

Brussels, 7 December 2000

Meeting of Presidents of Supreme Audit Institutions in Sofia (Bulgaria) 7-8 December 2000: Modernising financial control in accession countries and in the EU

Modernising financial control in accession countries has been a major concern of both the Commission and the European Court of Auditors for some years, and central to the Commission's recent reforms. The subject also forms a special chapter in the Enlargement Negotiations [- Chapter 28 "Financial Control"].

Good and prudent management and control of public finance is a key element of what is generally called the Community's "*acquis*". The "heart" of the system of public finance is the responsibility of the public authority to manage well, and subsequently account for, the taxpayer's money.

Systems of financial management and control, compatible with the Community ones, need to be in place in the candidate countries now. The pre-accession aid instruments, PHARE, ISPA and SAPARD can (and should) be implemented in a decentralised way. This needs to be done according to agreed criteria and conditions, which require reliable financial control systems. The challenge of decentralisation of pre-accession aid can be used as a testing phase for the implementation of Structural Policies after accession.

One way that this process can be encouraged is through forming close links to others that have such systems in place. The Commission therefore welcomes the networks growing between the European Court of Auditors and the Supreme Audit Institutions in the Member States and candidate countries. These foster the institution-building process of external and internal control.

Whilst these activities have focussed initially on the establishment of independent external audit bodies, Supreme Audit Institutions also have a decisive role to play in the establishment and functioning of internal control and audit systems. This covers not only verification of the existence of such systems but also recommendations designed to improve their functioning and eliminate weaknesses.

By doing this, the Supreme Audit Institutions together with the European Court of Auditors have become strong and most welcome allies of the Commission. But co-ordination of our activities needs to be improved further in this area, so as to avoid conflicting signals and duplication of work.

Recent discussions between the European Court of Auditors and the Commission have confirmed the need for enhanced co-ordination between the two Institutions and have provided the starting point for a more systematic and comprehensive co-operation aimed at fostering reliable Public Internal Financial Control (PIFC) systems.

In order to bring about the financial control environment, one needs:

- To extend co-operation on matters relating to enlargement and financial control between relevant Commission services and their counterparts in the candidate countries
- To continue the reform of the Commission in the area of Financial Control
- To increase protection of the financial interests of the Community.

Co-operation with candidate countries

Launched in the early 90', this co-operation arose through decentralised implementation of the PHARE programme. Later it was extended through the accession negotiations. From the very beginning the overall objective has been to assist candidate countries in setting-up and/or upgrading their Public Internal Financial Control systems, so as to improve management and control of public funds in general and Community financial assistance in particular.

Co-operation involved:

- **High level fact-finding missions** to Government control organisations and Supreme Audit Institutions of all PHARE countries from 1991. These missions assessed the systems and examined possible improvements;
- **Annual Seminars** in one of the capitals of PHARE countries on the management and control of PHARE money in that country ;
- **Training Seminars** in Brussels for officials from national control organisations.

Since the start of accession negotiations co-operation has been extended through:

- **Conclusion of bilateral Administrative Co-operation Agreements (ACA)** relating to Financial Control with 12 of the 13 candidate countries designed to form the framework for a permanent dialogue with financial control counterpart bodies on Government level. The Agreement with Turkey is in the process of negotiation;
- **Creation of the Contact Group** of European Financial Control Organisations providing for a « trilogue » on Financial Control matters between the Commission, the 15 Member States and the 13 candidate countries. The Group holds Annual Meetings, which provide a forum for exchange of information and discussion on key issues. This year's meeting took place in Berlin 9/10 October 2000.
- **Setting up an information and communication network** between all parties interested in the subject of Enlargement and Financial Control, e.g. relevant Commission services, candidate countries (notably Ministries of Finance and Supreme Audit Institutions), the European Court of Auditors, OECD/SIGMA and many others. This network is supported by a specialised Financial Control Contact website on the Internet, accessible to the European financial control organisations. This site contains all relevant documentation (e.g. Policy Papers, Regular Reports, National and Community Legislation, information on Contact Group meetings, training seminars etc.)

Within a relatively short period, through these co-operation activities, the majority of candidate countries have been able to set out a comprehensive concept of Public Internal Financial Control, tailored to their constitutional provisions. Subsequently they have been able to adopt the relevant legislation and rules setting up the structures and laying down procedures of internal control and audit throughout Government. In most cases, a central co-ordination point in the Ministry of Finance (in some cases even in the Prime Minister's Office) has overseen the process. The Commission has contributed to the development of such systems and has supported their improvement.

The enlargement negotiations are into the heart of the "*acquis*" now. Since the beginning of this year a series of final assessments has been launched to provide common positions on the state of progress in each of the negotiation chapters in each candidate country. For Chapter 28 « Financial Control », if these assessments show that the country has prepared the conceptual and legislative aspects successfully, and has gone far enough in establishing the necessary institutional framework, the chapter will be provisionally closed. Further monitoring will continue to ensure the implementation of the new systems in accordance with timetables agreed with the relevant country.

Chapter 28 has been provisionally closed for four of the six countries of the so-called Luxembourg group, namely Cyprus, Hungary, Poland and Slovenia. For the two remaining countries Czech Republic and Estonia, which did not pass the assessments last summer, the Commission will now relaunch the procedure on the basis of recent developments which show a good deal of progress in these countries, notably as regards the adoption of the necessary legislation.

Those countries which have achieved provisional closure of Chapter 28 and subsequently show positive results during the monitoring phase as regards implementation of the control systems, will be best placed to obtain the « green light » for fully decentralised implementation of the pre-accession aid instruments.

Decentralisation for the SAPARD programme is simply a « must » right from the beginning, as this programme is due to cover large numbers of relatively small projects in rural development. These projects cannot be run one by one from headquarters Brussels (or even via the EU Delegations). Therefore the necessary national structures (« paying and certifying agencies ») need to be in place and accredited by the Commission before any SAPARD instalments can be paid.

For PHARE and ISPA, the existing « semi-decentralised » structures and procedures for the implementation of the PHARE programme (with contract endorsements by the Delegations) can be used during a transitional period. However, the Extended Decentralised Implementation System (EDIS) for these two programmes needs to be launched rapidly with the overall objective of reaching full decentralisation by the end of next year (deadline fixed in the ISPA Regulation). Preparations have started already by means of a « checklist » established in accordance with the criteria and conditions laid down in the so-called Co-ordination Regulation (Council Regulation 1266/99) and transmitted to the candidate countries. Once the replies are received the Commission will evaluate them and organise verification audits in order to assess if the national management and control systems do comply with the aforesaid criteria and conditions. For Cyprus and Malta a similar approach has been decided, adapted to their specific situation.

Commission Reform in the area of Financial Control (recasting of the Financial Regulation)

Helping candidate countries to get ready for enlargement is one thing. But the EU itself must ensure that they are well prepared to meet the challenge of a much larger Community as well. The EU's budgetary and financial systems were originally designed for a Community of just 6 Member States and for a limited number of Community policies, of which the most important one in money terms, the common agricultural policy, was decentralised from the outset and administered at Member State level. The rules and procedures devised for this initial situation, including financial control have proved their value over a long period of time and guaranteed proper and efficient management and control of Community funds.

The Community's enlargement from 6 to 15 Member States and the transfer of new tasks to Community level saw an increase in budgetary resources and the number of financial transactions. The early system of financial management and control set up in 1977 has come under increasing strain and needs urgent reform.

The reform has four cornerstones, which – as we see it – form the key elements of a modern internal control and audit system:

1. Abolition of the centralised financial control function (the so-called *ex-ante* control) in favour of decentralised internal control systems throughout the management chain.

2. Making those who approve a programme or project also fully responsible for its correct implementation.

3. Separating the functions of *ex ante* financial control and *ex post*

internal audit, currently united under the Financial Controller (which runs the risk of potential conflicts of interest).

4. Creating a central advisory body on financial procedures to ensure uniform application of those procedures by all relevant departments.

Some of the changes implied by the reform presuppose the amendment of our Financial Regulation.

The Commission has recently launched a substantial recast of the Financial Regulation to be approved by the Council, with the aim of achieving a fundamental improvement and streamlining of budgetary procedures, including the restructuring of Financial Control. The most urgent element of this restructuring, namely the separation of *ex ante* control and *ex post* audit has been tabled as a « fast track » proposal to precede the general overhaul of the Financial Regulation. We hope that the Council at the latest early in the New Year will adopt this fast track proposal.

Meanwhile preparations have started to set up the new control environment within the Commission. A new centralised Internal Audit Service has been created together with an Audit Progress Committee of 5 (4 Commissioners + 1 External Member). Moreover, the deconcentration of central *ex-ante* control to operational DG's is due to start in the near future.

The central advisory body has been set up under the name of « Central Financial Service » (CFS) within DG BUDGET and is now becoming fully operational. Its main task is to develop « minimum standards » for management (e.g. contract management) and internal control and help departments to apply those standards correctly. It is supposed to function as a « help-desk » for those in the Commission who deal with the management of Community funds on a day-to-day basis.

The CFS also includes the particular « help-desk » and « networking » functions relating to the setting-up or upgrading of public financial control systems in the candidate countries.

Protection of the Community's financial interests

In May 1999 the European Anti-Fraud Office (OLAF) was created. It covers two different functions, investigations, where its independence is assured, and drawing up and fraud proofing EU regulations, policy setting and negotiating agreements, as a department of the Commission.

About two months ago, the Commission proposed to the Intergovernmental Conference on the Reform of the Institutions the establishment of the function of the European Public Prosecutor in order to complement and indeed reinforce the role and function of OLAF.

The Commission proposal is confined to what is absolutely necessary. The new Treaty Article 280a proposal is intended to form the legal basis for this new function. It is restricted to a minimum of provisions such as appointment, resignation and independent status of the European Public Prosecutor, as well as the definition of his activities. His responsibilities will be strictly confined to the protection of the Community's financial interests in accordance with Article 280 of the Treaty, which remains unchanged.

The new Article 280a only creates the general framework for the European Prosecutor. Details like the definition of offences (and related penalties) as well as the procedural rules to be followed will need to be laid down subsequently in a detailed Council Regulation.

The creation of a European Public Prosecutor would be an important step forward towards the effective protection of the Community's financial interests under criminal law. Against the alarming power of organised crime and the scale of cross-border fraud the existing range of legal instruments has proved to be a blunt sword, though at times remarkably effective. In order to avoid that OLAF's administrative investigations and preventive actions remain too limited, the corresponding measures under criminal law must be strengthened and unified.

The 1995 Convention on the Protection of the Financial Interests of the EU and its Protocols, negotiated under the so-called Third Pillar, laid down minimum requirements for a uniform definition of fraud related to Community finances and urged Member States to adapt their criminal law accordingly. The Convention has, however, still to be ratified by a majority of Member States. The only credible answer to the steadily growing volume of fraudulent attacks against the Community's financial interests is a minimum of enforceable law at the Community level, together with the office of a European Public Prosecutor. The latter would take the responsibility for initiating and co-ordinating the prosecution of cross-border fraud and corruption cases against EU financial interests and act as prosecutor before the competent national courts.