

**ANNUAL REPORT ON THE ACTIVITIES
FUNDED BY THE SEVENTH, EIGHTH, NINTH
AND TENTH EUROPEAN DEVELOPMENT
FUNDS (EDFS)**

(2009/C 269/02)

Annual Report on the activities funded by the seventh, eighth, ninth and tenth European Development Funds (EDFs)

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THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

INTRODUCTION

1. The European Development Funds (EDFs) are the result of international conventions or agreements ⁽¹⁾ between the Community and its Member States, on the one hand, and certain African, Caribbean and Pacific (ACP) States, on the other hand, and of Council Decisions on the association of overseas countries and territories (OCT).

2. The Commission has responsibility for and takes charge of the management of most of the expenditure of the EDFs. The EDF's investment facility has been fully managed by the European Investment Bank (EIB) since 1 April 2003. This facility is not covered by the Court's Statement of Assurance or the European Parliament's discharge procedure ⁽²⁾ ⁽³⁾.

3. The structure of the EDF is presented in **Diagram 1**. The EDFs are managed under different arrangements: the centralised, joint and decentralised management modes ⁽⁴⁾. In the centralised management mode, the Commission manages contract award procedures and payments to final beneficiaries itself. In the joint management mode, certain implementation tasks are entrusted to international organisations provided that the accounting, audit, control and procurement procedures of the organisations offer guarantees equivalent to internationally accepted standards. In the decentralised management mode, the daily management is ensured by the National Authorising Officer (NAO) ⁽⁵⁾ of each beneficiary country and the Commission (see **Diagram 2**). They are responsible for:

- (a) checking regularly that operations have been properly implemented;
- (b) taking appropriate measures to prevent irregularities and serious non-compliance with laws and regulations and, if necessary, bringing prosecutions to recover funds wrongly paid.

⁽¹⁾ The Yaoundé I Convention dates back to 1964. The most recent agreement (Cotonou) dates from 23 June 2000 and was revised on 25 June 2005.

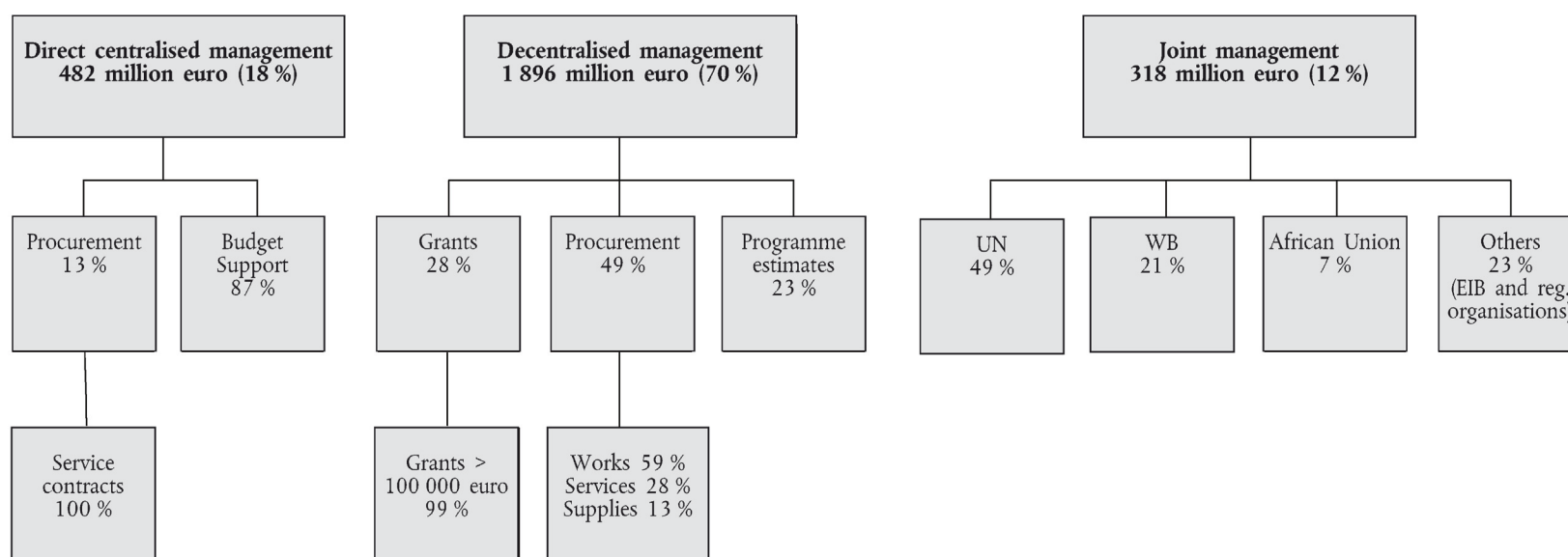
⁽²⁾ See Articles 118, 125 and 134 of the Financial Regulation of 18 February 2008 applicable to the tenth EDF (OJ L 78, 19.3.2008). In its Opinion No 9/2007 on the proposal for this Regulation (OJ C 23, 28.1.2008), the Court stressed that these provisions reduce the scope of the European Parliament's powers of discharge.

⁽³⁾ A tripartite agreement between the EIB, the Commission and the Court (Article 134 of the Financial Regulation of 18 February 2008 applicable to the tenth EDF referred to above) sets out rules for the audit of these operations by the Court.

⁽⁴⁾ Articles 21 to 29 of the Financial Regulation applicable to the tenth EDF.

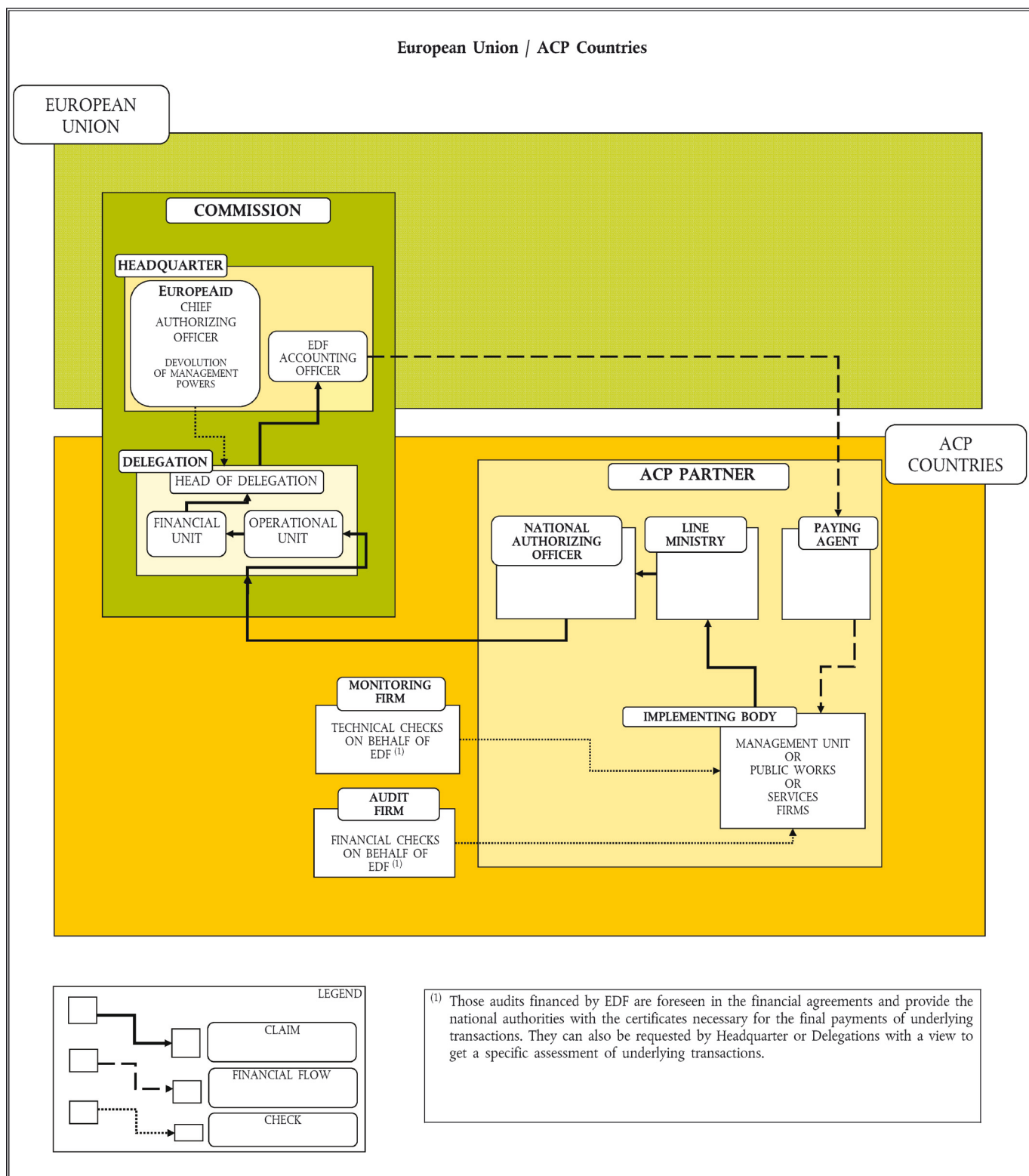
⁽⁵⁾ Cotonou Agreement, Annex IV, Article 35.

Diagram 1 — Structure of the EDF (in terms of contract value)



Source: AIDCO Annual Activity report for 2008 (Annex 5 - Internal Control Templates).

Diagram 2 — Principle of decentralised management



THE COURT'S OBSERVATIONS

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4. Within the Commission, almost all of the EDF programmes are managed by the EuropeAid Cooperation Office (hereinafter called EuropeAid), which is also responsible for the management of most of the External Relations and Development expenditure financed by the General Budget of the European Union ⁽⁶⁾. A small proportion of the EDF projects ⁽⁷⁾ relates to humanitarian aid and is managed by the Directorate-General for Humanitarian Aid (DG ECHO).

CHAPTER I — IMPLEMENTATION OF THE SEVENTH, EIGHTH, NINTH AND TENTH EDFs

Financial implementation

5. In 2008, the seventh, eighth, ninth and tenth EDFs were implemented simultaneously. The Authorising Officer of the EDF closed the seventh EDF on 31 August 2008 ⁽⁸⁾. At closure 10 381 million euro had been paid (98,3 % of the 10 559 million euro allocated to aid measures). The balance of 178 million euro was transferred to the ninth EDF.

6. The tenth EDF covering the period from 2008 to 2013 and providing for Community aid of 22 682 million euro entered into force on 1 July 2008. Of this amount, 21 966 million euro is allocated to the ACP countries, 286 million euro to the OCTs. These amounts include 1 500 million euro and 30 million euro to the Investment Facility managed by the EIB for the ACP countries and OCTs respectively. Lastly, 430 million euro are foreseen for the Commission's expenditure for programming and implementation of the EDF.

7. **Table 1** shows the cumulative use of EDF resources managed by the Commission and their financial implementation. **Charts I** and **II** show the cumulative resources and cumulative decisions by sector of intervention. In 2008 the financial implementation forecasts set by the Commission for global commitments, individual commitments and payments were all exceeded, reaching record levels for global commitments (4 723 million euro), individual commitments (2 649 million euro) and net payments (3 143 million euro). This is partly explained by the fact that the implementation of the tenth EDF got off to a quick start, and by the strong increase in budget support operations, with global commitments and payments reaching 2 583 million euro and 606 million euro respectively. Outstanding payments increased by 15 %, which is reasonable, given the record level of commitments reached during the year. At the same time, old and dormant outstanding payments decreased by 33 %.

5. *In the interests of sound financial management of the EDF, the Commission has continued its efforts to wind down old projects, and the 7th EDF was closed as planned on 31 August 2008.*

7. *This year the Commission has again performed exceptionally well as regards commitments and payments and in the management of outstanding amounts. This proves that the efforts made in recent years to speed up programme implementation have borne fruit.*

⁽⁶⁾ See Chapter 8 of the Annual Report of the Court of Auditors on the implementation of the budget concerning the financial year 2008.

⁽⁷⁾ Representing 0,6 % of 2008 payments.

⁽⁸⁾ Commission Decision PE/2008/4803 of 29.8.2008.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

The Commission's annual report on the financial management of the seventh to tenth European Development Funds

8. The Financial Regulation applicable to the tenth EDF ⁽⁹⁾ requires the Commission to report each year on the financial management of the EDFs. In the Court's opinion, the report on the financial management presents an accurate description of the achievement of the Commission's operational objectives for the financial year (particularly concerning financial implementation and control activities), the financial situation and the events that had a significant influence on the activities carried out in 2008.

⁽⁹⁾ Articles 118 and 124.

Table 1 — Cumulative use of EDF resources at 31 December 2008

(million euro)

	Situation at end of 2007		Budgetary implementation during the financial year 2008					Situation at end of 2008					
	Global amount	Implementation rate ⁽²⁾	7th EDF	8th EDF	9th EDF	10th EDF	Global amount	7th EDF Closed	8th EDF	9th EDF	10th EDF	Global amount ⁽³⁾	Implementation rate ⁽²⁾
A — RESOURCES ⁽¹⁾	37 328,7		– 765,0	– 53,4	725,4	21 260,1	21 167,1	0,0	10 785,9	16 631,8	21 260,1	48 677,7	
B — USE													
1. Financial commitments	37 279,4	99,9 %	– 765,0	– 53,4	774,7	4 766,4	4 722,7	0,0	10 785,8	16 631,8	4 766,4	32 184,1	66,1 %
2. Individual legal commitments	32 046,0	85,8 %	– 699,2	54,6	3 163,2	130,4	2 649,1	0,0	10 539,2	14 207,4	130,4	2 649,1	51,1 %
3. Payments	26 700,0	71,5 %	– 522,8	323,1	3 253,0	89,8	3 143,1	0,0	9 928,6	10 006,7	89,8	20 025,1	41,1 %
C — Outstanding payments (B1-B3)	10 579,4	28,3 %						0,0	857,3	6 625,1	4 676,6	12 159,0	25,0 %
D — Available balance (A-B1)	49,3	0,1 %						0,0	0,0	0,0	16 493,7	16 493,7	33,9 %

⁽¹⁾ Initial allocations to the 7th, 8th, 9th and 10th EDFs, interest, sundry resources and transfers from previous EDFs.⁽²⁾ As a percentage of resources.⁽³⁾ These figures do not include an amount of 9 818 million euro for the 7th EDF which was closed during the year.

Source: Court of Auditors, based on the EDF Reports on financial implementation and Financial statements at 31 December 2008.

Charts illustrating the consolidated eighth, ninth and tenth EDFs as at 31 December 2008

Chart I: Cumulative resources

Total = 48 677,73 million euro

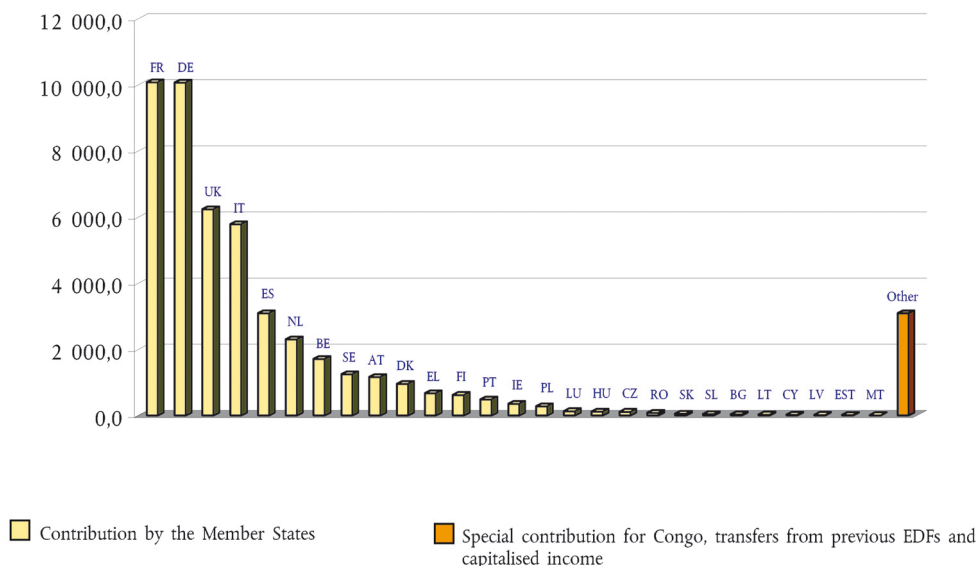
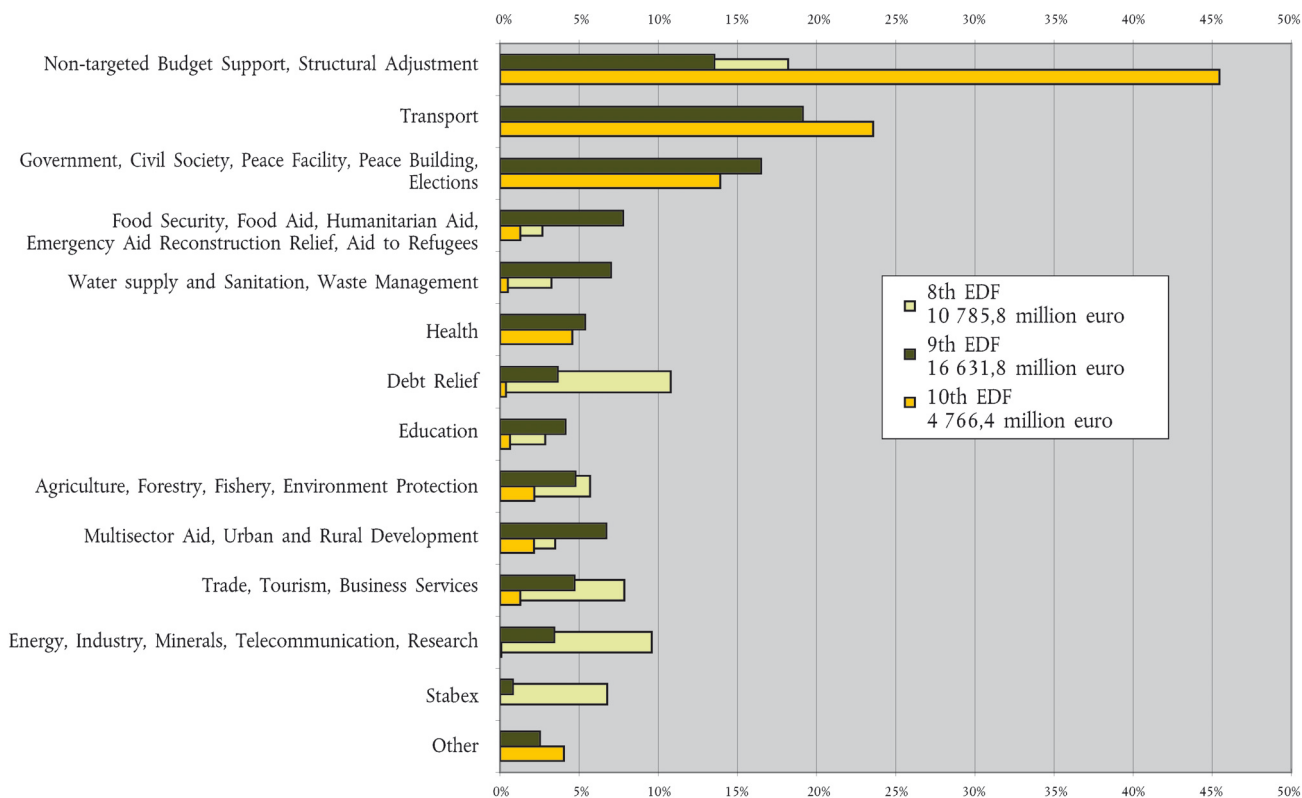


Chart II: Cumulative decisions

Total = 32 184,06 million euro ⁽¹⁾



Source: Court of Auditors, on the basis of the data in the accounting system.

⁽¹⁾ The difference between the cumulative resources (48 677,73 million euro) and the cumulative decisions (32 184,06 million euro), equals the available balance to be allocated (16 493,67 million euro).

CHAPTER II — STATEMENT OF ASSURANCE BY THE COURT OF AUDITORS ON THE EDFs

Statement of Assurance by the Court of Auditors on the seventh, eighth, ninth and tenth European Development Funds (EDFs) for the financial year 2008

I. Pursuant to the provisions of Article 248 of the Treaty the Court has audited:

- (a) the 'Final annual accounts for the financial year 2008 of the seventh, eighth, ninth and tenth European Development Funds' which comprise the consolidated financial statements⁽¹⁰⁾ and the consolidated report on the financial implementation of the seventh, eighth, ninth and tenth EDFs; and
- (b) the legality and regularity of the underlying transactions within the legal framework of the EDFs in respect of the part of the EDF resources for whose financial management the Commission is responsible⁽¹¹⁾.

Management's responsibility

II. In accordance with the Financial Regulations applicable to the seventh, eighth, ninth and tenth EDFs, management⁽¹²⁾ is responsible for the preparation and fair presentation of the final annual accounts of the EDFs and the legality and regularity of the underlying transactions:

- (a) The management's responsibility concerning the final annual accounts of the EDFs includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies, on the basis of the accounting rules adopted by the EDF accounting officer⁽¹³⁾, and making accounting estimates that are reasonable in the circumstances. The Commission approves the final annual accounts of the EDFs.
- (b) The way in which management exercises its responsibility for legality and regularity of underlying transactions depends on the method of implementation of the EDFs. In the case of direct centralised management, implementation tasks are performed by the Commission's departments. Under decentralised management implementation tasks are delegated to third countries and under indirect centralised management to other bodies. In the case of joint management, implementation tasks are shared between the Commission and international organisations. Implementation tasks have to comply with the principle of sound financial management, requiring designing, implementing and maintaining effective and efficient internal control including adequate supervision and appropriate measures to prevent irregularities and fraud and, if necessary, legal proceedings to recover funds wrongly paid or used. Regardless of the method of implementation applied, the Commission bears the ultimate responsibility for the legality and regularity of the transactions underlying the accounts of the EDFs.

⁽¹⁰⁾ The consolidated financial statements comprise the balance sheet, the statement of economic outturn, the statement of cash flow and the table of items payable to the European Development Funds. The financial statements and information supplied by the EIB are not covered by this Statement of Assurance (see footnote 11).

⁽¹¹⁾ Pursuant to Articles 1 and 103(3) of the Financial Regulation applicable to the ninth EDF and Articles 2, 3, 4 and 125(3) of the Financial Regulation applicable to the tenth EDF the Statement of Assurance does not extend to the part of the ninth and tenth EDFs resources that are managed by the EIB and for which it is responsible.

⁽¹²⁾ At the level of the Commission management includes the Members of the Institution, Authorising Officers by delegation and sub-delegation, the Accounting Officer and the leading staff of financial, audit or control units. At the level of Beneficiary States, management includes National Authorising Officers, Accounting Officers, Paying Agents and the leading staff of implementing organisations.

⁽¹³⁾ The accounting rules adopted by the EDF accounting officer are derived from International Public Sector Accounting Standards (IPSAS) issued by the International Federation of Accountants or, in their absence, International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board. In accordance with the Financial Regulation, the 'Consolidated financial statements' for the financial year 2008 are prepared on the basis of these accounting rules adopted by the EDF accounting officer, which adapt accruals based accounting principles to the specific environment of the Communities, while the consolidated reports on implementation of the EDFs continue to be primarily based on movements of cash.

Auditor's responsibility

III. The Court's responsibility is to provide, on the basis of its audit, the European Parliament and the Council with a statement of assurance as to the reliability of the accounts and the legality and regularity of the underlying transactions. The Court conducted its audit in accordance with the IFAC and INTOSAI International Auditing Standards and Codes of Ethics. These standards require that the Court plans and performs the audit to obtain reasonable assurance whether the final annual accounts of the EDFs are free from material misstatement and the underlying transactions, taken as a whole, are legal and regular.

IV. In the context described under paragraph III, an audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the final consolidated accounts and the legality and the regularity of the underlying transactions. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the final consolidated accounts and of material non-compliance of the underlying transactions with the requirements of the legal framework of the EDFs, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the preparation and fair presentation of the final consolidated accounts, and supervisory and control systems implemented to ensure legality and regularity of underlying transactions, in order to design audit procedures that are appropriate in the circumstances. An audit in this context also includes evaluating the appropriateness of accounting policies used and reasonableness of accounting estimates made, as well as evaluating the overall presentation of the final consolidated accounts and the annual activity reports.

V. The Court did not obtain all the necessary information and documentation concerning 10 sampled payments made to international organisations. For this reason, the Court is not able express an opinion on the regularity of expenditure amounting to 190 million euro, or 6,7 % of the annual expenditure.

VI. Subject to the limitation mentioned in paragraph V, the Court considers that the audit evidence obtained is sufficient and appropriate to provide a basis for its statement of assurance.

Opinion on the reliability of the accounts

VII. In the Court's opinion, the final annual accounts of the seventh, eighth, ninth and tenth EDFs present fairly, in all material respects, the financial position of the EDFs as of 31 December 2008, and the results of their operations and cash flows for the year then ended, in accordance with the provisions of the Financial Regulation and the accounting rules adopted by the accounting officer.

VIII. Without qualifying the opinion expressed in paragraph VII, the Court draws attention to the fact that the method used to estimate the provision for costs incurred is not valid for certain types of contracts and to the Commission's decision to refine it from the financial year 2009 onward.

Opinion on legality and regularity of the transactions underlying the accounts

IX. In the Court's opinion the revenue and commitments of the seventh, eighth, ninth and tenth European Development Funds for the year ended 31 December 2008 were free from material error.

X. Without calling into question the opinion expressed in paragraph IX, the Court draws attention to the high incidence of non-quantifiable error that occurred in budget support commitments albeit not included in the estimation of total error.

XI. In the Court's opinion the payments by the seventh, eighth, ninth and tenth European Development Funds for the year ended 31 December 2008 were affected by material error.

XII. The Court has identified significant improvements in the Commission's supervisory and control systems. The Court notes that there is scope for clearer conclusions as to how the results of various controls contribute to the Director-General's assurance and for improving the design and/or implementation of certain systems. The Court also draws attention to the need for the Commission to pursue its efforts to substantiate its decisions on the eligibility of budget support. This requires a structured and formalised demonstration that the recipient countries have a relevant reform programme.

16 and 17 September 2009

Vítor Manuel da Silva Caldeira

President

European Court of Auditors
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THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Information in support of the Statement of Assurance***Audit scope and approach***

9. The observations regarding the reliability of the accounts of the EDFs, set out in paragraphs VII and VIII of the Statement of Assurance, are based on an audit of the consolidated financial statements⁽¹⁴⁾ and the consolidated report on the financial implementation of the seventh, eighth, ninth and tenth EDFs⁽¹⁵⁾. The audit comprised an appropriate range of audit procedures designed to examine, on a test basis, evidence relating to the amounts and disclosures. It included an assessment of the accounting principles used, significant estimates made by management and the overall presentation of the consolidated accounts.

10. The observations regarding the regularity⁽¹⁶⁾ of transactions, set out in paragraphs IX to XII of the Statement of Assurance, are based on the following components:

- (a) substantive testing of a representative statistical sample of 225 items, corresponding to 45 financial and individual legal commitments and 180 payments made by EuropeAid central services and Delegations, including 40 advance payments. Where necessary, implementing organisations and final beneficiaries were visited on the spot in order to verify underlying payments declared in financial reports or cost statements;
- (b) an assessment of the effectiveness of supervisory and control systems at EuropeAid's central services and in the Delegations, including the follow-up of previous key Statement of Assurance observations (see **Annex 2**):
 - (i) ex-ante checks of contracts and payments by authorising officers,
 - (ii) monitoring of implementing organisations,
 - (iii) external audits,
 - (iv) monitoring by EuropeAid central services,
 - (v) internal audit;
- (c) an assessment of the Annual Activity Report and Declaration by the Director-General of EuropeAid.

⁽¹⁴⁾ See Article 122 of the Financial Regulation of 18 February 2008 applicable to the tenth EDF: the financial statements shall comprise the balance sheet, the statement of economic outturn, the statement of cash flow, and the table of items payable to the EDF.

⁽¹⁵⁾ See Article 123 of the Financial Regulation of 18 February 2008 applicable to the tenth EDF: the reports on financial implementation shall comprise tables describing the appropriations, the commitments and the payments.

⁽¹⁶⁾ For the sake of brevity, the term 'regularity of transactions' is used throughout the report to denote 'legality and regularity of underlying transactions'.

THE COURT'S OBSERVATIONS

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11. In the context of the audit, five countries were visited on the spot in order to perform detailed auditing of the transactions: Angola, the Republic of Congo, Malawi, Mozambique and Mauritania.

12. The Court's audit included a review of the procedures in place concerning the accounting and monitoring of the recovery orders issued.

Reliability of the accounts

13. The 2008 annual accounts are the fourth set of accounts prepared under the accruals-based accounting rules. The Court has indicated in its previous Annual Reports that the EDF accounting system did not have all the features necessary for efficient and effective reporting of economic information on an accruals basis, increasing the risk of accounting errors as a result of the extensive manual operations required to convert cash-based data into accrual-based annual accounts. However, despite this risk, the Court's audit found the annual accounts to be free from material error.

14. The new accrual based accounting system ABAC FED was opened in February 2009. All the EDF operational, financial and accounting data have been transferred to the new system. This should further strengthen the EDF accounting environment.

15. The annual accounts contain a provision of 2 113 million euro for the costs incurred in the reporting period but for which no invoices have been received at the year-end. This provision is estimated on the basis of a number of assumptions, notably the linearity of contract expenditure. As announced in its reply to the Court's Annual Report on the EDF concerning the financial year 2007 ⁽¹⁷⁾, the Commission carried out a study which confirmed that this assumption is not valid for certain types of contracts. As indicated in the Notes to the annual accounts, the Commission has decided to refine its method from the financial year 2009.

Regularity of transactions

16. The main features and results of sample-based substantive testing are presented in **Annex 1**.

Revenue

17. The Court's audit of revenue transactions found them to be free from material error.

Project commitments

18. The Court's audit of project commitments found them to be free from material error.

13. The introduction of the new accounting system in 2009 has overcome the past limitations. The new system has all the features required for efficient and effective accrual based reporting. In the financial year 2008, as in previous years, the manual processing is subject to rigorous controls in order to reduce risks.

15. A study was conducted to check the validity of the method used to estimate the provision for invoices receivable. It concluded that the method was valid in the great majority of cases. In the light of the study's conclusions, the Commission will refine the method for the closure for 2009.

⁽¹⁷⁾ Paragraph 17.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Budget support commitments

19. The Court's audit of budget support commitments found them to be affected by a high level of non-quantifiable errors. In comparison with previous years, the Court found that the Commission's assessments of compliance with the Cotonou Agreement requirements are improving; the demonstration is better structured and formalised, notably for Millennium Development Goals (MDG) contracts. However, the Court still found frequent cases where the Commission did not demonstrate in a structured and formalised manner that public finance management was sufficiently transparent, accountable and effective (see paragraphs 44 to 46).

19. The Commission welcomes the recognition by the Court that its continuous and ongoing efforts to improve the clarity and structure of assessments of compliance with the Cotonou Agreement with regard to budget support eligibility (Article 61 of the Agreement) are showing noticeable results. The Commission's focus is on continuing the process of improvement in a bid to eliminate any cases of ambiguity in its assessments. This is to be achieved through further refinements to the guidance on budget support, training and promoting awareness of the importance of demonstrating eligibility in a structured and formal way.

To further improve its analysis of the credibility of beneficiaries' public finance management reform programmes, the Commission is developing an assessment methodology for use by Delegations.

Project payments

20. The Court's audit of advance payments found them to be free from material error.

21. In spite of the Commission's intervention in order to facilitate the audit work to be carried out, the Court did not obtain all the necessary information and documentation concerning 10 transactions managed by international organisations⁽¹⁸⁾. The Court is therefore not in a position to express an opinion on the regularity of these transactions. The Court notes that the verifier mandated by the Commission to perform a verification mission at one of these organisations⁽¹⁹⁾ had reported a similar problem.

21. The Commission fully supports the Court's requests for information. It recognises that for two organisations representing five transactions the requested documentation came too late despite the Commission's intervention. However, these organisations are increasingly willing to cooperate. The Commission has since reminded these organisations of the importance of the timely delivery of information requested on account of the Court's tight work deadlines.

22. The Court's audit revealed a material level of error affecting the amount of the payments audited⁽²⁰⁾. The frequency and types of errors, as well as the impact of quantifiable errors, are presented in **Annex 1 (Part 1, 1.3 and 1.4)**.

22. The Commission has put in place a control system based on the work of external auditors, supervisors, and internal checks which prevent or detect and correct many errors before payments are made. It must be recognised, however, that some Delegations have to work in particularly difficult circumstances, as was the case in Angola which formed part of the Court's audit. The Commission continues to improve its control system, seeking an appropriate balance of cost-effectiveness that provides reasonable assurance.

23. The main types of quantifiable errors detected are the following:

- (a) eligibility: expenditure incurred outside the implementation period, exceeding the budget allowed, or relating to ineligible items;
- (b) occurrence: absence of invoices or other supporting documents;
- (c) accuracy: calculation errors.

⁽¹⁸⁾ African Union, World Bank, World Health Organisation.

⁽¹⁹⁾ World Health Organisation.

⁽²⁰⁾ The Court sets the materiality threshold at 2 %.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

24. The non-quantifiable errors detected mainly concern compliance with legally prescribed bank guarantees, the contract type used, the visibility of EDF financial support, prior approval of procurement documents and contractual deadlines for the presentation of financial reports.

25. Most of the errors should have been detected and corrected by the local supervisors or the authorising officers before the payments were authorised (see paragraphs 33 and 34). Most of the cases of missing supporting documentation relate to the closure of old seventh EDF projects in Angola, which had been implemented in a period of armed conflict and political turmoil. This difficult context and the length of time since the end of the projects meant that it was extremely difficult for the Delegation, which, moreover, had not been responsible for the management of these projects, to retrieve all necessary supporting documents.

Budget support payments

26. The Court's audit of budget support payments found them to be affected by a high level of non-quantifiable errors. The cases encountered include a lack of evidence that the foreign exchange transfers had been accounted for according to the applicable provisions, assessment by the Commission of compliance with conditions made on the basis of outdated data or not carried out, insufficient analysis of factors hindering the implementation of the public finance management reform programme and the use of an incorrect reference period for the assessment of the achievement of indicators (see paragraphs 44 to 46).

Annual Activity Report and Declaration by the Director-General of EuropeAid

27. In its examination of the annual activity report and the declaration by the Director-General of EuropeAid for the financial year 2008, the Court has assessed the extent to which they present a fair picture (i.e. with no significant distortions) of the effectiveness of the procedures in place. In particular, it examined whether the supervisory and control systems generate the necessary assurance insofar as the regularity of transactions are concerned.

24. Following the Court's recommendations, the Commission has taken measures to tighten up checks on bank guarantees, and new instructions on visibility are being finalised. The other points raised by the Court are very much linked to project implementation and hence to constraints on the ground.

25. There are specific risks involved in managing cooperation in countries affected by particular difficulties such as war, riots, etc., as was the case in Angola. The scale of the problem of missing documentation observed by the Court in Angola must not in any way be viewed as the general rule across all ACP cooperation management, as demonstrated by the excellent results in the other audited bodies.

26. The Commission notes that in a number of cases these non-quantifiable errors are due to the lack of clarity in financing agreements that were drawn up before the most recent guidance was adopted in 2007. More recent financing agreements drawn up in line with the 2007 guidance are more clearly structured. It is expected that payments made on the basis of these more recent agreements will give rise to clearer assessments and substantially fewer errors. In addition, the Commission is promoting widespread awareness throughout its services of the need for a more structured and formal approach to assessing budget support payments.

Furthermore, in February 2009 the Commission revised the financial circuits for budget support payments to strengthen the role of financial verification in the approval process. This is expected to further improve the rigour of payment assessments and hence compliance with the conditions set out in the financing agreements.

THE COURT'S OBSERVATIONS

28. As indicated in paragraph 4, EuropeAid's mission is to implement most of the external assistance instruments ⁽²¹⁾ financed from the General Budget of the European Community and the EDFs. The annual activity report and the declaration make no distinction between the General Budget and the EDF-financed operations, which present the same inherent risks and are governed by largely similar implementation arrangements. Therefore, unless otherwise specified, the Court's observations concerning the annual activity report and the declaration, as well as the supervisory and control systems, refer to the whole area of responsibility of EuropeAid.

29. The annual activity report is consistent with the Court's findings concerning the implementation and results of the supervisory and control systems in place. In comparison with previous years, the Court notes that the quality of the annual activity report has significantly improved: it is better structured, clearer and more informative, notably through a greater use of quantitative indicators. However, there is scope for more explicit conclusions on how the results of the various controls contribute to the Director-General's assurance. A key indicator for the estimated financial impact of residual errors after all ex-ante and ex-post controls have been implemented would also provide the Director-General with a stronger basis for determining whether it remains below the materiality criteria set.

30. The annual activity report refers to significant staff constraints ⁽²²⁾. The high proportion of short-term staff in EuropeAid's central services and the related turnover in recruitment are said to result in a loss of institutional memory, which has detrimental effects on the continuity and visibility of operational management and on the efficient use of resources. In the Delegations the vacancy rate is presented as being dangerously high and on an upward trend.

THE COMMISSION'S REPLIES

29. *The Commission recognises that as part of its ongoing efforts to improve the overall internal control system, further work is needed on the architecture of the control systems for external aid and their contribution to the Director-General's Statement of Assurance. With this in mind, and in conjunction with the Commission's work on tolerable risk, EuropeAid will launch a review of its control strategy in 2010.*

30. *The turnover issue is related to the constraint caused by the maximum duration of three years for contractual agents in Brussels. In order to reduce the risk of losing institutional memory because of turnover, EuropeAid has put in place a number of measures: debriefing, compulsory hand-over notes in the framework of the Internal Control Standards, systematic supervision of Contractual Agents by officials in Delegation.*

⁽²¹⁾ Except pre-accession aid, assistance to the West Balkans, humanitarian aid, macro-financial aid, Common Foreign and Security Policy (CFSP) and the Rapid Reaction Mechanism.

⁽²²⁾ Page 43.

THE COURT'S OBSERVATIONS

31. In its Annual Report on the EDFs concerning the financial year 2007 the Court recommended that a review should be carried out to assess whether EuropeAid's central services and the Delegations have the level and type of human resources required to ensure the quality of control ⁽²³⁾. It also recommended that a human resources policy should be developed on the basis of an analysis of the skills and knowledge needed in relation to the management of budget support in view of its increasing importance ⁽²⁴⁾.

32. The Director-General of EuropeAid declares that he has obtained reasonable assurance that the control procedures put in place give the necessary guarantees concerning the regularity of transactions, whereas the Court's audit revealed a material level of error. The Court found that, whilst significant progress continued to be made, the effect of certain recent measures were not yet fully visible in 2008 and there is scope for improving the design or implementation of certain controls (see paragraphs 33 to 43). A summary of the results of the Court's follow-up of key Statement of Assurance observations can be found in **Annex 2**.

Effectiveness of the systems**Ex-ante checks by authorising officers**

33. The Court assessed ex-ante checks as partially effective at detecting and correcting errors, particularly in respect of the calculation of the amounts claimed, the availability of the required supporting documents and compliance with procurement rules. As indicated in paragraph 25, the errors found in Angola are due to exceptional circumstances and do not call into question the Delegation's ex-ante check system.

THE COMMISSION'S REPLIES

31. *In the zero growth environment for Commission posts until 2013 EuropeAid addresses staffing matters through three elements:*

Detailed needs assessment based on workload assessments on a yearly basis for both Operational and Finance, Contracts and Audit sections in Delegations. Selection and recruitment of staff with qualifications and skills that are required to match needs; the selection panels are composed of all relevant geographic and thematic services; an extensive training programme which responds to the current needs of external aid management in Delegation and headquarters.

Candidates for budget support related posts are tested and selected based on proven budget support knowledge and skills. Budget support training delivered in the field has increased from 7 available courses in 2006 to 14 in 2007 and 24 in 2008. This is in addition to headquarters training, where the average participation from Delegations is 40 %. Annual regional seminars are also organised for budget support practitioners.

32. *EuropeAid has designed its controls to cover the full lifecycle of its multi-annual projects so that it is able to prevent or detect and correct most of the financial errors in the normal course of its controls. The Commission's ex-post controls confirm — and further reduce — this very low level of residual error, which informs the EuropeAid Director-General's Statement of Assurance.*

Nevertheless, the Commission accepts that the effects of recent enhancements in the overall control architecture were not yet fully visible in 2008 and that there is still scope for further improvement.

⁽²³⁾ Paragraph 55(b).

⁽²⁴⁾ Paragraph 56(f).

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Monitoring of implementing organisations

34. As in previous years, significant weaknesses were detected in the financial procedures and controls of implementing organisations, supervisors and National Authorising Officers (NAOs):

- (a) the main weaknesses at implementing organisations were inadequate procedures concerning supporting documents and filing and accounting systems that do not ensure that the expenditure is correctly recorded and reported;
- (b) in some cases, the quality of the controls carried out by supervisors on works contracts was inadequate;
- (c) the lack of capacity or ownership in most of the NAO services results in poorly documented and ineffective checks.

35. In general, the Delegations were aware of these weaknesses and had placed limited reliance on these controls. They had also taken appropriate measures to address the weaknesses identified, in particular by requiring mandatory audits and expenditure verifications before the financial closure of projects, commissioning technical audits of ongoing works contracts and providing technical assistance to strengthen the capacity of the NAO services. Moreover, in 2008 EuropeAid initiated work aimed at producing better guidance and communication tools to address recurrent weaknesses identified at the level of final beneficiaries and implementing organisations.

34. Support to organisations in charge of the implementation of EDF-funded projects is already significant and includes provision of print guidelines, a well maintained finance and contracts EuropeAid website, training in the field and on the spot advice from the finance and contracts staff in Delegations. In the ACP region, 150 days of finance and contracts training and 20 audit trainings were offered in the field in 2008 of which 94 % places were taken up by NAO staff, technical ministries and project staff.

- (a) The Commission has developed various information and management tools, aimed mainly at technical assistants (specific guide) and NGOs (a seminar was held on 23 and 24 March 2009 with the Concorde group on these issues). It is continuing its efforts to provide a financial management toolkit for beneficiary organisations in the near future.
- (b) The Commission has defined specific terms of reference for the technical audit of infrastructure, which have been available to delegations since 2009.
- (c) A new training contract was signed in 2009 to guarantee the continuity of training for NAO services. In addition, a large number of programmes have been set up in support of NAOs in order to boost their capacity.

35. The Commission welcomes the Court's appraisal of the measures taken by delegations to address weaknesses identified in NAO services and of the support work for beneficiaries and implementing organisations

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

External audits

36. Financial and systems audits of projects before final payments are a key component of EuropeAid's supervisory and control systems⁽²⁵⁾. Although they were not yet fully operational in 2008, as that was the first year of implementation, the use of the new standardised terms of reference for about two-thirds of the audits launched and the introduction of an audit management information system (CRIS Audit) are important steps forward for ensuring more consistent reporting from auditors and appropriate monitoring of audit activities and analysis of audit results⁽²⁶⁾.

37. The Court's audit found that the Delegations did not consistently follow EuropeAid's operational guidelines when preparing their annual audit plan for 2008 and that there was a lack of clarity as to how risk-based audits had been selected and, thus, the extent to which these contribute to the Director-General's assurance. EuropeAid is, however, well aware of the need to make improvements in this respect; it prioritised Internal Control Standard 6 'Risk management' in its Annual Management Plan for 2008 and a number of actions have been adopted, in particular staff training, to ensure more effective implementation of this standard.

38. The level of implementation of the annual audit plans was low: 56 % of audits in the annual audit plan for 2008 were launched within the year, the others being postponed or sometimes cancelled, and 67 % in the annual audit plan for 2007 were completed by the end of 2008. This is partly due to inadequate planning of the annual audit plan, the duration of the audit process and the Delegations' limited capacity to organise and follow up audits.

39. Despite repeated reminders from EuropeAid central services, many Delegations did not record data in CRIS Audit in a timely and complete manner, which undermines the usefulness of this IT system. EuropeAid's guidelines of November 2008 for audit task managers address this weakness.

36. *The widespread use of the standardised terms of reference and of CRIS Audit will contribute to improving the consistency in quality of audits and the consolidation of audit results.*

37. *In order to increase consistency in the contribution of Delegations to the Annual Audit Plan, a harmonised format will be compulsory as of the AAP 2010. The risk analysis foresees a degree of flexibility, which is necessary in a complex and constantly varying external aid context. However, basic principles detailed in the methodology will have to be respected. The Commission believes that these revisions will increase the transparency and consistency of the AAP.*

38. *The Commission would underline the steady progress made in the implementation of the annual audit plans. Indeed, 455 audits were finalised in 2008, which is a 35 % increase on 2007 (337).*

Since June 2008, AAP execution has been regularly monitored by EuropeAid management.

EuropeAid's central services will continue to provide assistance to Delegations to improve their audit planning. In the context of the preparation of the 2009 AAP, Delegations have been invited to pay specific attention to the availability of resources.

39. *2008 was the first year of compulsory use of CRIS Audit. Overall, CRIS Audit was correctly used. The Commission recognises nevertheless that progress needs to be made in the timely upload of documents.*

⁽²⁵⁾ Audits include both assurance audits and other types of assignments, in particular conformity checks ('four pillar') on international organisations' accounting, internal control, audit and procurement procedures against internationally accepted standards and subsequent verification missions.

⁽²⁶⁾ More recent improvements, which will take effect as of 2009, concern a modified planning process for the annual audit plan and new guidance to Audit Task Managers issued in November 2008.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Monitoring by EuropeAid central services

40. Audits mandated by EuropeAid's central services under the framework contract agreement are subject to quality review. EuropeAid also analyses the results of these audits and follows up recurrent findings at the level of final beneficiaries and implementing partners, as mentioned in paragraph 35. It also carried out a quality review on a sample of audits mandated by the Delegations. No overall analysis of the findings and recommendations of the audits mandated by the Delegations has yet been performed.

41. The introduction of CRIS Audit is to be welcomed. Certain refinements still need to be made to allow for the assessment of the audit coverage of expenditure and more efficient use of this system for collating, analysing and acting upon audit findings and recommendations.

42. In 2008 EuropeAid's central services performed eight monitoring missions. These missions were well designed and identified relevant recommendations to improve internal control in the Delegations examined.

43. As indicated in Court's Annual Report on the EDFs for the financial year 2007 ⁽²⁷⁾, EuropeAid's transactional ex-post control system provides an effective mechanism for the identification of compliance errors affecting transactions but is less effective at identifying errors which have an impact upon the amount of the payment. The Court noted that, in respect of the EDF operations, the responsible Directorate had extended the scope of these controls during 2008: it performed systematic checks on a sample of documents supporting the declared expenditure and on the accuracy of calculations regarding price revisions. Furthermore, it introduced a half-yearly follow-up of actions taken by the Delegations in response to the findings of these controls. This type of approach is likely to improve the relevance and effectiveness of transactional ex-post controls both as regards the examination of the regularity of transactions and the assessment of the quality of ex-ante checks performed by the authorising officers.

40. As of 2009, EuropeAid central services will focus their quality review of audit reports on non-framework contractors. In addition, a number of improvements to be incorporated in CRIS Audit will make it easier to analyse the findings of auditors outside the framework contract.

41. CRIS Audit functionalities are constantly being improved in an effort to make optimum use of the database.

43. As regards transactional ex post controls, EuropeAid is currently assessing whether the checks conducted by the Directorate responsible for ACP countries could be extended to other regions of activities. This will, however, be subject to priority allocations and resources constraints.

⁽²⁷⁾ Paragraph 46.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Budget support

44. The Cotonou Agreement states that budget support shall be granted where public expenditure management is sufficiently transparent, accountable and effective⁽²⁸⁾. The Commission interprets this condition in a dynamic manner⁽²⁹⁾. In its view, the weaknesses affecting public finance management at the time of the financing decision do not preclude the launch of a budget aid programme, provided that a commitment to reform exists and the reforms planned are deemed to be satisfactory. The European Parliament has questioned the Commission's 'dynamic interpretation' of the eligibility criteria for budget support and stated that budget support should only be undertaken in countries that already meet a minimum standard of credible management of public finances⁽³⁰⁾.

45. In its Annual Reports on the EDFs concerning the financial years 2006⁽³¹⁾ and 2007⁽³²⁾, the Court recommended that compliance with the Cotonou Agreement should be benchmarked against baseline requirements. The Commission did not accept this recommendation because it considers the setting of common minimum standards to be uniformly applied to all countries is inappropriate. As the European Parliament pointed out in its report on discharge for the financial year 2007⁽³³⁾, this approach gives the Commission a high degree of discretion which must be counterbalanced by an equally high degree of transparency. As stated by the Court in its Special Report No 2/2005 concerning EDF budget aid to ACP countries⁽³⁴⁾ this requires the assessment of compliance with the Cotonou Agreement requirements to be presented in a structured and formalised manner.

44. The Commission has extensively justified its approach to assessing eligibility for budget support in response to the positions adopted by the Court and Parliament respectively. In particular, the letter from Commissioner Michel of 9 January 2009 to the Court, with copy to the European Parliament, sets out the detailed background to the Commission's position. This stresses that the Commission's approach is in line with that of other key donors (e.g. the International Monetary Fund and the World Bank). At the same time, it notes that an approach based on minimum standards would not be consistent with OECD guidelines on support for public financial management reform, or with the Paris and Accra principles on aid effectiveness.

45. The Commission understands and accepts the demand for even greater transparency in the treatment of budget support. In this context, the Commission proposes to provide more in-depth coverage of budget support issues in future annual reports on the 'European Community's Development and External Assistance Policies and their Implementation'.

The Commission recognises that improvements can be made by taking a more structured and formalised approach to assessing budget support eligibility, in line with the Cotonou Agreement. The Commission is therefore in the process of further refining its guidance on budget support to reinforce its approach.

⁽²⁸⁾ Article 61(2)(a).

⁽²⁹⁾ See paragraphs 28 and 29 of Special Report No 2/2005 concerning EDF budget aid to ACP countries (OJ C 249, 7.10.2005).

⁽³⁰⁾ Resolution of the European Parliament of 22 April 2008 with observations forming an integral part of the decision on discharge in respect of the implementation of the budget of the Sixth, Seventh, Eighth and Ninth European Development Funds for the financial year 2006, paragraph 32 (OJ L 88, 31.3.2009).

⁽³¹⁾ Paragraph 55 (OJ C 259, 31.10.2007).

⁽³²⁾ Paragraph 56(a) (OJ C 286, 10.11.2008).

⁽³³⁾ Resolution of the European Parliament of 23 April 2009 with observations forming an integral part of the decision on discharge in respect of the implementation of the budget of the Seventh, Eighth and Ninth European Development Funds for the financial year 2007, paragraphs 46 and 47.

⁽³⁴⁾ Paragraph 85.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

46. As mentioned in the Court's Annual Report on the EDFs concerning the financial year 2007 ⁽³⁵⁾, the financing agreements of budget support programmes financed under the ninth EDF are often incomplete or unclear, and thus do not provide a sufficiently clear framework to carry out such a structured and formalised assessment. In 2008 the Court noted a significant improvement with the financing agreements of budget support programmes financed under the tenth EDF. In some cases there is scope for further improvement in the identification of both priority public financial management measures to be implemented by the recipient country as well as the sources of information to check compliance with the agreed conditions.

Internal audit

47. The Internal Audit Capability (IAC) operated effectively and in compliance with its primary objective to provide the Director-General with assurance as to the effectiveness and efficiency of risk management, control and internal governance processes in EuropeAid. In the opinion of the IAC, the results of the work performed in 2008 indicate that there are no important systemic weaknesses that might adversely affect the functioning of the internal control system taken as a whole. The Court draws attention to the fact that the IAC audit could not obtain full assurance as to the CRIS-EDF system's capacity to produce reliable and accurate operational information data as from January 2009.

48. The Commission's Internal Audit Service (IAS) carried out a joint audit with the IAC on the financial management procedures of the Directorate responsible for ACP countries, regarding its devolved delegations, and another audit on recoveries ⁽³⁶⁾. The audit findings are in line with those of the Court as regards the management of bank guarantees (see paragraph 24), the utilisation of CRIS Audit (see paragraph 39), and the centralised follow-up of audits mandated by the Delegations (see paragraph 40).

49. The IAS performed a follow-up audit on the implementation of the FAFA ⁽³⁷⁾. It concludes that the control environment should be strengthened, both at partner and project level, notably by improving coordination and understanding with the UN bodies on verification and assurance issues.

46. *The Commission welcomes the Court's recognition of the improvement in the clarity of recent financing agreements. At the same time, the Commission also recognises that further improvements can be made and is thus further refining its guidance in order to address the points raised by the Court with regard to establishing clear reform expectations in the area of public financial management and the monitoring of progress in these areas.*

47. *When the IAC audit was conducted, the new CRIS system was still at the development stage. However, all the necessary measures had been taken to enable the system to start up in early 2009. Migration to the new CRIS/ABAC system was carried out according to timetable and operations started as normal in early 2009.*

49. *The report recognised the progress made on the implementation of the majority of the recommendations. The verification issue was discussed at the 6th FAFA meeting in Brussels (April 09). The terms of reference are used consistently by the Commission during the verification missions to UN partners.*

⁽³⁵⁾ Paragraph 27.

⁽³⁶⁾ Report from the Commission to the European Parliament and Council: Annual report to the discharge Authority on internal audits carried out in 2008 (COM(2009) 419 final of 5.8.2009).

⁽³⁷⁾ Financial and Administrative Framework Agreement.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Conclusions and recommendations

50. Based on its audit work, the Court concludes that the EDF accounts for the financial year ending 31 December 2008 present fairly, in all material respects, the financial position of the EDFs and the results of their operations and cash flows for the year then ended, in accordance with the provisions of the Financial Regulation and the accounting rules adopted by the accounting officer. The Court draws attention to the observation in paragraph 15 concerning the provision for costs incurred.

51. Due to the circumstances described in paragraph 21, the Court was not able to fully audit the 10 sampled payments made to certain international organisations. Therefore, the Court is unable to express an opinion on the regularity of expenditure amounting to 190 million euro, i.e. 6,7 % of the annual expenditure.

52. Subject to the limitation mentioned in the preceding paragraph and based on its audit work, the Court concludes that for the financial year ending 31 December 2008:

(a) revenue and commitments of the EDFs were free from material error; and

(b) the payments of the EDFs were affected by material error. The most likely error rate lies between 2 % and 5 %.

53. Based on its audit work, the Court concludes that the supervisory and control systems of EuropeAid are partially effective in ensuring the regularity of payments. **Annex 1, Part 2** gives an overview of the Court's assessment of EuropeAid's supervisory and control systems ⁽³⁸⁾.

52.

(b) *The Commission would point out that the overall error rate was very strongly affected by one delegation having to work in a post-conflict environment.*

⁽³⁸⁾ See Chapter 8, External aid, development and enlargement, of the Annual Report of the Court of Auditors on the implementation of the budget concerning the financial year 2008 for an assessment of the supervisory and control systems of DG ECHO.

THE COURT'S OBSERVATIONS

54. In 2008 EuropeAid continued to make significant improvements to its supervisory and control systems. It started to use the new terms of reference for audits and implemented a management information system, CRIS Audit, which should improve EuropeAid's capacity to plan and monitor audits, as well as to analyse and follow up audit findings and recommendations. The Annual Activity Report is better structured, clearer and more informative, particularly because of greater use of quantitative indicators. There is scope for clearer conclusions on how the results of the various controls contribute to the Director-General's assurance and for developing a key indicator on the estimated financial impact of residual errors after all ex-ante and ex-post controls have been implemented.

55. EuropeAid has set up a comprehensive control strategy and is pursuing its efforts to ensure more efficient and effective implementation of controls. The following recommendations should be considered in this context:

- (a) ex-ante checks should be improved by focusing more on key risks;
- (b) annual audit plans should be prepared on the basis of more structured risk analysis and more realistic assessment of the resources available for the purpose;
- (c) the implementation of annual audit plans should be closely monitored throughout the year in order to detect significant deviations and take corrective action in a timely manner;
- (d) the functionalities of CRIS Audit should be developed to enable more efficient and effective monitoring of audit activities as well as analysis and follow-up of audit findings and recommendations;

THE COMMISSION'S REPLIES

54. *The Commission recognises that as part of its ongoing efforts to improve the overall internal control system, further work is needed on the architecture of the control systems for external aid and their contribution to the Director-General's Statement of Assurance. With this in mind, and in conjunction with Commission's work on tolerable risk, EuropeAid will launch a review of its control strategy in 2010.*

55.

(a) *Ex-ante checks of each and every transaction before it is authorised is the primary assurance mechanism for regularity. Ex-ante controls are important as they prevent errors and avoid the need for ex-post corrective action. The level of risk is taken into account in the checks performed. EuropeAid has implemented a number of measures in particular as regards training to take better into account recurrent risks.*

(b) *The risk analysis to be conducted in the preparation of the Annual Audit Plan foresees a degree of flexibility, which is necessary in a complex and constantly varying external aid context. However, basic principles detailed in the methodology will have to be respected.*

In the context of the preparation of the 2009 AAP, Delegations have been invited to pay specific attention to the availability of resources.

(c) *Since June 2008, AAP execution has been regularly monitored and presented at management meetings. The breakdown of implementation per geographical zone and headquarters/Delegations allows appropriate corrective action to be taken.*

(d) *CRIS Audit is being improved on a regular basis.*

For example, since the beginning of 2009, each audit contracted in CRIS is automatically linked to a CRIS Audit number, which completes the registration process in CRIS Audit.

Other improvements are scheduled in the coming months, such as more accurate registration of audit findings and of ineligible expenditure.

THE COURT'S OBSERVATIONS

- (e) EuropeAid should ensure that the Delegations record data in CRIS Audit in a comprehensive and timely manner;
- (f) in the light of the results of the approach adopted by Directorate responsible for ACP countries, EuropeAid should carry out a review of the transactional ex-post control system with a view to assessing the need and feasibility of extending the scope of such controls.

56. As regards budget support, the Court recommends that EuropeAid:

- (a) pursues its efforts to support its decisions on the eligibility of budget support with a structured, formal demonstration that the recipient country has a relevant reform programme to address all significant weaknesses over a foreseeable timetable and that there is commitment on the country's part to implement it;
- (b) ensures that all future financing agreements provide a comprehensive and clear basis for the assessment of compliance with payment conditions.

THE COMMISSION'S REPLIES

- (e) *At the beginning of 2008, an instruction note was sent by the Director-General requiring the services concerned (headquarters and Delegations) to enter all audits in CRIS Audit. This was monitored in 2009 and the units responsible have regularly reminded the Audit Tasks Managers of this obligation.*
- (f) *As regards transactional ex post controls, EuropeAid is currently assessing whether the checks conducted by Directorate responsible for ACP countries could be extended to other Directorates. This will, however, be subject to priority allocations and resources constraints.*

56.

- (a) *The Commission agrees and is further revising its guidance to address this point. It is expected that this will be completed by the end of 2009. The Commission also intends to further improve the transparency of its budget support by enhancing its reporting.*
- (b) *The Commission is further revising its guidance to address this point. It is expected that this will be completed by the end of 2009.*

ANNEX 1

PART 1: MAIN FEATURES OF SAMPLE BASED TRANSACTION TESTING

1.1 — Size of the sample

Year	Number of Commitments tested	Number of Payment transactions tested
2008	45	170
2007	60	148

1.2 — Structure of the sample

Percentage of transactions tested which were	2008			2007
	Projects	Budget Support	TOTAL	
Commitments				
Global commitments	33 %	22 %	56 %	50 %
Individual legal commitments	44 %	0 %	44 %	50 %
Total	78 %	22 %	100 %	100 %
Payments				
Advances	24 %	0 %	24 %	0 %
Interim/Final	65 %	12 %	76 %	100 %
Total	88 %	12 %	100 %	100 %

1.3 — Frequency and estimated impact of errors in the sample of interim/final payments

Errors	2008			2007
	Projects	Budget Support	TOTAL	
Frequency of error:	25 % {27}	40 % {8}	27 % {35}	37 % {55}
Frequency of quantifiable errors:	38 % {15}	9 % {1}	31 % {16}	53 % {31}
Impact of quantifiable errors:				
Most likely error rate falls in the range (*)	Between 2 % and 5 %	Below 2 %	Between 2 % and 5 %	Between 2 % and 5 %

(*) The Court distinguishes three ranges for most likely error rate: below 2 %, between 2 % and 5 %, above 5 %.
The figures in the {} brackets are absolute numbers.

1.4 — Types of errors in the sample of interim/final payments

Percentage of errors in transactions tested which concern	2008			2007
	Projects	Budget Support	TOTAL	
Quantifiable errors				
Eligibility	47 %	0 %	44 %	68 %
Occurrence	47 %	0 %	44 %	23 %
Accuracy	7 %	100 %	13 %	10 %
Total	100 %	100 %	100 %	100 %
Non-quantifiable errors				
Non-quantifiable error that may have financial impact	20 %	60 %	31 %	79 %
Non-quantifiable error where the financial impact is not possible to quantify	32 %	40 %	34 %	0 %
Non-quantifiable error with no financial impact	48 %	0 %	34 %	21 %
Total	100 %	100 %	100 %	100 %

System concerned	Ex-ante checks	External Audit		Monitoring					Internal Audit	Overall assessment
		Quality	Quantity/implementation of the audit plan	Monitoring missions		Ex-post controls	Audit			
				Quality	Quantity		Follow-up of individual audit findings/Effective recovery procedures	Overall monitoring by central services of audits commissioned by Delegations		
Central services EuropeAid										
Delegations				N/A	N/A	N/A		N/A		

Legend:

	Effective
	Partially effective
	Not effective
N/A	Not applicable: does not apply or not assessed

FOLLOW-UP OF KEY STATEMENT OF ASSURANCE OBSERVATIONS

	Court observation	Court analysis	Court recommendations	Commission reply
1.	EuropeAid's control strategy should include key indicators supporting the level of assurance to be given by the Director-General, the coverage of some controls, the coordination between ex-ante and ex-post controls, as well as the human resources required. (Annual Report concerning the financial year 2007, paragraph 55(a))	In 2008 EuropeAid continued to make significant improvements to its supervisory and control systems. It started to use the new terms of reference for audits and implemented a management information system, CRIS Audit, which should improve EuropeAid's capacity to plan and monitor audits, as well as to analyse and follow up audit findings and recommendations. The Annual Activity Report is better structured, clearer and more informative, particularly because of greater use of quantitative indicators. (Annual Report concerning the financial year 2008, paragraph 54) EuropeAid has set up a comprehensive control strategy and is pursuing its efforts to ensure a more efficient and effective implementation of some controls. (Annual Report concerning the financial year 2008, paragraph 55)	There is scope for clearer conclusions on how the results of the various controls contribute to the Director-General's assurance and for developing a key indicator on the estimated financial impact of residual errors after all ex-ante and ex-post controls have been implemented. (Annual Report concerning the financial year 2008, paragraph 54)	<i>The Commission recognises that as part of its ongoing efforts to improve the overall internal control system, further work is needed on the architecture of the control systems for external aid and their contribution to the Director-General's Statement of Assurance. With this in mind, and in conjunction with its work on tolerable risk, EuropeAid will launch a review of its control strategy in 2010.</i>
2.	A review should be carried out to assess whether EuropeAid's central services and the Delegations have the level and type of human resources required to ensure the quality of controls. (Annual Report concerning the financial year 2007, paragraph 55(b))	The annual activity report refers to significant staff constraints. The high proportion of short-term staff in EuropeAid's central services and the related turnover in recruitment are said to result in a loss of institutional memory, which has detrimental effects on the continuity and visibility of operational management and on the efficient use of resources. In the Delegations the vacancy rate is presented as being dangerously high and on an upward trend. (Annual Report concerning the financial year 2008, paragraph 30) In the zero growth environment for Commission posts until 2013 EuropeAid addresses staffing matters through three elements:	Satisfactory action has been taken in the context of the zero growth environment.	

	Court observation	Court analysis	Court recommendations	Commission reply
		Detailed needs assessment based on workload assessments on a yearly basis for both Operational and Finance, Contracts and Audit sections in Delegations. Selection and recruitment of staff with qualifications and skills that are required to match needs; the selection panels are composed of all relevant geographic and thematic services; an extensive training programme which responds to the current needs of external aid management in Delegation and headquarters. (Commission's reply to paragraph 31 of the Annual Report concerning the financial year 2008)		
3.	The management of implementing organisations should be better supported. This should involve greater presence of Delegation staff in the field, supporting accounting systems and training especially for projects implemented by programme estimates. (Annual Report concerning the financial year 2007, paragraph 55(e))	In general, the Delegations were aware of these weaknesses and had placed limited reliance on these controls. They had also taken appropriate measures to address the weaknesses identified, in particular by requiring mandatory audits and expenditure verifications before the financial closure of projects, commissioning technical audits of on going works contracts and providing technical assistance to strengthen the capacity of the NAO services. Moreover, in 2008 EuropeAid initiated work aimed at producing better guidance and communication tools to address recurrent weaknesses identified at the level of final beneficiaries and implementing organisations. (Annual Report concerning the financial year 2008, paragraph 35)	Satisfactory action has been taken.	
4.	Checks performed by Delegations before authorising payments should better scrutinise the payment requests and intensify the focus on the reality, eligibility and accuracy of the expenditure. The quality of work performed by supervisors and auditors should be better monitored. (Annual Report concerning the financial year 2007, paragraph 55(d))	The Court assessed ex-ante checks as partially effective at detecting and correcting errors, particularly in respect of the calculation of the amounts claimed, the availability of the required supporting documents and compliance with procurement rules. As indicated in paragraph 25, the errors found in Angola are due to exceptional circumstances and do not call into question the Delegation's ex-ante check system. (Annual Report concerning the financial year 2008, paragraph 33)	Ex-ante checks should be improved by focusing more on key risks. (Annual Report concerning the financial year 2008, paragraph 55(a))	<i>Ex-ante checks of each and every transaction before it is authorised is the primary assurance mechanism for legality and regularity. Ex-ante controls are important as they prevent errors and avoid the need for ex-post corrective action. The level of risk is taken into account in the checks performed.</i> <i>The Commission has defined specific terms of reference for the technical audit of infrastructure, which have been available to Delegations since 2009.</i> <i>Furthermore, EuropeAid central services are performing quality reviews of audit reports.</i>

	Court observation	Court analysis	Court recommendations	Commission reply
5.	The implementation of CRIS Audit should allow monitoring of the audit coverage and the audit results. Qualitative information as to the recommendations made and the improvements which should be put in place to address the findings is vital to ensure that the ultimate objectives of commissioning audits are met. (Annual Report concerning the financial year 2007, paragraph 55(e))	Although they were not yet fully operational in 2008, as that was the first year of implementation, the use of the new standardised terms of reference for about two-thirds of the audits launched and the introduction of an audit management information system (CRIS Audit) are important steps forward for ensuring more consistent reporting from auditors and appropriate monitoring of audit activities and analysis of audit results. (Annual Report concerning the financial year 2008, paragraph 36)	The functionalities of CRIS Audit should be developed to enable a more efficient and effective monitoring of audit activities as well as analysis and follow-up of audit findings and recommendations. (Annual Report concerning the financial year 2008, paragraph 55(d))	CRIS Audit is being improved on a regular basis and new functionalities are operational (linkage of a CRIS audit contract to a CRIS audit number) as 2009. New Improvements are scheduled in the coming months, such as more accurate registration of audit findings and of ineligible expenditure.
6.	Transactional ex-post controls should include a better examination of supporting documentation to ensure that transactions are not affected by errors of eligibility and occurrence as well as to verify whether checks performed before the payment was authorised were adequate. (Annual report concerning the financial year 2007, paragraph 55(f))	EuropeAid's transactional ex-post control system provides an effective mechanism for the identification of compliance errors affecting transactions but is less effective at identifying errors which have an impact upon the amount of the payment. The Court noted that, in respect of the EDF operations, the Directorate responsible for ACP countries had extended the scope of these controls during 2008: it performed systematic checks on a sample of documents supporting the declared expenditure and on the accuracy of calculations regarding price revisions. Furthermore, it introduced a half-yearly follow-up of actions taken by the Delegations in response to the findings of these controls. This type of approach is likely to improve the relevance and effectiveness of transactional ex-post controls both as regards the examination of the regularity of transactions and the assessment of the quality of ex-ante checks performed by the authorising officers. (Annual Report concerning the financial year 2008, paragraph 43)	In the light of the results of the approach adopted by the Directorate responsible for ACP countries, EuropeAid should carry out a review of the transactional ex-post control system with a view to assessing the need and feasibility of extending the scope of such controls. (Annual Report concerning the financial year 2008, paragraph 55(f))	As regards transactional ex-post controls, EuropeAid is currently assessing whether the checks conducted by the Directorate responsible for ACP countries could be extended to other regions. This will, however, be subject to priority allocations and resources constraints.

	Court observation	Court analysis	Court recommendations	Commission reply
7.	The standardised methodology for monitoring missions should be finalised and the number of such missions increased. The new methodology should maintain the focus on the examination of the set-up and functioning of the supervisory and control systems. (Annual Report concerning the financial year 2007, paragraph 55(g))	In 2008 EuropeAid's central services performed eight monitoring missions. These missions were well designed and identified relevant recommendations to improve internal control in the Delegations examined. (Annual Report concerning the financial year 2008, paragraph 42)	Satisfactory action has been taken.	
8.	Compliance with the Cotonou Agreement should be benchmarked against baseline requirements, such as the availability of timely published and audited accounts, to be met before budget support is granted. (Annual Report concerning the financial year 2007, paragraph 56(a)) EuropeAid should ensure, before the start of a budget support programme, that there is a clear and complete assessment of the public finance management and that the recipient country has a credible and relevant reform programme to address all significant weaknesses over a foreseeable timetable. (Annual Report concerning the financial year 2007, paragraph 56(d))	In its Annual Reports on the EDFs concerning the financial years 2006 and 2007, the Court recommended that compliance with the Cotonou Agreement should be benchmarked against baseline requirements. The Commission did not accept this recommendation because it considers the setting of common minimum standards to be uniformly applied to all countries is inappropriate. As the European Parliament pointed out in its report on discharge for the financial year 2007, this approach gives the Commission a high degree of discretion which must be counter-balanced by an equally high degree of transparency. As stated by the Court in its Special Report No 2/2005 concerning EDF budget aid to ACP countries, this requires the assessment of compliance with the Cotonou Agreement requirements to be presented in a structured and formalised manner. (Annual Report concerning the financial year 2008, paragraph 45)	EuropeAid should pursue its efforts to support its decisions on the eligibility of budget support with a structured and formalised demonstration that the recipient country has a relevant reform programme to address all significant weaknesses over a foreseeable timetable and that there is commitment on the country's part to implement it. (Annual Report concerning the financial year 2008, paragraph 56(a))	<i>The Commission agrees and is further revising its guidance to address this point. It is expected that this will be completed by the end of 2009</i>
9.	The performance indicators used should permit clear evidence of progress in public finance management to emerge where appropriate. This could be achieved by strengthening indicators which measure progress of results over time in combination with process indicators on the performance of one-off events. (Annual Report concerning the financial year 2007, paragraph 56(b))	The Court will follow-up these observations in its non-DAS audits		

	Court observation	Court analysis	Court recommendations	Commission reply
10.	In order to set out its conclusions as regards progress in public finance management in a structured manner, the Commission should ensure that the data used as a basis for disbursement decisions is reliable and should rely more on measurements of events that have already taken place than on predictions of future occurrences. (Annual Report concerning the financial year 2007, paragraph 56(c))	The Court will follow-up these observations in its non-DAS audits		
11.	The quality of Financing Agreements should be improved by including general conditions in all cases, unambiguous stipulations and clear requirements for progress of public finance management. (Annual Report concerning the financial year 2007, paragraph 56(e))	As mentioned in the Court's Annual Report on the EDFs concerning the financial year 2007, the financing agreements of budget support programmes financed under the ninth EDF are often incomplete or unclear, and thus do not provide a sufficiently clear framework to carry out such a structured and formalised assessment. In 2008 the Court noted a significant improvement with the financing agreements of budget support programmes financed under the tenth EDF. In some cases there is scope for further improvement in the identification of both priority public financial management measures to be implemented by the recipient country as well as the sources of information to check compliance with the agreed conditions. (Annual Report concerning the financial year 2008, paragraph 46)	EuropeAid should ensure that all future financing agreements provide a comprehensive and clear basis for the assessment of compliance with payment conditions. (Annual Report concerning the financial year 2008, paragraph 56(b))	<i>The Commission welcomes the recognition by the Court that its ongoing efforts to improve the clarity and structure of eligibility assessments are showing noticeable results. Our focus is on continuing the process of improvement with the objective of eliminating any cases of ambiguity in our assessments. This is to be achieved through further refinements to guidance on budget support, training and promoting awareness of the importance of demonstrating eligibility in a structured and formal way.</i>
12.	A human resources policy should be developed on the basis of an analysis of the skills and knowledge needed in relation to the management of budget support in view of its increasing importance. (Annual Report concerning the financial year 2007, paragraph 56(f))	Candidates for budget support related posts are tested and selected based on proven budget support knowledge and skills. Budget support training delivered in the field has increased from 7 available courses in 2006 to 14 in 2007 and 24 in 2008. This is in addition to headquarters training, where the average participation from Delegations is 40 %. Annual regional seminars are also organised for budget support practitioners. (Commission's reply to paragraph 31 of the Annual Rapport concerning the financial year 2008)	Satisfactory action has been taken.	