



EUROPEAN COMMISSION

Annual Activity Report

2010

**Directorate General
Economic and Financial Affairs**

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1. POLICY ACHIEVEMENTS

1.1. Level of the Policy Area (general objectives)

The economic and financial crisis, which erupted in the course of 2008 and led to the largest global recession since the Second World War in the course of 2009, continued to have a significant impact on the activities of DG ECFIN during 2010. The achievement of the objectives which were identified in the 2010 Annual Management Plan of DG ECFIN have to be assessed in the light of the unprecedented new challenges for the EU and euro area economies that emerged in spring 2010. These challenges were triggered by the transformation of the financial and economic crisis into a sovereign debt crisis for individual countries of the euro area which brought to bear considerable pressure on the euro area as a whole through the related contagion effects and risks. The debt crisis in Greece required the establishment of new financing mechanisms in May 2010 to enable effective crisis management through the provision of financial assistance in combination with adjustment programmes under tight conditionality. DG ECFIN helped to contain the contagion risks associated with developments in Greece and later in Ireland inter alia by designing and monitoring financial adjustment programmes for both countries. At the same time, DG ECFIN has contributed to a comprehensive approach to addressing the crisis combining action to respond to short-term stabilisation needs and new frameworks for better crisis prevention and management in the future. Part of this comprehensive approach was enhancing the future framework for economic and financial policies by facilitating the swift adoption of new financial surveillance legislation in 2010 and launching a new package of legislative proposals on strengthening economic governance in the context of the European Semester. Through its work on the Commission's first Annual Growth Survey, DG ECFIN helped prepare the successful launch of the first European Semester. At the behest of the European Council, the DG also worked on the design for a European Stability Mechanism.

A. "Tackling the crisis and sustaining Europe's social market economy"

In relation to the Commission's strategic objective of "Tackling the crisis and sustaining Europe's social market economy" and DG ECFIN's general objective for 2010 "To foster EU growth, employment creation and sustainable development", the following has been achieved:

1) Economic and Monetary Union – the economic and financial crisis

While the European Economic Recovery Plan (EERP) had been successful in the middle of the greatest recession in generations in supporting demand and employment and in protecting output potential, the transformation of the economic and financial crisis into a debt crisis of individual euro area Member States brought on a new set of serious challenges for the euro area as a whole in the course of spring 2010. Sovereign risk premia shot up to levels unprecedented in EMU in Member States with perceived high budgetary and macro-financial risks. This required immediate action to prevent a panic, to quell contagion effects, and to restore confidence in the ability of the EU to address the acute crisis. The immediate need was fulfilled through the creation of appropriate financing mechanisms and in two cases (Greece and Ireland) the launch and monitoring of financial adjustment programmes with strong conditionality. A credible response to the new crisis also required putting in place additional building blocks for a stronger and more credible economic governance framework for the future able to support strong fiscal consolidation and debt reduction; frontloaded structural reforms that are growth-enhancing and raise economies' adjustment capacity; and a swift repair of the financial sector.

a. Budgetary surveillance under the Stability and Growth Pact (SGP):

Extraordinary circumstances combining a financial crisis with a recession justified a co-ordinated budgetary expansion in the EU in 2009/10, although it has led some Member States to breach the 3%

of GDP deficit reference value of the TFEU. For Member States considered to be in an excessive deficit, corrective action has to be taken in timeframes consistent with the recovery of the economy. This is fully in line with the provisions of the Stability and Growth Pact which guarantee that the excessive deficit will be corrected in due time, ensuring long-term sustainability of the public finances.

In 2010, DG ECFIN took a series of actions under the Excessive Deficit Procedure (EDP). The actions refer notably to the recommendations related to the existence of an excessive deficit and setting the deadline for its correction, but also to revising deadlines and assessing effective action to correct the excessive deficit. All EU Member States were concerned with the exception of Estonia, Luxembourg and Sweden. The assessment by DG ECFIN of the Stability and Convergence Programmes of the 27 Member States was also part of the budgetary surveillance. In the same context, DG ECFIN published its annual Report on Public Finances in EMU, which in 2010 focused on the further public finance implications of the financial and economic crisis, including the need to reduce debt and to tackle external imbalances, and as usual blended a summary of surveillance issues with state-of-the-art analysis. To this add major contributions to three important Communications in May, June and September 2010.

b. Setting up financial assistance mechanisms for euro-area countries in distress

A financial rescue package for Greece was agreed on 8 May 2010, conditional on a financial adjustment programme. The Greek adjustment programme jointly monitored by the Commission, the ECB, and the IMF, made a strong start overall, and Greece managed impressive budgetary consolidation during the first half of 2010. Major steps forward have also been made in the broader structural reform agenda. At the request of the Euro Area Member States, the Commission has taken over the coordination and management of the pooled bilateral loans. The European Financial Stability Facility (EFSF) was established by the Council on 9 May 2010. Based on an intergovernmental agreement of the euro area Member States, the mechanism provides financial assistance in the form of loans or credits to Member States in difficulties. A European Financial Stabilisation Mechanism (EFSM) has been established by the Council on 11 May 2010 based on Article 122.2 to preserve financial stability in the EU by responding in a coordinated, rapid and effective manner to acute difficulties of particular Member States. Upon request by Ireland, on 21 November 2010, the mechanism has been activated and the financial support is planned to be disbursed as from January 2011. The programme for Ireland, jointly monitored by the Commission, the ECB, and the IMF, envisages an overhaul of Ireland's banking system, growth-enhancing reforms, and the reduction of Ireland's government deficit to below 3% of GDP by 2015.

On 28 November 2010, Euro-area finance ministers agreed on the future European Stability Mechanism (ESM) to replace the current European Financial Stability Facility (EFSF) as of mid-2013. The ESM will safeguard financial stability in the euro area and will build on the existing European Financial Stability Facility (EFSF) and complement the new framework for reinforced economic surveillance in the EU entailed in the Commission's legislative proposals of 29 September 2010.

c. Balance of payment support to Member States outside the euro area

Of the EUR 14.6 bn committed so far under the EU Balance of Payments (BoP) facility, for Hungary (6.5 bn), Latvia (3.1 bn), and Romania (5 bn), a total of EUR 12.1 bn had been disbursed by the end of 2010. The overall ceiling for such assistance is at EUR 50 bn. This EU assistance has been part of coordinated international packages which include loans from the IMF, the World Bank, the EIB, the EBRD and, in the case of Latvia, bilateral support. In order to finance these instalments, the Commission issued corresponding bonds on the financial markets obtaining very competitive rates as supranational issuer.

BoP assistance has given the three countries breathing room to implement reforms necessary to place public finances on a sounder footing and restore access to private external financing. The latter has also been achieved through agreements in the context of Bank Coordination Initiatives in which DG ECFIN has taken an increasingly active role. It represents an important flanking measure to the

balance of payment support and is targeted to maintain foreign banks' exposure in the new Member States receiving the financial assistance. In the context of the initiative, successful meetings with the parents of foreign banks operating in those countries were held and the exposure was broadly maintained. External imbalances have narrowed and progress has been made on important reforms in the three countries, allowing gross international reserves to increase again, suggesting that the correction of the BoP problem is underway.

Programme reviews have been completed or were ongoing for the three countries concerned – Hungary, Latvia and Romania – with delays in some cases, and the programme for Hungary expired in November 2010 after EUR 5.5 bn had been disbursed. Fiscal consolidation continued and the three countries have designed and implemented important reforms (in the areas of fiscal governance, efficiency of public administration, etc) to stimulate growth in the medium term, help avoid future destabilising fiscal policy, and ensure the medium- and long-term sustainability of government finances.

d. Strengthening Economic Surveillance in the EU and the euro area

The implementation of a comprehensive exit strategy and the prevention and better handling of future crises required a significant strengthening of the EU's and the euro area's economic governance in the course of 2010. The urgency of an enhanced economic governance framework became particularly pressing with the sovereign debt crisis and the need to restore confidence that the EU and its institutions could handle the immediate crisis and chart the course towards a more stable future. DG ECFIN worked on the elements of a comprehensive and well-sequenced exit strategy from the financial and economic crisis long before the onset of the sovereign debt crisis. This exit strategy, whose principles were spelled out over the course of the autumn of 2009 by the ECOFIN Council, was to encompass fiscal consolidation from 2011 at the latest, financial sector repair, and the frontloaded implementation of growth-enhancing structural reforms. These priorities were recognised in the Commission Communication on Europe 2020. To facilitate their implementation, the Communication proposed to strengthen economic country surveillance by pursuing a wider and more integrated approach to analysis and policy guidance covering fiscal policy as well as macroeconomic imbalances, and macro-relevant structural reforms.

In May 2010 DG ECFIN identified the main weaknesses of the existing surveillance mechanisms, which had allowed public debt to rise significantly over time even before the crisis and macroeconomic imbalances to widen and go largely unchecked. Subsequently in June 2010 DG ECFIN made suggestions on the broad outlines for improved and new tools to strengthen economic governance in the EU and the euro area. This work was reflected in two Commission Communications. It resulted in a package of six legislative proposals presented on 29 September 2010, aiming on the one hand to strengthen fiscal surveillance under the SGP by encouraging more prudent fiscal policy making and by placing greater importance on the debt criterion as well as by introducing minimum standards for national fiscal frameworks. On the other hand, the package proposed the entirely new instrument of an Excessive Imbalances Procedure (EIP) to provide systematic surveillance of macroeconomic imbalances based on an alert mechanism, including a scoreboard. New legislation on financial sanctions both under the SGP and the EIP was also part of the package. The sanctions were intended as strong and coherent incentives favouring good policy. Importantly, the proposal reduced the possibility for politically side-stepping the rules of the mechanisms by introducing a reverse majority for decisions on sanctions, such that only a qualified majority in the Council could block a Commission proposal implying a sanction.

e. Macro-financial stability

DG ECFIN participated in the design and communication of the results of the second EU-wide stress testing exercises coordinated by CEBS (now EBA). Compared to the previous exercise, the 2010 exercise involved much greater transparency, with results published on an aggregate and bank-by-bank basis. The sovereign exposure of each of the tested banks has also been disclosed. In addition, the scope of the test has been expanded to include more banks and a larger number of scenarios.

Initially, the publication of the stress test results and bank exposures to sovereign debts appeared to have had a positive impact on financial market sentiment. However, as time elapsed, the optimism generated by the last stress test has faded away and the credibility of stress test exercises has been under severe pressure in the financial press for various reasons including the methodology applied for the sovereign shock, the absence of stress on the liquidity/funding side and the failure to detect the fragilities of the Irish banks. While the new scope and sample were better defined to address market expectations, the lack of time to conduct necessary cross-checks and scrutiny of the results is now considered to have considerably affected the quality of the assessment. These conclusions were the focus of the post-mortem analysis in December 2010 and are expected to be addressed in the next exercise.

f. Adoption of the financial supervision legislative package in September 2010.

Following the adoption of the legislative package on financial supervision and the first round of discussions with the Council at the end of 2009, DG ECFIN followed through with the negotiations with the European Parliament. DG ECFIN participated to the negotiations in trilogue format, which were successfully concluded by the adoption in September 2010 by the European Parliament of amended regulations satisfying also the Council and the Commission (adoption at first reading). The Council also formally adopted the texts in November 2010, and these legal acts were eventually published in the Official Journal on 15 December 2010, allowing for the effective establishment of the European Systemic Risk Board and the three new supervisory authorities. The ESRB, which could count on the immediate support of the ECB, lost no time and organised already in December 2010 a first informal meeting of the voting members of the General Board, to which Commissioner Rehn participated.

g. Efforts to strengthen the external representation of the euro area/EU

DG ECFIN continued its reflections on how to develop a more co-ordinated and assertive European foreign economic policy, including through a better representation at the International Monetary Fund (IMF). The Commission (DG ECFIN) also continued to take a proactive role in the co-ordination of EU member states with respect to the World Bank's governance reform and the Multilateral Development Banks' capital increases.

2) Economic and Monetary Union (EMU) – enlargement of the euro area

In its convergence report of 12 May 2010 the Commission concluded that Estonia met the criteria for adopting the euro and made a proposal to the Council to this effect. The other eight countries with a so-called 'derogation' were assessed as having made uneven progress towards the euro and do not meet all the conditions for euro adoption. Level of knowledge on euro increased in all post-2002 changeover countries. Around 90% of the population considered themselves well informed at the end of changeover communication campaign in Cyprus, Malta, Slovenia and Slovakia. In Estonia, this figure increased importantly during 2010 and stood at 89% six weeks before the euro changeover. Euro was considered a 'good thing' for Europe by 67% respondents in euro area in the autumn 2010, 3pp down from autumn 2009 level.

3) Europe 2020

DG ECFIN has provided substantive input into developing the Europe 2020 strategy that replaced the Lisbon Strategy from 2010 as the European Union's strategy for growth and as framework for implementing a well sequenced and comprehensive exit strategy from the economic and financial crisis. The strategy also acts as the Commission's economic work programme during the term of this Commission. In the context of the Commission's overarching strategy, DG ECFIN proposed for implementation in 2011 a wider and more integrated approach to the analysis and policy guidance covering fiscal policy as well as macroeconomic imbalances, and macro-relevant structural reforms as part of the "European Semester" approach to macroeconomic country surveillance. The DG has worked on promoting smart, integrated and flexible financial instruments addressing a range of policy objectives as a means to leverage EU budgetary funds and foster investment within the framework of

the Europe 2020 Strategy. Within this context, it prepared the meetings of the Commissioners Group on Innovative Financial Instruments chaired by Commissioner Rehn.

B. "Developing an ambitious and coherent external agenda with global outreach"

In relation to the Commission strategic objective "**Developing an ambitious and coherent external agenda with global outreach**" and the DG ECFIN 2010 general objective "**To promote prosperity beyond the EU**", DG ECFIN accomplishments concern the following issues:

1) Enlargement and neighbourhood policy

Bilateral economic dialogues were held in 2010 with all candidate and potential candidate countries, except with Iceland that was recognised as a candidate country in June. DG ECFIN completed its annual assessment of the medium-term economic programmes of candidate and potential candidate countries. DG ECFIN further drafted the economic chapters of the Commission's annual Country Progress Reports, as well as a section of the Strategy Paper on candidate and potential candidates. DG ECFIN contributed to the Commission Opinions on Albania, Montenegro and Iceland that were adopted in 2010. It also started preparing the Opinion due on Serbia in fall 2011. DG ECFIN issued regular monitoring reports and one staff publication on the impact and features of the crisis in pre-accession countries.

In addition to candidate and potential candidate countries, DG ECFIN was involved in various activities related to the countries covered by the European Neighbourhood Policy (ENP). It conducted economic dialogues with number of these countries, contributed to the preparation of the annual progress reports on the implementation of the ENP Action Plans and issued its annual economic review of the neighbour countries. It also prepared the discussions at the annual meeting of the Economy and Finance Ministers in June and Senior Officials in April, in the context of the UfM (Union of the Mediterranean).

2) Macro-financial assistance for third countries

The international economic and financial crisis has resulted in balance of payments difficulties in a number of third countries and macro-financial assistance (MFA) was in increasing demand. In 2010, new MFA operations were decided by the co-legislators for Ukraine and the Republic of Moldova. The implementation of these operations started in 2010; the Commission also continued the implementation of the operations decided in the previous years: programmes in favour of Kosovo, approved in 2006 (this operation was implemented partly and expired at the end of 2010), and programmes in favour of Serbia, Bosnia-Herzegovina, Armenia and Georgia, approved in 2009 (the implementation of the programme for Georgia was completed in the course of 2010). Furthermore, the Commission finalised a proposal for an additional MFA operation to Georgia that it submitted to the Parliament and the Council in early 2011. Finally, the MFA programme for Lebanon, approved in 2007, expired in 2010.

3) EU's economic policy regarding third countries

In 2010, the crisis has further underlined the need for a close involvement of the EU in international discussions on both medium-term reforms and short-term macroeconomic and financial policy responses. This involvement materialised in bilateral and multilateral meetings. Bilateral macro-economic dialogues were held with a number of Third countries. At multilateral level, the Commission has played an active role in the G20 in 2010. This represents another step towards a more cohesive and assertive voice of the EU in global economic and financial affairs. The Commission most notably played an important role in ensuring a successful participation of President Barroso and President Van Rompuy to the G20 Summits in Toronto and Seoul, and, in the case of the Commissioner for economic and monetary affairs, to the three Finance Ministerial meetings that took place in preparation of the Summits. It also coordinated the EU input on economic and financial issues dealt in this forum on the basis of Terms of Reference agreed with the Member States, and ensured an active

representation of the EU in a number of G20 working groups, including the Framework for Growth group, the IMF Reform group, and the Financial Safety Nets group.

4) Strengthening cooperation with the EIB, the EBRD and other International Financial Institutions

In April 2010, the Commission finalised the mid-term review of the EIB external mandate and submitted a proposal for its amendment to Council and Parliament, based on the recommendations of the Steering Committee of Wise Persons. The proposal was welcomed in the Council's general approach in June and is currently being discussed by several EP committees. Depending on the final decision, which could be adopted in early 2011, preparations should start for a post-2013 mandate.

In the context of the regular capital resource review (CRR4) of the EBRD - which had been advanced to spring 2010 following the call of the G20 - the Commission representing the EU supported the Bank and its activities, as well as the capital increase of EUR 10 billion to expand the EBRD's financing in response to the crisis and compensate for a sharp decline in private capital flows in its countries of operations, approved by its Board of Governors during the annual meeting in May 2010.

Following the recommendation by the Group of Wise Persons concerning the mid-term review of the EIB external mandate, DG ECFIN continues to work to set up a Working Group to discuss with Member States, European Financial Institutions and other stakeholders the scope and composition of a "EU Platform for Co-operation and Development".

DG ECFIN was actively involved in following the discussions in the several multilateral facilities such as the Western Balkans Investment Framework (WBIF), as well as investment facilities for Central Asia and Latin America. Under the Neighbourhood Investment Facility, project approval progressed.

POLICY AREA: Economic and Financial Affairs		
GENERAL OBJECTIVE nr 1: To foster EU growth, employment creation and sustainable development		
Indicator	Impact achieved	
	Target (long-term)	Situation at end 2010
Degree to which Member States record budgetary outturns in line with the Stability and Growth Pact	Within a general framework oriented towards budgetary positions close to balance or in surplus, the attainment by Member States of medium-term budgetary objectives (differentiated for individual Member States to take into account their economic diversity as well as of the fiscal risk to the sustainability of public finances) allowing them to deal with normal cyclical fluctuations while keeping the government deficit within the reference value of 3% of GDP.	<p>The aggregated budgetary position of the 27 EU Member States in 2010 is the following:</p> <ul style="list-style-type: none"> • a headline deficit of 6.89% of GDP • a structural deficit, i.e. cyclically-adjusted primary deficit net of one-offs and temporary measures, of 2.57% of GDP. <p>In 2010, government finances remained at the same level relative to GDP as in 2009, while a significant worsening occurred in 2009 compared with 2008. This is linked to the profound impact the financial and economic crisis in 2008 and 2009 had on public finances. As indicated by the discrepancy between the headline deficit and the structural deficit, a large part of the budgetary deterioration reflects the automatic reaction of the budget balance to the economic downturn. Moreover, due to the responsiveness of tax elasticities to strong cyclical variations, a part of the structural deterioration is also accounted for by the economic downturn. Finally, a discretionary fiscal stimulus continued in 2010 in a number of Member States in order to support economic activity, which also weighs on the deterioration of the structural balance.</p>
Potential growth /output	Increase in potential growth output	The shock of the global crisis still casts its shadow over the EU economy. Arguably, it will take time for the EU economies to work through the inevitable financial and economic adjustment, thus muting the prospects for employment, consumption and investment over the forecast horizon. Potential growth is currently estimated at just below 1% for both the EU and the euro area (down slowly recovering further from some 1½% in 2008). Bearing in mind that it is intrinsically difficult to distinguish cyclical from longer-term developments, estimates based on the Commission's 2010 autumn forecast

		show potential growth recovering to just above 1% by 2012.
GENERAL OBJECTIVE nr 2: To promote prosperity beyond the EU		
Indicator	Impact achieved	
	Target (long-term)	Situation at end 2010
Progress in countries' compliance with the Copenhagen criteria for accession	Full compliance	Compliance with criterion of "being a functioning market economy": Croatia and Turkey, as well as Iceland, meet the criterion, other pre-accession countries not yet. Compliance with the criterion of "being able to withstand competitive pressure and market forces within the EU": expected to be complied with by Croatia.
Countries benefiting from macro-financial assistance achieve a sustainable macro-economic situation.	Benefiting countries have seen an increase in their official exchange reserves.	The global financial crisis has continued to challenge some of the economic stabilisation outcomes of previous MFA programmes in a number of countries, and their external and internal sustainability. A number of new operations had thus to be launched in 2010 for countries having benefited in the past of MFA: Ukraine, Moldova and Georgia. A number of other countries with a vulnerable balance of payments position and financing arrangements with the IMF may require EU MFA support in 2011).

1.2. Achievements by ABB activities

1.2.1 Activity "Economic and Monetary Union"

1.2.1.1. Objective "To ensure effective policy co-ordination and overall policy consistency in developing an EU response to the economic crisis, in the context of achieving the Europe 2020 agenda and sustainable development and in order to raise the growth potential of Member States and make the EU more competitive"

Result indicators	Latest known result	Target (result)
Formulate a legislative proposal on strengthening the economic governance in the EU.	The Council has formed an Ad hoc Working Group to formulate its "general approach" as basis for a possible first-reading agreement with Parliament. The Parliament rapporteurs (ECON Committee) have presented their reports on the package at end-2010. On the excessive imbalances procedure, the scoreboard for triggering in-depth country studies is currently being discussed and negotiated with Member States. Work has also begun at a technical level on how to make the alert mechanism operational.	College adoption of the legislative package in fall 2010 and initiation of discussions by co-legislators on the legislative proposals, and on main technical elements of the alert mechanism. Also to prepare the transition to integrated country surveillance, in particular through the integrated assessments of Stability and Convergence Programmes and National Reform Programmes.
Main policy outputs		

Communication (COM(2010)250 final) on the establishment of a system of enhanced policy coordination based on broader and deeper surveillance with the aim of the strengthening the functioning of the Stability and Growth Pact, extend surveillance to macro-economic imbalances, align national budget and policy planning through a "European Semester" for early European economic policy coordination, and to make the European stabilisation mechanism decided on 9 May fully operational.

Communication on enhancing economic policy coordination for stability, growth and jobs and tools for stronger EU economic governance (COM(2010) 367/2) to develop the proposals for greater economic policy co-ordination and surveillance and to set out effective enforcement mechanisms, and proposes a European semester for policy co-ordination. The Communication is the basis for the subsequent legislative proposal.

Proposal of a comprehensive package of legislative measures on strengthening economic governance to strengthen the Stability and Growth Pact with prudent fiscal policy-making (COM(2010) 522 final, COM(2010) 526 final), to prevent and correct macroeconomic imbalances (COM(2010) 527 final), to establish national fiscal frameworks of quality (COM(2010) 523) and to provide stronger instruments for enforcement (COM(2010) 524 final, COM(2010) 525 final).

1.2.1.2. Objective "To further prepare the enlargement of the euro area and to support the continuing changeover to the euro at Community level in order to take full advantage of EMU's potential"

Result indicators	Latest known result	Target (result)
Level of support in the euro as reported by Eurobarometer	Level of knowledge on euro increased in all post-2002 changeover countries. Around 90% of population considered themselves well informed at the end of changeover communication campaign in Cyprus, Malta, Slovenia and Slovakia. In Estonia, this figure increased importantly during 2010 and stood at 89% six weeks before the euro changeover.	Self perceived level of information considered at least 'good' by at least 85 percent of respondents at the end of the changeover communication campaign. Level of support for euro higher at the end of the campaign.
Progress by Member States towards sustainable convergence	The last convergence assessment in May 2010 concluded that pre-in Member States had recorded uneven progress towards sustainable convergence, as they still absorb the impact of the financial crisis. Three out of 9 examined Member States fulfilled the criterion on price stability; two fulfilled the fiscal criterion; two fulfilled the exchange rate criterion and three fulfilled the criterion on long-term interest rates. External imbalances have been unwinding but external financing conditions remain fragile, with three Member States requiring international financial assistance	Fulfilment of convergence criteria by Member States taking into account the economic environment

Main policy outputs

- Convergence Report 2010
- Proposal for Council Decision under Art. 140 (2) on euro area entry of Estonia.
- Proposal for a Council regulation amending Regulation (EC) n° 974/98 as regards the introduction of the euro in Estonia
- Proposal for a Council Regulation on Conversion rates of the currencies of concerned Member States
- Tenth and eleventh reports on the practical preparations for the future enlargement of the euro area.

1.2.1.3. Objective "To promote the pursuit by Member States of sound budgetary positions and of public finances that are sustainable and of high quality in terms of their contribution to growth"

Result indicators	Latest known result	Target (result)
Percentage of individual Commission recommendations related to the	24 out of 27 Member States (89%) are in excessive deficit procedure (EDP) at	All of the recommendations

<p>Stability and Growth Pact (SGP) implemented by Member States (contingent upon their adoption by the Council)</p>	<p>the start of 2011. The state of implementation of the Commission recommendations to the Council to correct the excessive deficit can be summarised as follows:</p> <ul style="list-style-type: none"> — For 6 Member States (HU, LV, PL, LT, RO and MT), action taken in response to the EDP recommendations was assessed in early 2010. For 3 of them, LT, RO, and MT, new recommendations were issued. — For 13 Member States (States (AT, BE, CZ, DE, ES, FR, IE, IT, NL, PT, SI, SK, UK), the assessment of action taken was concluded in June 2010. — For 2 Member States (LT, RO), the assessment of action taken in response to recommendations issued earlier that year was concluded in October 2010. — For MT, the assessment of action taken is scheduled for December 2010. — For all Member States mentioned above, the EDP is currently in abeyance pending a positive assessment for Malta. — For 4 Member States (BG, CY, DK, FI), the EDP was initiated in June 2010, for which the effective action will be assessed early 2011. <p>For one Member State (EL), the Commission issued a recommendation for a Council decision under Art. 126(9) and Art. 136 in February 2010. Since then, recommendations are reviewed on a quarterly basis.</p>	
<p>Main policy outputs</p>		
<p>Commission recommendations on the application of the Stability and Growth Pact</p>		

1.2.1.4. Objective "To promote macro-financial stability and to restore confidence, stability and sustainability in the financial markets by devising and help implementing appropriate policy responses in order to limit the impact of the financial crisis on the real economy of the EU"

Result indicators	Latest known result	Target (result)
<p>1. OIS spreads (interbank market spreads)</p>	<p>In early November 2010, the spread was 23 basis points, a fairly low level compared to the peak of 196 basis points on 10 October 2008. In 2010 so far, the level has remained below that prevailing before the collapse of Lehman Brothers (i.e. 63 basis points on 12 September 2008).</p>	<p>Indicator returning to normal pre-crisis reference values.</p> <p>(Before the financial crisis started, the average spread for unsecured lending rates versus OIS rates was less than 10 basis points).</p>
<p>2. Itraxx default risk financials</p>	<p>In early November 2010, the Itraxx default risk was 126 basis points for senior financials and 195 basis points for subordinated financials. Although these levels remain below the peaks recorded in March 2009, they are above early 2010</p>	<p>Indicator returning to normal pre-crisis reference values.</p> <p>(Before the financial crisis started, the Itraxx for senior financials had a ceiling of 10 basis points; 15 basis points for subordinated</p>

	levels.	financials.)
3. Emerging Market spreads	In early November 2010, the emerging markets' spread was at 236 basis points down from 295 basis points in May; it had peaked at 865 basis points on 24 October 2008.	Indicator returning to normal pre-crisis reference values. (Before the financial crisis started, the spread had fallen below 200 basis points.)
4 Corporate bond spreads	In early November 2010: For AAA - corporates: 72 bps For AA - corporates: 137 bps For A - corporates: 156 bps For BBB- corporates: 183 bps. The spreads are below the peaks recorded late 2008 but increased since early 2010.	Indicator returning to normal pre-crisis reference values. (Before the financial crisis started, the spreads had fallen to very low levels, in an investor's search for yield, in basis points: For AAA-corporates: below 16 For AA-corporates: 25- For A-corporates: 40- For BBB-corporates: 66-
Main policy outputs		
Recommendation for a Council decision on the reinforcement and deepening of the financial surveillance of Greece.		

1.2.1.5. Objective "To preserve financial stability in the EU, by providing financial assistance to euro area Member States facing a severe deterioration of their borrowing conditions and to Member States outside the euro area facing difficulties with their balance of payments"

Result indicators	Latest known result	Target (result)
Supporting euro-area countries under financial difficulties	A European Financial Stabilisation Mechanism (EFSM) has been established by the Council on 11 May 2010 to preserve financial stability in the EU by responding in a coordinated, rapid and effective manner to acute difficulties of particular MS. Following a request by Ireland, on 21 November 2010, the mechanism has been activated in early January 2011	The EFSM will contribute with up to €22.5 billion to the programme agreed with the Irish authorities to restore financial market confidence in the banking sector and the sovereign, enabling the economy to return to sustainable growth. The EFSF, IMF and bilaterals will cover the remaining € 45 billion of the external support to the programme
Sovereign debt stress in Greece and other euro area Member States	The programme under the Greek facility: The first two tranches of the 110 billion Euro area/IMF assistance package in the amount of EUR 29 billion are disbursed: EUR 21 billion paid by the euro-area Member States and EUR 8 billion by the IMF. The overall assessment is that the program has made a strong start. Greece has managed impressive budgetary consolidation during 2010, in spite of statistical revisions increasing the fiscal deficit and debt. Total budgetary measures adopted in four successive packages are projected to reduce the government deficit from 15.4 percent of GDP in 2009 to 9.6 percent in 2010. Major steps have also been made in the broader structural reform agenda.	<ul style="list-style-type: none"> • Avoidance of an acute crisis in Greece and the euro area and contagion to other vulnerable markets, Member States and the financial sector. • Progress in implementing the reform agenda in Greece
Sovereign debt stress in Ireland and other euro area Member States, funding problems banks	The Irish programme: The European Council adopted a decision on financial assistance to Ireland on 7 December 2010. The package includes EUR 35 billion to support Irish banks and EUR 50 billion to cover the financing needs of the Irish government's budget. Half of the banking support measures will be funded by Ireland from its Treasury cash buffer and pension reserves. The	<ul style="list-style-type: none"> • Avoidance of an acute crisis in Ireland and the euro area and contagion to other vulnerable markets, Member States and the financial sector. • Recapitalization and downsizing

	programme will involve an overhaul of Ireland's banking system, growth-enhancing reforms and the reduction of Ireland's government deficit to below 3% of GDP by 2015.	of the Irish banking system, lower reliance of Irish banks on Eurosystem funding
Balance of payment stress (gross international reserves, exchange rate developments).	A total EUR 14.6 bn (out of a ceiling of EUR 50 bn) has been committed so far under the EU Balance of Payments (BoP) facility, following the approval of loans to Hungary (6.5 bn), Latvia (3.1 bn) and Romania (5 bn). By end 2010, a total of 11.4 bn had been disbursed. EU assistance has been part of coordinated international packages which include loans from the IMF, the World Bank, the EIB, the EBRD and, in the case of Latvia, bilateral support from other MS. BoP assistance gave the three countries breathing room to implement reforms necessary to place public finances on a sounder footing and restore access to private external financing.	<ul style="list-style-type: none"> • Avoidance of an acute BoP crisis and disorderly exchange rate adjustment in the EU countries • Decline in external imbalances (current account deficit, external gross debt) compared to pre-crisis levels, feeding into broader macro-economic stabilisation. • Return to a situation of gradual accumulation of foreign exchange reserves in those countries currently receiving BoP assistance.
Regular programme reviews, addressing the main sources of vulnerability in EU Member States receiving BoP assistance.	<p>Progress has been made in addressing vulnerabilities. Programme reviews have been completed or are ongoing for the three countries concerned – Hungary, Latvia and Romania - with delays in some cases, and the programme for Hungary expired in November 2010 after EUR 5.5 bn had been disbursed. Fiscal consolidation continued and the three countries have designed and implemented important reforms (in the areas of fiscal governance, efficiency of public administration, etc), which will stimulate growth in the medium term, help avoid future destabilising fiscal policy and ensure the medium- and long-term sustainability of government finances.</p> <p>Proposal for a framework of heightened surveillance during the post-programme period, involving regular missions, reporting, information sharing, and enforcement of EU rules.</p>	<p>Completion of programme reviews (a review is completed when it is considered that policy conditionality has been respected by the country concerned):</p> <ul style="list-style-type: none"> • Hungary: post programme surveillance • Latvia: by January 2012 • Romania: by May 2011 <p>Respect of the fiscal targets agreed in the context of the programmes, consistent with the EDP.</p> <ul style="list-style-type: none"> • Assessment of programmes, highlighting best practices. • Post-programme surveillance, to be aligned to the maximum extent with other EU procedures.
Monitoring non-programme vulnerable countries and contingency planning.	Monitoring of financing needs (fiscal and BoP) for non-programme vulnerable countries. Development of a centralised monitoring system of financial sector, fiscal, and balance of payment stress indicators.	<ul style="list-style-type: none"> • Developing a centralised and regularly updated dataset on financing needs and stress indicators in vulnerable countries. • Calculations of financing gap estimates under several stress scenarios. • Crisis preparation and contingency planning for Member States requesting EU financial assistance.
Main policy outputs		
<ul style="list-style-type: none"> • Communication from the Commission to the Council on Greece. • Recommendation for a Council Decision concerning the 10 May 2010 Council decision addressed to Greece. • Communication on the EFSM • Recommendation for a Council Decision Granting financial assistance to Ireland 		

1.2.1.6. Objective "To conduct economic research and to monitor macroeconomic developments and the economic situation in the EU, the euro-area and Member States in order to support the smooth functioning of EMU and the EU economy"

Result indicators	Latest known result	Target (result)
Reference to and usage of analytical tools and EU reference indicators as well as the Economic Papers by governments and research institutes in Europe, and beyond.	Economic research and analytical tools (mainly simulations with the Quest III model) have been used extensively during 2010 as inputs into the economic policy debate. This includes substantial contributions to the analytical chapters in the European Economic Forecast; to the 2010 Public Finance Report; to the EPC's Lisbon Methodology (LIME) working group; to the EPC's Output Gap Working Group (OGWG) with respect to budgetary surveillance issues; to the Spring and Autumn 2010 forecasting exercise (output gaps; risk scenarios for the forecasts); as well as assessments of the impact of financial market regulations on economic activity.	Reference to and usage of analytical tools and EU reference indicators and other products comparable to those of the other major international institutions, such as the IMF, OECD, ECB. The target variables include downloads of data, references to the publications, number of attendants of the events.
Accuracy of the forecast exercises	A study Oct. 2007 shows that overall the Commission's forecasts continue to dispose a reasonable track record. Forecasts for the EU generally seem to be unbiased, efficient and display a high success rate for directional accuracy. Finally, the Commission's forecasts' track record for GDP is broadly comparable with the ones of Consensus, the IMF and the OECD.	Accuracy comparable to the accuracy of the forecasts of the other major international forecasters, such as the IMF, OECD, consensus. The target variables include GDP growth, total investment, inflation, the unemployment rate, the general government balance and the current account to GDP ratio with forecast error (respective to the outturn data)
Main policy outputs		

1.2.2. Activity "International Economic and Financial Affairs"

1.2.2.1. Objective "To support the enlargement process, the implementation of the EU Neighbourhood Policy and EU priorities in other third countries by conducting economic analysis and providing policy assessment, advice and input to negotiations on international economic and financial affairs"

Result indicators	Latest known result	Target (result)
Progress in candidate countries' accession negotiations on EMU	With Turkey, negotiations on EMU Chapter (N° 17) were not opened. As regards Croatia, the EMU Chapter was provisionally closed in December 2008. Negotiations launched on Iceland in July 2010: first step being the "screening" (started in November 2010, expected to be completed the first part of 2011)..	Negotiation Chapter on economic and monetary policy provisionally closed
Main policy outputs		
<ul style="list-style-type: none"> • <u>Annual economic review</u> of the Neighbourhood countries. • Semi-annual <u>economic forecasts for non-EU countries</u>: forecasting economic developments in America, Asia, the countries of the European Free Trade Association (EFTA), Russia, the other Neighbourhood countries, Latin America and Sub-Saharan Africa with simplified individual forecasts for the biggest economies of the last two regions (Brazil, Mexico, Argentina, South Africa and Nigeria). 		

1.2.2.2. Objective "To improve the EU profile, external representation and liaison with the EIB and EBRD, other international financial institutions, and relevant economic fora aiming at strengthening convergence between their strategies and operations and EU external priorities"

Result indicators	Latest known result	Target (result)
<p>Progress in EU coordination with the main IFIs and MDBs in the external field</p>	<p>In 2010, EU coordination at the World Bank (WB) resulted in a similar number of statements co-signed by the EU as in 2009. In the context of WB governance reform and capital increase, the Subcommittee on IMF-Related Issues (SCIMF) based in Brussels helped to establish common EU positions in this respect (as well as the capital increases in other MDBs) whereas these matters were usually not coordinated in Brussels.</p> <p>DG ECFIN (together with the ECB) prepared more than 20 common statements on IMF policy and country items (excluding ECFIN assessment of IMF Article IV reports on the euro area and EU Members).</p>	<p>Increased frequency of common EU positions, statements</p>
<p>Progress in ensuring that IFIs and MDBs have adequate resources in the external field</p>	<p>In April 2010, the Commission finalised the mid-term review of the EIB external mandate and submitted a proposal for its amendment to Council and Parliament, based on the recommendations of the Steering Committee of Wise Persons. The proposal was welcomed in the Council's general approach in June and is currently being discussed by several EP committees. Depending on the final decision, which could be adopted in early 2011, preparations should start for a post-2013 mandate.</p> <p>In the context of the regular capital resource review (CRR4) of the EBRD - which had been advanced to spring 2010 following the call of the G20 - the Commission representing the EU supported the Bank and its activities, as well as the capital increase of EUR 10 billion to expand the EBRD's financing in response to the crisis and compensate for a sharp decline in private capital flows in its countries of operations, approved by its Board of Governors during the annual meeting in Zagreb on 14/15 May 2010.</p> <p>Following the recommendation by the Group of Wise Persons concerning the mid-term review of the EIB' external mandate, DG ECFIN continues to work to set up a Working Group to discuss with Member States, European Financial Institutions and other stakeholders the scope and composition of a "EU Platform for Co-operation and Development".</p> <p>DG ECFIN was actively involved in following the discussions in the several multilateral facilities such as the Western Balkans Investment Framework (WBIF), as well as investment facilities for Central Asia and Latin America. Under the Neighbourhood Investment Facility, project approval progressed.</p>	<p>Improve the EU co-ordination in the different governing bodies of MDBs asking for capital in-creases (e.g. implement the EBRD capital increase).</p> <p>Effective and efficient coordination related to EU resources allocated to IFIs and MDBs.</p>
<p>Main policy outputs</p>		
<p>Bilateral economic dialogues were held with Brazil, China, India, Russia and Japan. Meetings of Finance Ministers were held with Mediterranean partners (in the context of the Union for the Mediterranean) and with EFTA partners.</p> <p>At the multilateral level, DG ECFIN prepared the EU position at various G20 meetings through the submission of a note on the G-20 trade finance initiative and the Terms of Reference on EU position at G20 to the EFC. The main events in 2009 were the G-20 summit in London in April that focused on global financial stability and the Pittsburgh Summit in September that</p>		

introduced a new global macroeconomic surveillance system (the Framework for Strong, Sustainable and Balanced Growth).

DG ECFIN contributed to the preparation of the various G7 and G8 meetings that took place during 2009. In the context of ASEM (the Asia-Europe meeting), DG ECFIN contributed to the Finance Deputies exchange of views on the response to the crisis.

Finalisation of the mid-term review of the EIB external mandate and submission of a proposal for its amendment to Council and Parliament.

Agreement on a new Tripartite MoU between the EIB, the EBRD and the Commission in respect of cooperation outside the European Union.

1.2.2.3. Objective "To provide macro-financial assistance to third countries with a view to resolve their balance of payment crises and restore external debt sustainability"

Result indicators	Latest known result	Target (result)
Current account balance (% of GDP)	Georgia: - 11.7% in 2009, -12.0% in 2010 Moldova: -9.4% in 2009 and -11.5% in 2010 Lebanon: -9.5% in 2009 and -11.5% in 2010 Kosovo: -18.6% in 2009 and -18.5% in 2010 Serbia: - 7.0% in 2009 and - 6.2% in 2010 Bosnia and Herzegovina: -6.8 % in 2009 and - 6.8% in 2010	Decrease of current account deficit to pre-crisis levels
External debt (% of GDP)	Georgia: - 58.4% in 2009, -66.4% in 2010 Moldova: - 66.3% in 2009 and -76.7% in 2010 Lebanon: -171.2% in 2009 and -160.3% in 2010 Kosovo: - 19.3% in 2008 (lack of recent reliable data). Est. 17.7% in 2010 Serbia: - 72.3% in 2009, - 78.8% in 2010 Bosnia and Herzegovina: - 17.2 % in 2009 and - 21.8% in 2010	Decrease of external debt to pre-crisis levels
Official foreign exchange reserves in months' imports of goods and services	Georgia: 4.1 in 2009, 4.1 in 2010 Moldova: 3.99 in 2009, 4.0 in 2010 Lebanon: 10.33 in 2009, 10.3 in 2010 Kosovo: not relevant (euro is the legal tender): est. EUR 554 Million in 2010 Bosnia & Herzegovina: 4.4 in 2009, 5.6 in 2010 Serbia: 9.6 in 2009, 7.9 in 2010	Increase of reserves to pre-crisis levels

Main policy outputs

The Commission on 9 June 2010 approved a legislative proposal for a decision on granting assistance to Moldova. The proposal was eventually approved by the co-legislators in October 2010.

The Commission completed negotiations on economic policy conditions of assistance to Armenia, Bosnia and Herzegovina, Moldova and Serbia.

The Commission made disbursements under MFA programmes to Georgia (EUR 30.7 mio – part of first and second tranche of 2009 programme), Kosovo (EUR 30 mio – first tranche of 2006 programme) and Moldova (EUR 40 mio – first tranche of 2010 programme).

1.2.3. Activity "Financial Operations and Instruments"

1.2.3.1. Objective "To promote the EU interest in the governing bodies of the EIB/EIF and strengthen the EU-EIB/EIF co-operation to ensure the alignment of EIB/EIF lending with EU policy priorities in particular within the EU"

Result indicators	Latest known result	Target (result)
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<p>Implementation of ex-ante coordination mechanism between the EIB and the Commission on projects and programmes and closer cooperation with the EIB Group and other financial institutions in particular within the EU.</p>	<p>Through the Article 19 consultation, the Commission's view on all EIB financing projects is coordinated with a large number of other DGs. In 2010, 441 Commission opinions on EIB projects were prepared.</p> <p>In 2010, interventions of the Commission representatives in the Boards of Directors were prepared for 10 Board meetings at the EIB and 10 Board meetings at the EIF as well as for the Board of Governors of the EIB and the Annual General Meeting of the EIF.</p> <p>ECFIN actively ensured a close coordination of the EIB Group contribution to the Europe 2020 Strategy, in particular regarding innovative financial instruments for the next multi-annual financial framework.</p> <p>EU contribution to the capital increase of the European Investment Fund: The last tranche was completed by purchasing 39 shares in order to maintain the 30% shareholding.</p>	<p>Timely delivery of the large number of Commission opinions issued on EIB projects</p> <p>Timely preparation of briefing material for Commission representatives in the Boards of the EIB and EIF.</p>
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Main policy outputs

After the activity peak of in 2009 to offset the contraction of credit due to the financial crisis and support economic activity, the EIB reduced its loan volumes from EUR 79.1bn to EUR 68.9bn in 2010 which is still considerably above the pre-crisis levels. At the same time, it extended its possibilities to finance riskier projects by increasing considerably the ceiling for Special Activities from EUR 4.9bn to EUR 8bn (i.e. lower graded loans and Structured Finance Facility products including joint COM-EIB initiatives such as the Risk Sharing Finance Facility (RSFF) or the Loan Guarantee Instruments for TEN-T projects (LGTT)).

In accordance with its Statutes, the EIF's objective is to contribute to the pursuit of Community objectives while achieving an appropriate return for its shareholders. The policy objective has been reinforced in recent years through the active support of the Lisbon strategy for growth and employment, of which enhancing SMEs' access to finance and the financing of research and innovation are key issues. 2010 global equity commitments exceeded the 2009 figures by 27%, reflecting the countercyclical role of EIF. The securitisation market was still heavily impacted by the financial crisis with only a few transactions coming to the market, allowing the EIF to achieve only 60% of the 2010 target.

1.2.3.2. Objective "To improve the financial environment for business and infrastructure, especially SMEs, TEN-T projects and RTD projects, fight against climate change and the efficiency of the EU financial instruments"

Result indicators	Latest known result	Target (result)
<p><i>Number of beneficiary SMEs receiving financial support</i></p>	<p>(Cumulated figures for the entire programme period; status of CIP data: 30 June 2010) CIP: 77,894 (SMEG07:77,780; GIF 114)</p> <p>(Cumulated figures for the entire programme period; status of MAP data: 31 Dec 2009 – last available) MAP: 234,272 (SMEG01: 234,080; ESU01: 192) Final figures for SMEG01 since end of availability period has been reached.</p>	<p>CIP (target for the entire duration of the programme): At least 327,000</p> <p>MAP: At least 200,000</p>

<p>Total investment/loan volume leveraged (EU + other sources):</p>	<p>Figures as of 30 June 2010</p> <p>CIP: a) GIF: EUR 1,313 million¹; b) SME Guarantee (SMEG 2007): EUR 5,162 million.</p> <p>Figures as of 31 December 2009</p> <p>MAP: a) ETF Start-up ("ESU01"): EUR 1,280.1million; b) SME Guarantee ("SMEG01"): EUR 16,850.6 million (total SME financing guaranteed.)</p> <p>ELENA: For the projects approved so far, the minimum leverage ratio of 25 has been significantly exceeded each time. Based upon current estimates, the 2009 EU ELENA contribution of EUR 15 million should result in a leveraging of a total investment volume in excess of EUR 1.2 billion. A similar result is expected for the 2010 contribution of EUR 15 million.</p>	<p>CIP (target for the entire duration of the programme): EUR 13,000 million</p> <p>MAP: 8,000 million</p>
<p><i>Nr of jobs created or maintained in SMEs receiving new financing</i></p>	<p>CIP: SMEG07</p> <p>Number of employees at final beneficiaries (at inclusion date): 286,956</p>	<p>CIP (target for the entire duration of the programme): 378,400</p>

Main policy outputs

- The CIP interim evaluation, which assessed the Framework Programme as a whole, was conducted in the second half of 2009. The findings published in 2010, confirmed strong intervention logic for EU support and strong prospects for European added value being generated in the area of financial instruments.
- The financial crisis and its impact on the economy resulted in a slow-down in Venture Capital activities during 2010. However, in the last months of the year, a clear revival of demand for venture capital deals was observed and it is expected that the increasing trend for these activities will remain also in 2011. SMEG, on the other hand, is a counter-cyclical instrument and the demand for guarantees by financial intermediaries is therefore likely to be sustained.
- **The SME Guarantee Facility (SMEG)** has been operational since September 2007 and by the end of 2010, 32 transactions with financial intermediaries from 15 countries had been approved (of which 16 in 2010 including extensions of existing contracts). The EU commitments amount to €285,7 million. Most of the SMEG deals are under the Loan Guarantee window. There are six deals under the Microcredit window (in France, Ireland, Spain, Norway, Turkey and Poland) and one Equity window deal (Spain). By the third quarter of 2010, almost 90.289 SMEs had received financing supported by SMEG, through nearly 106.204 loans. By the end of 2010, a number of other deals for both GIF and SMEG were in the pipeline for assessment.
- **The High Growth and Innovative SME Facility (GIF)** has been operational since November 2007 and is implemented by the European Investment Fund (EIF) on behalf of the Commission. By the end of 2010, 21 GIF transactions with Venture capital funds targeting investments in 17 participating countries had been approved (of which 5 in 2010), committing EU investments of €292,3 million in total. Five of these venture capital funds are investing in eco-innovation across Europe, supported by EU commitments of about €69 million.
- A new financial instrument in the area of microfinance targeting particularly the socially excluded, the Progress Microfinance Facility (PMF) has been developed. A Framework agreement for the implementation of the micro-credit guarantees was signed with the EIF on 1 July 2010. A "Fonds commun de placement - Fonds d'investissement spécialisé (FCP-FIS) was established on 22 November 2010, which will allow providing micro -credit to final beneficiaries. The aggregate total of commitments in 2010 amounts to €28 million. This amount was committed to the EIF for both, guarantees - €10 million- and FCP-FIS - €18 million. The aggregate total of payments in 2010 amounts to €21 million. In 2010 two guarantee operations had already been signed between the EIF and FIs in December 2010.
- To further raise awareness, EU finance days for SMEs were organised in the CIP participating countries. In 2010, EU finance days were organised jointly with DG ENTR in 8 EU capitals.

¹ Amount lower compared to last year's AMP; due to the financial crisis, several venture capital funds have reduced the investment amount.

- Furthermore, DG ECFIN supported other Commission services in the development of new financial instruments in the context of energy efficiency (enlarged Elena facility and European Energy Efficiency Fund) and it designed a new proposal for innovative financial instrument for infrastructure projects (Europe 2020 Project Bonds) . In order to enhance the efficient implementation of the financial instruments, DG ECFIN continued to propose improvements in the Financial Regulation and provided policy input in the context of the budget review. Finally, the work on the follow-up of the PPP Communication continued with a conference organised in December 2010.
- DG ECFIN signed the ELENA² contribution agreement with the EIB for the 2010 budget in December 2010. It is expected to achieve a total investment volume of at least EUR 375 million.

1.2.3.3. Objective: "To ensure sound and efficient management and follow-up of non-budgetary operations"

Result indicators	Latest known result	Target (result)
<p>Treasury management</p> <p>A. Active treasury management</p> <p>Continuation of asset management under different mandates, the main being ECSC, providing good return based on low risk assets the interest income on the ECSC portfolio being used by RTD to finance research in the coal and steel sector.</p>	<p>Treasury management</p> <p>A. Active treasury management</p> <p>Despite the financial crisis, the assets managed by ECFIN in 2010 show a good relative performance compared to the benchmark.</p> <p>The volatility of the return has been substantially reduced by shortening the duration (to 2.07 years at year-end 2010 from 2.67 years at year-end 2009) and increasing the relative share of sovereign investments (from 77% at year-end 2009 to 90% at year-end 2010 for ECSC).</p> <p>The ECSC portfolio outperformed the benchmark for the 12-month period ending at year-end 2010 by 91 basis points (bps)³ , i.e. by 7.58 bps per month</p>	<p>Treasury management</p> <p>A. Active treasury management</p> <p>The assets under management are to be invested in such a way as to ensure that funds are available as and when needed, while still generating the highest return available, consistent with maintaining a high degree of security and stability.</p>
<p>B New mandate Competition fines</p> <p>Implementation of a new mandate for managing the assets obtained by the Commission as provisionally cashed fines from competition cases.</p>	<p>B. New mandate Competition fines</p> <p>Based on the Commission decision of June 2009 for mandating ECFIN-L, a solution comparable to an investment fund has been worked out, with all details set out in a Service Level Agreement between DG ECFIN and DG BUDG which has been signed end 2009.</p> <p>The so-called BUFI Fund has become operational during 2010 and by the end November of 2010 reached a size of almost EUR 530 million. In the period from 22 September to 31 December 2010, the BUFI portfolio yielded 19.72 bps, whereas the benchmark (net of 20 bps p.a.) returned 18.62 bps. Thus, the relative performance of the BUFI portfolio amounted to +1.10 bps.</p> <p>At year-end 2010, the duration of the BUFI portfolio (0.93 years) was close to that of the benchmark (0.99 years).</p>	<p>B. New mandate Competition fines</p> <p>Efficiently manage the substantial new inflows of fines and fine-tuning of operational aspects.</p> <p>Actual return (excluding direct costs) at least as high as the guaranteed return (benchmark minus 20 bps p.a.).</p>
<p>C. Mandates as Asset Management Designated Service</p>	<p>C. Mandates as Asset Management Designated</p>	<p>C. Mandates as Asset Management Designated Service</p>

² ELENA is a European Facility aiming, through technical assistance, at supporting regional or local authorities in accelerating their investment programmes in the fields of energy efficiency and renewable energy sources.

³ 100 basis points is one percentage point (100 bps = 1%)

<p>(AMDS)</p> <p>Monitoring of certain asset management mandates outsourced under which the EIB invests off-budget funds on behalf of the Commission.</p>	<p>Service (AMDS)</p> <p>Risk and performance reports, based on investment strategies agreed between EIB and ECFIN, have been constantly monitored and found satisfactory.</p> <p>During 2010, the Guarantee Fund for external actions - the largest asset management mandate - showed a total return of 1.06% against a benchmark return of 1.20%.</p> <p>Over the same period, other asset management mandates yielded results consistent with their respective benchmarks, returning on average 0.85%, against an average benchmark return of 0.65%.</p>	<p>(AMDS)</p> <p>Manage the different portfolios in accordance with the Investment Guidelines as implemented in the corresponding Annual strategies.</p>
<p>Management of borrowings</p> <p>Execution of all borrowing operations for EC-BoP, EC-MFA, EC-Art. 122 and Euratom at spread levels that are typical for first class Sovereign Supranationals and Agencies (SSA) sector borrowers</p>	<p>Management of borrowings</p> <p>EUR 2.8 billion have been borrowed during 2010 and on-lent for balance of payments support to Latvia and Romania. The achieved terms were similar to the ones obtained by institutions comparable in terms of rating and shareholders to the EU (like the EIB) and AAA rated SSA sector borrowers.</p> <p>The European Financial Stability Mechanism has been designed, in close cooperation with the Member States. Its legal base has been prepared and signed and the EU's entrance into the market as a real benchmark has been prepared in close cooperation with the banks. The activation through a EUR 5 billion bond issue in favour of Ireland was prepared in December 2010, the bond closed early January 2011.</p> <p>The support for the EFSF establishing it as a new borrower has led to ensure its AAA rating and a successful market entrance in January 2011, prepared in 2010.</p>	<p>Management of borrowings</p> <p>Execute all legal mandates for borrowing and lending with a view to obtain best market terms in favour of the loan beneficiaries.</p>
<p>Management of the Stability Support for Greece</p> <p>Management of disbursement and of capital and interest repayments as well as rebalancing mechanism.</p>	<p>Management of the Stability Support for Greece</p> <p>Direct involvement mainly at three levels:</p> <ul style="list-style-type: none"> - Structuring of the operation, coordination of the loan pooling 15 bilateral facilities and preparation of the legal documentation (Loan Agreement and Intercreditor Agreement). - Although these loans are provided by Member States, the process is coordinated by the Commission: Overall management of the EUR 80 billion pooled bilateral loan to Greece, including the development of working procedures (Procedures Manual of the Financial Support to Greece; Higher Funding Costs Methodology) and the development of automated financial models that allow the adequate management of the Greek programme (Forecast Model of the Greek Facility; Higher Funding Costs model). - On-going financial management and monitoring of the programme, including : <ul style="list-style-type: none"> a) the preparation of reports to the Euro-area Member States and the EWG, b) the disbursement of two instalments in May and September 2010 (for a total amount of EUR 	<p>Management of the Stability Support for Greece</p> <p>Execute the coordinating role of the Commission for the Member States in a timely and accurate way.</p>

	<p>21 billion) and of a third one finally delayed until January 2011 (which involved a complex exercise of recalculation of interest rates for each of the Member States as a Higher Funding Cost situation arose), and</p> <p>c) middle and back office work related to the execution of payments, including the coordination of some 15 payments from the various countries at the time of each disbursement, and the quarterly reporting, validation of accounting balances and allocation of interest payments amongst the Lenders.</p>	
<p>Main policy outputs</p>		
<ul style="list-style-type: none"> • Commission Decisions on the borrowing operations under the BOP loan facility • Reports to participating Member States on the implementation of the Greek facility 		

2. MANAGEMENT AND INTERNAL CONTROL SYSTEMS

2.1. Introduction to DG ECFIN

2.1.1. Financial environment

Globally speaking, DG ECFIN is a policy-making DG with diverse financial instruments. It can nevertheless be considered as a DG with a relatively low level of budgetary spending (EUR 395 million of commitments and EUR 227 million of payments in 2010) and a low number of budgetary operations (647 commitments, 901 payments, and 109 recovery orders). Financial operations (budget and off-budget) are mainly concentrated in the “Financial Operations and Instruments” activities. Over and above **administrative** expenditure under DG ECFIN control, the main budget lines cover:

- **EMU-related expenditure**, with roughly EUR 16.3 million both in commitment and payment appropriations. The main spending activities are the coordination and surveillance of EMU and the communication activities on EMU and the euro (PRINCE).
- **Expenditure related to international financial matters**, which includes macro-financial assistance (MFA) to third countries for global commitment and payment appropriations of EUR 90.2 million and EUR 138.7 million respectively.
- **Financial operations and instruments** with global commitment and payment appropriations of respectively EUR 285.5 million and EUR 171.4 million. The bulk of the commitment appropriations (some EUR 167 million) relates to the CIP. In terms of payments, main appropriations are reserved for the provisioning of the Guarantee Fund (EUR 93.8 million), for the CIP (EUR 48.6 million), for the completion of the programme for enterprises, more particularly the improvement of the financial environment for SMEs (EUR 14.5 million) and for participation in the increase of the EIF capital (EUR 14.5 million).

Main 2010 budgetary figures (in EUR million)

	Appropriations		Implementation	
	Commitments	Payments	Commitments	Payments
Administrative expenditure under DG ECFIN control	6.4	6.4	6.4	4.4
EMU	16.3	16.3	14.9	12.5
International financial matters	90.2	138.7	90.1	101.0
Financial operations and instruments	280.7	172.1	279.7	109.6
Total	393.6	333.5	391.1	227.5

In addition to the above-mentioned budgetary activity, the DG has an **important off-budget activity** in its Luxembourg site, encompassing treasury operations relating to the management of some EUR 2.8 billion – representing assets of the European Coal and Steel Community in liquidation (ECSC i.L.) and other mandated funds – and banking operations (borrowing and lending activities) for which both the outstanding borrowing and lending positions amounted to close to EUR 13.2 billion as of end-2010.

Finally, the DG oversees the management of the Guarantee Fund for external actions, which is entrusted to the EIB. The assets of the Fund at end 2010 stood at EUR 1.35 billion.

From an administrative point of view, DG ECFIN is applying a partially centralised financial circuit. The Financial Regulation (Art. 60.4) requires application of the four-eye principle for the operational

and financial initiation, meaning that both the operational and financial aspects of a transaction have to be verified. The initiation function is divided into the operational part (carried out by officials in the various Directorates concerned – Operational Initiating Agents) and the financial part (carried out by officials in the central financial unit – Financial Initiating Agents). Together they are involved in the complete cycle of the procurement and grant procedures, from the publication of the contract notices to the award decision, and are responsible for putting together the transaction files (budgetary commitments/de-commitments, payments, recovery orders, etc.). Afterwards, each and every file is checked by a central, independent ex-ante verification team in the financial unit (Verifying Agents) who carry out both financial and operational verification tasks.

2.1.2. Inherent risks linked to financial operations

The most important inherent risks linked to the specific characteristics of DG ECFIN financial operations are the following:

- (1) The DG is located at **two sites** and has one Directorate in Luxembourg. Consequently, particular effort is needed to ensure an appropriate level of controls across the two sites.
- (2) The **limited number and specialised nature of budgetary operations** pose challenges to the financial organisation of the DG, given the requirement of the Financial Regulation to involve several independent actors in the treatment of each operation. In this context, several initiatives aiming at streamlining and simplifying processes and procedures have been - and are still being - undertaken by the financial unit.
- (3) Several **specific instruments** managed by the DG pose particular challenges to the control systems.

(3.1) Off-budget operations

DG ECFIN manages various financial operations which do not constitute classical budgetary operations and can be grouped under the following three categories:

(3.1.1) Borrowing and lending

- **Balance of payments support to non-euro area Member States**

The economic and financial crisis has triggered the reactivation of this EU instrument which had not been used since the early nineties. This balance of payment support always takes the form of a loan to a beneficiary Member State (only countries outside the euro area are eligible) which is funded through a borrowing on the capital markets. It is decided by the Council upon a Commission proposal and is in principle embedded in a broader multilateral financing package involving the IMF. It is associated with comprehensive policy conditionality, so as to overcome underlying imbalances and vulnerabilities. The assistance is provided in instalments, subject to compliance with policy conditionality, monitored by the Commission and is paid to the central bank of the beneficiary country. The major inherent risk is a default of the beneficiary country and its impact on the EU budget which guarantees the full and timely reimbursement of the borrowed funds on the due date.

- **Financial stability support to euro-area Member States**

On 9 May 2010, the Council and the Member States of the EU decided on a comprehensive package of measures to preserve financial stability in Europe, including a European Financial Stabilisation Mechanism (EFSM). The decision allows the Commission to raise funds for an amount of up to EUR 60 billion in case Member States would request financial support through the EFSM. The functioning of this financial support is similar to what is described above for the balance of payments support. The major inherent risk is here also a default of the beneficiary

country and its impact on the EU budget which guarantees the full and timely reimbursement of the borrowed funds on the due date.

- **Macro-financial assistance to third countries (loan)**

This is an instrument for exceptional macroeconomic support to third countries with balance of payments or budgetary difficulties which generally complements financing provided in the context of an IMF-supported adjustment and reform programme. Its disbursement depends on the IMF programme being on track and on the fulfilment of a set of economic and financial policy conditions agreed upon between the Commission and the beneficiary country. Given the exceptional character of the instrument, each operation has its own legal base which is adopted by the Council. Operations can consist of loans or grants or a combination of the two. When this macro-financial assistance takes the form of a loan to the beneficiary country, it is funded through a borrowing on the capital markets. This loan is provided to the Central Bank of the beneficiary country but their final destination is (e.g. building up of reserves, foreign exchange market interventions) is generally left to be decided by the authorities in agreement with the IMF.

There are two major inherent risks linked to this instrument: (a) the default of the beneficiary country and its impact either on the Guarantee Fund for External Actions of the EU or the EU budget which guarantees the reimbursement of the borrowed funds on the due date; (b) while the specific destination of EU funds is not formally defined in the Memorandum of Understanding or the Council decision, there is however a need to ensure that the money is properly used. In view of mitigating the risk of improper use of funds, prior operational assessments of the financial circuits of the central bank and the Ministry of Finance of the beneficiary countries are carried out by external auditors on behalf of the Commission. In case weaknesses are identified in this context, corrective actions have to be implemented by the beneficiary country concerned prior to the disbursement of the assistance.

(3.1.2) **Asset Management**

DG ECFIN manages assets of the European Coal and Steel Community in Liquidation (ECSC i.L.) and other assets mandated by the Commission. These various assets are invested in a variety of financial products (major part in sovereign bonds) according to principles of prudent management with a view to minimising the inherent risks of such activities, i.e. operational, counterparty and market risks. As such, these asset management activities are not explicitly covered by the provisions of the Financial Regulation and therefore do not fall under the responsibility of the Commission's Accounting Officer, except for the need to include them in the Commission financial statements at year-end. Therefore, specific investment and control procedures have been put in place for governing these investment operations.

(3.1.3) **Greek Facility**

In response to the Greek debt crisis in early 2010, the Euro Area Member States decided to grant pooled bilateral loans to Greece. While the EU is not providing the funding for the rescue package to Greece, the Commission has accepted the tasks relating to the coordination and management of the stability support which are executed by DG ECFIN.

(3.2) **Programmes managed by International Financial Institutions (IFI's)**

In these instruments, DG ECFIN uses its experience with financial markets and its close contacts with some major international financial institutions such as the EIB, the EIF, the EBRD, the CEB to channel funds from its own budget lines (and from DG ELARG, DG ENTR, DG ENER and DG MOVE) towards final beneficiaries through a network of existing financial intermediaries. The main control challenge for this type of instruments is to ensure (a) the proper implementation of the legal base and of the provisions of the management agreements signed with these IFI's as well as (b) the appropriate level of controls in the chain of

responsibilities (programme DG – DG ECFIN – IFI – financial intermediaries – final beneficiaries), and to clarify control responsibilities of all the involved partners. In this context, an IAC audit on one of these programmes carried out in 2009 showed that improvements in the control environment implemented in the course of 2008 have significantly reduced the risk of improper use of EU funds. The associated action plan was completely implemented in October 2010.

(3.3) **Macro-financial assistance to third countries (grant)**

As indicated under point (3.1.1) above, this macro-financial assistance can take the form of a loan to the beneficiary country. However, in some cases, it can also take the form of a grant (or a combination of loan and grant). The objectives and conditions of this grant assistance are similar to those of the loan assistance. However, as it does not provide by definition for a reimbursement by a given date, the major inherent risk is limited to the improper use of these EU funds which is mitigated by operational assessments of the financial circuits of the central bank and the Ministry of Finance of the beneficiary countries, as described above.

A detailed description of the management and control framework put in place for the main financial activities of the DG can be found in the Internal Control Templates in Annex 5.

2.1.3. Working arrangements with the Commissioner

Annex 2 of the 10 February 2010 Communication from the President on the "Working Methods of the Commission 2010-2014" describes the principles governing working relations between the Members of the Commission, their cabinets and the services of the Commission. According to section 1.3 of this annex, DG ECFIN and its responsible Commissioner have established by common accord the practical arrangements complementing, where necessary, the principles set out in the annex.

As far as internal control issues are concerned, section 5.2 of annex 2 provides that "*the Member of the Commission and the Director General meet at least twice a year to discuss the internal control weaknesses highlighted or the caveats expressed in the services' annual activity report and the action plans devised in order to remedy them.*" More generally, section 5.2 provides for the need for the Commissioner to be informed with a view to allow him to exercise his political authority over the service and, where appropriate, to carry out monitoring as part of the budgetary discharge procedure.

In the same context, according to Internal Control Standard #9, twice a year, a meeting on internal control issues is organised between the Commissioner and the Director General. Due to the heavy workload, the second meeting of 2010 was postponed several times during the second half of the year. It took eventually place on 24 January 2011 and covered the whole year 2010.

2.2. The functioning of the entire control system

2.2.1. Compliance with the requirements of the internal control standards (ICS)

A desk review of the ICS baseline requirements was carried out by the responsible unit, with input from specialised services when needed. This review showed that the baseline requirements can be considered as implemented across-the-board - 51 out of 61 baseline requirements were considered as implemented, and one is not applicable to DG ECFIN activities -, with a few minor exceptions requiring some additional work:

- *ICS#4: Staff evaluation and development*

While DG ECFIN follows the Commission procedures concerning the evaluation of its staff, not all DG ECFIN officials had individual identified objectives in 2010.

- *ICS#7: Operational structure*

In relation with the delegation of authority, in principle, all Units have defined it in their Unit manual. However, following the major reorganisation and the heavy workload faced by many operational services since then, not all Unit manuals have been updated or drafted.

- ICS#8: Processes and procedures

Despite the fact that this ICS was prioritised in 2010, further action is still required to ensure that the DG's internal procedures are aligned with DG HR DS Security Standards and implementing rules relating to the Commission Decision on security of information systems. This ICS has been re-prioritised for 2011.

- ICS#9: Management supervision

The DG usually meets the Commissioner twice a year to discuss internal control and audit issues. However, in the second half of 2010, the meeting had to be postponed several times because of the work pressure related to the sovereign crisis in some MS. A meeting eventually took place on 24 January 2011, which covered internal control and audit issues for the whole year 2010.

- ICS#10: Business continuity

In relation with the need to put in place deputising arrangements, all Units have defined them in their Unit manual. However, as already mentioned under ICS#7 above, not all these Unit manuals have been updated following the major reorganisation of the DG.

- ICS#11: Document management

The two baseline requirements of this ICS have been considered as partially implemented. Firstly, while the rules on protection of personal data are applied, the use of specific IT tools for the processing of sensitive information is not systematic in the DG. Staff needs to receive more training on handling classified and/or sensitive information. Secondly, there are good registration and filing practices in DG ECFIN, except in some cases when applicable rules are not fully complied with, due to tight deadlines and resulting time pressure.

- ICS#12: Information and Communication

In relation with the compliance with the Commission's standard Information Systems Security Policy, DG ECFIN has adopted an IT Security Plan. However, as already mentioned under ICS#2 above, it still needs to be aligned with Commission standards (Implementing rules and Security standards).

2.2.2. Effectiveness of the implementation of the prioritised control standards

The table below reports on the results of the actions taken to improve the effectiveness of the three ICS identified in the Annual Management Plan 2010. Overall, progress was mitigated for two of the three ICS and further follow-up actions are needed and planned in 2011.

- ICS#3: Processes and procedures

Context: A 2009 follow up audit of the 2008 joint IAS-IAC audit on the implementation of selected ICS considered that DG ECFIN should finalise and adopt the "Strategic people management" document. Once DG HR scoreboards and HR indicators would be finalised, DG ECFIN would have to implement them at directorate and unit levels.

Progress made: Expectations in relation with the ICS were completely met:

- The senior management has decided to abandon the 'Strategic People Management' project but the monitoring of staff seniority, which was to be ensured in the context of the abandoned strategy, has been instead integrated in the yearly APE exercise.

- All relevant HR indicators are now monitored at requested levels through DG ECFIN own tools (with the exception of training attendance which is managed at DG HR level).

- ICS#5: Objectives and Performance Indicators

Context: The above mentioned follow up audit has considered that the work done in 2009 on the identification and assessment of performance indicators was not completed and required additional actions in 2010. More specifically, a 'customers' satisfaction survey remained to be organised.

Progress made: Expectations in relation with this ICS were partially met:

- With a view to assess customer satisfaction, a questionnaire, to be sent out once a year to the DG's main stakeholders, was developed in 2009 and approved early in 2010.
- However, the questionnaire was eventually not sent because of the apparent need to review both the indicators and questionnaires following the July 2010 wide-scope reorganisation that aligned DG ECFIN's organizational structure with the new priorities of the DG, in particular, regarding broadened and deepened surveillance at country level. This review could not be organised because of the heavy workload the DG had to face in the second half of 2010. This pending issue will be dealt with in 2011. Therefore, this ICS has been selected for further prioritisation in the Management Plan 2011.

- ICS#8: Processes and procedures

Context: The above mentioned follow up audit has recommended that regarding the DG security policy, further action was required to ensure that the DG's internal procedures are aligned with DG HR-DS Security Standards and implementing rules.

Progress made: Expectations in relation with this ICS were partially met:

- After having taken several measures to comply with the requirements of the audit recommendation, DG ECFIN asked DG HR-DS to validate its revised security policy with regard to the Commission's security policy guidelines. Since DG HR-DS found it inappropriate to do such a validation, the IAS asked DG ECFIN to issue a self-assessment on compliance with these guidelines.
- Here again, the reorganisation put a lot of pressure on the competent services, so that this self-assessment was not finalised in 2010. This will be done in 2011.

2.2.3. Conclusion

In 2010, significant efforts have been undertaken in increasing the effectiveness of the ICS in DG ECFIN. Even though due to specific events, achievements did not always match expectations, there is satisfactory evidence that the internal control system is implemented effectively in DG ECFIN. This is confirmed by the IAC opinion on the state of internal control (see section 3.1.2. below)

Further improvements are nevertheless needed and the following ICS have been listed for priority actions in the Management Plan 2011:

- 1) **Staff allocation and mobility (ICS#3):** On 20 July 2010 the Commission has adopted a reorganisation package for DG ECFIN, accompanied by a substantial reinforcement of human resources. It took force on 16 September 2010. This reorganisation is the deepest and widest ever endeavoured in DG ECFIN. An unprecedented number of new members need to be integrated and the existing staff needs to adapt to new tasks.

The aim, by selecting this ICS, is to contribute to the success of the reorganisation, which depends on ability of the management to align the organisational structures and staff allocations with priorities and workload whenever necessary. After the transition period, the positive impact of

reorganisation should be visible in lower vacancy rates, reduced turnover of staff and reduced reliance on overtime and more importantly in improved quality of services provided.

- 2) **Objectives and performance indicators (ICS# 5) and Processes and procedures (ICS#8):** As explained in section 2.2.2.above, expectations in relation with these ICS were partially met: The objective, by selecting them, is to implement two long-standing IAS audit recommendations referred to above.
- 3) **Operational structure (ICS#7):** The objective is to comply with the first baseline requirement, which states in particular that delegation of authority should be clearly defined, assigned and communicated in writing.

This delegation has always been formalised in the Unit manuals. Following the reorganisation mentioned above, Unit manuals have to be drafted or updated, including for what concerns delegation of authority.

- 4) **Business continuity (ICS#10):** The reason for selecting this ICS is also linked to the need for update or drafting of Unit Manuals. Indeed, the first baseline requirement of ICS#10 provides in particular that adequate measures, including deputising arrangements for relevant operational activities and financial transactions, should be in place to ensure continuity of service. These deputising arrangements have to be formalised in Unit Manuals.

2.3. Information to the Commissioner

The main elements of this report and assurance declaration have been brought to the attention of Commissioner Olli Rehn.

3. BUILDING BLOCKS TOWARDS THE DECLARATION OF ASSURANCE (AND POSSIBLE RESERVATION TO IT)

3.1. Building blocks towards reasonable assurance

Introduction

The overarching elements of the management and control systems in DG ECFIN are the following:

- Being ultimately responsible for the sound financial management of the different activities and projects under their control, the Authorising Officers by Sub-Delegation (AOSD) and the operational units under their supervision carry out the monitoring and control activities which they deem necessary or appropriate.
- In order to cope with the requirements of the Financial Regulation in an environment with a limited number of budgetary operations, DG ECFIN has opted for a centralised financial structure (model 2 financial circuit). Each and every file is checked by a central, independent ex-ante verification team in the Financial Unit.
- A centralised ex-post control function is in place. Its objective is to provide additional assurance regarding the correct implementation of the financial operations of DG ECFIN as regards their legality, regularity and compliance with the principle of sound and efficient management. Several factors are considered in order to establish the ex-post control work programme such as the value and complexity of the financial operations, the controls put in place to mitigate the risk of the operations, the lessons from past findings and the work of other auditors.
- The Internal Control Management Group (ICMG) oversees the functioning of the internal control systems in DG ECFIN and steers the ex-post control programme. It provides a useful forum to discuss specific internal control-related issues and possibly formulate appropriate corrective actions.
- The Advisory Committee on the Use of Resources (ACUR) ensures that the allocation of budgetary resources reflects the DG's priorities. For this purpose, it examines the quality and costs of individual proposed projects, makes proposals to the senior management when choices between projects are needed or suggests actions which it considers necessary. ACUR also discusses the budgetary planning of projects and programmes.
- As far as off-budget operations are concerned, both the Treasury Management Committee (TMC) and the Risk Management function are in place. The former meets normally every month to assess the implementation of the investment strategy, discuss recent developments in the markets and possible tactical reactions to these, taking into account the financial risks affecting the portfolios. The latter ensures – and reports on - the monitoring of potential risks for the off-budget financial instruments and assets managed and serves as a control entity for the off-budget activities (e.g. limit control).
- The Internal Audit Capability (IAC) of the DG assists the Director General and the management of DG ECFIN to control risks and to monitor compliance with rules, regulations, policies and procedures, to provide an independent and objective opinion on the quality of management and control systems, and to make recommendations regarding the effectiveness and the efficiency of operations and the cost-effective use of resources. A risk-based approach is used to establish the annual work programme of the IAC and this is coordinated with the IAS.

3.1.1. Assessment by management

The reasonable assurance of the Director General that the resources assigned to the activities described in this report have been used for their intended purpose and in accordance with the principles of sound financial management is based on the following elements:

- Effective mitigation of the risks related to **procurement and grant** procedures from the publication of the contract notices to the award decision thanks to independent ex-ante controls. The partially centralised financial circuit applied in DG ECFIN since 2003, which entrusts the operational initiation of files to the various directorates concerned while financial initiation and ex-ante verification are performed by a central and independent expert team, has continued to demonstrate its adequate character for DG ECFIN's activities and organisation.
- Operational financial actors (authorising officers and initiating agents) receive **training and guidance** on a regular basis. In-house training sessions on important aspects of financial management are organised and a structured dialogue on outstanding issues is established between the financial unit and its main clients. The internal manual of budgetary and financial procedures is regularly updated and streamlined while the intranet section of the financial unit constitutes the core platform for informing users about applicable procedures and forms. These efforts allowed for a stabilisation of the number of overrides of the negative opinion of the ex-ante verification team in 2010 (7 compared to 6 in 2009).
- **Off-budget operations** are governed by specialized manuals of procedures conform to market practice. In particular, in view of the creation of the European Financial Stabilisation Mechanism (EFSM) in 2010 and the large amounts involved, a revision of the corresponding manual of procedures is under way. The implementation of investment policy and risk management principles is regularly monitored by independent committees and functions and only a few minor errors were detected and rectified afterwards.
- During the **ex-post controls** performed on various activities and programmes, no significant financial errors were identified and the observations made only concerned potential improvements in the management of certain programmes.
- The **permanent improvement of the control system** of DG ECFIN following the implementation of the recommendations of the IAC, IAS and ECA (if any) as well as on the basis of the corrective actions formulated by the Internal Control Management Group (ICMG).
- The **opinion of the IAC** on the state of internal control in DG ECFIN.

The following indicators demonstrate the effectiveness of the internal control system.

3.1.1.1. Key indicators on legality and regularity and sound financial management

As far as budgetary operations are concerned, the first level of monitoring and control lies with the AOSD, while the independent ex-ante verification team ensures a second level of control by verifying 100% of the budgetary operations. Additionally, the ex-post control team verifies a selection of budgetary transactions.

Furthermore, as DG ECFIN manages a range of activities presenting specific inherent risks, either off-budget or budgetary (as described under 2.1.2. above), appropriate additional controls are necessary to effectively mitigate them. In general, such additional controls are carried out within the responsible operational services of DG ECFIN.

The following key indicators will successively present the resources devoted to the controls carried out ("input indicators"), the degree and the nature of controls ("output indicators"), the main findings resulting from these controls ("result indicators") and, finally, their possible impact on the assurance regarding the legality and regularity of expenditure ("impact indicators"). For each type of indicators,

the information provided will successively cover the following three categories of controls: ex-ante, ex-post and additional controls, as each of them has its own indicators. As far as the latter category is concerned ("additional controls"), the indicators presented relate to 4 categories of operations which are considered to be the most relevant for assurance purposes on the year 2010 (due to amounts involved and inherent risks): off-budget financial operations, macro-financial assistance, balance of payments operations for non-euro area Member States, and the programmes implemented by IFIs.

All together, these indicators cover all budgetary and off-budget financial operations managed by DG ECFIN, with a particular emphasis on those which present specific risks and corresponding control challenges. As a consequence, these indicators provide sufficient material evidence for the assessment of the management of resources in DG ECFIN and, ultimately, for the declaration of assurance of the AOD.

Input indicators

Both the ex-ante verification team of the financial unit and the ex-post control team count 4 staff members. For the latter, the FTE (full-time equivalent) was 3.2 due to staff turnover.

Furthermore, additional controls are performed in different operational services as follows:

- The successive steps of all off-budget financial operations are controlled by a dedicated team possessing the required specialized competences:
 - Borrowing and lending operations: 9 staff members
 - Asset management activities (back office): 4 staff members
 - Authorised signatures: 3 staff members
 - SWIFT network confirmations: 7 staff members
 - Bank accounts reconciliation: 3 staff members.

These controls occur one after the other which implies that every transaction is subject to a chain of successive controls for ensuring their regularity. Furthermore, the borrowing/lending and asset management activities are supervised by an independent financial risk manager controlling risk limits and samples of transactions while complementary *a posteriori* controls are carried out by external auditors in the context of their audit of the financial statements for the off-budget activities having been prepared by a dedicated team of accountants in DG ECFIN.

- For macro-financial assistance to third countries (off-budget), the financial component of each borrowing and lending transaction is covered by the above-mentioned dedicated team controlling off-budget operations while the macro-economic part (implementation of the economic conditionality conditions attached to every operation) is carried out by staff members of the responsible operational department. In 2010, thirteen staff members were concerned to varying degrees by MFA operations, either ongoing (Armenia, Bosnia and Herzegovina, Georgia, Kosovo, Lebanon, Serbia and Ukraine) or under preparation (Moldova and the Kyrgyz Republic).

To this figure must be added one staff member conducting assessments of the public financial management framework in the beneficiary countries (in principle the Ministry of Finance and the Central Bank) aimed at verifying its conformity with international standards. These so-called 'operational assessments' are carried out prior to the disbursement of the first tranche of a new operation with the support of external consultants.

The management of the Guarantee Fund for External Actions (which covers macro-financial assistance risks) is monitored by 4 staff members as well as by the above-mentioned financial risk manager.

- Similarly, the financial component of balance of payments and EFSM operations (off-budget) is also controlled by the above-mentioned dedicated team controlling off-budget operations while the monitoring of economic reform conditions imposed on the three countries benefiting from balance

of payments (Hungary, Latvia, Romania) is ensured by 18 staff members from the responsible operational services – 6 for each country. Under the EFSM, the decision on financial assistance to Ireland was taken in December 2010 and the equivalent of 2 men/months was devoted to the monitoring of short-term conditions imposed on the country.

- For programmes implemented by International Financial Institutions (IFI), 24 staff members ensure the verification of all transactions. In addition, the financial statements relating to these programmes are certified by external auditors.

Output indicators

As required, the centralised ex-ante verification team of the financial unit has checked all budgetary financial transactions. Additionally, as foreseen in DG ECFIN's assurance building strategy, in-depth checks were performed on a sample of transactions: in practice, the cost claims of 7 partner institutions co-operating with the Commission under the Business and Consumer Surveys (BCS) scheme, have been examined in great detail, on the basis of additional documentation and evidence requested from the institutes concerned.

During 2010, six ex-post control reports were issued while two others were in progress at year end. Each control assignment covered several projects/transactions. In total, the control assignments covered an extensive array of the diverse budgetary activities of the DG.

The issued reports, in particular, examined projects funded by the EU budget and implemented by 30 external institutions⁴. This work also covered the involvement of three International Financial Intermediaries which manage the day-to-day implementation of certain programmes in the context of which the above-mentioned projects were implemented.

The value of the projects covered € 40.7 million in terms of amount paid to beneficiaries over a number of years. Put into perspective, this amount represents 14% of the budgetary payments in 2010 (ca. €285 m) or 13% of the average payments in the 5-year period 2006-2010 (€309 m).⁵

Furthermore, the outputs relating to the additional controls carried out were as follows:

- As far as off-budget operations are concerned, all transactions have been verified by the above-mentioned dedicated team. Furthermore, in the framework of the regular quarterly checks on compliance with rules and procedures, the financial risk manager has verified the following samples (expressed in percentage of the total number of transactions): securities – 40%, deposits – 8%, currency transactions (spot) – 100%, borrowings and loans – 100%. Finally, additional checks have been carried out by external auditors.

For macro-financial assistance operations, twelve missions, involving ten staff, were carried out in 2010. Only one of them, to Georgia, was a monitoring mission *stricto sensu*; it aimed at reviewing the conditions for the release of the second instalment under the programme launched in 2009. Also, three visits for the carrying out of 'operational assessments' were organised with the support of the external consultants. The other missions were essentially devoted to the preparation of new operations or to the negotiations of the economic and financial conditions of the EU assistance.

⁴ Some of these institutions managed one or more projects, each including usually many different sub-projects/transactions.

⁵ This figure includes payments made by DG ECFIN under cross-sub-delegations received from other DGs.

Concerning the related Guarantee Fund for External Actions, the staff members in charge of its monitoring have checked the compliance with the investment strategy on a quarterly basis. No call on guarantee took place in 2010.

- For balance of payments assistance, responsible desk officers carried out in total 11 monitoring missions covering the three EU Member states benefiting from this type of assistance. These missions were generally carried out on a quarterly basis (except for Hungary where only three missions were carried out) with the objective of checking the implementation of the respective set of economic reform conditions imposed on these three Member states or helping in budget preparation. Under the EFSM, the monitoring activities were limited to desk work.
- With regard to programmes implemented by International Financial Institutions, the verifications done in the responsible service of DG ECFIN have covered the final approval of all transactions, the payment request for all fee invoices, the monthly reconciliation of relevant bank accounts and the information contained in the quarterly/six-monthly/annual reports produced by the International Financial Institutions concerned. Furthermore, 19 monitoring visits have also been carried out by staff members from the responsible service of DG ECFIN. Finally, annual audit certificates are also delivered by external auditors.

Result indicators

Out of a total of 1657 ABAC transactions (commitments, payments, recoveries, forecasts of revenues) checked by the ex-ante verification team, 1525 transactions were accepted, 89 needed technical corrections and 43 were rejected (21 commitments and 22 payments). The additional in-depth controls of the cost claims of the 7 institutions contributing to the BCS scheme were all satisfactory.

The negative opinion of the ex-ante verification team was overridden by the responsible AOSD at the end of the process for 7 transactions, a figure quite stable compared to 2009 (6) and much lower than in 2008 (17).

The ex-post control work did not identify any critical issues as regards the controlled financial operations. For instance, in the case of the SME Guarantee Facility managed by the European Investment Fund (EIF) - which is one of the most important programmes of DG ECFIN – the control examined a representative sample and estimated that the error level was below the acceptable limits⁶. Nevertheless the various controls carried out found a number of financial errors as well as certain weaknesses that need improvements.

As far as additional controls are concerned, the following results have to be taken into account:

- Concerning off-budget operations, out of some 741 transactions, 7 errors were detected during the reconciliation of bank accounts of which four were caused by a counterparty financial institution. The discrepancies discovered have been followed up and cleared within a few days. Moreover, all transactions checked by the financial risk management function were carried out in full compliance with internal procedures. One breach of a risk limit in SAP was detected but remained within the rules according to the investment guidelines. The annual audits for the FY 2010 by the external auditors for the asset management as well as the borrowing/lending activities are currently in the process of being finalised. Based on the feedback to date no significant issues have been highlighted by the external auditors.
- For macro-financial assistance, the monitoring mission to Georgia concluded that the conditions were met, which allowed the Commission to release the second tranche amounting to EUR 30.7 million. Other disbursements took place in 2010: the first instalment under the programme for

⁶ The most likely error rate was estimated at 0.48% of the value of the examined *population* of the guarantee payments, a rate that is below the tolerable threshold typically used by the European Court of Auditors (2%) when auditing the budget expenditure of the EU.

Kosovo (EUR 30 million) was released following the conclusion of an arrangement with the IMF; this was the main condition for the payment of the instalment as all the other conditions had already been met. The first instalment under the programme for Moldova (EUR 40 million), also released in 2010, was only conditional to the IMF programme being 'on track' (which was the case). In the context of three 'operational assessment' missions, the external consultants identified weaknesses in the public financial management framework (Ministry of Finance and Central Bank) of the beneficiary countries. As usual, remedy measures to major weaknesses were (or are to be) included in the set of conditions to be fulfilled by the beneficiary countries and actually verified by DG ECFIN staff prior to the disbursement of the assistance.

- Concerning balance of payments operations, the monitoring visits showed that the assistance has given the three countries breathing room to implement reforms necessary to place public finances on a sounder footing and restore access to private external financing. Programme reviews have been completed or were ongoing for the three countries concerned – Hungary, Latvia and Romania – with delays in some cases, and the programme for Hungary expired in November 2010 after EUR 5.5 bn had been disbursed. Fiscal consolidation continued and the three countries have designed and implemented important reforms (in the areas of fiscal governance, efficiency of public administration, etc) to stimulate growth in the medium term, help avoid future destabilising fiscal policy, and ensure the medium- and long-term sustainability of government finances. Under the EFSM, short-term conditions imposed on Ireland were broadly met at end-December.
- As far as programmes managed via IFIs are concerned, there were no major findings made during the 19 monitoring visits carried out by staff members of the two responsible operational units. The annual audits for the FY 2010 by the external auditors for the different programmes managed by IFIs are currently under way. Based on the feedback to date, no issues have been highlighted by the external auditors except for one case. For one programme managed by the EIF the external auditors have asked for a restatement of the comparative balances of 2009 in the balance sheet of that particular programme. A restatement will not be needed in the EU financial statements since the correction is not considered as being material for these accounts.

Impact indicators

The financial organisation adopted by DG ECFIN has now been in place for seven years and has come to maturity. The implementation of DG ECFIN's budget in 2010 has been largely satisfactory thanks to a good implementation of the regulatory framework by financial actors inside the Directorate General and of contractual provisions by external partners (either other entities implementing EU programmes on behalf of DG ECFIN and/or final beneficiaries of EU funds).

With regard to balance of payments operations, the resurgence of the instrument was accompanied already in 2009 by the necessary reinforcement of the staff of the services responsible for the effective implementation of the financial assistance operations decided by the Council, in particular the fulfilment of the agreed economic policy conditions. These monitoring tasks are essential for ensuring a proper use of the on-lent EU funds and, ultimately, their reimbursement by the beneficiary country by the due date.

The DG benefited from a new and more significant reinforcement of staff in 2010 to allow for a better monitoring of reforms in Member States facing financial stability problems.

3.1.1.2. AOSD reporting

AOSDs were invited to follow a standard structure laid down in a template report, so as to ensure coverage of all relevant aspects. Most reports remained merely factual (amounts spent, number and type of operations, projects financed, etc.) and hence largely based on the information supplied by the financial unit. Some included more substantive or qualitative information on difficulties experienced, on the assessment of results achieved and objectives being reached (or not) or on lessons and recommendations for the future.

3.1.2. Results from independent audits during the reporting year

The **European Court of Auditors** (ECA) did not identify any significant weakness relating to internal control in the context of the audit of DG ECFIN activities in the course of 2010. In this context, the preliminary findings resulting from the 2010 audit of the SME Guarantee Facility, which will serve as a basis for the ECA Special Report on this activity, did not raise any issue that could be critical and, consequently, could lead to a reservation.

The **IAS** did not finalise any audit on DG ECFIN activities in 2010.

In 2010, the **IAC** finalised three new assurance audits and was drafting the report for a fourth audit. As far as the level of importance of the findings is concerned, out of a total of 25 recommendations issued, there were none classified as "critical", 8 have been classified as "very important", 16 as "important" and 1 as "desirable". It should be noted that only 1 of these "very important" recommendations can be considered as having a financial character but for which no financial errors were identified.

In its opinion on the state of internal control in the DG, the **IAC** of DG ECFIN concluded that, based on the results of the finalised audits, which included 8 "very important" recommendations concerning 6 specific issues, the internal control system in place in DG ECFIN provides reasonable assurance regarding the achievement of business objectives set up for the processes audited. According to the Action Plans which were prepared by the relevant services for all the audits, the "very important" recommendation having a financial character should be implemented in the third quarter of 2011, the other seven ones around mid-year 2011.

3.1.3. Follow up of action plans in reply to audit work performed in previous years and previous year's reservation

3.1.3.1. Follow up of previous year's reservation

DG ECFIN had no reservation in its 2009 Annual Activity Report.

3.1.3.2. Follow up of ECA findings and recommendations

For four years, the ECA has not issued any audit recommendation concerning DG ECFIN activities and all previous recommendations are completed. In its latest Annual Report covering the calendar year 2009, the Court concluded, in relation to the legality and regularity of budgetary financial transactions, that the supervisory and control systems of the DG were effective. In addition, the Court also found that, in 2009, the Guarantee Fund for External Actions was managed in a satisfactory manner.

3.1.3.3. Follow up of other weaknesses (other audit reports)

Audit recommendations are followed up using a dedicated system in the context of a six-monthly report to the Commissioner. A quarterly report on critical recommendations is also issued when necessary but no critical recommendations were issued in 2010 and there were none open from previous years.

As far as **IAS** is concerned, the implementation of the Action plan set up by the DG as a follow-up to the joint 2008 IAS/IAC audit on the effectiveness of the implementation of ICS in the policy-making Units has made further progress in 2010. Out of a total of seven, two recommendations remained in progress at end-2010, and the revised target date for their implementation has been fixed at mid-2011 for one of them and at end-2011 for the other one. Both of them have the status 'important' and have no particular significance in terms of potential financial impact.

Four recommendations from the 2009 audit on Treasury and Accounting Systems have been implemented in 2010, which leaves six recommendations in progress – one 'very important' and five

'important' ones. The pending 'very important' recommendation aims at ensuring the security of – mainly IT – systems and has as such no financial character. Out of the six sub-items of this recommendation, only one, relating to the update of the job description of the Local Information Security Officer (LISO) remains to be implemented. The target date for the implementation of all recommendations has been revised and it is now planned that two of them will be implemented by end-March, three by end-June (including the 'very important' one) and one by end-December 2011.

As far as IAC is concerned, from the follow up audit activity carried out in 2010, it seems that in general the auditees have considered all recommendations issued and made efforts to take actions which addressed the issues arising. Considering the five follow up audits carried out in 2010, the closure rate was satisfactory with 24 of the 28 recommendations assessed as closed by the auditors. The four remaining ones relate to the audit on training for which two 'important' recommendations are still in progress, and to the audit on the validation of user access rights in ABAC and SAP for which two 'very important' recommendations are not yet completed. Finally, the audits on the SMEG 2007 CIP approval process, on the management of the Venture Capital programme and on internal communication were considered as closed.

It was noted that from the 187 IAC recommendations issued in the years 2004-2009, 163 were considered as completed by the operational services. Of the 24 recommendations issued before 2010 and remaining in progress, six are significantly delayed: four concern the 2005 audit of local IT and the other two the audit on training. All these delayed recommendations are expected to be implemented in 2011.

3.1.4. Assurance received from other Authorising Officers in case of crossed sub-delegations

A co-delegation has been signed with OPOCE for the budget lines EMU and PRINCE only for the purpose of payments to be made in the framework of publications. OPOCE is reporting monthly on the use of the delegated financial resources.

With regard to the crossed sub-delegations with the EU representations in China, Japan and the USA in the framework of the PRINCE programme, a yearly report on activities carried out in 2010 was received in March 2011 from Beijing, Tokyo and Washington.

Finally, a crossed sub-delegation has also been given to DG EMPL in 2009 for a specific study. The second yearly report on this delegation was received on 28 January 2010. In his report, the AOSD indicates that all outstanding payment appropriations have been used up for the study in question and provides reasonable assurance that the delegated budgetary resources were used for the intended purpose and in conformity with the principle of sound financial management.

3.1.5. Completeness and reliability of the information reported in the building blocks

As far as the completeness of the information is concerned, all financial (budgetary or off-budget) activities of DG ECFIN are covered by appropriate and efficient control systems, on which information has been provided. Particular emphasis has been put on the activities for which specific control procedures have been put in place, because of their inherent risks and/or the amounts concerned.

Concerning the reliability of the information, all operational services with financial responsibilities and all control actors in the DG have been actively involved in the provision of relevant information and in the final approval of the AAR.

Finally, all major control actors within DG ECFIN have actively contributed to the drafting of the report. Most of them have a long experience in financial and/or internal control-related issues, which adds to the pertinence of the analysis.

3.2. Reservations

DG ECFIN considers that there is no need to present any new reservation on the 2010 declaration. Moreover, as mentioned in section 3.1.2 above, the preliminary findings of the 2010 ECA audit of the SME Guarantee Facility tend to show that DG ECFIN's decision to lift, in its 2009 Annual Activity Report, the 2008 reservation regarding the implementation of the 'additionality' requirements for a financial programme was appropriate.

3.3. Overall conclusions on the combined impact of the reservations on the declaration as a whole

There are no findings which could prevent the Director General from giving his reasonable assurance on the use of the resources.

4. DECLARATION OF ASSURANCE

I, the undersigned,

Director-General of the Economic and Financial Affairs Directorate General

In my capacity as authorising officer by delegation

Declare that the information contained in this report gives a true and fair view⁷.

State that I have reasonable assurance that the resources assigned to the activities described in this report have been used for their intended purpose and in accordance with the principles of sound financial management, and that the control procedures put in place give the necessary guarantees concerning the legality and regularity of the underlying transactions.

This reasonable assurance is based on my own judgement and on the information at my disposal, such as the results of the self-assessment, ex-post controls, the work of the internal audit capability, the observations of the Internal Audit Service and the lessons learnt from the reports of the Court of Auditors for years prior to the year of this declaration.

Confirm that I am not aware of anything not reported here which could harm the interests of the institution.

Brussels, 31 March 2011

[s i g n e d]

Marco Buti

⁷ *True and fair in this context means a reliable, complete and correct view on the state of affairs in the service.*