

**ANNUAL REPORT ON THE ACTIVITIES
FUNDED BY THE 8TH, 9TH AND 10TH
EUROPEAN DEVELOPMENT FUNDS (EDFs)**

(2011/C 326/02)

Annual Report on the activities funded by the 8th, 9th and 10th European Development Funds (EDFs)

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THE COURT'S OBSERVATIONS

INTRODUCTION

1. This Annual Report presents the Court's assessment of the European Development Funds (EDFs). Key information on the activities covered and the spending in 2010 is provided in **Table 1**.

Specific characteristics of the European Development Funds

2. The European Development Fund (EDF) is the main instrument for providing European Union aid for development cooperation to the African, Caribbean and Pacific (ACP) States and Overseas Countries and Territories (OCTs). It was created in 1957 under the Treaty of Rome. The partnership agreement, signed in Cotonou on 23 June 2000 for a period of 20 years ('the Cotonou Agreement'), is the framework for the European Union's relations with ACP states and OCTs. It is centred on the objective of reducing and eventually eradicating poverty, consistent with the objectives of sustainable development and the gradual integration of the ACP countries and OCTs into the world economy. It is based on three complementary pillars:

- development cooperation,
- economic and trade cooperation, and
- the political dimension.

3. Operations financed by each EDF are programmed at the beginning of the period covered. A Country Strategy Paper, prepared by the ACP State or OCT concerned and the EU following consultations with a wide range of actors in the development process, sets out the country's medium-term development objectives and strategies and indicates the EU programmable financial allocation from which the country may benefit.

Table 1 — European Development Funds — Key information 2010

(million euro)

Budget Title	Policy area	Description	Payments 2010	Management Mode
European Development Funds	8th EDF	Administrative expenditure	0	
		Operational expenditure		
		<i>Projects</i>	21	Centralised direct
		<i>Budget Support</i>	0	Centralised direct
		<i>Projects</i>	133	Decentralised
		<i>Projects</i>	2	Joint management
			157	
	9th EDF	Administrative expenditure	8	
		Operational expenditure		
		<i>Projects</i>	204	Centralised direct
		<i>Budget Support</i>	63	Centralised direct
		<i>Projects</i>	29	Central indirect
		<i>Projects</i>	921	Decentralised
	<i>Projects</i>	81	Joint management	
			1 305	
	10th EDF	Administrative expenditure	78	
		Operational expenditure		
		<i>Projects</i>	181	Centralised direct
<i>Budget Support</i>		1 017	Centralised direct	
<i>Projects</i>		11	Central indirect	
<i>Projects</i>		215	Decentralised	
<i>Projects</i>	271	Joint management		
		1 772		
Total administrative expenditure			86	
Total operational expenditure			3 147	
<i>Projects</i>			2 068	
<i>Budget Support</i>			1 079	
Total payments ⁽¹⁾			3 233	
Total individual commitments ⁽¹⁾			3 304	
Total global commitments ⁽¹⁾			2 187	

⁽¹⁾ Financial Year 2010 net amounts.

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

THE COURT'S OBSERVATIONS

4. The EDFs are funded by the Member States, governed by their own financial regulation and managed by a specific committee. The European Commission is responsible for the financial implementation of operations funded with resources from the EDFs. Within the Commission, in 2010 almost all the EDF programmes were managed by the EuropeAid Cooperation Office (EuropeAid), which is also responsible for the management of most of the External Relations and Development expenditure financed by the General Budget of the European Union⁽¹⁾. A small proportion of the EDF projects⁽²⁾ relates to humanitarian aid and is managed by the Directorate-General for Humanitarian Aid (DG ECHO). The European Investment Bank (EIB) manages the Investment Facility. The Investment Facility is not covered by the Court's Statement of Assurance or the European Parliament's discharge procedure⁽³⁾⁽⁴⁾, even though the operations are conducted by the EIB on behalf of and at the risk of the European Union, using EDF resources.

5. Following the entry into force of the Treaty of Lisbon on 1 December 2009, the European External Action Service was launched on 1 December 2010. Its mission is to support the European Union's High Representative in fulfilling her mandate to implement the European Union's Common Foreign and Security Policy and other areas of external representation. In this context, EuropeAid and DG Development merged at the end of 2010 to DG for Development and Cooperation — EuropeAid (DG DEVCO) which has been implementing most of the EDF programmes since January 2011.

6. The EDFs' contribution is implemented through projects (66 % of 2010 payments) and budget support⁽⁵⁾ (34 % of 2010 payments) and managed under three main arrangements (**Table 1**): centralised, joint and decentralised management⁽⁶⁾.

⁽¹⁾ See chapter 5 'External aid, Development and Enlargement' of the Court's 2010 Annual Report on the implementation of the EU budget.

⁽²⁾ Representing 1,1 % of payments made in 2010.

⁽³⁾ See Articles 118, 125 and 134 of Council Regulation (EC) No 215/2008 of 18 February 2008 on the Financial Regulation applicable to the 10th European Development Fund (OJ L 78, 19.3.2008, p. 1) and the Court's Opinion No 9/2007 on the proposal for this Regulation (OJ C 23, 28.1.2008).

⁽⁴⁾ A tripartite agreement between the EIB, the Commission and the Court (Article 134 of the Financial Regulation of 18 February 2008 applicable to the 10th EDF referred to above) sets out rules for the audit of these operations by the Court.

⁽⁵⁾ Budget support involves the transfer of funds by the Commission to the national treasury of the partner country to provide additional budgetary resources to support a national development strategy.

⁽⁶⁾ Articles 21 to 29 of the Financial Regulation applicable to the 10th EDF.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

7. Under centralised management (49 % of payments in 2010), the Commission implements the aid activities directly. Under joint management (11 % of payments in 2010), international organisations are responsible for implementing European Union funded actions, provided that the accounting, audit, control and procurement procedures of the organisations offer guarantees equivalent to internationally accepted standards. EuropeAid's main partners are the United Nations' agencies and the World Bank. Under decentralised management (40 % of payments in 2010), the Commission may entrust the management of certain tasks to the authorities of the beneficiary countries. The principle of EDF decentralised management is illustrated in **Diagram 1**.

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

8. *The Commission mitigates these risks through substantial early detection and correction interventions. EuropeAid (at HQ and in delegations) performs a high level of ex-ante control both in terms of coverage and in terms of the nature of these controls, going well beyond the financial safeguards required by legislation. Preventative measures also play a very significant part in the control strategy including substantial training provision both for Commission staff and specifically designed for NAO staff. In addition 'NAO support' has been put in place in a number of countries. Guidance has also been significantly expanded in recent years including the publication in 2010 of a new 'Financial Management Toolkit' for recipients of EU funds.*

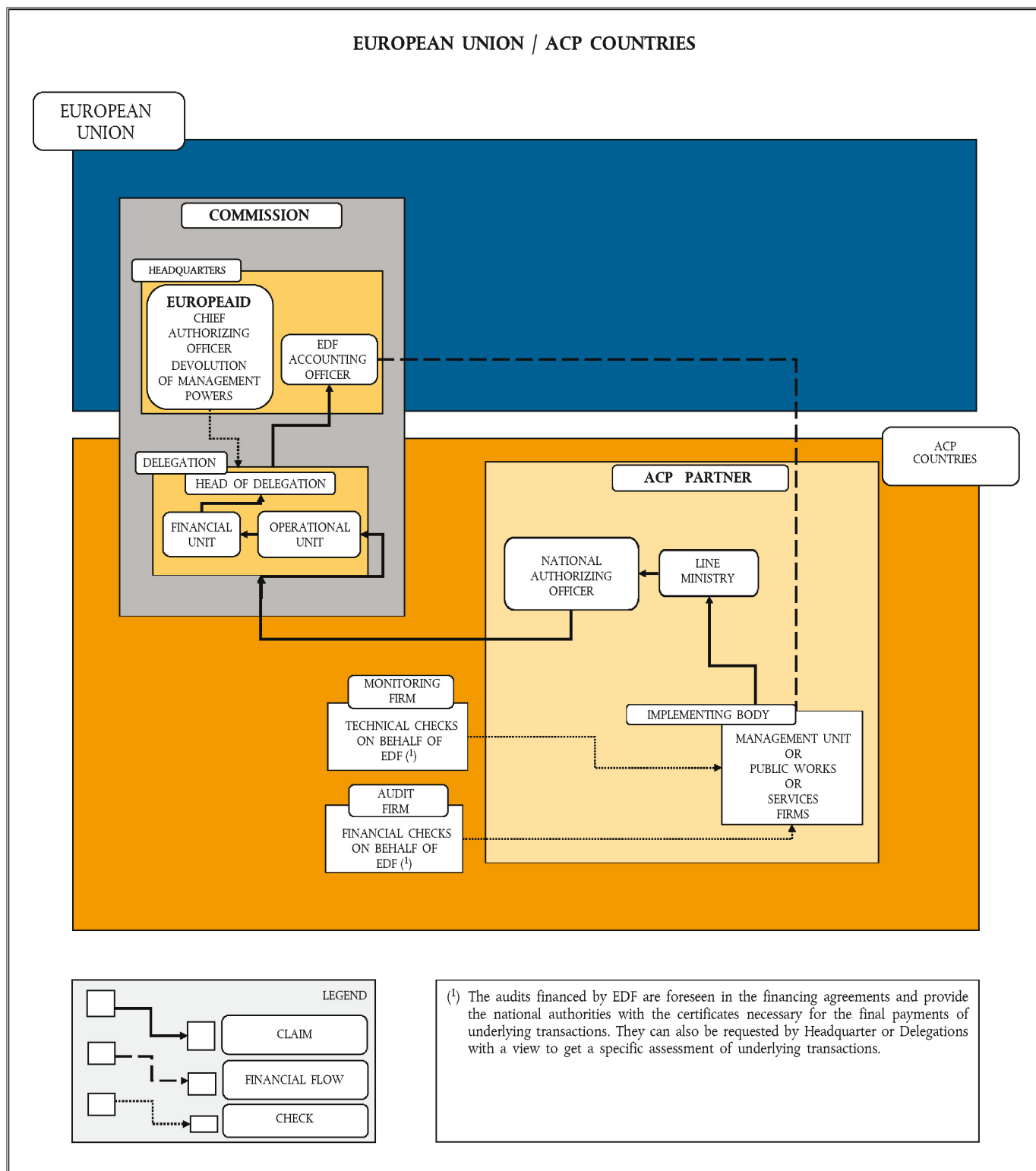
CHAPTER I — IMPLEMENTATION OF THE 8TH, 9TH AND 10TH EDFs

Financial implementation

9. In 2010, the 8th, 9th and 10th EDFs were implemented simultaneously. Each EDF agreement is usually concluded for a commitment period of around 5 years, but payments can be made over a longer period. The 8th EDF covers the period from 1995 to 2000 and provides European Union aid amounting to 14 625 million euro. The 9th EDF covers the period from 2000 to 2007 and provides for European Union aid amounting to 15 200 million euro.

10. The 10th EDF, covering the commitment period from 2008 to 2013, provides for European Union aid amounting to 22 682 million euro. It entered into force on 1 July 2008. Of this amount, 21 967 million euro are allocated to ACP countries and 285 million euro to OCTs. These amounts include 1 500 million euro and 30 million euro for the Investment Facility managed by the EIB for the ACP and OCT countries respectively. Finally, 430 million euro are earmarked for the Commission's expenditure for the programming and implementation of the EDF.

Diagram 1 — Principle of Decentralised management



THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

11. Total contributions from the Member States amounted to 3 500 million euro received in 2010. Contributions were still called up from the 9th EDF. In 2011, the final call under the 9th EDF will be made and the first contributions under the 10th EDF, in which all 27 Member States participate, will be called.

12. **Table 2** shows the cumulative use of EDF resources managed by the Commission and their financial implementation. In 2010, gross global commitments were made for an amount of 2 662 million euro (net 2 187 million euro) which is 13 % below financial implementation forecasts by the Commission⁽⁷⁾. This is mainly explained by the Commission's decisions not to proceed with several financing decisions under the Intra-ACP programme⁽⁸⁾ and some V-FLEX activities⁽⁹⁾, and delays in finalising the 10th EDF programming documents for the OCTs and the 10th EDF Mid-Term Review of the Country Strategy Papers. EuropeAid reports that individual commitments⁽¹⁰⁾ made in 2010 reached 3 710 million euro (net 3 304 million euro), exceeding the financial implementation forecasts by 410 million euro or 13 %. However, at least 305 million euro result from the correction of data related to commitments made in previous years.

13. Despite being 8 % below the target, gross payments reached a record high of 3 321 million euro (net 3 233 million euro) in 2010. Unspent commitments decreased by 8 % from 12 490 million euro to 11 444 million euro, which is explained by the high level of 2010 payments in comparison with new 2010 commitments. Old and dormant unspent commitments⁽¹¹⁾ further increased by 11 % from 1 217 million euro to 1 353 million euro.

12. *The Commission confirms that it intentionally delayed a number of projects which were not sufficiently advanced; this explains why the level of total commitments utilised was slightly lower than forecast.*

13. *As the Court states, payments have reached record levels, thus reducing outstanding commitments. The Commission has also carried out the important task of closing old projects under the 8th EDF.*

The increase in old and dormant commitments can be explained by the high level of commitments in previous years and, in particular, 2007 when the 10th EDF opened.

⁽⁷⁾ Global commitments relate to financing decisions. The difference between gross and net amounts results from decommitments.

⁽⁸⁾ In accordance with the Cotonou Agreement, intra-ACP cooperation is embedded in the regional cooperation and integration framework and covers all regional operations that benefit many or all ACP states.

⁽⁹⁾ Support to developing countries to cope with the impact of the financial crisis.

⁽¹⁰⁾ Relate to individual contracts. The difference between gross and net amounts results from decommitments.

⁽¹¹⁾ Old unspent commitments are funds committed more than 5 years ago and still unspent. Dormant unspent commitments are funds committed but neither contracted nor spent in more than 2 years.

Table 2 — Cumulative use of EDF resources at 31 December 2010

(million euro)

	Situation at end of 2009		Budgetary implementation during the financial year 2010 (net)				Situation at end of 2010				
	Global amount	Implementation rate ⁽²⁾	8th EDF ⁽³⁾	9th EDF ⁽³⁾	10th EDF	Global amount	8th EDF	9th EDF	10th EDF	Global amount	Implementation rate ⁽²⁾
A — RESOURCES ⁽¹⁾	48 746		– 85	– 151	282	46	10 701	16 482	21 609	48 792	
B — USE											
1. Global commitments	35 591	73,0 %	– 46	– 116	2 349	2 187	10 698	16 463	10 617	37 778	77,4 %
2. Individual commitments	29 021	59,5 %	8	476	2 820	3 304	10 507	15 683	6 134	32 324	66,2 %
3. Payments	23 101	47,4 %	157	1 304	1 772	3 233	10 240	13 121	2 973	26 334	54,0 %
C — Outstanding payments (B1-B3)	12 490	25,6 %					458	3 342	7 644	11 444	23,5 %
D — Available balance (A-B1)	13 155	27,0 %					3	19	10 992	11 014	22,6 %

⁽¹⁾ Include initial allocations to the 8th, 9th and 10th EDFs, co-financing, interest, sundry resources and transfers from previous EDFs.

⁽²⁾ As a percentage of resources.

⁽³⁾ Negative amounts correspond to decommitments.

Source: Court of Auditors, based on the EDF Reports on financial implementation and Financial statements at 31 December 2010.

THE COURT'S OBSERVATIONS

The Commission's Annual Report on the financial management of the 8th to 10th European Development Funds

14. The Financial Regulation applicable to the 10th EDF ⁽¹²⁾ requires the Commission to report each year on the financial management of the EDFs. In the Court's opinion, this report presents an accurate description of the achievement of the Commission's operational objectives for the financial year (particularly concerning financial implementation and control activities), as well as of the financial situation and the events that had a significant influence on the activities carried out in 2010. The Court draws attention to its observation in paragraph 12 on the accounting correction in 2010 of data related to individual budget support commitments made in previous years.

⁽¹²⁾ Articles 118 and 124.

CHAPTER II — THE COURT'S STATEMENT OF ASSURANCE ON THE EDFs**The Court's Statement of Assurance on the 8th, 9th and 10th European Development Funds (EDFs) to the European Parliament and the Council — Independent Auditor's Report**

I — Pursuant to the provisions of article 287 of the Treaty on the functioning of the European Union (TFEU) and Article 141 of the Financial Regulation applicable to the 10th EDF, which also applies to previous EDFs, the Court has audited:

- (a) the annual accounts of the 8th, 9th and 10th European Development Funds which comprise the consolidated financial statements⁽¹³⁾ and the consolidated reports on the financial implementation of the 8th, 9th and 10th EDFs for the financial year ended 31 December 2010; and
- (b) the legality and regularity of the transactions underlying those accounts within the legal framework of the EDFs in respect of the part of the EDF resources for whose financial management the Commission is responsible⁽¹⁴⁾.

Management's responsibility

II — In accordance with Articles 310 to 325 of the TFEU and the Financial Regulations applicable to the 8th, 9th and 10th EDFs, management is responsible for the preparation and fair presentation of the annual accounts of the EDFs and the legality and regularity of the transactions underlying them:

- (a) Management's responsibility in respect of the annual accounts of the EDFs includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies, on the basis of the accounting rules adopted by the EDF accounting officer⁽¹⁵⁾; and making accounting estimates that are reasonable in the circumstances. The Commission approves the annual accounts of the EDFs.
- (b) The way in which management exercises its responsibility for legality and regularity of underlying transactions depends on the method of implementation of the EDFs foreseen in the EDF Financial Regulations. Implementation tasks have to comply with the principle of sound financial management, requiring designing, implementing and maintaining effective and efficient internal control including adequate supervision and appropriate measures to prevent irregularities and fraud and, if necessary, legal proceedings to recover funds wrongly paid or used. Regardless of the method of implementation applied, the Commission bears the ultimate responsibility for the legality and regularity of the transactions underlying the accounts of the EDFs (Article 317 of the TFEU).

⁽¹³⁾ The consolidated financial statements comprise the balance sheet, the statement of economic outturn, the statement of cash flow and the table of items payable to the European Development Funds.

⁽¹⁴⁾ Pursuant to Articles 2, 3, 4,125(4) and 134 of the Financial Regulation applicable to the 10th EDF this Statement of Assurance does not extend to the part of the EDFs resources that are managed by the EIB and for which it is responsible.

⁽¹⁵⁾ The accounting rules adopted by the EDF accounting officer are derived from International Public Sector Accounting Standards (IPSAS) issued by the International Federation of Accountants or, in their absence, International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board. In accordance with the Financial Regulation, the consolidated financial statements for the financial year 2010 were prepared on the basis of these accounting rules adopted by the EDF accounting officer, which adapt accruals based accounting principles to the specific environment of the European Union, while the consolidated reports on implementation of the EDFs continue to be primarily based on movements of cash.

Auditor's responsibility

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

IV — An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated accounts and the legality and the regularity of the transactions underlying them. The procedures are selected based on the auditor's judgment, including an assessment of the risks of material misstatement of the consolidated accounts and of material non-compliance of the underlying transactions with the requirements of the legal framework of the EDFs, whether due to fraud or error. In assessing those risks, the auditor considers internal control relevant to the preparation and fair presentation of the final consolidated accounts, and supervisory and control systems implemented to ensure legality and regularity of underlying transactions, in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and reasonableness of accounting estimates made, as well as evaluating the overall presentation of the consolidated accounts and the Annual Activity Reports.

V — The Court considers that the audit evidence obtained is sufficient and appropriate to provide a basis for its statement of assurance.

Reliability of the accounts

Opinion on the reliability of accounts

VI — In the Court's opinion, the annual accounts of the 8th, 9th and 10th EDFs present fairly, in all material respects, the financial position of the EDFs as of 31 December 2010, and the results of their operations and cash flows for the year then ended, in accordance with the provisions of the EDF Financial Regulation and the accounting rules adopted by the accounting officer.

Legality and regularity of the transactions underlying the accounts

Revenue

Opinion on the legality and regularity of revenue underlying the accounts

VII — In the Court's opinion, revenue underlying the accounts for the year ended 31 December 2010 is legal and regular in all material respects.

*Commitments***Opinion on the legality and regularity of commitments underlying the accounts**

VIII — In the Court's opinion, commitments underlying the accounts for the year ended 31 December 2010 are legal and regular in all material respects.

*Payments***Basis for adverse opinion on the legality and regularity of payments underlying the accounts**

IX — The Court's audit revealed that the supervisory and control systems are partially effective in ensuring the regularity of payments. The Court's estimate for the most likely error rate for payments from the 8th, 9th and 10th EDFs is 3,4 %.

Adverse opinion on the legality and regularity of payments underlying the accounts

X — In the Court's opinion, because of the significance of the matters described in the basis for adverse opinion on the legality and regularity of payments underlying the accounts paragraph, the payments underlying the accounts for the year ended 31 December 2010 are materially affected by error.

1 September 2011

Vítor Manuel da SILVA CALDEIRA

President

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THE COURT'S OBSERVATIONS

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

15. The observations regarding the reliability of the accounts of the EDFs set out in paragraphs VI of the Statement of Assurance, are based on an audit of the consolidated financial statements⁽¹⁶⁾ and the consolidated report on the financial implementation of the 8th, 9th and 10th EDFs⁽¹⁷⁾. The audit examined, on a test basis, evidence relating to the amounts and disclosures. It included an assessment of the accounting principles used, significant estimates made by management and the overall presentation of the consolidated accounts.

16. The Court's overall audit approach and methodology regarding the regularity of transactions underlying the accounts is described in Annex 1.1, Part 2, to Chapter 1 of the 2010 Annual Report of the Court of Auditors on the implementation of the budget. The observations regarding the regularity of EDF transactions, set out in paragraphs VII to X of the Statement of Assurance are based on the following components:

- (a) an audit of a sample of 195 transactions, corresponding to 30 individual commitments and 165 interim and final payments made by Delegations or the Commission's central services⁽¹⁸⁾. Where necessary, implementing organisations and final beneficiaries were visited on-the-spot in order to verify the underlying payments declared in financial reports or cost statements;
- (b) an assessment of the effectiveness of supervisory and control systems at EuropeAid's central services and delegations; this covered the following elements:
 - (i) control environment and Internal Control Standards;
 - (ii) *ex-ante* controls of contracts and payments by the authorising officers, including the National Authorising Officers;
 - (iii) monitoring and supervision;
 - (iv) external audits;
 - (v) internal audit;

⁽¹⁶⁾ See Article 122 of the Financial Regulation of 18 February 2008 applicable to the 10th EDF: the financial statements shall comprise the balance sheet, the statement of economic outturn, the statement of cash flow, and the table of items payable to the EDF.

⁽¹⁷⁾ See Article 123 of the Financial Regulation of 18 February 2008 applicable to the 10th EDF: 'the reports on financial implementation shall comprise tables describing the appropriations, the commitments and the payments'.

⁽¹⁸⁾ EuropeAid: 128 projects and 20 budget support transactions; DG ECHO: 7 project transactions on humanitarian aid; DG External Relations: 10 transactions on administrative expenditure.

THE COURT'S OBSERVATIONS

- (c) a review of Commission management representations, which covered the assessment of the Annual Activity Report of EuropeAid.

Reliability of the accounts

17. The Court concludes that the accounts of the EDFs for the financial year ending 31 December 2010 fairly present, in all material respects, the financial position of the EDFs and the results of their operations and cash flows, in accordance with the provisions of the respective Financial Regulation and the relevant accounting rules adopted by the accounting officer.

18. However, as in 2009, EuropeAid's transactional *ex-post* controls and the Court's own controls identified a still high frequency of encoding errors⁽¹⁹⁾. While the Court's audit of the financial statements did not reveal material error due to such errors, these remain a source of concern as they may affect the accuracy of data used for the preparation of the annual accounts, in particular with respect to the annual cut-off exercise at year-end⁽²⁰⁾. Such errors also affect the reliability of EuropeAid financial management data.

Regularity of transactions

19. **Annex I** contains a summary of the results of transaction testing. The Court's testing of the sample of payments found 27 % to be affected by error. The most likely error estimated by the Court is 3,4 %⁽²¹⁾. The Court describes significant observations in further detail below.

THE COMMISSION'S REPLIES

17. The Commission welcomes the Court's conclusion that the EDF accounts for 2010, as in previous years, were free of material error.

18. EuropeAid has made particular efforts since 2009 to improve the quality of IT data entry. Major reviews of the contracts and audit modules of the management information system (CRIS) — as well as horizontal data quality initiatives — have been initiated in 2010/2011 with this in mind.

As the Court points out, this had no material impact on the annual accounts in 2010.

19. The Commission notes that in the previous year (2009) the EDF part of the EuropeAid portfolio was found to be free of material error (i.e. below 2 %) by the Court while the Budget portfolio had an estimated error rate of 2-5 %. For 2010 the Budget part of the EuropeAid portfolio has been found to be free of material error (1,7 %) by the Court but the EDF activities transactions are above the 2 % threshold (at 3,4 %). Thus the performance of EuropeAid's control architecture seems to be relatively stable over the last 2 years vis-à-vis the Court's audit, and continuing to show improvements in relation to the period prior to 2009.

⁽¹⁹⁾ E.g. contract type, contract start and end dates.

⁽²⁰⁾ The cut-off exercise seeks to ensure that both revenue and expenditure is completely and accurately recorded in the correct accounting period.

⁽²¹⁾ The Court calculates its estimate of error from a representative statistical sample. The figure quoted is the best estimate (known as the MLE). The Court has 95 % confidence that the rate of error in the population lies between 1,0 % and 5,9 % (the lower and upper error limits respectively).

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Revenue

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

Commitments

21. The Court's audit of commitments did not find any material error. However, individual commitments made for projects implemented under the decentralised management mode were affected by a significant frequency (four out of 14) of non-quantifiable errors regarding compliance with tendering rules and legal deadlines for the signature of contracts.

22. No errors were found in individual commitments made under other management modes. As regards budget support, the Court found that, in the context of the Commission's dynamic interpretation⁽²²⁾, EuropeAid demonstrated in a sufficiently structured and formalised manner compliance with the eligibility criteria set by the Cotonou Agreement.

Payments

23. The Court's audit found that payments were affected by material error.

Project payments

24. Quantifiable and non-quantifiable errors were found for all types of projects, except for supply contracts.

25. The main types of quantifiable errors detected in project payments were the following:

- (a) accuracy: calculation errors;
- (b) occurrence: absence of invoices or other supporting documents for services rendered or goods supplied, quantities claimed in excess of works carried out;
- (c) eligibility: compliance with procurement procedures, expenditure incurred outside the implementation period or related to activities and services not stipulated in the contract and undue payment of VAT.

21. The Commission will continue its efforts to step up the specific training on contractual procedures for both the offices of National Authorising Officers and Commission departments.

22. The Commission welcomes the recognition of the significant improvements made during 2009/2010 on structuring and formalising the process of assessing and demonstrating compliance with eligibility requirements.

23. See reply to paragraph 19.

25.

(c) The Commission has issued new instructions on the problem of the taxes imposed by beneficiary countries. These instructions should simplify the processing of certain invoices subject to VAT.

⁽²²⁾ See paragraphs 28 and 29 of Special Report No 2/2005 concerning EDF budget aid to ACP countries (OJ C 249, 7.10.2005).

THE COURT'S OBSERVATIONS

26. The most frequent types of non-quantifiable errors concerned performance guarantees⁽²³⁾ which were not adjusted following the increase of contract amounts; non-compliance with authorisation and contracting procedures for administrative expenditure authorised by the Directorate-General for External Relations; insufficient supporting documents; and inconsistencies within contractual rules.

Budget support payments

27. The Court's audit found budget support payments to be affected by a high frequency of non-quantifiable errors due to insufficiently structured demonstration of satisfactory progress made by the recipient governments in public finance management. The main explanation was the lack of an appropriate assessment framework since certain recipient governments' public finance management reform programmes were only in preparation or did not have realistic, clear and prioritised objectives. In a few cases, the Delegations' public finance management assessment report did not assess progress against the objectives set for the reference period. However, following the introduction of a revised framework for monitoring and reporting on progress in public finance management in June 2010, no such errors were found in the transactions examined for the second half of 2010.

Effectiveness of systems

28. **Annex 2** contains a summary of the results of the examination of systems. The Court found that the systems were partially effective in ensuring the regularity of transactions.

29. As stated in paragraph 4, EuropeAid's mission is to implement most of the external assistance instruments⁽²⁴⁾ financed from the General Budget of the European Union and the EDFs. Therefore, unless otherwise specified, the Court's observations concerning both the effectiveness of supervisory and control systems and the reliability of the Director-General's Annual Activity Report and declaration refer to all of EuropeAid's area of responsibility.

THE COMMISSION'S REPLIES

27. The Commission welcomes the finding that no errors relating to the demonstration of progress in public finance management have been detected since the introduction of the revised framework for assessing progress in public financial management in June 2010. The Commission is applying this approach rigorously.

⁽²³⁾ A performance guarantee (for works and supply contracts) is held against payment to the Contracting Authority for any loss resulting from the Contractor's failure to fully and properly perform his obligations under the contract.

⁽²⁴⁾ Except pre-accession aid, assistance to the West Balkans, humanitarian aid, macro-financial aid, Common Foreign and Security Policy and the Rapid Reaction Mechanism.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Control environment

30. EuropeAid's control environment is assessed as effective at the level of both delegations and central services.

31. EuropeAid has a clear control strategy to prevent or detect and correct errors and the Commission's Internal Control Standards are largely implemented. In 2010, EuropeAid pursued its efforts to further strengthen its supervisory and control systems. As set out in the Commission's replies to the 2008⁽²⁵⁾ and 2009⁽²⁶⁾ Annual Reports of the Court on the EDFs, EuropeAid set up and started to implement an 'Action Plan for a strengthened EuropeAid management and control pyramid' (Action Plan)⁽²⁷⁾. The plan addresses most observations and recommendations from the Court's previous Annual Reports and also includes actions to better align staffing with corporate objectives⁽²⁸⁾. However, the plan was still at an early stage of implementation in 2010.

Ex-ante controls

32. The Court assessed *ex-ante* controls by authorising officers in EuropeAid's central services and in the Delegations as partially effective at preventing or detecting and correcting errors.

Projects

33. In respect of project payments, weaknesses were found in the checks on the accuracy, occurrence and eligibility of expenditure (see paragraph 25). Depending on the type of contracts, EuropeAid's *ex-ante* checks often largely rely on certificates from external supervisors (for works contracts) or external audits and expenditure verifications (for programme estimates, grants and fee-based service contracts). However, the frequency of errors found by the Court in expenditure which had been subject to such external certifications, audits and verifications shows that the assurance that can be derived from those is limited. As an example, the Court found errors in 12 transactions related to grant contracts which were all authorised following external audits or expenditure verifications.

31. The 'Action Plan for a strengthened EuropeAid management and control pyramid' is progressing on schedule with many of the actions already implemented by mid 2011. One major activity, the establishment of a new web-based twice yearly reporting tool (External Assistance Management Report) with key performance indicators drawn from the management information systems, will be launched in July 2011.

33. The Commission does not rely solely on these expenditure verifications for assurance. EuropeAid's (mandatory) audit methodology includes an annual risk assessment of projects to select activities which should be subject to a 'risk based' audit — most often in addition to mandatory expenditure verifications. Moreover EuropeAid is continuing its efforts to raise the quality of expenditure verifications — most recently by the issue of mandatory standard Terms of Reference for auditors (whether contracted by the Commission or by beneficiaries). Delegations and HQ also have a role in reviewing the quality of the verifications submitted.

⁽²⁵⁾ Paragraph 54.

⁽²⁶⁾ Paragraph 54(b).

⁽²⁷⁾ Action Plan for a strengthened EuropeAid management and control pyramid of 19.11.2010.

⁽²⁸⁾ Action Plan for a strengthened EuropeAid management and control pyramid of 19.11.2010, actions 7.1 and 7.2.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

Budget support

34. As regards budget support, one significant improvement was the introduction of a new format and scheme for Delegations' annual reporting on reforms of public finance management systems in recipient countries during the second half of 2010. This aims to ensure that disbursements are based on a structured assessment of payment conditions. However, certain recipient governments' public finance management reform programmes were only in preparation or did not have realistic, clear and prioritised objectives, which hampered a structured assessment of the progress of reform (see paragraph 27).

Monitoring and Supervision

35. The Court assessed monitoring and supervision as effective for EuropeAid's central services and as partially effective for Delegations.

EuropeAid's central services

36. At EuropeAid's central services, a number of tools are in place to monitor the operational activities and the functioning of key controls.

37. Central services analyse delegations' bi-annual External Aid Management Reports in order to monitor the implementation of projects in recipient countries and other aspects like Delegations' internal controls and human resources. For the Delegations visited in 2010, the Court found that the reports provided relevant and reliable information. EuropeAid's Action Plan aims to further strengthen their role as a key control and to place these reports 'as the foundation of the control pyramid and the main accountability tool between Delegations and headquarters.' In this context, for the financial year 2011, Heads of Delegations will be required for the first time to provide annual assurance on the performance and the legality and regularity of operations to support the Director-General's annual assurance declaration⁽²⁹⁾.

34. The Commission welcomes the acknowledgement of the improvement introduced through the new format for annual reporting on progress in public financial management reforms. It is expected that as this approach is consolidated there will be increased clarity in objectives and the use of appropriate reference periods for assessment.

⁽²⁹⁾ Action Plan for a strengthened EuropeAid management and control pyramid, 19.11.2010, actions 2.1 and 2.2.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

38. Verification missions to Delegations help EuropeAid's central services to assess project implementation and the adequacy of the Delegations' internal organisation, systems and processes. In addition to 14 verification missions carried out during the year, EuropeAid made an analysis of the results of 14 verification missions performed in 2008 and 2009. The analysis stresses the need for further capacity building of Delegations' operational and financial sections and to enhance project monitoring and ownership by partner countries.

39. At the end of 2009 EuropeAid's central services issued additional guidance for Delegations' on-the-spot monitoring visits, including selection criteria to ensure proper coverage of both operational and financial aspects. However, most Delegations visited in 2010 by the Court were not yet following the recommended procedures (see paragraph 44). The Court also found that, in order to improve project monitoring and ownership by partner countries, EuropeAid's central services and Delegations continued to provide support to the services of EDF National Authorising Officers (see paragraph 43).

40. Audits mandated by EuropeAid under the framework contract agreement provide valuable information on the systemic weaknesses affecting projects' control systems and the level and nature of potentially ineligible expenditure. EuropeAid's central services analyse and follow-up these audit results annually. Most of the findings are of a recurrent nature and include missing or inadequate documentation and the use of incorrect procurement procedures by implementing organisations. In this context, one significant achievement was the 'Financial Management Toolkit for recipients of EU funds for external actions', which was finalised and disseminated at the end of 2010 in order to improve the knowledge of financial management and eligibility rules by implementing organisations.

41. EuropeAid's central services also monitor compliance issues also via transactional *ex-post* controls. As in previous years, these controls frequently found errors concerning incomplete and inaccurate data in EuropeAid's CRIS⁽³⁰⁾ information system. Findings were also identified in the weak documentation of procurement procedures. However, errors with a financial impact mainly related to unjustified clearings of advance payments, which were likely to be anyway corrected before contracts are closed. Although EuropeAid has further developed the system of transactional *ex-post* controls over the years, it is still not effective in detecting errors in the regularity of underlying transactions and weaknesses in *ex-ante* controls performed by authorising officers.

39. EuropeAid's current guidelines on on-the-spot visits are not mandatory instructions. EuropeAid is currently reflecting on how to better systematise the monitoring framework (including on-the-spot visits), within the current resource constraints of staffing, mission budget and taking into account security issues. In particular EuropeAid is planning to introduce multi-annual monitoring and evaluation plans and strengthen monitoring guidance and reporting — notably in the 2011 redesign of the External Assistance Management Reports (submitted twice yearly by delegations) and the new Programme and Project Cycle Management Guidelines.

41. EuropeAid is currently reviewing its internal control architecture and will look again at the cost effectiveness of the *ex-post* transactional control system.

⁽³⁰⁾ Common RELEX Information System.

THE COURT'S OBSERVATIONS

42. EuropeAid has not set up management information systems to monitor the results and the follow-up of on-the-spot visits, external audits and expenditure verifications, which makes it difficult for the Director-General and the Heads of Delegation to have an assurance that remedial action has been taken in a timely manner, notably as regards the correction of errors found. In addition, EuropeAid's information systems CRIS Audit and CRIS Recovery Orders, are not yet linked, which complicates the monitoring of corrective actions.

Delegations

43. As in previous years, the Court found poorly documented and ineffective checks at most National Authorising Officers in EDF beneficiary countries. EuropeAid's central services and the Delegations frequently provide technical assistance to strengthen these checks, but often with limited results, either because the National Authorising Officers do not perform their tasks adequately or because of resource constraints or high staff turnover rates.

44. Most Delegations visited by the Court in 2010 were not following EuropeAid's guidelines on conducting on-the-spot monitoring visits (see paragraph 39). The summary conclusions drawn by EuropeAid in 2010 from 14 verification missions to Delegations carried out in the period March 2008 to September 2009 ⁽³¹⁾ are that Delegations are subject to resource constraints which often limit their capacity to perform certain key monitoring activities, such as project monitoring on-site, particularly as regards financial aspects. EuropeAid's Action Plan addresses the need to enhance project monitoring ⁽³²⁾.

External audits

45. The Court assessed the external audit function as effective with regard to EuropeAid's central services and partially effective in respect of the Delegations.

THE COMMISSION'S REPLIES

42. *The absence of a standardised IT tool does not mean that audit and monitoring findings are not followed up. Every authorising officer by subdelegation follows up the audits and issues recovery orders if necessary.*

EuropeAid expects the system modules for processing of audit results and for establishing recovery orders to be linked in the management information system (CRIS) by the close of 2011.

See also replies to paragraphs 31 and 62(c).

43. *See reply to paragraph 8.*

44. *See reply to paragraphs 39 and to 62(c).*

⁽³¹⁾ EuropeAid 01: 'Verification Missions from March 2008 to September 2009: summary of main recommendations', dated 17 December 2010.

⁽³²⁾ Action Plan for a strengthened EuropeAid management and control pyramid, dated 19 November 2010, action 6.2.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

EuropeAid's central services

46. EuropeAid's central services have developed a common methodology on the set-up, implementation and follow-up of annual audit plans which is compulsory for EuropeAid's central services and Delegations. A significant improvement for 2010 was the introduction of a common benchmark providing for a 5 % annual audit coverage. EuropeAid's central services complied with this methodology.

47. EuropeAid's central services closely monitor the Delegations' external audit functions and the quality of external audits carried out under the Commission's audit framework contract. Comprehensive annual quality reviews provide useful information on the need for further improvements and serve as the basis for further instructions and guidance to external auditors.

Delegations

48. In most respects, Delegations have carried out their external audits in accordance with the methodology. However, the Court found that there remain areas where improvement is necessary. As indicated already in the 2009 Annual Report of the Court on the EDFs ⁽³³⁾, staff constraints in Delegations limit their capacity to launch risk-based audits, the priority being given to compulsory audits. They also have a negative impact on the timeliness of the audit clearance process, which involves a risk that ineligible expenditure may become irrecoverable.

Internal Audit

49. The Court assessed internal audit as effective.

50. The Internal Audit Capability (IAC) ⁽³⁴⁾ operated in compliance with its objective to provide the Director-General with assurance as to the effectiveness and efficiency of risk management, control and internal governance processes. Staff shortages faced in 2009 were solved and the IAC was able to fully implement its 2010 work plan.

46. The Commission welcomes the Court's recognition of the significant improvements being made year on year to EuropeAid's external audit methodology.

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

⁽³³⁾ Paragraph 47.

⁽³⁴⁾ The IAC is a unit of a Commission Directorate-General. It is managed by a Head of Unit who reports directly to the Director-General. Its mission is to provide independent assurance on the effectiveness of the internal control system with a view to improve the Directorate-General's operations.

THE COURT'S OBSERVATIONS

51. In 2010, there was a significant reduction in the average time taken by EuropeAid's services to comment on draft audit reports and to follow up recommendations made by IAC and the Internal Audit Service (IAS) ⁽³⁵⁾. There were still significant delays in the implementation of some recommendations from previous years, mainly related to human resources and IT issues.

Reliability of Commission management representations

52. **Annex 3** contains a summary of the results of the review of Commission management representations.

53. The Annual Activity Report gives a fair picture of the implementation and results of the various supervisory and control systems in place. It is clear and informative, in particular through the use of quantitative indicators. The report states that, given the design and the results of its multi-annual control architecture, EuropeAid does not believe that the residual error rate ⁽³⁶⁾ on its portfolio merits a reservation in the Director-General's declaration of assurance. However, it still does not provide evidence to support this assertion.

54. In order to demonstrate how different control layers contribute to the detection and correction of errors, EuropeAid presented for the first time a summary of errors detected and corrected by *ex-ante* and transactional *ex-post* controls ⁽³⁷⁾. However, these data are incomplete since there is no comprehensive information on errors detected and corrected following audits and expenditure verifications launched by EuropeAid outside the audit framework contract or launched by beneficiaries.

55. EuropeAid has not yet developed a key indicator for the estimated financial impact of residual errors after all *ex-ante* and *ex-post* controls have been carried out. As already indicated in the 2009 Annual Report of the Court on the EDFs ⁽³⁸⁾, in the absence of such an indicator EuropeAid is not in a position to demonstrate that the financial impact of shortcomings and errors is below the materiality criteria set. The Court notes that EuropeAid is developing a methodology to provide such information ⁽³⁹⁾.

THE COMMISSION'S REPLIES

51. Significantly delayed implementation of audit recommendations relate to human resources policy and information technology systems, both of which are extremely difficult to implement quickly, given the lead times for policy change and implementation within an annual planning cycle. However, the implementation of all recommendations is very carefully and regularly followed up within EuropeAid including through its six-monthly 'audit' management reporting.

53. The Commission believes that the qualitative and quantitative indicators set out in the four assurance building blocks of the EuropeAid Annual Activity Report do indeed provide the necessary evidence to underpin the Director General's Statement of Reasonable Assurance and give an accurate assessment of financial management in EuropeAid in relation to regularity.

54. The Annual Activity Report clearly documents that the data setting out errors detected and corrected by auditors, only covers those auditors procured under EuropeAid's audit framework contract, i.e. the actual monetary figure for EuropeAid's annual error detection and correction is much higher than that given in the report. In the medium term, IT developments could allow central registration of financial findings for even locally procured auditors, but the cost effectiveness of this development has yet to be fully assessed.

55. EuropeAid's work on the development of a methodology for estimating the residual error rate in the DG's portfolio (once all controls have been executed) was launched as planned in 2010 and is continuing on schedule in 2011. The methodology was approved in March 2011 and a pilot study was launched in May 2011 to test it and to elaborate a detailed work program for its full implementation.

⁽³⁵⁾ The IAS is a Directorate-General of the Commission. It is headed by the Commission's Internal Auditor and reports to the Audit Progress Committee of the Commission. Its mission is to provide independent assurance on the effectiveness of the internal control systems and to help the Commission by means of opinions, advice and recommendations.

⁽³⁶⁾ Error rate after all *ex-ante* and *ex-post* controls have been implemented.

⁽³⁷⁾ EuropeAid 2010 Annual Activity Report, paragraph 3.1.2.2.4, p. 30.

⁽³⁸⁾ Paragraph 50.

⁽³⁹⁾ EuropeAid 2010 Annual Activity Report, paragraph 3.1.2.2.4, p. 30.

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

56. With respect to the financial year 2010, EuropeAid's Director-General declared that he had obtained reasonable assurance that existing control procedures gave the necessary guarantees concerning the regularity of transactions. The Court's audit does not corroborate this assertion. It found that EuropeAid's systems were partially effective and that payments made by EuropeAid from the EDFs and from the General Budget of the European Union for External Relations and Development were affected overall by material error⁽⁴⁰⁾.

57. The Court considers that the Director-General's declaration and Annual Activity Report give a partially fair assessment of financial management in relation to regularity.

Conclusions and recommendations

Conclusions

58. Based on its audit work, the Court concludes that the EDFs accounts for the financial year ending 31 December 2010 fairly present, in all material respects, the financial position of the EDFs and the results of their operations and cash flows for the year then ended, in accordance with the provisions of the Financial Regulation and the accounting rules adopted by the accounting officer.

59. Based on its audit work, the Court concludes that for the financial year ending 31 December 2010:

- (a) the revenue of the EDFs was free from material error;
- (b) the individual commitments entered into by the EDFs were free from material error but affected by a significant frequency of non-quantifiable errors; and
- (c) the payments made by the EDFs were affected by material error.

60. Based on its audit work, the Court concludes that EuropeAid's supervisory and control systems were partially effective in ensuring the regularity of payments.

56. The Commission has designed its controls to cover the full lifecycle of its multi-annual projects. It believes that these supervisory and control systems are effective and have significantly improved year on year. The recommendations made by the Court in previous years have been acted on. Many of the improvements made have been recognised by the Court, resulting in significant elements of the key control system being judged 'effective', including for 2010 an 'effective' rating on EuropeAid's control environment.

See also reply to paragraph 19.

57. See reply to paragraph 53.

59.

(c) See reply to paragraph 19.

60. See reply to paragraph 56.

⁽⁴⁰⁾ See Chapter 5 'External Aid, Development and Enlargement' of the 2010 Annual Report of the Court of Auditors on the implementation of the EU budget, paragraph 5.35 and 5.36 and Annex 5.1.

THE COURT'S OBSERVATIONS

61. As noted in previous Annual Reports on the EDFs, EuropeAid has set up a comprehensive control strategy, but weaknesses remain in certain areas. At the end of 2010, EuropeAid launched an 'Action Plan for a strengthened EuropeAid management and control pyramid'. The plan addresses many observations and recommendations from the Court's previous and current Annual Report and can bring significant improvements to the design and implementation of EuropeAid supervisory and control systems.

Recommendations

62. **Annex 4** shows the result of the Court's review of progress in addressing recommendations made in previous Annual Reports. Following this review and the findings and conclusions for 2010, the Court recommends that EuropeAid should finalise the following actions foreseen in its Action Plan:

- (a) Develop a key indicator for the estimated financial impact of residual errors after all *ex-ante* and *ex-post* controls have been implemented (see paragraph 55 ⁽⁴¹⁾).
- (b) Assess the cost-effectiveness of the various controls, notably of the transactions *ex-post* control systems (see paragraphs 41 and 61 ⁽⁴²⁾).
- (c) Strengthen the effectiveness of project monitoring, including on-the-spot visits, on the basis of multiannual monitoring and evaluation plans (see paragraph 44).

THE COMMISSION'S REPLIES

61. See reply to paragraph 31.

62.

- (a) EuropeAid's work on the development of a methodology for estimating the residual error rate in the DG's portfolio (once all controls have been executed) was launched as planned in 2010 and is continuing on schedule in 2011. The methodology was approved in March 2011 and a pilot study was launched in May 2011 to test it and to elaborate a detailed work program for its full implementation.
- (b) The Commission started work on the cost effectiveness of controls within a wider review of EuropeAid's control strategy in 2010. This work will be reviewed and relaunched in 2011/2012 in the context of the final outcome of the current revision of the Financial Regulation.

See also reply to paragraph 41.

- (c) EuropeAid is planning to introduce multiannual monitoring and evaluation plans and strengthen monitoring guidance and reporting — notably in the 2011 redesign of the External Assistance Management Reports (submitted twice yearly by Delegations) and the new Programme and Project Cycle Management Guidelines.

⁽⁴¹⁾ See also the 2009 Annual Report of the Court on the EDFs, paragraph 54(a).

⁽⁴²⁾ See also the 2009 Annual Report of the Court on the EDFs, paragraph 54(b).

THE COURT'S OBSERVATIONS

THE COMMISSION'S REPLIES

63. The Court also recommends that EuropeAid should:

- (a) review the reliability of certificates from external supervisors, audits and expenditure verifications (see paragraph 33);
- (b) introduce management information systems which allow the Director General and the Heads of Delegation to better monitor the follow-up of results from on-the-spot visits, external audits and expenditure verifications (see paragraph 42);
- (c) link the CRIS Audit and CRIS Recovery Orders information systems (see paragraph 42);
- (d) continue its efforts to ensure that data are recorded in an accurate, comprehensive and timely manner in the CRIS information system (see paragraphs 18 and 41).

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

- (a) Ensure that Delegations consistently apply the new format and scheme for Delegations' annual reporting on reforms of public finance management systems in recipient countries so as to provide a structured and formalised demonstration of public finance management progress (paragraph 34).
- (b) Promote through policy dialogue the setting of clear assessment frameworks in recipient countries' reform programmes on public finance management (paragraph 34).

63.

- (a) *Commission staff does currently review certificates from external supervisors, audits and expenditure verifications in relation to their quality and reliability. In addition, in 2008 the Commission made technical audits mandatory on all works contracts above 15 million euro and later issued standard terms of reference. Technical audits cover the full life cycle of the project from design to implementation including verification of supervisors' certificates. The full benefits of these changes were not necessarily yet visible in 2010. The Commission is currently also reflecting on possible mechanisms to raise the quality of expenditure verifications contracted by beneficiaries.*
- (b) *The Commission is developing management information systems (notably via a new web-based delegation reporting system) allowing management to better monitor the operational and financial management data available from the field.*

See also reply to paragraph 62(c).

- (c) *EuropeAid expects the system modules for processing of audit results and for establishing recovery orders to be linked in the management information system (CRIS) by the close of 2011.*
- (d) *EuropeAid will pursue the significant efforts launched in 2009 to improve the quality of data entry. Major reviews of the contracts and audit modules of the management information system (CRIS) have been initiated in 2010/2011 with this in mind.*

64.

- (a) *The Commission will ensure that the revised format is rigorously applied in order to underpin its structured and formalised approach to assessing progress in public finance management.*
- (b) *The Commission recognises the importance of establishing clear assessment frameworks for beneficiaries' public finance management reform strategies from the outset of its budget support operations. This approach will be underpinned by regular policy dialogue with the relevant authorities.*

ANNEX 1

RESULTS OF TRANSACTION TESTING FOR EUROPEAN DEVELOPMENT FUNDS

	2010			2009	2008	2007
	Projects	Budget Support	Total			
Total of commitments	20	10	30	50	45	60
Total of payments (of which):	145	20	165	170	170	148
Advances	0	0	0	0	40	0
Interim/Final payments	145	20	165	170	130	148

SIZE AND STRUCTURE OF THE SAMPLE

RESULTS OF TESTING FOR PAYMENTS ⁽¹⁾ ⁽²⁾

Proportion of payments tested found to be:

Free of error	74 %	(107)	65 %	(13)	73 %	(120)	78 %	76 %	63 %
Affected by one or more errors	26 %	(38)	35 %	(7)	27 %	(45)	22 %	24 %	37 %

Analysis of payments affected by error

Analysis by type of error

Non-quantifiable errors:	39 %	(15)	100 %	(7)	49 %	(22)	65 %	61 %	49 %
Quantifiable errors:	61 %	(23)	0 %	(0)	51 %	(23)	35 %	39 %	51 %
Eligibility	70 %	(16)	0 %	(0)	70 %	(16)	23 %	44 %	68 %
Occurrence	17 %	(4)	0 %	(0)	17 %	(4)	23 %	38 %	21 %
Accuracy	13 %	(3)	0 %	(0)	13 %	(3)	54 %	19 %	11 %

ESTIMATED IMPACT OF QUANTIFIABLE ERRORS ON PAYMENTS

Most likely error rate

3,4 %

Lower error limit

1,0 %

Upper error limit

5,9 %

⁽¹⁾ To improve insight into areas with different risk profiles within the policy group, the sample was split up into segments.

⁽²⁾ Numbers quoted in brackets represent the actual number of transactions.

ANNEX 2

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

Assessment of selected supervisory and control systems

System concerned	Control environment	Ex-ante controls	Monitoring and supervision	External audits	Internal audits	Overall assessment
Central Systems EuropeAid	Effective	Partially effective	Effective	Effective	Effective	Partially effective
Delegations	Effective	Partially effective	Partially effective	Partially effective	N/A	Partially effective

Overall assessment of supervisory and control systems

Overall assessment	2010	2009	2008	2007
	Partially effective	Partially effective	Partially effective	Partially effective

ANNEX 3

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

Main DGs concerned	Nature of declaration given by Director-General (*)	Reservations given	Court observations	Overall assessment of reliability	
				2010	2009
AIDCO	without reservations	N/A	EuropeAid has set up a comprehensive control strategy and continued to bring significant improvements to the design and implementation of its supervisory and control systems. However, the Court's audit found that there remain weaknesses in certain controls and that the payments were affected by material error.	B	B

(*) By reference to the declaration of assurance of director-general, he/she has reasonable assurance that the control procedures put in place give the necessary guarantees concerning the regularity of transactions.

A: the Director-General's declaration and the Annual Activity Report give a fair assessment of financial management in relation to regularity.

B: the Director-General's declaration and Annual Activity Report give a partially fair assessment of financial management in relation to regularity.

C: the Director-General's declaration and the Annual Activity Report do not give a fair assessment of financial management in relation to regularity.

FOLLOW-UP OF PREVIOUS RECOMMENDATIONS FOR THE EUROPEAN DEVELOPMENT FUNDS

Year	Court Recommendation	Progress made	Commission reply	Court analysis
2009	EuropeAid should, in the context of its planned review of its overall control strategy, develop a key indicator for the estimated financial impact of residual errors after all <i>ex-ante</i> and <i>ex-post</i> controls have been implemented, based for example in an examination of a representative statistical sample of closed projects (2009 Annual Report, paragraph 54(a)).	EuropeAid is in the process of reviewing its overall control strategy; reference is made to the 'EuropeAid Action Plan for the Strengthening of the Control Pyramid'. EuropeAid contracted an external consultant to develop a reliable and feasible methodology. The adoption by EuropeAid is foreseen for the first half of 2011.	<i>EuropeAid's work on the development of a methodology for estimating the residual error rate in the DG's portfolio (once all controls have been executed) was launched as planned in 2010 and is continuing on schedule in 2011. The methodology was approved in March 2011 and a pilot study was launched in May 2011 to test it and to elaborate a detailed work programme for its full implementation.</i>	The Court takes note of the Commission reply.
	EuropeAid should, in the context of this review, assess the cost-effectiveness of the various controls, notably of the transactional <i>ex-post</i> control system (2009 Annual Report, paragraph 54(b)).	As mentioned in the previous recommendation, EuropeAid is in the process of reviewing its overall control strategy. An estimate of the costs of controls has been prepared.	<i>The Commission started work on the cost effectiveness of controls in 2010. This work will be reviewed and relaunched in 2011/2012 in the context of the final outcome of the current revision of the Financial Regulation.</i>	The Court takes note of the Commission reply.
	EuropeAid should finalise and disseminate the financial management toolkit targeting the high inherent risk of errors at the level of implementing organisations, contractors and beneficiaries to ensure adequate knowledge of financial management and eligibility rules (2009 Annual Report, paragraph 54(c)).	The Financial Toolkit was finalised and dissemination started in December 2010. It is available online since February 2011.	<i>This recommendation has been fully implemented.</i>	The Court takes note of the Commission reply.
	EuropeAid should continue its efforts to ensure that the Delegations record data in CRIS Audit in a comprehensive and timely manner (2009 Annual Report, paragraph 54(d)).	Despite EuropeAid's efforts to address this issue, a limited quality of data in CRIS audit was still found for three out of the seven Delegations visited in 2010.	<i>EuropeAid has launched a review of the audit module of CRIS in 2011. Together with the ongoing horizontal work on CRIS data quality this should bring significant improvements to the data quality issues in the audit module in the medium term.</i>	The Court takes note of the Commission reply.

Year	Court Recommendation	Progress made	Commission reply	Court analysis
	The design of CRIS Audit should be modified to provide information on the amounts of final ineligible expenditure and financial corrections done after the audit clearance process with the auditee has been completed (2009 Annual Report, paragraph 54(e)).	No progress concerning this issue was observed during 2010.	<i>This recommendation was issued in the 2009 ECA Annual Report published in November 2010 and was accepted by the Commission. However the lead times involved in IT developments not already integrated into the annual planning cycle are very significant. Although the conceptual/design work started on the revision of CRIS audit in 2011, system changes are unlikely to be implemented before 2012.</i>	The Court takes note of the Commission reply.
2009	EuropeAid should ensure that the specific conditions for performance-based variable tranches clearly specify the indicators, targets, calculation methods and verification sources (2009 Annual Report, paragraph 55(a)).	All 10th EDF Budget Support Financing Agreements audited in 2010 specify the indicators, targets, calculation methods and verification sources in a clear and unambiguous manner.	<i>This recommendation has been fully implemented.</i>	The Court takes note of the Commission reply.
	EuropeAid should ensure that Delegations' reports provide a structured and formalised demonstration of public finance management progress by clearly setting the criteria against which progress was to be assessed (i.e. the results that the recipient Government had to achieve during the period concerned), the progress made and the reasons why the reform programme may have not been implemented according to plan (2009 Annual Report, paragraph 55(b)).	A new format for Delegation's PFM Annual Monitoring Reports, including a new assessment scheme for PFM reform progress was introduced in June 2010. The comparison of achievements with clear and realistic priority objectives for the short (next 12 months) and medium term (next 3 years) by the recipient government promotes structured and formalised assessment. However, the Court detected cases in 2010 where PFM Reform Programmes/ action plans were only in the process of adoption or didn't have realistic, clear and prioritised objectives. This hampered such structured and formalised assessment.	<i>This recommendation has been fully implemented. In addition to the guidance issued on reporting in June 2010, the Commission has developed a structured framework for assessing the relevance and credibility of beneficiaries' public financial management strategies which is to be applied before embarking on budget support programmes. This places particular emphasis on setting out an assessment framework with clear baselines and objectives that can be monitored for the duration of the programme. In February 2011 this framework was issued to ACP Delegations for use in the preparation of new programmes.</i>	The Court takes note of the Commission reply.