

Briefing note in preparation for

**The joint meeting of the FEAC, EFAC & PAC with
European Court of Auditors (ECA) member, Mr Leo
Brincat**

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House of Representatives, Parliament of Malta



HOUSE OF REPRESENTATIVES
PARLIAMENT OF MALTA

The European Court of Auditors (ECA)

The European Court of Auditors is the independent audit institution of the European Union. It issues audit reports and opinions which are used to hold to account those responsible for managing the EU budget. This is primarily the responsibility of the European Commission, along with the other EU institutions and other bodies. But for around two-thirds of spending – principally natural resources and cohesion – responsibility is shared with the Member States. In 2016, EU spending reached €136.4 billion, or around €267 for every citizen. This amounts to around 1% of EU gross national income and represents approximately 2% of total public spending in EU Member States. In 2016, most money went to natural resources (€57.9 billion), cohesion (€35.7 billion) and growth and jobs (€15.2 billion).

Each year, the auditors check the EU accounts and provide their opinion on two questions: whether the accounts are accurate and reliable, and to what extent there is evidence of money being received or paid out in error (known as regularity and legality). The auditors test samples of transactions to provide statistically-based estimates of the extent to which revenue and the different spending areas are affected by error. They measure the estimated level of error against a materiality threshold of 2%, above which revenue or spending is considered to be irregular.

A “clean” opinion means the figures present a true and fair view and follow the rules of financial reporting. A “qualified” opinion means that the auditors cannot give a clean opinion, but the problems identified are not pervasive. An “adverse” opinion indicates widespread problems.

The auditors have given a clean opinion of the EU’s accounts since 2007. But until now their opinion on the regularity and legality of spending has been adverse for every year since 1994. The estimated level of error is not a measure of fraud, inefficiency or waste. It is an estimate of the money that should not have been paid from the EU budget because it was not used in accordance with applicable rules. In 2016, the auditors found 11 instances of suspected fraud out of approximately 1,000 transactions audited (in 2015, the auditors found 12 instances). These cases were forwarded to EU anti-fraud office, OLAF.

Definitions

What are entitlement and cost reimbursement payments? EU spending is characterised by two types of expenditure involving distinct patterns of risk:

- Entitlement payments, based on meeting certain conditions; such payments include among others student and research fellowships (under competitiveness spending), direct aid for farmers (under ‘Natural resources’), or salaries and pensions for EU staff (under ‘Administration’).
- Cost reimbursement payments, where the EU reimburses eligible costs for eligible activities. Such payments are for example made for research projects (under competitiveness spending), investment in regional and rural development and training schemes (covered by expenditure under ‘Economic, social and territorial cohesion policy’ and ‘Natural resources’) and development aid projects (under ‘Global Europe’).

The ECA’s 2016 annual reports on the EU budget and the European Development Funds

The annual report covers the reliability of the accounts, the regularity of income and spending and overall performance aspects of the budget. The main conclusion is that in 2016 the EU accounts were true and fair and that the share of irregular spending was further reduced.

The European Court of Auditors gives a clean opinion on the reliability of the 2016 accounts of the European Union. Revenue for 2016, taken as a whole, was legal and regular, as in previous years. Payments for 2016 were legal and regular, except for cost reimbursement payments.

- The 2016 accounts were prepared in accordance with international standards and present, in all material aspects, a true and fair view. Therefore, as has been the case every year since 2007, the ECA is issuing a clean opinion on their reliability.
- There has been a sustained improvement in the estimated level of error in the payments made from the EU budget over the last few years: 2016: 3.1 %, 2015: 3.8 % and 2014: 4.4 %. Moreover, in 2016, a significant part of the audited expenditure - *entitlement payments* - was not affected by a material level of error. Therefore, for the first time since the ECA started to provide a statement of assurance in 1994, it is issuing a *qualified opinion* on 2016 payments.
- *Entitlement payments* are made to beneficiaries for meeting conditions rather than to reimburse costs. They represent about half of expenditure audited in 2016 and include direct aid to farmers, the biggest part of spending under ‘Natural Resources: Market and direct support’ (with an estimated level of error of 1.7 %) and ‘Administration’ (0.2 %). Both these areas had an estimated level of error below the 2 % materiality threshold. Other activities

funded through entitlement payments are student and research fellowships and agri-environment measures.

- *Cost reimbursement payments* are made to beneficiaries who have incurred costs that can be refunded with EU money. They include spending in the areas with the highest error rates: Natural Resources: Rural development, the environment, climate action and fisheries' (with an estimated level of error of 4.9 %) and 'Economic, social and territorial cohesion' (4.8 %). Other activities funded through cost reimbursement payments are research projects, training schemes and development programs.
- The Commission's reporting on regularity is for most areas broadly in line with the ECA's results. The Commission also finds a material level of error overall.
- Corrective action by authorities in the Member States and by the Commission had a positive impact on the estimated level of error. Without this action, the ECA's overall estimated level of error would have been 1.2 % higher. Sufficient information was available to prevent, or to detect and correct, a significant proportion of errors. Had this information been used to correct errors, the estimated level of error for the overall spending on 'Economic, social and territorial cohesion' and 'Global Europe' would have been below the 2 % materiality threshold in 2016.
- This year, the total amount of payments the EU committed itself to making from future budgets was higher than ever before. This amount is projected to continue to rise through to 2020. Clearing this backlog and preventing a new one from forming should be priorities when planning the Multiannual Financial Framework (MFF) for the period starting in 2020.

Summary of main points

The EU's accounts present a true and fair view - The EU's accounts for 2016 were prepared in accordance with international public sector accounting standards and present, in all material respects, a true and fair view of the EU's financial results for the year and its assets and liabilities at the end of the year. The ECA was therefore able to give a clean opinion on the reliability of (i.e. 'sign off') the accounts, as it has done every year since 2007.

EU expenditure is legal and regular, except for cost reimbursement payments - The ECA tested a sample of transactions from across the EU budget to provide estimates of the extent to which revenue and the different spending areas are affected by error. It concluded that revenue was free from material error.

For 2016, the ECA issued a qualified opinion on payments made from the EU budget. The ECA is doing so for the first time since it started providing a statement of assurance in 1994. For expenditure, the ECA estimates the level of error in expenditure as a whole at 3.1 %. This compares to 3.8 % in 2015 and 4.4 % in 2014.

Questions

What is the auditing method used by the ECA? How reliable is it? How does the ECA arrive at a conclusion such as a 'clean' opinion?

Do you think Brexit will somehow affect the work of the ECA?

Could you please explain to us the procedure in case of serious irregularities such as fraud and who is responsible for initiating and executing these steps?

The share of irregular spending has been reduced compared to the previous year. Is there a reason why this has happened, and is the ECA considering taking any action in order to further reduce irregular spending?

What are the main challenges that the ECA is currently facing?

The ECA has issued a qualified opinion on payments (cost reimbursement payments) from the EU budget. Why was this the case and will the ECA take any measures or actions so that the same problems encountered in 2016 do not re-occur?

Could you please give us some information in relation to EU spending in Malta?

For more information, please contact:

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