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Annual Report on the Financial Management of the 6th-9th European Development Funds (EDFs) in 2005

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1. INTRODUCTION

The Commission's Annual Report on the Financial Management of the 6th-9th European Development Funds (EDFs) in 2005 fulfills the requirements of Articles 96, 102 and 135 of the Financial Regulation applicable to the 9th European Development Fund. Article 96 paragraph 2 states that:

'The EDF accounts shall be accompanied by a report on financial management during the preceding year containing an accurate description of:

(1) the achievement of the objectives for the financial year, in accordance with the principle of sound financial management;

(2) the financial situation and the events that had a significant influence on the activities carried out during the financial year.'

The European Development Fund (EDF) finances EC co-operation with:

- sub-Saharan Africa, the Caribbean and the Pacific under the ACP-EC partnership enshrined in the Cotonou Agreement;
- the 20 Overseas Countries and Territories (OCTs) linked constitutionally to Member states[1]; and
- European Investment Bank (EIB) programmes in ACP states.

The Cotonou Agreement forms the basis of the EU's partnership with ACP countries. EU and ACP Member States signed the agreement in 2000, and agreed to revise it every five years until it expires in 2020. They made the first such revision in 2005. A separate decision by the EU's Council of Ministers governs the partnership between the EU and the OCTs of the Member States.[2]

In addition, some of the Commission's ACP development programmes are funded outside the Cotonou Agreement, from the general EU budget. This report does not cover these programmes. They include:

- the Commission's activities in South Africa;
- thematic budget lines covering food security, democracy and human rights, and the environment; and
- support for banana producers under the Special Assistance Framework. The European Investment Bank (EIB) also funds activities in ACP states from the Investment Facility and its own resources.

Two Commission departments are responsible for devising and implementing EU development policy and programmes in ACP countries and OCTs:

- DG Development establishes policies and programming with ACP partners, and
- EuropeAid puts the policies into practice by delivering programmes and projects.

The 9th EDF took effect on 1 April 2003, once all Member States had ratified the agreement. The Commission transferred to the 9th EDF the outstanding balances from previous EDFs. The 9th EDF expires in December 2007.

[1] Annex II to the EC Treaty lists 21 Overseas Countries and Territories (OCTs). The Commission has direct relations with 20 of them, as the Overseas Association Decision does not apply to Bermuda (at its request).

[2] OJ L 314, 30 November 2001.

2. ACHIEVING THE OBJECTIVES IN 2005

The Commission set itself objectives and defined performance indicators and quantified targets for the EDFs in 2005 to measure progress in improving the:

- quality of programmes;
- speed and efficiency of their implementation; and
- functioning of control systems.

2.1. Raising programmes' and projects' quality

During 2005, the Commission stepped up its efforts to improve new programmes' quality. It submitted proposals for peer review by a Quality Support Group (QSG) involving officials from EuropeAid, DG Development and other DGs when necessary. The QSG conducts these reviews before the Commission takes its financing decisions – at the programme identification stage, early on in the project management cycle, and then again at the later technical formulation stage. In 2005, 35 QSG meetings reviewed programmes amounting to over € 3 800 million.

In 2005, the Commission increased EDF investment in education and health, infrastructure and budget support, to help achieve the Millennium Development Goals (MDGs). It also devoted EDF funds to other areas where progress is needed to achieve the MDGs - democracy, the rule of law, governance and agriculture.

In 2005, the Commission devoted the greatest share of EDF resources - 36% - to the provision of basic social services - education, health, clean water and basic sanitation. These are key to achieving the MDGs. The Commission assigned the next largest shares to budget and balance of payments support (figures include food security and Stabex operations) and to transport, communications and energy. Toegther, these three areas accounted for 84% of EDF global commitments.

EDF commitments and payments by OECD-DAC sector, 2005 (€m, gross)[3]

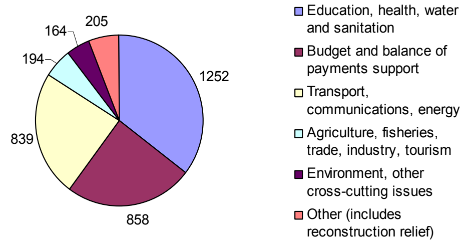
Sector	Commitments		Payments	
	€m	% of total	€m	% of total
Education, health, water, basic sanitation	1 252	36%	711	29%
Budget and balance of payments support[4]	858	24%	628	26%
Transport, communications, energy	839	24%	584	24%
Agriculture, fisheries, trade, industry, tourism	194	6%	214	9%
Environment, other cross-cutting issues	164	5%	72	3%
Other, including reconstruction relief	205	5%	248	9%
Sub-total	3 511	100%	2 456	100%
ACP-EU Peace Facility[5]			88	
Total	3 511		2 544	

[3] Reporting to the OECD DAC is provided on the basis of gross amounts. Details on the net EDF funding are provided in point 6.1 of the technical annex to this report

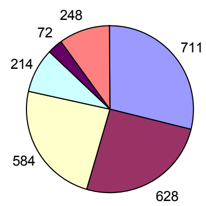
[4] According to the OECD DAC sector definitions, this sector includes in addition to budget and balance of payments support, also some types of food security and Stabex operations.

[5] The funding of the Peace Facility is not accounted as ODA (Official Development Assistance) under the OECD-DAC definitions.

Global commitments 2005 (€m, gross)



Payments 2005 (€m, gross)



To improve the sustainability and impact of its aid, the Commission continued to provide macroeconomic budget support – referred to as general budget support (GBS) - and sectoral policy support programmes (SPSPs). The share of EDF commitments comprising GBS and SPSPs continued to rise, from 18% in 2004 to 32% in 2005. The Commission approved:

- GBS in 13 countries, amounting to €705 million;
- SPSPs in 9 countries, totalling €416 million.

2.2. Delivering programmes and projects faster

The Commission continued to deliver programmes faster in 2005. This was reflected in its strong commitments and payments performance.

EDF key performance figures, 2001-05 (€m, gross)[6]

	2001	2002	2003	2004	2005
Global commitments	1 927	2 125	3 769	2 648	3 511
Individual commitments	2 488	2 436	3 062	3 038	3 057
Payments	1 779	1 922	2 345	2 464	2 544

The Commission achieved a 33% increase in global commitments in 2005 compared to 2004. The Quality Support Group helped ensure quality, while the volume of operations approved rose steadily.

After committing funds for a programme (global commitments), the Commission must then sign contracts (individual commitments) with the entities that will deliver it (government, firms, NGOs, international organisations) and then disburse funds to them (payments). The Commission achieved its second-highest level ever of individual commitments in 2005 - €3 057 - and record payments of €2 544 million.

2.3. Applying controls that meet the highest standards

The EDF is governed by its own Financial Regulation.[7]. The Commission ensures sound financial management and proper accountability by clearly dividing

[6] These figures take into account the reclassification of certain Stabex operations, for which a detailed account was submitted with the EDF Financial Management Report for 2004. Payments shown in the table above include transfers €4.4 million paid from Stabex funds, although these actually took place in 2002 and 2003.

[7] Available at: http://europa.eu.int/eur-lex/pri/en/oj/dat/2003/l_083/l_08320030401en00010031.pdf

responsibilities. One set of people manages any given programme; another audits the programme's financing and ensures it complies with the regulation.

The Financial Regulation separates responsibility for managing the fund between an authorising officer and an accounting officer:

- the authorising officer performs his/her role under section 2 of the Regulation;
- the accounting officer is an official in the Commission's budget department, acting under the rules in section 3 of the regulation.

The EDF also has its own accounting system, which the Commission is currently modernising by shifting to an accruals-based framework (ABAC).

EuropeAid made progress with its main internal control objectives, covering filing and Stabex. The Directorate responsible for EDF programmes successfully adopted new filing systems for both financial and non-financial dossiers.

3. FINANCIAL SITUATION, 6-9TH EDFS – FUNDS ALLOCATED, COMMITTED, SPENT AND UNSPENT, END 2005 (€M, NET)

The table below shows funds allocated to programmes in ACP countries and OCTs, and to the European Investment Bank's Investment Facility. Investment Facility funds from the 9th EDF are reported separately in the EIB's financial statements.

Funds allocated to ACP states (by EDF)[8]			Funds committed	Funds spent	Funds/commitments outstanding		
6th-8th	9th	Total, 6th- 9th			Funds uncommitted	Commitments unspent (RAL)	Total remaining funds unspent
a	b	c (a+b)	d	e	f (c-d)	g (d-e)	h (f+g)
29 512	14 943	44 455	38 727	28 403	5 728	10 324	16 052

4. EVENTS SIGNIFICANTLY INFLUENCING ACTIVITIES IN 2005

4.1. Backloading

The uneven spread of global commitments over the year remained a problem in 2005. The Commission committed 38% of the 2005 total by the end of September, against a target of 55%. In response, EuropeAid is monitoring the project pipeline more closely than in the past, and using the Quality Support Group to ensure deadlines are respected in addition to supporting quality.

4.2. Stabex

In 2005, the Commission laid the ground for addressing outstanding Stabex issues,[9] but this will only bear fruit in 2006 and 2007. The Commission clarified legal and budgetary issues to allow outstanding Stabex commitments to proceed.

8 Taking into account the transfers from the former EDFs into the 9th EDF.

9 Stabex is a financial instrument created by the Lomé Convention (Articles 186-212) intended to offset instability in ACP states' export earnings. The Cotonou Agreement replaced Stabex with a new instrument, Flex.

The Commission intends to commit all outstanding Stabex funds for beneficiary countries through Frameworks of Mutual Obligations (FMOs). Target deadlines are:

- FMOs approved - end 2007
- contracting - end 2008
- disbursement - end 2010.

To control Stabex funds, the Commission operates separate sets of accounts. It transfers Stabex funds from the main account into "security accounts" in Europe, which the Commission's Accounting Officer manages. When the required conditions are met, the Commission then transfers funds to "double signature accounts", which the beneficiary country's National Authorising Officer (NAO) and the Commission's Head of Delegation manage jointly.

The Commission attaches particular importance to reporting on "double signature" Stabex accounts. In 2005 it reminded NAOs that the Cotonou Agreement requires them to report regularly on Stabex. The Commission also appointed an official as overall Stabex Coordinator and plans to establish by March 2007 a database to follow up Stabex accounts more closely. In addition, delegations must include statements on the situation of Stabex accounts in their twice-yearly External Assistance Management Reports (EAMRs).

Annex 7 below comprises a statement of the balances and operations as at 31st December 2005 of Stabex "double signature accounts" and indicates reporting that remains outstanding.

4.3. Management information

The Commission's management information tools - CRIS and OLAS - do not yet provide the information needed to make fast, accurate EDF forecasts and to monitor and report on EDF performance indicators. This is in part because of incomplete data inputting. The Commission is working to replace OLAS with CRIS-EDF and to introduce a new accounting system, ABAC. Training in CRIS-EDF will also be reinforced.

4.4. Regulatory limits to co-financing

The EDF Financial Regulation limits participation in co-financing operations, so the Commission will pursue its proposal for a fast-track revision of the Financial Regulation and 9th EDF Internal Agreement.

4.5. Internal control

In 2005, EuropeAid transferred responsibility for ex-post controls to its geographic directorates. The ACP directorate recruited new staff for this task in September 2005.

The Directorate also conducted a detailed risk analysis and applied a representative sampling methodology. On this basis, it drew up its Ex-Post Control Action Plan for transactions effected in 2005, and established a target of reviewing in detail 3% of transactions completed between January and end September 2005. Progress in implementing the Action Plan at the time this report was submitted (May 2006) was as follows:

Ex-post control of transactions in Jan-end Sept. 2005 – status, May 2006		
	No. of transactions	% of total transactions, Jan-end Sept 2005
Total no .of transactions, Jan-end Sept. 2005	19 500	100%
Transactions for which controls planned	590	3%
Transactions for which controls completed/ongoing	307	1.5%

The Directorate missed its 3% target for 2005, as it took longer than expected to phase in the Action Plan. At the time this report was submitted (May 2006), the Directorate had implemented ex-post controls on 52% of the 2005 transactions it planned to analyse.

EuropeAid will use its experience of implementing ex-post controls in 2004 and 2005 to define an Action Plan for 2006 which will innovate in two areas:

- the scope of controls applied to each transaction and
- the proportion of transactions targeted for ex-post control.

4.6. Resources

To manage EDF funds, the Commission relies on staff both in EuropeAid headquarters and in Delegations. Since its reorganisation in March 2005, EuropeAid has been working at the limits of its staffing capacity, which stood at 194 people in total at end 2005. In addition, several changes of middle management staff responsible for managing the EDF took place between March and year-end.

As a result, the Commission has had to prioritise certain activities over others, leading to some slippage, for instance in:

- updating internal and external web sites;
- monitoring Stabex programmes; and
- implementating ex-post controls.

The management of EDF funds also relies on other EuropeAid directorates' resources, in particular the:

- Operations Quality Support Directorate, which helps prepare, monitor and evaluate programmes;
- two directorates providing more general support and resources for EuropeAid's operations.

Point 8 of the technical annex below discusses in more detail ACP delegations' resources situation now that EuropeAid has completed its devolution process.

An important measure of the intensity with which EuropeAid uses its resources is the number of staff that EuropeAid employs on average for every €10 million in funding which it manages. Accurately allocating "overhead" staff, and hence the precise ratio, specifically for EDF funds, is difficult. However, the ratio for EuropeAid as a whole fell by 6% between 2004 and 2005, from 4.8 to 4.5. The Commission will continue to deploy staff as efficiently as possible and order its priorities strictly in 2006.