



Sigma Draft for RCOA comments

Working Group on Audit Manuals and Methods

Topic: The Audit of EU Agricultural Funds
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Workshop Summary Report

Introduction

The origins of the Common Agriculture Policy (CAP) lie in the 1950s where post-war Western Europe was unable to guarantee food supplies to its population. The principal aim during these times was therefore to ensure better productivity, and farmers were encouraged to do so by means of subsidies and guaranteed prices.

Such was the effectiveness, however, that 30 years later, any questions of ensuring self-sufficiency in food supplies were no longer justifiable. Surpluses were evident in most major food products, as seen by the fabled wine lakes and butter mountains. And it was expensive. At its peak, the CAP accounted for over two thirds of the EU budget. Reform of the CAP became an economic and political necessity.

The MacSharry reforms of 1994 introduced production limits and quotas designed to help reduce surpluses, and a rural development policy was introduced to encourage rural initiatives. Later, financial disciplinary mechanisms were

introduced in order to control further CAP spending.

Another evolution is that society has become more concerned with the sustainability of agriculture. There is a demand for more emphasis to be placed on issues linked with quality and safety of food, and the protection of the environment. These changing priorities were fully reflected in the most recent, and fundamental, reform of the CAP agreed by EU Agriculture ministers in June 2003.

The new CAP, in brief

Today's CAP is barely recognisable from its predecessors. It is demand driven, and now the vast majority of aid is paid to farmers independently of what they produce (known as de-coupling). Furthermore, payments are now linked to other factors such as respect of the environment, food safety and animal welfare standards (known as cross-compliance). The new CAP also places much greater emphasis on rural development measures, with Member

States (MS) able to transfer money from market and income support to this area (known as modulation).

Exponents of the new CAP claim that it simplifies matters, for example in the way it is financed or because the plethora of different direct payment schemes have been largely amalgamated into one single payment. However, owing to the various options available and transition periods, the reform of 2003 has left farmers, CAP administrators and auditors with a policy which is in many ways more complicated than ever.

For example, of the 15 MS pre-2004 enlargement, the new CAP is already in place in 10 since 2005, while another 5 MS opted for implementation 2007. There are also transitional phases for certain products, such as durum wheat, rice, nuts etc. It also allows MS to choose different models for applying the single payment scheme at regional level, as well as for some MS to maintain some coupling of aids in certain sectors.

For the new MS, while accession implied applying the *acquis communautaire*, and hence the new rules for CAP, access to the full payments from CAP will be gradual, notably in the area of direct payments where there is a gradual phasing-in over a 10 year period. There are also various possibilities, e.g. they can choose to operate a simplified system of direct payments, known as SAPS (Standard Area Payment Schemes). Eight of the ten new MS have opted for SAPS, the exceptions being Malta and Slovenia.

Enlargement and Agriculture

The 2004 enlargement expanded the single market from 380 million to 454 million people. Its impact on agriculture was, however, more dramatic. The number of farmers increased from 7 million to

11 million, and the number of hectares of land farmed increased by about 30%. The gross value added, however, is only expected to increase by about 6%. In other words, the new MS have a large agricultural potential which is only partially realised.

These figures will be further amplified when Romania and Bulgaria join the EU. In Romania over 40% of the labour force are engaged in agriculture (compared to an EU-15 average of less than 5%). Many farmers in the new MS are still considered to be "semi-subsistence", producing for their own consumption but who market part of their production. Only a small proportion of farms are already competitive in international terms. Many require modernisation and investment, and it is in this area that Sapard, the pre-accession instrument for agriculture and rural development, has made a significant contribution since its introduction in the year 2000.

The Sapard pre-accession programme has also helped 10 Central and Eastern European countries (CEECs) prepare for their participation in CAP. The programme is, uniquely, fully decentralised and administered by the CEECs themselves, thereby providing them with the opportunity to gain experience of applying the mechanisms for the management of agriculture and rural development programmes in advance of EU membership.

The workshop - who and why?

Representatives of the SAIs from the new Member States and Candidate Countries, along with Albania, met in Romania for three days to discuss and exchange experiences on the subject of auditing EU agricultural funds.

Clearly, given the nature of the topic and the variety of countries with regard to their experiences of auditing agricultural funds, the subject was going to be of interest in different ways for the participants: new MS who were already implementing the new CAP; new MS using a simplified system of direct payments; new MS with and without Sapard experience; Candidate Countries with and without Sapard experience; and other countries with little or no experience of auditing agricultural funds but who could expect to be involved in this area in the future.

Given the differing backgrounds of the participants in terms of experience in auditing agricultural funds, a special emphasis was placed on discussing good practices when first building up a capacity and capability for the Audit of EU Agriculture Funds, whether in the context of a Candidate Country or a new Member State.

The presentations, from the European Commission (DG Agri) and the ECA, old and new MS, and Candidate Countries, were intended to facilitate an exchange of knowledge and practical experiences of current practices and standards for such audits. And, despite the differences in backgrounds, a large number of common points emerged during discussions.

- **Legislation - too complicated**

Although it was generally considered that Sapard and the CAP Multi Annual Financing Agreement (MAFA) provided a clear framework for auditors to work from, there were concerns about Article 3 of the MAFA.

Under this Article “the Commission and the Court of Auditors of the European Communities” shall have the right to carry out audits. This right should be extended to the SAIs - in certain beneficiary

countries (like Romania), the current restriction is used to prevent SAIs from access to all entities to audit Sapard expenditure, unless accompanying others having that right.

As far as the CAP was concerned, it was a recurring theme that the CAP regulations were too numerous and too complicated. So far, the CAP reform has led to 24 new regulations, of which 20 are in force. The central acts are Council Regulation 1782/2003 which deals with direct support schemes, including the single payment scheme, and Council Regulation 1783/2003 concerning support for rural development.

The criteria for the EAGGF are complex, and moreover there are too many modifications to existing regulations. A consolidated version of each modified regulation should be made available immediately after approval of the modification (e.g. published on the Europa web-site). The lines of communication between MS SAIs and Brussels should be more clearly defined in order to ensure changes in legislation are notified in a timely manner.

Auditors in MS often see clearly the negative effects of poorly conceived regulations, but their views are usually not well enough known to national and European legislators.

- *The Commission should consider modifying Article 3 of the MAFA. A proposal to this effect could be put to the Commission by SAIs.*
- *The Commission should strive to improve the clarity of regulations and eligibility criteria.*
- *Any changes in legislation should be fully discussed in thorough consultation and communicated in a systematic manner to relevant parties, including SAIs.*

- *As a general rule, national administrations should ensure that SAIs are consulted on any proposals for new regulations (whether EU or national) involving EU expenditure.*
- *The shared management concept was not well understood and more effort needs to be made to delegate accountabilities clearly to MS authorities and find new ways to ensure controls compliance.*
- *SAIs should support the developments to create a better functioning “chain of control” and “single audit” systems and the wider use of COSO framework concepts to improve financial management and control in this area.*

- **Paying Agencies / Sapard Agencies - a vital link in the chain**

The Sapard programme requires organisational features similar to those necessary for implementation of the CAP. One of these features is the Sapard agency, equivalent of the CAP Paying Agency (PA), where national management authorities are responsible for implementing the measures of the program and making payments to beneficiaries.

With such agencies the problem of too complex and constantly changing procedures was often apparent. Decentralisation of PAs was generally considered preferable, although this could lead to problems with training, supervision etc. PAs did not always do enough to educate beneficiaries, nor did they always have the information they required to do their job.

- *Paying Agencies should do more to explain eligibility criteria to beneficiaries.*
- *Accessible databases with information on land registration were essential to the proper functioning of PAs .*

- **Certifying Bodies - when task carried out by an SAI**

Checking the accounts of the PA is a task carried out by the certifying body (CB). Where an SAI assumes the tasks of a CB, there is a need to take measures to ensure that conflict of interest and loss of independence are avoided. The experience of this situation in Romania shows that it had been a good way for staff to gain experience of auditing EU agricultural expenditure and developing more modern and advanced financial audit methods.

The number of SAIs who were also CBs in the new MS was in the minority (in the old MS, only in the UK and Sweden does this situation exist). There was a feeling that SAIs in this situation did not have sufficient contacts with the Commission.

Where SAIs do not act as CBs, their role in relation to the audit of EU funds (and to CBs) should be clarified.

- *The Commission could provide guidance on the subject of independence of CBs. This could be a subject of further discussion within the future network of auditors of EU agriculture expenditure proposed by the ECA.*
- *Further consideration should be given to understanding and mitigating SAI problems with “independence” issues so that more SAIs may wish to become CBs.*
- *The Commission should liaise more closely and communicate better with the SAIs acting as CBs (and presumably also with other certifying bodies).*

- **SAIs - challenges faced**

It is clear that, from a practical point of view, many SAIs had major problems with

the actual task of carrying out audits in the field of EU agricultural expenditure. Dealing with a new subject area and having to become familiar with detailed and overly complicated legislation. Along with a lack of internal resources within the SAI, all contribute an inherent risk in this area.

The lack of auditors with experience in agriculture was mentioned. Better training is required whenever agricultural measures are audited. Specific training is necessary on “good agricultural practice” as this principle (and the regulations behind it) form nowadays the basis of any public assistance given to farmers.

- *Special training in agricultural concepts and techniques would be appreciated.*
- *The use of experts with specialist knowledge in the field should be considered.*
- *Auditors, even those from Romania and Bulgaria, should currently be undergoing specific training for the audit of the Integrated Administration and Control System (IACS).*
- *SAIs need to coordinate and use the work of internal auditors better. Using the International Auditing Standard 610 is a key for this.*

- **Developing the capability of SAIs to audit agriculture – training, guidelines, networks etc.**

Auditors expressed an interest in receiving more help, either from independent experts or the ECA. Developments such as a common methodology, or providing check lists, were mooted as ways which could help. Sharing information would also be a simple yet effective aid to auditors.

Bringing together people on the same subject, even with different needs, and

allowing auditors to learn more about what was happening in other countries (as was done in this workshop), highlighted the value and importance of cooperation.

The need for more specialised workshops was expressed. Some topics which could be considered for the future were also identified - audit criteria definition, preparation of audit check lists, the EAGGF in particular, and looking at more practical cases concerning the audit of agriculture.

The network of EU agriculture auditors proposed by the ECA, as announced at the Contact Committee meeting of 2004 and reiterated by the ECA during the workshop, was considered to be a positive and important development.

- *A common audit methodology should be established for the auditing of EU Agricultural Funds.*
- *SAIs should endeavour to exchange more information, such as reports, manuals, checklists, etc.*
- *Participants should become proactive themselves, and build upon individual contacts created during this workshop.*
- *Cooperation between SAIs and the ECA is very useful. Participants were encouraged to ensure that their SAI not only responded to the ECA’s invitation to set up a network (the Bernicot letter), but also make clear exactly what they expected it to do and achieve. This is very important and SAIs need to be proactive in demanding more cooperation and contact in the area.*
- *The ECA needs to develop procedures to enable it to work together with, and rely more on the work of CBS and SAIs on EU Agricultural funds.*

Conclusions

It is not only farmers who face new challenges in agriculture, both in the MS

with the CAP reform and in the candidate countries where a certain degree of restructuring of the industry is inevitable. Auditors also face challenges. It is the job of auditors, in this field as in others, to determine whether managers are not just making sure that money has been spent, but also that the money has been spent properly.

For auditors facing the subject for the first time, such a task can seem especially daunting. Agriculture, and the EU regulations governing this field, are complicated matters for most people. Even an organisation like the ECA with its

large experience of auditing EU agricultural funds has recognised the difficulties arising from the latest reform of the CAP.

These difficulties with regards to auditing agriculture will surely diminish over time as SAIs become more familiar with the subject and gain more experience. However, it is the problems currently faced by SAIs which need to be resolved, by means of improved communication and greater co-operation.

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¹ www.oecd.org/gov/sigma **Support for Improvement in Governance and Management.** A joint initiative of the OECD and the European Union, principally financed by the EU.