

## **Summary of the presentation ‘The audit of legality and regularity by the European Court of Auditors’ by Arjen Lok<sup>1</sup>**

### Introduction of the European Court of Auditors and its statement of assurance

The European Court of Auditors (ECA) is the European Union’s (EU) external auditor. One of its highlighted reports is the annual report on the implementation of the budget. This report includes the statement of assurance on the financial statement and on legality and regularity of transactions underlying the accounts. In addition to the statement of assurance the annual report provides the budgetary authorities with specific assessments of the main policy areas the European Union’s budget covers. Next to revenue it relates to the spending areas agriculture, rural development, regional policy, employment and social affairs, external relations, research and administration.

### Representative of the whole

The statement of assurance was introduced in Treaty of Maastricht. In his contribution ‘The first ten years of DAS’<sup>2</sup> Mr Giorgio Clemente, Member of ECA at the time the statement of assurance was introduced, describes it as: “an opinion on the accuracy of the recording of accounting transactions (accuracy of entries), similar to the sort issued by independent auditors in the private sector. It did not provide certainty, since this could only be achieved by analysing all transactions (which would not have been desirable because of the unfavourable cost/benefit ratio), but an opinion based on the audit of a sample of transactions held to be representative of the whole and identified within the mass of the institution’s transactions through a statistical method.”

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<sup>1</sup> The information, views and opinions expressed in this presentation are the presenter’s personal views and do not necessarily reflect those of the European Court of Auditors.

<sup>2</sup> DAS is the French acronym of statement of assurance ‘déclaration d’assurance’. The contribution of Mr Giorgio Clement is included in ‘Reflections/réflexions’ available at: [http://www.eca.europa.eu/Lists/ECADocuments/REFLECTIONS\\_35TH\\_ANNIVERSARY/Reflections\\_35anniversary.pdf](http://www.eca.europa.eu/Lists/ECADocuments/REFLECTIONS_35TH_ANNIVERSARY/Reflections_35anniversary.pdf)

### Legality and regularity of transaction underlying the accounts

A second particular element in the statement of assurance is the requirement to provide an opinion on the legality and regularity of transactions underlying the accounts. Mr Giorgio Clemente describes this as: “The certification of the legality of the individual transactions underlying the accounts is a conceptually different operation. ... In this connection, we must assess whether individual transactions comply with the regulatory parameters on which they are based - both the substantive provisions (sector regulations, conventions, agreements and contracts) and the accounting provisions (budget nomenclature, Financial Regulation and internal management standards). Consequently, for expenditure, the audit reached down to the level of the final beneficiaries of EU funds, with the possibility of verifying the physical aspects of the operations funded. For revenue, where there are limits to the checks that can be carried out on debtors, for traditional own resources, the audit looked at supporting documents relating to the establishment of the amounts owed by debtors rather than material operations. Finally, the Court interpreted the treaty to mean that it required a statement of assurance every year.”

### Shared management

A third element to consider is the way the budget is managed. The financial management of the EU budget is shared between the European Commission (Commission) and Member States (MS) for most part of the budget (approximately 75%). The rest of the budget is managed by the Commission alone and to a small extent through international organisations like the World Bank, the United Nations and Red Cross.

There are a large number of beneficiaries receiving payments every year. For example over 7 million farmers receive support from the Common Agriculture Policy. Individually payments may be relatively small and focussing the audit on only the highest amounts paid would still leave out significant amounts not subject to the chance of being examined.

### Pyramid of assurance; is a fourth element missing?

Review of provided assurance on the shared part of management by external independent parties is a logic fourth element to consider. This is often used in the private sector, mainly within the structure of audit organisations. In its opinion No 2/2004<sup>3</sup> ECA set out objectives and conditions; and discussed structures, costs and benefits of a “single audit” model.

Progress has been made in this respect, however in ECA’s special report 16/2013<sup>4</sup> it is concluded that “However, the Court identified a number of risks in the Commission’s reliance on the error rates reported by audit authorities and the information on financial corrections reported by Member States. The Commission may therefore underestimate the problems in its reporting to the European Parliament and the Council and incorrectly assess what is needed to achieve an unqualified audit opinion in the Cohesion area.”

Also in an area where the Commission manages expenditure itself (direct management), the research policy area the Court included in its annual report 2012<sup>5</sup>: “8.26 For the cost statements audited by the Court for which a certificate had been provided (29 out of the 90 sampled transactions), the Court compared the results of its own audit with the conclusion of the independent auditor. In nine cases where the independent auditor had certified the cost statement, the Court found a significant level of error in the declared costs.

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<sup>3</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2004:107:0001:0020:EN:PDF>

<sup>4</sup> Special Report 16/2013: “Taking stock of ‘single audit’ and the Commission’s reliance on the work of national audit authorities in Cohesion”  
[http://www.eca.europa.eu/Lists/ECADocuments/SR13\\_16/SR13\\_16\\_EN.pdf](http://www.eca.europa.eu/Lists/ECADocuments/SR13_16/SR13_16_EN.pdf)

<sup>5</sup> Annual report on the implementation of the budget (2013/C 331/01)  
[http://www.eca.europa.eu/Lists/ECADocuments/AR12/AR12\\_EN.pdf](http://www.eca.europa.eu/Lists/ECADocuments/AR12/AR12_EN.pdf)

8.27. While certification of cost statements helps to reduce the level of error for the FPs<sup>6</sup> as a whole, the Court continues to find a significant level of error in cost statements certified by the independent auditor. This control procedure is partially effective.”

This point was taken up by the European Parliament in its discharge 2012 by including in its resolution: “that the Court still finds a significant error rate in the cost statements drawn up by independent auditors; considers, therefore, that the Commission and Member States should supply auditors with all the necessary background material and training material to facilitate correct auditing of cost statements; stresses that certified cost statements make sense only if the Commission can rely on them.”

#### Combining the elements

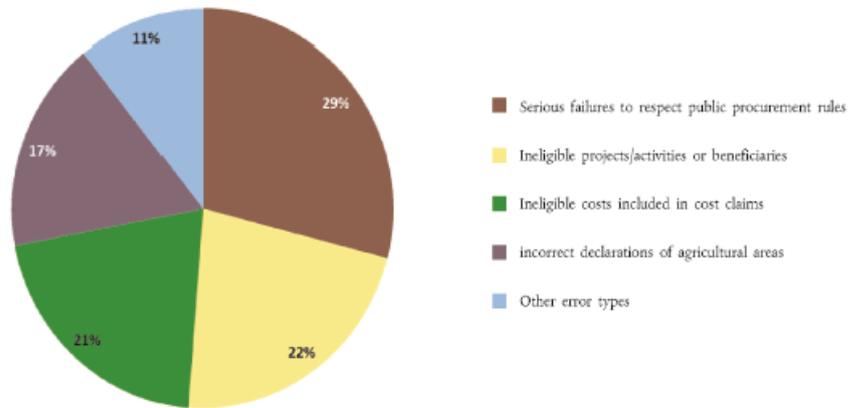
ECA provides a statement of assurance to the discharge authorities (Council and European Parliament) on the accounts and on the transactions underlying the accounts. The statement of assurance needs to cover the whole of the implementation of the budget, but does not necessarily have to be based on examination of all transactions. This would not be feasible, but still a representative view on the whole is wanted. For most expenditure assurance is obtained by substantive testing performed by the European Court of Auditors’ staff.

The transactions examined lead to observations that feed into the total, where all elements of operational expenditure contribute. There are categories of findings that contribute significantly, like the incorrect declaration of area in agriculture and serious failures to respect public procurement roles.

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<sup>6</sup> FP: frameworkprogrammes for research

Graph 1.2 — Contribution to overall estimated error by type



### Future outlook: 2014-2020

The new programming period 2014-2020 will provide further opportunities for a pyramid of assurance, with legality and regularity audits at Member State level for agriculture and structural funds.