

**Realigning Execution of the European Social Fund Budget:  
Implementing the European Commission's  
Integrated Internal Control Framework in a EU Structural Fund (A)**

The European Union (EU) is an economic and political partnership between 27 European countries aiming for peace, prosperity and freedom for almost 500 million citizens. Article 174 of the treaty on the functioning of the European Union provides that, in order to strengthen its economic and social cohesion, the Community is to aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas. Article 175 of the treaty requires this action to be supported by several instruments, including Structural Funds. The oldest structural fund is the European Social Fund (ESF), which was established in 1958, just a year after the formation of the European Economic Community, the EU's predecessor.

The ESF, like other Structural Funds, operate on a multi-annual basis, specifically a seven year period of budget execution. In the run-up to a given execution period, the European Parliament and European Council authorize Structural Fund spending by legislating the EU's Financial Programme. For the current execution period (2007-2013), authorized Structural Funds spending is approximately €300 billion, representing about a quarter of the total EU budget. The authorized ESF spending is €75 billion, equivalent to nearly 10% of the entire EU Budget.

In implementing the ESF, the EU co-finances hundreds of thousands of measures across the 27 Member States, grouped together on a geographic and policy basis as operational programmes. An operational programme begins life as a document submitted by a Member State and adopted by the Commission setting out a development strategy with a coherent set of priorities to be carried out with the aid of EU funds. Operational programmes supported by the ESF are geared to meeting future occupational and skills requirements, strengthen outplacement and worker mobility schemes, train workers to prevent and anticipate unemployment, support career guidance, and improve access to training for low skilled and older workers. The summary description of the ESF's main aim is to "help people fulfil their potential by giving them better skills and better job prospects."

The ESF budget is executed by the European Commission. The Commission's responsibility derives from Article 317 of the EU Treaty: "The Commission shall implement the budget in cooperation with the Member States...on its own responsibility and within the limits of the appropriations, having regard to the principles of sound

financial management.” The Commission’s internal arrangements include the delegation of budget execution authority to the Director General for Employment, Social Affairs, and Equal Opportunities (DG EMPL), in the first instance. The Director-General of DG EMPL, in turn, delegates budget execution authority to Heads of Unit within its geographical directorates.

The ESF is not only co-financed, but under shared management. Under Council Regulation 1083/2006, which covers all Structural Funds, “the efficient and correct implementation of operational programmes” is the responsibility of the Member States. This responsibility includes prevention, detection and correction of irregularities and infringements of European Union law. The arrangements within Member States for governance and management of operational programmes are complex and vary from country to country. The roles within Member States include managing authorities, certifying bodies, and audit authorities (see Articles 59-62). Their respective responsibilities are also specified in Council Regulation 1083/2006 in considerable detail.

In many respects, the role of DG EMPL is to “control the control” of operational programmes in the Member States. The Commission is authorized to suspend payments for an operational programme if it determines that “there is a serious deficiency in the management and control system of the programme” and “for which corrective measures have not been taken.” Using this enforcement power, however, brings political difficulties for all concerned, including the Commission. The predicament has been stated sharply by Nikolaus van der Pas, who became Director-General of DG EMPL in the first year of the 2007-2013 execution period:

We *have* to make sure the money is getting spent *very* close to people, so the system has to be highly regionalised and highly localised. We *have* to assume that errors will occur. The responsibility for control is ours. I don’t have the means to control – if I did it would be a control framework which was more expensive than the funds themselves. So, every year we will have a political fire. I am the final receiver of the blows. I find it unacceptable.

Much effort was devoted to changing the legal framework set out in Council Regulation 1083/2006, giving the Commission a stronger hand in the game of controlling the control performed by the Member States. The adoption of this legal framework set the stage for a major change in DG EMPL’s approach to controlling operational programs funded under the ESF.

### **Administrative and Political Context**

The Director General of DG EMPL is accountable to the (EC) College of Commissioners through the Commissioner with portfolio responsibility for employment, social affairs, and equal opportunities. The Director General is also accountable to the

Commission through the EC's Secretariat General (SG), DG Financial Programming and Budget (DG BUDG), and the Internal Auditing Service (IAS). Since 2002, the formal accountability process has pivoted around the preparation and scrutiny of the DG's annual activity report (AAR). The bottom line of this report is the Director General's statement of assurance. By design, this statement includes specific reservations about the control of EU budget execution, together with planned measures to redress each of them. The standards followed in preparing the management section of the AAR are set by the Central Financial Service, a directorate within DG BUDG. Compliance with these internal control standards is judged through a peer review process in which the draft form of an AAR is scrutinized by senior Commission personnel in the SG, DG BUDG, IAS, and areas related to DG EMPL. The final version of DG EMPL's AAR is made public; the SG integrates its views on this AAR into its annual synthesis report on the activities of the Commission, which also becomes a public document.

An important part of the DG EMPL's context during 2005-2006 was the Commission's Action Plan toward an Integrated Internal Control Framework (IICF). The IICF Action Plan emerged as a response to a 2004 political decision by the College of Commissioners, presided over by José Manuel Barroso, to reverse the long-standing pattern of negative audit opinions on EU budget execution issued by the European Court of Auditors (ECA) in its annual reports. Siim Kallas, Vice President of the Commission for Administration, Audit, and Anti-Fraud, decided to tackle the long-simmering issue of the Commission's competence and performance in controlling execution of the EU budget, as he prepared for hearings with the European Parliament's Committee on Budgetary Control, following his nomination by Barroso in September 2004. The budget control issue had been revived with each well-publicized negative ECA audit opinion about the legality and regularity of the transactions through which the EU budget is executed. ECA audit opinions provided grist for the mill of the annual budget discharge procedure by which the European Parliament (EP), under the EU Treaty, holds the Commission to account for budget execution – with potentially catastrophic political consequences in the event the EP does not grant the discharge. In this panorama, the Barroso College followed Kallas's lead in proclaiming its political objective for the Commission to receive a positive Declaration of Assurance (DAS) from the ECA before its own mandate was completed at the end of 2008.

The IICF Action Plan was the Commission's chosen means to act on this political commitment. Integrated internal control had become a firmly established normative approach to corporate governance within the accounting and auditing professions more than a decade earlier, with a major referent point known as the COSO standards. A low profile element of the Commission's dramatic management reform undertaken in the 2000-2003 period was the promulgation by DG BUDG of internal control standards, patterned on the COSO version. Some DG's were known to have been successful in complying with many of these internal control standards, but not those responsible for the Structural Funds and actions external to the EU. As it emerged in 2004-5, the IICF Action Plan translated the Commission's integrated internal control approach as applied

to direct management activities into analogous planned measures for controlling the co-financed and co-managed operational programmes of EU Structural Funds, including ESF. Commission officials – including representatives from DG EMPL -- worked to implement this integrated internal control framework as it participated in writing legislation that became Council Regulation 1083/2006.

A time of reckoning followed the DAS opinion on the 2006 budget, which was the first budget to have been both formulated and executed by the Barroso Commission. While the DAS opinion on the 2006 budget was unproblematic for many areas of EU spending, the structural funds were not among them. The ECA opinion stated that deficiencies in the legality and regularity of ESF-related transactions far surpassed the materiality threshold in 2006. Some 12 percent of the ESF budget was put into question by the ECA.

The negative DAS opinion for the ESF contributed to the rocky ride travelled by the Commission during the annual budget discharge procedure that transpired in early 2008. Fears erupted that the Parliamentary Committee on Budget Control (COCOBU) would recommend withholding the budget discharge. This near-death experience for the Barroso Commission sparked a redoubling of efforts to modify ESF budget execution, with a view to achieving less unfavourable DAS audit opinions and more straightforward budget discharge procedures.

### **Governance of DG EMPL's execution of the ESF**

Council Regulation 1083/2006 was the outcome of a lengthy legislative process. In the words of one active member of the Commission's negotiating committee from DG EMPL:

The Commission generally makes the legislative proposals 2 ½ to three years in advance of the upcoming financial programming period (2007-2013). The legislation was being adjusted to try and cope with some of the difficulties in the previous round (1999-2006). Some of the proposals of the Commission were accepted and some of them weren't.

The previous Council regulation for Structural Funds, 1260/1999, was repealed with the enactment of 1083/2006. An unprecedented feature of the new legislation was Title VI, "Management, Monitoring, and Controls." Its first chapter concerned management and control systems within Member States. This chapter outlined the roles and functions of each part of such control systems, including managing authorities, certifying authorities, and audit authorities. The functional goals of the systems in Member States were also enumerated. These included ensuring the correctness and regularity of expenditure declared under the operational programme (Article 58).

Chapter II of Council Regulation 1083/2006's Title VI concerned monitoring of operational programmes. Article 67 imposed a duty on managing authorities to prepare an "annual report" on the "implementation" of each operational programme, for submission to

the Commission. The reporting requirements to be satisfied by the annual report were extensive and detailed. Article 68 called upon the Commission to scrutinize annual reports on implementation. The same article called upon the Commission to provide written feedback to the managing authority as the agent of the Member State. A final provision of Article 68 was for Member States to inform the Commission of how they followed up on the comments.

The annual reporting requirement imposed on Member States bears a striking resemblance to the requirement that the Commission's own directorates-general report annually, in the form of an "annual activity report," subject to scrutiny by other power centres within the institution. Council Regulation 1083/2006 may be seen as mimicking the way DG EMPL itself was controlled within the Commission. In this sense, Chapter II was put in place as a cornerstone of an integrated internal control framework whose reach included not only the Commission, but key roles within the operational programmes of Member States.

Any operational programme is a time-limited venture, with a beginning, middle, and end. Title VI of the same chapter in Council Regulation 1083/2006 outlined novel steps to be followed during the start-up phase, specifically following the point where the Commission has adopted a Member State's operational programme. For each operational programme, the first steps included a description and assessment of its management control and auditing systems, together with an "opinion" about their adequacy by the respective Member State. Article 71 made clear that this opinion sent to the Commission should be drawn up by an entity considered independent from managing authorities. The opinion, which was also referred to as a compliance assessment, was also to be based on internationally accepted audit standards. The two provisions, together, implied that compliance assessments would resemble professional audit opinions. Article 71 suggested that such opinions could point out aspects of a programme's control and audit systems that were considered inadequate, in relation to relevant standards. In other words, Article 71 permitted Member States to qualify their assurances about an operational programme's control and auditing systems, in the form of reservations. The reservations, then, were to provide an initial baseline for an iterative process intended to bring a management and auditing system for an operational programme into compliance with relevant standards:

If the opinion contains reservations, the report shall indicate the seriousness of the shortcoming....The Member State shall inform the Commission of the corrective measures to be taken and the timetable for their implementation and subsequently provide confirmation of the implementation of the measures and the withdrawal of the corresponding reservations.

The same regulatory provision called upon the Commission to respond to Member States' submissions of compliance assessments in the form of "observations." The language intimated that observations could refer not only to the stated reservations, but also to other matters that the Commission wished to raise (for example, taking account of audit opinions issued by the ECA).

Once the Commission's observations had been communicated, the ball returned to the court of the Member State. The follow-on steps within the iterative start-up phase of an operational programme were not specifically laid out in the legislation. However, Article 71 indicated that the iterative process would come to an end "in the absence of observations by the Commission." Crucially, the clear implication was that the Commission would not make the first interim payment to Member States for a given operational programme until it was satisfied by the actions taken in response to its observations.

Title VII of the 2006 Council regulation, entitled Financial Management, replaced a title in Council regulation 1260/1999 with the same name. This Title dealt with such matters as suspension of payments and financial corrections, two of the established means by which the Commission could penalize Member States for what it deemed as unacceptable departures from sound financial management of an operational programme. Article 91, a new provision within Title VII, gave the Commission conditional authority to interrupt payments, relative to a pre-established schedule, for up to six months. The same article also mandated that the Member State and the certifying authority be informed immediately of the reasons for the interruption and that the interruption end as soon as the necessary measures have been taken by the Member State. Article 91 specified that the authority to interrupt payments was to rest with authorising officers by delegation, a role played in the case of DG EMPL by the director-general. In other terms, interruption of payments, unlike suspension of payments, did not require approval by the College of Commissioners. In this sense, the hand of DG EMPL was strengthened, relative to the situation that prevailed during the 2000-2006 execution period under Council regulation 1260/1999.

Title VII also dealt with the Commission's most lethal enforcement mechanism, financial corrections. This established mechanism allows the Commission to demand that funds already disbursed to Member States be returned, if it no longer accepts the Member State's assurances that the operational programme is under control. Article 99 laid out the conditions under which the Commission would be within its rights to conduct a "correction procedure." Its sister provision, Article 100, on the procedure itself, put down specific time-frames within which actions needed to be completed as part of a financial correction procedure. For instance, when a Member State is informed of the Commission's provisional conclusions, it is requested to submit its comments within two months. Once the Commission and the Member State came to an agreement on the terms of reference for the procedure, the Member State would be given two more months to complete its examination. The time-frames for hearings and other optional steps in the procedure were also spelled out. For example, the article stated that the Commission shall take a decision on the financial correction within six months of the date of a hearing, if one were to be held.

Whether the legal infrastructure of Council regulation 1083/2006 would influence execution of the ESF budget during the 2007-13 period was not entirely pre-ordained. Much would depend on how DG EMPL incorporated this legal infrastructure into its functioning as an organization.

## Appendix 1

Excerpts from **COUNCIL REGULATION (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999**

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:210:0025:0025:EN:PDF>

(1) Article 158 of the Treaty provides that, in order to strengthen its economic and social cohesion, the Community is to aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas. Article 159 of the Treaty requires this action to be supported by the Structural Funds, the European Investment Bank (EIB) and the other existing Financial Instruments.

(7) The Funds providing assistance under the cohesion policy are therefore limited to the European Regional Development Fund (ERDF), the European Social Fund (ESF) and the Cohesion Fund. The rules applicable to each Fund are to be specified in implementing regulations adopted under Articles 148, 161 and 162 of the Treaty.

(23) Action by the Community should be complementary to that carried out by Member States or seek to contribute to it. The partnership should be strengthened through arrangements for the participation of various types of partner, in particular regional and local authorities, with full regard to the institutional arrangements of the Member States.

(24) Multiannual programming should be directed towards achieving the Funds' objectives by ensuring the availability of the necessary financial resources and the consistency and continuity of joint action by the Community and the Member States.

(28) Under Article 274 of the Treaty, in the context of shared management, the conditions allowing the Commission to exercise its responsibilities for implementation of the general budget of the European Union should be specified and the responsibilities of cooperation by the Member States clarified. Applying these conditions should enable the Commission to satisfy itself that Member States are using the Funds in a legal and regular manner and in accordance with the principle of sound financial management within the meaning of the Financial Regulation.

(38) The programming and management of the Structural Funds should be simplified having regard to their specific features by providing for operational programmes to be financed by either the ERDF or the ESF, with each being able to finance in a complementary and limited fashion actions which fall under the scope of the other Fund.

(60) In accordance with the principle of subsidiarity and subject to exceptions provided for in Regulation (EC) No 1080/2006 of the European Parliament and of the Council of 5 July 2006 on the European Regional Development Fund (1), Regulation (EC) No 1081/2006 of the European Parliament and of the Council of 5 July 2006 on the European Social Fund (2) and Council Regulation (EC) No 1084/2006 of 11 July 2006 on the Cohesion Fund (3), there should be national rules on the eligibility of expenditure.

(62) Member States should adopt adequate measures to guarantee the proper functioning of their management and control systems. To this end, it is necessary to establish the general

principles and the necessary functions which the control systems of all operational programmes are to fulfil on the basis of the body of Community law in force for the programming period 2000 to 2006.

(63) It is therefore necessary to designate a single managing authority for each operational programme and to clarify its responsibilities as well as the functions of the audit authority. It is also necessary to guarantee uniform quality standards for the certification of expenditures and of payment requests before they are sent to the Commission. It is necessary to clarify the nature and based and, to this end, to establish the functions of the certifying authority.

(64) Monitoring of operational programmes is necessary to ensure the quality of their implementation. To this end, monitoring committees should be set up and their responsibilities defined, together with the information to be transmitted to the Commission and the framework for examining that information. In order to improve the exchange of information on the implementation of operational programmes, the principle of exchange of data by electronic means should be established.

(65) In accordance with the principles of subsidiarity and proportionality, Member States should have the primary responsibility for the implementation and control of the interventions.

(66) The obligations on the Member States as regards management and control systems, the certification of expenditure, and the prevention, detection and correction of irregularities and infringements of Community law should be specified to guarantee the efficient and correct implementation of operational programmes. In particular, concerning management and control, it is necessary to establish the procedures by which Member States give the assurance that the systems are in place and function satisfactorily.

(67) Without prejudice to the Commission's powers as regards financial control, cooperation between the Member States and the Commission in this field should be increased and criteria should be established which allow the Commission to determine, in the context of its strategy of control of national systems, the level of assurance it can obtain from national audit bodies.

(70) In addition to the suspension of payments where a serious deficiency is detected in the management and control systems, there should be measures allowing the authorising officer by delegation to interrupt payments where there is evidence to suggest a significant deficiency in the sound operation of these systems.

## TITLE I

### OBJECTIVES AND GENERAL RULES ON ASSISTANCE

#### CHAPTER I

##### *Scope and definitions*

##### *Article 1*

##### **Subject matter**

This Regulation lays down the general rules governing the European Regional Development Fund (ERDF), the European Social Fund (ESF) (hereinafter referred to as the Structural Funds) and the Cohesion Fund...

This Regulation lays down the principles and rules on partnership, programming, evaluation, management, including financial management, monitoring and control on the basis of responsibilities shared between the Member States and the Commission.

#### *Article 2*

### **Definitions**

For the purposes of this Regulation, the following terms shall have the meanings assigned to them here:

(1) 'operational programme': document submitted by a Member State and adopted by the Commission setting out a development strategy with a coherent set of priorities to be carried out with the aid of a Fund, or, in the case of the Convergence objective, with the aid of the Cohesion Fund and the ERDF;

(2) 'priority axis': one of the priorities of the strategy in an operational programme comprising a group of operations which are related and have specific measurable goals;

(3) 'operation': a project or group of projects selected by the managing authority of the operational programme concerned or under its responsibility according to criteria laid down by the monitoring committee and implemented by one or more beneficiaries allowing achievement of the goals of the priority axis to which it relates;

(4) 'beneficiary': an operator, body or firm, whether public or private, responsible for initiating or initiating and implementing operations. In the context of aid schemes under Article 87 of the Treaty, beneficiaries are public or private firms carrying out an individual project and receiving public aid;

(7) 'irregularity': any infringement of a provision of Community law resulting from an act or omission by an economic operator which has, or would have, the effect of prejudicing the general budget of the European Union by charging an unjustified item of expenditure to the general budget.

#### *CHAPTER IV*

### ***Principles of assistance***

#### *Article 10*

### **Programming**

The objectives of the Funds shall be pursued in the framework of a multiannual programming system organised in several stages comprising the identification of the priorities, the financing, and a system of management and control.

#### *Article 14*

### **Shared management**

1. The budget of the European Union allocated to the Funds shall be implemented within the framework of shared management between the Member States and the Commission, in accordance with Article 53(1)(b) of Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities (1), with the exception of the technical assistance referred to in Article 45 of this Regulation.

The principle of sound financial management shall be applied in accordance with Article 48(2) of Regulation (EC, Euratom) No 1605/2002.

2. The Commission shall exercise its responsibility for implementing the general budget of the European Union in the following ways:

(a) the Commission shall check the existence and proper functioning of management and control systems in the Member States in accordance with the procedures described in Articles 71, 72 and 73;

(b) the Commission shall interrupt the payment deadline or suspend all or part of payments in accordance with Articles 91 and 92 if the national management and control systems fail, and shall apply any other financial correction required, in accordance with the procedures described in Articles 100 and 101;

(c) the Commission shall check reimbursements of payments on account and automatically decommit budget commitments in accordance with the procedures laid down in Article 82(2) and Articles 93 to 97.

## CHAPTER V

### *Financial framework*

1. The resources available for commitment from the Funds for the period 2007 to 2013 shall be EUR 308 041 000 000 at 2004 prices in accordance with the annual breakdown shown in Annex I.

#### *Article 20*

### **Resources for the Regional competitiveness and employment objective**

Overall resources for the Regional competitiveness and employment objective shall amount to 15,95 % of the resources referred to in Article 18(1) (i.e. a total of EUR 49 127 784 318) and shall be distributed between the different components.

## TITLE III

## **PROGRAMMING**

### CHAPTER I

### *General provisions on the structural funds and the cohesion Fund*

#### *Article 32*

### **Preparation and approval of operational programmes**

1. The activities of the Funds in the Member States shall take the form of operational programmes within the national strategic reference framework. Each operational programme shall cover a period between 1 January 2007 and 31 December 2013. An operational programme shall cover only one of the three objectives referred to in Article 3, save as otherwise agreed between the Commission and the Member State.

2. Each operational programme shall be drawn up by the Member State or any authority designated by the Member State, in cooperation with the partners referred to in Article 11.

3. The Member State shall submit a proposal for an operational programme to the Commission containing all the components referred to in Article 37 as soon as possible but no later than five

months following the adoption of the Community strategic guidelines on cohesion, as referred to in Article 26.

4. The Commission shall appraise the proposed operational programme to determine whether it contributes to the goals and priorities of the national strategic reference framework and the Community strategic guidelines on cohesion. Where the Commission, within two months following the receipt of the operational programme, considers that an operational programme does not contribute to the achievement of the objectives of the national strategic reference framework and the Community strategic guidelines on cohesion, it may invite the Member State to provide all necessary additional information and, where appropriate, to revise the proposed programme accordingly.

5. The Commission shall adopt each operational programme as soon as possible but no later than four months following its formal submission by the Member State and not before 1 January 2007.

## CHAPTER II

### *Programming content*

#### Section 1

#### **Operational programmes**

##### *Article 37*

#### **Operational programmes for the Convergence and Regional competitiveness and employment objectives**

1. Operational programmes relating to the Convergence and Regional competitiveness and employment objectives shall contain:

(g) the implementing provisions for the operational programme, including:

- (i) designation by the Member State of all the entities referred to in Article 59 or, if the Member State exercises the option provided for in Article 74, the designation of other bodies and procedures in accordance with the rules laid down in Article 74;
- (ii) a description of the monitoring and evaluation systems;
- (iii) information about the competent body for receiving the payments made by the Commission and the body or bodies responsible for making payments to the beneficiaries;
- (iv) a definition of the procedures for the mobilisation and circulation of financial flows in order to ensure their transparency;
- (v) the elements aiming at ensuring the publicity and the information of the operational programme as referred to in Article 69;
- (vi) a description of the procedures agreed between the Commission and the Member State for the exchange of computerised data to meet the payment, monitoring and evaluation requirements laid down by this Regulation;

#### Section 3

#### **Global grants**

##### *Article 42*

## **General provisions**

1. The Member State or the managing authority may entrust the management and implementation of a part of an operational programme to one or more intermediate bodies, designated by the Member State or the managing authority, including local authorities, regional development bodies or non-governmental organisations, in accordance with the provisions of an agreement concluded between the Member State or the managing authority and that body. Such delegation shall be without prejudice to the financial responsibility of the managing authority and of the Member States.

2. The intermediate body responsible for managing the global grant shall provide guarantees of its solvency and competence in the domain concerned as well as in administrative and financial management. It shall as a general rule be established or represented in the region or regions covered by the operational programme at the moment of its designation.

*Article 43*

## **Implementing rules**

The agreement referred to in the first subparagraph of Article 42(1) shall detail in particular:

- (a) the types of operation to be covered by the global grant;
- (b) the criteria for selecting beneficiaries;
- (c) the rates of assistance from the Funds and the rules governing that assistance, including as regards the use of any interest accruing;
- (d) the arrangements for monitoring, evaluating and ensuring the financial control of the global grant referred to in Article 59(1) vis-à-vis the managing authority, including the arrangements for recovering amounts unduly paid and the presentation of accounts;
- (e) where applicable, any use of a financial guarantee or equivalent facility, unless the Member State or the managing authority provides such guarantee according to the institutional arrangements of each Member State.

TITLE VI

## **MANAGEMENT, MONITORING AND CONTROLS**

### *CHAPTER I*

#### ***Management and control systems***

*Article 58*

#### **General principles of the management and control systems**

The management and control systems of operational programmes set up by Member States shall provide for:

- (a) the definition of the functions of the bodies concerned in management and control and the allocation of functions within each body;
- (b) compliance with the principle of separation of functions between and within such bodies;
- (c) procedures for ensuring the correctness and regularity of expenditure declared under the operational programme;

- (d) reliable accounting, monitoring and financial reporting systems in computerised form;
- (e) a system of reporting and monitoring where the responsible body entrusts the execution of tasks to another body;
- (f) arrangements for auditing the functioning of the systems;
- (g) systems and procedures to ensure an adequate audit trail;
- (h) reporting and monitoring procedures for irregularities and for the recovery of amounts unduly paid.

*Article 59*

**Designation of authorities**

1. For each operational programme the Member State shall designate the following:

- (a) a managing authority: a national, regional or local public authority or a public or private body designated by the Member State to manage the operational programme;
- (b) a certifying authority: a national, regional or local public authority or body designated by the Member State to certify statement of expenditure and applications for payment before they are sent to the Commission;
- (c) an audit authority: a national, regional or local public authority or body, functionally independent of the managing authority and the certifying authority, designated by the Member State for each operational programme and responsible for verifying the effective functioning of the management and control system.

The same authority may be designated for more than one operational programme.

2. The Member State may designate one or more intermediate bodies to carry out some or all of the tasks of the managing or certifying authority under the responsibility of that authority.

3. The Member State shall lay down rules governing its relations with the authorities referred to in paragraph 1 and their relations with the Commission.

Without prejudice to this Regulation, the Member State shall lay down the mutual relations between the authorities referred to in paragraph 1, which shall carry out their tasks in full accordance with the institutional, legal and financial systems of the Member State concerned.

4. Subject to Article 58(b), some or all of the authorities referred to in paragraph 1 may be part of the same body.

5. Specific rules on management and control are laid down in the Regulation (EC) No 1080/2006 for operational programmes under the European territorial cooperation objective.

6. The Commission shall adopt implementing rules of Articles 60, 61 and 62 in accordance with the procedure referred to in Article 103(3).

*Article 60*

**Functions of the managing authority**

The managing authority shall be responsible for managing and implementing the operational programme in accordance with the principle of sound financial management and in particular for:

- (a) ensuring that operations are selected for funding in accordance with the criteria applicable to the operational programme and that they comply with applicable Community and national rules for the whole of their implementation period;
- (b) verifying that the co-financed products and services are delivered and that the expenditure declared by the beneficiaries for operations has actually been incurred and complies with Community and national rules; verifications on-the-spot of individual operations may be carried out on a sample basis in accordance with the detailed rules to be adopted by the Commission in accordance with the procedure referred to in Article 103(3);
- (c) ensuring that there is a system for recording and storing in computerised form accounting records for each operation under the operational programme and that the data on implementation necessary for financial management, monitoring, verifications, audits and evaluation are collected;
- (d) ensuring that beneficiaries and other bodies involved in the implementation of operations maintain either a separate accounting system or an adequate accounting code for all transactions relating to the operation without prejudice to national accounting rules;
- (e) ensuring that the evaluations of operational programmes referred to in Article 48(3) are carried out in accordance with Article 47;
- (f) setting up procedures to ensure that all documents regarding expenditure and audits required to ensure an adequate audit trail are held in accordance with the requirements of Article 90;
- (g) ensuring that the certifying authority receives all necessary information on the procedures and verifications carried out in relation to expenditure for the purpose of certification;
- (h) guiding the work of the monitoring committee and providing it with the documents required to permit the quality of the implementation of the operational programme to be monitored in the light of its specific goals;
- (i) drawing up and, after approval by the monitoring committee, submitting to the Commission the annual and final reports on implementation;
- (j) ensuring compliance with the information and publicity requirements laid down in Article 69;
- (k) providing the Commission with information to allow it to appraise major projects.

#### *Article 61*

#### **Functions of the certifying authority**

The certifying authority of an operational programme shall be responsible in particular for:

- (a) drawing up and submitting to the Commission certified statements of expenditure and applications for payment;
- (b) certifying that:
  - (i) the statement of expenditure is accurate, results from reliable accounting systems and is based on verifiable supporting documents;

- (ii) the expenditure declared complies with applicable Community and national rules and has been incurred in respect of operations selected for funding in accordance with the criteria applicable to the programme and complying with Community and national rules;
- (c) ensuring for the purposes of certification that it has received adequate information from the managing authority on the procedures and verifications carried out in relation to expenditure included in statements of expenditure;
- (d) taking account for certification purposes of the results of all audits carried out by or under the responsibility of the audit authority;
- (e) maintaining accounting records in computerised form of expenditure declared to the Commission;
- (f) keeping an account of amounts recoverable and of amounts withdrawn following cancellation of all or part of the contribution for an operation. Amounts recovered shall be repaid to the general budget of the European Union prior to the closure of the operational programme by deducting them from the next statement of expenditure.

#### *Article 62*

#### **Functions of the audit authority**

1. The audit authority of an operational programme shall be responsible in particular for:

- (a) ensuring that audits are carried out to verify the effective functioning of the management and control system of the operational programme;
- (b) ensuring that audits are carried out on operations on the basis of an appropriate sample to verify expenditure declared;
- (c) presenting to the Commission within nine months of the approval of the operational programme an audit strategy covering the bodies which will perform the audits referred to under points (a) and (b), the method to be used, the sampling method for audits on operations and the indicative planning of audits to ensure that the main bodies are audited and that audits are spread evenly throughout the programming period.

Where a common system applies to several operational programmes, a single audit strategy may be submitted;

(d) by 31 December each year from 2008 to 2015:

- (i) submitting to the Commission an annual control report setting out the findings of the audits carried out during the previous 12 month-period ending on 30 June of the year concerned in accordance with the audit strategy of the operational programme and reporting any shortcomings found in the systems for the management and control of the programme. The first report to be submitted by 31 December 2008 shall cover the period from 1 January 2007 to 30 June 2008. The information concerning the audits carried out after 1 July 2015 shall be included in the final control report supporting the closure declaration referred to in point (e);
- (ii) issuing an opinion, on the basis of the controls and audits that have been carried out under its responsibility, as to whether the management and control system functions effectively, so as to provide a reasonable assurance that statements of expenditure presented

to the Commission are correct and as a consequence reasonable assurance that the underlying transactions are legal and regular;

(iii) submitting, where applicable under Article 88, a declaration for partial closure assessing the legality and regularity of the expenditure concerned.

When a common system applies to several operational programmes, the information referred to in point (i) may be grouped in a single report, and the opinion and declaration issued under points (ii) and (iii) may cover all the operational programmes concerned;

(e) submitting to the Commission at the latest by 31 March 2017 a closure declaration assessing the validity of the application for payment of the final balance and the legality and regularity of the underlying transactions covered by the final statement of expenditure, which shall be supported by a final control report.

2. The audit authority shall ensure that the audit work takes account of internationally accepted audit standards.

3. Where the audits and controls referred to in paragraph 1(a) and (b) are carried out by a body other than the audit authority, the audit authority shall ensure that such bodies have the necessary functional independence.

4. The Commission shall provide its comments on the audit strategy presented under paragraph 1(c) no later than three months from receipt thereof. In the absence of comments within this period it shall be considered to be accepted.

## CHAPTER II

### *Monitoring*

#### *Article 63*

#### **Monitoring committee**

1. The Member State shall set up a monitoring committee for each operational programme, in agreement with the managing authority, within three months from the date of the notification to the Member State of the decision approving the operational programme. A single monitoring committee may be set up for several operational programmes.

2. Each monitoring committee shall draw up its rules of procedure within the institutional, legal and financial framework of the Member State concerned and adopt them in agreement with the managing authority in order to exercise its missions in accordance with this Regulation.

#### *Article 64*

#### **Composition**

1. The monitoring committee shall be chaired by a representative of the Member State or the managing authority. Its composition shall be decided by the Member State in agreement with the managing authority.

2. At its own initiative or at the request of the monitoring committee, a representative of the Commission shall participate in the work of the monitoring committee in an advisory capacity.

A representative of the EIB and the EIF may participate in an advisory capacity for those operational programmes to which the EIB or the EIF makes a contribution.

*Article 65***Tasks**

The monitoring committee shall satisfy itself as to the effectiveness and quality of the implementation of the operational programme, in accordance with the following provisions:

- (a) it shall consider and approve the criteria for selecting the operations financed within six months of the approval of the operational programme and approve any revision of those criteria in accordance with programming needs;
- (b) it shall periodically review progress made towards achieving the specific targets of the operational programme on the basis of documents submitted by the managing authority;
- (c) it shall examine the results of implementation, particularly the achievement of the targets set for each priority axis and the evaluations referred to in Article 48(3);
- (d) it shall consider and approve the annual and final reports on implementation referred to in Article 67;
- (e) it shall be informed of the annual control report, or of the part of the report referring to the operational programme concerned, and of any relevant comments the Commission may make after examining that report or relating to that part of the report;
- (f) it may propose to the managing authority any revision or examination of the operational programme likely to make possible the attainment of the Funds' objectives referred to in Article 3 or to improve its management, including its financial management;
- (g) it shall consider and approve any proposal to amend the content of the Commission decision on the contribution from the Funds.

*Article 66***Arrangements for monitoring**

1. The managing authority and the monitoring committee shall ensure the quality of the implementation of the operational programme.
2. The managing authority and the monitoring committee shall carry out monitoring by reference to financial indicators and the indicators referred to in Article 37(1)(c) specified in the operational programme.

Where the nature of the assistance permits, statistics shall be broken down by sex and by the size of the recipient undertakings.

3. Data exchange between the Commission and the Member States for this purpose shall be carried out electronically, in accordance with the implementing rules of this Regulation adopted by the Commission in accordance with the procedure referred to in Article 103(3).

*Article 67***Annual report and final report on implementation**

1. For the first time in 2008 and by 30 June each year, the managing authority shall send the Commission an annual report and by 31 March 2017 a final report on the implementation of the operational programme.

2. The reports referred to in paragraph 1 shall include the following information in order to obtain a clear view of the implementation of the operational programme:

(a) the progress made in implementing the operational programme and priority axes in relation to their specific, verifiable targets, with a quantification, wherever and whenever they lend themselves to quantification, using the indicators referred to in Article 37(1)(c) at the level of the priority axis;

(b) the financial implementation of the operational programme, detailing for each priority axis:

(i) the expenditure paid out by the beneficiaries included in applications for payment sent to the managing authority and the corresponding public contribution;

(ii) the total payments received from the Commission and quantification of the financial indicators referred to in Article 66(2); and

(iii) the expenditure paid out by the body responsible for making payments to the beneficiaries.

Where appropriate, financial implementation in areas receiving transitional support shall be presented separately within each operational programme;

(c) for information purposes only, the indicative breakdown of the allocation of Funds by categories, in accordance with the implementation rules adopted by the Commission in accordance with the procedure referred to in Article 103(3);

(d) the steps taken by the managing authority or the monitoring committee to ensure the quality and effectiveness of implementation, in particular:

(i) monitoring and evaluation measures, including data collection arrangements;

(ii) a summary of any significant problems encountered in implementing the operational programme and any measures taken, including the response to comments made under Article 68(2) where appropriate;

(iii) the use made of technical assistance;

(e) the measures taken to provide information on and publicise the operational programme;

(f) information about significant problems relating to compliance with Community law which have been encountered in the implementation of the operational programme and the measures taken to deal with them;

(g) where appropriate, the progress and financing of major projects;

(h) the use made of assistance released following cancellation as referred to in Article 98(2) to the managing authority or to another public authority during the period of implementation of the operational programme;

(i) cases where a substantial modification has been detected under Article 57.

The breadth of information transmitted to the Commission shall be proportional to the total amount of expenditure of the operational programme concerned. Where appropriate, such information may be provided in summary form.

Information referred to in points (d), (g), (h) and (i) shall not be included if there has been no significant modification since the previous report.

3. The reports referred to in paragraph 1 shall be judged admissible where they contain all the appropriate information listed in paragraph 2. The Commission shall inform the Member State on the admissibility of the annual report within 10 working days from the date of its receipt.

4. The Commission shall inform the Member State of its opinion on the content of an admissible annual report on implementation submitted by the managing authority within two months from the date of receipt. For the final report on an operational programme, the time limit shall be a maximum of five months from the date of receipt of an admissible report. If the Commission does not respond within the time limit laid down, the report shall be deemed to be accepted.

#### *Article 68*

### **Annual examination of programmes**

1. Every year, when the annual report on implementation referred to in Article 67 is submitted, the Commission and the managing authority shall examine the progress made in implementing the operational programme, the principal results achieved over the previous year, the financial implementation and other factors with a view to improving implementation.

Any aspects of the operation of the management and control system raised in the last annual control report, referred to in Article 62(1)(d)(i), may also be examined.

2. After the examination referred to in paragraph 1, the Commission may make comments to the Member State and the managing authority, which shall inform the monitoring committee thereof. The Member State shall inform the Commission of the action taken in response to those comments.

3. When the *ex post* evaluations of assistance granted over the 2000 to 2006 programming period, where appropriate, are available, the overall results may be examined in the next annual examination.

## *CHAPTER IV*

### ***Responsibilities of Member States and of the Commission***

#### Section 1

### **Responsibilities of Member States**

#### *Article 70*

### **Management and control**

1. Member States shall be responsible for the management and control of operational programmes, in particular through the following measures:

- (a) ensuring that management and control systems for operational programmes are set up in accordance with Articles 58 to 62 and function effectively;
- (b) preventing, detecting and correcting irregularities and recovering amounts unduly paid together with interest on late payments where appropriate. They shall notify these to the

Commission and keep the Commission informed of the progress of administrative and legal proceedings.

2. When amounts unduly paid to a beneficiary cannot be recovered, the Member State shall be responsible for reimbursing the amounts lost to the general budget of the European Union, when it is established that the loss has been incurred as a result of fault or negligence on its part.

3. The implementing rules for paragraphs 1 and 2 shall be adopted by the Commission in accordance with the procedure referred to in Article 103(3).

#### *Article 71*

#### **Setting up of management and control systems**

1. Before the submission of the first interim application for payment or at the latest within twelve months of the approval of each operational programme, the Member States shall submit to the Commission a description of the systems, covering in particular the organisation and procedures of:

(a) the managing and certifying authorities and intermediate bodies;

(b) the audit authority and any other bodies carrying out audits under its responsibility.

2. The description referred to in paragraph 1 shall be accompanied by a report setting out the results of an assessment of the systems set up and giving an opinion on their compliance with Articles 58 to 62. If the opinion contains reservations, the report shall indicate the seriousness of the shortcomings and, where the shortcomings do not concern the whole programme, the priority axis or axes concerned. The Member State shall inform the Commission of the corrective measures to be taken and the timetable for their implementation and subsequently provide confirmation of the implementation of the measures and the withdrawal of the corresponding reservations.

The report referred to in the first subparagraph shall be deemed to be accepted, and the first interim payment shall be made, in the following circumstances:

(a) within two months of the date of receipt of the report when the opinion referred to in the first subparagraph is without reservations and in the absence of observations by the Commission;

(b) if the opinion contains reservations, upon confirmation to the Commission that corrective measures concerning key elements of the systems have been implemented, and the corresponding reservations withdrawn, and in the absence of observations by the Commission within two months of the date of confirmation. Where the reservations concern only a single priority axis, the first interim payment shall be made as regards the other priority axes of the operational programme for which there is no reservation.

3. The report and the opinion referred to in paragraph 2 shall be drawn up by the audit authority or by a public or private body functionally independent of the managing and certifying authorities, which shall carry out its work taking account of internationally accepted audit standards.

4. Where a common system applies to several operational programmes, a description of the common system may be notified under paragraph 1 accompanied by a single report and opinion under paragraph 2.

5. The implementing rules for paragraphs 1 to 4 shall be adopted by the Commission in accordance with the procedure referred to in Article 103(3).

## Section 2

### **Responsibilities of the Commission**

#### *Article 72*

### **Responsibilities of the Commission**

1. The Commission shall satisfy itself in accordance with the procedure laid down in Article 71 that the Member States have set up management and control systems that comply with Articles 58 to 62 and, on the basis of the annual control reports and annual opinion of the audit authority and its own audits, that the systems function effectively during the periods of implementation of operational programmes.

2. Without prejudice to audits carried out by Member States, Commission officials or authorised Commission representatives may carry out on-the-spot audits to verify the effective functioning of the management and control systems, which may include audits on operations included in operational programmes, with a minimum of 10 working days' notice, except in urgent cases. Officials or authorised representatives of the Member State may take part in such audits. The implementing rules of this Regulation concerning the use of data collected during audits shall be adopted by the Commission in accordance with the procedure referred to in Article 103(3). Commission officials or authorised Commission representatives, duly empowered to carry out on-the-spot audits, shall have access to the books and all other documents, including documents and metadata drawn up or received and recorded on an electronic medium, relating to expenditure financed by the Funds. The aforementioned powers of audit shall not affect the application of national provisions which reserve certain acts for agents specifically designated by national legislation. Authorised Commission representatives shall not take part, *inter alia*, in home visits or the formal questioning of persons within the framework of the national legislation of the Member State concerned. However, they shall have access to information thus obtained.

3. The Commission may require a Member State to carry out an on-the-spot audit to verify the effective functioning of systems or the correctness of one or more transactions. Commission officials or authorised Commission representatives may take part in such audits.

#### *Article 73*

### **Cooperation with the audit authorities of the Member States**

1. The Commission shall cooperate with the audit authorities of operational programmes to coordinate their respective audit plans and audit methods and shall immediately exchange the results of audits carried out on management and control systems in order to make the best possible use of resources and to avoid unjustified duplication of work.

In order to facilitate this cooperation in cases where a Member State designates several audit authorities, the Member State may designate a coordination body. The Commission and the audit authorities, and the coordination body, where such a body has been designated, shall meet on a regular basis and at least once a year unless otherwise agreed between them in order to examine together the annual control report and opinion presented under Article 62 and to

exchange views on other issues relating to the improvement of the management and control of operational programmes.

2. In determining its own audit strategy, the Commission shall identify those operational programmes for which the opinion on the compliance of systems under Article 71(2) is without reservations, or where reservations have been withdrawn following corrective measures, where the audit strategy of the audit authority is satisfactory and where reasonable assurance has been obtained that the management and control systems function effectively on the basis of the results of audits by the Commission and the Member State.

3. For those programmes, the Commission may conclude that it can rely principally on the opinion referred to in Article 62(1)(d)(ii) with regard to the effective functioning of the systems and that it will carry out its own on-the-spot audits only if there is evidence to suggest shortcomings in the system affecting expenditure certified to the Commission in a year for which an opinion under Article 62(1)(d)(ii) has been provided which contains no reservation in respect of such shortcomings. Where the Commission reaches such a conclusion, it shall inform the Member State concerned accordingly. Where there is evidence to suggest shortcomings, it may require the Member State to carry out audits in accordance with Article 72(3) or it may carry out its own audits under Article 72(2).

## TITLE VII

### FINANCIAL MANAGEMENT

#### CHAPTER I

#### *Financial management*

##### Section 4

#### **Interim payments**

##### *Article 85*

#### **Interim payments**

Interim payments shall be made for each operational programme. The first interim payment shall be made in accordance with Article 71(2).

##### *Article 86*

#### **Acceptability of applications for payment**

1. Each interim payment made by the Commission shall be subject to the following conditions being met:

- (a) the Commission must have been sent a application for payment and a statement of expenditure in accordance with Article 78;
- (b) no more than the maximum amount of assistance from the Funds as laid down in the decision of the Commission approving the operational programme has been paid by the Commission during the whole period for each priority axis;
- (c) the managing authority must have sent the Commission the most recent annual implementation report in accordance with Article 67(1) and (3);

(d) there is no reasoned opinion by the Commission in respect of an infringement under Article 226 of the Treaty as regards the operation(s) for which the expenditure is declared in the application for payment in question.

2. If one or more of the conditions referred to in paragraph 1 are not met, the Member State and the certifying authority shall be informed by the Commission within a period of one month so that the necessary steps can be taken to remedy the situation.

#### *Article 89*

### **Conditions for the payment of the final balance**

1. The Commission shall pay the final balance provided that:

(a) the Member State has sent an application for payment comprising the following documents by 31 March 2017:

(i) an application for payment of the final balance and a statement of expenditure in accordance with Article 78;

(ii) the final implementation report for the operational programme, including the information set out in Article 67;

(iii) a closure declaration referred to in Article 62(1)(e); and

(b) there is no reasoned opinion by the Commission in respect of an infringement under Article 226 of the Treaty as regards the operation(s) for which the expenditure is declared in the application for payment in question.

2. Failure to send any of the documents referred to in paragraph 1 to the Commission shall automatically result in the decommitment of the final balance, in accordance with Article 93.

3. The Commission shall inform the Member State of its opinion on the content of the closure declaration referred to in paragraph 1(a)(iii) within five months of the date of its receipt. The closure declaration shall be deemed to be accepted in the absence of observations by the Commission within that five month period.

#### Section 6

### **Interruption of the payment deadline and suspension of payments**

#### *Article 91*

### **Interruption of the payment deadline**

1. The payment deadline may be interrupted by the authorising officer by delegation within the meaning of Regulation (EC, Euratom) No 1605/2002 for a maximum period of six months if:

(a) in a report of a national or Community audit body there is evidence to suggest a significant deficiency in the functioning of the management and control systems;

(b) the authorising officer by delegation has to carry out additional verifications following information coming to his attention alerting him that expenditure in a certified statement of expenditure is linked to a serious irregularity which has not been corrected.

2. The Member State and the certifying authority shall be informed immediately of the reasons for the interruption. The interruption shall be ended as soon as the necessary measures have been taken by the Member State.

*Article 92***Suspension of payments**

1. All or part of the interim payments at the level of priority axes or programmes may be suspended by the Commission where:

(a) there is a serious deficiency in the management and control system of the programme which affects the reliability of the procedure for certification of payments and for which corrective measures have not been taken; or

(b) expenditure in a certified statement of expenditure is linked to a serious irregularity which has not been corrected; or

(c) there is a serious breach by a Member State of its obligations under Article 70(1) and (2).

2. The Commission may decide to suspend all or part of interim payments after having given the Member State the opportunity to present its observations within a period of two months.

3. The Commission shall end suspension of all or part of interim payments where the Member State has taken the necessary measures to enable the suspension to be lifted. Where the required measures are not taken by the Member State, the Commission may adopt the decision to cancel all or part of the Community contribution to the operational programme in accordance with Article 99.

*CHAPTER II**Financial corrections*

## Section 1

**Financial correction by Member States***Article 98***Financial corrections by Member States**

1. The Member States shall in the first instance bear the responsibility for investigating irregularities, acting upon evidence of any major change affecting the nature or the conditions for the implementation or control of operations or operational programmes and making the financial corrections required.

2. The Member State shall make the financial corrections required in connection with the individual or systemic irregularities detected in operations or operational programmes. The corrections made by a Member State shall consist of cancelling all or part of the public contribution to the operational programme. The Member State shall take into account the nature and gravity of the irregularities and the financial loss to the Funds.

The resources from the Funds released in this way may be reused by the Member State until 31 December 2015 for the operational programme concerned in accordance with the provisions referred to in paragraph 3.

3. The contribution cancelled in accordance with paragraph

2 may not be reused for the operation or operations that were the subject of the correction, nor, where a financial correction is made for a systemic irregularity, for existing operations within the whole or part of the priority axis where the systemic irregularity occurred.

4. In the case of a systemic irregularity, the Member State shall extend its enquiries to cover all operations liable to be affected.

## Section 2

### **Financial corrections by the Commission**

#### *Article 99*

##### **Criteria for the corrections**

1. The Commission may make financial corrections by cancelling all or part of the Community contribution to an operational programme where, after carrying out the necessary examination, it concludes that:

(a) there is a serious deficiency in the management and control system of the programme which has put at risk the Community contribution already paid to the programme;

(b) expenditure contained in a certified statement of expenditure is irregular and has not been corrected by the Member State prior to the opening of the correction procedure under this paragraph;

(c) a Member State has not complied with its obligations under Article 98 prior to the opening of the correction procedure under this paragraph.

2. The Commission shall base its financial corrections on individual cases of irregularity identified, taking account of the systemic nature of the irregularity to determine whether a flat rate or extrapolated correction should be applied.

3. The Commission shall, when deciding the amount of a correction, take account of the nature and gravity of the irregularity and the extent and financial implications of the deficiencies found in the operational programme concerned.

4. Where the Commission bases its position on facts established by auditors other than those of its own services, it shall draw its own conclusions regarding the financial consequences after examining the measures taken by the Member State concerned under Article 98(2), the reports supplied under Article 70(1)(b), and any replies from the Member State.

5. When a Member State does not comply with its obligations as referred to in Article 15(4), the Commission may, in relation to the degree of non-compliance with these obligations, make a financial correction by cancelling all or part of the Structural Funds contribution to the Member State concerned.

The rate applicable to the financial correction referred to in this paragraph shall be laid down in the implementing rules of this Regulation adopted by the Commission in accordance with the procedure referred to in Article 103(3).

#### *Article 100*

##### **Procedure**

1. Before taking a decision on a financial correction, the Commission shall open the procedure by informing the Member State of its provisional conclusions and requesting the Member State to submit its comments within two months.

Where the Commission proposes a financial correction on the basis of extrapolation or at a flat rate, the Member State shall be given the opportunity to demonstrate, through an examination of the documentation concerned, that the actual extent of irregularity was less than the Commission's assessment. In agreement with the Commission, the Member State may limit the scope of this examination to an appropriate proportion or sample of the documentation concerned. Except in duly justified cases, the time allowed for this examination shall not exceed a further period of two months after the two-month period referred to in the first subparagraph.

2. The Commission shall take account of any evidence supplied by the Member State within the time limits mentioned in paragraph 1.

3. Where the Member State does not accept the provisional conclusions of the Commission, the Member State shall be invited to a hearing by the Commission, in which both sides in cooperation based on the partnership shall make efforts to reach an agreement concerning the observations and the conclusions to be drawn from them.

4. In case of an agreement, the Member State may reuse the Community funds concerned in conformity with the second subparagraph of Article 98(2).

5. In the absence of agreement, the Commission shall take a decision on the financial correction within six months of the date of the hearing taking account of all information and observations submitted during the course of the procedure. If no hearing takes place, the six-month period shall begin to run two months after the date of the letter of invitation sent by the Commission.

#### *Article 101*

#### **Obligations of Member States**

A financial correction by the Commission shall not prejudice the Member State's obligation to pursue recoveries under Article 98(2) of this Regulation and to recover State aid under Article 87 of the Treaty and under Article 14 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 88 of the EC Treaty (1).

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 11 July 2006.

*For the Council*

*The President*

E. HEINÄLUOMA