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From:	Mr Vítor CALDEIRA, President of the European Court of Auditors
date of receipt:	28 November 2013
To:	Mr Linas LINKEVICIUS, President of the Council of the European Union
Subject:	Report on the annual accounts of the European Joint Undertaking for ITER and the Development of Fusion Energy for the financial year 2012 together with the Joint Undertaking's replies

Delegations will find attached the European Court of Auditors' report on the annual accounts of the European Joint Undertaking for ITER and the Development of Fusion Energy for the financial year 2012.

This report is accompanied by the Joint Undertaking's replies and will shortly be published in the *Official Journal of the European Union*.

Encl.: Report on the annual accounts of the European Joint Undertaking for ITER and the Development of Fusion Energy for the financial year 2012 together with the Joint Undertaking's replies.¹

¹ In English only. The other languages of this report are available on the European Court of Auditors' website: <http://eca.europa.eu/>.

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EUROPEAN COURT OF AUDITORS
COUR DES COMPTES EUROPÉENNE
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Report on the annual accounts of the
European Joint Undertaking for ITER and the Development of Fusion Energy
for the financial year 2012

together with the Joint Undertaking's replies

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INTRODUCTION

1. The European Joint Undertaking for ITER¹ and the Development of Fusion Energy (F4E) was set up in March 2007² for a period of 35 years. While the main fusion facilities are to be developed at Cadarache in France, the Joint Undertaking is located in Barcelona.

2. The tasks of the Joint Undertaking are³:

- (a) to provide the contribution of Euratom to the ITER International Fusion Energy Organisation⁴;
- (b) to provide the contribution of Euratom to 'Broader Approach' (complementary joint fusion research) activities with Japan for the rapid development of fusion energy;
- (c) to prepare and coordinate a programme of activities in preparation for the construction of a demonstration fusion reactor and related facilities, including the International Fusion Materials Irradiation Facility.

3. The members of the Joint Undertaking are Euratom, represented by the European Commission, the Member States of Euratom and other countries which have concluded cooperation agreements with Euratom in the field of

¹ ITER: International Thermonuclear Experimental Reactor.

² Council Decision 2007/198/Euratom of 27 March 2007 establishing the European Joint Undertaking for ITER and the Development of Fusion Energy and conferring advantages upon it (OJ L 90, 30.3.2007, p. 58).

³ The **Annex** summarises the Joint Undertaking's competences, activities and available resources. It is presented for information purposes.

⁴ The ITER International Fusion Energy Organisation was set up in October 2007 for an initial period of 35 years to implement the ITER project, which aims to demonstrate the scientific and technological feasibility of fusion energy. The Members are Euratom, the People's Republic of China, the Republic of India, Japan, the Republic of Korea, the Russian Federation and the United States of America.

controlled nuclear fusion and have expressed their wish to become members (as at 31 December 2012: Switzerland).

INFORMATION IN SUPPORT OF THE STATEMENT OF ASSURANCE

4. The audit approach taken by the Court comprises analytical audit procedures, testing of transactions at the level of the Joint Undertaking and an assessment of key controls of the supervisory and control systems. This is supplemented by evidence provided by the work of other auditors (where relevant) and an analysis of management representations.

STATEMENT OF ASSURANCE

5. Pursuant to the provisions of Article 287 of the Treaty on the Functioning of the European Union (TFEU), the Court has audited:

- (a) the annual accounts of the Joint Undertaking for ITER and the Development of Fusion Energy, which comprise the financial statements⁵ and the reports on the implementation of the budget⁶ for the financial year ended 31 December 2012, and
- (b) the legality and regularity of the transactions underlying those accounts.

The management's responsibility

6. In accordance with Articles 33 and 43 of Commission Regulation (EC, Euratom) No 2343/2002⁷, the management is responsible for the preparation

⁵ The Court received the annual accounts on 1 July 2013 and a corrigendum to these accounts on 8 October 2013. These include the balance sheet and the economic outturn account, the cash-flow table, the statement of changes in net assets, a summary of the significant accounting policies and other explanatory notes.

⁶ These comprise the reports on implementation of the budget, a summary of budgetary principles and other explanatory notes.

⁷ OJ L 357, 31.12.2002, p. 72.

and fair presentation of the annual accounts of the Joint Undertaking and the legality and regularity of the underlying transactions.

- (a) The management's responsibilities in respect of the Joint Undertaking's annual accounts include designing, implementing and maintaining an internal control system relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies on the basis of the accounting rules adopted by the Commission's accounting officer⁸, and making accounting estimates that are reasonable in the circumstances. The Director approves the annual accounts of the Joint Undertaking after its accounting officer has prepared them on the basis of all available information and established a note to accompany the accounts in which he declares, *inter alia*, that he has reasonable assurance that they present a true and fair view of the financial position of the Joint Undertaking in all material respects.
- (b) The management's responsibilities in respect of the legality and regularity of the underlying transactions and compliance with the principle of sound financial management consist of designing, implementing and maintaining an effective and efficient internal control system comprising adequate supervision and appropriate measures to prevent irregularities and fraud and, if necessary, legal proceedings to recover funds wrongly paid or used.

⁸ The accounting rules adopted by the Commission's accounting officer are derived from the International Public Sector Accounting Standards (IPSAS) issued by the International Federation of Accountants or, where relevant, the International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board.

The auditor's responsibility

7. The Court's responsibility is, on the basis of its audit, to provide the European Parliament and the Council⁹ with a statement of assurance as to the reliability of the annual accounts and the legality and regularity of the underlying transactions. The Court conducts its audit in accordance with the IFAC International Standards on Auditing and Codes of Ethics and the INTOSAI International Standards of Supreme Audit Institutions. These standards require the Court to plan and perform the audit to obtain reasonable assurance as to whether the annual accounts of the Joint Undertaking are free from material misstatement and the underlying transactions are legal and regular.

8. The audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the accounts and the legality and regularity of the underlying transactions. The procedures selected depend on the auditor's judgement, which is based on an assessment of the risks of material misstatement of the accounts and material non-compliance by the underlying transactions with the requirements in the legal framework of the European Union, whether due to fraud or error. In assessing these risks, the auditor considers any internal controls relevant to the preparation and fair presentation of the accounts, as well as the supervisory and control systems that are implemented to ensure the legality and regularity of underlying transactions, and designs audit procedures that are appropriate in the circumstances. The audit also entails evaluating the appropriateness of accounting policies, the reasonableness of accounting estimates and the overall presentation of the accounts.

9. The Court considers that the audit evidence obtained is sufficient and appropriate to provide a basis for the opinions set out below.

⁹ Article 185(2) of Council Regulation (EC, Euratom) No 1605/2002 (OJ L 248, 16.9.2002, p. 1).

Opinion on the reliability of the accounts

10. In the Court's opinion, the Joint Undertaking's annual accounts present fairly, in all material respects, its financial position as at 31 December 2012 and the results of its operations and its cash flows for the year then ended, in accordance with the provisions of its financial rules and the accounting rules adopted by the Commission's accounting officer.

Opinion on the legality and regularity of the transactions underlying the accounts

11. In the Court's opinion, the transactions underlying the annual accounts for the 1 year ended 31 December 2012 are, in all material respects, legal and regular.

12. The comments which follow do not call the Court's opinion into question.

COMMENTS ON BUDGETARY AND FINANCIAL MANAGEMENT***Presentation of the accounts***

13. In the notes to the financial statements, the table and the information included under Heading 4.3.1.1 "ITER Procurement Arrangements with the ITER International Organization" reflect the procurement arrangements signed (column 3) and the procurement arrangements credited so far (column 4). It does not show, however, the degree of advancement of the works in progress. This information is essential to reflect the status of the activities carried out so far by F4E as regards the procurement arrangements signed with the ITER International Organisation.

Implementation of the budget

14. The utilisation rates for the available commitment and payment appropriations were 99,9 % and 94,5 %, respectively. However, the utilisation rate for the payment appropriations referred to in the 2012 initial budget was

71 %¹⁰. Of the 1 440 million euro in commitment appropriations available for operational activities, only 55,4 % was implemented through direct individual commitments, while the remaining 44,6 % was implemented through global commitments.

COMMENTS ON KEY CONTROLS OF THE JOINT UNDERTAKING'S SUPERVISORY AND CONTROL SYSTEMS

15. The Court of Auditors previously reported that the Joint Undertaking's internal control systems had not been fully established and implemented. Although significant progress was made during 2012, a number of actions still need to be implemented:

- a management system to regularly monitor the validity of project cost estimates and report on cost deviations (see paragraph 29);
- the accounting officer's validation of the underlying systems was initiated in 2012, but direct testing of the Joint Undertaking's key controls at transaction level was still required at the end of the year. In 2013 the Joint Undertaking contracted a consulting firm¹¹ to complete the compliance validation work of the accounting system. While the overall conclusion is that F4E's accounting system is compliant with DG Budget Guidance, F4E's Financial Regulation, policies and procedures, several exceptions were reported¹²;

¹⁰ The original budget for payment appropriations was 503 million euro. It was then reduced to 377 million euro through the amending budgets of 28 March and 11 December 2012 (this amount includes the 2011 carry-over of 32,9 million euro in assigned revenue).

¹¹ Notwithstanding the added value of the consulting firm report, the exercise of validating the accounting systems falls under the responsibility of the Accounting Officer as laid down in Article 46 of the JU's Financial Regulation.

¹² Among other exceptions, the report points out that the deadlines adopted in the action plans in response to the Internal Auditor, the Commission Internal Audit Service and the Court's reports have expired for many of the actions without

- further efforts are necessary with regard to the systematic verification, prior to payment, of technical acceptance reports and the audit certificates on financial statements (see paragraphs 16 to 20);
- a comprehensive overall control and monitoring system for grants and operational contracts was presented to the Governing Board in December 2012 (see paragraph 23);
- the action plans adopted by the Joint Undertaking in response to internal audits¹³ have not been fully implemented. As regards the Commission's Internal Audit Service report on the preparation of procurement arrangements¹⁴, all ten recommendations are being implemented;
- the corporate risk management system was presented to the F4E Audit Committee in July 2012. Ten areas of very high risk were identified.¹⁵ Mitigating actions have yet to be implemented.

Operational procurement and grants

16. Negotiated procedures constituted 40 %¹⁶ of all operational tendering procedures launched in 2012¹⁷ (65 % in 2011). The Joint Undertaking still

having achieved full implementation. It also points out that the local reporting portal (DWH) does not yet provide an effective reconciliation between the accounting and the project management system.

¹³ Action plans in response to the internal audits on financial circuits, grant management, expert contracts, operational pre-procurement activities and procurement in the area of ITER buildings were adopted by the Joint Undertaking on 30 June 2010, 14 February 2011, 19 November 2011, 1 March 2012 and 21 September 2012 respectively.

¹⁴ Commission IAS report of 7 November 2012 on procurement arrangements.

¹⁵ Among others: low budget implementation, lack of competition in operational procurement, delays in the reception of data from the ITER Organisation.

¹⁶ Out of this percentage, 25 % can be considered as exceptional negotiated procedures as the estimated contract value exceeded 250 000 euro-

needs to increase the competitiveness of procurement procedures and further reduce the use of negotiated procedures¹⁸. Regarding grants, the average number of proposals received was only one per call.

17. Grant agreements concluded by the Joint Undertaking do not have a provision similar to Article II.25 of the European Commission's model grant agreement¹⁹, which stipulates financial penalties for beneficiaries that make false declarations or seriously fail to meet their obligations. In one grant agreement the Joint Undertaking accepted the whole amount of indirect costs as eligible despite a scope limitation in the audit certificate in respect of consumables²⁰.

18. The Joint Undertaking has not developed an internal procedure to systematically assess the risk of a payment being made while a non-conformity report is under review. In one payment related to an operational contract, the Joint Undertaking validated an invoice as ready for payment despite a major situation of non-conformity noted in the technical acceptance report, which was still under review by the ITER Organisation at the date of payment.

19. For joint procurement procedures, the Joint Undertaking has not yet established appropriate criteria to verify whether the procurement rules of the

¹⁷ Twenty negotiated procedures out of 50 tendering procedures launched for operational procurement in 2012.

¹⁸ According to the Commission Vademecum on public procurement, negotiated procedures should be the exception rather than the rule.

¹⁹ Article II.25, on financial penalties, states that: "1) A beneficiary that has been guilty of making false declarations or has been found to have seriously failed to meet its obligations under this grant agreement shall be liable to financial penalties of between 2 % and 10 % of the value of the financial contribution of [the Union] [Euratom] received by that beneficiary. The rate may be increased to between 4 % and 20 % in the event of a repeated offence within five years following the first infringement."

²⁰ The consumables item, which could not be quantified or verified, was part of the total 0,76 million euro in indirect costs submitted by the beneficiary.

other contracting authority are equivalent to its own, as required by Article 83 of the Joint Undertaking's implementing rules²¹.

20. As regards the five operational procurement procedures audited, the following weaknesses were identified:

- in two procurement procedures, the Joint Undertaking did not advertise the contract by means of a pre-information notice, although the Commission Vademecum on public procurement advises that this be done in order to increase visibility and competition;
- in one procurement procedure, the early warning system (indicating, *inter alia*, whether the natural or legal person concerned is in a situation of exclusion) was not consulted before the award because the Joint Undertaking had no access at that time to the system;
- in one case, the Joint Undertaking made an advance payment of 10 % of the total amount although the bond provided to the Joint Undertaking was issued by a commercial bank that did not meet the BBB rating stipulated in the contract;
- in two procedures, the cost estimates were greatly underestimated²². This shows the difficulties faced by the Joint Undertaking in calculating the cost

²¹ According to Article 83(1) and (2) of the implementing rules to the F4E Financial Regulation, in the event of a joint procurement procedure between the Joint Undertaking and another contracting authority, the Joint Undertaking's procurement procedures shall apply. Where the share pertaining to or managed by the other contracting authority in the total estimated value of the contract is equal to or above 50 %, or in other duly justified cases, the Director, with the prior approval of the Executive Committee, may decide that the procurement procedures applicable to the other contracting authority may apply, provided that they can be considered as equivalent to those of the Joint Undertaking.

²² In one of the procedures there was a difference of 9,3 million euro between the initial estimate of 2,8 million euro and the value of the contract resulting from the negotiated procedure, which was 12,1 million euro. In the other there was a difference of 3,7 million euro between the initial estimate of 2,3 million euro and the final estimate of 6 million euro.

estimates of the EU contribution to the construction phase of the ITER project (see paragraphs 28 to 31).

Overall control and monitoring of operational procurement contracts and grants

21. The Joint Undertaking has a system for performing audits²³ at the level of contractors with the aim of checking compliance with the quality assurance requirements²⁴.

22. , The Joint Undertaking visited six beneficiaries of grant agreements for *ex-post* financial and compliance controls on grants. The errors detected during these controls amounted to 1,3 % of the total value of the cost claims audited (8,3 million euro).

23. In response to previous Court observations²⁵, the Joint Undertaking presented, in November 2012 to the F4E Audit Committee and in December 2012 to the Governing Board, two documents on the overall control and monitoring strategy and the multiannual *ex-post* control strategy, by which it extended its quality audits to include the verification of financial aspects of operational contracts.

²³ Of the 25 quality audits carried out during 2012, 14 were closed by April 2013. The audits qualified two projects' performance as below standard, identified twelve situations of non-conformity with the procedures and 168 areas for improvement.

²⁴ The audits covered the quality plan, situations of non-conformity, purchase control and subcontracting management, documentation and data management, changes and deviations management, the civil works quality control plan, the detailed project schedule, contract risk management and the technical works quality control plan.

²⁵ Paragraph 23 of the Court's 2011 report.

OTHER MATTERS

Intellectual property rights and industrial policy

24. On 28 March 2012 the Governing Board adopted the F4E policy on intellectual property rights and the dissemination of information, and on 29 June 2012 it adopted detailed rules for implementing this policy. The F4E industrial policy was adopted by the Governing Board on 10-11 December 2012. A plan to systematically monitor and report on the observance of the rules adopted on intellectual property rights and the dissemination of information, and on compliance with the F4E industrial policy, has not yet been implemented.

Late payment of membership contributions

25. The 2012 contributions by eight members, totalling 1,2 million euro, were subject to delays ranging from 15 days to four months.

Rules implementing the Staff Regulations

26. F4E has not yet adopted all the rules implementing²⁶ the Staff Regulations, as required by Article 10(2) of the Annex to the F4E Statutes.

EU contribution to ITER construction phase

27. The Council conclusions adopted on 7 July 2010²⁷ on the ITER status and the possible way forward approved a final figure of 6,6 billion euro.

28. On 13 January 2012, the internal auditor's report on pre-procurement activities for the ITER project pointed out that: (i) neither of the two cost estimating exercises carried out by that date had broken down the cost

²⁶ *Inter alia* on recruitment of temporary agents, classification in grade and step upon engagement, part-time work, appraisal of the Director and modified provisions on family leave, parental leave and pension rights.

²⁷ Council conclusion on ITER status of 7 July 2010 (Ref.11902/10).

estimates of the EU contribution to the ITER construction phase by contract; (ii) the Joint Undertaking was exposed to significant financial risks linked to the evolution of commodity prices; and (iii) the Joint Undertaking did not yet have in place a tool for regularly monitoring the validity of the estimates and reporting on potential cost deviations.

29. In its progress report of September 2012 to the European Competitiveness Council, the Joint Undertaking stressed that there was a risk of cost deviations in the range of 180-250 million euro, or 3 % of the latest estimated project cost of 6,6 billion euro.

30. On 13 June 2013, the Joint Undertaking completed an exercise to update the cost estimate of the EU contribution to the construction phase of the project. As a result of this exercise, the current risk of increase is estimated at 290 million euro, or 4,4 % of the budget approved by the Council. According to the Joint Undertaking, there has been a significant escalation in the costs of the components to be provided to the ITER project. These are mainly attributed to the system engineering and configuration management processes at the overall ITER project level. The Joint Undertaking also considers the current ITER reference schedule to be unrealistic.

31. In this regard, the cost estimates for two of the five operational procurement procedures selected for audit were significantly underestimated (see paragraph 20).

Annual activity report

32. According to article 43 of the F4E Financial Regulation the annual activity report shall indicate the results of the Joint Undertaking's operations by reference to the objectives set, the risks associated with these operations, the use made of the resources provided and the efficiency and effectiveness of the internal control system. However, because of the date of availability of the revised cost estimation (see paragraph 30), the 2012 F4E Annual Report does

not include up to date information on the risks associated with deviations from the approved 6,6 billion euro budget.

Follow-up of previous observations

Host State agreement

According to the Host State Agreement signed with the Kingdom of Spain on 28 June 2007, permanent premises should have been made available to the Joint Undertaking by June 2010. At the time of the audit (April 2013), this had not occurred.

This Report was adopted by Chamber IV, headed by Dr Louis GALEA, Member of the Court of Auditors, in Luxembourg at its meeting of 22 October 2013.

For the Court of Auditors

Vítor Manuel da SILVA CALDEIRA
President

European Joint Undertaking for ITER and the Development of Fusion Energy (Barcelona)

Competences and activities

<p>Areas of Union competence deriving from the Treaty</p> <p><i>(Articles 45 and 49 of the Treaty establishing the European Atomic Energy Community)</i></p>	<p>Chapter 5, on 'Joint Undertakings', of the Treaty establishing the European Atomic Energy Community, and in particular:</p> <ul style="list-style-type: none"> - Article 45 <p><i>"Undertakings which are of fundamental importance to the development of the nuclear industry in the Community may be established as Joint Undertakings within the meaning of this Treaty, in accordance with the following Articles ..."</i></p> <ul style="list-style-type: none"> - Article 49 <p><i>"Joint Undertakings shall be established by Council decision. Each Joint Undertaking shall have legal personality."</i></p>
<p>Competences of the Joint Undertaking</p> <p><i>(Council Decision 2007/198/Euratom)</i></p>	<p>Objectives</p> <ul style="list-style-type: none"> - To provide the contribution of the European Atomic Energy Community (Euratom) to the ITER International Fusion Energy Organisation; - To provide the contribution of Euratom to Broader Approach activities with Japan for the rapid realisation of fusion energy; - To prepare and coordinate a programme of activities in preparation for the construction of a demonstration fusion reactor and related facilities, including the International Fusion Materials Irradiation Facility (IFMIF). <p>Tasks</p> <ul style="list-style-type: none"> - Oversee preparation of the ITER project site; - provide components, equipment, materials and other resources to the ITER Organisation; - manage procurement arrangements vis-à-vis the ITER Organisation and, in particular associated quality assurance procedures; - prepare and coordinate Euratom's participation in the scientific and technical exploitation of the ITER project; - coordinate scientific and technological research and development activities in support of Euratom's contribution to the ITER Organisation; - provide Euratom's financial contribution to the ITER Organisation; - arrange to make human resources available for the ITER Organisation; - interface with the ITER Organisation and carry out any other activities in furtherance of the ITER Agreement.
<p>Governance</p>	<p>Governing Board, Director and other bodies</p> <p>The Governing Board is responsible for the supervision of the Joint Undertaking in the pursuit of its objectives and ensures close collaboration between the Joint Undertaking and its members in the implementation of its activities. Together with the Governing Board and the Director, who is the chief executive officer responsible for the day-to-day management of the Joint Undertaking and its legal representative, the Joint Undertaking has several bodies:</p> <p>Bureau, Technical Advisory Panel, Executive Committee, Administration & Finance Committee, Audit Committee.</p> <p>Internal auditor: internal audit capability and the European Commission's Internal Audit Service (IAS) since 01/01/2012.</p> <p>External auditor: European Court of Auditors.</p> <p>Discharge authority: the European Parliament, on a recommendation from the Council.</p>

Resources available to the Joint Undertaking in 2012	Budget 379,5 million euro final revenue (payment appropriations), of which 76,5 % funded by Community contribution. Staff at 31 December 2012 <ul style="list-style-type: none">- 262 EU official and temporary agent posts provided for in the establishment plan, of which 218 posts were occupied;- 125 contract agent posts occupied.
Activities and services provided in 2012	For detailed information concerning the activities and services provided in 2012, please consult the F4E website at http://www.fusionforenergy.europa.eu/

Source: European Joint Undertaking for ITER and the Development of Fusion Energy.
