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SIMPLIFICATION AND PROPORTIONALITY IN MANAGEMENT AND CONTROL SYSTEMS OF COHESION POLICY

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POLICY DEPARTMENT B: STRUCTURAL AND COHESION POLICIES

REGIONAL DEVELOPMENT

SIMPLIFICATION AND PROPORTIONALITY IN MANAGEMENT AND CONTROL SYSTEMS OF COHESION POLICY

NOTE

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Abstract

The European Commission proposal for a Regulation on common provisions for Structural and Cohesion Funds 2014-2020 includes proposals for simplification and proportionality through the merger of authorities, a new system of accreditation and annual clearance and rolling closure of accounts. These proposals raise a number of issues and have met with considerable resistance on the part of the Member States and the European Court of Auditors. This briefing note seeks to highlight the arguments and propose recommendations for dealing with these issues.

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LIST OF ABBREVIATIONS

CAP	Common Agricultural Policy
CFP	Common Fisheries Policy
CMO	Common Market Organisation
COM	European Commission
CoR	Committee of the Regions
CPR	Common Provisions Regulation
CSF	Common Strategic Framework
EAFRD	European Agriculture Fund for Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
ECA	European Court of Auditors
ECOSOC	Economic and Social Committee
EMFF	European Maritimes and Fisheries Fund
ERDF	European Regional Development Fund
ESF	European Social Fund
ETC	European Territorial Cooperation
ITI	Integrated Territorial Investment Plans
MMF	Multiannual Financial Framework
MS	Member State
TFEU	Treaty of the Functioning of the EU

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EXECUTIVE SUMMARY

The subject of this briefing note is the reform of the architecture of the management and control authorities and the proportionality principle in auditing presented in the Commission Proposal for a Regulation on common provisions for Structural and Cohesion Funds 2014-2020 (the draft CPR Regulation).

One of the overarching objectives of the regulatory amendments is simplification. Management and control systems should find a balance between costs and the risks involved. The draft CPR Regulation is largely built on the provisions of the amended Financial Regulation 1995/2006 and the Commission proposal for a new Financial Regulation (COM(2010) 815 final). A major change is the introduction of an accreditation procedure for managing and certifying authorities. This instrument is expected to reduce bureaucracy and cost since it would be possible to merge both functions within one authority.

It is further intended to put more emphasis on proportionality and a risk based approach. Hence, small interventions are expected to carry lower risks and will thus be exempt from a regular Commission review. It is expected that such a more risk-based approach reduces transaction costs as Commission resources can be allocated more efficiently to areas with higher risk. Without further explanation in the draft Regulation it is not convincing that smaller interventions are less prone to risk.

The proposal also foresees a mandatory annual closure of completed operations or expenditure in the framework of the annual clearance of accounts. This aims to reduce the burden associated with a long retention period of documents for individual beneficiaries and the risks associated with the loss of the audit trail.

The key elements:

- Merger of authorities
- New accreditation process
- Annual clearance and rolling closure

Of the proposed future legislative package were analysed in desk research and interviews with stakeholders in some Member States (Germany, Ireland and Slovenia). It should be mentioned that the draft CPR Regulations (especially the institutional provisions addressed in this note) have not undergone a feasibility study at EU or at national level, neither from a legal nor from an economic point of view, and that the note thus also draws on the sometimes contradictory arguments which constitute the debate at EU and Member State level. Despite some positive feedback, especially on the rolling closure, the provisions of the draft CPR Regulation addressed in this note seem to have triggered an overwhelmingly negative reaction of the Member States in relation to the new accreditation provisions and the intended merger of authorities.

The results are presented in chapters relating to the key elements of the institutional changes and the application of the proportionality principle in the auditing exercise.

The merger of authorities

Member States have always had the option of having one authority to manage the tasks of the Managing Authority and the Certifying Authority (even of the entire management and control system) as long as there was functional independence among the units within the one authority. In contrast to the mainstream programmes, the current proposal of merger of authorities is however obligatory and hence of practical relevance for the ETC programmes – Art. 22 of the ETC draft Regulation stipulates that the Managing Authority "*shall* additionally carry out the functions of the Certifying Authority". For the multi-level and bi/multi-national set-up of the ETC programmes any reduction of complexity could be a relief for the management and implementation of the programme. The question is whether an intended simplification through a merger of authorities is not outweighed by the effects of a re-organisation of existing systems and new tasks and functions assigned to the Managing Authorities.

Accreditation

The decision of mandatory accreditation is based on the apparently positive experiences with the accredited paying authorities in the CAP. The question is if it makes economic sense in relation to Cohesion Policy. A number of aspects need to be considered: The first is the assurance of efficient and responsible expenditure (accountability), the second is financial risk associated with legal uncertainty and the third is related to institutional costs that should be reduced but run the risk of being increased.

In legal terms, the major question relates to the reconcilability between accreditation of a public national authority required by the Commission and the national administration law that may not include provisions for accrediting national authorities by other national authorities.

Both the Member States and the European Court of Auditors (ECA) seem to hold the view that, even though the draft CPR Regulation calls for simplification of assurance and further result orientation of policy, the proposed architecture appears to be threatening to achieve the opposite.

The application of the proportionality principle in the auditing exercise

It goes without saying that the effort of control should be proportional to the financial input of a public intervention (i.e. the expenditure). However, the audit costs in small programmes are relatively higher than in large programmes. This skewed proportion is a major strain on the budget available. The Commission aims to address this problem by introducing financial ceilings beneath which a simplified approach is allowed. This should be possible on the one hand for programmes below the threshold of Euro 250 million (Articles 113, 117 and 140) and on the other hand for operations for which the total eligible expenditure is below or equal to Euro 100,000 (Article 140).

The main weakness of the proportionality approach adopted by the Commission is the arbitrary definition of financial thresholds and the absence of a genuine risk-based approach. Also the possible argument that operations of that small size are less affected by the failure in properly applying public procurement or state aid rules (because they are below the de minimis threshold), usually representing the bulk of irregularities in Cohesion Policy, is not fully convincing.

Annual clearance of accounts

In the best case, the annual clearance of accounts could facilitate a rolling partial closure of programmes. The main advantage of this would be the gradual clearance of accounts (strengthening the discharge exercise) rather than having a huge workload at the end of the programming period. The rolling closure approach could have the advantage of increasing legal certainty for beneficiaries and reducing the audit burden implied by the rules on the retention of documents. However, a mandatory annual clearance of accounts is not really commensurate with the multi-annual perspective of EU Cohesion Policy. According to some observers, the annual part-closure would imply a massive increase of audit effort in the Member States which again might imply considerable additional bureaucratic costs. Since there is no guarantee that the annual clearance will be approved quickly by the Commission, it is also doubtful that the latter will really contribute to a shorter retention period of documents.

Legislative procedures

Following the Lisbon Treaty, the system of comitology was reformed. With Articles 290 and 291, Treaty of the Functioning of the EU (TFEU), delegated and implementing acts were introduced. These acts relate to non-essential elements of EU legislation that may be handled by the COM. Delegated acts are considered important for many decision relevant procedures in Cohesion Policy and the CAP.

Recommendations

The recommendations are structured in accordance to the two leading questions of this briefing note: Merger of authorities and accreditation, and proportionality. They suggest that a genuine risk-based approach taking account the empirical evidence of error in sectors and geographical regions seems to be superior to the relatively inflexible system of mandatory accreditation and the general financial thresholds for programmes and operations. The application of accreditation could be considered as an auxiliary instrument to foster assurance in countries where audits in accordance to Article 62 of Regulation 1083/2006 suggest a high error rate. In countries with a low prevalence of error in the samples the principle of single audit should be pursued. This would relieve the burden of the Commission to audit operations in addition to the corresponding activities of the audit authorities. If this is not an option then the role of the audit authorities should at least not overlap with those of an Accrediting Authority. Failing that, there should at least be a legal assessment of feasibility of the new proposals which has not been done so far.

As regards the merger of authorities, the differentiation between mainstream programmes where the merger is facultative and the ETC programmes where it is compulsory should be abandoned and the option should be facultative for both types of programmes.

Regarding proportionality, the approach of annual clearance should be further scrutinized in its theory and practical feasibility by launching a survey or study on possible benefits and costs in Member States before casting the draft provisions into final legislation. An EU wide uniform sampling approach is recommended. Monetary unit sampling could be considered as an approach emphasizing larger operations statistically but not leaving out the smaller ones.

The application of implementing and delegated acts has been an important improvement for policy management at the Commission level. However, there should be a more responsible handling of the TFEU provisions, especially regarding a too lax interpretation of what is non-essential and what are key elements - the latter should be adopted with full parliamentary codecision in order to ensure the appropriate legitimacy of the legal framework.

1. KEY ELEMENTS OF THE INSTITUTIONAL CHANGES

KEY FINDINGS

- Member States have always had the option of combining the tasks of Managing Authority and Certifying Authority in one authority providing there was functional independence between the units dealing with the two tasks.
- The merger of authorities is only mandatory for the ETC programmes, for the others it remains optional.
- While the reduction of complexity through the merger of authorities could be a relief for the multi-level and bi/multi-annual set up of the ETC programmes, the question is whether the intended simplification through the merger of authorities is not outweighed by the effects of the reorganisation of the existing systems.
- While the mandatory accreditation of paying authorities in the CAP seems to meet with approval, the proposed accreditation exercise in the framework of Cohesion Policy is met with scepticism in particular concerning accountability, financial risk and institutional costs.
- Given the lack of a feasibility study, it is also questionable whether the mandatory accreditation is in line with national administration law.

1.1. The proposed changes in the CPR Regulation: A substantial reform raising important questions in the Member States

In October 2011, the European Commission adopted a draft legislation package for the future EU Cohesion Policy in the period 2014-2020, with allocations amounting to Euro 376 billion (including Euro 40 billion for the Connecting Europe Facility). In addition to this, the CAP and the fisheries policies, which are not part of Cohesion Policy but strongly linked to it, will contribute with further Euro 97 billion. In this package the European Commission has introduced a major reform effort, comprising important changes in the design and modes of implementation of Cohesion Policy. The new legislative package is aimed at responding to absorption and effectiveness issues implied by the financial crisis since 2008 and to foster the important role of EU Cohesion Policy in delivering the Europe 2020 Strategy. The Multiannual Financial Framework (MFF) proposal is negotiated in a different framework than the legislative package whereby the EP has the power of consent but not co-decision. The negotiations on the MMF should be finalised at the end of 2012.

The character of the new package can be described by stronger co-ordination between Cohesion Policy and the European Agriculture Fund for Rural Development (EAFRD) and the European Maritimes and Fisheries Fund (EMFF) through a Common Provisions Regulation (CPR)[1], a concentration on the Europe 2020 Strategy, more emphasis on incentive in rewarding performance, some more preference on integrated programming through multi-

[1] European Commission (2011d), *Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund covered by the Common Strategic Framework and laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1083/2006.*

fund interventions, focusing on results through better monitoring tools and progress towards agreed objectives, reinforcing territorial cohesion and simplifying delivery through different kinds of simplified cost options and eligibility.

Major amendments of the regulatory framework relate to

- The reduction to only one objective: Investment in growth and jobs
- The introduction of an intermediary layer of target regions (75-90% of the EU GDP average) instead of phasing-in or phasing-out regions
- The introduction of Partnership contracts between the European Commission and the Member States setting out the overall contribution, at national level, to the thematic objectives and the commitments to concrete actions in delivering Europe 2020 objectives
- The introduction of ex-ante, ex-post and macro conditionalities
- Integrated programming, common management arrangements
- More devolution to local spatial levels (LEADER approach, ITI)
- Joint Action Plans which represent an extension of the present system of simplified costs to all types of operations[2]
- Re-introduction of the performance reserve
- Use of "third generation" financial instruments (derivative financing through project bonds)[3]
- Stronger thematic concentration in innovation, SME competitiveness, R&D, low-carbon economy
- Application of lump sums, flat rates and/or standard unit costs to simplify financial management
- Differentiated risk-based audit procedures depending on the financial volumes
- Mandatory annual closure of operations within the annual clearance of accounts to relieve administrative burden of the beneficiaries
- Facultative merger of Managing Authority and Certifying Authorities, except for ETC programmes where the merger is compulsory (see below)
- An integrated programme and certification management through accreditation of the authorities
- More use of E-Cohesion Policy

[2] It appears that the Joint Action Plans do not replace the 'global grants' which are still mentioned in the CPR (Article 113). The management of part of an operational programme may be still be entrusted to an intermediate body by way of an agreement in writing between the intermediate body and the Member State or managing authority. Joint Action Plans are operations comprising a group of projects as part of an operational programme, with specific objectives, result indicators and outputs agreed between the Member State and the Commission and are distinct from major projects. (Article 93, CPR). The beneficiary of Joint Action Plans shall be a public law body.(Article 93). Payments to the beneficiary of a joint action plan shall be treated as lump sums or standard scales of unit costs (Article 98). The public support allocated to a joint action plan shall be a minimum of EUR 10 000 000 or 20 % of the public support of the operational programme or programmes, whichever is lower (Article 93) (cf. European Commission 2011d).

[3] This is especially aimed at materialising the « Connecting Europe Facility », that is part of the draft CPR regulation (cf. European Commission 2011c).

The new regulatory framework aims to enhance effectiveness and policy coherence of Cohesion Policy and to obtain more value for money. Nevertheless the framework appears highly complex and not yet fully consistent in its aims and in its approach. Some aspects are therefore subject to a critical debate that is presently going on between the managing authorities of Member States, the European Parliament (notably the REGI Committee) and the European Commission.

One of the overarching objectives of the regulatory amendments is simplification. Management and control systems should find a balance between costs and the risks involved. A major change is the introduction of an accreditation procedure for managing and certifying authorities. This instrument is expected to reduce bureaucracy and cost since it would be possible to pool both functions within one authority. However, some Member States believe that this central accreditation instance would not be commensurate with the principle of subsidiarity in accordance with Article 5 TFEU at least as long as EU Cohesion Policy is not centrally administered at the EU level. If managing and certifying authorities are sovereign national authorities, accreditation at the EU level will not be in line with national administrative law in a number of Member States. This is a central point at issue in Member States and will be further discussed in section 2 below.

It is further intended to put more emphasis on a risk based approach. Hence, small interventions are expected to carry lower risks and will thus be exempt from a regular Commission review. It is expected that such a more risk-based approach reduces transaction costs as Commission resources can be allocated more efficiently to areas with higher risk. Without further explanation in the draft Regulation it is not convincing that smaller interventions are less prone to risk. Especially in cases where a number of smaller interventions add up to a substantial share of a programme budget it is to apprehend that many risks will remain concealed. In its first opinion, the European Court of Auditors (ECA) has strongly criticized the assumption that small interventions are less risky than larger ones[4]. Some managing authorities have voiced a more massive warning that there is a further risk in an extended devolution of programme management to the local level. E.g. the introduction of Integrated Territorial Investment Plans (ITI) could limit the manoeuvring room of the programme administration and might thus lead to a higher error rate because of insufficient administrative capacity at the local levels.

The proposal also foresees a mandatory annual closure of completed operations or expenditure in the framework of the annual clearance of accounts. This aims to reduce the burden associated with a long retention period of documents for individual beneficiaries and the risks associated with the loss of the audit trail. Several managing authorities and the German Federal Council (Bundesrat) have disagreed to that new provision. The typical operations funded by Cohesion Policy have a multi-annual perspective. The mandatory annual closure is possibly not commensurate with the character of Cohesion Policy. According to some observers there is therefore a danger that the effort of controls will increase instead of relieving the situation. Because there is no guarantee that an annual closure will be approved by the Commission on time there is also not necessarily a warranty for the curtailment of the compulsory period of record keeping.

Further important measures are related to the simplified cost options. For the ESF and the ERDF the Regulations 396 and 397/2009 were already introduced for the current programming period. These two Regulations allow the application of a 20% flat rate of indirect costs incurred in operations, the application of standard unit costs (e.g. hourly wage rates) and lump sums for smaller expenditures (less than 50,000 Euro). The take-up

[4] European Court of Auditors (ECA), 2011a, *Opinion 7/2011*, p. 32.

of these new options has just started and not all Member States have already adopted these new provisions. Therefore, there is not yet much evidence of relevant experience to base decisions on, at least regarding the ERDF. First studies suggest that for the ESF, the application of the simplified cost options has led to a reduction of administrative burden; concerning the ERDF the picture is mixed. A number of beneficiaries interviewed in Austria reported that 20% flat rates are too inflexible and do not reflect the range of industry specific levels of indirect costs. The applied standard unit costs should ensure cost-coverage. Also, beneficiaries reacted with reluctance. First results suggest that for the programming period 2014-20, the Regulation should be more flexible than the Regulations 396 and 397/2009. It is not yet clear how future multi-fund financed operations will be addressed by simplified cost options. These are only applicable for ESF and ERDF. The EAFRD and the EMFF are exempt from those options but may be involved in local operations (LEADER or ITI) or common action plans.

Regarding the issues dealt with in this note, the draft CPR Regulation has triggered a mostly sceptical reaction of the Member States and other stakeholders such as the ECA. Among the most critically commented chapters are the provisions for simplification and financial management. This is noteworthy insofar as it was intended to reduce red-tape, administrative cost and burden and to improve the performance of the programmes by reducing dispensable transaction costs. This suggests that either the reforms for simplified financial management do not meet the needs of the programme stakeholders or the stakeholders have not yet fully conceived the purpose and approach of the draft Regulation. The latter explanation is unlikely, even though there is some evidence of cacophony among the commentators. As far as insufficient need orientation is the reason, the reluctance could be assumed as an important indicator for the feasibility of the new provisions.

Summarised in few words, the new draft CPR Regulation is aimed at optimising the balance of resource allocation and error rate: "The strap line ... for reforming the assurance system is a 'streamlined and simpler delivery model', while 'greater flexibility' and 'greater reduction of the risk of error' are identified as core priorities in the Commission's Budget reform proposals on Cohesion Policy..."[5].

The subject of this briefing note is focussed on the reform of the architecture of the management and control authorities (Key elements of the institutional changes) and proportionality principle in auditing. For the future Cohesion Policy in general and these fields in particular, the double goal of simplification and higher assurance can be described as follows:

[5] Mendez, C et al (2011), *Comparative study on the Visions and Options for Cohesion Policy after 2013,* European Parliament Study, EPRC University of Strathclyde, Glasgow.

Table 1: Simplification versus higher assurance in Cohesion Policy

SIMPLIFICATION (GENERAL)	BETTER ASSURANCE (GENERAL)
"The delivery system should be as simple and streamlined as possible to ensure efficient implementation and the reduction of administrative burden for beneficiaries." (CPR draft Regulation, p. 10)	"The proposal envisages a management and control system which is similar across shared management instruments and is based on common principles. A system of national accreditation is put in place to emphasize the commitment of Member States to sound financial management. The arrangements underpinning the assurance of the Commission with regard to the regularity of expenditure have been harmonised and new common elements such as a management declaration of assurance and annual clearance of accounts have been introduced to reinforce assurance." (CPR draft Regulation, p.9)
SIMPLIFICATION THROUGH ACCREDITED MANAGING AND CERTIFYING AUTHORITIES	**BETTER ASSURANCE THROUGH ACCREDITED MANAGING AND CERTIFIYING AUTHORITIES**
"It [the draft Regulation] also offers the possibility to merge the managing and certifying authority and thus decrease the number of involved authorities in the Member States. A smaller number of bodies in place would reduce the administrative burden and enhance the possibility for building stronger administrative capacity, but also permit a clearer distribution of responsibilities ... [control costs are expected to be reduced through the option to merge the managing and certifying authorities, which could allow the Member State to save a substantial part of the 4% of the current costs relating to certification due to better administrative efficiency, reduced need for coordination and reduction of the scope of audits;" (CPR draft Regulation, p. 167 f.)	"In order to reinforce accountability, programme authorities would be accredited by a national accrediting body in charge of their ongoing supervision. The proposal offers the flexibility to keep the current architecture of three key authorities by programme in cases where the current system has been proven to be effective." (CPR draft Regulation, p. 167)
SIMPLIFICATION THROUGH THE PROPORTIONALITY PRINCIPLE IN THE AUDITING EXERCISE	**BETTER ASSURANCE THROUGH THE PROPORTIONALITY PRINCIPLE IN THE AUDITING EXERCISE**
• "proportionate control arrangements for management verifications and for audits; • annual closure, which will reduce the cost of retention of documents for control purposes for public administrations and beneficiaries." (CPR draft Regulation, p. 168)	• "Annual closure of operations or expenditure, which decreases audit trail errors by shortening the time period for document retention and avoids the substantial build-up of administrative workload linked to the one-off closure at the end of the programming period." (CPR draft Regulation, p. 169) • the submission of certified annual accounts and an annual management declaration, which implies having carried out all necessary controls within the accounting year (which may require additional administrative effort); • the need for additional audit activity by the audit authorities to audit the management declaration or the need to finish its audits and express an audit opinion in a shorter period of time compared to the current obligations." (CPR draft Regulation, p. 168)

Source: CPR draft Regulation[6]

[6] European Commission 2011d, pp. 9, 10, 167ff.

1.2. The new role of the Member States in the field of accreditation

1.2.1. Proposed changes in the CPR and fund-specific Regulations and gaps in the Regulations

EU Cohesion Policy is implemented according to shared management. Implementation is delegated to the Member States along with the obligation to manage the programmes by ensuring legality and regularity of the expenditure. Through the establishment of an effective control system Cohesion Policy should become accountable at the level of Member States. The final responsibility for the EU budget remains with the Commission in fulfilling its supervisory role and making use of its mandate to implement financial corrections where irregularities have occurred. To keep Cohesion Policy effective, the right balance needs to be found between necessary assurance and the administrative burden imposed on Member State administrations and final beneficiaries.

The draft CPR Regulation is largely built on the provisions of the amended Financial Regulation 1995/2006 and the Commission proposal for a new Financial Regulation (COM(2010) 815 final)[7] and envisages (i) a facultative merger of the managing and certifying authorities and (ii) the mandatory accreditation of the Managing and Certifying Authorities in EU Cohesion Policy. The facultative merger of the managing and certifying authorities should contribute to simplification by reducing red-tape and administrative burden. There has always been the option that the tasks of Managing Authority and Certifying Authority (even of the entire management and control system) are carried out by one authority. The only condition has been a functional independence among the units within the one authority. As regards the new architecture, a study of the Committee of Regions points out that "… some simplification measures, such as the possibility to merge the managing and certifying authority, seem to be relatively minor in comparison to the administrative burden and the number of procedures that Member States and LRAs have to go through[8].

The decision of mandatory accreditation is based on the apparently positive experiences with the accredited paying authorities in the CAP.

> *"... Overall, the assessment of the management and control system in rural development policy by officials from DG Agri was generally very positive. The most crucial elements contributing to the good performance of the system were: the work of paying agencies and the annual certification, as well as the system of accreditation of the paying agencies involving a pre-accreditation audit by an independent body. Also, the programming at the level of individual measures based on a list of standardised rural development measures enabled gathering of financial information at measure level (e.g. the declaration of expenditure received by DG Agri at measure level on yearly basis)...."*[9]

As regards rural development programmes funded by the EAGGF/EAFRD, the Commission has not been directly involved in assurance of the paying authority as these had to be accredited by a recognised national authority. Assurance is based on criteria agreed at community level. Those have been permanently verified by the national accreditation

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[7] European Commission (2010a), *Proposal for a new Financial Regulation (COM(2010) 815 final)*, Brussels.

[8] Dhéret C et al (2012), *EU Financial Regulation: Analysis of the simplification measures* mentioned *in both the proposal for a EU Financial Regulation and the Cohesion Policy legislative package*, European Policy Centre, Brussels, p.20.

[9] CSIL (2010), *Lessons from shared management in cohesion, rural development and fisheries policies*, DG Regio study, Milan, p.51.

bodies. In assessing adequacy of EAFRD type accreditation patterns in Cohesion Policy one has to differentiate between the EAFRD policy system that has traditionally evolved as a more centrally administered EU policy and the EU Cohesion Policy that has traditionally been administered by shared management. Even though the second pillar of the CAP (rural development) has been also administered by shared management, its origin is the CAP. This might explain that there has been the need to accredit national authorities as they represent the interest of the European Commission (in terms of EU financial accountability) in the Member States. The major question is whether the positive experiences of accreditation of paying authorities in rural development programmes suggest doing something similar in Cohesion Policy.

Principally, the current system of management and control in Cohesion Policy has steadily improved as compared to the respective forerunner periods. Assurance has been improved through the introduction of important ex-ante preventative elements and there is now a better division of functions and responsibilities between the different actors at EU and national level. Some observers also expect that the system has meanwhile generated positive spill-over effects on administrative systems in Member States and enhancing administrative capacity[10].

In the current programming period (and also already during 2000-2006) the Managing Authorities for Cohesion Policy had to assure the Commission that the respective management and control systems are adequate. A corresponding report (since 2007 to be further accompanied by a formal statement of the Audit Authority or another recognised national audit body) was to be submitted to the European Commission in order to claim a first interim payment (Article 5 Regulation 438/2001 and Article 71 Regulation 1083/2008). In addition to that, the audit strategies were to be submitted to the COM, which retains the final decision competence. Hence, the European Commission has been largely involved in the assurance of the systems ("blanket" review by the Commission for all Operational Programmes as a quasi-accreditation at national level).

However, Cohesion Policy is still a policy field with unacceptably high error rates. Error is most prevalent in public procurement, state aid environmental policy rules and eligibility (see below). The commonly agreed threshold of maximum 2% could not be achieved[11].

The Commission assumes one of the major weaknesses of the former system of management and control was that there has been insufficient incentive for Member States to ensure an adequate control system due to a lack of independent opinion about the management and control system, as stated in an internal Commission working document "However, there was no independent verification by an audit body of the set up of the system at national level and there was no financial incentive for Member States to ensure that the set up of the system was adequate before submitting the systems descriptions...".[12]

For the current period the European Commission considers the assurance architecture as satisfactory: *"This approach is consistent with the overall approach for the 2007-13 programming period ..."* However, *"the Commission seeks to place greater reliance on the*

[10] Mendez et al (2011), p.108.

[11] In its annual report on the financial year 2010 the ECA points out that 19% of the 243 audited operations in cohesion policy were affected by errors in the application of public procurement law. Substantial errors were found in 5%. However, it has to be stated that the message of an average error rate is rather limited. One can establish a high variation both among the instruments and also geographically. Hence, the risk is not evenly distributed.

[12] DG Regio (2010), *Evaluation of the Compliance Assessment Process*, Brussels, p.1.

controls at national level and in particular, on the assurance provided by the Audit Authority ...".[13]

It is not clear whether and how the European Commission expects more efficiency and a lower error rate through more reliance on the controls at national level. There is only an indirect logic to the Commission expectation in that the control procedures will become more tailor-made (and thus efficient) when carried out under the sole responsibility of the Member States.[14] In fact DG Regio representatives expect that, when making the Member States fully accountable, it would enable the Commission to audit mainly programmes which appear problematic and would make it easier to stop payments or make financial corrections when needed. Furthermore, "... the compliance assessment process could be more proportional and better targeted, focusing on the assessment of systems of the most important programmes (in terms of financial volume)"[15].

This is an expectation that is based on (i) the correct assumption that misstatement among cohesion programmes is distributed unevenly but (ii) also on a less substantiated assumption, namely that a decentralised assurance would be inherently more efficient. In fact, it could be also possible (there is no reservation) for the European Commission to follow a more risk-based approach of assurance. Some member states plead for better control in the countries affected and voice a critical standpoint. The Austrian Court of Auditors stresses the uneven distribution of error, notably in geographical terms. It is pointed out that 95% of errors in ERDF programmes during 2000-2006 occurred in Spain (59%), Italy (32%) and the UK (4%).[16]. The trend described above has continued until now. In its recent Staff Working Paper on errors in Cohesion policy 2006-2009 the European Commission found that for ERDF and the Cohesion Fund still "nearly 60% of errors reported by the Court were identified in programmes in three Member States (ES, IT and the UK)", even though with a rather large variation in the single three years, and in 2007 also with a relatively high prevalence of error in Greece and the Czech Republic[17]. The activities launched by Commission to address the problem of error comprise closer monitoring and capacity building. However, there is no indication in the draft CPR allowing countries or regions with low occurrence of error to apply a simpler control system (e.g. without accreditation).

The following Figure 1 illustrates the relationship of monetary unit audit costs (the entire cost of auditing one Euro PPS spent) and the assurance rate of, say, two different countries. The cost intervals with decreasing marginal utility are the critical ones where to decide about limiting additional audit expenditure. A uniform approach based on the distribution of misstatement in the most error-affected regions would thus imply persistent over-auditing in the less error affected regions.

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[13] DG Regio (2010), p. 2.

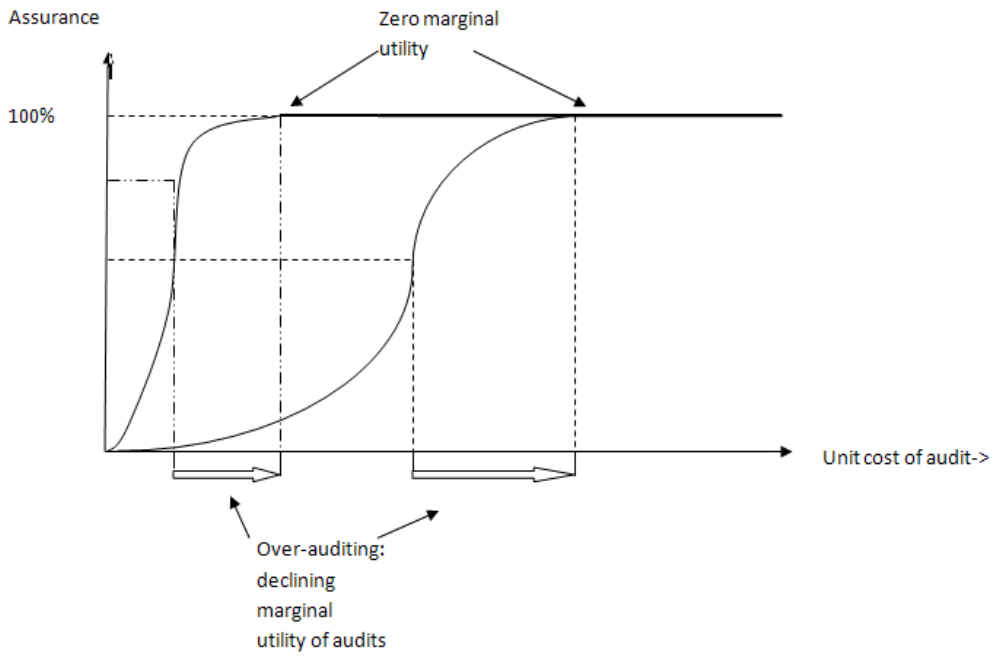
[14] The impact assessment on the draft CPR Regulation (SEC 2011/1141) points out that « … despite the progress made in comparison with 2000-2006, cohesion policy remains the policy group most affected by error, indicating further need for improvement. Furthermore, the current option with its blanket review arrangements can lead to inefficient use of resources, as they are not adjusted proportionately to the levels of risks involved. Commission resources in particular may be used in a suboptimal fashion, as equal resources are deployed in the compliance assessment of both very large and very small programmes. ».

[15] CSIL (2010), p. 54.

[16] Rechnungshof (2011), *Aktuelle Entwicklungen der EU-Finanzkontrolle: Reform der EU-Haushaltsordnung*, Wien, p. 10.

[17] European Commission (2011b), *Commission Staff Working Paper: Analysis of Errors in Cohesion Policy for the Years 2006-2009 – Actions taken by the Commission and the Way forward*, Brussels, p. 12. Interestingly, misstatement cannot be generalised for the countries mentioned but is concentrated in few programmes/regions of the member states.

Figure 1: Marginal audit utility compared



Source: PRAC Bergs & Issa Partnership Co., inspired by Austrian Rechnungshof 2011

This would make it also easier to apply a genuine single audit approach in countries with a low error rate and more scrutiny (also with a view to improve the institutional capacity) in the countries mentioned above[18]. Accreditation as proposed by the European Commission would be a fixed cost factor of control. Therefore it would be disadvantageous for regions with lower error rates. Accreditation – as far as it corresponds to national administration law - could then be better conceived as an auxiliary and temporary instrument in Member States with higher error rates, just to assure the European Commission that compliant systems are not only in place but also functioning. A general application of accreditation in all Member States, as proposed by the draft CPR Regulation seems inefficient[19].

[18] This is also advocated by the Dutch Ministry of Economic Affairs: « The Netherlands is in favour of varying the intensity of audits on the basis of risk selection. A review of the current audit practice, in consultation with the European Commission, the Member States and the European Court of Audit, is therefore necessary. » (Ministerie van Economische Zaken (2010), *The Future of Cohesion Policy: Joint Position Paper of the Dutch Central, Regional and Local Government*, The Hague). The interviewee from Slovenia argued that: "financial thresholds do seem rather rigid, so we do have preference for a more flexible, differentiated approach. All the empirical evidence coming out in the last year or two (e.g. concentration of errors in only a handful of MS) seems to suggest that differentiation based on risk assessment seems to be much more appropriate...".

[19] The fixed cost problem can also be regarded from another point of view. For small countries, the creation of new administration structures is relatively more costly than for bigger countries. This has been the critical remark of the interviewees from Ireland and Slovenia, as it would be the case here, e.g. : … » Inappropriateness of the proposal is especially obvious in centralized implementation systems, which tend to be used in small countries (like the Baltics or Slovenia). In such settings the accreditation body represents another (new) layer in the hierarchy, which will unavoidably significantly increase complexity of the system and further blur responsibilities! There would be no improvement in terms of error rates and efficiency of the system, if anything, things would get worse. Thus, the proposal should either be dropped altogether or at least derogation for centralised systems on the basis of proportionality argument should be allowed. … » (from the interview with the Slovene representative).

In the opposite sense – if one further contemplates this provision -, accreditation could also mean that the Commission would trust national authorities more than its own capabilities, what is certainly not the case. But the simple argument that accreditation would allow the Commission to better concentrate supervisory resources on the problematic programmes is not convincing. Accreditation is just a formal act but no guarantee of a lower error rate as long as accrediting authorities are not themselves supervised. Hence, the reasoning behind accreditation to reduce the error rate and to improve efficiency remains vague. By and large, the final rationale of accreditation, as a tool for improvement, is not sufficiently explained. Neither the draft CPR Regulation nor any fund-specific draft Regulation provides a clear-cut justification. At a first glimpse it appears to be the case that the European Commission strives to get rid of the major responsibility of overall financial accountability by delegating responsibility to the national authorities (as an "Black Peter" principle). In fact, especially in Cohesion Policy the European Commission has been suspected to execute a police function with widespread perception of unfairness. Since the most error-affected fields are concentrated in Cohesion Policy (e.g. public procurement rules, state aid and environmental policy rules) "… this has led to increasing concerns about Cohesion Policy becoming a "police force" or "filter" through which errors in the implementation of other EU legislation are detected and compliance enforced. Moreover, it raises questions of fairness because the impacts are relatively greater in the poorer Member States and regions where Cohesion Policy funding is concentrated. …"[20].

A reformation of the assurance system in the sense of national accreditation would disengage the European Commission from its unpopular "police role" but it is not clear whether there are really benefits for Cohesion Policy as such. In the end, the assessment of accreditation is basically a matter of legal and economic considerations.

Economic considerations

In terms of economy, the major question relates to the benefit. This can be understood from several viewpoints. The first is assurance of efficient and responsible expenditure (accountability), the second is financial risk associated with legal uncertainty and the third is related to institutional costs that should be reduced but run the risk of being increased.

(i) Does accreditation improve accountability and assure a lower error rate? There is at least no evidence for that; the draft CPR Regulation does not substantiate this expectation (see discussion above). On the contrary, the European Court of Auditors considers accreditation and delegation of financial accountability without further involvement of the Commission as a major risk:

> *"The Court is of the opinion that the Commission, as holder of the ultimate responsibility in the budget implementation, should have a supervision role in this process to mitigate the risk of leaving the detection of any failure to subsequent checks, which may lead to more frequent checks, action plans requirements and financial corrections. This is particularly the case for procurement procedures, a key pre-condition for the implementation of the internal market. [...]. If public administrations and beneficiaries in the Member States are unable to improve the implementation of the procurement rules, Cohesion Policy would continue to be systematically affected."*[21]

[20] Mendez et al (2011), p. 109.
[21] ECA (2011a), footnote p. 15.

Hence, especially the sensitive issue of public procurement seems not to be adequately addressed by the provisions of the draft CPR Regulation. But this is of major importance because at least according to the ECA and the budget control committee of the European Parliament "... Member States shoulder a significant share of the blame for the high error rate, underlining the lack of political responsibility and accountability over expenditure and a relaxed approach to enforcement..."[22]. Hence, the major question remains why a nationally accredited system should be more reliable than a system with Commission involvement.

(ii) This is also related to the issue of legal certainty. The assurance process, as it has been exercised in the current programming period, has been based on the approval of the European Commission (Article 72, Regulation 1083/2006). This has provided legal certainty, whereas the accreditation system as proposed in the new CPR Regulation makes the management and control system of a programme fully and permanently dependent on the opinion of a national accrediting body. This could at any time lead to interruptions of payment, as soon as the respective Accrediting Authority and the accredited bodies disagree about compliance of the systems. Consequently payment interruptions or clawbacks based on system irregularities would also affect those beneficiaries who had fully complied with their financial provisions or who operated in good faith. Even though this can also happen under the current provisions, compliance approval by the European Commission has been perceived as more dependable.

(iii) According to Dherét et al 2012, the positive effect of some simplification measures is likely to be minimised by the introduction of further institutional structures, which may appear necessary for the communication interface with the COM, if a multi-fund approach is pursued, but which will also create more administrative burden. Article 64 addresses the mandatory accreditation and the facultative co-ordination. "... Therefore and as indicated by the Commission in Annex 5 of COM (2011) 615 final, simplification measures, particularly those related to management and control, will not lead to a reduction of costs but rather to 'a redistribution of the burden'. However, it is difficult at this stage to see whether the Commission's statement, saying that the burden redistribution will enable more effective mitigation of risks and lead therefore to an error rate below 5% can be delivered..."[23].

Another point related to institutional efficiency is that there is also no real clarity about the division of tasks between the Accrediting Authority and the Programme Audit Authorities. Since the Audit Authority undertakes regular system controls anyway, it remains unclear where the dividing line between the two sorts of authorities runs. As it seems, the Accrediting Authority will base its decision on the findings of the Audit Authority. The question is, on which additional information (beyond the interest of the Audit Authorities) the Accrediting Authority will depend. The purpose of the two authorities needs to be clearly defined in order to justify the existence of both and to avoid over-bureaucracy. As it appears in the draft CPR regulation, there could be the risk of creating duplicated structures as both kinds of authority appear to follow common purposes leading to the identical decisions.

[22] Mendez et al (2011), p. 109.

[23] Dherét (2012), p.20. *Regarding the last two paragraphs cf. also (Bundesregierung 2010, Stellungnahme der Bundesregierung zu den Schlussfolgerungen des Fünften Berichts der Europäischen Kommission zum wirtschaftlichen, sozialen und territorialen Zusammenhalt: Die Zukunft der Kohäsionspolitik, p. 15, arguing in the same way.*

If it turns out that there is no perceptible economic benefit of accreditation of the management and control systems, the major question is whether there are alternatives. As stated above, the current system of assurance has been appreciated by both the Member States authorities and the European Commission itself. Could maintaining the current system be a feasible option (most managing authorities are in favour of this)? Where could it be worthwhile to consider amendments?

It is a matter of interpretation whether the description of management and control systems according to Article 71, Regulation 1083/2006 that had to be accompanied by an opinion of the Audit Authority (or another public or private but functionally independent audit body) would really suffice the requirement of an independent verification. Since the Audit Authority itself belongs to the management and control system, it is certainly true that an accompanying opinion on the Article 71 report, prepared by the Audit Authority itself, cannot be considered as an independent statement, even if it is functionally independent in the system. However, if an audit body outside the management and control system is entrusted with the opinion statement (this is also possible in accordance with Article 71, subparagraph 3) the quality of independence should be considered different.[24]

Nevertheless, the new draft CPR Regulation disregards possibilities to modify existing rules with a view to ensure more independence but instead aims to improve accountability and assurance through accreditation of the Managing and Certifying authorities.

Legal considerations

In terms of law, the major question relates to the reconcilability between accreditation of a public national authority required by the Commission and the national administration law that may not include provisions for accrediting national authorities by other national authorities. While for the current programming period the system of management and control has to be proved and attested to be in line with the Regulation, the new ideas require certification of due diligence of an authority. This does not only seem to induce some flavour of mistrust between the Commission and the Member States, in some countries such principles are unusual or even illegal, because accreditation would be in conflict with the principle of shared management.

In Ireland, there is some reluctance regarding accreditation, since this could imply the creation of a new quasi-political authority (or at least under political control). This could affect the independence of this authority and it is not yet clear how such a system could work in Ireland (information based on an interview).

Regarding the latter issue the German Federal Council has spelled out a substantial legal critique stating its determined rejection of the provision of accreditation in Cohesion Policy. According to the German Federal Council the nature of Cohesion Policy is essentially characterized by the principle of subsidiarity. Accreditation of national authorities through other national authorities is not supported by the German administration law. But exactly this is stipulated by Article 64 of the draft CPR regulation, where the link to Article 56(3) of the draft Financial Regulation is defined. Even though this article defines the shared management with the member states, the provision may be in fact inconsistent with the principle of subsidiarity and shared management. Referring to Article 53 (Financial Regulation 1605/2002 and amended Financial Regulation 1995/2006) shared management

[24] There is no evidence that such considerations were discussed (cf. COM Staff Working Paper: A Budget for Europe 2020: the current system of funding, the challenges ahead, the results of stakeholders consultation and different options on the main horizontal and sectoral issues).

in Cohesion Policy is indeed a standard principle. Only in policy fields where the Commission is entrusted with the central responsibility might other provisions apply.[25]

This position seems, however, not be shared by all Bundeslaender. In a corresponding comment of the Landtag Baden-Württemberg no inconsistencies with the subsidiarity principle are established[26]. It is not clear whether this contradicting opinion is based on a lack of co-ordination and interpretation or whether Baden-Württemberg represents a minority position in this question.

We also explored the fact that there has been no objection against accreditation of the paying authorities in EAGGF/EAFRD programmes in Germany. In fact, also in Germany paying authorities were accredited. But there are three important facts to be considered. The first is that rural development policy has originated from a centrally administered policy field, namely the CAP, even though the second pillar belongs to shared management in the EU budget. The second is that there has been no consensus about the legality of accreditation of paying authorities and the third is that there has been some autonomous shift of decision making power from the Member States to the Commission that originated in the financial Regulation 1605/2002. In the 1990s the criteria of accreditation for paying authorities had to be defined by the Member State and not formally by the Commission. In Regulation 1663/95 of 7 July 1995 laying down detailed rules for the application of Council Regulation (EEC) No 729/70 regarding the procedure for the clearance of the accounts of the EAGGF Guarantee Section it still reads:

> *"... Before accrediting any paying agency, the competent authority shall be satisfied that the administrative and accounting arrangements of the body concerned offer the guarantees referred to in Article 4 (1) (a) of Regulation (EEC) No 729/70. The criteria shall be established by the Member State and applied by the competent authority for the purpose of accreditation, taking account of the Commission's guidelines for those criteria as set out in the Annex. Failure to meet any criteria of significant relevance to the paying agency's operations shall lead to the application of Article 4 (4) of the abovementioned Regulation. ..."*

Nowadays, the Commission Regulation 885/2006 defines the implementation of the accreditation of paying authorities. Article 1 and annex 1 clearly set out the common criteria as defined by the Commission. Hence, it seems that the change of the system in the CAP has been based on tacit toleration in some Member States even though it could be in conflict with national administration law. The new draft CPR Regulation is clearly inspired by this process, fully exploiting provisions of delegated acts. Correspondingly, the draft CFS Regulation says in recital 88:

"In order to supplement and amend certain non-essential elements of this Regulation, the power to adopt acts in accordance with Article 290 of the Treaty should be delegated to the

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[25] "… Der Bundesrat lehnt die vorgesehene Akkreditierung von Verwaltungs- und Kontrollstellen entschieden ab. Die Umsetzung der Kohäsionspolitik durch die Mitgliedstaaten entspricht dem Subsidiaritätsgrundsatz in der EU. Dass die Strukturfondsförderung zum Bereich der geteilten Mittelverwaltung im Sinne von Artikel 53 Absatz 1 Buchstabe b der geltenden EU-Haushaltsordnung (EU-HHO) gehört, ist ein in Artikel 4 Absatz 7 normierter Grundsatz der Kohäsionspolitik. Dieser leitet sich direkt aus dem Subsidiaritätsprinzip des Artikels 5 EUV ab. Nur wenn Haushaltsmittel von der Kommission zentral und indirekt verwaltet werden, bestimmt Artikel 53 Absatz 2 der geltenden EU-HHO, dass dies nach Maßgabe der Artikel 54 bis 57 EU-HHO erfolgt […] In diesem Zusammenhang weist der Bundesrat darauf hin, dass eine Akkreditierung von staatlichen Behörden durch andere staatliche Behörden in Deutschland keinen Rückhalt im Verwaltungsrecht findet und generell auch als Eingriff in die Organisationshoheit der Mitgliedstaaten abzulehnen ist. Soweit staatliche Behörden die Verwaltungs- und Kontrollaufgaben wahrnehmen, muss jedwede Akkreditierung bereits aus diesem Grund ausscheiden. …".

[26] Landtag Baden-Württemberg (2011), *Mitteilung der Landesregierung, EU-Strukturpolitik ab 2014*, p. 7.

Commission in respect of [...] the accreditation criteria for managing authorities and certifying authorities. ..."

Consequently, through delegated acts the Commission would then decide about accreditation criteria while for the EAGGF/EAFRD paying authorities only guidelines have been provided by the COM. In the end it will be a matter of the EU principle of subsidiarity, the administration law of the single Member States and its respective interpretation when assessing the feasibility of accreditation in Cohesion Policy. But finally it is the benefit of such a procedure that should be the overarching criterion rather than distracting legal controversies.

In the next chapter we reflect on good practice and the *pros* and *cons* that can be determined from former experiences with similar provisions.

1.2.2. Good practice on how to set up the procedure so that it brings real simplification

There is not yet any practical experience with a system of accreditation of managing and certifying authorities in Cohesion Policy. The idea of this reform, as set out in the draft CPR Regulation, stems from the system of the control in the CAP.

Pros

Positive experiences that could be considered as good practice have been a higher efficiency in programme implementation. Rural development programmes seem less prone to delays in implementation. In a recent study about lessons from shared management in cohesion, rural development and fisheries policies[27], a comparative assessment of policies was carried out. The empirics of this study is based on collecting the views of European Commission representatives of several DGs, including Agri, Regio, Empl, Budg and Mare. The response on the accreditation system as applied in the CAP has been largely positive.

> *"...Respondents from DG Agri stressed that there is no ex-ante assessment in the rural development policy framework as the system relies on accredited paying agencies which undergo regular audits by external certification bodies. This accreditation process under the responsibility of the MS without interference by the Commission is deemed to be central to the system and, to a large extent accounts for its effectiveness. An ex-ante system would shift the responsibility from the MS to the Commission and could slow down payments. In general, MS are reported to be quite comfortable with the current system..."*[28].

This inspired representatives of the DG Regio to assume that the compliance assessment process of the 2007-2013 programming period (Article 71) – even though it has much improved as compared to the forerunner periods – should be replaced by a system similar to the CAP.

> "... According to some respondents from DG Regio, the compliance assessment could be improved by asking national authorities to take responsibility for providing assurance on compliance of systems without verification of the Commission. Making the MS fully accountable would enable the Commission to audit mainly programmes which appear problematic and would make it easier to stop payments or make financial corrections when needed. Also, in the opinion of another interviewee, the compliance assessment process could be more proportional and better targeted,

[27] CSIL (2010).
[28] CSIL (2010), p.51.

focusing on the assessment of systems of the most important programmes (in terms of financial volume)..."[29].

This position is the same as set out in the impact assessment on the draft CPR Regulation (SEC 2011/1141) discussed above.

Cons

A quasi-con should be the establishment that the CSIL study is only based on the opinion of the COM representatives interviewed. The empirical horizon is therefore much reduced. If national stakeholders were involved in the exchange of opinion one would expect a less uniform appreciation of the system as it is exercised in the CAP.

But even the CSIL study suggests a number of caveats. A major counter-argument is related to the comparability of rural development policy and Cohesion Policy. There is some evidence that the "error rate remained higher for rural development compared to the first pillar, despite the efforts to apply the same control system." The error rate in rural development policy is still lower than that of Cohesion Policy, but this is not necessarily caused by the accreditation system but rather by "the intrinsic characteristics of the policies. In the respondent's personal view, rural development policy would be easier to control in terms of financial flows, due to higher recourse to direct grants to beneficiaries rather than public procurement tendering procedures."[30]

If this is true, the question is therefore whether there are really benefits in adopting the accreditation system from the CAP.

We also looked at practical experiences in Member States how the system of accreditation of the paying authorities in the CAP works and how reliable it is. In a recent report of the Rhineland palatinate Court of Auditors, the system as it has worked for the rural development programme PAUL was quite substantially criticised. Here it was found that the Certifying Authority which is responsible for the regular examination of the compliance of the paying authority did not adequately check the proofs of the paying authority and it was not clear how the certifying authority used the common criteria to assess compliance in order to grant accreditation.[31]

Consequently, if an Accrediting Authority simply decides on the findings of a certifying authority without carrying out its own further auditing activities, there is the risk that important errors remain undetected until an external Court of Auditors examines the system.

1.2.3. The merger of Authorities – option or obligation?

The merger of Certifying and Managing Authorities, presented as an option for programmes under the investment for Growth and Jobs goal in the draft CPR Regulation, is in fact nothing new. Already in the current programming period Certifying Authority and Managing Authority may be part of the same body, however functionally separated. (Art 59.4/1083)

In contrast to the mainstream programmes, the current proposal of merger of authorities is however obligatory and hence of practical relevance for the ETC programmes – Art. 22 of the ETC draft Regulation stipulates that the Managing Authority "*shall* additionally carry out the functions of the Certifying Authority".

[29] CSIL (2010).
[30] CSIL (2010).
[31] Rechnungshof Rheinland-Pfalz (2011), *Jahresbericht 2011*, Mainz, pp. 80 ff.

The European Commission seems to be confident that the system proposed will lead to an overall reduction of administrative burden. By having a managing and certifying authority under one roof potentially duplicating functions could be cut down and the layers of control reduced. The streamlining of the implementation structure of the ETC programmes is considered as being in line with the principle of proportionality given the relatively smaller size of ETC programmes.

For the multi-level and bi/multi-national set-up of the ETC programmes any reduction of complexity could be a relief for the management and implementation of the programme. The question is whether an intended simplification on the one hand (merger of authorities) is not outweighed by the effects of a re-organisation of existing systems and new tasks and functions assigned to the Managing Authorities on the other hand.

These new tasks compared to the current programming period are for the Managing Authority above all**:**

- To draw up an annual management declaration of assurance on the functioning of the management and control system together with
- A report on the results of management controls carried out, any weaknesses detected and corrective actions taken (Art. 114 draft CPR Regulation)

For the Certifying Authority

- The drawing up and certification of the annual accounts.

The annual accounts, the management declaration accompanied by the report on the controls carried out as well as the audit opinion on the annual accounts (plus the report of audits carried out) are to be submitted by February 1 of each year following the accounting year (n+1) to the European Commission.

In order to properly fulfil these tasks and functions in line with the Regulations minimum separation of operational functions within the MA should be ensured. The following tasks have to be carried separately: Selecting and approving of operations, the approving of payments to the beneficiaries, processing the payments to beneficiaries, carrying out management controls (MA core task), preparing payment claims to the Commission and of certifying the payment claim (CA task).

In practical terms this means the setting-up of different operational departments within the Managing Authority, i.e. at least a managing and a certifying department plus an internal audit.

For programmes with budgets from EU funds below EUR 250 million the draft CPR Regulation additionally foresees the possibility to integrate the Audit Authority into the same body as the Managing and Certifying Authority, which could be an additional department. Overall, the intended simplification by "forcing" ETC programmes to merge Managing and Certifying Authority leads to following preliminary conclusions:

The Certifying exercise per se – apart from the introduction of the annual accounts – will not substantially change or increase. It is the workload for the Managing Authorities and the requirement of a re-organisation of structures which will – at least in the initial stage – impose a further burden and costs on currently functioning systems. This is especially related to the recruitment of new working staff in the premises of the Managing Authorities and a transfer of know-how from and building up of new knowledge and skills relating to the certifying exercise in the Managing Authorities, or vice versa: Be it the current Certifying Authority which will become the new Managing Authority (as an option proposed by the Commission) and is in need of suitable staff and know how.

Rather as an obligation also for ETC programmes the merger of authorities should be introduced as an option which leaves it up to the programmes which way to go in the future.

1.2.4. Stability and continuity versus intended reduction of error rate

Because of little financial free rein to increase cohesion and CAP budgets and the enormous strains on regional economies caused by the current financial crisis it was considered necessary to shift resources from policy administration to policy intervention in order to make policy more result-oriented, in other words: to change the system from an input focus to more emphasis on output. However, this important consideration is to some extent inconsistent with the need to improve the accountability of Cohesion Policy. In fact, Cohesion Policy belongs to the policy fields with the highest error rate. But errors do not only occur because of low institutional capacity or a sometimes alleged propensity to be more relaxed on financial accountability; errors may also occur simply because of the enormous complexity of the Cohesion Policy system[32].

Apparently, there is therefore an important trade-off between Cohesion Policy as a result-oriented policy (serving the economic needs of stability as a public good in the EU) on the one hand and financial accountability on the other. In other words there are two stances from which to address Cohesion Policy and the CAP: One is to achieve more policy impacts with smarter instruments, better monitoring and less money, the other is to reduce the error rate.

To solve this apparent contradiction it is worth looking at the arguments of Cohesion Policy stakeholders on the one hand and the audit bodies (notably the ECA) on the other hand. In fact there is no controversy around the question whether Cohesion Policy is too input oriented; red tape is the major factor that prevents reconciling result orientation and financial accountability. Excessive complexity is the core of the problem. The interesting question is whether the arguments of both parties are really conflicting. Bureaucracy and the related institutional costs are commonly held responsible for the efficiency gap in Cohesion Policy. This has also been the main argument for simplification.

The ECA and numerous national audit courts in the EU have noted that there has been a tendency to further furnish EU Regulations when adopting them into national law ("gold plating"). This has made administration and implementation of Cohesion Policy and the CAP even more complex and error prone. The ECA opinion 7/2011 makes it clear how the new CPR draft Regulation is expected to be over-complex:

> *"The arrangements for Cohesion spending are complex. There are six layers of rules (common provisions, general provisions, Fund-specific provisions, delegated acts, implementing acts, Commission's guidelines). National legislation will, in some cases, constitute an additional layer. The Court notes the positive efforts to reduce beneficiaries' administrative burden (for example, through the increased use of lump sums and standard costs). However, the burden for the EU and national administrations remains high, and will even possibly become higher than is currently the case."*

Furthermore the ECA also critically underscores that "...Despite the claimed focus on results, the scheme remains fundamentally input-based, and therefore oriented towards compliance rather than performance"[33]. This statement from the major EU institution

[32] Mendez et al (2011), pp. 65, 109, 115.
[33] ECA (2011a), p. 7.

controlling compliance in public expenditure makes clear that the point at issue cannot be the trade-off between result orientation and financial accountability. It rather seems that the problems with high prevalence of financial errors in Cohesion Policy and the CAP are home-made by both, the European Commission and the Member State administrations, and that the new draft CPR Regulation might even exacerbate red tape costs.

Member State reactions are unambiguous in this respect:

"Slovenia is not completely happy with the EU Commission's proposal to simplify procedures [...] The Ministry for Economic Development and Technology said that the 120 proposed changes are a step in the right direction, but some provisions would only increase red tape. The ministry believes that simplifying this field is a delicate process, as EU institutions demand ever stricter adherence to the rules, while those eligible for the funds want to see the drawing process simplified and more result-oriented. Some changes in the Commission's proposal would not simplify the procedures and Slovenia does not support the plan to introduce new institutions on the national level, as this move could endanger the possibility of merging various bodies, which would be a reasonable step [...] The ministry also believes that there are still several issues pending as regards to annual finalisation of accounts and related red tape. Moreover, Slovenia would like to see more respect for the cost-benefit principle, meaning that only administrative procedures that make up for the cost should be carried out..."[34].

The direly needed reorientation of Cohesion Policy to a more result oriented system can hardly be reconciled with some central provisions of the draft CPR Regulation. Legal uncertainty such as the dependence on an accreditation agent deciding on the flow of funds and interruption/withdrawal of payments, or some of the ex ante and macro conditionalities applied, put strong emphasis on the tool of sanctions. This uncertainty creates an additional cost position for administrations and beneficiaries. Research on the expectations of a more result and performance oriented Cohesion Policy by stakeholders all over Europe suggests a more relaxed dealing with the error rate.

Florio et al. (2011) underscore that a new set up for a result-oriented policy delivery in the administrative sphere should be minimising compliance with procedures and bringing about simplification. "The MAs shall be freed from the excessive burden resulting from controls and audit...", more importantly, "...Error rates should have a higher tolerance and simplification of costs must be decisively introduced."[35]

The unequivocal message of the CSIL study is: "The focus of the policy should shift away from compliance and spending and concentrate on results. This requires a radical change in administrative culture. ..."[36].

The quintessence of both, MS stakeholder as well as ECA standpoints is that, even though the draft CPR Regulation calls for simplification of assurance and further result orientation of policy, the proposed architecture appears to be threatening to achieve the opposite.

[34] http://www.europa.gov.si/en/content/news/news/select/economy/news/.
[35] Florio et al (2011), *Moving towards a more result/performance-oriented delivery system for Cohesion Policy*, European Parliament Study, CSIL, Milan, p. 118.
[36] Florio et al (2011), p.18-19.

2. APPLICATION OF THE PROPORTIONALITY PRINCIPLE IN THE AUDITING EXERCISE

KEY FINDINGS

- While proportionality in auditing makes sense, the main weakness in the current proposals is the arbitrary definition of the financial thresholds and the absence of a genuine risk-based approach based on a uniform sampling.
- The argument that small operations are less risky than larger ones is not convincing.
- The proper application of public procurement or state aid rules affects large and small operations alike.
- In the best case, an annual clearing of accounts could represent a reduction in administrative burden towards the end of the programming period.
- The rolling closure could potentially have the advantage of increased legal certainty for beneficiaries and reducing the audit burden implied by the rules on the retention of documents. However, since there is no guarantee that the Commission will approve the annual clearance quickly, there is also no guarantee that the audit trail will really be shortened.
- The annual clearance of accounts is also not really compatible with the multi-annual nature of EU Cohesion Policy.
- While the application of implementing and delegating acts for non-essential elements of EU legislation represent an improvement in the management of Cohesion Policy and the CAP, they are sometimes used to address key rather than non-essential elements of legislation.

2.1. Proportionality in the new Regulations

2.1.1. The proportionality principle in the Cohesion Policy context

The Treaty of Lisbon lays down the principle of proportionality. Protocol No 2 annexed to the Treaties stipulates: "Draft legislative acts shall be justified with regard to the principles of subsidiarity and proportionality (…) and "(…) shall take account of the need for any burden, whether financial or administrative, falling upon the Union, national governments, regional or local authorities, economic operators and citizens, to be minimised and commensurate with the objective to be achieved"[37].

The fact that any action and involvement of institutions in implementing European policies has to be in adequate proportion with the necessary aims to be achieved was reflected with regard to Cohesion Policy in a number of documents preceding the release of the draft CPR Regulation and fund specific Regulations in October 2011. For example, Barca summarizes different positions indicating "*that costs borne by the Commission and Member States (in terms of administrative burden and uncertainty) do not seem to prevent a high intensity of*

[37] Lisbon Treaty, Protocol 2, Article 5.

errors"[38]. Consequently, in his "Orientation paper" dated December 2009, the former Commissioner Samecki calls for more efficient and simpler management and control systems[39].

The strengthening of the effectiveness of Cohesion Policy spending finally found entrance into the Multi-annual financial framework for the period 2014-2020 issued in June 2011.

In the Impact Assessment of the legislative proposal for the draft CPR Regulation streamlining the delivery and minimizing the error risk four options were analyzed ranging from "no policy change" as compared to the current programming period, to a flexible, a prescriptive and lastly a "proportional approach" (payments of real cost or simplified cost option, mandatory e-governance, proportional approach to the ex-ante review of management and control systems)." The latter was deemed to be the preferred option leading to a "significant potential reduction in the cost of controls and a decline in workload; for administrations the proportional approach to assurance would represent a decline in workload by around 4% compared to the no change option."[40]. In comparison to the current status-quo this option is clearly reflecting a decreased level of involvement of Commission in audit and control.

In practical terms this means:

- Operational programmes below a size of 250 million are exempt from a Commission review.
- On project level operations not exceeding a total eligible expenditure of 100.000 are only audited once per programming period/before rolling closure by either the Audit Authority or the European Commission[41].
- The proposed rolling closure of programmes on an annual basis, which is estimated to reduce the cost of retention of documents for control purposes for public administrations and beneficiaries[42]. On the other hand this procedure is seen as an appropriate way to decrease audit trail errors by shortening the time period for document retention. It is also seen as measure to avoid the substantial build-up of administrative workload linked to the one-off closure at the end of the programming period.[43]
- Audit Authority and Managing Authority could be part of the same institution (in smaller programmes below a size of 250 million EUR).

2.1.2. Implications of the new Regulations concerning the auditing exercise

This section looks at the implications of the new Regulations concerning the limitation of the auditing exercise to larger programmes and riskier management and control systems and the risk analysis of the proportional auditing scheme. It goes without saying that the effort of control should be proportional to the financial input of a public intervention (i.e. the expenditure). The question here relates to the problem that control is inherently prone

[38] Barca F (2009), *An Agenda for a Reformed Cohesion Policy, A place-based approach to meeting European Union challenges and expectations*, Independent Report prepared at the request of the Commissioner for Regional Policy, Brussels, p.184.
[39] Samecki P (2009), *Orientation paper on the future of Cohesion Policy*, Brussels.
[40] European Commission (2011a), *Commission staff Working Paper, Executive Summary if the Impact Assessment Accompanying the Document Proposal for a Regulation of the European Parliament and of the Council (…) SEC(2011)1142*, Brussels.
[41] European Commission (2011d), Article 140.
[42] European Commission (2011d), p. 168.
[43] European Commission (2011d), p. 169.

to become a factor of fixed costs in administrative activity. In other words, the audit costs in small programmes are relatively higher than in large programmes. This skewed proportion is a major strain on the budget available. The Commission aims to address this problem by introducing financial ceilings beneath those a simplified approach is allowed. This should be possible on the one hand for programmes (Articles 113, 117 and 140) and on the other hand for operations (Article 140).

Smaller programmes with a budget from EU funds below the threshold of Euro 250 million may entrust a functionally independent department of the Managing Authority with the tasks of the programme Audit Authority[44]. Furthermore in such smaller programmes the European Commission will not request the report and the opinion of the independent audit body and the description of the management and control system. In addition to that, Article 140 (3rd sub-paragraph) of the draft CPR Regulation allows that the European Commission will refrain from carrying out its own on-the-spot audit activities as long as there is a reliable opinion of the Audit Authority, i.e. "...unless there is evidence of deficiencies in the work of the audit authority work for an accounting year for which the accounts have been subject to a clearance decision."[45]

Apart from programmes, also the audit of operations is subject to possible simplification. Operations for which the total eligible expenditure is below or equal to Euro 100,000 shall not be subject to more than one audit by either the audit authority or the Commission prior to the rolling closure of the expenditure concerned. The possibility of the rolling clearance is described in Article 131 of the draft CPR Regulation. Article 131 regulates a procedure never applied before in Cohesion Policy. It should be possible that at the level of each priority axis a list of finalised operations is included in the annual accounts for each operational programme. The corresponding expenditure subject to the clearance decision should be considered as closed.

The main weakness of the proportionality approach adopted by the Commission is the arbitrary definition of financial thresholds and the absence of a genuine risk-based approach. As regards Article 140, the ECA rightly notes "… that there is no evidence that operations whose eligible expenditure is below Euro 100,000 are less error prone than other operations. The Regulation should clarify how proportional controls will affect the sampling to be done by the audit authorities."[46]

Also the possible argument that operations of that small size are less affected by the failure in properly applying public procurement or state aid rules (because they are below the *de minimis* threshold), usually representing the bulk of irregularities in Cohesion Policy, is not fully convincing. A widespread approach in Cohesion Policy has been the separation of big operations into several smaller ones. Among those operations there have been legal ones but also many with occurrence of irregularities or even fraud. As the ECA notes for example, there have been artificial splits of works and services in several tenders:

> *"In the case of several ERDF projects in the same OP, works and services related to making a river navigable for cruise ships were contracted out in an irregular manner. The contracting authority apportioned the works and services in such a way as to reduce the contract values below the thresholds specified in EU and national public procurement rules, circumventing thus the normal tendering requirements.*

[44] This option is in fact also possible for current programming period.
[45] It is not further explained what further deficiencies in the work of Audit Authorities may mean, when at the same time the COM has concluded that it can rely on the opinion of the audit authority.
[46] ECA (2011a), p. 32.

> *Subsequently, several of these contracts were awarded to the same contractor.", or "absence of tendering for additional works foreseen by initial tender documentation: In the case of an ERDF project, works related to the renovation of a university building were awarded directly to a contractor. Although these works had been planned in the preliminary terms of reference, the contracting authority treated them as additional works that could not have been foreseen when tendering the main contract."* [47]

Irregularities in such smaller operations may remain undetected if they are already closed by the formal procedure of rolling clearance. Even though the potential financial loss (in absolute terms) of a small operation is proportionally small compared to bigger operations, the major issue is the individual structure of programmes. These can comprise relatively few but also relatively many small operations. Those many small operations would then add up to a large investment amount that will be subject to reduced audit requirements and the risk of error will increase for programmes with relatively many small operations (e.g. in several ETC programmes).

2.1.3. Cooperation between the Commission's and the Member States' auditing systems

Background

Coordination of audits and proportionality is a sensitive issue in the discussion of simplifying management and control in Cohesion Policy. The new draft CPR Regulation makes a number of important provisions, but these have to be reflected in relation to experiences made in recent years. It is important to look at the purpose of multi-level auditing, the cost and effort needed and the trade-off between proportionality and error rate. In this connection one has to differentiate between programme specific and overall co-operation of audit systems. While the programme specific co-operation is just related to the Audit Authorities and the European Commission audit unit (Unit DG Regio J.4) the overall co-operation also includes the national and regional courts of auditors and the ECA. All authorities and courts mentioned are entitled and assigned to audit operations and systems in Cohesion Policy.

A major problem has been the massively increased programme specific audit effort since 2007, not only because a more demanding sampling method but also because of the complexity and sometimes vagueness of the Cohesion Policy system as the main challenge in the system itself. As the recent study by Blomeyer & Sanz points out:

> *"The benefits of audit in terms of identifying and preventing irregularities are recognised, however, case study work points to the complex regulatory framework as one of the key causes - as one of the interviewees put it: 'the system produces irregularities'. ... Moreover, [...] irregularities are often caused by the fact that the regulatory requirements allow room for different interpretations."*[48]

Member States bother about the assurance system because of the excessive thrust of punitive enforcement. Driven by reform needs of the 1999 financial management crisis and the permanent pressure to reduce the error rate, the 'audit overkill' in Cohesion Policy has fuelled a culture of control and compliance rather than result and performance orientation.

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[47] ECA (2011b), *Annual Report on the Implementation of the Budget, Official Journal of the European Union, 2011/C 326/01*, p.110.

[48] Blomeyer & Sanz (2011), *What are the implications of the current legislation for cost-effectiveness and quality control in Structural Fund spending – what role for performance auditing?*, European Parliament Study, Guadalajara, p.3.

The associated increase in costs and administrative burden has substantially reduced the capacity and incentives to emphasise performance[49].

Among the current Cohesion Policy programmes, between 30 and 60% of expenditure has been audited in 2010. A case study on the audit activities of the OP Northrhine-Westfalia shows that during 2010 and 2011 around 190 operations were audited, while for the entire forerunner programme alone only 170 operations were audited. Effort and cost have been described as "overkill"[50].

Audit costs even only for programme specific audits are already extremely high. 14,100 person years are allocated and around Euro 1.05 billion will be spent for SF audits during 2007-2013.[51] Even though Article 74 of Regulation 1083/2006 stipulates proportionality in control arrangements, namely that for smaller programmes without reservations in the "Article 61 report" the Commission can rely on the opinion of the Audit Authority, the audit costs of the Audit Authorities and the DG Regio seem to be far from proportional.

In addition to the programme specific audits, programmes may also be affected by additional audits carried out by national and regional courts of auditors and also the ECA. All those courts are operating independently and often with very different audit strategies, both in terms of sampling methods as well as thematic focus. Moreover, those institutions are also carrying out on-the-spot checks and system audits. It is an inherent attribute of their independence that there is no co-ordination of audits, but only mutual acknowledgement of results that are eventually used for heuristic purposes complementing the statistical sampling. So in the end it can happen, that a beneficiary will not be only audited several times but also with rather different audit results. At a first glimpse this uncoordinated audit activities might appear chaotic and rather thriftless. But a closer look reveals important advantages. A case study on the Operational Programme Central Bohemia finds:

> *"...While in 2010 the Audit Authority has certified the ROP Central Bohemia to be free of irregularities and error, the findings of the ECA (and the SAO) do not suggest that the audits carried out by the Audit Authority always meet the standards of proper auditing. [...] Hence, at least for the Czech programmes there is substantial justification to maintain a system of several independent tiers of control for the time being. If there were more co-ordination between the Audit Authority and the different courts (ECA, SAO), more irregularities and fraud would possibly remain undiscovered. ..."*[52].

Proportionality 2007-2013 vs. proportionality 2014-2020

As mentioned above, Article 74 (Regulation 1083/2006) includes provisions for programmes below public expenditure of 750 million and less than 40% co-financing to disburden the European Commission from own audit activities, provided the report and opinion on the management and control systems (Article 71) suggests full reliability. Apart from that, all operations can be subject to audits. These have to be selected by a proper statistical sampling method. Article 17 of Regulation 1828/2006 (Implementing Regulation)

[49] Mendez et al (2011).

[50] PRAC (2011), *European Parliament Study on Structural Funds / Cohesion Fund (SF/CF) Cost Effectiveness - Focus on Audit Arrangements - Case Study: ERDF Operational Programme "Regional Competitiveness" Northrhine-Westfalia 2007-2013*, unpublished.

[51] SWECO 2010, Regional governance in the context of globalisation: reviewing governance mechanisms & administrative costs, Stockholm, p.38).

[52] PRAC (2011), *European Parliament Study on Structural Funds / Cohesion Fund (SF/CF) Cost Effectiveness of Audit Arrangements - Case Study: ERDF Operational Programme "Convergence" Central Bohemia (CZ) 2007-2013,* unpublished.

stipulates a statistical approach. "The method used to select the sample and to draw conclusions from the results shall take account of internationally accepted audit standards and be documented." There is no specific requirement about the approach. Depending on the respective sampling method, the coverage of operations will differ in size and structure.

The draft CPR Regulation contains similar but also very different provisions. The goal stated is simplification and less administrative burden.

Recital 87 says that "the frequency of audits on operations should be proportionate to the extent of the Union's support from the Funds. [...]. Nevertheless, it should be possible to carry out audits at any time where there is evidence of an irregularity or fraud, or, following closure of a completed operation, as part of an audit sample. In order that the level of auditing by the Commission is proportionate to the risk, the Commission should be able to reduce its audit work ...". This is then formally regulated in article 140. The major difference between proportionality of audits for the current programming period and that foreseen for future Cohesion Policy is the fact that two artificial thresholds are used to differentiate operations.

If operations with eligible expenditure not exceeding euro 100,000 are exempted from more than one audit (either by the Audit Authority or the Commission) prior to closure and also the larger operations' audits are limited to once a year, there will be certainly a reduction of audit effort, but only if this is really done. Consequently one threshold constitutes the 100,000 euro margin; the other threshold is "once" or "once a year" respectively. If this approach materialises, it could pave the way to introduce the genuine single audit approach where each level builds and relies on the assurance of the previous level.

The open question, however, is related to feasibility. In the past there have been doubts by several observers that the European Commission has really applied the provisions of Article 74 to a sufficient extent[53]. Because Article 140 (4th sub-paragraph) of the draft CPR Regulation allows the European Commission at any time to carry out audits of operations "for the purpose of assessing the work of an audit authority by re-performance of its audit activity", it remains open which share of operations will be really treated by the simplification approach. This problem is - by the way - not necessarily caused by any alleged "control freakishness" of the Commission but rather by real need, because both the persisting high error rate as well as inconsistencies in the new provisions regarding annual clearance (see below) do not yet allow the application of the genuine single audit approach to a sufficient extent.

Critical assessment

As stated above, the ECA has been critical as regards the artificial threshold of Euro 100,000. Further to that one has to note that Article 140 of the draft CPR Regulation is linked to Article 131 (rolling closure) and Articles 75 ff. referring to annual clearance. Here the issue is discussed controversially.

Some observers share the positive expectation connected with this provision. According to some the annual clearance of accounts could facilitate a rolling partial closure of programmes. The main advantage of this would be the timely clearance of accounts (strengthening the discharge exercise). The rolling closure approach could have the

[53] Mendez et al (2011), p.110.

advantage of increasing legal certainty for beneficiaries and reducing the audit burden implied by the rules on the retention of documents.[54]

Interviewees from Ireland and Slovenia see also some potential benefit of the annual clearance. This way, the administrative workload of clearance could be more evenly distributed over the programme horizon instead of having work peaks of financial management at the end of a programming period, although the Slovene interviewee spelled out some caveats related to the difference between theory and practice: "In theory the annual clearance might well have number of advantages (especially worth pointing out is reduced uncertainty), we are seriously concerned however about how the system could work in practice. Multi-annuality is an obvious problem, but we are also concerned about how realistic it is to prepare all the necessary documentation in the time foreseen, every year. Assuming the information systems would be working perfectly this might not represent too big a problem, in reality however, assumption of perfect information systems does seem overoptimistic..."

In contrast to Mendez et al. and partly the interviewees, there are important critical voices expecting just the opposite to happen than that which is intended. The ECA recognises formal inconsistencies between the Commission's ambition and the legal reality: The rolling closure, according to the Commission, should in fact provide legal certainty to the individual beneficiaries about expenditure for a given year and reduce the administrative burden associated with a long retention period of records. Both the clearance of accounts and the rolling closure is inherently subject to further checks and cannot therefore represent a final closure of operations (cf. ECA).

According to the ECA 2011 this is because the annual clearance decision would not cover the legality and regularity of the underlying transactions.[55] "... According to the Financial Regulation (Article 53b) the aim of the clearance of accounts is to establish the amount of expenditure recognised as chargeable to the budget after the Commission has performed appropriate checks. In the proposal of the general Regulation, the Commission's checks would only take place after the clearance and therefore this process would not take into account subsequent financial corrections..."[56]. The ECA also stresses that Cohesion Policy is set out as a multi-annual perspective: "... Full compliance of expenditure is not sought by the Commission annually, but several years later and ultimately at the stage of the closure of operational programmes. Financial corrections mechanisms are the key instrument for this purpose..."[57]. It remains therefore questionable whether in the end there will really be a perceptible relief of audit work.

A similar standpoint is represented by the German Federal Council. A mandatory annual clearance of accounts is not commensurate with the multi-annual perspective of EU Cohesion Policy. According to the Council, the annual part-closure would imply a massive increase of audit effort in the Member States which again might imply considerable additional bureaucratic costs on the part of the national management systems and the beneficiaries. The unequivocal message is the apprehension that the introduction of annual clearance would thwart the very principle of simplification aimed at by the COM. Since

[54] Mendez et al (2011), p. 112.
[55] This problem that was already established for the annual clearance system of the CAP (cf. ECA 2010).
[56] ECA (2011a), p. 19. The Court also points out that the *de facto* role of annual accounts and of their audit remains vague in the Commission's proposal. In fact "extensive accounting information is to be provided at the mid-point of the financial year (at present not required for Commission's accounts) but there is no clear requirement for reliable information at year end (information that is required for Commission's accounts)." The ECA asks for significant clarification about this provision in the Regulation draft.
[57] ECA (2011a).

there is no warranty that an annual clearance will be approved quickly by the COM, there are also doubts that annual closure of operations will really contribute to a shorter retention period of documents. The Federal Council has also important objections against the required summary of all audits carried out in the preceding year (Article 75, sub-paragraph 1c). Since there is anyway a detailed annual report to be prepared by the audit authorities (according to article 116, sub-paragraph 5), according to the Federal Council such an additional summary report would simply be a duplication of reporting and would create an unnecessary additional administrative burden[58]. The interviewee from Ireland deplores the introduction of the audit opinion on the yearly management declaration as a third kind of check to be executed by the audit authorities that would absorb considerable personnel resources of the audit authority.

A further at least temporary complication could be the overlap of the programming periods in 2014 and 2015 (n+2), where two different systems of audit would have to be carried out. The draft CPR Regulation makes different provisions as regards the commencement of annual reporting. While for the current programming period the first audit report was to be submitted only by 31 December 2008 (i.e. 24 months after the start of the programmes), which was possible due to the multi-annual perspective of clearance, there are no corresponding provisions in the draft CPR Regulation. Audits and audit reports have to be submitted already for the first year. It is therefore likely that especially in the first year enormous overlaps of differently conceptualised audit work may occur.

Only one aspect of that provision could be found to be an improvement. In the opinion of ECA "... the rolling closure of operations may potentially bring some benefits for the Cohesion area as national checks and audits will have to take place at an earlier stage, hence permitting better preventive control arrangements. The fact that any irregularity detected subsequent to the presentation of the annual accounts will lead automatically to a net financial correction (Article 137(6) of the draft general Regulation) is the consequence of the increased Member States' responsibilities and reliance on their reimbursement claims."[59]

But this potential additional assurance is obtainable only at substantially higher control cost in the Member States.

2.2. Analysis of the legislative procedures to change the system of auditing - Delegated and implementing acts

The purpose of comitology is to speed-up decision making and policy implementation in the EU. Speed, efficiency, flexibility, control and technical decisions are keywords. In the past, there were five comitology procedures (advisory procedure, management procedure, regulatory procedure, regulatory procedure with scrutiny and safeguard procedure). All in all, the spheres where the European Commission needed regulatory power has grown steadily and by 2009 there were 266 comitology committees. Following the Lisbon Treaty the system has been reformed. With Articles 290 and 291, Treaty of the Functioning of the

[58] Bundesrat (2011), p. 25 f. It is not fully clear whether the summary reports described in Article 75 (1c) and Article 116 (5) are really different documents. In fact, this would not make sense. However, Article 75 (3) asks for an additional synthesis report which is in fact an additional administration effort at national level that appears dispensable. A similar argumentation is produced by the Austrian Court of Auditors: Rechnungshof (2010), p. 15.

[59] ECA (2011a), p. 19.

EU (TFEU), delegated and implementing acts were introduced. These new provisions are to some extent similar, but there are also major differences.

Implementing acts are routine and technical implementing measures adopted by the Commission, under the control of the Member States and with possible referral to the European Parliament and the Council[60]. There are possibilities to apply implementing acts in exceptional cases (notably in case of market disruption in agriculture or in case of risks for the financial interests of the EU). This act can be repealed again in case of a negative opinion of the appeal committee. Similarly, implementing acts with immediate effect can be adopted. This may happen in an emergency case. But also this act can be repealed afterwards.

Delegated acts are similar to the former regulatory procedure with scrutiny. These acts relate to non-essential elements of EU legislation that may be handled by the European Commission. Important changes compared to *pre-Lisbon* are that there is no horizontal framework, no committees, the right to object to a delegated act on any grounds and the ultimate control mechanism of revocation[61].

For both of these categories (delegated and implementation acts) the procedures are simplified compared to the past, and there is a larger number of actors involved that makes information more accessible. Control by revocation is stricter, but it is unlikely that it will be frequently used[62].

Even though transparency and control may be enhanced by the TFEU, there are also possible weaknesses and caveats.

The legal service of the Council of the European Union has spelled out a rather critical opinion on delegated and implementing acts[63]: These address for instance the fact that delegation of powers can be tacitly or automatically extended or major problems of clarity regarding a situation of exceptional cases (see above). Consequently, "... The Legal Service considers that use of the urgency procedure should be confined to cases where there are imperative or overriding general interest requirements, in line with the case law of the Court."[64]

Several members of the European Parliament are also fairly sceptical as regards the legal architecture with special reference to the CSF: "The main concern relates to the appropriateness of the legal nature of the CSF as proposed in Article 12 of the CPR. Adoption of the CSF through a delegated act goes against the views formerly expressed by the European Parliament. To allow for co-legislators to provide for the highest legitimacy for the CSF, the ordinary legislative procedure should be applied, resulting in a directly applicable Regulation." [65]

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[60] Hill & Knowlton, *The new comitology system: Understanding delegated and implementing acts*, http://www.hillandknowlton.be/news/new-comitology-system-understanding-delegated-and-implementing-acts.

[61] Hadacre A and Kaeding M (2011), *Delegated and Implementing Acts: The new Comitology*, EIPA, Maastricht, pp. 12 ff.

[62] Hadacre and Keading (2011), p. 20.

[63] EU Council/Opinion of the Legal Service (2011), *Application of Articles 290 (delegated acts) and 291 (implementing acts)* TFEU, Brussels 11 April 2011.

[64] EU Council/Opinion of the Legal Service (2011), p. 9.

[65] European Parliament Committee on Regional Development (Rapporteurs: Lambert van Nistelrooij, Constanze Angela Krehl) (2012), *Draft Report on the Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund covered by the Common Strategic Framework and laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1083/2006, p.3*.

This new comitology is of major relevance of the draft CPR Regulation. But in fact there is no comprehensive description of legislative procedures. Article 142 specifically regulates the exercise of delegated acts that is fully geared towards Article 290 of the TFEU. Delegated acts are considered important for many decision relevant procedures in Cohesion Policy and the CAP. This is clearly expressed by the draft CPR Regulation in broadly using implementing acts in connection with articles 5, 12, 20, 29, 32, 33, 34 35, 36, 54, 58, 112, 114, 116, 117, 132, 136 and 141. Among them also the system of control and payment corrections is affected by this new comitology.

As regards legislative procedures of auditing and financial corrections, the respective articles which refer to delegated acts are specifically:

- Article 112 (Responsibilities of Member States in managing and control systems): "Member States shall ensure that management and control systems for operational programmes are set up in accordance with Articles 62 and 63..."
- Article 116 (Functions of the audit authority):" The audit authority shall ensure that audits are carried out on the management and control systems, on an appropriate sample of operations and on the annual accounts."
- Article 136 (Criteria for financial corrections): "1. The Commission shall make financial corrections by means of implementing acts by cancelling all or part of the Union contribution to an operational programme in accordance with Article 77. 6."

But there is also an interaction with other provisions where the application of delegated acts is not explicitly mentioned. These are is notably Articles 137-139 describing procedures obligations of Member States and the repayment, and article 135 ruling the financial corrections at the Member State level as this is also closely connected with Article 136 giving the Commission the power to make corrections where the respective Member State fails or is incapable to do so. Here some considerable criticisms have been aired, namely that delegated acts seem to address key rather than non-essential elements of legislation.

"The Court notes in particular that matters to be covered by delegated acts, meant to cover non-essential elements of EU legislation, deal in reality with key elements of the future Cohesion scheme (Such as the adoption of a Common Strategic Framework; the adoption of detailed rules on financial instruments; the responsibilities of Member States concerning the procedure for reporting irregularities and recovery of sums unduly paid; the conditions of national audits; the accreditation criteria for managing authorities and certifying authorities; the level of financial correction to be applied; the amendment of the method for establishing the performance framework and the set of ex ante conditionalities). Concerning the conferral on the Commission of implementing powers the Court observes that in several cases the procedure (advisory or examination) for adoption of these acts following the Regulation (EU) No 182/2011 is not specified. As a result, the respective roles of the Commission and of the Member States remain undefined (for example, in case of suspension of payments and financial corrections, see Articles 134(2) and 137(5) of the general Regulation)."[66]

[66] ECA (2011a), p.8, Similarly, European Parliament Committee on Regional Development (Rapporteurs: Lambert van Nistelrooij, Constanze Angela Krehl) (2012). The authors of this note firmly plead for the ordinary legislative procedure in adopting the CSF.

3. RECOMMENDATIONS

The following recommendations are structured in accordance to the two leading questions of this briefing note. The new draft CPR Regulation is subject to a rather controversial debate and we are aware that conclusions sometimes suggest far-reaching adjustment which may not be any more realistic. As regards the problem of accreditation, our recommendations are therefore structured along a cascade system to facilitate changes that are still feasible.

Accreditation and merger of authorities

(1) A genuine risk-based approach taking account the empirical evidence of error in sectors and geographical regions seems to be superior to the relatively inflexible system of mandatory accreditation and the general financial thresholds for programmes and operations: The application of accreditation could be considered as an auxiliary instrument to foster assurance in countries with a high error rate (a threshold would need to be defined). A possible approach would be the assignment of a completely independent private body, like one of the big international auditing companies, on which results the Commission would decide about direct accreditation. This would also create a greater incentive to improve the supervision capacities of operations. Furthermore, in this case national authorities are not accredited by other national authorities (which could become legally questionable in some countries), but by the European Commission itself. This could contribute to a more balanced distribution of responsibility between the European Commission and the related member states. In countries or regions with a constantly low error rate the principle of single audit should be pursued. This would relieve the burden of the Commission to audit operations in addition to the corresponding activities of the audit authorities.

(2) If recommendation 1 is not deemed adequate (also due to political sensitivity connected with some discrimination between groups of countries or regions), the role of the audit authorities should at least not overlap with those of an Accrediting Authority. Since in this case there is anyway the creation of a new authority, it could also be possible to separate the tasks of on-the-spot checks on the one hand and the system checks on the other hand. Since the Accrediting Authority will base its decisions exclusively on the system checks of the Audit Authorities, it would appear more consistent if the Accrediting Authorities themselves took over the responsibility of running the system checks.

(3) If neither recommendation 1 nor 2 are deemed acceptable by the Commission, there should at least be a legal assessment of feasibility. There is a large variation of constitutions and the level of decentralisation among EU countries. Administration law is directly affected by constitutional affairs. Cohesion Policy is executed by shared management, thus implementation on the ground is under the full responsibility of the Member State. Potentially, the issue of accrediting a public authority through another one could be in legal conflict with national administration law. There are definitively major doubts in Germany. But also in other countries there could be potential inconsistencies. It should be therefore examined, where legal barriers are important and how best to furnish the provision so that it does not conflict with constitutional basics.

(4) As regards the merger of authorities, the differentiation between mainstream programmes where the merger is facultative and the ETC programmes where it is compulsory should be abandoned. In order to enhance institutional efficiency, the individual settings should be the major criterion to decide on and not the type of a programme. The option should be facultative for both types of programmes.

Proportionality

(1) The approach of annual clearance should be further scrutinized in its theory and practical feasibility by launching a survey or study on possible benefits and costs in Member States before casting the draft provisions into final legislation. Such a study should be launched very soon to be relevant in the decision making process leading to the final adoption of the Regulation. If it turns out that there are really major caveats, it should be still possible to abandon this approach.

(2) An EU wide uniform sampling approach is recommended. So far it is hardly possible to compare the message of error rates in different countries or even different programmes within countries. Monetary unit sampling could be considered as an approach emphasizing larger operations statistically but not skipping the smaller ones. So there are no generalized thresholds like the Euro 100,000 for operations and Euro 250 million for programmes. Moreover, monetary unit sampling could be easily "calibrated" to the individual error rate which occurred in the past, based on the Poisson distribution of former misstatement.

(3) Cohesion Policy should become genuinely simplified. This policy materializes on the ground in the regions, where not only Community law is applied but sometimes also national law further regulating and complicating Community law. It appears rather uneconomic to relieve home-made red-tape with other home-made remedies. The superior and less costly approach would be simply to avoid home-made red-tape. There should be thus some common action to reduce this kind of "gold plating" at national level. This would substantially relieve the control effort needed and would directly contribute to proportionality at a lower cost level.[67]

(4) The application of implementing and delegated acts has been an important improvement for policy management at the Commission level. However, there should be a more responsible handling of the TFEU provisions, especially regarding a too lax interpretation of what is non-essential and what are key elements. The procedures of implementing acts (advisory or examination) are to be explicitly defined in the Regulation.

The recommendations structured above should be addressed soon. At the moment (May 2012) the Financial Regulation is still under revision in the European Parliament. The Financial Regulation and the CPR regulation are still subject to further improvement of mutual consistency. Voting of the REGI and CONT committees are foreseen before summer 2012.[68]

[67] Derek Vaughan from the European Parliament pleads for « smart simplification », what means that the level of detail in regulation should be need oriented, neither overly complex for simple cirumstances nor overly simply in a financially risky environment (cf. Vaughan 2012, p.3).

[68] See also: Vaughan 2012 op.cit., pp. 3 ff.

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