

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

(2010/C 303/02)



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

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## THE COURT'S OBSERVATIONS

## INTRODUCTION

1. This Annual Report presents the Court's assessment of the European Development Funds (EDFs). Key information on the activities covered and spending in 2009 is provided in **Table 1**.

**Table 1 — European Development Funds — Key information**

(million euro)

Budget Title	Policy area	Description	Payments 2009	Management Mode
European Development Funds	8th EDF	Administrative expenditure	0	Centralised direct
		Operational expenditure	0	Central indirect
			20	Centralised direct
			152	Decentralised
			0	Joint management
			<b>172</b>	
	9th EDF	Administrative expenditure	4	Centralised direct
		Operational expenditure	36	Central indirect
			439	Centralised direct
			1 188	Decentralised
			177	Joint management
			<b>1 844</b>	
	10th EDF	Administrative expenditure	71	Centralised direct
		Operational expenditure	2	Central indirect
			663	Centralised direct
		110	Decentralised	
		261	Joint management	
		<b>1 107</b>		
Total administrative expenditure			75	
Total operational expenditure:			3 048	
<b>Total payments <sup>(1)</sup></b>			<b>3 123</b>	
<b>Total individual commitments <sup>(2)</sup></b>			<b>4 141</b>	
<b>Total global commitments <sup>(2)</sup></b>			<b>3 405</b>	

<sup>(1)</sup> Gross payments, excluding recoveries.

<sup>(2)</sup> The totals of individual and global commitments contain the decommitments.

Source: European Court of Auditors on the basis of data provided by AIDCO DataWarehouse.

## THE COURT'S OBSERVATIONS

**Specific characteristics of the European Development Funds**

2. The European Development Fund (EDF) is the main instrument for providing European Union aid for development cooperation to the African, Caribbean and Pacific (ACP) States and Overseas Countries and Territories (OCTs). It was created in 1957 under the Treaty of Rome.

3. The EDFs are funded by the Member States, governed by its own financial regulation and managed by a specific committee. The European Commission is responsible for the financial implementation of operations funded with resources of the EDFs. Within the Commission, almost all the EDF programmes are managed by the EuropeAid Cooperation Office (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 <sup>(1)</sup>. A small proportion of the EDF projects <sup>(2)</sup> relates to humanitarian aid and is managed by the Directorate-General for Humanitarian Aid (DG ECHO). The European Investment bank (EIB) manages the Investment Facility. The Investment Facility is not covered by the Court's Statement of Assurance or the European Parliament's discharge procedure <sup>(3)</sup> <sup>(4)</sup>.

4. The EDFs are managed under three main arrangements (**Table 1**): centralised, joint and decentralised management <sup>(5)</sup>. Under centralised management (40 % of payments in 2009), the Commission implements the aid activities directly; this relates mainly to budget support. Under joint management (14 % of payments in 2009), international organisations are responsible for implementing Community funded actions, provided that the accounting, audit, control and procurement procedures of the organisations offer guarantees equivalent to internationally accepted standards. EuropeAid's main partners are the United Nations' agencies and the World Bank. Under decentralised management (46 % of payments in 2009), the Commission entrusts the management of certain tasks to the authorities of the beneficiary countries. The principle of EDF decentralised management as regards the payment process is illustrated in **Diagram 1**.

<sup>(1)</sup> See Chapter 6 of the 2009 Annual Report of the Court of Auditors on the implementation of the budget.

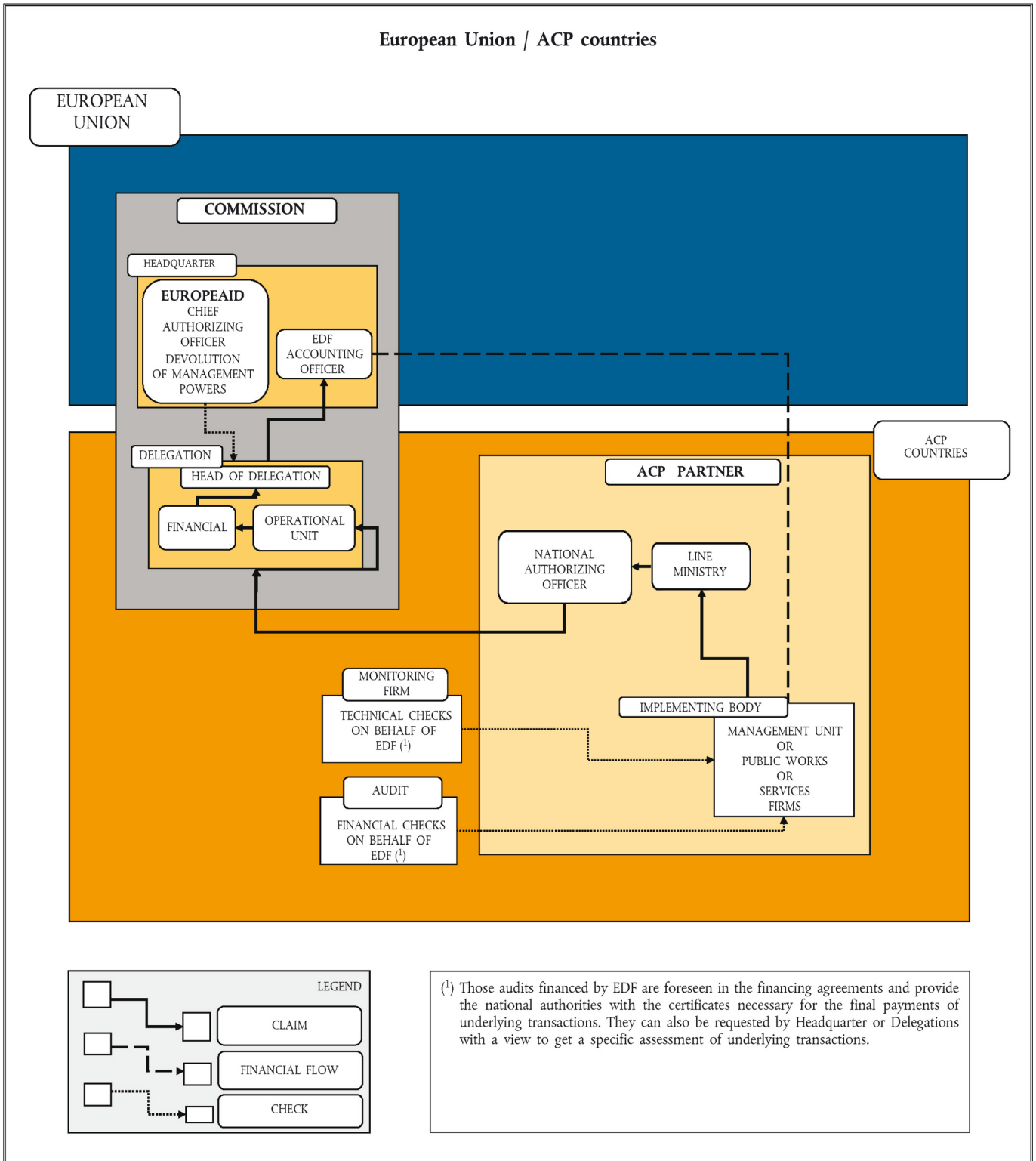
<sup>(2)</sup> Representing 0,9 % of 2009 payments.

<sup>(3)</sup> See Articles 118, 125 and 134 of Council Regulation (EC) No 215/2008 of 18 February 2008 on the Financial Regulation applicable to the tenth European Development Fund (OJ L 78, 19.3.2008, p. 1). 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.

<sup>(4)</sup> 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.

<sup>(5)</sup> Articles 21 to 29 of the Financial Regulation applicable to the tenth EDF.

Diagram 1 — Principle of Decentralised management as regards the payment process



## THE COURT'S OBSERVATIONS

5. EDF interventions are implemented in and by countries in which internal control systems are generally weak. The lack of capacity of most National Authorising Officers in beneficiary countries and weaknesses in the establishment and application of financial procedures and controls of implementing organisations and supervisors constitute a high risk for the regularity of transactions. The remoteness of many project sites and the existence of conflicts in certain regions also increase the difficulty to perform verifications.

**CHAPTER I — IMPLEMENTATION OF THE EIGHTH, NINTH AND TENTH EDFs****Financial implementation**

6. In 2009, the eighth, ninth and tenth EDFs were implemented simultaneously. Each EDF agreement is usually concluded for a period of around five years, whereby the programming cycles generally follow the partnership agreement/convention cycles. Although funds for each EDF are committed over a period of five years, payments can be made over a longer period.

7. Total contributions from the Member States amounted to 3 296 million euro received in 2009. Contributions are still being called up from the ninth EDF.

8. The tenth EDF covers the period from 2008 to 2013. It provides for Community aid worth 22 682 million euro and entered into force on 1 July 2008. Of this amount, 21 966 million euro are allocated to the ACP countries and 286 million euro to the OCTs. These amounts include 1 500 million euro and 30 million euro for the Investment Facility managed by the EIB for the ACP and OCT countries respectively. Finally, 430 million euro are earmarked for the Commission's expenditure for programming and implementation of the EDF.

## THE COMMISSION'S REPLIES

5. *The EDF is designed to help countries which are, by definition, in difficulty, and development aid policies must ensure that national authorities are in charge of development strategies. The National Authorising Officer plays a key part in this process. In order to ensure compliance with the applicable procedures and rules, a training programme specifically designed for staff in the offices of National Authorising Officers has been run for a number of years.*

6. *Although each EDF covers a period of around five years, the implementation of projects and programmes and the related payments may cover a longer period which is nevertheless limited by the regulations.*

## THE COURT'S OBSERVATIONS

9. **Table 2** shows the cumulative use of EDF resources managed by the Commission and their financial implementation. In 2009, the financial implementation forecasts set by the Commission for global commitments, and individual commitments were exceeded, reaching 3 406 million euro for global commitments and a record level of 4 140 million euro for individual commitments. Net payments amounted to 3 069 million euro which represented 92 % of the initial forecast. This shortfall is explained by the below forecast payments in countries subject to the consultation procedure laid down in article 96 of the Cotonou Agreement or other dialogue measures <sup>(6)</sup>, countries that had not yet ratified the Cotonou Agreement <sup>(7)</sup> and countries where budget support payments were not made due to that no confirmation had been provided as to the fulfilment of general or specific conditions <sup>(8)</sup>. Outstanding payments increased by 3 %, which is reasonable, given the gap between the level of global commitments and the net payments reached during the year. At the same time, old and dormant outstanding payments increased by 23 %, which is explained by the high level of global commitments made in 2007 so as to use up the remaining resources of the ninth EDF, but which did not lead to the same level of individual commitments.

## THE COMMISSION'S REPLIES

9. *The exceptional performance in relation to global and individual commitments testifies to the success of the policy adopted by the Commission to speed up programme implementation.*

*The increase in outstanding payments in 2009 is explained by the particularly high level of commitments in 2007 and by the EDF project cycle, which lasts on average three years, with the biggest payments generally being made in the first year and at the end of the final year.*

<sup>(6)</sup> Madagascar, Mauritania, Niger and Guinea Conakry.

<sup>(7)</sup> Sudan and Equatorial Guinea.

<sup>(8)</sup> Malawi, Haiti, Democratic Republic of Congo and Ethiopia.

Table 2 — Cumulative use of EDF resources at 31 December 2009

(million euro)

	Situation at end of 2008		Budgetary implementation during the financial year 2009				Situation at end of 2009				
	Global amount	Implementation rate <sup>(2)</sup>	8th EDF <sup>(3)</sup>	9th EDF <sup>(3)</sup>	10th EDF	Global amount	8th EDF	9th EDF	10th EDF	Global amount	Implementation rate <sup>(2)</sup>
<b>A — RESOURCES <sup>(1)</sup></b>	<b>48 677,7</b>		0,8	1,0	66,6	<b>68,4</b>	10 786,7	16 632,8	21 326,7	<b>48 746,1</b>	
<b>B — USE</b>											
<b>1. Financial commitments</b>	<b>32 185,3</b>	<b>66,1 %</b>	- 41,7	- 53,8	3 501,0	<b>3 405,5</b>	10 744,4	16 579,0	8 267,4	<b>35 590,7</b>	<b>73,0 %</b>
<b>2. Individual legal commitments</b>	<b>24 880,8</b>	<b>51,1 %</b>	- 41,8	997,4	3 184,1	<b>4 139,7</b>	10 499,1	15 206,8	3 314,5	<b>29 020,5</b>	<b>59,5 %</b>
<b>3. Payments <sup>(4)</sup></b>	<b>20 031,1</b>	<b>41,2 %</b>	152,1	1 805,8	1 111,4	<b>3 069,3</b>	10 082,4	11 816,9	1 201,1	<b>23 100,4</b>	<b>47,4 %</b>
<b>C — Outstanding payments (B1-B3)</b>	<b>12 154,1</b>	<b>25,0 %</b>					662,1	4 762,1	7 066,3	<b>12 490,3</b>	<b>25,6 %</b>
<b>D — Available balance (A-B1)</b>	<b>16 492,5</b>	<b>33,9 %</b>					42,3	53,8	13 059,3	<b>13 155,4</b>	<b>27,0 %</b>

<sup>(1)</sup> Initial allocations to the 8th, 9th and 10th EDFs, co-financing, interest, sundry resources, transfers from previous EDFs and migration adjustments.

<sup>(2)</sup> As a percentage of resources.

<sup>(3)</sup> Negative amounts correspond to decommitments.

<sup>(4)</sup> Net payments after recoveries.

Source: Court of Auditors, based on the EDF Reports on financial implementation and Financial statements at 31 December 2009.

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THE COURT'S OBSERVATIONS

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

10. The Financial Regulation applicable to the tenth EDF <sup>(9)</sup> 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), as well as of the financial situation and the events that had a significant influence on the activities carried out in 2009.

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<sup>(9)</sup> Articles 118 and 124.

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

### Independent Statement of Assurance by the Court of Auditors on the eighth, ninth and tenth European Development Funds (EDFs) for the financial year 2009

I — Pursuant to the provisions of Article 287 of the Treaty on the functioning of the European Union and Article 141 of the Financial Regulation applicable to the tenth EDF, which also applies to previous EDFs, the Court has audited:

- (a) the 'Final annual accounts for the financial year 2009 of the eighth, ninth and tenth European Development Funds' which comprise the consolidated financial statements<sup>(10)</sup> and the consolidated report on the financial implementation of the 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<sup>(11)</sup>.

#### *Management's responsibility*

II — In accordance with the Financial Regulations applicable to the eighth, ninth and tenth EDFs, management<sup>(12)</sup> 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<sup>(13)</sup>, 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.

<sup>(10)</sup> 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.

<sup>(11)</sup> Pursuant to Articles 2, 3, 4, 125(4) and 134 of the Financial Regulation applicable to the tenth EDF this Statement of Assurance does not extend to the part of the EDFs resources that are managed by the EIB and for which it is responsible.

<sup>(12)</sup> 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.

<sup>(13)</sup> 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 2009 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 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**

VI — In the Court's opinion, the final annual accounts of the eighth, ninth and tenth EDFs present fairly, in all material respects, the financial position of the EDFs as of 31 December 2009, 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.

VII — Without qualifying the opinion expressed in paragraph VI, the Court draws attention to an understatement of the amount of guarantees received in respect of prefinancing and to an overstatement of the amount of retention guarantees disclosed in the notes to the financial statements.

### **Opinion on legality and regularity of the transactions underlying the accounts**

VIII — In the Court's opinion the revenue, commitments and payments underlying the accounts of the eighth, ninth and tenth European Development Funds for the year ended 31 December 2009, in all material respects are legal and regular.

IX — Without calling into question the opinion expressed in paragraph VIII, the Court draws attention to the high frequency of non-quantifiable errors affecting commitments and payments albeit not included in the estimation of total error.

X — The Court concludes that the Commission's supervisory and control systems are partially effective in preventing or detecting and correcting errors.

9 September 2010

Vitor Manuel da SILVA CALDEIRA

*President*

European Court of Auditors  
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## THE COURT'S OBSERVATIONS

**INFORMATION IN SUPPORT OF THE STATEMENT OF ASSURANCE****Audit scope and approach**

11. The observations regarding the reliability of the accounts of the EDFs, set out in paragraphs VI and VII of the Statement of Assurance, are based on an audit of the consolidated financial statements<sup>(14)</sup> and the consolidated report on the financial implementation of the eighth, ninth and tenth EDFs<sup>(15)</sup>. 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.

12. The Court's overall audit approach and methodology regarding the regularity of transactions underlying the accounts is described in Part 2 of Annex 1.1 to Chapter 1 of the 2009 Annual Report of the Court of Auditors on the implementation of the budget. The observations regarding the regularity of transactions of the EDFs, set out in paragraphs VIII to X of the Statement of Assurance, are based on the following components:

- (a) substantive testing of a representative statistical sample of 220 items, corresponding to 50 financial and individual commitments and 170 interim and final payments made by EuropeAid's central services and the Delegations. Where necessary, implementing organisations and final beneficiaries were visited on the spot in order to verify the 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 Delegations; this covered the following elements:
  - (i) ex-ante controls of contracts and payments by the authorising officers, including the National Authorising Officers,
  - (ii) monitoring and supervision,
  - (iii) external audits,
  - (iv) internal audit;
- (c) a follow-up of previous observations is summarised in **Annex 4**.

<sup>(14)</sup> 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.'

<sup>(15)</sup> 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.'

## THE COURT'S OBSERVATIONS

## THE COMMISSION'S REPLIES

**Reliability of the accounts**

13. The Court concludes that the accounts of the EDFs for the financial year ending 31 December 2009 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.

14. The 2009 annual accounts of the EDFs are the first set of accounts prepared using the new accrual based accounting system ABAC FED (the same system used for the General Budget of the European Union). It was implemented in February 2009 after the migration process from the previous cash-based accounting system (OLAS) had been successfully ended. The new system supports accrual based reporting better, for example, by reducing the number of manual adjustments needed to obtain accrual based accounts at year-end. The ABAC-FED has thus strengthened the accounting environment.

15. EuropeAid's ex-post controls identified an increased frequency of encoding errors<sup>(16)</sup>. While the Court's audit of the financial statements did not reveal material error due to such errors, these remain a source of concern as they may affect the accuracy of data used for the preparation of the annual accounts, in particular with respect to the cut-off exercise at year-end.

16. As announced in its reply to the 2008 Annual Report of the Court of Auditors on the EDFs<sup>(17)</sup>, the Commission has refined its method of estimating the provision for invoices to be received. The Court's audit confirmed the correct application of this method and found the amount of the accrued charges disclosed in the financial statements to be free from material error.

17. Note 2.2 to the financial statements regarding the ongoing amount of guarantees received in respect of pre-financing includes an amount of 413,6 million euro as at the end of 2009. The Court concludes that this amount was understated by 82,3 million euro, or 19,9 %.

**Reliability of the accounts**

13. The Commission agrees with the Court's observations on the reliability of the accounts of the EDFs for the financial year ending 31 December 2009. It notes that the accounts are prepared in accordance with the provisions of the Financial Regulation and the accounting rules adopted by the accounting officer.

14. The Commission agrees with the Court's observations on the 2009 annual accounts of the EDFs. It notes that the accounts are prepared using the new accrual based accounting system ABAC FED, which was implemented in February 2009 after the migration process from the previous cash-based accounting system (OLAS) had been successfully ended. The new system supports accrual based reporting better, for example, by reducing the number of manual adjustments needed to obtain accrual based accounts at year-end. The ABAC-FED has thus strengthened the accounting environment.

15. *In some cases migration to the new IT system for project management may have caused confusion in the encoding of dates. EuropeAid has organised a large number of training courses in Delegations and at headquarters to improve use of this system.*

*At the end of 2009 EuropeAid's central services also set up a department to monitor the quality of information encoded in CRIS, which should further improve the reliability of the data used to prepare the annual accounts.*

*As the Court points out, this had no material impact on the annual accounts.*

16. The Commission agrees with the Court's observations on the method of estimating the provision for invoices to be received. It notes that the Court's audit confirmed the correct application of this method and found the amount of the accrued charges disclosed in the financial statements to be free from material error.

17. *The Commission accepts this observation and the Authorising Officer has recorded the necessary corrections in 2010.*

*The Commission notes that the Court found a single error of 3.5 million euro identified in a sample of 39 contracts which was extrapolated.*

<sup>(16)</sup> E.g.: contract type, contract start and end dates.

<sup>(17)</sup> Paragraph 15 (O) C 269, 10.11.2009).

## THE COURT'S OBSERVATIONS

18. The amount of retention guarantees disclosed in note 5.1 to the financial statements was 186,2 million euro as at the end of 2009. The Court concludes that this amount was overstated by 58,4 million euro, or 31,4 %.

**Regularity of transactions**

19. The results of the transaction testing are summarised in **Annex I**.

*Revenue*

20. The Court's audit of revenue transactions did not find material error.

*Commitments*

21. The Court's audit of commitments did not find material error but a significant frequency of non-quantifiable errors. The errors detected concerned compliance with tendering rules, legal deadlines for the signature of contracts and provisions regarding mandatory guarantees. As regards budget support commitments, the Court found that, in the context of the Commission's dynamic interpretation<sup>(18)</sup>, EuropeAid demonstrated in a formalised and structured manner compliance with the Cotonou Agreement requirements.

*Payments*

22. The Court's audit of payments did not find material error<sup>(19)</sup>. However, it detected some errors which are analysed in paragraphs 23 to 25.

**Project payments**

23. The main types of quantifiable errors detected on project payments were the following:

- (a) accuracy: calculation errors;
- (b) occurrence: absence of invoices or other supporting documents for services rendered or goods supplied;
- (c) eligibility: expenditure incurred outside the implementation period or related to items not foreseen in the contract, undue payment of VAT or non-application of mandatory penalties.

## THE COMMISSION'S REPLIES

**18.** *The Commission accepts the observation, but notes that the Court found a single error identified in a sample of 39 contracts which was extrapolated.*

**21.** *The Commission would stress that no payment was made without the coverage of financial guarantees. The Commission welcomes the finding that budget support eligibility was demonstrated in a formalised and structured manner.*

<sup>(18)</sup> See paragraphs 28 and 29 of Special Report No 2/2005 concerning EDF budget aid to ACP countries (OJ C 249, 7.10.2005).

<sup>(19)</sup> The Court sets the materiality threshold at 2 %.

## THE COURT'S OBSERVATIONS

## THE COMMISSION'S REPLIES

24. The non-quantifiable errors concerned mainly non-compliance with applicable rules on bank guarantees, which may have a financial impact in the event of the insolvency of the contractor, and incorrect calculations of the reimbursement of advances from contractors.

**Budget support payments**

25. The Court's audit found budget support payments to be affected by a high frequency of non-quantifiable errors due to lack of formalised and structured demonstration of the compliance with payment conditions. The main explanation was that the Delegations' public finance management assessment reports did not explain the criteria against which progress had to be assessed (i.e. the steps that had to be taken and the results achieved during the period concerned), the progress made and the reasons why the reform programme may not have been implemented according to the recipient Government's plan. However, such errors mainly affected payments made under ninth EDF financing agreements (which did not provide a clear assessment framework) and additional budget support payments made under the Vulnerability (V) FLEX facility and Envelope B (emergency aid) to compensate for the social and economic impact of the global financial crisis and soaring food prices. Except in one case, payments made under the tenth EDF financing agreements were not affected by such errors (see paragraph 32).

**Effectiveness of systems**

26. The results of the systems examination are summarised in **Annex 2**.

27. As stated in paragraph 3, EuropeAid's mission is to implement most of the external assistance instruments<sup>(20)</sup> financed from the General Budget of the European Union and the EDFs. Therefore, unless otherwise specified, the Court's observations concerning both the effectiveness of supervisory and control systems and the reliability of the Director-General's annual activity report and declaration refer to all of EuropeAid's area of responsibility.

28. Overall, the Court assessed EuropeAid's supervisory and control systems as partially effective.

24. The Commission would point out that all the errors in calculating the reimbursement of advances were rectified before the end of the contract.

25. The Commission welcomes the observation that a substantial improvement in the demonstration of eligibility can be discerned under 10th EDF owing to clearer assessment frameworks that are now routinely used.

*In order to underpin this improvement and eliminate such errors, the Commission acknowledges the need to further reinforce the structured approach to demonstrating progress in public financial management. The Commission has therefore developed a revised framework for monitoring and reporting progress in public financial management which focuses on results achieved against initial baseline expectations. This revised format was finalised in June 2010 and country reports using this revised approach will be the basis on which eligibility will be assessed for disbursements for the remainder of 2010 and beyond. Against this background, the Commission expects to be able to demonstrate continued improvement in the level of non-quantifiable errors related to this issue in future DAS exercises.*

*For the emergency instruments referred to (Vulnerability (V) FLEX facility and Envelope B) the Commission maintained a rigorous approach to assessing eligibility as evidenced by a number of such programmes where disbursements were not made.*

28. EuropeAid has designed its controls to cover the full lifecycle of its multiannual projects. It believes that these supervisory and control systems are effective and have significantly improved year on year as reflected in the increase in the proportion of entirely regular payments found by the Court in its sample. The recommendations made by the Court in past years have been implemented and many of these improvements have been recognised by the Court, resulting in significant elements of the key control systems being judged 'effective'.

<sup>(20)</sup> 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.

## THE COURT'S OBSERVATIONS

*Ex-ante controls***EuropeAid's central services**

29. The Court assessed ex-ante controls by authorising officers in EuropeAid's central services as effective.

**Delegations**

30. The Court assessed ex-ante controls by authorising officers in the Delegations as partially effective at detecting and correcting errors.

31. In respect of project payments, weaknesses were found in the checks performed on the eligibility of expenditure, the calculation of the amounts claimed and the availability of the required supporting documents.

32. With regard to budget support, the Court's audit confirmed the improvement noted in its 2008 Annual Report on the EDFs <sup>(21)</sup>. Tenth EDF financing agreements provide clearer frameworks for the assessment of general eligibility conditions. In respect of the public finance management eligibility criterion, financing agreements refer to assessment schemes agreed between Governments, the Commission and other donors. These include Performance Assessment Frameworks which are to be used in the context of joint annual budget support reviews. The application of such frameworks for establishing priority objectives, timetables and the sources of information to be used facilitates formalised and structured progress assessments and thus promotes the transparency of disbursement decisions. However, specific conditions related to the performance-based disbursements of variable tranches are often not sufficiently clear in respect of target values for indicators, verification sources and calculation methods; this may affect the transparency of disbursement decisions.

33. Another improvement noted in 2009 was the Commission's introduction of new guidance on budget support to fragile states, which requires certain very basic elements to be in place as regards public finance management systems before budget support can be granted. The Commission also established a modified financial circuit which sets out a more logical sequence for the financial and operational checks in the payment approval process.

## THE COMMISSION'S REPLIES

**30.** *The Commission provides continuous training for staff at headquarters and in the Delegations under an extensive training programme tailored to the needs of external aid management.*

**32.** *The Commission welcomes the Court's recognition of a sustained improvement in the clarity of the assessment frameworks for the general eligibility conditions.*

*The Commission recognises the importance of similar clarity for specific conditions and performance-based disbursements. Where appropriate, the Commission is seeking to formally address the specific observations made by the Court in this regard by means of revisions to the respective Financing Agreements. At the same time, this issue is receiving closer attention during EuropeAid's peer review process (Quality Support Group) for the consideration of new programmes.*

**33.** *The Commission welcomes the acknowledgement by the Court of these two important contributions to ensuring budget support is delivered in a more structured and formalised way.*

<sup>(21)</sup> Paragraph 46.

## THE COURT'S OBSERVATIONS

## THE COMMISSION'S REPLIES

*Monitoring and supervision***Delegations**

34. The Court assessed the monitoring and supervision by Delegations as partially effective.

35. As in previous years, the Court found that the lack of capacity of most National Authorising Officers (NAO) in beneficiary countries resulted in poorly documented and ineffective checks. The Delegations frequently provide technical assistance to strengthen this capacity, but often with limited results, either because the National Authorizing Officers do not perform their tasks adequately or because of resource constraints or high staff turnover rates.

36. The Court's audit also detected shortcomings in the financial procedures and controls instituted by implementing organisations and supervisors:

- (a) weak controls of the eligibility of expenditure, inadequate filing and safeguard of supporting documents, weak accounting controls that do not ensure that the expenditure is correctly recorded and reported or do not prevent arithmetical errors from occurring;
- (b) for certain works contracts, inadequate supervisor controls of contractors' invoices.

37. In general, Delegations were aware of these weaknesses and had placed limited reliance on these controls, for example by re-performing certain checks, requiring mandatory and risk based audits or expenditure verifications before the financial closure of projects, or commissioning technical audits of ongoing works contracts. However, the Delegations are subject to resource constraints which often limit their capacity to perform certain activities, such as project monitoring on-site, training and supporting project management.

**EuropeAid's central services**

38. The Court assessed monitoring and supervision by EuropeAid's central services as effective.

35. *In addition to the support and technical assistance provided by Delegations to National Authorising Officers, EuropeAid runs a large number of training courses each year for staff in the offices of National Authorising Officers and specialised ministries. Extensive information on procedures is also available on EuropeAid's website.*

36. *The Commission notes that the control tools and procedures established in recent years are bearing fruit. Nevertheless, it promises to continue its efforts to train staff and disseminate information on management and control tools.*

- (a) *The Commission expects that the Financial Management toolkit for the beneficiaries to be made available towards the end of 2010. The main purpose of the Financial Management toolkit is to provide basic practical guidance in an easy-to-use format to help beneficiaries to comply with the financial management rules in EC financed external aid actions.*

37. *Delegations conduct a large number of additional checks to offset the weaknesses of National Authorising Departments.*

## THE COURT'S OBSERVATIONS

39. Audits mandated under the framework contract agreement provide valuable information on the weaknesses affecting projects' control systems and on the level and nature of potentially ineligible expenditure. EuropeAid's central services analyse these results annually and follow up recurrent findings with the implementing organisations; these include missing or inadequate documentation and the use of incorrect procurement procedures. In particular, EuropeAid's central services are in the process of developing a financial management toolkit, which aims to address the causes of errors by increasing the knowledge and understanding of financial management rules by these implementing organisations. In 2009 EuropeAid's central services carried out 14 verification missions. In addition, the geographical Directorates performed their own visits to the Delegations at their own initiative. All these resulted in useful training and support as well as relevant recommendations for improving internal control in the Delegations examined.

40. EuropeAid's central services' analysis of the Delegations' bi-annual External Aid Management Reports indicates that high turnover and difficulties in finding staff with the appropriate expertise, especially for fragile countries, were the most common hindrances to effective aid implementation. The vacancy rates in Delegations have been included in EuropeAid's risk register as a critical risk for 2010.

41. EuropeAid's central services monitor compliance issues via transactional ex-post controls. They decided in 2009 to expand the scope of these controls to cover compliance with financing agreements and contract procedures with effect from 2010. In addition, EuropeAid intends to carry out an overall review of its approach in 2010 to explore ways to further improve the relevance and effectiveness of such controls as regards the examination of the regularity of the underlying transactions and the quality of ex-ante controls performed by authorising officers.

*External audits*

42. The Court assessed the external audits as effective with regard to EuropeAid's central services, and partially effective in respect of the Delegations.

43. The Court's audit found that the management of external audits improved significantly in 2009. The annual audit plans were prepared on the basis of structured risk assessments performed in accordance with EuropeAid's guidelines. Audits were performed in a timely manner, and the implementation rate of the consolidated annual audit plan improved as compared with previous years.

## THE COMMISSION'S REPLIES

39. *The Commission is pleased that the Court appreciates the measures taken by EuropeAid in following up audits and carrying out monitoring missions.*

40. *In the zero growth environment for Commission posts until 2013, EuropeAid is addressing staffing matters in Delegation with an active human resources policy within the limits of its competences. The issue of vacancies mainly concerns contract agents; it is not the high turnover as such but rather a matter of finding staff with the appropriate expertise. Their selection, previously managed by HQ, has now been delegated to Heads of Delegation to shorten this lengthy process. Simultaneously, EuropeAid continues to request regular new reserve lists with an adequate number of candidates to allow recruitments for all profiles and for every category of country.*

## THE COURT'S OBSERVATIONS

## THE COMMISSION'S REPLIES

44. The new terms of reference, adopted in October 2007, were used appropriately, thus promoting a more standardised audit approach. In the cases examined by the Court, audit conclusions had been acted upon, in particular as regards the financial correction of ineligible amounts through recoveries or deduction from subsequent or final payments. However, the full effect of the improved terms of reference was not yet visible in 2009 since many final audit reports were still based on the previous terms of reference, which were less precise, in particular as regards the wording of the audit opinion.

45. There remain several areas where improvement is necessary. Staff constraints in Delegations limit their capacity to launch risk-based audits, the priority being given to compulsory audits. They also have a negative impact on the length of the audit clearance process, which involves a risk that ineligible expenditure may become irrecoverable.

46. CRIS Audit has increased EuropeAid's capacity to monitor audit activities, as well as collate, analyse and act upon audit findings and recommendations. However, as in previous years<sup>(22)</sup>, and despite reminders from EuropeAid's central services and updated guidelines, not all Delegations record data in a timely and complete manner; this affects the reliability of the aggregate data used as management information, such as the nature of audit opinions and rates of ineligible expenditure. Furthermore, CRIS Audit does not always provide accurate data on the cost of audits, nor is it designed to provide information as regards financial corrections performed as the result of audits. As a result, EuropeAid does not yet make full use of the potential of this tool, in particular to ensure that its audit strategy is cost-effective.

### Internal Audit

47. The Court assessed internal audit as partially effective.

44. More than 95 % of the 2009 audit reports by the framework contractors were presented in the 'post 1 October 2007' format as opposed to about 40 % in 2008. (see AAR footnote 38 in section 3.1.2.1.2.)

45. While it is true that staffing constraints can have a negative impact on the length of the audit clearance process, the vast majority of audit reports must be received before the Commission makes final payment and therefore the risk that funds become irrecoverable is extremely limited.

In 2009 EuropeAid continued its efforts in the audit field and ran six EDF training courses covering 15 Delegations which were attended by 180 Delegation staff members and 220 outside staff (staff from the offices of Authorising Officers, ministries, project managers, NGOs and audit firms).

46. Delegations are regularly reminded of the need for timely updating of CRIS Audit records, including during audit seminars and training. Since February 2010, whenever a contract is signed for an audit (CRIS Contract), the date of signature is automatically transferred to CRIS Audit. Also, the new results screen is more complete and easier to fill in, and an audit cannot be closed if this field is not completed. This includes the audit opinion and the amount of ineligible expenditure. Information on recovery orders issued as the result of audits, is included in CRIS Recovery Order module. Some improvements could be considered with a view to consolidation, but would require further IT developments. Information is available on the amount of final ineligible expenditure detected and corrected at the time of final payment. In 2009 this represented 0.7 % by value of invoiced amounts.

47. The Commission considers that AIDCO's internal audit, despite the disruption of its operational capacity in 2009, was effective during that year. Despite the post of Head of the IAC Unit being vacant between 1 July and 15 November the unit finalised 9 follow-up audits (in relation to the 8 planned). As for new audits, out of the four planned for 2009, one final audit report and two draft audit reports (equivalent to 85 % of a final audit report according to IAS' methodology) were submitted in 2009.

<sup>(22)</sup> Paragraph 39 of the 2008 Annual Report on the EDFs.

## THE COURT'S OBSERVATIONS

48. The Internal Audit Capability (IAC) operated in compliance with its objective to provide the Director-General with assurance as to the effectiveness and efficiency of risk management, control and internal governance processes. However, its operational capacity was significantly disrupted due to staff shortages beyond its control, including the absence of the Head of Unit for most of the year. For these reasons the IAC was not fully able to implement its 2009 work plan. In its report on the second follow-up audit on the validation of the self-assessment of EuropeAid's IAC, the Internal Audit Service (IAS) mentioned again the significant amount of time needed for EuropeAid's management to follow up the IAC's recommendations.

*Reliability of Commission management representations*

49. The results of the review of the Commission's management representation are summarised in **Annex 3**.

50. The annual activity report gives a fair picture of the implementation and results of the various supervisory and control systems in place. It is clear and informative, in particular through its use of quantitative indicators. It states that, given the design and the results of its multiannual control architecture, EuropeAid does not believe that the residual error rate on its portfolio merits a reservation in the Director-General's declaration of assurance<sup>(23)</sup>. However, it does not provide evidence to support this assertion. In the absence of a key indicator for the estimated financial impact of residual error after all ex-ante and ex-post controls have been implemented<sup>(24)</sup>, EuropeAid is not in a position to demonstrate that the financial impact of shortcomings and errors remains below the materiality criteria set.

51. With respect to the financial year 2009, EuropeAid's Director-General declared that he obtained reasonable assurance that existing control procedures gave the necessary guarantees concerning the regularity of transactions. The Court's audit does not corroborate this assertion. It found that EuropeAid's systems were partially effective and that payments were overall affected by material error; whilst payments made from the EDFs were free from material error, payments made by EuropeAid from the General Budget of the Community for External Relations and Development were affected by material error<sup>(25)</sup>. The Court considers that the Director-General's declaration and annual activity report give a partially fair assessment of financial management in relation to regularity.

## THE COMMISSION'S REPLIES

50. The Commission believes that the qualitative and quantitative indicators set out in the four 'assurance' building blocks of the Annual Activity Report do indeed provide the evidence to underpin the Director General's statement of reasonable assurance. Nevertheless, EuropeAid recognises that further work could be done to develop specific indicators in relation to the multiannual control framework, and work started in 2010 on consideration of possible methodologies for the estimated financial impact of residual error.

<sup>(23)</sup> Page 56.

<sup>(24)</sup> See paragraphs 29 and 54 of the 2008 Annual Report of the Court of Auditors on the EDFs.

<sup>(25)</sup> See Chapter 6 of the 2009 Annual Report of the Court of Auditors on the implementation of the budget.

## THE COURT'S OBSERVATIONS

## THE COMMISSION'S REPLIES

**Conclusions and recommendations**

52. Based on its audit work, the Court concludes that the accounts of the EDFs for the financial year ending 31 December 2009 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 observations in paragraphs 17 and 18 concerning the amounts of guarantees.

53. Based on its audit work, the Court concludes that for the financial year ending 31 December 2009:

- (a) the revenue of the EDFs was free from material error;
- (b) the commitments of the EDFs were free from material error but affected by a significant frequency of non-quantifiable errors; and
- (c) the payments of the EDFs were free from material error. However, they were affected by frequent non-quantifiable errors.

54. As was already noted in the 2008 Annual Report of the Court of Auditors on the EDFs <sup>(26)</sup>, EuropeAid has set up a comprehensive control strategy. In 2009, EuropeAid continued to bring significant improvements to the design and implementation of its supervisory and control systems but weaknesses remain in certain areas. Based on its audit work, the Court concludes that EuropeAid's supervisory and control systems were partially effective in ensuring the regularity of payments. The following recommendations should be considered in this context:

- (a) EuropeAid should, in the context of its planned review of its overall control strategy, develop a key indicator for the estimated financial impact of residual errors after all ex-ante and ex-post controls have been implemented, based for example on an examination of a representative statistical sample of closed projects;
- (b) EuropeAid should, in the context of this review, assess the cost-effectiveness of the various controls, notably of the transactional ex-post control system;

54. EuropeAid has designed its controls to cover the full lifecycle of its multiannual projects. It believes that these supervisory and control systems are effective and have significantly improved year on year as reflected in the increase in the proportion of entirely regular payments found by the Court in its sample. The recommendations made by the Court in past years have been implemented and many of these improvements have been recognised by the Court, resulting in significant elements of the key control systems being judged 'effective'.

- (a) The Commission started work on the consideration of possible methodologies for the development of a key indicator for the estimated financial impact of residual errors in 2010, as set out in the Commission replies to the 2008 Annual Report.
- (b) The Commission started work on the review of its control strategy in early 2010, as set out in the Commission replies to the 2008 Annual Report. The Commission will produce a Communication on the Tolerable Risk of Error in the field of external aid in 2010.

<sup>(26)</sup> Paragraph 55.

## THE COURT'S OBSERVATIONS

- (c) EuropeAid should finalise and disseminate the financial management toolkit targeting the high inherent risk of errors at the level of implementing organisations, contractors and beneficiaries to ensure adequate knowledge of financial management and eligibility rules;
- (d) EuropeAid should continue its efforts to ensure that the Delegations record data in CRIS Audit in a comprehensive and timely manner;
- (e) the design of CRIS Audit should be modified to provide information on the amounts of final ineligible expenditure and financial corrections done after the audit clearance process with the auditee has been completed.

55. As regards budget support, the Court recommends that:

- (a) EuropeAid should ensure that the specific conditions for performance-based variable tranches clearly specify the indicators, targets, calculation methods and verification sources;
- (b) EuropeAid should ensure that Delegations' reports provide a structured and formalised demonstration of public finance management progress by clearly setting the criteria against which progress was to be assessed (i.e. the results that the recipient Government had to achieve during the period concerned), the progress made and the reasons why the reform programme may have not been implemented according to plan.

## THE COMMISSION'S REPLIES

- (c) *The Financial Management toolkit will be finalised in 2010 and due consideration will be given to the issues raised by the Court.*
- (d) *EuropeAid will continue its efforts to ensure that information is encoded in CRIS Audit accurately and in good time.*
- (e) *The amount of ineligible expenditure must be introduced in CRIS Audit before closing an audit record (mandatory field since February 2010). Information on recovery orders issued as a result of audits, is included in CRIS Recovery Order module. Some improvements could be considered with a view to consolidation but this would require further IT developments. Information is available on the amount of final ineligible expenditure detected and corrected at the time of final payment. In 2009 this represented 0,7 % by value of invoiced amounts.*

55.

- (a) *The Commission recognises the importance of greater rigour in defining performance targets, calculation methods and verification sources. This issue is receiving greater attention during EuropeAid's peer review process (Quality Support Group) for the consideration of new programmes.*
- (b) *The Commission has developed a revised framework for monitoring and reporting on progress in public financial management which focuses on results achieved against initial baseline expectations. This revised format was finalised in June 2010 and country reports using this revised approach will be the basis on which eligibility will be assessed for disbursements for the remainder of 2010 and beyond.*

## ANNEX 1

## RESULTS OF TRANSACTION TESTING FOR THE EUROPEAN DEVELOPMENT FUNDS

	2009						2008	2007
	Projects		Budget Support		Total			
<b>SIZE AND STRUCTURE OF THE SAMPLE</b>								
Total of commitments:	40		10		50		45	60
Total of transactions (of which):	150		20		170		170	148
Advances	0		0		0		40	0
Interim/Final payments	150		20		170		130	148
<b>RESULTS OF TESTING</b>								
<i>(in % and numbers of transactions)</i>								
Transactions not affected by error	80 %	{120}	65 %	{13}	78 %	{133}	76 %	63 %
Transactions affected by error	20 %	{30}	35 %	{7}	22 %	{37}	24 %	37 %
<b>ANALYSIS OF TRANSACTIONS AFFECTED BY ERROR</b>								
<i>(in % and numbers of transactions)</i>								
<b>Analysis by type of error</b>								
Non-quantifiable errors	57 %	{17}	100 %	{7}	65 %	{24}	61 %	49 %
Quantifiable errors	43 %	{13}	0 %	{0}	35 %	{13}	39 %	51 %
<i>comprising:</i> Eligibility	23 %	{3}	0 %	{0}	23 %	{3}	44 %	68 %
Occurrence	23 %	{3}	0 %	{0}	23 %	{3}	38 %	21 %
Accuracy	54 %	{7}	0 %	{0}	54 %	{7}	19 %	11 %
<b>ESTIMATED IMPACT OF QUANTIFIABLE ERRORS</b>								
Most likely error rate:								
< 2 %	X							
2 % to 5 %							X	X
> 5 %								

## ANNEX 2

RESULTS OF EXAMINATION OF SYSTEMS FOR EUROPEAN DEVELOPMENT FUNDS AND DEVELOPMENT AID  
UNDER THE GENERAL BUDGET

## Assessment of selected supervisory and control systems

System concerned	Ex-ante controls	Monitoring and supervision	External audits	Internal audits	Overall assessment
Central services EuropeAid					
Delegations				N/A	

## Overall assessment of supervisory and control systems

Overall assessment	2009	2008	2007

## Legend

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

## ANNEX 3

## RESULTS OF REVIEW OF COMMISSION MANAGEMENT REPRESENTATIONS FOR THE EUROPEAN DEVELOPMENT FUNDS AND DEVELOPMENT AID UNDER THE GENERAL BUDGET

Main DGs concerned	Nature of declaration given by Director-General (*)	Reservations given	Court observations	Overall assessment of reliability
AIDCO	without reservations	N/A	EuropeAid has set up a comprehensive control strategy and continued to bring significant improvements to the design and implementation of its supervisory and control systems. However, the Court's audit found that there remain weaknesses in certain controls and that the payments were affected by material error.	B

(\*) By reference to the Declaration of Assurance of Director-General, he/she has reasonable assurance that the control procedures put in place give the necessary guarantees concerning the regularity of transactions.

A: the Director-General's declaration and the annual activity report give a fair assessment of financial management in relation to regularity

B: the Director-General's declaration and annual activity report give a partially fair assessment of financial management in relation to regularity

C: the Director-General's declaration and the annual activity report do not give a fair assessment of financial management in relation to regularity

## FOLLOW-UP OF KEY STATEMENT OF ASSURANCE OBSERVATIONS

	Court observation	Court analysis	Court recommendations	Commission reply
1.	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. (2008 Annual Report, paragraph 54)	The 2009 Annual Activity Report presents fairly the implementation and results of supervisory and control systems in place. It is clear and informative, notably through the use of quantitative indicators. However, it does not provide a clear demonstration that the results of the various controls contribute to the Director-General's reasonable assurance that the financial impact from deficiencies and errors remains below the materiality criteria set.	EuropeAid should, in the context of its planned review of its overall control strategy, develop a key indicator on the estimated financial impact of residual errors after all ex-ante and ex-post controls have been implemented.	<i>The Commission started work on the consideration of possible methodologies for the development of a key indicator for the estimated financial impact of residual errors in 2010, as set out in the Commission replies to the 2008 Annual Report.</i>
2.	Ex-ante checks should be improved by focusing on key risks. (2008 Annual Report, paragraph 55(a))	There remain weaknesses in the verifications carried out in respect of the eligibility of expenditure, the calculation of the amounts claimed and the availability of the required supporting documents.	EuropeAid should finalise and disseminate the financial management toolkit targeting the high inherent risk of errors at the level of implementing organisations, contractors and beneficiaries to ensure adequate knowledge of financial management and eligibility rules.	<i>The Financial Management toolkit will be finalised in 2010 and due consideration will be given to the issues raised by the Court.</i>
3.	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. (2008 Annual Report, paragraph 55(b))	The annual audit plans were prepared on the basis of structured risk assessment performed as provided for by EuropeAid's guidelines. Staff constraints in Delegations limit their capacity to launch risk-based audits, the priority being given to compulsory audits. They also negatively impact on the delays for the audit clearance process, which involves a risk that ineligible expenditure may become irrecoverable.	Satisfactory action has been undertaken as regards the Annual Audit planning process.	<i>The Commission agrees that substantial improvements have been achieved in the audit planning process.</i>
4.	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. (2008 Annual Report, paragraph 55(c))	EuropeAid's central services, including the geographical Directorates, monitor regularly the implementation over time. Where necessary, deviations are investigated and corrective actions are undertaken.	Satisfactory action has been taken.	<i>The Commission agrees that substantial improvements have been achieved in the monitoring of the implementation of audit plans.</i>

	Court observation	Court analysis	Court recommendations	Commission reply
5.	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. (2008 Annual Report, paragraph 55(d))	CRIS Audit does not always provide accurate data on the cost of audits nor provides any information as regards financial corrections done as a result of audits.	The design of CRIS Audit should be modified to provide information on the amounts of final ineligible expenditure and financial corrections done after the audit clearance process with the auditee was completed.	<i>Following improvements introduced in CRIS Audit in February 2010, the amount of ineligible expenditure must be indicated before closing an audit record. As to recovery orders issued as the result of audits, this information is included in CRIS Recovery Order module.</i>
6.	EuropeAid should ensure that the Delegations record data in CRIS Audit in a comprehensive and timely manner. (2008 Annual Report, paragraph 55(e))	Despite reminders from EuropeAid's central services and updated guidelines, all Delegations do not record data in a timely and complete manner. This affects the reliability of aggregate data used as management information, such as the nature of audit opinions and rates of ineligible expenditure.	EuropeAid should continue its efforts to ensure that the Delegations record data in CRIS Audit in a comprehensive and timely manner.	<i>EuropeAid continues its efforts to ensure correct and timely encoding of data in CRIS Audit.</i>
7.	In the light of the results of the approach adopted by Directorate C 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. (2008 Annual Report, paragraph 55(f))	EuropeAid expanded the scope of these controls in 2009 to cover compliance with financing agreements and contract procedures. EuropeAid intends to carry out in 2010 an overall review of its approach to explore ways to further improve the relevance and effectiveness of such controls as regards the examination of the regularity of the underlying transactions and the quality of ex-ante controls performed by authorising officers.	EuropeAid should, in the context of the review, assess the cost-effectiveness of the various controls, notably of the transactional ex-post control system, and examine the relevance and feasibility of an annual audit of a representative statistical sample of closed projects.	<i>The Commission started work on the review of its control strategy (including a possible indicator for the residual error rate based on an audit of a representative statistical sample of closed projects) in early 2010, as set out in the Commission replies to the 2008 Annual Report. The Commission will produce a Communication on the Tolerable Risk of Error in the field of external aid in 2010.</i>
8.	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. (2008 Annual Report, paragraph 56(a))	Tenth EDF financing agreements provide clearer frameworks for the assessment of general conditions on eligibility. In respect of the public finance management related criterion, financing agreements refer to assessment schemes agreed between Governments, Commission and also other donors, such as the Performance Assessment Frameworks (PAF) to be used in the context of joint annual budget support reviews. The application of such frameworks defining priority objectives, timetables and the sources of information to be used facilitates formalised and structured progress assessments and thus promotes the transparency of disbursement decisions.	Satisfactory action has been taken.	<i>The Commission agrees that substantial improvements have been achieved in the decision making framework for budget support eligibility, and for disbursement conditions.</i>

	<b>Court observation</b>	<b>Court analysis</b>	<b>Court recommendations</b>	<b>Commission reply</b>
9.	EuropeAid should ensure that all future financing agreements provide a comprehensive and clear basis for the assessment of compliance with payment conditions. (2008 Annual Report, paragraph 56(b))	Specific conditions related to performance based disbursements of variable tranches are often not sufficiently clear in respect of target values for indicators, verification sources and calculation methods; this may affect the transparency of disbursement decisions.	EuropeAid should ensure that specific conditions for performance-based variable tranche define clearly the indicators, targets, calculation methods and verification sources.	<i>The Commission recognises the importance of greater rigour in defining performance targets, calculation methods and verification sources. This issue is receiving greater attention during EuropeAid's peer review process (Quality Support Group) for the consideration of new programmes.</i>