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REPLIES OF THE COMMISSION TO THE EUROPEAN COURT OF AUDITORS' DRAFT ANNUAL REPORT 2013

CHAPTER 6 "EMPLOYMENT AND SOCIAL AFFAIRS"

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INTRODUCTION

6.9. The Commission has taken specific actions in order to mitigate the risks identified, which include preventive and corrective measures such as guidance, training, simplification and a strict policy on interruptions and suspensions of payments, when necessary. The Commission is in particular actively promoting the use of simplified cost options by the Member States and addressing identified cases of "gold plating" involving unnecessary complex eligibility rules set out by some Member States. The Commission also insists on the importance of first level checks. In this respect, DG Employment, Social Affairs and Inclusion has carried out a risk based thematic audit on the management verifications and has shared the audit conclusions and recommendations with the ESF Managing Authorities.

6.10. Member States approve projects on a rolling basis as foreseen in the priority axis of multi-annual Operational Programmes. The concerned monitoring committees are required to ensure that projects with EU added value are selected and approved and the spending is subject to multiple checks from national and EU authorities.

REGULARITY OF TRANSACTIONS

Common reply of the Commission to paragraphs 6.13 and 6.14.

The Commission disagrees with the inclusion of an error with a significant impact despite the fact that no evidence is available to conclude that the concerned project implemented by a beneficiary currently under preliminary investigation on which no judgement has been made yet by the judicial authorities, was affected by any irregularities and despite the fact that the allegations, which concern potential overcharging of expenditure would in any case not apply to the operation audited by the Court since it was implemented through standard unit costs (see paragraph 6.16) approved by the Managing Authority. Should the allegations be finally confirmed, the Commission will apply the necessary financial corrections.

The Commission notes a decrease in the frequency of errors detected by the Court in the policy area of Employment and Social Affairs in 2013 27% as compared to 35% in 2012 and 40% in 2011.

The Commission understands that the error rate reported by the Court is an annual estimate which takes into account corrections of project expenditure or reimbursements affected by errors detected and recorded before the Court's audit. The Commission underlines that it is bound by the Financial Regulation which stipulates, in Article 32 (2) (e), that its internal control system should ensure, amongst other things, “adequate management of the risks relating to the legality and regularity of the underlying transactions taking into account the multiannual character of programmes and the nature of payments”. The Commission will continue to exercise its supervisory role, in particular by implementing financial corrections and recoveries at a level that corresponds to the level of irregularities and deficiencies identified.

The Commission further notes that given the multiannual character of the management and control systems under Cohesion policy, errors made in 2013 may also be corrected in subsequent years even after the closure of the programmes. To illustrate this, in 2013 financial corrections concerning the ESF 2000-2006 and 2007-2013 programming periods amounted to 689 Mio €, which includes the corrections that the Court has already taken into account in determining its error rate. Furthermore, financial corrections amounting to €153m for the 1994-1999 programming period were also implemented in 2013. Total recoveries amounted to €56m in 2013.

6.15. The Commission will follow up all errors reported by the Court and will apply financial corrections where appropriate and legally possible. The Commission notes that in some cases national or regional rules applied to ESF funded expenditure are more demanding than those foreseen in the national legislation for similar expenditure nationally funded. Therefore, these additional requirements can be seen as an instance of gold plating, self-imposing unnecessary administrative burden and complexity to ESF funded expenditure, as described in the recently published Commission report[1].

6.16. The Commission has actively worked since the introduction of the simplified cost options to progressively extend their use and considers that these efforts have already led to positive results. The Commission continues to actively promote the use of simplified cost options in the 2014-2020 programming period in order to both reduce the administrative burden on the beneficiaries and to further reduce the risk of error.

6.17. The Commission will follow all cases identified by the Court and will ensure that corrective measures take place.

6.20. While the Commission and the Court audit compliance with public procurement rules in the same way, the Commission applies since the 2000-2006 programming period proportionate flat-rate corrections thereby addressing the risk of damage to the EU budget and taking into account the nature and gravity of the actual irregularities.

These flat rates are applied by the Commission and by most national authorities when imposing financial corrections for infringements of public procurement rules, including when following up the errors reported by the Court.

The Commission also notes that the Discharge Authority called on the Commission and the Court to harmonise their methodologies to quantify public procurement errors (European Parliament decision of 17 April 2013 on discharge in respect of the implementation of the general budget of the European Union for the financial year 2011).

The Commission has updated in 2013 its decision on the quantification of public procurement errors in shared management, including inter alia cohesion spending and rural development (see Commission decision C(2013)9527 final).

Based on this Commission decision, the Commission estimates that the quantification of errors for public procurement errors in 2013 would be up to 0,1 percentage point lower than calculated by the Court when using its own quantification.

6.22. The Commission will follow up all errors reported by the Court and ensure that corrective measures take place.

6.23. See Commission reply to Box 6.4 (a).

Box 6.4 – Examples of excessive costs claimed

(a) The salary situation in ESF funded projects in Romania was one issue identified by DG Employment, Social Affairs and Inclusion in an audit conducted in 2012. A flat rate financial correction of 25% has been applied to this OP. As a result the Managing Authority concerned commissioned a study on the cost structure and the wage bill to serve as a basis for establishing maximum wage levels to be applied in future projects. The Commission has provided further recommendations to the Managing Authority concerning the parameters to be used for the determination of wage ceilings to be applied to ESF funded projects since the current ones are still considered too high.

[1] http://www.europarl.europa.eu/document/activities/cont/201311/20131115ATT74496/20131115ATT74496EN.pdf

(c) Discrepancies between the payments from the Union to the priority and the effective Funds contribution to the operations co-financed under that priority could occur. This is a consequence of the flexibility that the managing authorities have in applying different co-financing rates to individual operations as stated in Article 53(4) of the General Regulation.

In accordance with the closure guidelines adopted by the Commission on 20.3.2013, the beneficiaries should receive at closure an amount of public contribution (national Funds and ESF) at least equal to the ESF amount reimbursed by the Commission to the Member State.

6.24. The Commission has developed new guidance in order to further strengthen the reliability of management verifications in the 2014-2020 programming period. This guidance, which draws on the lessons learned from the previous programming period, has been presented to Member States and will be issued in the second half of 2014.

6.25. Further to the extensive work on management verifications done in the regular audits conducted by DG Employment, Social Affairs and Inclusion, the risk based thematic audit referred to by the Court focused on specific operational programmes in order to identify and address the root causes of the insufficient reliability of the management verifications. The results of this thematic audit have been presented by the Commission to Managing and Audit Authorities in 2014 and have been used in developing the guidance referred to in §6.24.

Common Commission reply to paragraphs 6.26 and 6.27

Concerning the 2000-2006 programming period, the Commission aims to ensure that the error rate at closure will not exceed 2% for each operational programme. To this end, besides the significant number of audits conducted during the 2000-2006 programming period, DG Employment, Social Affairs and Inclusion has performed between 2011 and 2013 14 risk based closure audits covering 21 2000-2006 OP's, which represent 8.8% of the total number of OPs and 25.6% of the total amount of expenditure.

Based on this extensive audit work, and in order to protect the EU budget, significant financial corrections have been implemented at closure. As disclosed in DG's Employment, Social Affairs and Inclusion 2013 AAR (page 121), as of the end of 2013, 233 OPs have been closed for the 2000-2006 programming period. The Commission has implemented cumulative financial corrections for the 2000-2006 programming period amounting to €1.7bn, of which €452m in 2013, when final payments and clearings for the 2000-2006 programming period amounted to €3.3bn. The Commission will follow up the specific errors identified by the Court and notes that it can make further financial corrections until three years after the formal closure of a programme when residual errors are detected.

While acknowledging the above risks, the Commission emphasizes that by nature it is almost unavoidable that individual instances of ineligible expenditure at project level remain after the closure process, since this process aims to reach the assurance that the overall remaining error rate is below the materiality threshold of 2%. Moreover, by applying flat rate financial corrections at closure the Commission effectively protects the EU budget without necessarily correcting each case of ineligible expenditure at project level.

EXAMINATION OF SELECTED CONTROL SYSTEMS

6.29. The audit authorities play a central role in the assurance building process, as from the beginning of the programming period and set-up of systems.

The regulation provides the Commission the possibility to rely on the work of an audit authority for its assurance under certain conditions (Article 73 of Regulation (EC) No 1083/2006). The Commission is closely cooperating and coordinating with them, and has started reviewing their methodologies and audit results as early as 2009. This contributed to capacity building by providing advice, guidance and recommendations to audit authorities through the Commission's re-performance of audit work carried out by audit authorities.

In its 2013 Annual Activity Report (see pages 42 to 44), DG Employment, Social Affairs and Inclusion provided a detailed assessment of the accuracy and reliability of the audit information and results reported by audit authorities in their 2013 Annual Control Reports.

6.32.

(a) The Commission concluded that a reliable error rate could not be calculated on the basis of the elements available. It therefore decided to provisionally apply a flat rate of 10%, in accordance with the Commission Decision C(2011)7321 of 19.10.2011 - Guidelines on the principles, criteria and indicative scales to be applied in respect of financial corrections 2007 – 2013.

6.34. According to the Commission's standing instructions for the 2013 AAR a reservation is required only if the cumulative financial risk is above 2%, which was not the case for the large majority of the OPs referred to by the Court, since the necessary financial corrections have been implemented. As mentioned in DG's Employment, Social Affairs and Inclusion 2013 AAR out of the 41% payments to OPs referred to by the Court 30 percentage points referred to OPs with an error rate between 2 and 5% and only 11 percentage points of the payments were made to OPs with an error rate above 5%. This clearly reflects the strict interruptions and suspensions policy systematically implemented by DG Employment, Social Affairs and Inclusion, which has resulted in 25 interruptions, 12 warning letters and 11 suspension decisions adopted in 2013.

6.35. The Commission agrees that the Court's error rate and Commission's one are not directly comparable. However, the objective of this process is essentially the same, i.e. assessment of the risk to the EU budget in a particular year.

The Commission takes into account all these differences in its assessment, in particular timing, differences in quantification of public procurement and other errors and the impact of flat rate corrections it imposes to programmes (see Commission reply to paragraph 11 of the Court's Special Report 16/2013).

Except for the differences noted above, the Commission considers that for the 2013 annual report, as it was the case for the last three years in a row for DG Employment before this annual report, the result of the Commission's assessment is in line with the error rates calculated by the Court.

6.38. See the Commissions replies to paragraphs 10.32 to 10.39.

CONCLUSIONS AND RECOMMENDATIONS

Common Commission reply to paragraph 6.39 (a) and (b)

The Commission shares the Court's assessment with the exception of one error (see Commission reply to paragraph 6.13).

The Commission has a thorough process to verify the reliability of the error rates reported by the audit authorities which are revised where appropriate. The fact that the error rates reported in the AAR of DG Employment, Social Affairs and Inclusion are in line with the error rate established by the Court corroborates the reliability of the auditing and reporting systems.

The Commission understands that the error rate reported by the Court is an annual estimate which takes into account corrections of project expenditure or reimbursements affected by errors detected and recorded before the Court's audit. The Commission underlines that it is bound by the Financial Regulation which stipulates, in Article 32 (2) (e), that its internal control system should ensure, amongst other things, "adequate management of the risks relating to the legality and regularity of the underlying transactions taking into account the multiannual character of programmes and the nature of payments”. The Commission will continue to exercise its supervisory role, in particular by implementing financial corrections and recoveries at a level that corresponds to the level of irregularities and deficiencies identified.

The Commission further notes that given the multiannual character of the management and control systems under Cohesion policy, errors made in 2013 may also be corrected in subsequent years even after the closure of the programmes.

The Commission will follow all cases identified by the Court and will ensure that corrective measures take place.

6.42. The Commission has taken specific actions in order to mitigate the risks identified, which include in particular preventive and corrective measures such as guidance, training, simplification and a strict policy on interruptions and suspensions of payments and financial corrections.

Recommendation 1: The Commission accepts this recommendation and agrees on the importance of the "first level" checks conducted by the Member States and shares the view that these should be further strengthened. Therefore, it has given guidelines to Member States on the way Managing Authorities should define and implement their management verifications. Furthermore, a comprehensive guidance note on management verifications for the 2014-2020 programming period, drawing on the lessons learned in the 2007-2013 programming period and the Court's findings, has been drafted and will be issued in the second half of 2014.

Recommendation 2: The Commission accepts this recommendation and agrees to disclose in the annual activity reports instances where it considers that due to insufficient assurance on the reported information on withdrawals and recoveries it did not take this information into account in the calculation of the cumulative residual risk.

The Commission will also continue to take account of the Member States' audit results in this area, and will envisage requesting additional controls from audit authorities where necessary.

In addition, the Commission will increase the coverage of its audits on recoveries and withdrawals in the forthcoming years in order to obtain additional assurance on the accuracy of reported data.

Recommendation 3: The Commission does not accept this recommendation.

While the Commission agrees with the Court that the flexibility in allocating Funds to operations at a rate lower or higher than the co-financing rate fixed for the priority axis that has been granted to the Member States by the 2007-2013 and 2014-2020 regulations may lead to differences between the contribution from the Funds paid by the Commission to the Member and the amount of ESF reimbursed by Member State at project level, it considers that this cannot be assimilated to pre-financing.

In line with the CPR for the 2014-2020 programming period and for each payment claim received and at closure, the Commission ensures that the ESF paid to the Member State at priority axis level is not higher than the public eligible contribution indicated in the payment application for the priority (article 130.2 of Regulation (EU) No 1303/2013). In addition, Art. 132.1. stipulates that the managing authorities shall ensure that beneficiaries receive the total amount of eligible public expenditure in full and no later than 90 days from the date of submission of the payment claim by the beneficiary. Finally, the Member State shall ensure that by closure of the operational programme, the amount of public expenditure paid to beneficiaries is at least equal to the contribution from the Funds paid by the Commission to the Member State (article 129 of Regulation (EU) No 1303/2013).

Recommendation 4: The Commission accepts this recommendation, but believes that these issues need to be addressed on a case-by-case basis. This point has already been raised in several audit reports issued by the Commission (DG Employment, Social Affairs and Inclusion). For certain Member States, where the problem was considered to be of a systemic nature, action plans have been requested addressing specifically this phenomenon.

Recommendation 5: The Commission accepts this recommendation and is already implementing it. Regarding simplification for the 2014-2020 programming period, the Commission has taken the necessary actions to ensure that Member States implement the relevant measures as foreseen by the European Structural and Investment Funds regulations in their Operational Programmes. The necessary support is given to the Member States to ensure that all possibilities for simplification are considered through training, guidance on simplified cost options and Technical Working Groups which encourage an active exchange of best practices. Such possibilities for implementing simplification measures are also reflected in the adoption of Partnership Agreements whereby the Member States are required to demonstrate the necessary actions to achieve a reduction in the administrative burden as well as their administrative capacity. A guidance note on simplification is also being prepared in order to assist Member States to fully leverage the significantly strengthened simplification opportunities in the new programming period.

Recommendation 6: The Commission accepts the recommendation and agrees to disclose further details in annex to the annual activity reports for those individual cases where based on its assessment of the specific situations it takes a reasoned decision not to make reservations or not to include the issue in the quantification of the reservation.