

# Abstract

## **The European Union and the Flemish Community: an explanatory study**

### **Managerial message**

In its report about the European Union and the Flemish Community the Court of Audit sketched the relevant evolutions of institutions, budget and financial management in the UE. It examined the money flows from the European Union to the Member States in the form of structural funds. More particularly it drew up an inventory of the control and management of structural funds in Flanders.

The Court of Audit noted that in the past the draft EU regulations and directives were insufficiently submitted to the Flemish Parliament by the competent Flemish departments. The Flemish Government only provides the Flemish Parliament with six-monthly overviews of EU files that are especially relevant for Flanders.

European subsidies from the structural funds for Flemish projects are linked to co-financing by the Flemish authority. In their budget documents the Ministry, services with separate management and Flemish public bodies do not always mention Flemish subsidies as co-financing. Moreover the file follow-up systems set up in Flanders for structural funds do not provide centralized information about all amounts paid out for Flemish co-financing.

The Flemish circular letter about cash accounts and clearing accounts contributes very little to a transparent registration of European funds. The Flemish authority does not get a correct insight into European money flows by lack of a coordinating department. Reporting to the Flemish Parliament is neither comprehensive nor uniform.

The Court of Audit recommends that the Flemish authority should aim at more transparent registration of Flemish co-financing funds as well as European resources from structural funds. The Ministry, services with separate management and Flemish public bodies as well as the ESF Agency must strive for more transparency. The Flemish authority could uphold this aim by ordering a central inventory of all European structural funds. This in turn would make uniform reporting to the Flemish Parliament possible.

### **Summary**

#### *Evolutions of institutions, budget and financial management in the EU*

By joining the EU, Member States agree to transfer part of their sovereignty to independent bodies. The Flemish Parliament is empowered

to formulate advice about draft Commission regulations and directives to the Flemish Government. A procedure was set up to ensure a smooth submission of the proposals, enabling the concerned departments to submit the European Commission's proposals to the Flemish Parliament via their minister. But so far this procedure has almost never been implemented. Since 2005, however, the Flemish Government has provided the Flemish Parliament every six months with an overview of relevant EU-files.

The EU receipts and expenditure must be balanced. The ceiling of own resources indicates the maximum amount of funds the EU can use for its expenditure. The own resources maximum takes into account the financial perspectives, i.e. the expenditure limit within the budget. In 2005 and 2006 accounts will be for the first time rendered about an EU budget for twenty-five Member States.

One of the most striking current evolutions is the Treaty establishing a Constitution for Europe. Besides important provisions about EU decision making this Treaty contains a number of concrete obligations for the Member States, notably about avoiding excessive government deficits and combating fraud. The member States have a time limit of two years to agree to the Treaty. It will only come into force when it has been ratified by all EU Member States, otherwise the issue will be examined by the European Council.

Several forums within the EU are discussing the collaboration between institutions responsible for managing and controlling EU funds. The European Commission is in charge of defining how funds received by the Member States are to be managed and controlled. Whenever money flows are managed jointly – that is: when the Commission and the Member States are collectively responsible for implementing the policy – the Commission mostly leaves the responsibility to the Member States. The European Commission carries out its own internal controls. Subsequently the European Court of Auditors performs an independent external control. In addition, the national audit institutions of the Member States can also (in most cases) carry out independent checks of EU funds spending.

#### *European structural funds*

There are still significant social and economic disparities between regions within the EU. In order to improve cohesion, the European Commission created structural funds: the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Guidance Section of the European Agricultural Guidance and Guarantee Fund (EAGGF) and the Financial Instrument for Fisheries Guidance (FIFG). These funds require additional financing from the Member States and cooperation between the Commission and the national authorities. The measures are initiated by the Member States. In order to make the structural measures efficient the structural funds regulation for the period 2000-2006 address three priority intervention objectives:

- Objective 1 aims to promote the development and structural adjustment of regions whose development is lagging behind. As in the previous period two thirds of all structural measures are related to this objective.
- Objective 2 aims to support the economic and social conversion of areas facing structural difficulties.
- Objective 3 refers to all actions aimed at developing human resources.

Besides, the European Union has also set up four special programmes, the so-called Community Initiatives, in order to find global solutions to problems that arise everywhere in Europe. Unlike the above mentioned structural measures, the Community programmes are not initiated by the Member States, but by the European Commission itself. Every initiative is financed by one of the funds. The following initiatives were developed in the period 2000-2006: INTERREG III, LEADER+, EQUAL and URBAN II.

Financial aid from structural funds amounted to approximately 195 billion EUR in the period 2000-2006, of which 69,7% was allocated to Objective 1, 11,5% to Objective 2, 12,3% to Objective 3, 0,5% for FIG outside Objective 1, 5,35% to Community Initiatives and 0,65% to innovative actions and technical support.

The Commission must obtain assurance that Member States have smoothly functioning management and control systems aimed at auditing programmes that benefit from European funding through the structural funds. The managing authority must account for the efficiency and regularity of the management and implementation of the programme. A paying agency that operates independently is responsible for drawing up and submitting the payment requests and for receiving payments from the Commission. Finally a monitoring committee must satisfy itself as to the effectiveness and quality of the structural measures. The Commission itself checks the efficiency of the control regulations that are set up by managing authorities and payment agencies.

In 2003 the European Court of Auditors examined the functioning of monitoring and control systems both at the Commission and in the Member States. It found weaknesses as regards compliance with regulations on assignment and separation of functions, management checks and external control and certification of expenditure. According to the Court of Auditors the Commission must use its powers to suspend payments to programmes whose systems show serious weaknesses.

For single or systematic irregularities the Member States must apply financial corrections by withdrawing part or whole of the Community contribution. Financial corrections do not entail a reduction of the support to the programme concerned, as the amounts can be allocated to other operations. If the Member States do not comply, the Commission can withdraw its contribution from the structural funds.

Whenever the Commission implements the budget in shared management, budgetary implementation is delegated to the Member States. However, the European Court of Auditors has already found for several years in its audit of the DAS statement that there are frequent errors in the underlying transactions, mainly in cases of shared management. In the regulations it is drawing up for the next programme period the European Commission intends to provide a clear definition of the framework and the respective responsibilities of the Member States and the Commission in matters of budgetary implementation.

### *European structural funds in Flanders*

Three structural funds are active in Flanders: ESF, ERDF and FIG. ERDF subsidizes development initiatives in areas facing structural difficulties. ESF aims at contributing to an optimal human-resource development. FIG concentrates on projects in the fisheries and aquiculture sector.

The granting of aid is linked to the three priority objectives. Areas that previously received aid, but are no longer eligible qualify for support received on a transitional basis (*phasing out*). In Flanders four regions qualify for assistance under Objective 2 programmes: Limburg, Antwerp, Coast and East-Flanders. European funding under these programmes mostly comes from ERDF. ESF participates in all Objective 2 programmes except that of East-Flanders. Every programme also includes a phasing-out part. These transitory provisions never include ESF aid. The Flemish Objective 3 programme is focused on a number of priorities, which correspond to the four strategic aims of the European employment strategy. This programme targets the whole of Flanders.

With a view to efficient management of ESF programmes in Flanders the ESF Agency was set up as a temporary statutory non-profit organization. The agency is currently steering a middle course between two statutes: non-profit organization and body governed by public law. As a consequence it is not submitted to all obligations regarding public bodies (e.g. checks by the controller of commitment appropriations or the Court of Audit).

The Ministry of the Flemish Community (section EWBL) acts as managing authority for all Flemish Objective 2 programmes. The Economy department and the ESF Agency act respectively as paying authorities for ERDF and ESF. For each programme a monitoring committee has been set up, which is in charge of the general strategy and global monitoring and a management committee is responsible for allocating European aid to concrete individual projects on the basis of predetermined, objective selection criteria. The European Commission found in its annual report on structural funds 2003 that the four programmes under Objective 2 in the Flemish Region have now reached cruising speed and have a satisfactory evolution.

For all Flemish programmes under Objective 3 the ESF Agency acts as managing and paying authority, with separation of functions and one

coordinator for each authority. The Flemish monitoring committee (VMC) controls the overall strategic aspects of ESF under Objective 3. For each priority the VMC has set up strategic task forces. In its annual report the European Commission found that the implementation of the different priorities under Objective 3 is satisfactory.

The FIG annual report 2003 provides for two managing authorities for Flanders: the Agriculture and Horticulture Support Policy Department of the Agriculture and Horticulture Administration and the Agriculture and Fisheries Policy Department in Ostend. On 30 June 2004 the Agriculture and Fisheries Policy Department informed the European Commission that it would stop acting as managing authority. The paying agency is Agriculture and Fisheries Policy Department of EWBL. The implementation of the programme is monitored by a monitoring committee. In its annual report the European Commission describes the overall implementation process of FIG in Europe as rather slow.

As several bodies are involved in the audit of structural funds, coordination of the audit activities is of uttermost importance. Under the regulation on the structural funds the Commission and the Member States shall coordinate their checks on the basis of bilateral administrative arrangements. The Court of Audit noticed that such a regulation still does not exist in Flanders.

Control of structural funds programmes at the Flemish level is carried out in four steps. The managing authority's foremost task is to check the submitted expenditure and the concrete realisation of individual projects. This first step includes checks of sample transactions. The second step is the so-called 5%-control: before each programme is wound up, an independent body must have checked at least 5% of the total amount of expenditure eligible for EU funding. The Flemish Region has outsourced the sample checks of Objective 2 programmes under ERDF to an external private audit firm. In the future it would be well-advised to mention in the specifications that the Inspection of Finances, the Internal Audit, the Court of Audit, every EU control body and the European Court of Auditors are entitled to inspect the working papers of the appointed external private audit firm. The social legislation inspectors of the Employment Department are responsible for sample checks regarding the ESF funds. The cell Inspection and Audit of the Agriculture and Horticulture Administration carries out the 5%-controls for FIG. The Internal Audit of the Ministry of The Flemish Community is in charge of the third step of the control. The intention is to perform annual system audits – spread over the whole programme period - for ESF, ERDF and FIG and to draw up a report for each of them, with a follow-up in the next year. Finally, the fourth step is entrusted to the Inspection of Finances, which draws up the closure statement of the assistance package.

The European Commission and the European Court of Auditors control the structural funds at the European level. The services of the European Commission examined which systems the Flemish Community had set up to manage the funds. The European Court of Auditors' checks were related to the Statement of Assurance (DAS).

The Belgian Court of Audit examined in how far Flemish subsidies for structural funds programmes were mentioned as co-financing in the budgetary documents of the Ministry of the Flemish Region, the services with separate management and the Flemish public bodies. It showed that the heading 'co-financing' did not always appear clearly in the definitions of budget items. The file monitoring systems set up by the Flemish Economy department and the ESF Agency are also unable to provide centralized information about all amounts paid out for co-financing in Flanders.

The Ministry and the services with separate management do not have at their disposal unambiguous regulations for the registration of European funds. The Flemish circular letter about cash and clearing accounts does not provide for a specific subheading for clearing accounts of European funds.

The Court of Audit received from the Foreign Policy within Europe section of the Ministry the results of an enquiry into the volume of European money flows in Flanders. However, these results were limited to indicative data gathered on a one-time basis. At the EWBL department and the ESF Agency the Court of Audit was only able to retrieve unchecked figures about the structural funds, because the Flemish regulations related to the registration of European funds are still insufficiently transparent. The Court of Audit came to the conclusion that Flemish policy makers still have no correct insight into all European flows of money that are transferred to the Flemish authority.

At the moment reporting to the Flemish Parliament regarding all European structural funds in Flanders is only fragmentary and lacks uniformity. As far as ESF is concerned the ESF Agency draws up an annual report including an evaluation report and the Agriculture and Horticulture department's annual report includes an appendix devoted to European assistance under FIGG. There is no reporting to the Flemish Parliament about ERDF matters.

## **Conclusions**

The Flemish Parliament is empowered to formulate advice for the Flemish Government about draft EU regulations and directives (Article 92 quater of the special 8 August 1980 law on devolution). On 9 July 1996 the Flemish Government approved the further developed procedures for submission of the draft documents to the Flemish Parliament. But so far this procedure has almost never been implemented. Since 2005, however, the Flemish Government has provided the Flemish Parliament every six months with an overview of relevant EU-files.

The ESF Agency, which is responsible for the general management of all Flemish ESF programmes, was set up as a temporary statutory non-profit organization as long as reforms under the Scheme for Improvement of Administrative Management are not implemented. On the one hand it is submitted to the legislation on non-profit organizations and under its provisions it has to establish an annual report and have its accounts

checked by a company auditor. On the other hand, it does not have to submit its budget nor its accounts to the Flemish authority. Although it is a statutory organization and gets subsidies, among others for co-financing, from the general expenditure budget of the Flemish Community, the Agency as a non-profit organization is not subject to the control of the controller of commitment appropriations or of the Court of Audit. So far no management agreement has been set up, although it is required under article 4 of the organic decree. Every year the Agency, however, draws up an evaluation report which is submitted to the competent minister and the Flemish Parliament.

Article 38, paragraph 3, of the Council Regulation laying down general provisions on the Structural Funds provides the legal basis for cooperation and coordination of plans, methods and implementation of checks. Still, there is as yet no bilateral administrative law provisions agreed upon between the European Commission and the controlling bodies of the Flemish Community.

The Flemish Region decided to outsource the 5%-sample checks of Objective 2 programmes. However, the specifications do not mention that the Inspection of Finances, the Internal Audit, the Court of Audit, every EU control body and the European Court of Auditors are entitled to inspect the working papers of the appointed external private audit firm.

Budget items of the Ministry of the Flemish Region, the services with separate management and the Flemish public bodies do not always explicitly mention the heading '*co-financing by the Flemish community*' in the description of subsidies granted by the Flemish authority to projects receiving European monies from the structural funds.

The Economy department and the ESF Agency, which manage respectively the European and Flemish funds within ERDF and ESF were not always able to produce centralized detailed information about the budget items related to co-financing by the Ministry of the Flemish Community, the services with separate management and the Flemish public bodies. The file monitoring systems for structural funds do not contain information split up by project about the amounts paid out for Flemish co-financing nor any identification of budget item for each payment.

In accordance with the prevailing budget regulations, the budget departments of the Ministry of the Flemish Region and the services with separate management do not register European funds in the budget, but in clearing accounts. A Flemish circular letter describes the different types of funds from third parties, including the European funds, but does not recommend the use of a specific subheading for clearing accounts for European funds. The current procedure makes instant reporting about all European funds more complicated.

By lack of an inventory the Flemish authority hasn't got a correct insight into all European flows of money that are transferred to it.

At the moment reporting to the Flemish Parliament about projects getting assistance from European structural funds is only fragmentary and lacks uniformity.

### Recommendations

- The Flemish Government should ensure that EU draft regulations and directives are submitted to the Flemish Parliament, such as provided in article 92 quater, of the 8 August 1980 special law on devolution, following the procedure adopted by the Government on 9 July 1996.
- The Flemish Government must re-examine the statute of the ESF Agency and maybe consider the integration of other Flemish bodies also dealing with European matters, such as the Flemish non profit organization Leonardo da Vinci Agency. Moreover the ESF Agency should be checked by the controller of commitment appropriations and by the Court of Audit. According to article 4 of its organic decree, a management agreement is also compulsory.
- It is advisable for Flanders to take the initiative of entering into a bilateral administrative law arrangement on audits with the European Commission, in accordance with the structural funds regulation.
- If the 5%-sample checks are outsourced, it should be mentioned in the specifications that the Inspection of Finances, which draws up the closure statement of the assistance package, the Internal Audit, the Court of Audit, every EU control and audit body and the European Court of Auditors are entitled to inspect the working papers of the appointed external private audit firm.
- In order to make budget documents more transparent? the next budget instructions of the Flemish Finance and Budget Minister should clearly mention the heading 'co-financing' in the definition of budget items of the Ministry of the Flemish Region, the services with separate management, the Flemish public bodies and the Agencies created under the Scheme for Improvement of Administrative Management.
- As the European Commission requires co-financing as a condition for granting European subsidies, the file monitoring systems of the three structural funds should include for each project every amount paid out for co-financing and the corresponding budget item identification of the different budget departments of the Flemish Community. This is the only way to ensure transparent reporting for each structural funds programme.
- The description of clearing accounts by the budget departments of the Ministry of the Flemish Region and the services with separate management must be structured in such a way that all European funds from third parties can be identified, e.g. by using a specific subheading for European funds. It is therefore also recommended to adapt the Flemish circular letter on cash and clearing accounts accordingly. Only this adaptation will enable the Flemish authority to

make an instant inventory of all European funds from third parties that would take into account new or suppressed clearing accounts.

- The Flemish Community should set up a central inventory of all European money flows that are transferred to the Flemish authority and define them in an unambiguous and uniform way. This central inventory of European funds must be supported by appropriate accounting methods. In a first phase information can be collected about money flows regarding European structural funds.
- The Court of Audit advocates annual, exhaustive and uniform reporting by the Flemish Government to the Flemish Parliament about all structural funds and Community Initiatives

### **Minister's response**

The minister for Foreign Policy replied to the Court of Audit's provisional report on 3rd October 2005. He valued the conclusions and recommendations and was willing to implement some of them immediately. However, he had objections against implementing some of the Court's other recommendations.