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COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT

PROTECTION OF THE EUROPEAN UNION BUDGET TO END 2012

{SWD(2013) 404 final/2}

Table of Contents

1. OBJECTIVE, SCOPE AND CONCLUSION

This Communication on the protection of the European Union Budget has been requested by the European Parliament in the context of the 2011 discharge procedure[1] and is therefore addressed to this institution, as well as to the Council and the European Court of Auditors (ECA). It should be read in conjunction with the figures disclosed in Note 6 of the 2012 EU annual accounts.

The objective of this Communication is to provide:

(1) an overview of the mechanisms foreseen in the legislation which define the process of identifying and then dealing with administrative errors, irregularities and suspected fraud[2] detected by EU bodies and by Member States; and

(2) a best estimate of the total amounts[3] concerned for 2012 and cumulative so as to illustrate in real terms how:

   a. the EU budget is protected from expenditure incurred in breach of law, and
   b. the Member States are involved and impacted.

In addition to the above, information is also provided on amounts recovered relating to advances (pre-financing) paid out that have not been used by the beneficiary. Furthermore, information is given on the additional corrections reported as effected by Member States under Cohesion policy following their own controls and audits, for the programming period 2007-2013.

More detailed information on the stages and forms of preventive and corrective measures, as well as the financial impact on the EU and/or national budgets, under the different policy areas and implementation methods, is given in the Commission Staff Working Document ("SWD") accompanying this Communication.

The importance of financial corrections and recoveries is particularly highlighted when considering multi-annual residual error rates. This is because these rates take into account both detected error rates and financial corrections and recoveries over the entire life cycle of programmes and projects. Therefore, they indicate the real impact of irregular expenditure and represent key indicators for assessing how supervisory and control systems manage the risks relating to the legality and regularity of operations financed by the EU budget.

The figures presented in this Communication demonstrate that the result of the multi-annual preventive and corrective activities undertaken by the Commission is that the EU budget is adequately protected from expenditure incurred in breach of applicable law.

[1] European Parliament resolution of 17 April 2013 with observations forming an integral part of its Decisions on discharge in respect of the implementation of the general budget of the European Union for the financial year 2011, Section III – Commission and executive agencies (COM(2012)0436 – C7-0224/2012 – 2012/2167(DEC)) – Priority Action 1.

[2] See also the 2012 Annual Report on the Protection of the European Union's financial interests — Fight against fraud which has been adopted on 24 July 2013.

[3] Due to the rounding of figures into millions of Euros, amounts in some tables may appear not to add up.

2. LEGISLATION ON THE PROTECTION OF THE EU BUDGET

The obligation of both the Commission and the Member States to manage adequately the risks relating to the legality and regularity of operations financed by the EU Budget is laid down in the Treaty on the Functioning of the European Union (TFEU[4][5]), which states that:

> **Article 317:**
>
> The Commission shall implement the budget in cooperation with the Member States in accordance with the provisions of the regulations made pursuant to Article 322, on its own responsibility and within the limits of the appropriations, having regard to the principles of sound financial management. Member States shall cooperate with the Commission to ensure that appropriations are used in accordance with the principles of sound financial management.
>
> The regulations shall lay down the control and audit obligations of the Member States in the implementation of the budget and the resulting responsibilities. They shall also lay down the responsibilities and detailed rules for each Institution concerning its part in effecting its own expenditure.
>
> ...

According to the Financial Regulation[6], its rules of application[7] and the various sector-specific regulations, the Commission protects the EU budget, i.e. EU spending, from undue or irregular expenditure via two main methods:

(1) preventive actions; and
(2) correction mechanisms (primarily financial corrections imposed on Member States and, to a lesser extent, recoveries from recipients of EU payments).

It is stressed that the primary objective of financial corrections is to ensure that EU funds are used correctly and for the purposes for which they were given. This is why, for example, under the legislation in force for Cohesion Policy, detected irregular expenditure must always be excluded, often by being replaced by regular spending at Member State level. However, recoveries (and financial corrections related to the Common Agricultural Policy ("CAP")) result in the return of previously paid irregular amounts to the EU Budget.

In accordance with Article 32 of the Financial Regulation, covering the internal control on budget implementation, the Commission, and Member States for shared management (see section **3.1**), have to respect the following principles:

[4] See Official Journal C 115 of 9 May 2008.
[5] See also Article 325 of the TFEU, which states that:
"1. The Union and the Member States shall counter fraud and any other illegal activities affecting the financial interests of the Union through measures to be taken in accordance with this Article, which shall act as a deterrent and be such as to afford **effective protection** in the Member States, and in all the Union's institutions, bodies, offices and agencies.
2. Member States shall take the same measures to counter fraud affecting the financial interests of the Union as they take to counter fraud affecting their own financial interests.
...
5. The Commission, in cooperation with Member States, shall each year submit to the European Parliament and to the Council a report on the measures taken for the implementation of this Article."
[6] Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 (Official Journal L 298, 26 October 2012).
[7] Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 (Official Journal L 362, 31 December 2012).

Article 32 – Internal control on budget implementation

1. The budget shall be implemented in compliance with effective and efficient internal control as appropriate in each method of implementation, and in accordance with the relevant sector-specific rules.

2. For the purposes of the implementation of the budget, internal control is defined as a process applicable at all levels of management and designed to provide reasonable assurance of achieving the following objectives:
(a) effectiveness, efficiency and economy of operations;
(b) reliability of reporting;
(c) safeguarding of assets and information;
(d) ***prevention, detection, correction and follow-up of fraud and irregularities***;
(e) adequate management of the risks relating to the legality and regularity of the underlying transactions, ***taking into account the multiannual character of programmes*** as well as the nature of the payments concerned.
...

Article 80 of the same regulation goes on to say:

Article 80 – Rules on recovery

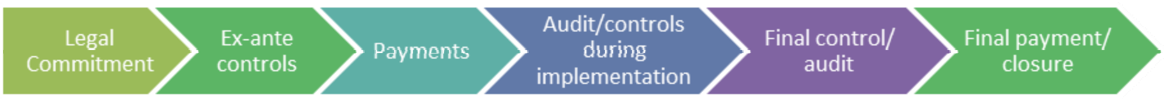
...
3. **The Member States shall in the first instance be responsible for carrying out controls and audits and for recovering amounts unduly spent**, as provided for in the sector-specific rules. To the extent that Member States detect and correct irregularities on their own account, they shall be exempt from financial corrections by the Commission concerning those irregularities.

4. **The Commission shall make financial corrections on Member States in order to exclude from Union financing expenditure incurred in breach of applicable law**. The Commission shall base its financial corrections on the identification of amounts unduly spent, and the financial implications for the budget. Where such amounts cannot be identified precisely, the Commission may apply extrapolated or flat-rate corrections in accordance with the sector-specific rules.
The Commission shall, when deciding on the amount of a financial correction, take account of the nature and gravity of the breach of applicable law and the financial implications for the budget, including the case of deficiencies in management and control systems.
The criteria for establishing financial corrections and the procedure to be applied may be laid down in the sector-specific rules.

5. The methodology for applying extrapolated or flat-rate corrections shall be laid down in accordance with the sector specific rules with a view to enabling the Commission to protect the financial interests of the Union.

It is also important to underline that for a significant portion of EU expenditure, e.g. Cohesion and Research policies, the programmes concerned are of a multi-annual nature and, as highlighted above in Article 32 (e) of the Financial Regulation, this must be taken into account when designing and implementing preventive and corrective measures, as well as when assessing the results of these actions.

The life-cycle of an EU funded project/programme could be viewed as follows:

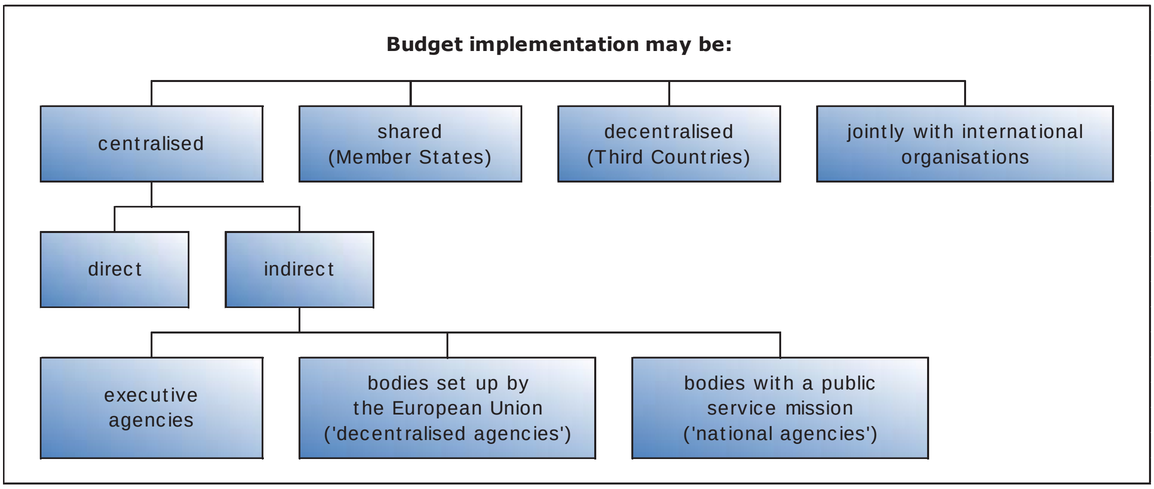


Financial corrections and recoveries can be made at any stage once expenditure has been incurred and/or a payment has been made. Nonetheless the majority of corrections tend to occur at the closure of the project/programme, which can be years after the first expenditure has been incurred and/or first payment was made.

3. METHODS OF IMPLEMENTING AND CONTROLLING THE EU BUDGET

Preventive actions and responsibilities depend on the method of implementation of the EU budget[8]. This also impacts how and when corrective actions are implemented. Furthermore, when setting up such procedures and controls, the Commission is bound by Article 32 (4g) of the Financial Regulation to take into consideration efficiency and, in particular, "improving the cost-benefit ratio of controls".

In summary, the 2012 EU budget was implemented via the following methods[9]:



3.1. Shared Management

Under shared management (i.e. Agriculture and Cohesion policy expenditure), which accounts for around 80% of the annual EU Budget, the Commission relies on Member States for the implementation of EU programmes, i.e. the EU contribution is paid, following receipt of payment applications, to national certifying and management authorities or payment agencies, who are then responsible for the payments made to final beneficiaries. As a result, ***Member States are primarily responsible for the prevention, detection and correction of errors and irregularities committed by the beneficiaries, while the European Commission ensures an overall supervisory role*** (i.e. verifying the effective functioning of Member States' management and control systems and applying financial corrections where necessary) – see Article 59 of the Financial Regulation below[10]:

Article 59 - Shared management with Member States

1. Where the Commission implements the budget under shared management, implementation tasks shall be delegated to Member States. The Commission and the Member States shall respect the principles of sound financial management, transparency and non-discrimination and shall ensure the visibility of Union action when they manage Union funds. To this end, the Commission and the Member States shall fulfil their respective control and audit obligations and assume the resulting responsibilities laid down in this Regulation. Complementary provisions shall be laid down in sector-specific rules.

[8] It is noted that the Commission's Anti-Fraud Strategy adopted in June 2011 led, with OLAF's involvement and support, to important progress in the field of fraud prevention and detection.
[9] The methods of implementing the EU budget have been adapted following the adoption of the new Financial Regulation and the new methods will come into force in 2014.
[10] The clear responsibility for Member States to make controls and to recover monies from beneficiaries is also laid down in Article 80 of the Financial Regulation, as quoted earlier.

2. When executing tasks relating to the implementation of the budget, **Member States shall take all the necessary measures**, including legislative, regulatory and administrative measures, **to protect the Union's financial interests**, namely by:

(a) ensuring that actions financed from the budget are implemented correctly and effectively and in accordance with the applicable sector-specific rules and, for that purpose, designating in accordance with paragraph 3, and supervising bodies responsible for the management and control of Union funds;
(b) **preventing, detecting and correcting irregularities and fraud**.

In order to protect the Union's financial interests, Member States shall, respecting the principle of proportionality, and in compliance with this Article, and the relevant sector-specific rules, carry out ex-ante and ex-post controls including, where appropriate, on-the-spot checks on representative and/or risk-based samples of transactions. **They shall also recover funds unduly paid and bring legal proceedings where necessary in this regard**.
...

Under shared management, preventive measures used vary, as explained in more detail in the SWD. For example, Member States have the legal obligation to set up management and control systems. Another example, for Cohesion spending and in the future for CAP, is where serious failings in the management and control systems have led or could lead to individual or systemic irregularities, the Commission can interrupt or suspend payments. Other measures include guidance and training to support Member States.

Regarding corrective measures, system weaknesses, errors, irregularities and fraud are addressed by the Commission itself almost exclusively by means of what is known as a financial correction procedure, with recoveries used in limited cases. The results of these Commission corrective actions are summarised below (see also sections **4, 5 & 6**), with more details given in the SWD.

It must be highlighted that the primary responsibility of the Commission in implementing to EU budget is to protect the Union's financial interests, or in other words, to protect the EU budget from irregular expenditure. In the context of shared management, this has two important consequences:

(1) While the Commission applies financial corrections (as well as interruptions and suspensions) linked to Member State system weaknesses, it remains the Member States' responsibility to react to these measures and make improvements in their systems; and
(2) The protection of the national budgets, in particular by recovering amounts from final beneficiaries, remains the responsibility of the Member States. It is, however, underlined that financial corrections do not relieve the Member States from the obligation to recover the undue payments from the beneficiaries whenever it is feasible and cost-effective.

Even if the Member States do not recover irregular expenditure from the final beneficiary, the effective deduction of the irregular expenditure either by the Member States or by the Commission ensures that the EU budget is protected. As a result, expenditure incurred in breach of law is no longer funded by the EU budget.

3.2. Other methods of budget implementation

The European Commission also implements policies under other management modes, as shown above. In these areas, representing approximately 20% of the annual EU budget, the key preventive actions to highlight include the Commission's internal control system, as well as support and guidance to beneficiaries, staff training and eligibility assessments. The processes are explained in more detail in the SWD.

Corrective actions are made via the actual recovery of unduly paid amounts, executed by recovery order or offsetting with a subsequent payment to the beneficiary – see Articles 78 and 80 of the Financial Regulation, as well as the SWD.

Article 78 – Establishment of amounts receivable

1. The establishment of an amount receivable is the act by which the authorising officer responsible:

(a) verifies that the debt exists;
(b) determines or verifies the reality and the amount of the debt;
(c) verifies the conditions according to which the debt is due.

2. ...

3. **Amounts wrongly paid shall be recovered.**
...

Article 80 – Rules on recovery

1. **The accounting officer shall act on recovery orders for amounts receivable duly established by the authorising officer responsible**. The accounting officer shall exercise due diligence to ensure that the Union receives its revenue and shall ensure that the Union's rights are safeguarded.
The accounting officer shall recover amounts by offsetting them against equivalent claims that the Union has on any debtor who in turn has a claim on the Union. Such claims shall be certain, of a fixed amount and due.
...

4. FINANCIAL CORRECTIONS AND RECOVERIES IMPLEMENTED[11] IN 2012

Financial corrections and recoveries are primarily dependent on the level of irregularities of previous years, i.e. if weaknesses/ deficiencies observed increase, it is the Commission's obligation to ensure that the corresponding financial corrections and recoveries are made. But given the multi-annual character of the control framework and the complexity of the corrective mechanisms and procedures, this can only happen over time. Sections **6.2.3** and **6.2.4** give an idea of the impact of the corrective measures over a longer period: for Agriculture (EAGF) (1.5% of all payments for the period 1999-2012 covering all clearance of accounts decisions) and for ERDF and ESF (4% of all payments for the programming period 2000-2006 which is in the closure stage).

However, looking exclusively at 2012, and in order to give an idea of the amplitude of the financial corrections and recoveries implemented in 2012, it is noted that the amounts, while mostly relating to irregularities of past years, represent in financial terms 3.2% of all 2012 budget payments.

Table 4: Financial corrections and recoveries implemented in 2012

EUR millions

	2012 EU budget payments	Financial Corrections	Recoveries	2012 Total	% of payments of the EU budget
Agriculture:					
EAGF[12]	44 551	610	161	**771**	*1.7%*
Rural Development	13 123	59	166	**225**	*1.7%*
Cohesion Policy*:					
ERDF	27 457	2 416	N/A	**2 416**	*8.8%*
Cohesion Fund	9 626	207	N/A	**207**	*2.2%*
ESF	11 295	430	N/A	**430**	*3.8%*
*FIFG/EFF***	481	1	N/A	**1**	*0.2%*
*EAGGF Guidance***	138	17	3	**20**	*14.5%*
Other	106	N/A	11	**11**	*10.4%*
Sub-total	*106 777*	*3 741*	*341*	***4 081***	*3.8%*
Internal policy areas	16 278	1	229	**230**	*1.4%*
External policy areas	7 064	N/A	99	**99**	*1.4%*
Administration	8 564	N/A	9	**9**	*0.1%*
Total	**138 683**	**3 742**	**678**	**4 419**	***3.2%***

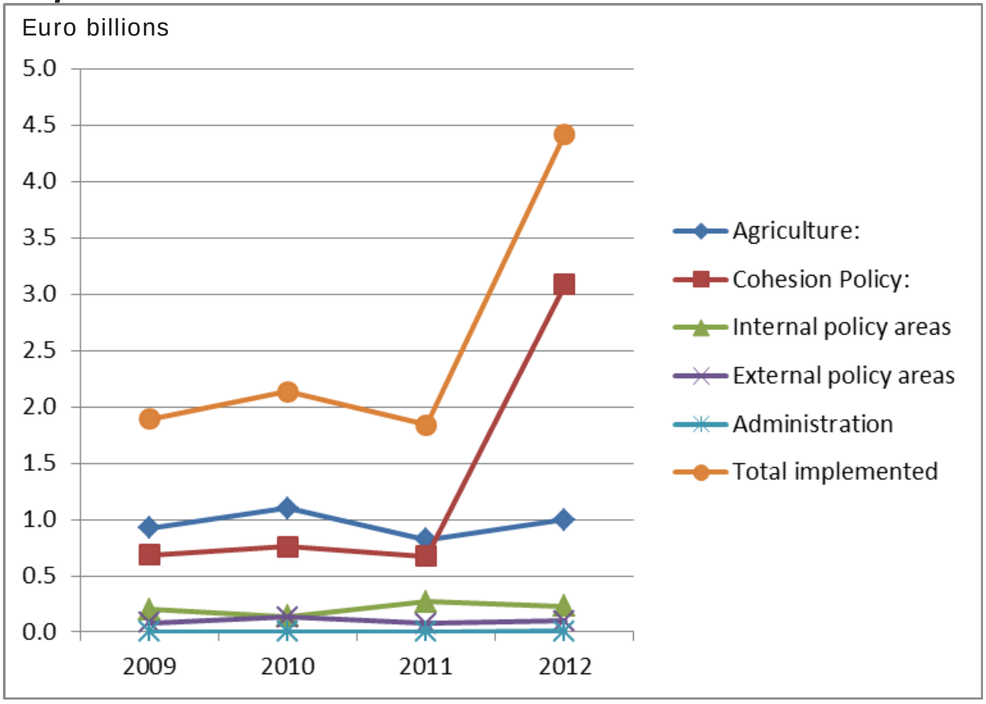
* Implemented financial corrections under Cohesion policy also include recovery orders issued by the Commission
** FIFG/EFF and EAGGF Guidance belong to Cohesion policy only for the programming period 2000-2006 and before

[11] As explained in more detail in the SWD, implementation is the last step in the financial correction or recovery process. Implementation means that for a financial correction or recovery that has been previously detected and then decided/agreed upon, the observed situation of undue expenditure is definitively corrected.
[12] EAGF amounts executed under shared management total EUR 44 495 million.

5. CUMULATIVE FINANCIAL CORRECTIONS AND RECOVERIES TO END 2012

Cumulative figures provide information on the significance and the real impact of the corrective mechanisms used by the Commission taking into account the multi-annual character of programmes and projects. The graph below shows the evolution of financial corrections and recoveries implemented during the last 4 years:

Graph 5: Financial corrections and recoveries 2009-2012



The average amount of financial corrections and recoveries implemented per year by the Commission during the period 2009 to 2012 was **EUR 2.6 billion** or 2% of the average amount of payments from the EU budget of EUR 127.2 billion (shared management: EUR 2.3 billion or 2.3% of the average amount of payments (EUR 97.2 billion)). 2012 amounts were significantly higher due to cohesion corrections relating to the closure of the 2000-2006 programmes for one Member State, Spain, and a quicker implementation of financial corrections for current programmes. The table shows the cumulative financial corrections implemented to end 2012:

Table 5.1 Cumulative financial corrections implemented to end 2012

EUR millions

	Implemented to end 2012					Total decided at end 2012	% Implemented
	Programming Period			Cumulated annual amounts	Total		
	1994-1999 Period	2000-2006 Period	2007-2013 Period				
Agriculture:	**-**	**93**	**81**	**7 728**	**7 902**	**8 525**	**92.7%**
EAGF	-	-	-	7 728	7 728	8 286	93.3%
Rural Development	-	93	81	-	174	239	72.8%
Cohesion Policy:	**2 535**	**6 359**	**779**	**-**	**9 673**	**10 787**	**89.7%**
ERDF	1 764	4 626	154	-	6 544	7 305	89.6%
Cohesion Fund	264	464	87	-	815	984	82.8%
ESF	407	1 206	538	-	2 150	2 224	96.7%
FIFG/EFF	100	5	0	-	105	201	52.2%
EAGGF Guidance	0	58	-	-	58	72	80.6%
Other	**-**	**-**	**-**	**2**	**2**	**2**	**100%**
Total	**2 535**	**6 452**	**861**	**7 730**	**17 577**	**19 313**	**91.0%**

The different programming periods in the cohesion policy clearly show the multi-annual nature of the EU budget cycle. Since the 2000-2006 period is approaching the end of its closure process, the amount of financial corrections is considerably higher than for the 2007-2013 period. Financial corrections for this period will of course increase in the next years as its programmes start to close. The situation of cumulative financial corrections per Member States for Agriculture (EAGF) for all decisions taken up to 2012 and for Cohesion for the programming period 2000-2006 is shown in section **6.2**.

The table below shows the breakdown of recoveries per year for the period 2009-2012:

Table 5.2 Recoveries implemented 2009-2012

EUR millions

Recoveries	**Years**				**Total as at end 2012**	**Still to be recovered**
	2009	**2010**	**2011**	**2012**		
Agriculture:						
EAGF	148	172	178	161	659	50
Rural Development	25	114	161	166	466	0
Cohesion	102	25	48	14	189	9
Internal policy areas	100	162	268	229	759	50
External policy areas	81	136	77	99	393	38
Administration	9	5	2	9	25	4
Total	**464**	**614**	**734**	**678**	**2 491**	**151**

6. IMPACT OF FINANCIAL CORRECTIONS AND RECOVERIES ON THE EU BUDGET AND ON NATIONAL BUDGETS

6.1. Impact on the EU Budget

The budget implementation type and the policy area influence how the EU budget is impacted by the different correction mechanisms, but in all cases, the correction mechanisms ensure that the EU budget funds only regular and eligible expenditure. In some cases, notably under the CAP, the corrective action leads to the return of previously paid amounts to the EU budget. However, for other policy areas, many financial corrections do not result in reimbursements to the EU budget because, in line with the legislation, the corrected amounts can be re-used to fund other eligible projects[13].

Table 6.1 Impact of financial corrections & recoveries on the EU Budget

Policy domain	Total amount implemented in 2012 (in EUR millions)	Exclusion of expenditure incurred in breach of law (Yes/No)	Reimbursement to EU budget (Yes/No)
Agriculture:			
EAGF financial corrections	610	Y	Y
EAGF recoveries	161	Y	Y
Rural development financial corrections	59	Y	Y
Rural development recoveries	166	Y	N*
Cohesion Policy			
Financial corrections implemented by withdrawals	738	Y	N
Financial corrections implemented by recoveries	49	Y	Y
Financial corrections implemented by decommitment/ deduction at closure	2 284	Y	N*
Recoveries	14	Y	Y
Other policy areas			
Financial corrections implemented by decommitment/ deduction at closure	1	Y	N*
Financial corrections implemented by recoveries	0	Y	Y
Recoveries	337	Y	Y
TOTAL	**4 419**		

* Under the current legal framework, financial corrections can lead to reduction in expenses/envelope only:
- If Member States are unable to present sufficient eligible expenditure;
- After the closure of programmes where replacement of expenditure is no longer possible;
- In case of disagreement with the Commission.

[13] For example, for the implementation mechanism of financial corrections for cohesion policy see explanations provided in the accompanying SWD, section **4.2.1**.

6.2. Impact on national budgets

6.2.1 Introduction

Under shared management, all financial corrections and recoveries have an impact on national budgets regardless of their method of implementation. It has to be underlined that even if no reimbursement to the EU budget is made, the impact of financial corrections is always negative at Member State's level. In order not to lose EU funding, the Member State must replace ineligible expenditure by eligible operations. That means that the Member State bears with own resources (from the national budget) the financial consequences of the loss of EU co-financing of the expenditure considered ineligible, unless it recovers the amounts from individual beneficiaries. This is not always possible, for example in the case of flat rate corrections at programme level (due to deficiencies in the national administration managing the programme) which are not linked to individual irregularities at project level. However, those flat rate corrections do protect adequately the EU Budget.

The impact of these financial corrections both for the current year (2012) and cumulatively (per Member State for Agriculture (EAGF) and for the programming period 2000-2006 for ERDF & ESF) is shown below.

6.2.2 Financial corrections implemented per Member State in 2012

A breakdown of the financial corrections implemented per Member State for the different shared management areas is shown in the table below:

Table 6.2.2: Shared management financial corrections implemented per Member State in 2012

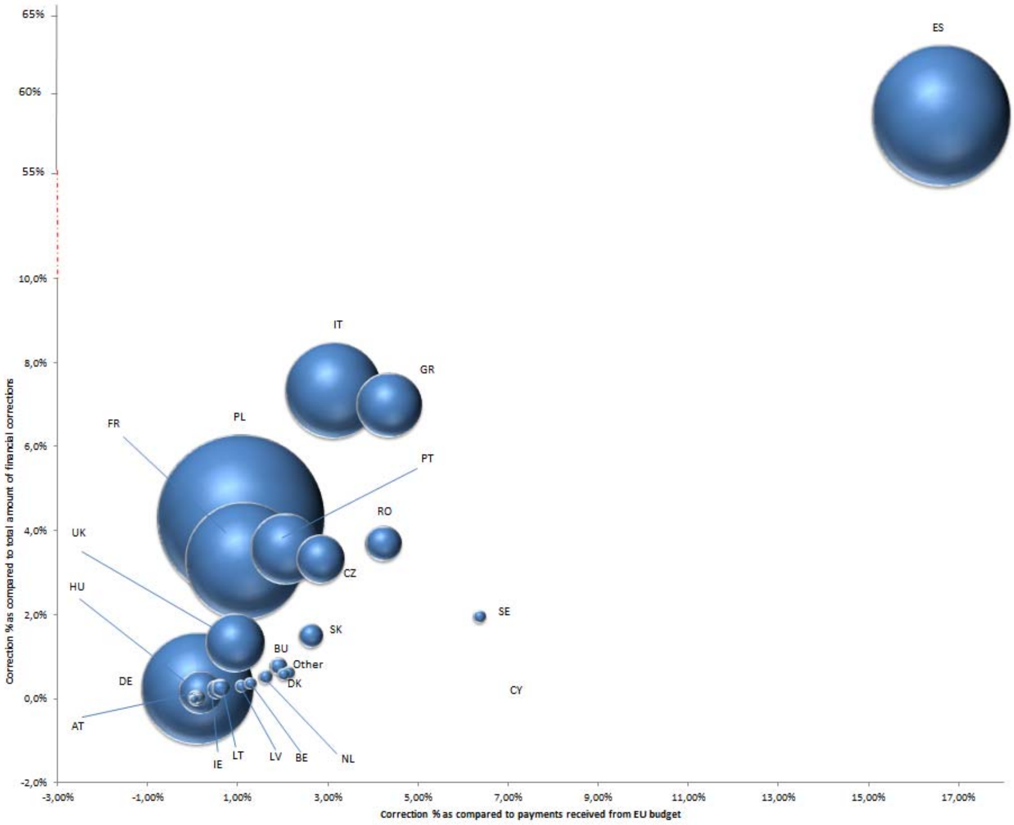
EUR millions

Member State	Payments received from the EU budget	*Financial corrections*								
		EAGF	Rural Develop ment	ERDF	Cohesion Fund	ESF	Other	Total 2012	% as compared to payments received from the EU budget	% as compared to the total amount of financial corrections
Belgium	1 114	0	3	0	-	11	0	**14**	*1.3%*	*0.4%*
Bulgaria	1 590	15	7	0	6	1	-	**30**	*1.9%*	*0.8%*
Czech Republic	4 433	0	-	116	8	-	0	**125**	*2.8%*	*3.3%*
Denmark	1 101	22	-	0	-	-	-	**22**	*2.0%*	*0.6%*
Germany	10 358	(16)	3	23	-	0	0	**10**	*0.1%*	*0.3%*
Estonia	915	0	1	0	0	0	-	**1**	*0.1%*	*0.0%*
Ireland	1 750	(1)	10	-	-	-	-	**9**	*0.5%*	*0.2%*
Greece	6 022	85	5	0	13	159	0	**262**	*4.4%*	*7.0%*
Spain	12 967	47	2	1 952	81	84	7	**2 172**	*16.8%*	*58.0%*
France	10 868	64	1	20	-	37	2	**123**	*1.1%*	*3.3%*
Italy	8 835	209	0	57	-	3	7	**275**	*3.1%*	*7.3%*
Cyprus	111	8	0	-	-	-	0	**8**	*7.2%*	*0.2%*
Latvia	1 128	-	-	1	1	9	0	**12**	*1.1%*	*0.3%*
Lithuania	1 644	3	4	3	1	0	0	**10**	*0.6%*	*0.3%*
Luxembourg	52	0	-	0	-	-	-	**0**	*0.0%*	*0.0%*
Hungary	3 973	6	0	0	-	-	0	**6**	*0.2%*	*0.2%*
Malta	101	0	-	-	-	-	-	**0**	*0.0%*	*0.0%*
Netherlands	1 247	17	2	0	-	-	0	**20**	*1.6%*	*0.5%*
Austria	1 513	1	-	-	-	-	0	**1**	*0.1%*	*0.0%*
Poland	15 417	12	2	45	79	23	0	**162**	*1.1%*	*4.3%*
Portugal	6 526	15	1	117	0	-	0	**134**	*2.1%*	*3.6%*
Romania	3 290	24	12	22	-	81	-	**139**	*4.2%*	*3.7%*
Slovenia	836	0	0	-	-	-	0	**0**	*0.0%*	*0.0%*
Slovakia	2 190	0	-	29	17	11	-	**57**	*2.6%*	*1.5%*
Finland	1 107	1	0	0	-	-	0	**1**	*0.1%*	*0.0%*
Sweden	1 166	72	2	0	-	0	-	**74**	*6.3%*	*2.0%*
United Kingdom	5 384	27	4	4	-	12	2	**50**	*0.9%*	*1.3%*
Non-split	1 140	-	-	24	-	-	-	**24**	-	-
TOTAL	**106 777**	**610**	**59**	**2 416**	**207**	**430**	**19**	**3 742**	***3.5%***	***100%***

The graph below takes into account both the absolute “contribution” of each Member State to the total financial corrections and the relative weight of the financial corrections for each Member State compared to the payments received from the EU budget.

In 2012, 11 Member States present overall percentages below 1% and a further 11 Member States between 1% and the average of 3.5% - in total these 22 contribute to 29% of the total corrections. Finally, 5 Member States present percentages higher than the average, over 4.2% in all cases, and contribute to 71% of the amount of financial corrections implemented in 2012. Spain with a percentage of 16.8% is clearly the most significant due to specific and complex corrections that were implemented in 2012 in the context of the closure of 2000-2006 programming period.

Graph 6.2.2: Share of Member States' financial corrections implemented as compared to payments received from the EU budget in 2012*



** The size of the "bubble" is proportionate to the EU Funds received.*

Attention is drawn to the fact that the above data relates to one year only, 2012. The level of both the global corrections amount and the split by Member State can change significantly depending on the year. Therefore, a meaningful assessment of the corrective capacity of supervisory and control systems has to be based on a multi-annual perspective (see also section **5** above). For this reason, information on the cumulative financial corrections per Member State is presented below for Agriculture (since the first clearance of accounts decision in 1999) and for the ERDF and ESF 2000-2006 programmes, which are in the closure phase.

6.2.3 Agriculture (EAGF): financial corrections under clearance of accounts

Concerning **Agriculture** (**EAGF**), the amount of financial corrections imposed by the Commission since the first clearance of accounts decision in 1999, totals EUR 8 286 million. Once decided by the Commission, the amounts are automatically applied. It is to be noted that in a few cases the date of implementation was deferred by 18 months, and some decisions are also reimbursed in 3 deferred annual instalments. This is notably the case for Member States subject to financial assistance in accordance with the European Financial Stability Framework Agreement signed on 7 June 2010.

The table below gives a breakdown of the financial corrections that are reimbursed by the Member States concerned to the EU budget. Year on year, the total amounts of financial corrections remain relatively stable and even show a positive trend over the period, in absolute amounts and also in terms of percentage of expenditure.

Table 6.2.3 Cumulative financial corrections decided under EAGF clearance of accounts from the first decision in 1999 to end 2012: Breakdown by Member State

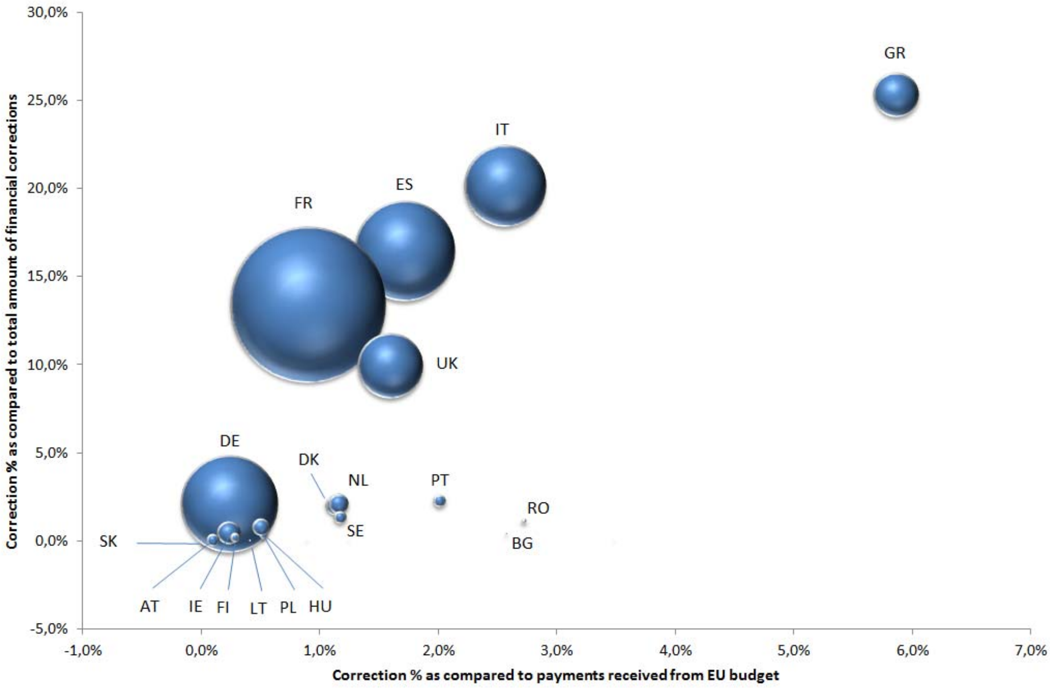
EUR millions

Member State	Payments received from EU budget	Cumulated financial corrections at end 2012	% as compared to payments received from EU budget	% as compared to total amount of financial corrections
Belgium	11 018	34	*0.3%*	*0.4%*
Bulgaria	1 441	37	*2.6%*	*0.4%*
Czech Republic	3 904	1	*0.0%*	*0.0%*
Denmark	15 414	173	*1.1%*	*2.1%*
Germany	76 997	178	*0.2%*	*2.1%*
Estonia	428	0	*0.0%*	*0.0%*
Ireland	18 225	42	*0.2%*	*0.5%*
Greece	35 793	2 102	*5.9%*	*25.4%*
Spain	79 733	1 366	*1.7%*	*16.5%*
France	124 663	1 115	*0.9%*	*13.5%*
Italy	64 791	1 672	*2.6%*	*20.2%*
Cyprus	287	10	*3.5%*	*0.1%*
Latvia	601	0	*0.0%*	*0.0%*
Lithuania	1 732	7	*0.4%*	*0.1%*
Luxembourg	399	5	*1.3%*	*0.1%*
Hungary	6 007	31	*0.5%*	*0.4%*
Malta	22	0	*0.0%*	*0.0%*
Netherlands	15 549	179	*1.2%*	*2.2%*
Austria	9 731	9	*0.1%*	*0.1%*
Poland	13 569	67	*0.5%*	*0.8%*
Portugal	9 511	193	*2.0%*	*2.3%*
Romania	3 573	97	*2.7%*	*1.2%*
Slovenia	568	5	*0.9%*	*0.1%*
Slovakia	1 714	0	*0.0%*	*0.0%*
Finland	7 376	21	*0.3%*	*0.3%*
Sweden	9 847	116	*1.2%*	*1.4%*
United Kingdom	51 953	826	*1.6%*	*10.0%*
Total	**564 847**	**8 286**	***1.5%***	***100%***

The following graph takes into account both the absolute "contribution" of each Member State to the total financial corrections and the relative weight of the financial corrections for each Member State compared to the payments received from the EU budget.

15 Member States present overall rates of correction below 1% - corrections for these 15 Member States contribute to 18% of the total corrections. A further 4 Member States present rates between 1% and the average rate of 1.5% and represent 6% of the total corrections. Finally, 8 Member States present a rate of correction above the average of 1.5% and contribute to 76% of the total amount of corrections.

Graph 6.2.3 Share of Member States' cumulative financial corrections under EAGF clearance of accounts from the first decision in 1999 to end 2012 as compared to payments received from the EU Budget*



** The size of the "bubble" is proportionate to the EU Funds received.*

6.2.4 Cohesion Policy: Closure of the 2000-2006 programming period

As the closure of the period 2000-2006 for Cohesion Policy is in the completion stage, the overall results of the corrective actions and the total monies spent can be compared and a more complete view of the impact of corrective mechanisms is possible, as indicated in a recent report of the Commission services[14]. For the ERDF and ESF funds at the end of 2012 the combined rate of financial correction, based on Commission supervision only, was 4% of the allocations (EUR 196.9 billion). This corresponds to almost EUR 8 billion of financial corrections at end 2012.

The closure process has been essential in ensuring that residual risks are appropriately covered for both Funds since financial corrections imposed at the closure stage by the Commission represent roughly one third of the total financial corrections imposed by the Commission.

This includes amounts of corrections in progress at end 2012 corresponding to 0.9% of the allocations (EUR 1.7 billion), which are included in closure letters formally communicated to Member States authorities but not yet accepted by Member States.[15 16]

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[14] "Report on financial corrections carried out for ERDF and ESF on 2000-2006 programmes", reference note ARES(2013)689652 of 12/04/2013, sent to CONT and note ARES(2013)1041808 of 14/05/2013 sent to the ECA.

[15] These estimated rates of financial correction do not include additional potential ERDF corrections linked to unfinished projects nor additional corrections that may result from the completion of the closure process. In the context of the ESF, at the end of 2012, there were still 61 programmes to be closed where potential financial corrections might be identified.

Table 6.2.4 ERDF & ESF – Programming period 2000-2006: Financial corrections decided/confirmed and in progress at 31/12/2012 – Breakdown by Member State

EUR millions

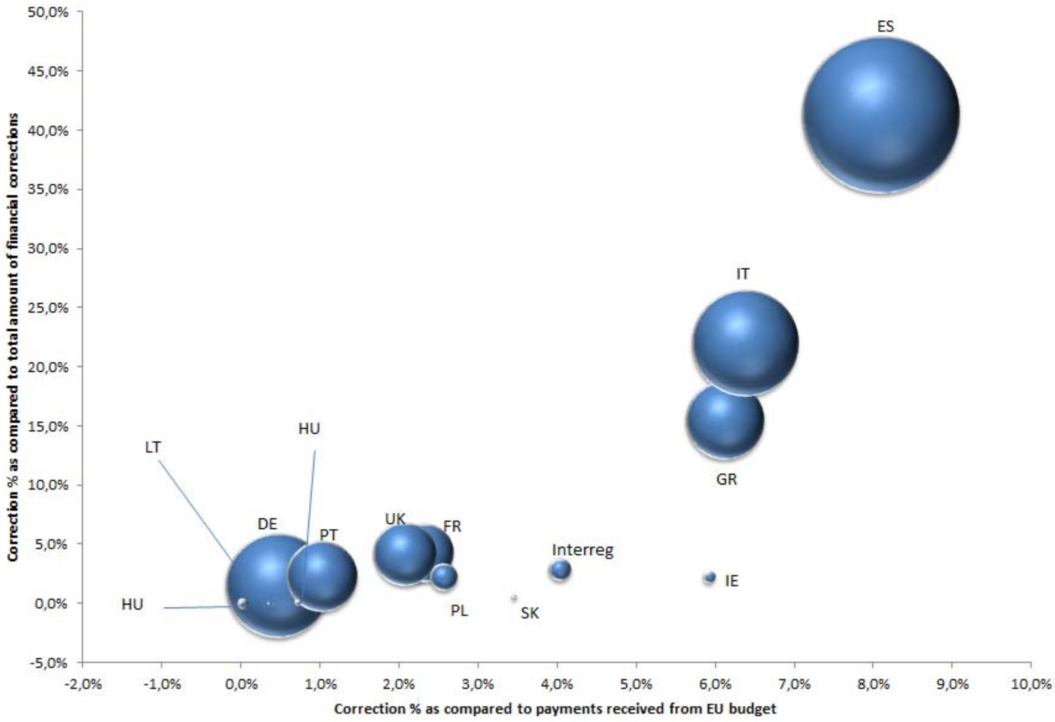
Member State	ERDF+ESF contribution amount	Financial corrections decided/ confirmed	Financial corrections in progress (closure letters sent)	Total financial corrections imposed for 2000-2006	Percentage of financial corrections in relation to the ERDF+ESF contributions	Share of financial corrections imposed compared to total financial corrections
Belgium	1 945	12	2	14	0.7%	0.2%
Czech Republic	1 456	5	10	15	1.0%	0.2%
Denmark	570	0	-	0	0.1%	0.0%
Germany	26 960	36	88	124	0.5%	1.6%
Estonia	305	1	-	1	0.4%	0.0%
Ireland	3 067	21	160	181	5.9%	2.3%
Greece	20 211	1 154	81	1 235	6.1%	15.5%
Spain	40 686	2 921	368	3 289	8.1%	41.3%
France	14 825	309	33	342	2.3%	4.3%
Italy	27 501	1 011	740	1 751	6.4%	22.0%
Cyprus	53	0	-	-	0.0%	0.0%
Latvia	518	4	-	4	0.8%	0.1%
Lithuania	773	3	-	3	0.3%	0.0%
Luxembourg	71	2	-	2	2.6%	0.0%
Hungary	1 695	12	-	12	0.7%	0.2%
Malta	57	-	-	-	0.0%	0.0%
Netherlands	2 702	0	-	0	0.0%	0.0%
Austria	1 647	0	-	0	0.0%	0.0%
Poland	7 032	180	-	180	2.6%	2.3%
Portugal	18 178	181	3	184	1.0%	2.3%
Slovenia	215	2	-	2	0.9%	0.0%
Slovakia	1 245	43	-	43	3.4%	0.5%
Finland	1 789	0	-	0	0.0%	0.0%
Sweden	1 634	12	0	12	0.7%	0.1%
United Kingdom	16 129	293	40	333	2.1%	4.2%
Interreg	5 645	25	202	227	4.0%	2.9%
Total	**196 911**	**6 229**	**1 726**	**7 955**	**4.0%**	**100%**

The following graph takes into account both the absolute “contribution” of each Member State to the total financial corrections and the relative weight of the financial corrections for each Member State compared to the payments received from the EU budget.

15 Member States present overall rates of correction equal to or below 1% - corrections for these 15 Member States contribute to just 2% of the total corrections. A further 5 Member States, plus INTERREG, present rates between 1% and the average rate of 4% and represent 14% of the total corrections. Finally, 5 Member States present a rate of correction above the average of 4% and contribute to 84% of the total amount of corrections.

[16] A prudent estimate of the Commission services of additional corrections carried out by Member States themselves and reported to the Commission until March 2010 is EUR 0.96 billion for the ERDF and 0.32 billion for the ESF, representing at least 0.7% and 0.5% of allocations respectively. This means that by end 2012 the overall rate of correction for the 2000-2006 period is at least 5.6% for the ERDF decided allocations and 2.9% for the ESF (for details, see Report on Financial corrections carried out for ERDF and ESF on 2000-2006 programmes sent to EP CONT Commitment on 12/04/2013 ARES(2013)689652 pages 12 to 18).

Graph 6.2.4 Share of Member States' cumulative financial corrections decided/confirmed and in progress (at 31/12/2012) for ERDF & ESF programming period 2000-2006*



** The size of the "bubble" is proportionate to the EU Funds received.*

6.3. Further consequences of financial corrections

It is underlined that the reported amounts in the sections above do not reflect the totality of the amount of financial corrections accepted by Member States as a result of the supervisory role of the Commission. **Remedial action plans may have a preventive impact on expenditure already incurred by beneficiaries and registered at national level in the certifying authority's accounts but not yet declared to the Commission.** For such expenditure, the certifying authority (under Cohesion policy) applies the financial correction requested by the Commission prior to declaring expenditure. Particularly in the case of extrapolated or flat rate corrections, where there are weaknesses in management and control systems covering a large population of projects, the amounts concerned can be significant.

Preventive effect of financial corrections under Cohesion policy

As a result of the Commission action plan and interruptions, at the end of 2012, the Czech Republic accepted a Commission request for a correction of about EUR 450 million covering two ERDF programmes. The Commission could formally report only EUR 108 million as withdrawals from previously certified expenditure; the remaining corrections do not appear in the official Commission reporting, as an amount of EUR 151.4 million was not included in the certification of October 2012 and a further amount of approximately EUR 189 million will be deducted by the certifying authority before certifying future claims to the Commission in 2013. A similar preventive effect, not reflected in the official reporting of financial corrections, concerns an ERDF/CF Slovak programme where a 7.3% deduction of all expenditure certified and to be certified in the future for hundreds of contracts was deemed necessary by the Commission in order to adequately protect the EU budget and it is now implemented by the Member State.

Another case concerns an ESF flat-rate correction for Romania: The Commission identified serious problems in a Romanian operational programme during 2012. The Commission and Romanian authorities agreed on a 25% flat-rate correction covering all expenditure incurred as at end 2012, plus further claims affected by the same irregularities identified by the Commission. As a result, Romania made a further declaration of expenditure (exceeding 25 % of all expenditure declared previously), on the basis of which the Commission paid a very small amount to Romania in December 2012 after offsetting the agreed financial correction. The impact of the financial correction is that expenditure incurred, which was in breach of law, is excluded from Union expenditure.

This preventive effect of the Commission supervisory role is not reflected in the official reporting even though it leads to an increased protection of the EU budget. For example, **warning letters sent out by the Directorates-General** when system deficiencies are identified before a payment claim is submitted to the Commission may have the same preventive effect on the protection of the EU budget, but in this case no financial correction is reported by the European Commission/ Member States either.

Recoveries from beneficiaries may also result from audits and financial corrections by the Commission services. When the Member State recovers irregular amounts from farmers before the financial correction is decided by the Commission, these amounts are reimbursed to the EU budget and are deducted from the financial correction. Amounts recovered from beneficiaries after the execution of the financial correction shall not be reimbursed to the EU budget. This system encourages Member State in their efforts to actually recover irregular payments.

Recoveries linked to financial corrections under Agriculture

In Italy for the financial year 2008, the calculated risk for the EU budget of weaknesses in the Land Parcel Identification System (LPIS) was EUR 29.6 million. Due to amounts recovered by the Italian authorities following an update of their LPIS (EUR 23 million), the financial correction finally amounted to EUR 6.6 million.

In Ireland for claim years 2005 to 2007, the calculated risk due to weaknesses in the LPIS was EUR 5 Million. However taking into account amounts recovered from the farmers, the financial correction eventually amounted to EUR 0.02 million.

A comparable situation appeared in Austria, where for claim years 2006, 2007 and 2008 the total calculated risk represented EUR 6.9 million. Also in this case, further to an update of their LPIS and subsequent retroactive cross-checks, the Austrian authorities recovered EUR 3.3 million from the farmers. The final financial correction amounted to EUR 3.6 million.

In addition, where the Commission considers that the time taken for a Member State to recover amounts from a final beneficiary is too long, it can and does launch **infringement procedures against the Member State involved**. This of course is in addition to the fact that the EU Budget may already be protected via the original financial correction. In the field of the CAP, a specific mechanism also exists under which 50% of undue payments which the Member States have not recovered from the beneficiaries within 4 years (or 8 years in case of judicial proceedings), are automatically charged to their national budgets. This gives a strong incentive to the national authorities to complete the recovery procedures in a timely manner. In addition, the Commission may also charge the entire amount still to be recovered (and not only 50%) if it considers that the Member States' authorities have been negligent in the management of the recovery procedure for specific individual cases.

Infringement procedure following financial corrections

In 2013, the European Commission, via a letter of formal notice, called on Italy to take action to address deficiencies in the implementation of EU legislation concerning imposition of surplus levy on milk and other milk products among milk producers who have contributed to the overruns of the national quotas, and specifically to effectively recover levy due from such liable producers.

The failure to ensure the effective recovery undermines the possibility for that system to achieve its objectives of stabilisation of the market and also creates distortions of competition with other European and Italian producers having abided to the system of production limitation or having regularly paid the surplus levies due in case of overrun. The total of levy still not recovered amounts to at least EUR 1.4 billion and it is due to the Italian budget.

The Commission has already imposed financial corrections amounting to EUR 750 million linked to this problem. Furthermore, it raised the issue of Italy's inability to comply with the obligation of taking all measures necessary to ensure the timely payment of surplus levy by the concerned producers in its numerous correspondences with the Italian authorities. Italy manifestly did not take the appropriate measures to effectively recover the levy due from such liable producers, despite the repeated requests coming from the Commission. The Commission has accordingly decided to initiate the infringement procedure under Article 258 of the TFEU.

7. ROLE OF FINANCIAL CORRECTIONS AND RECOVERIES IF ERROR RATES ARE PERSISTENTLY HIGH

The European Parliament resolution on the integrated internal control framework adopted on 3rd July 2013[17] requested a strict application of the Article 32 (5) of the Financial Regulation which states:

Article 32 – Internal control on budget implementation

...

5. If, during implementation, the level of error is persistently high, the Commission shall identify the weaknesses in the control systems, analyse the costs and benefits of possible corrective measures and take or propose appropriate action, such as simplification of the applicable provisions, improvement of the control systems and re-design of the programme or delivery system.

The Commission is required to implement this provision of the Financial Regulation in the most economical way, taking into account the resources available, in particular during a period of staff reduction.

However, difficulties have arisen in the legislative procedure for the period 2014-2020 which could affect the proposed simplification. The remaining risks caused by overly complex rules complicate the prevention of errors and therefore lead to a high cost of control. This is why the Commission considers that, especially in the area of shared management, the implementation of this new requirement foreseen in Article 32(5) cannot be limited to actions which only focus on identifying and correcting errors at the level of final recipients.

Financial corrections and recoveries at the level of the Member States, which are implemented during the lifetime of multi-annual programmes, will always be an important factor to be taken into consideration, as well as the continued efforts to simplify rules, redesign and strengthen systems.

[17] Ref. P7_TA(2013)0319

8. CORRECTIVE ACTIONS MADE BY MEMBER STATES UNDER COHESION POLICY ON THEIR OWN INITITATIVE

Under shared management, Member States have the primary obligation to prevent and detect irregularities, and thus to make financial corrections and recover undue amounts from beneficiaries. Thus, they perform management verifications, controls and audits in the first instance, these being in addition to those of the Commission detailed above. Under the regulations for the current programming period, Member States have to report annually the corrections stemming from all controls performed. Such a requirement was only introduced for 2007-2013 and the Commission is performing risk-based audits to test the reliability of these figures for the purpose of its assurance process.

The cumulative corrections implemented to end 2012, following the controls made by the Member States for Cohesion Policy programming period 2007-2013, are given below. These amounts are in addition to, and after deduction of, the corrections reported cumulatively by the Commission above.

Table 8: Cumulative corrections at end 2012 reported by Member States for Cohesion Policy period 2007-2013

EUR millions

Member State	**ERDF/CF**	**ESF**	**EFF**	**Total 2012**
Belgium	3	11	-	**14**
Bulgaria	13	2	0	**15**
Czech Republic	191	37	-	**228**
Denmark	0	0	0	**0**
Germany	290	49	1	**340**
Estonia	4	0	0	**4**
Ireland	0	5	0	**5**
Greece	63	-	0	**63**
Spain	204	39	9	**252**
France	42	37	0	**79**
Italy	141	27	0	**168**
Cyprus	0	0	0	**1**
Latvia	10	-	0	**10**
Lithuania	6	0	0	**6**
Luxembourg	-	0	-	**0**
Hungary	26	-	0	**26**
Malta	1	0	-	**1**
Netherlands	1	2	0	**3**
Austria	4	1	0	**5**
Poland	204	-	0	**204**
Portugal	46	28	1	**75**
Romania	43	-	0	**43**
Slovenia	5	5	-	**10**
Slovakia	33	4	0	**37**
Finland	1	0	0	**1**
Sweden	2	1	1	**4**
United Kingdom	38	13	1	**52**
Cross-border	8	-	-	**8**
TOTAL IMPLEMENTED	**1 377**	**261**	**14**	**1 652**

9. OTHER RECOVERIES

9.1. Recovery of pre-financing amounts

Another important control of the Commission, which is not covered by any of the above mechanisms, is the recovery of unused (i.e. unspent) pre-financing amounts. When a beneficiary has not used (spent) the advances received from the EU on eligible expenditure, the Commission issues a recovery order to return the monies to the EU budget. This procedure represents an important step in the control system of the EU to ensure that no excess money is kept by the beneficiary without proper expense justification, thus contributing to the protection of the EU budget. The amounts are the result of the issuance of a recovery order by the Commission, and are recorded in the accounting system as such. The above recovery of unused pre-financing amounts should not be confused with irregular expenditure recovered. Where Commission services identify and recover such expenditure in relation to pre-financing amounts paid out, these are included in the normal financial correction or recovery processes described above.

Table 9.1: Recovery of pre-financing amounts

EUR millions

	2012
Agriculture:	
EAGF	0
Rural Development	0
Cohesion Policy:	
ERDF	38
Cohesion Fund	5
ESF	214
FIFG/EFF	0
EAGGF Guidance	5
Internal policy areas	207
External policy areas	104
Administration	2
Total recovered Pre-Financing	**575**

9.2. Recoveries relating to own resource revenues

So as to provide a complete picture of all the tools used by the Commission to protect the EU budget, it is also necessary to consider the recoveries made in the area of own resource revenue. Own resource revenue is the primary element of the EU's operating revenue and therefore the bulk of expenditure is financed by it. The Commission makes on-the-spot inspections so as to verify that the correct amounts are being supplied to the EU budget. Amounts can also be audited as part of the ECA's annual audit process. In 2012, the amounts recovered were as follows:

Table 9.2: Recoveries relating to own resource revenues

EUR millions

	2012
Amounts recovered:	
- Principal	133
- Interest	160
Total recovered	**293**