurostat.

53. The prioritisation of the country checks by Eurostat was based on the results of the risk assessment model and other relevant framework documents. Country officers overall prioritised their checks (including organisation of GNI information visits) according to the risk levels of countries in their portfolio.

Furthermore, the decreasing trend of placing action points shows that Eurostat strove to place action points as early as possible in the process.

56. GNI components for direct verification were selected in accordance with the respective framework documents, namely the document GNIC/333 regarding Risk assessment model for verification of GNI for own resource purposes and the document GNIC/334 providing the Guidelines for direct verification.

The results of the second part of the risk assessment do not oblige the country officer to choose for direct verification the areas with the highest scores. Risk assessment (second part) is a tool that facilitates the choice – results in a pool to choose from – but does not ultimately determine it. The selection of each area of direct verification was based on the risk assessment in place, qualitative reflection of the country officer and consultation of the team leader of the GNI team.

58. Each action point was agreed between Eurostat and the Member State concerned. This agreement included a deadline to be respected which is de-facto a prioritisation of the work, taking

into account several factors, such as availability of statistical sources, complexity of the issues at stake, revisions, timetables, burden and workload, etc.

59. The Commission considers that Member States are well placed to judge the complexity and potential impact of action points and to plan and prioritise the work on them accordingly where needed, in agreement with Eurostat. This practice was followed throughout the verification cycle.

62. The Commission welcomes the Member States' appreciation of the quality of cooperation and of the guidance provided in the GNI verification process.

63. The two issues relating to Margins on trading financial assets and to the treatment of Daily allowances are very complex subjects for which time was needed by the experts concerned (ECB experts for Margins on trading financial assets and Eurostat experts for the treatment of Daily allowances respectively) to develop clear and operational guidelines which the countries need in order to address the reservations.

The Commission takes note of some NSIs' suggestions but is of the opinion that the relevant guidance, e.g. in form of the GNIC/GNIG recommendations, has already been provided as part of the GNI OR verification process and through relevant channels.

66. Globalisation related issues have been addressed by Eurostat since many years from a business statistics perspective (e.g. focusing on asymmetries in trade flows and micro-data linking) which has contributed to the improvement of the underlying infrastructure to measure globalisation within the national accounts. However, the major GNI-impacts came from sudden and large changes in MNEs' business models after EU Regulatory/tax changes in the mid-2010s, affecting some Member States in particular, such as a relocation of entire balance sheets as shown by the Irish case reported in the ECA's paragraph 68.

67. There was a slow evolution of MNE business models in the EU over many years until some quite big changes in a few large MNEs in the period 2014 onwards. In particular, the abolition of some tax minimisation arrangements, and changes in the EU's VAT regime, led to rapid changes in some MNE's business models.

70. The application of the globalisation reservation has been discussed with the Member States in the meetings of the GNI Expert Group. During these discussions, the year 2016 was put forward as possible starting reference year. However, several Member States objected to that solution, arguing that it was too far away in the past and stressing the practical impossibility of getting the required additional information for 2016 from MNEs, in the light of their experience from the GNI Pilot exercise. Taking that situation into account, relevant evidence from the GNI MNE Pilot exercise, the potential problems of coverage and reliability and the burden for MNEs and NSIs, the Commission has decided on 2018 as a starting reference year.

71. The Commission considers that the timing of the reservation on globalisation, i.e. covering the years 2018 onwards, is appropriate. The Commission services reiterate that in their view the approach and timing thoroughly discussed in dedicated meetings with the NSIs are sound and proportionate, they are based on the risks assessed and they are fully consistent with the assurance already gathered. The Commission did not accept the related part of the ECA's recommendation in the 2020 Statement of Assurance report and maintains its position in this respect.

72. The potential impact on GNI of the transversal issue of globalisation was assessed in the context of the risk analysis of transversal issues with the view to prioritise the work on these issues (and consequently, the work on globalisation was given high priority). The main factor taken into account at that time was the magnitude of the phenomenon of globalisation, as there was no evidence available from dedicated analyses of potential distortions to value added and GNI due to possible deficient treatment of globalisation in national accounts.

At the time of placing the transversal reservation, such evidence was however available and taken into account. According to the findings of “Report on the GNI MNE Pilot Exercise” (November 2019), no evidence of major distortions to value added was identified from the scrutiny of the MNEs (the year on which the approach followed in the MNE pilots was based was 2016).

73. “Significant impact on national accounts” of globalisation does not necessarily lead to distortions to GNI to be addressed through reservation.

From the work undertaken so far, e.g. within the GNI MNE Pilot, there is no evidence of major distortions to GNI due to possible deficient treatment of these issues in national accounts.

It should be noted that the “Irish case” itself was correctly treated according to the conceptual guidance (meaning that the established compilation system correctly captured and reflected the existence of the phenomenon in question in the GNI data).

Concerning the results of the work on their reservations transmitted by one Member State in September 2021, the relevant reports are being analysed by Eurostat.

75. The Commission reiterates that the scope and the period covered by the reservation on globalisation were thoroughly discussed with the Member States in the meetings of the GNI Expert Group and that they reflect the opinions expressed during these discussions.

77. The Commission completed all verifications as planned, i.e. by the end of 2019. In the specific case of France, the completion of the verifications could not be finalised by the end of 2019 because of the non-availability of the French GNI Inventory of sufficient quality that was kept under a general reservation. The French GNI Inventory was transmitted in March 2020, checked and the general reservation was lifted in 2021.

With regard to the reservations being in place after the completion of the verification cycle, the Commission notes that this is a normal feature of the GNI verification process.

83. In relation to the materiality threshold, the GNI Committee approved the materiality threshold of 0.1% of GNI proposed by Eurostat in October 2014. As the ECA’s survey to NSIs confirms (see paragraph 86), this threshold is perceived as adequate by large majority of the Member States.

85. As the framework document on Materiality threshold (GNIC/283) mentions in paragraph 5, *“In principle, the threshold could be fixed as a value or as a percentage. From the two possible options, Eurostat clearly prefers the percentage, as using a value could, for small countries, lead to an insignificance conclusion for almost all issues.”*

89. The NSIs drew up their GNI inventories following the GNI Inventory Guide, one of the framework documents prepared by Eurostat and agreed on by the GNI Expert Group. It is left at the

discretion of the Member States if they use the opportunity to skip the description of a given item, under the conditions given in the Guide.

90. When formulating the questions to the NSIs, Eurostat desk officers followed the GNI Inventory Assessment Questionnaire (GIAQ), one of the framework documents prepared by Eurostat and agreed on by the GNI Expert Group.

91. In line with the “Outline of the control approach” (GNIC 332), the practice of placing of action points and reservations was as follows: if evidence existed that the possible impact of the identified deficiency was below the materiality threshold no action point or reservation was placed on this deficiency. Eurostat followed this practice throughout the 2016-2019 GNI verification cycle in all its main verification tools (GNI Inventory Assessment Questionnaire (GIAQ), information visits, direct verifications, cross-country comparisons).

For most of the action points placed, there had been no estimate of potential impact of the issue at stake on GNI available at the moment of placing – meaning that one could not exclude material impact.

The Commission considers that Member States are best placed to provide information on non-materiality. If action points were placed this means that full evidencing of non-materiality was not readily available.

An existing action point or GNI reservation where the (possible) impact on GNI had not been known at the time of placing could be lifted if evidence of non-materiality was provided.

92. The Commission observes that the results of the ECA’s analysis described in paragraph 92 mean that for as many as 25% of the examined cases of action points where the initial impact indicated by the countries was thought to be non-material, the final impact proved to be material.

93. The Commission reiterates its position that the application of the materiality threshold occurred throughout the 2016-2019 GNI verification cycle, including at an early stage of the verification, in cases where the full evidencing was readily available.

94. When an action point A was agreed between Eurostat and the Member State concerned, a possible improvement of methodology was required. At the time of such an agreement, generally the Member States either could not provide full evidence allowing to exclude materiality of the issues at stake or preferred to clarify the respective methodology first.

In the context of the GNI verification, the Member States are best placed (at any stage of the verification process) to provide evidence and demonstrate that an issue is not material. On that basis Eurostat then assesses the solidity of the evidence. During the 2016-2019 GNI verification cycle, where full evidence was provided by the Member States that the impact of the deficiency was not material, no action points or reservations were issued.

95. In 2014, the new accounting standard, ESA 2010, was implemented in the national accounts of the Member States. Therefore, the 2016-2019 cycle was particularly challenging, and it involved a number of new elements, such as risk assessment, cross-country analyses of some horizontal issues, enhanced use of direct verifications etc. This enhanced scrutiny resulted in a high number of action points and reservations and in a related high workload for both Eurostat and the countries. [In the Commission’s view this effort was necessary to attain the ultimate goal of the GNI

verification process, which is to give reasonable assurance on the quality of the GNI data used for own resource purposes.]

96. Eurostat's reservation database contains where available a rough assessment of the impact/potential impact of the reservation on GNI. The exact final impact on GNI and its components is part of the technical opinion on lifting reservations for all years under reservations. In most cases, no detailed information about impact on GNI is available at the time of encoding the reservation, the country reservation files/database are continuously updated and the final impact is encoded in technical opinion.

Eurostat has however taken steps to facilitate an overview of the impact on GNI of the action points and reservations placed and addressed during the cycle 2020-2024.

97. A high number of reservations resulting from action points analysed (24 out of 130 action points) means that the final average/median/maximum impact from the issues covered by action points analysed for the six countries will most probably be higher (and the share of points with no impact will be lower). It is plausible to assume that the points transformed into reservations concern more complex and/or bigger issues than the points that could be addressed and closed and will therefore lead to bigger revisions.

99. At the time of the audit only a small proportion of the reservations was lifted. A high number of reservations that were still pending means that the final average/median/maximum impact from the issues covered by reservations will most probably be even higher (and the share of reservations with no impact will be lower). It is plausible to assume that the reservations that are still pending concern more complex and/or bigger issues than the ones that could be addressed and closed quickly and may therefore lead to bigger revisions.

102. The Commission would like to point out that GNI verification is a highly complex process and its documentation reflects this complexity. Eurostat defined the documentation standards for this process in "Documentation guidelines (GNIC/335)" approved by the GNI Committee with the view to properly document each stage of the verification. It is the Commission's view that, despite the acknowledged complexity of the documentation, the guidelines for it were followed and it served its purpose well (e.g. ensuring operational continuity over time and allowing management to perform its oversight roles).

104. Eurostat took steps to further enhance and standardise the documentation of the GNI verification work in the cycle 2020-2024 (e.g. by revising the documentation guidelines, adding instructions on how to fill in GIAQ, designing the common template for the log-files to further augment the homogeneity of the documentation, integrating information on the action points, reservations, non-material issues for follow-up, including the impacts on GNI, in the log files, etc.)

CONCLUSIONS (Paragraphs 105-109)

106. The Commission considers that overall, there was a prioritisation of the order and scope of the checks in the countries based on the results of the risk assessment and the work on transversal issues clearly reflected the results of the relevant prioritisation exercise (see also replies to paragraphs 44-48, 50, 51 and 53).

The selection of each area of direct verification was based on the risk assessment in place, qualitative reflection of the country officer and consultation of the team leader of the GNI team at Eurostat, as foreseen by the relevant framework documents. The Commission considers that the documentation of the GNI verification process is already very comprehensive in this respect (see also replies to paragraph 56).

During the 2016–2019 verification cycle, while there was no formal establishing of priority levels of action points (apart from distinguishing between action points A and B), the prioritisation of the work on action points was enforced through setting different deadlines for individual points, in agreement between the Member States and Eurostat. This agreement included a deadline to be respected which is de-facto a prioritisation of the work, taking into account several factors, such as availability of statistical sources, complexity of the issues at stake, revisions, timetables, burden and workload, etc. (see also replies to paragraphs 58 and 59).

Recommendation 1- Increase prioritisation of high-risk issues

The Commission accepts recommendation 1 a).

The Commission accepts recommendation 1 b). The Commission will strive to further prioritise and streamline the future GNI cycles in this regard, in line with the ECA's recommendations.

The Commission accepts recommendation 1 c). The Commission will continue to monitor and improve its documentation of selection of areas for direct verification taking also into account the recommendation from the ECA relating to documentation.

The Commission accepts recommendation 1 d). The Commission will investigate in cooperation with Member States possible ways of further improving prioritisation of the work on action points.

107. The Commission notes the satisfaction of the countries with the adequacy and timeliness of Eurostat's guidance on transversal issues, as reported by the ECA (see paragraphs 61 and 62).

Eurostat, together with the Member States, made extensive efforts to tackle the issue of globalisation. The Commission considers that all the initiatives reported by the ECA in the paragraph 69 ensured a timely and adequate support to the countries on this issue (see also replies to paragraphs 66 and 67).

Concerning the impact of globalisation on GNI, the Commission considers that the application of the reservation on globalisation to the years from 2018 onwards is appropriate. In the Commission's view the approach and timing, thoroughly discussed in dedicated meetings with the NSIs, are sound and proportionate; they are based on the risks assessed and they are fully consistent with the assurance already gathered. From the work undertaken so far, e.g. within the GNI MNE Pilot, there is no evidence of major distortions to GNI due to possible deficient treatment of these issues in national accounts (the year on which the approach followed in the MNE pilots was based was 2016).

Recommendation 2 - Improve the timeliness of the support provided to Member States and better justify decisions to limit the period of application for reservations

The Commission accepts recommendation 2 a). The Commission notes the satisfaction of the countries with the adequacy and timeliness of Eurostat's guidance on the high-risk issues and it will strive to further provide such support by considering the ECA's recommendation.

The Commission partially accepts recommendation 2 b). The Commission agrees to provide adequate justification for the periods covered by the future reservations, where appropriate. The Commission considers that adequate analysis and justification were given in the case of the reservation on globalisation that is underlying this recommendation of the ECA. While the Commission agrees that the periods covered by the reservations should be adequately justified, it considers that carrying out even deeper analyses (than in the reported case of globalisation) in this context would not lead to cost-effective use of resources. Therefore, the Commission rejects the part of the sub-recommendation that calls for such far-going analyses.

109. With regard to the reservations being in place after the completion of the verification cycle, the Commission notes that this is a normal feature of the GNI verification process.

The scope of Eurostat's checks was determined by the GNI verification model designed in a close cooperation with and approved by the GNI Committee. In the 2016-2019 GNI cycle there was a need for enhanced scrutiny due to the implementation of the new national accounting standard, ESA 2010.

The Commission acknowledges that application of the materiality threshold in the GNI verification has its limitations, as in many cases the potential impact of the identified deficiencies on GNI is not known at the time of their identification.

Recommendation 3 - Further improve the efficiency of the verification cycle

The Commission accepts recommendation 3 a). The Commission notes the positive opinion of the Member States expressed in the ECA's survey concerning the current level of the materiality threshold. Nevertheless, the Commission will strive to further improve the efficiency of the verification cycle, in close cooperation with the GNI Expert Group, by analysing the appropriateness of the current level of materiality threshold.

The Commission accepts recommendation 3 b). The Commission will discuss with Member States possible ways to better integrate the concept of materiality into the verification work in the future cycles.

The Commission accepts recommendation 3 c). Eurostat has already taken some steps to enhance and standardise the documentation of the GNI verification work in the cycle 2020-2024 that go in the direction recommended by the ECA and it will analyse the possibility of further improvements in this regard.