



National Audit Office

# Financial Management in the European Union

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# SUMMARY

**1** In 2005, expenditure by the European Union totalled €104.8 billion (£71.7 billion)<sup>1</sup> and its revenue was €105.7 billion (£72.3 billion). The United Kingdom made a net contribution to the European Union of €3.7 billion (£2.5 billion), comprising payments of €12.2 billion (£8.3 billion) after deducting an abatement of €5.2 billion (£3.5 billion), less receipts of €8.5 billion (£5.8 billion).

**2** In October 2006, the European Court of Auditors (the Court) published its report on the implementation by the European Commission (the Commission) of the 2005 budget. For the twelfth successive year the Court decided not to provide a positive Statement of Assurance on the legality and regularity of European Community expenditure. The Court concluded that the Community's accounts faithfully reflected revenue and expenditure

for the year but some errors were noted in relation to balance sheet items. The underlying transactions taken as a whole were legal and regular with respect to revenue, administrative expenditure and expenditure on pre-accession<sup>2</sup> but there were material errors on the main operational programmes, although progress was maintained on agricultural payments subject to the Integrated Administration and Control System.

**3** In January 2005, the Barroso Commission made it a strategic objective to strive for a positive Statement of Assurance from the Court. The Commission has embarked on a number of initiatives aimed at improving financial management and, in January 2006, it published an Action Plan setting out a series of measures designed to achieve a positive Statement of Assurance.

4 This report, following similar reports produced by the National Audit Office in previous years: summarises the main findings from the Court's work; provides an update on the various initiatives at European and national level to improve financial management; and sets out the information available on the level of irregularities and possible fraud. Our approach and methods used in this examination are summarised in Appendix 1.

## Main findings and conclusions

5 The Court's latest report suggests that the improvements in financial management noted in recent years, for example the strengthening of the declarations provided by Directors-General in their Annual Activity Reports, were consolidated in 2005.

6 In 2005 the Commission produced the annual accounts on an accruals basis for the first time. This development was achieved within an ambitious timescale. The Court noted some errors in its implementation which the Commission will need to address in order to move towards a positive Statement of Assurance on the reliability of the accounts.

7 The lack of a positive Statement of Assurance does not indicate that European Union expenditure is subject to an excessive level of fraud. OLAF, the European anti-fraud office, has strengthened the systems for Member States to report potential fraud although it still has difficulty in ensuring that all Member States report fraud accurately and promptly.

8 Significant further progress towards a positive Statement of Assurance depends on success in implementing the Commission's Action Plan and in addressing the issues noted by the United Kingdom Committee of Public Accounts in its 2005 report *Financial Management in the European Union*.<sup>3</sup> In particular this involves simplifying the rules and regulations governing European Union programmes. Efforts to simplify regulations must be maintained, while ensuring that they are sufficiently clear to avoid disputes between the Commission and Member States. The United Kingdom authorities, with other Member States, should work to ensure that the Commission's intention to simplify the framework of regulations governing programmes is carried through into the day-to-day regulations governing the management of programmes.



9 The risk of errors occurring in the administration of programmes is increased by delays in closing programmes. Delays in closing some 1994-1999 Structural Measures programmes, for example, continue to divert administrative resources, in both the Commission and Member States, away from managing the current programmes. Setting up new programmes while others are running down requires officials to work to different sets of rules drawn up for different time periods. Prompt and efficient closure of the 2000-2006 programmes is essential if the Commission is to reduce errors and thereby increase the chances of obtaining a positive Statement of Assurance.

10 The Court's report notes some weaknesses in the United Kingdom's management and control of Structural Measures programmes. As recommended in our report last year, the Department for Communities and Local Government and the Department for Work and Pensions should redouble their efforts to ensure that the guidance they issue to the relevant public bodies makes clear the scheme requirements and that day-to-day management checks are carried out. The relevant United Kingdom authorities should ensure that their risk management arrangements place sufficient, yet proportionate, emphasis on the need for proper control and management of European Union funds.

**11** In November 2006 Her Majesty's Treasury announced that the United Kingdom will produce a consolidated national Statement of Assurance on the use of European Union funds.<sup>4</sup> The Government intend to lay before Parliament such a statement which will be prepared to international accounting standards and audited by the National Audit Office, also to international standards. The Commission has endorsed this initiative, which might provide a useful source of assurance for the whole Community were it to be adopted more widely. The United Kingdom Government should seek the agreement of the other 26 Member States to adopt a similar approach in their jurisdictions.

**12** In its 2005 report *Financial Management in the European Union*, the United Kingdom Committee of Public Accounts urged the Court to consider arranging a peer review of its audit approach and to test the quality and relevance of its work. The Court is currently preparing for an external peer review. In advance of this, the Court has carried out a self-assessment using a structured model developed by the European Institute for Public Administration and the Innovative Public Service Group. The self-assessment has resulted in an action plan that is currently being implemented.

## Overall conclusion

**13** There has been welcome progress in strengthening the financial management of European Union funds. Producing accruals-based accounts for 2005 was a considerable achievement by the Commission. The achievement of a positive Statement of Assurance nevertheless remains a significant challenge for the future. It is essential to maintain the momentum which will involve support and cooperation by all the authorities – the Commission, the Council of the European Union, the Court and Member States.