



EUROPEAN COMMISSION  
DIRECTORATE-GENERAL FOR ENERGY

# **Annual Activity Report 2010**

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## **1. Main Policy Achievements**

2010 has been a defining year for European Energy Policy: EU energy and climate goals are key components of the Europe 2020 strategy for smart, sustainable and inclusive growth of June 2010 and its flagship-initiative "Resource efficient Europe". In the Energy 2020 strategy of November 2010 the Commission set out the necessary steps to deliver Europe's medium term policy objectives. The strategy aims to consolidate existing achievements and to step up activities needed to face new challenges. It served as background for a discussion by Heads of State and Government at the special Energy Summit on 4 February 2011.

The following section, structured according to the four ABB (Activity Based Budgeting) activities of DG ENER, provides an overview of main policy achievements during 2010, contributing to the achievement of the three general objectives of DG Energy: competitive energy; sustainable energy; and secure energy supply.

### **1.1 Conventional and renewable energy**

On 10 November, the Commission adopted the Communication Energy 2020 - A strategy for competitive, sustainable and secure energy. The new strategy presents the main challenges ahead and puts forward five priorities to address them: an efficient use of energy that translates into 20% savings by 2020; an integrated market providing competitive prices, choice and security of supply; secure, safe and affordable provision of energy for citizens and businesses; technological leadership delivering innovative and cost-efficient solutions; and strong international partnership, notably with our neighbours. In parallel, the Directorate-General pursued preparations for the presentation of the Energy Roadmap 2050 during the second half of 2011.

As a consequence of the Deepwater Horizon oil rig accident the issue of the safety of offshore oil and gas activities became a new priority for the Directorate-General. The Commission adopted a Communication on the topic in October.

Some progress has been achieved against the objective to fully implement the internal energy market. Despite the efforts of the Commission, the degree of implementation and enforcement of legislation is nevertheless still unsatisfactory. By the end of 2010, the Commission had to report 64 open infringement procedures concerning the Second Energy Package. The target to have at least 3 suppliers for electricity and gas by household and non-household consumers at the end of 2010 has not been reached yet in all MS (by the end of 2010 22 MS had at least 3 suppliers for electricity and 19 Member States for gas).

Work also concentrated on preparations for the entry into force of the Third Energy Package on 3<sup>rd</sup> March 2011. Significant progress was achieved in putting in place the governance structures and staff of the Agency for the Cooperation of Energy Regulators (ACER).

In December 2010, the Commission adopted a proposal for a regulation on energy market integrity and transparency on wholesale energy markets, to prevent market manipulation and insider trading. It also adopted a Communication on Regional Initiatives in December seeking stakeholders' views on possible options for strengthening the effectiveness of the regional initiatives going forward.

The Directorate General undertook preparatory work on guidelines and harmonised network management rules across the EU in cooperation with the European Regulators' Group for Electricity and Gas (ERGEG) and the European Networks of Transmission System Operators

(ENTSO). Intense discussions took place with stakeholders in several meetings of the Madrid and Florence fora. The Citizen's Energy Forum discussed consumer aspects.

The Regulation concerning the notification to the Commission of investment projects in energy infrastructure, proposed by the Commission in 2009, was adopted in April 2010. On the basis of this, and after consulting relevant stakeholders, the Commission adopted the Regulation containing the tables for notifying this information in September 2010.

In order to strengthen provisions for solidarity and coordination in the case of gas supply disruptions, discussions on the Regulation on Gas Security of Supply were successfully concluded with its adoption in first reading. It considerably strengthens prevention and crisis response mechanisms. In this context, the DG also coordinated the crisis response mechanism put in place to handle the Belarus crisis affecting two Member States during the summer and the threat of a possible supply shortage in Poland during the autumn.

Close cooperation with MS and the International Energy Agency (IEA) ensured a high level of preparedness for emergency situations with regard to oil and petroleum products. The overall EU stock levels reached 125 days which is significantly above 90 days minimum required by legislation. Overall, the identified risk of disruptions of oil or gas supply was closely followed and the related action plan implemented. The Directorate-General also started to prepare the implementation of the new oil stocks Directive (transposition by MS: end of 2012).

In order to increase the share of renewable energy in the energy mix the Commission's work in the area of renewables in 2010 has in particular focused on implementation and transposition of the Directive on the promotion of the use of energy from renewable sources (2009/28). The Directive sets legally-binding national targets for the share of renewable energy to be achieved in each Member State and provides a comprehensive biofuels sustainability scheme.

By the end of 2010 all Member States had submitted their National Renewable Energy Action Plan required by Directive 2009/28. Moreover, a major Concerted Action Project aimed at assisting Member States in correctly and effectively implementing the Directive began in 2010.

In accordance with Article 17(9) of Directive 2009/28, the Commission adopted a report on sustainability requirements for the use of solid and gaseous biomass in February. Furthermore, to assist Member States in implementing the sustainability criteria for biofuels and bio liquids in the Directive, the Commission adopted two Communications on various aspects of the sustainability scheme in June. In August, the Commission, in accordance with Article 19 (4) of Directive 2009/28, adopted a report on greenhouse gas emissions from cultivation in third countries. In December the Commission adopted a report on indirect land-use change related to biofuels and bio liquids.

Against the objective to increase energy efficiency, even though there has been considerable progress, the EU is not on track to achieve the 20 % reduction by 2020. As underlined at the European Council on Energy on 4 February 2011, the commission will address the issue in a new Energy Efficiency Plan scheduled for March 2011. In the international context, the EU became a member of the International Partnership for Energy Efficiency Cooperation where work is now in full progress. A number of legislative advances in key energy consumption areas were made in 2010:

- Buildings: the recast of the Energy Performance of Buildings Directive was adopted by the legislators. It extends the scope of application of the Directive, strengthens the current system of national building efficiency requirements (to be set taking into account the entire life cycle costs) and provides for better information provision and quality checks.
- Products: the recast Energy Labelling Directive was adopted by the legislators. The scope of the Directive has been extended from household appliances to all energy-related products and new provisions on advertisements, promotional material and distance selling were added. Under this new framework the Commission adopted some product-specific delegated acts, as well as under the Iodising Directive during 2010.
- Supported by advice from the Commission, the Member States have progressed with implementing the Energy Services Directive and the Combined Heat and Power directive.

The promotion of renewables and increase of energy efficiency through the Intelligent Energy – Europe (IEE) Programme continued. The programme has helped to promote energy efficiency and renewable energy sources, while supporting small- and medium-sized enterprises. The programme also seeks to promote investments made by European stakeholders in sustainable energy. The introduction of the European Local ENergy Assistance (ELENA) (technical assistance for local and regional authorities when putting together "bankable" projects) proved to be very successful.

This implementation of the IEE is delegated to the Executive Agency for Competitiveness and Innovation. It implements its activities in close cooperation with its parent DGs, including DG Energy.

With the aim of contributing to European economic recovery through investing in the energy sector, significant funds were allocated to different projects via the European Energy Programme for Recovery (EERP). The implementation of all 44 gas and electricity infrastructure projects with an EU contribution of €2.27 billion has started. Three projects (gas inter-connectors between Romania and Hungary and between Hungary and Croatia, as well as one gas reverse flow project in Austria) have been in operation since the end of 2010. All six carbon capture and storage demonstration projects had started by the first half of 2010 with a €1 billion EU contribution.

The entire €65 million EU contribution to the nine offshore wind projects was committed in 2010. In order to mitigate the identified risk of failure to commit funds under the EERP, a regular reinforced monitoring has been introduced by the Directorate General covering all steps of project implementation. More details are given in section 3 and annex.

Key achievements undertaken to foster security of supply through an active external policy include the following:

- A renewed commitment came out of the 10th anniversary conference of the EU-Russia Energy Dialogue and the Permanent Partnership Council on energy held in 2010.
- The extension of the Energy Community Treaty to Moldova and Ukraine and progress in ongoing discussions with Turkey. The target that 80% of legislation in contracting

States to the Energy Community Treaty comply with the EU acquis at the end of 2010 was reached.

- In the Caspian and Central Asia region, the Commission continued to stimulate the development of the Southern Gas Corridor. Commissioner Oettinger visited Baku and Ashgabat in April 2010. This was followed by an Azerbaijan-Turkey transit arrangement in June 2010 and the ratification by all parties of the Nabucco Intergovernmental Agreement in August 2010.
- The Directorate General pursued numerous other activities with external partners, including the development of a series of instruments to assist the Southern Mediterranean countries with energy market reforms and the promotion of renewables, cooperation with US under the auspices of the EU-US Energy Council, enhancement of energy dialogue with China, launch of the trilateral EU-Brazil-Africa cooperation on sustainable bio-energy, and development of further cooperation under the EU-Africa Energy Partnership.

In the context of activities focused on the promotion of indigenous fossil fuels, the Commission started more detailed analyses of the potential of unconventional gas, and namely shale gas, in Europe.

## **1.2 Energy Infrastructure**

With the aim of improving security of energy supply through infrastructure, the Commission adopted the Communication on the Energy Infrastructure needs for 2020 and beyond on 17<sup>th</sup> November 2010. The Communication was a major input to the European Council of 4 February 2011 and lays the ground for the New Energy Security and Infrastructure Instrument to be presented in 2011. It also reflects infrastructure needs for the deployment of Carbon Capture and Storage (CCS) and stresses the importance of electricity highways. It is based on, among others, the TEN-E implementation report of March 2010 and the first Report on the EEPR of April 2010.

The European Network of Transmission System Operators for Electricity (ENTSO-E), with support from the European Commission, the European Regulators' Group for Electricity and Gas (EREG), and many key stakeholders, published its first pilot Ten-Year Network Development Plan on electricity infrastructure.

Work related to energy infrastructure also concentrated on the Baltic Energy Market and Interconnection Plan which is supported by major infrastructure projects funded under the EEPR and the TEN-E programme. The TEN-E work programme 2010 was successfully implemented (commitments of €20.76 million to 20 electricity and gas projects during the year).

## **1.3 Nuclear Energy**

Within the context of guaranteeing a high level of nuclear safety, three important global events gave new impetus to the Commission's efforts during 2010: the International Conference on Access to Civil Nuclear Energy, the Nuclear Security Summit, and the Non-Proliferation Treaty (NPT) Review Conference. Throughout the year, close international cooperation, especially with the IAEA (International Atomic Energy Agency), continued. Nuclear safety and security have been the prime issues covered.

The Directorate-General continued to handle the EU database on civil nuclear materials. During 2010, about 1.5 million lines of accounting data were dealt with. In March 2010, the

transition period for operators to implement electronic reporting under the Commission (Euratom) Regulation on the application of Euratom safeguards ended: all EU nuclear installations now report following the new requirements. Also the Additional Protocol (AP) on reporting to the IAEA was complied with in a satisfactory manner.

In December 2010 The Commission adopted the proposal for a Directive on the management of spent fuel and radioactive waste. Throughout the year, the Commission services supported Member States in the transposition and implementation of the Directive on nuclear safety. The transposition deadline is July 2011.

The Directorate-General continues to manage the decommissioning funds for Bulgaria, Lithuania and Slovakia (€255 million in 2010). In July 2010 the Council adopted a Regulation providing a further €300 million in financial support to Bulgaria to cover the period 2010-2013.

The European Nuclear Safety Regulators Group and the European Nuclear Energy Forum gave substantial technical support to improve safety, security and transparency at European level. Both organisations provided valuable input for the proposal on the management of spent fuel and radioactive waste.

A Commission Communication on medical applications of ionizing radiation and security of supply of radioisotopes for nuclear medicine was adopted in August 2010. It proposes a way forward to resolve the urgent issue of shortage of supply of radioisotopes for nuclear medicine. Related Council conclusions were adopted on 6 December 2010.

The new Commission Recommendation on the application of Article 37 of the Euratom Treaty was adopted in October 2010. Under this article each Member State has to inform the European Commission about any plan for the disposal of radioactive waste. The recommendation ensures consistency and clarity of the provisions and simplifies the data requirements for Member States. Eleven "Article 37 Euratom" opinions were drafted.

Also during 2010, the Commission undertook seven verifications of Member States' facilities for monitoring radioactivity in the environment under Article 35 Euratom.

Under the objective of verifying the security of nuclear material, verification activities performed by the DG ENER identified no case of diversion of nuclear material from its intended use. In the same period, no irregularities were observed throughout the EU by the IAEA. The number of inspections carried out by DG ENER decreased slightly from 1544 in 2009 to 1415 in 2010 and the total number of inspection person-days decreasing from 4155 in 2009 to 4024 in 2010. This decrease is mainly due to full implementation of the common inspection scheme under IAEA Integrated Safeguards in all EU Non-Nuclear Weapon States (NNWS) from 1 January 2010.

DG ENER continued its close follow-up of the directive issued in 2004 under Art 82 of the Euratom Treaty to the UK Government relating to safeguarding the nuclear material stored in pond B30 of the Sellafield site. DG ENER also followed-up a number of outstanding commitments on the part of the Sellafield operator concerning the warning issued under Art 83 of the Treaty which had been closed in summer 2009.

Close contacts were maintained with EU Member States throughout the year. Various meetings were held on approaches to safeguards and their implementation, including a 2-day meeting in Luxembourg for Member States representatives on Euratom safeguards implementation and related issues. With the accession of Romania to the Safeguards

Agreement between all EU NNWS, Euratom and the IAEA on 1 May 2010, all NNWS in the EU now are subject to common safeguards.

With the objective of ensuring the security of nuclear fuel supply, bilateral cooperation with other international partners has been improved through the preparation or negotiation of Euratom Agreements: the agreement with Canada is being renegotiated; the negotiations for a renewed agreement with Australia were concluded and the text will be submitted to the Council for approval during 2011; the negotiation mandate for a new agreement with South Africa was adopted during 2010; and negotiations have started towards the conclusion of a new agreement with the Russian Federation.

#### **1.4 RTD activities related to Energy**

Under the objective to develop and demonstrate cost-effective low-carbon technologies, the implementation of the Strategic Energy Technology (SET) Plan achieved important milestones. A total of six European Industrial Initiatives (EIIs) were launched by the Commission during 2010. They are the result of a close cooperation between different Commission services. DG ENER directly manages three of them (wind, CCS, nuclear) and is associated to the management of the other three ones (solar, grids, bioenergy) through working arrangements with DG RTD.

In addition, a portfolio of roughly €1.3 billion of FP 7 projects was implemented, with fewer but more focussed and relevant topics with greater European added value, increasing the participation and commitment of industry in research and demonstration work. The time needed for handling the approval and amendment procedures improved further (in 2010 more than 50% faster than in 2007). The share of funding for industrial participants, which increased from 47% in 2007 to 54% in 2008 and to 64% in 2009, remained at this level in 2010. This was possible while maintaining a high level participation of small and medium sized enterprises of approximately 20%.

The research priorities under FP7 build on the first results from ongoing or recently completed FP6 projects. The main results were related to technological changes for cost reduction (with a learning curve estimated to 2.5% per year), efficiency gains and enhanced reliability in electricity generation, bioenergy, heating and cooling and energy efficiency for industry and buildings (notably CONCERTO communities).

FP7 projects include the development and deployment of technologies for environmentally safer and more sustainable use of coal and other fossil fuels, focusing mainly on the technologies for carbon capture and storage. The European Industrial Initiative on CCS, a joint initiative of the Commission, MS and industry, was launched in June 2010.

In July 2010, DG ENER received the FP7 Energy Mid-Term Evaluation which was carried out by an external consultant. The report gave a generally positive assessment of the management of the FP7 energy projects. Recommendations have been used for further policy initiatives for example on Smart Cities.

## 2. Management and Internal Control Systems

### 2.1 Introduction to DG ENER

On 17.2.2010 the Commission decided to split DG TREN into DG ENER and DG MOVE, thereby creating a Directorate-General devoted to developing a European-level policy in the energy sector. DG ENER began work without major problems, despite the additional workload for the common services, especially in the human resources, IT, budgetary and financial planning, reporting and internal control areas.

The mission statements of the DG and its units were revised to reflect the changes and published on the DG's intranet. While the tasks of most units remained the same, there were notable exceptions:

- The DG TREN resources directorate was transformed into a Shared Resources Directorate for both DG MOVE and DG ENER. An additional shared unit (ex-TREN.P2) dealing with Internal Communication (document management, post distribution, library) was added;
- Similarly the DG TREN Internal Audit Capability was transformed into a Shared Internal Audit Capability for the two DGs, reporting directly to both Directors-General;
- The Inter-institutional relations, Planning and Programming, External communication, Impact Assessment, Research Coordination, Economic Analysis and Evaluation functions (the old TREN A1, P1 and P2) were split between the two DGs

Responsibility for state aids in the coal sector also passed to DG COMP on 17.2.2010 and a team of 4 staff dealing with international relations in the energy sector moved to DG ENER from DG RELEX in May. The Director-General of the former DG TREN sent a handover note to the Director-General of DG ENER on 18.2.2010 and to DG COMP on 17.2.2010.

DG ENER has 600 staff, including 8 in the Shared Internal Audit Capability (SIAC). Of these, 525 are on permanent posts and 75 are external.

DG ENER uses the partially decentralised model for the operational activities and the centralised model for all administrative expenditure related to Brussels-based activities<sup>1</sup>. There were no changes in DG ENER from the model applied in DG TREN.

In 2010 DG ENER managed its funds as set out in the table below. It managed €2.5 billion in commitment credits and €1.5 billion in payment appropriations directly, with execution rates being 94% and 80% respectively (compared to 99% and 86% for DG TREN in 2009). Adding the EACI, where DG ENER is a parent DG, makes no difference to these figures.

For the commitments and payments under its responsibility, DG ENER uses a system of sub-delegation where each deputy director-general and director is the authorising officer by sub-delegation for the commitments and payments under their responsibility. Commitments can only be authorised by a director or above, while heads of unit (or their deputies) can authorise payments and recovery orders.

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<sup>1</sup> According to the terminology used in the last revision of the guidelines on the Financial Circuits of June 2010

**Table 1: Main DG ENER programmes by management mode**

Programmes concerned	Management mode	Organisation	2010 Commitments (million €)	2010 Payments (million €)
EEPR	Direct centralised	-	1833.07	700.91
Energy support activities	Direct centralised	-	3.52	3.96
TEN-E	Direct centralised	-	20.76	18.86
Intelligent Energy	Direct centralised	-	21.92	7.1
	Indirect centralised	EACI <sup>2</sup>	76.26	54.74
	Joint	EIB <sup>3</sup>	15.00	0.00
Nuclear Decommissioning	Joint	EBRD <sup>4</sup>	155.00	147.95
	Indirect centralised	CPMA <sup>5</sup>	100.00	71.15
Research FP5	Direct centralised	-	-	1.24
Research FP6	Direct centralised	-	-	40.95
Research FP7	Direct centralised	-	150.57	105.51

### 2.1.1 The general control environment

The DG's general control environment consists of the following elements:

#### *Management meetings*

The Director-General, his deputies and the directors, including the director of Executive Agency for Competitiveness and Innovation (EACI) and the Euratom Supply Agency (ESA), meet usually every week to analyse work programme implementation, discuss matters of importance and coordinate the actions of the DG.

In addition the Directors-Generals of DG MOVE and DG ENER meet regularly with the Director of the Shared Resources Directorate to ensure coordination.

<sup>2</sup> Intelligent Energy Programme (IEE);

<sup>3</sup> European Investment Bank

<sup>4</sup> European Bank for Reconstruction and Development

<sup>5</sup> Central Project Management Agency in Lithuania

### *Internal monitoring and verification committee ("Comité de suivi")*

This Committee has a more detailed focus on financial and control issues than the management meetings. It is chaired by the Director-General and includes his deputies, as well as the directors, including from the EACI and the ESA, representatives of the units concerned in the SRD and the Shared Internal Audit Capability. In 2010 the Committee met three times and a sub-committee once to analyse key implementation indicators including risk assessment and other internal control matters and discuss budgetary and financial execution matters. Whenever relevant, the follow-up to ongoing or completed internal and external audits was also discussed.

### *Risk management*

Risks for potential inclusion in the DG's Risk Register are first identified and discussed in a senior management meeting when preparing the Management Plan. Units concerned are then tasked with drawing up an action plan with mitigation measures for each risk. These are then approved by the Director-General.

The implementation of the action plans and the risks themselves are then monitored throughout the year and reviewed at meetings of the Comité de suivi. If other significant or critical risks are identified during the year these are then added to the register, monitored and mitigation measures taken.

### *Programming Committee*

The Director-General chairs the Programming Committee, which consists of the Resources Director, the Head of the Financial Resources Unit and the Assistants to the Director-General. It usually meets once a year to decide on the actions to be financed for the year N+1. Before validating the descriptions of the actions proposed by directorates, the Committee verifies their coherence with the DG's priorities, the annual work programme and the approved budgets. These actions give rise to the annual financing decision and to *ad hoc* financing decisions.

### *Cross-delegations*

DG ENER has given cross-delegations to DGs DIGIT, ECFIN, ENTR, JRC, MOVE and RTD, as well as to the OP and PMO. It has received a cross-delegation from DG MOVE.

### *DG ENER's "Commission consultative interne des achats et marchés" (CCAM)*<sup>6</sup>

When launching a call for tenders, the technical services concerned verify the validity of the offers, the compliance with the terms of reference, the eligibility of the actions and the partners, the efficiency and effectiveness of the methods proposed and the quality of the tenders or proposals received by DG ENER.

In addition, procurement procedures leading to contracts with a value above €60 000 are analysed by the joint DG ENER and DG MOVE CCAM before the contracts are signed by the competent Authoring Officer. Chaired by the Director of the Shared Resources Directorate or, in his absence, by his advisor or the Head of the Financial Resources Unit, the CCAM is composed of members selected for their particular competence in the field of public procurement and it gives an opinion on the way in which the procurement was carried out and on the draft contract proposed for signature.

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<sup>6</sup> Internal Advisory Committee on Procurement and Contracts

### *Internal control groups*

Two networks contribute to internal control:

- the HR assistants network (weekly meetings);
- the network of assistants dedicated to internal control issues (working mainly through email exchanges).

### *Supervision of the Agencies*

The operational units responsible for the policies entrusted to the EACI and ACER agencies follow their activities closely. DG ENER's officials participate in several working groups set up to discuss technical issues and regular meetings take place between them and the staff from the agencies. Senior Commission officials are members of the ACER administrative board and of the EACI's steering committee. For more information, see the dedicated section 2.1.4 below.

### *Exceptions*

In accordance with Internal Control Standard 8, each deviation from an established process or procedure is documented, justified and approved at the appropriate management level before this level takes action. These are then registered in the Internal Control Registry and reported to the "Comité de Suivi" so that appropriate measures are taken in order to avoid any recurrence of these cases.

### *Impact Assessment and Evaluation*

The DG conducts impact assessments on all new policy initiatives in accordance with the Commission rules. It also regularly evaluates both spending and non-spending programmes.

### *Operational control*

Deliverables received are checked by the operational services in order to verify compliance with the contractual obligations. If necessary, on-the-spot missions by the agent in charge are organised in order to check the effective implementation of the programme and the correctness of the information received. For some programmes (e.g. the research framework programmes) external experts provide technical reviews which feed into the operational services' assessments.

In general Heads of Units act as operational verifying agents, approving deliverables and being responsible for the follow-up and supervision of the programmes and projects entrusted to their unit. The operational services provide the 'certified correct' declaration.

### *Financial control*

The Financial Execution Unit (for Brussels) and the Financial cell attached to the Deputy Director-General for Nuclear Energy (for Luxembourg) carry out the financial initiation and verification and provide the "passed for payment" declaration. Before it can be given, each financial deliverable (invoice or cost claim) is thoroughly checked to assess its compliance with the applicable rules. All the financial transactions are then sent for signature to the Authorising Officer concerned.

### *Ex-post controls*

There are two types of ex-post controls in the DG:

- Audit - on the basis of the work programme approved by the Director-General; the Audit unit (SRD5) concentrates its efforts on research projects in line with the audit strategy common to all Research DGs, which is one of the elements of the action plan on the reservation. Other areas managed by the DG are also covered to a lesser extent;
- Desk Control – this aims to detect errors made by the beneficiaries in their cost claims during the implementation of the projects so that errors can be corrected before the Commission makes the final payment. This aims to raise the beneficiaries' awareness of the rules they must follow when implementing projects funded by the Commission. In accordance with the action plan set up to address the reservation on the accuracy of cost claims in FP6, it concentrates on research projects.

### *Financial Reporting*

Budgetary and financial reporting provides regular and detailed financial indicators to management, such as on the consumption of commitment and payment credits and its comparison with the Budget Implementation Plan, the contracting of the global commitments, payment delays, the number and nature of exceptions, abnormal RAL<sup>7</sup>, error rates, implementation of the audit plan, recoveries and the number of cases sent to OLAF.

#### *Reporting by the Authorised officers by sub-delegation (AOSD)*

Each year each Director prepares their annual report to the Director-General, in which they identify potential weaknesses in internal control and may propose areas for a 'reservation' or 'risk', as well as reporting on political achievements and progress on programmes and policies. These reports, approved by the responsible Deputy Director-General where appropriate, include input from the Heads of Unit, who are also AOSD for payments and recoveries.

## **2.1.2 Working arrangements with the Commissioners**

The working arrangements between DG ENER and the Commissioner in charge of Energy have been defined and approved in writing. They were published on the internal intranet on March 26<sup>th</sup> 2010. DG ENER informs the Commissioner as soon as possible of any issue requiring their attention or action.

Periodic reports were sent each semester including information on work programme implementation and other matters relating to financial management, agencies (Executive and Regulatory), human resources management and internal control.

## **2.1.3 Events of particular importance**

There were no events of particular importance other than the creation of the DG.

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<sup>7</sup> Reste à liquider is DG Budget's estimate of the value of the outstanding commitments which have not been de-committed, but almost certainly should have been.

## 2.1.4 Agencies

In 2010, DG ENER was involved in the work of three agencies and one joint undertaking.

### *The Agency for the Cooperation of Energy Regulators (ACER)*

DG ENER is the "parent DG" for the Agency for the Cooperation of Energy Regulators (ACER) reflecting the needs of regulation of the European-wide energy market. This is a regulatory agency, which in 2010 had a budget of €2 million, exclusively financed by the EU. The Agency was set up in 2010<sup>8</sup> and worked under DG ENER's responsibility. The Executive Director was appointed in May 2010 and 7 staff were employed during the year. The seat agreement was also signed, and the Agency moved from Brussels to its Ljubljana headquarters in February 2011.

The Commission takes part in the governance of ACER by participating as a member of the administrative board. The Agency board includes five representatives nominated by the Council of Ministers, two by the European Parliament and two Commission representatives. The Director-General and the Director of the SRD ensure the consistency of DG ENER's policy on the board. As regards voting rights, the Commission does not have a majority on the board.

The operational unit responsible for electricity and gas markets is responsible for monitoring the agency's activities. It consists of wide range activities including regular coordination meetings at management level, numerous contacts at working level and reporting. Coordination of the horizontal issues related to the agencies is dealt by the SRD for budget, finance and administrative issues and Directorate A for inter-institutional and governance issues. Whenever necessary, bilateral meetings between DG ENER and ACER are organised.

### *The Executive Agency for Competitiveness and Innovation (EACI)*

DG ENER is a parent DG for the Executive Agency for Competitiveness & Innovation "EACI" which implements and manages the Intelligent Energy Europe (IEE), Marco Polo, Enterprise Europe Network (EEN), and Eco-innovation programmes on behalf of the European Commission. The EACI is monitored by four parent directorates-general, of which DG ENER is responsible for the Intelligent Energy Europe programme. In 2010 DG ENER contributed a €6.6 million to the running costs of the agency.

DG ENER has a supervisory role over the EACI in accordance with the rules established by the Council Regulation (EC) No 58/2003 laying down the statute for Executive Agencies to be entrusted with certain tasks in the management of Community programmes and the Commission Regulation (EC) No 1653/2004 of 21 September 2004 on a Standard Financial Regulation for the Executive Agencies pursuant to Council Regulation (EC) No 58/2003. This includes the definition of priorities and result-oriented goals in the annual work programmes approved by the Commission and an assessment of the activities carried out by the agency through the annual activity reports (AARs).

According to the Regulation (EC) No 58/2003, the Steering Committee decides the organisation of the departments of the agency, its organisational chart and staff policy. It adopts the agency's annual work programme (comprising detailed objectives and performance indicators), its administrative budget, and any special rules needed to implement the right of

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<sup>8</sup> Regulation (EC) 713/2009 of the European Parliament and of the Council of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulators, OJ L 211, 14.8.2009, p. 1

access to documents. It also adopts<sup>9</sup> and applies measures to combat fraud and irregularities in the implementation of the agencies' activities. The Steering Committee is responsible for adopting and submitting the executive agency's Annual Activity Reports to the Commission, together with related financial and management data. In 2010, the Deputy-Director General in charge of the Intelligent Energy Europe II programme represented DG ENER in the Steering Committee of the EACI.

The operational unit concerned ensures the regular supervision and monitoring of the EACI's work through reports and meetings in line with the instruments of delegation that formalise the relationship between the parent DG and Agencies. This unit also provides support to the Steering Committee. Coordination of the horizontal issues related to the agencies is dealt with by the SRD for budget, finance and administrative issues and Directorate A for inter-institutional and governance issues.

The EACI is obliged by its Acts of Delegation to regularly report on the performance of its tasks. These reports are prepared quarterly.

With the aim of providing detailed guidance on how DG ENER and the other parent DGs should communicate with the EACI on a day-to-day basis, Memoranda of Understanding were concluded. In addition, there are established "Guidelines for effective exchange of information between the EACI and parent DGs" and "Guidelines for effective financial and budgetary relations between the EACI and the parent DGs". In 2010 a new set of guidelines was produced, "Guidelines for effective relations between DG ENER and EACI in the establishment and management of concerted actions".

The EACI also uses ePMS, an IT application owned by DG ENER and DG MOVE, to manage the IEE programme as well as the EEN, Marco Polo and Eco-Innovation programmes (under the responsibility of DGs ENTR, MOVE and ENV).

### *The Euratom Supply Agency*

The Euratom Supply Agency was established in 1960 to ensure all users of nuclear energy in the EU receive a regular and equitable supply of ores and nuclear fuels. It is neither a "regulatory" nor an "executive" agency. It reports directly to the Commission (not to the DG), which can veto its Director-General's decisions. Its Director-General has to consult an advisory committee composed of most Member States on most decisions. The Commission is not represented on this Committee.

According to its statutes<sup>10</sup>, the Director-General of the Agency forwards an estimate of its budget to the Commission, which includes it in its draft budget. In its vote on the 2008 draft budget, the European Parliament did not allocate any budget to the Agency, a situation that has continued in subsequent years. DG ENER now bears the Agency's expenses under its own budget.

This situation has been criticised by the European Court of Auditors<sup>11</sup> and the Court has recommended that the Commission, in consultation with all the interested parties, should analyse the possible measures to remedy this situation. This analysis is ongoing.

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<sup>9</sup> Rules were adopted on 14.7.2005

<sup>10</sup> OJ L 41, 15.2.2008, p.15

<sup>11</sup> See the Court's Declaration of Assurance 2009, OJ C 206, paragraph 9.34

## *The Fuel Cells and Hydrogen Joint Undertaking*

DG ENER contributes (2010: €19.7 million) to the financing of the Fuel Cells and Hydrogen Joint Undertaking (FCH JU), for which DG RTD is responsible. This Joint Undertaking aims at increasing investment in the fuel cells and hydrogen sector in Europe, in the Member States and in countries associated to FP7. As regards FCH JU, DG ENER was represented in the administrative board by the Deputy Director-General responsible for Coordination of Directorates B and C.

### **2.2 The functioning of the entire internal control system**

In 2010 DG ENER continued improving its Internal Control framework by:

- implementing the actions necessary to reach the "baseline requirements" of the internal control standards prioritised for 2010;
- monitoring the implementation of the critical and other significant risks identified in the 2010 risk management exercise. No cross-cutting risks were identified;
- identifying the critical and other significant risks for 2011 (again, no cross-cutting risks were identified), as well as the prioritised internal control standards for 2011;
- regularly discussing internal control issues in the "Comité de suivi";
- updating the sections of the Manual of Financial and Contractual Procedures dealing with internal control and risk management, as well as the internal control intranet pages.

#### **2.2.1 Compliance with the requirements of the control standards**

The annual review of compliance with each of the standards took into account:

- the results of the annual self-assessment questionnaire on the functioning of the DG's internal control system. The iCAT<sup>12</sup> tool, customised to ENER and SRD's specific needs, was used on a population formed from management and non-management staff, as well as key staff involved in implementing the internal control standards;
- the results of the actions completed for the prioritised Internal Control Standards for the reporting year (see section 2.2.2 below);
- progress with implementing actions stemming from internal audit recommendations.

It concluded that the DG complies with all the internal control standards except the three stated below:

- *ICS 5: Objectives and Performance Indicators* - The level of involvement/awareness of staff in the development phase of the Management Plan should be increased. An action plan is in the process of being drawn up.
- *ICS 8: Processes and Procedures* - Even though substantial progress has been achieved in 2010, the DG's manual of contractual and financial procedures has not been completely updated. Also the manual of operational / internal (i.e. non-financial) procedures needs to be updated and published. This will be done in 2011.

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<sup>12</sup> Internal Control Assessment Tool, it is provided by DG BUDG

- *ICS 12: Information and Communication* – Here several issues require addressing:
  - Information to staff on decisions, projects or initiatives that affect them. This will be addressed through the development of an internal communication and staff engagement strategy in 2011;
  - Reporting of internal control weaknesses by all staff. Here efforts will be made in 2011 to raise staff awareness on the concept and the steps to take;
  - External communication strategy. Here improvements to the documentation of external communication and on monitoring its impact/results are required. An action plan is in the process of being drawn up;
  - Staff awareness of IT security. Here measures will be taken to increase staff awareness in 2011.

### **2.2.1.1 Derogations granted to the mandatory staff mobility requirement for sensitive functions**

In 2010 DG ENER did not derogate from the mandatory staff mobility requirement for sensitive functions. Since none of the persons assigned to one of the 51 posts in DG ENER which are qualified as sensitive has been in the post for more than 5 years, there was no need to consider extending the assignment for another 2 years (maximum 7 years) or re-assigning the person to another post.

### **2.2.2 Effectiveness of implementation of the prioritised control standards**

The four standards prioritised in the 2010 MP are set out below together with the measures taken during the year to ensure their effective implementation.

- *ICS 1 Mission* – was prioritised to define and update mission statements of the DG after the split of DG TREN. The revised statements were agreed and published on the intranet in November 2010.
- *ICS 3 Staff Allocation and Mobility* – was prioritised as it was considered that organisational and institutional changes after the split of DG TREN may require a redefinition of staff allocation and careful monitoring of staff turnover in order to recruit and retain staff with required skills. During the year measures were taken to align staff allocation with workload and priorities and a reorganisation of DG ENER came into force in December 2010. Due to resource constraints the "job mapping" exercise (part of the action plan) to identify key job profiles in DG ENER and the SRD has been postponed to 2011.
- *ICS 8 Processes and Procedures* - was prioritised because the modifications to the financial circuits made in 2008 and 2009 and the entry into force of the Lisbon Treaty required revision of the Manual of Financial and Contractual Procedures. With the exception of the chapter on financial management the manual has been revised and published. The chapter on Financial Management and the translation of all chapters into English and French will be completed in 2011.
- *ICS 11 Document Management* – was prioritised due to the introduction of ARES in the DG. The action plan aimed to ensure that the DG's document management system

is both efficient and compliant with the rules and to help units manage their documents. It was implemented and the migration to ARES took place in June 2010. As a result of this migration the creation of the Specific Retention List<sup>13</sup> has been postponed to 2011.

In addition, the DG will continue to work to improve the effectiveness of all the ICS.

### **2.2.3 Conclusion**

The main elements of appreciation of the functioning of DG ENER control systems in 2010 are illustrated in the previous sections.

In the light of the results of the assessment of the compliance and effectiveness of the internal control against the Internal Control Standards we can consider that the DG's control system works as intended and adequately mitigates the main risks to the achievement of the objectives of the Directorate-General.

The further improvements needed to ensure compliance with ICS 5 (objectives and indicators), 8 (procedures and processes) and 12 (information and communication) do not have a significant effect on the overall effectiveness of the system. Nevertheless, the changes will be made in 2011 along with the implementation of actions on ICS 3 (Staff allocation and Mobility) and ICS 11 (Document Management) carried over from the ICS prioritised in 2010.

Particular attention will continue to be paid to addressing overpayments in personnel and indirect costs in research payments. The measures taken are described in more detail in section 3.

## **2.3 Information to the Commissioner**

The main elements of this report and assurance declaration, including the envisaged reservation, have been brought to the attention of Commissioner Oettinger.

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<sup>13</sup> The Specific Retention List is drawn up by each Directorate-General when they have specific types of files that do not concern any other DG/Service and are not included in the common Commission-level Retention List. The DG needs to identify the file type of each file created and held by the Directorates-General (DGs) and equivalent departments in order to ensure that it is properly preserved; lay down the retention period for each type of file, taking into account its administrative usefulness for the departments, the statutory and legal obligations and its potential historical value; to establish the administrative procedures for the elimination of documents which the DG must apply to certain types of files; to define the action to be taken by the DG on the various types of files once the Administrative Retention Period has expired; and to determine what action should be taken by the Commission's Historical Archives Service on the various types of files received.

### **3. Building blocks towards the declaration of reasonable assurance (and reservations to it)**

#### **3.1 Building blocks towards reasonable assurance**

Reasonable assurance is based on the:

- assurance given by DG ENER's management, including the Director of the EACI;
- assurance given by the Authorising Officers by Delegation (AOD) implementing funds in cross-delegation;
- information gained in the context of the joint management with the EBRD and EIB, and centralised indirect management through the CPMA in Lithuania;
- results from Court of Auditors' audits and implementation of the measures to address weaknesses identified;
- results of the Commission's services' audits and implementation of the measures to address weaknesses identified;
- internal control coordinator's assurance;
- reporting on exceptions.

The materiality criteria used are:

- for non-research activities: the scope and nature of the weakness; its recurrent nature; controls put in place to mitigate it; and that the amount at risk represents more than 2% of the budget of the ABB activity concerned.
- for research activities: see annexe 4.

The impact on the Commission's reputation was also considered.

#### **3.1.1 Building block 1: Assessment by the management**

DG ENER's control strategy builds on the following key controls: risk management, monitoring project implementation closely, *ex ante* and *ex post* controls, exception monitoring and reporting.

##### **3.1.1.1 Risk Management**

DG ENER's 2010 management plan identified one critical risk on the overpayment of research grants made under the 6th and 7th Framework Programmes. Mitigating actions were the same as those taken under the follow-up of the 2009 AAR reservation on overpayment of research grants made under FP6 (see section 3.1.3.1).

No cross-cutting risks were identified in the 2010 or 2011 Management Plans.

##### **3.1.1.2 Monitoring project implementation closely**

Different projects are monitored in different ways as set out for the DG's major programmes below and in the internal control templates annexed. Corrective action is taken if these show

potential causes for concern. This could lead to a decision to conduct an audit or desk control of the projects concerned, or to the project being suspended or terminated.

### *Research Programmes*

For the FP6 programme, 75 projects were ongoing at the end of the year and no new projects were signed in 2010. The average duration of each project closed in 2010 was 46 months. The following technical monitoring took place:

- of the 75 projects, 53 were the subject of a report linked to a payment during the year;
- 60 of the projects had been visited by external expert reviewers and these reviewers attended 21 review meetings during the year;
- in addition, 12 projects were visited by technical officers and these officers attended 37 review meetings during the year;
- only 15 projects were not reviewed during 2010. 10 of these will be reviewed in 2011; 2 of the projects have been cancelled and the 3 remaining have finished.

For the FP7 programme, 57 projects were ongoing, of which 5 began in 2010. No projects closed in 2010. The following technical monitoring took place:

- of the 57 projects, 18 were the subject of a report linked to a payment during the year. None of these was linked to a final payment;
- an external expert reviewer attended 1 review meeting during the year;
- in addition, 7 projects were visited by technical officers and these officers attended 32 review meetings during the year;
- of the 22 projects with no technical review, project visit or meeting with the coordinator during the year, 19 will be reviewed in 2011. The remaining 3 projects are insufficiently advanced to be reviewed in 2011.

As a result the level of technical monitoring for both programmes is high and reflects the degree of advancement of the project. Further information is given in the annexed internal control template. All this information shows that the necessary measures are in place to ensure that assurance can be given from a technical perspective for both FP6 and FP7.

### *Nuclear Decommissioning*

Representatives of the DG participate in monitoring committees<sup>14</sup>, and, in the case of the EBRD, the assembly of contributors. Further information is given in the annexed internal control template. All this information shows that the necessary measures are in place to ensure that assurance can be given from a technical perspective.

### *European Energy Programme for Recovery*

In 2010 DG ENER continued managing the European Energy Programme for Recovery. This has three strands of activity: Carbon Capture and Storage, Offshore Wind and Energy

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<sup>14</sup> Like those set up to monitor the nuclear decommissioning projects implemented by the Central Project Management Agency (CPMA) in Lithuania

Interconnectors. The DG set up a task force to coordinate and to monitor the programme's implementation closely. The following technical monitoring took place:

- for carbon capture and storage, three projects began in 2010 and three were already ongoing. All six projects have been the subject of at least one technical report by the end of the year. During the year the technical officers responsible visited one of the projects, attended four review meetings and reviewed all 20 deliverables submitted. External reviewers reviewed four deliverables and attended four review meetings;
- for offshore wind, all nine projects began in 2010, one of which was the subject of a technical report by the end of the year. The technical officer responsible visited three projects during the year and attended seven review meetings. Two deliverables were submitted. Both were reviewed by the technical officers and one by an external reviewer;
- for energy interconnectors, all 43 projects began in 2010, 10 of which were the subject of a technical report by the end of the year. Technical officers visited 15 projects in 2010 and attended 50 review meetings.

Given that the programme is relatively new and some of the projects have not advanced to the stage of having documents that could be read or installations that could be visited, the technical monitoring is proportionate to the needs. Further information is given in the annexed internal control template. All this information shows that the necessary measures are in place to ensure that, from a technical perspective, assurance can be given.

#### *Intelligent Energy Europe Programme*

Approximately two-thirds of the budget is managed by the EACI, one-sixth by the EIB and the final sixth by DG ENER.

As mentioned in section 2.1.4 above, DG ENER supervises the EACI. The Director of the EACI has also given his reasonable assurance on the Agency's activities (see section 2.1.4 and Annex 7)

DG ENER gives a cross sub-delegation to DG ECFIN to implement the European Local ENergy Assistance (ELENA) facility<sup>15</sup> with the European Investment Bank. The Director-General of DG ECFIN has given reasonable assurance. The facility is managed under joint management between the Commission and the EIB and there is a Steering Committee in which both the EIB and the Commission are equally represented. There is also a technical committee, in which DG ENER is represented, which met twice in 2010.

DG ENER and DG ECFIN have to approve each of the projects for funding by the EIB. During the lifetime of each project the beneficiary has to submit three separate reports on implementation, on which DG ENER and DG ECFIN are consulted before the payment is approved by the EIB. In addition, the EIB provides the Commission with monthly financial reporting on the fund and will submit an annual report to the Commission on the implementation of the facility, the first of which is planned for submission by the end of March 2011.

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<sup>15</sup> 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

At the end of 2010, 8 projects had been approved, 5 contracts signed and one report had been submitted by the beneficiary.

The final sixth is managed by the DG and is largely spent on procurement.

### *TEN-E*

DG ENER manages the Trans-European Networks for Energy budget, which amounts to around €20-€25 million each year. In 2010 the commitments were for €20.76 million. 90% of this budget is for studies and 10% for construction projects. In 2010, 83 projects were ongoing representing €101.4 million. The average project duration is 3-4 years.

DG ENER conducts monitoring on the basis of two deliverables:

- annual reports on implementation progress. These reports consider progress, including risks and mitigating measures. The reports are reviewed by DG ENER's technical staff and, if necessary, amending decisions are prepared (e.g. if a deadline extension or changes to the budget breakdown are required);
- reports accompanying requests for payment. These have to include a technical summary of the project, as well as an explanation of the project's results. An audit certificate is required for the costs incurred and the Member State concerned also has to certify that expenditure is directly related to the implementation of the project for which payment is claimed. If the payment is a final payment then the Member State concerned also has to give its assessment of the project. The Commission only approves the payment if all these elements are available and satisfactory. If the project is a construction work, the Commission official could make on-spot visit.

In addition, for construction projects, the Commission aims to visit once during the project, provided the project is visible (this is not the case for underwater pipelines, for example). In 2010 one project was visited by the Commission.

As a result the Commission considers that it can give reasonable assurance on the TEN-E expenditure for 2010.

### *Indicators*

Most indicators in the table below show good progress. This is particularly true for the reduced payment delays, the increased payments made by the contractual deadline and the reduced number of old contracts.

For payment delays<sup>16</sup> in particular, the improvement over the recent past has been dramatic. The time to payment has decreased from 47.5 days in 2008 to 26.7 days in 2010 and the percentage of payments made during the contractual deadline has also increased significantly from 58% in 2008 to 91% in 2010. In addition, for 99% of all payments, DG ENER's performance is above the Commission average.

The decrease in the commitments and payments percentages compared to the final annual budget was caused by the European Energy Programme for Recovery. For commitments, €146 million (3.7% of the EEPR envelope) could not be committed by the end of year

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<sup>16</sup> Unlike the figures in Table 6 of Annex 3, these figures include payments made by the PMO for administrative expenditure.

deadline. This amount was reallocated by the Council and Parliament to a new financial facility supporting energy efficiency and renewable energy initiatives and DG ENER has requested the carry over to 2011 of the corresponding amount. For payments, EEPR beneficiaries did not request pre-financing payments (for reasons such as delays in obtaining the required environmental permits, the need to provide bank guarantees) and there were less intermediate payments.

The FP6 error rate is discussed in more detail in section 3.1.1.5.

**Table 2: Indicators for Specific Objectives**

Specific objectives: “Plan, perform, monitor and report on the spending of financial resources so that sound and regular management of them is assured throughout the DG’s activities” and “Implement and maintain an effective and reliable internal control system so that reasonable assurance can be given that resources assigned to the activities are used according to 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.”		
Indicator	Latest known result	Target
Commitments budget carried out compared to final annual budget (%)	31/12/2010: 91% 31/12/2009: 99% 31/12/2008: 99 %	>98 %
Payments budget carried out compared to final annual budget (%)	31/12/2010: 80% 31/12/2009: 91 % 31/12/2008: 83%	>90 %
Average time taken to make payments (days)	31/12/2010: 26.7 31/12/2009/ 37.7 31/12/2008: 47.5	< 30
Payments made by contractual deadline (%)	31/12/2010: 91% 31/12/2009: 67 % 31/12/2008: 58 %	>80 %
Number of open contracts that are more than 5 years old	31/12/2010: 48 31/12/2009: 93 31/12/2008: 239	< 80
Individualisation of global commitments carried forward (%)	31/12/2010: 99.8% 31/12/2009: 98.2% 31/12/2008: 99 %	>99 %
FP6 budget free from material errors and thus contributing to implementing the FP6 Audit Strategy (%)	31/10/2010: 95.6% 31/10/2009: 96%	31/12/2010: < 98

During 2010 OLAF closed six of the eight open OLAF cases and ENER reported one new irregularity to OLAF. Three ENER cases are therefore being dealt with by OLAF, two of which are being investigated and one is being evaluated.

Four of the cases closed by OLAF required legal or financial follow-up. For three of them this has been completed.

### 3.1.1.3 Ex-ante control

#### 3.1.1.3.1 Procurement

In 2010 the internal CCAM analysed 30 files (27 DG ENER, 3 SRD) resulting in 8 unconditional positive opinions, 13 positive opinions subject to comments being taken into account and 9 suspended opinions. No negative opinions were given in 2010, meaning that no major procedural faults were detected and 29 files were ultimately given a positive opinion (one was withdrawn). To further improve the situation, two training sessions were given that have had a positive impact on the quality of procurement procedures.

#### 3.1.1.3.2 Financial initiation and verification

While the split of DG TREN into DG MOVE and DG ENER took place in mid-February, the budget lines for the two DGs were only split from June 2010. The main errors detected and corrected in interim and final payments were:

- *in contracts*: services were claimed that were not included in the purchase order; travelling expenses which exceeded the limits set (i.e. daily allowance, business class instead of economy, etc); and

**Table 3: Statistics for Contracts**

Invoice	TREN (up to June 2010)	ENER (from June 2010)
Number	625	463
Total amount (€)	16 038 661.12	14 231 200.17
Credit notes (number)	43	35
Credit notes (€)	436 138.13	845 243.91
Number corrected (%)	6.88	7.56
Amount corrected (%)	2.72	5.94

- *in grant agreements*: inconsistencies between the information supplied by grant beneficiaries (amount of costs, methods of calculation, periods, etc.) and that included in the audit certificate; incomplete (or missing) audit certificates; arithmetical errors; audit certificates not provided by a qualified auditor; costs incurred outside the eligibility period; costs not covered by the legal basis.

**Table 4: Statistics for Grant Agreements**

Cost claims	TREN (up to June 2010)	ENER (from June 2010)
Number	234	232
Total amount (€)	282 108 103.76	260 638 403.70
Corrections (number)	35	45
Non-eligible amounts (€)	4 771 596.10	3 411 425.20
Number corrected (%)	14.96	19.4
Amount corrected (%)	1.69	1.31

These figures show that the ex-ante financial control works adequately and that the errors detected were within an acceptable margin. This has prevented the payment of €9.5 million of ineligible expenditure corresponding to 1.65% of the total claimed by the contractors and beneficiaries.

#### **3.1.1.4 Exception reporting**

In 2010 all exceptions were documented in a register and periodic reporting to the "comité de suivi" took place. None of the exceptions was considered to have a negative impact on giving reasonable assurance.

#### **3.1.1.5 Ex-post control**

##### *3.1.1.5.1 Desk Control*

In 2010 31 controls on FP6 projects were worked on, of which 10 were new controls and 21 carryovers from 2009. As of 31 December 2010, 10 of these have been completed, 18 are ongoing, 2 have been cancelled and 1 has been transferred to the financial audit unit for a full audit.

Completion of desk control reports has been slower than planned. This was largely due to unoccupied posts and sick leave as well as with the difficulties of dealing with controls related to payments made before 2009. Changes have been made to the selection and control methodology during the year, which should lead to increased future output.

Of the 10 controls completed in 2010, 4 contained errors in favour of the Commission and 2 errors in favour of the contractor. The errors in favour of the Commission led to recommendations to recover €77 995.01 representing 7.54%<sup>17</sup> of the total amount controlled over the 10 completed controls. As these controls are risk-based the errors found are not representative and cannot be extrapolated to all FP6 payments.

Just as for audits, the errors found mainly concerned the incorrect calculation of personnel costs (use of estimated or average costs and use of non-actual productive hours).

<sup>17</sup> This figure, which is calculated according to the standard method agreed amongst the Research DGs, does not take into account errors in favour of the contractor.

### 3.1.1.5.2 Audits

During 2010, 91 audits were finalised<sup>18</sup> of which 90 were on the research programmes (2 for FP5, 82 for FP6<sup>19</sup>, and 6 for FP7) and 1 on the nuclear decommissioning funds (Ignalina CPMA). The resources devoted to the audits done by the DG and outsourced are shown in the table below.

**Table 5: Resources devoted to audits in 2010**

	2009	2010
Internal resources ex-post audits (FTE)	17	15.8
Cost of outsourced auditing (€)	1 335 472	1 421 066

### *Research*

For FP7 the figures presented are only for DG ENER's projects, whereas for FP5 and FP6 they concern both DG ENER and DG MOVE as the audit strategy was drawn up in the time of DG TREN.

### *FP5*

In 2010, 2 audits were finalised for FP5. No new audits were started.

**Table 6: FP5 Audits: quantity**

FP5	Planned cumulative period <sup>20</sup>	Achieved cumulative period	Planned in 2010	Achieved in 2010
Number of closed audits	n.a.	236	n.a.	2
Total amount audited (EC share in €)	n.a.	105 670 435.63	n.a.	1 236 698.09

The overall error rate in favour of the Commission was 11.87%, which corresponds to a recovered amount of €10.99 million. There are no ongoing FP5 projects.

<sup>18</sup> An audit is considered finalised when the final audit report is sent by the Financial Audit Unit (SRD.5) to the Financial Management Unit (SRD.3) for implementation.

<sup>19</sup> For FP5 and FP6 this includes both energy and transport.

<sup>20</sup> The cumulative period for FP5 is 2003-2010; for FP6 is 2007-2010; for FP7: 2010-2016.

**Table 7: FP5 Audits: results**

FP5	Achieved cumulative period	Achieved in 2010
Costs accepted by Financial Officers (EC share, in €) (A)	105 670 435.63	1 236 698.09
Systematic errors (number of extrapolation cases, as % of total)	n a	n a
Overall errors (in €) in favour of the Commission (B) (costs accepted by auditors - costs accepted by FO, in €)	-12 543 059.86	-2 384.53
Error rate in favour of the Commission (B/A)	-11.87%	-0.19%
Overall errors in favour of the beneficiary (EC share, in €) (C)	4 699 026.30	55 751.05
Error rate in favour of the beneficiary (for info) (C/A)	4.45%	4.51%
Total amount of adjustments implemented (EC share, in €)	-10 995 896.21	-
Residual error rate (%)	n.a.	n.a.

The payments made in 2010 for FP5 represent 0.09% of the total amount paid by DG ENER and 0.7% of the ABB activity. In view of the low impact of the amount at risk, together with the fact that there are no more ongoing projects, it is not considered necessary to qualify the declaration of assurance with a reservation.

## ***FP6***

### *Coverage*

When the FP6 audit strategy was set up DG TREN's objective was to finalise the audit of 344 contractors between 2007 and 2010. These 344 were to be composed of the 125 TOP<sup>21</sup> contractors by value corresponding to 50% of the budget, 161 MUS<sup>22</sup> contractors and 58 contractors selected on the basis of their risk. The split of DG TREN did not change this objective or the strategy, which remained common to the two DGs.

As can be seen in the table below, 323 audits were finalised by DG ENER and DG MOVE. Despite this being slightly below the target of 344 the overall objective can be considered met because a further 50 were considered unnecessary or were stopped.<sup>23</sup> This takes the real total to 373 audits.

In conclusion, for the purpose of the FP6 audit strategy, we can consider 373 audits as achieved, compared to the target of 344 audits.

<sup>21</sup> TOP contractors are the beneficiaries having received the most important financial contribution. Initially, 40% of the budget was included under this category. In 2009, this category was extended to 50% of the budget.

<sup>22</sup> MUS contractors are beneficiaries selected using the Monetary Unit Sampling. A statistical sample of 161 beneficiaries for each research Directorate General was selected to be audited.

<sup>23</sup> 42 audits were considered unnecessary as the beneficiaries had already been audited 3 times by the research DGs for at least 3 other projects, a further 5 were not necessary because the projects were terminated without any costs submitted, a further 4 contractors merged to form 2 (resulting in 2 rather than 4 audits) and one audit was stopped with full recovery of costs.

The number of risk audits (which include preventive audits<sup>24</sup>) was higher than planned and the number of TOP and MUS audits lower because, as mentioned above, some contractors had already been audited three times by other DGs. This was the case for 18 of DG TREN's TOP contractors and 24 of its MUS contractors. In addition, at the beginning of the audit strategy, many contractors had not submitted an expense claim to the Commission meaning that it would have been too early to conduct a meaningful audit. Additional risk audits were done partially to offset these factors.

The following table shows how the coverage has evolved.

**Table 8: FP6 audits: quantity**

FP6	Planned cumulative period	Achieved cumulative period	Planned in 2010	Achieved in 2010
Number of closed audits	344	323	101	82
Audits TOP contractors	124	98	20	16
Audits MUS contractors	161	96	71	43
Audits Risk-based contractors	58	129	10	23
Total amount audited (EC share in €)	n.a.	128 429 662.44	n.a.	18 616 515.41

### *Results*

The results of these audits give a residual error rate of 4.42% for the whole population<sup>25</sup>, which represents the rate that will be undetected and uncorrected after all controls have been put in place. Even if the rate of 4.42% is still above the control objective of 2% the fact that this rate is lower than for FP5 may indicate that the FP6 audit strategy has produced results. Nevertheless, the structural nature of the contractors participating in and the type of projects run by DG ENER and DG MOVE are likely to be the main causes of the error rate remaining above 2%. As results from a study have shown:

- participants are mainly from municipalities, ministries, national institutes owned by the government, police and research (but non-university) organisations, which are typically the organisations that have the highest error rates;
- they are generally smaller than the organisations audited by DG RTD and DG INFSO. Small organisations typically have a higher error rate than large organisations;
- they are more likely to use the full costs model for reimbursement, which is the one with the highest level of error;

<sup>24</sup> “Preventive” audits target types of expenditure where errors most often occur (mainly personnel costs). One of their objectives is to help final beneficiaries learn so that the residual error rate will decrease in the long term. Beneficiaries generally appreciate these audits as they can see which costs they have declared incorrectly and how they could declare them properly. As these audits are carried out while the project is running, errors can be corrected in subsequent cost claims thus avoiding the Commission recovering funds once the project has ended.

<sup>25</sup> The residual error rate is only based on the results of the MUS audits and does not take account of the results of risk-based audits.

- the projects are more likely to be "integrated projects"<sup>26</sup>, which have a high error rate.

The following table shows how error rates have evolved.

**Table 9: FP6 audit results**

FP6	Achieved cumulative period	Achieved in 2010
Costs accepted by Financial Officers (EC share, in €) (A)	128 429 662.44	18 616 515.41
Systematic errors (number of extrapolation cases, as % of total)	25.7%	26.83%
Overall errors (in €) in favour of the Commission (B) (costs accepted by auditors - costs accepted by FO, in €)	-9 813 129.88	-2 396 097.01
Error rate in favour of the Commission (B/A)	-7.64%	-12.87%
Overall errors in favour of the beneficiary (EC share, in €) (C)	3 381 377.77	1 283 683.81
Error rate in favour of the beneficiary (for info) (C/A)	2.63%	6.90%
Total amount of adjustments implemented (EC share, in €)	5 111 603.22	727 541.36
From audit implementation:	4 660 901.28	727 541.36
From audit extrapolation:	450 701.94	-
Residual error rate (%)	4.42%	-

### *Adjustments implemented*

Of the €8 million of errors in FP6 detected by the auditors, adjustments for €4.7 million (48%) have already been implemented and €2.2 million were in the contradictory procedure with the beneficiary. This means that 70% (€6.9 million) of the errors detected by the auditors have been processed by the AOSDs.

<sup>26</sup> An Integrated Project is an instrument to support objective-driven research, where the primary deliverable is new knowledge.

**Table 10: FP6: audit adjustments implementation progress**

Audit closing year	Results from external audits		Adjustments in contradictory procedure with the beneficiary		Adjustments implemented	
	Number of participations	Funding adjustments set by AOSDs	Number	Value	Number	Value
2007	1	34 631.32	0	0,00	1	34 631.32
2008	18	704 772.18	5	161 497.73	13	543 274.45
2009	118	4 674 844.94	35	1 319 390.79	83	3 355 454.15
2010	42	1 468 316.90	25	740 775.54	17	727 541.36
<b>Total</b>	<b>179</b>	<b>6 882 565.34</b>	<b>65</b>	<b>2 221 664.06</b>	<b>114</b>	<b>4 660 901.28</b>

Of the €4.7 million already implemented 68% was recovered through offsetting the adjustment from subsequent payments and 32% through recovery orders.

**Table 11: FP6 audit adjustments by implementation mode**

Audit closing year	Adjustments implemented by implementation mode(in value)		
	Offset from payments	Recoveries	Waived
2007	0.00	34 631.32	0.00
2008	471 619.98	71 654.47	0.00
2009	2 105 293.34	1 250 160.81	0.00
2010	593 784.79	133 756.60	0.00
<b>Total</b>	<b>3 170 698.11</b>	<b>1 490 203.20</b>	<b>0.00</b>

In addition, further corrections were made to the same beneficiaries participating in other DG MOVE/ENER research projects. These corrections stem from audits made by DG MOVE/ENER or other DGs in the research family where systematic errors were found. 433 such participations were found and the beneficiaries were asked to rectify the errors in DG MOVE/ENER projects and submit revised cost statements. On the basis of this 157 participations were judged not to be concerned by the systematic errors identified by DG MOVE/ENER or any of the other DGs. Of the remaining 276 participations, 43 have been corrected so far by DG MOVE/ENER leading to €450 000 being recovered. For 180 participations the beneficiary has been asked to revise their cost statements by the AOSD. The remaining 53 are being dealt with by other DGs.

**Table 12: FP6 audits: extrapolation progress**

Year	Number of participations with expected systematic errors	Number of participations without systematic errors	Implemented cases				Number of participations with extrapolation managed centrally <sup>27</sup>	Number of participations to be implemented <sup>28</sup>
			In favour of the Commission		In favour of beneficiary			
			Number	Value	Number	Value		
2007	6	0	1	70 366.85	0	0.00	0	5
2008	160	68	18	349 209.12	13	99 220.36	23	38
2009	194	59	5	31 125.97	6	28 097.23	30	94
2010	73	30	0	0.00	0	0.00	0	43
<b>Total</b>	<b>433</b>	<b>157</b>	<b>24</b>	<b>450 701.94</b>	<b>19</b>	<b>127 317.59</b>	<b>53</b>	<b>180</b>

### *Liquidated damages*

Liquidated damages are a financial penalty that the beneficiary has to pay if they breach contractual obligations. This includes when they overclaim contributions to funding in the research programmes. In these cases the beneficiary has to repay the overpaid amount plus the liquidated damages. The extent of the liquidated damages is proportionate to the overstated costs and the unjustified amount received by the beneficiary.

Since its creation, DG ENER has applied liquidated damages to beneficiaries who received unjustified EU contributions in the research programmes. By the end of 2010 there had been 12 cases and in 6 recovery orders have been issued totalling €12 505. For cost-effectiveness reasons, DG ENER does not apply liquidated damages when the amount to recover is less than €200. As a result no damages were sought in the 6 other cases.

### *Assessment of cost effectiveness*

Without prejudice to evaluating whether the DG's management and control systems have succeeded in reducing the error rate below the current materiality threshold of 2%,<sup>29</sup> it is also meaningful to assess whether the control system has been cost-effective<sup>30</sup> in accordance with "sound financial management"<sup>31</sup>.

When considering the total cost of control, covering all stages and elements of the entire (ex-ante and ex-post) control chain, it has to be understood that a significant part of the existing controls are established outside the scope of the AOD's discretionary decision-making

<sup>27</sup> Cases managed centrally refer to those with beneficiaries confronted with a large number of cases.

<sup>28</sup> Cases to be implemented are those for which the Commission has written to the beneficiaries requesting them to submit revised cost statements to correct the systematic issues detected.

<sup>29</sup> i.e. 'regardless' of the corresponding costs of control, and irrespective of whether or not an error rate within the range between 2% and 5% would one day be considered to be a "tolerable risk of error" (TRE) for the management of this policy area

<sup>30</sup> At a certain stage in the lifecycle of the programmes managed, it may be that a trade-off decision is to be made between still adding controls to try reducing even further the remaining risks (inspired by art 60.4 FR), or stop adding controls for reasons of sound financial management (inspired by art 27 & 60.1 FR) and reallocate resources to address risks in other management areas.

<sup>31</sup> in accordance with the principles of economy, efficiency and effectiveness

powers. The Financial Regulation requires many of the ex-ante controls regardless of whether their results, in terms of contributing to reasonable assurance, match the investment in inputs and coverage (e.g. the requirement of 100% coverage by ex-ante desk checks). In addition, for reasons such as a desire to speed up processes and to simplify the 'administrative' requirements to be fulfilled by beneficiaries of EC funds, some ex-ante controls have been reduced in scope and/or coverage (a trend which was accompanied by focusing more on ex-post controls). This may limit their potential contribution to reasonable assurance. As a result it is not meaningful to conduct a "full cost" analysis of the total cost<sup>32</sup> of the entire control system in order to determine whether it makes sense, from the perspective of sound financial management to invest more resources in additional controls.

In FP6, the AOD has considerable discretionary power<sup>33</sup> over ex-post controls (i.e. on-the-spot audits of beneficiaries). As this contributes significantly to giving reasonable assurance, the Research DGs have designed and implemented the "common FP6 audit strategy" mentioned in previous sections. As the scope and cost can vary per audit it is logical to look at them to determine the cost-effectiveness of the DG's control strategy.

Comparing the "marginal cost vs. marginal benefit" of these ex-post controls is useful to verify whether the optimal cut-off point in terms of cost-effective controls has been reached. This point is the level of control with a sound cost-efficiency ratio that limits the residual error rate to a reasonable level. This level will not necessarily be the current 2% materiality threshold. The costs of going beyond this level of control, such as by adding additional controls, would outweigh the benefits. As such the AOD could then consider reallocating resources to other actions<sup>34</sup>, which would be more cost-effective.

The "best-case scenario"<sup>35</sup>, which assumes that the next control delivers the highest yield in absolute terms, cannot be used in advance to determine the marginal benefit. Instead of using a purely "random selection"<sup>36</sup> or an "average-based" approach a pragmatic "in-between scenario" would be to rank the beneficiaries by funding received, so that, even when based on the (cumulative) average error rate, the expected return of adding a control on the 'next largest' beneficiary is greater than the cost of control.

Using this approach gives the following:

- the expected marginal cost of control is €60 000. This includes the cost of staff and or contractors as well as the cost of processing the audit results;
- the cumulative error rate expected (on the basis of representative FP6 controls undertaken to date) is 7.18%<sup>37</sup>;
- for there to be a marginal benefit of control the value of the error rate must be greater than €60 000.<sup>38</sup> It must therefore be assumed that €60 000 is equivalent to 7.18%. This

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<sup>32</sup> including costs which are to be considered as "sunk costs" for the purpose of managerial decision making

<sup>33</sup> the flexibility for ex-post controls provided for in article 60.4 of the financial regulation

<sup>34</sup> to the subsequent programme (while still ensuring a number of risk-based audits and/or audits for continued dissuasive effect) and/or to more sophisticated anti-fraud measures

<sup>35</sup> model 2A as described in the Commission Communication COM(2010)261 of 26.05.2010 and related working document SEC(2010)641

<sup>36</sup> model 2B in the aforementioned communication

<sup>37</sup> This differs from the 7.64% cumulative error rate shown in the table in the previous section. This is because the 7.64% includes the results of risk-based audits, which are not representative of the overall population and usually have higher than average error rates. The 7.18% only considers representative audits and is a better basis for calculation.

gives the threshold under which contracts should not be audited as €38 259 of EC funding received;

- For DG ENER/MOVE there are 34 non-audited contracts above this threshold.
- When ranked in order of value, the 34<sup>th</sup>, the value of the 'next' marginal control, gives a marginal benefit of €60 186.99.

Considering the general characteristics of the FP6 programme, while taking into account the specificities of DG ENER/MOVE in terms of (i) the typical 'size(s)' of its beneficiaries, (ii) its (cumulative) average detected error rate, and (iii) the average cost of an audit per beneficiary, it appears that the DG has not yet reached the optimal cut-off point in terms of cost-effective controls in the context of sound financial management. Consequently, additional controls remain necessary until the optimal cut-off point in terms of cost-effective controls has been reached.

### *Conclusion*

The DG's FP6 control strategy has been implemented successfully (see coverage) and quite effectively (see results); it has been able to improve assurance by reducing the residual error rate to a level of 4.42%. While this result is a significant improvement on FP5 the DG has not been able to attain the 2% materiality control target. Consequently, the conditions for maintaining a reservation on FP6 are still met.

### *FP7*

The FP7 audit strategy was agreed on 30 September 2009 and implementation started in March 2010. During the year six audits were finalised, of which only one can be considered part of a representative sample. While this number may seem low, this is normal because there is a time lag between when a framework programme begins and when its beneficiaries becomes sufficiently numerous (i.e. those having submitted cost statements large enough to allow a cost-effective audit mission) to allow sampling.

The coverage is shown in the table below.

**Table 13: FP7 audits: quantity**

FP7	Planned cumulative period	Achieved cumulative period	Planned in 2010	Achieved in 2010
Number of closed audits	274	6	5	6
Total amount audited (EC share in €)	n.a.	1.948.764,70	n.a.	1.948.764,70

The six contracts had an error rate of 2.96% and the one representative contract 13.86%. Given the low number of contracts audited, and that only one was randomly sampled, it would be premature to draw any conclusions or have a reservation.

The error rates are shown in the following tables.

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<sup>38</sup> assuming full recovery (via offsetting against next payments or via issuing recovery orders), resulting from the implementation of audit results, the extrapolation of audit results and/or the application of penalties

**Table 14: FP7 audits: results**

Year	Number of audits closed	Number of participations audited	EC share of the costs accepted by the FO (€)	EC share of the accumulated adjustments in favour of the EC		
				Amount (€)	Annual error rate %	Cumulative error rate %
2010	6	6	1.948.764,70	-57.726,37	-2,96%	-2,96%

***EPR***

No financial audits were carried out in 2010. The Financial Audit unit accompanied the Court of Auditors to one contractor that was sampled in the context of the 2010 Declaration of Assurance work. This did not result in any errors being identified by the Court. The lack of audits reflects the lack of cost statements to audit, which reflects the early stage of the projects. This situation will change in 2011, when more cost statements are expected but for 2010 reasonable assurance can be given.

***Nuclear Decommissioning***

In 2010 DG ENER finalised a follow-up financial audit of the CPMA at the Ignalina nuclear power plant. This confirmed the institutional assessment conducted in November and December 2008, which found that the following key pillars are well established and operational to a satisfactory degree: procurement; internal control system; accounting, external audit, public access to information; and publication of beneficiaries. This provides reasonable assurance that the CPMA meets the requirements of the Financial Regulation.

In addition, the EBRD, which manages most of the funds for the decommissioning programme, also conducted an internal audit of the funds' management.

Following on from observations made by the Court of Auditors during the preparation of their 2008 Declaration of Assurance, the Assembly of Contributors for the Bohunice Nuclear Decommissioning Fund decided in late 2009 to launch a financial audit. This was carried out by external auditors under the supervision of the Financial Audit unit in 2010 and a draft report was presented to the Assembly of Contributors in December 2010. The conclusions are still under discussion but it is clear that the financial errors found represent around 0.25% of the total budget of the fund. Assuming that there is a similar level of error in the other two decommissioning funds, reasonable assurance can be given.

***Other programmes***

No other audits on grants and other budget lines were finalised in 2010. 5 were ongoing on TEN-E.

**3.1.1.6 Assessment made by the Directors of the Executive Agencies in their AAR**

The Director of EACI gave his reasonable assurance that the resources assigned to the activities described in his 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 (see annex 7).

### 3.1.2 Building block 2: Results from audits during the reporting year (2010)

#### *Internal Audit Service (IAS)*

The Internal Audit Service issued its audit on "*Compliance with payment deadlines*" for selected DGs at the end of 2010, including for DG ENER. The DG has drawn up an action plan to address the audit's findings it accepted. This will be implemented in 2011. It has also sent a management letter (which is advisory) on "Governance and internal control" in the Commission's shared resources directorates, including DG ENER's SRD.

#### *Shared Internal Audit Capability (SIAC)*

In 2010 the Shared Internal Audit Capability (SIAC), which is shared between DG ENER and DG MOVE, did not issue any critical recommendations, nor were there any critical recommendations open from previous years. At the end of the year only one very important recommendation had still to be implemented but its deadline is only the end of 2011.

During 2010 eight very important recommendations stemming from the following audits conducted in previous years were implemented:

- nuclear inspections
- accounting processes and accounting closure 2008
- compliance and performance of the recovery procedures
- implementation of the security and hygiene rules defined for the sites in Luxembourg

The SIAC finalised five audits and three limited reviews in 2010 thereby implementing its 2010 work programme and those actions carried over from 2009. These resulted in four "very important" (VI) recommendations in the following two audits:

- "implementation of the management centre and supply store in Luxembourg" resulted in a satisfactory opinion with respect to the systems put in place, with one exception. This led to a VI recommendation, the implementation target date for which is the end of 2011; and
- "compliance of the financial transactions in the research area" resulted in a satisfactory opinion with respect to the systems put in place, with three exceptions. These led to three VI recommendations, which were implemented by the auditee.<sup>39</sup>

In its annual audit opinion for 2010, the SIAC concluded that, based on the audit work carried out and on other elements available, the internal control systems in place in DG for Energy provide a **reasonable assurance**<sup>40</sup> regarding the achievement of business objectives set up for the processes audited with the exception of the qualifications resulting from the very important recommendations mentioned above.

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<sup>39</sup> Their implementation was confirmed by a SIAC follow-up audit in October 2010.

<sup>40</sup> Even an effective internal control system, no matter how well designed and operated, has inherent limitations – including the possibility of circumvention or overriding of controls – and therefore can only provide reasonable assurance to Management and not absolute assurance.

*European Court of Auditors (ECA)*

*Statement of assurance (DAS) 2009*

The Court assessed the payments made in 2009 for the policy group Research, Energy and Transport as being affected by a material level of error in terms of the legality and regularity of transactions and that the supervisory and control systems are partially effective (meaning "yellow" in the Court's colour coding). The Court notes that the measures the Commission has taken in recent years continue to contribute to a reduction in the level of error. However, there is a risk that the positive effect of the changes may not continue under FP7, particularly due to difficulties in implementing the ex-ante certification of beneficiaries' costing methodologies.

The Court recommended that the Commission should<sup>41</sup>:

- ensure that the independent auditors who have incorrectly certified cost statements are made aware of the eligibility criteria for declared costs;
- review the operation of the system for the certification of beneficiaries' costing methodologies;
- reduce the backlog in recovering undue amounts paid, imposing sanctions where necessary.

The Commission's response in the Court's report is:

"The Commission pursues a policy of actively feeding back findings of ex-post audits to the beneficiaries in order to ensure - where necessary - improvements in the work of the auditors delivering audit certificates. To this effect every beneficiary is requested in the course of the audit procedure to inform the certifying auditor on material audit findings. The Commission observes, however, that the main cause of the Court's observations is not so much the design or concept of the audit certificate but rather the relative complexity of the rules, duly referred to by the Court under paragraph 5.16. This inherent complexity impacts the work performed by the external auditors mandated by beneficiaries to deliver audit certificates. For FP7 it is expected that with the reliance on agreed upon procedures, the degree of errors due to such misinterpretation will significantly decrease.

The certification on the methodology (CoM) is intended only for beneficiaries of multiple grants. The eligibility criteria for the CoM were reviewed in November 2008 and published in the FP7 Guide to Financial Issues. The Commission recently took action in order to reinforce the attractiveness of the ex-ante certification of beneficiaries costing methodologies. The Commission expressed its views in this respect in its Communication on simplification of 24 April 2010 as well as in its proposal for triennial revision of the Financial Regulation and its implementing rules adopted on 28 May 2010. Genuine simplification could be yielded by allowing methodologies applied as usual accounting practice as long as they are based on actual personnel costs registered in the accounts.

The Commission will further pursue its efforts to improve the timely implementation of audit results and continue to apply its guidelines on the application of liquidated damages. Furthermore the communication on the simplification of the recovery process adopted on 15 December 2009 provides measures to improve the performance of the recovery process."

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<sup>41</sup> OJ C 303, vol. 53, 09.11.2010, paragraph 5.49.

The Court identified one error, which the Commission did not accept.

### *Special Reports*

In 2010, the Court did not publish any special reports for which DG ENER was chef de file.

The Court sent the Commission one Statement of Preliminary Findings on the nuclear decommissioning funds. This audit is expected to be completed in 2011.

## **3.1.3 Building block 3: Follow-up of previous years' reservations and action plans for audits from previous years**

### **3.1.3.1 Follow-up of 2009 reservation**

In the AAR 2009 DG TREN made a reservation on the "rate of residual errors with regard to the accuracy of cost claims in Sixth Framework Programme (FP6) contracts". The corrective actions, which were designed to go beyond those recommended by the Court of Auditors in their annual reports and address the reservation were directed towards the:

- Implementation of the agreed common control strategy. The implementation of the above strategy is effective. The carrying out of financial audits is in line with the objectives for the period covered by the strategy (2007-2010).
- Implementation of the desk control strategy. The number of files completed is significantly higher compared to 2009<sup>42</sup>, albeit less than initially targeted. This is partly because the effect of two controllers new in 2009 becoming fully operational in 2010, and hence having significantly increased their output, was offset by the effects of unoccupied posts and a controller being on extended sick leave. Measures have been put in place to reduce the time needed to complete a desk control and to strengthen its preventive nature. These concentrate on the most recent transactions and reduce the scope of the controls. The impact of these changes will be known once controls launched in 2010 have been completed. Delays have also been experienced in the follow-up of desk control recommendations.
- Reinforcement of training and information activities for beneficiaries and certifying bodies. Two training sessions/seminars on FP6 and FP7 financial and contractual procedures were conducted as planned in 2010.
- Extrapolation of audit results in line with the overall strategy designed for the research programme. The implementation of the mechanism is effective. Of the 433 cases identified (for both ENER and MOVE) as potentially requiring extrapolation, errors have been corrected in 43, 157 cases have been found not to contain errors, 180 cases are still to be examined and 53 will be dealt with by other DGs.

After decreasing from 6.94% in 2008 to 4.04% in 2009 the rate increased slightly to 4.42% in 2010. This figure is for DG ENER and for DG MOVE, as the audit strategy for FP6 is common to both DGs.

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<sup>42</sup> In 2009, a total of 17 controls were completed for ENER and MOVE projects. In 2010, 27 controls were completed for ENER and MOVE projects (10 for ENER, 17 for MOVE).

### 3.1.3.2 Internal Audit Service

No critical or very important audit recommendations from audits conducted before 2010 were open at the beginning of the year.

### 3.1.3.3 Shared Internal Audit Capability (SIAC)

Follow-up activities covered eight IAC reports and 37 recommendations, of which 12 were rated very important. The overall indicator for the follow-up in 2010 shows an 86.5% level of implementation for recommendations. The very important recommendation that is due for implementation by the end of 2011 was taken into account for the qualification of the annual opinion.

**Table 15: internal audit indicators**

Indicator	Latest known result	Target
% of "critical", "very important" and "important" accepted audit recommendations implemented within deadlines / number of accepted recommendations	31/12/2010: 86.5% 31/12/2009: 91% 31/12/2008: 87.8 % 31/12/2007: 92.5%	>70 %
% of recommendations accepted by auditees / number of recommendations issued	31/12/2010: 100% 31/12/2009: 100% 31/12/2008: 100% 31/12/2007: 100%	>80 %
Work programme implemented as percentage of annual planned Work Programme (SIAC)	31/12/2010: 100 % 31/12/2009: 95% 31/12/2008: 95 % 31/12/2007: 100 %	>90 %

### 3.1.3.4 DG BUDG

All recommendations open at the beginning of 2010 on the DG's accounting and financial local systems were implemented by the auditees and closed by the auditor during the year.

### 3.1.3.5 Follow-up of Action plans in reply to the audit work of Court of Auditors

DG ENER continues to address the recommendations made by the Court of Auditors in its Annual Reports concerning the Research Framework Programmes. This is done through the audit strategy common to the research DGs and the actions taken to address the reservation. The implementation of the ex-post control strategy continues as set out section 3.1.3.1.

## 3.1.4 Building block 4: Assurance received from other Authorising Officers in cases of crossed sub-delegation

Assurance has been received from all the DGs and services mentioned in section 2.1.1.

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

The information in sections 3.1.1 to 3.1.4 comes from monitoring by management and auditors. It results from a systematic analysis of the available evidence. This approach results in an adequate coverage of the budget delegated to the Director General of DG ENER and provides sufficient guarantees of the completeness and reliability of the information reported.

The following table summarises the information given in section 3.1 for the main spending programmes managed by the DG. It can be seen that reasonable assurance can be given for all of them. A reservation is required for overpayments in grants under the FP6 programme.

**Table 16: Summary of assurance for main spending areas**

Programme	Reasonable assurance?	Reservation?	Reason
FP5	Yes	No	Despite high error rate found in the two audited projects, amount at risk is low and there are no more ongoing projects
FP6	Yes	Yes	See below
FP7	Yes	No	Low number of contracts audited, only one randomly sampled, premature to draw any conclusions
EEPR	Yes	No	Comprehensive technical and financial monitoring. No evidence of significant problems.
Intelligent Energy Europe	Yes	No	Adequate monitoring in place. Assurance received from the EACI and DG ECFIN.
Nuclear Decommissioning	Yes	No	Adequate monitoring in place. Financial errors below materiality threshold

### 3.2 Reservation

On the basis of the information and the materiality criteria provided above, a reservation is needed concerning the accuracy of the cost claims submitted in the framework of the FP6 (6<sup>th</sup> Framework Programme-Research).

More information on the reservation is given below.

**Table 17: reservation on FP6 overpayments**

DG	ENER
<b>Title of the reservation, including its scope</b>	Reservation concerning the rate of residual errors with regard to the accuracy of cost claims in Sixth Framework Programme (FP6) contracts.
<b>Domain</b>	Internal policy / Direct centralised management of grants under FP6
<b>ABB activity and amount</b>	RTD activities related to energy
<b>Reason for the reservation</b>	The residual error rate observed by ex-post controls is higher than the control objective (2%).
<b>Materiality criterion/criteria</b>	The materiality criterion is the cumulative residual error rate found by audits and the correction of errors in the population covered following the audit results. The materiality thresholds are set at 2% and 5% in line with the approach used by the European Court of Auditors.
<b>Quantification of the impact</b>	Residual error rate is of 4.42% for audits regarding FP6 projects. This rate does not take into account corrections in favour of beneficiaries.
<b>Impact on the assurance</b>	Potential impact on the legality and regularity of the FP6 payments concerned. Total FP6 payments in 2010 were €40.95 million, which represents 3.6% of the payments made by DG ENER. The residual error rate of 4.42% corresponds to an amount of €1.7 million potentially at risk, representing 1.12% <sup>43</sup> of the payments made on the ABB line and 0.15% <sup>44</sup> of the payments made by DG ENER in 2010. Consequently for the whole budget managed by DG ENER, relative assurance can be provided.
<b>Responsibility for the weakness and its correction</b>	The legislative authorities are responsible for the overly complex funding rules in the basic acts; the beneficiaries and the certifying auditors, for the correctness of cost claims and audit certificates; and the Commission services, for the management and control systems in place.
<b>Corrective action</b>	<ul style="list-style-type: none"> <li>• Audits of additional beneficiaries where it is cost-effective to do so;</li> <li>• Risk-based audits where necessary</li> <li>• Carrying out of follow-up audits to check implementation of audit recommendations.</li> <li>• Completion of ongoing desk controls;</li> <li>• Extrapolation of audit results in line with the overall strategy designed for the research programmes.</li> </ul>

<sup>43</sup> 1.7 million of 147.7 million

<sup>44</sup> 1.7 million of 1136.71 million

### **3.3 Overall conclusion on the impact of the reservation on the declaration**

The potential amount at risk deriving from the residual error rate detected in the FP6, represents only 0.15% of the total amount paid by DG ENER in 2010. Consequently, assurance can be provided for the whole of the budget managed by DG ENER.

In 2011, for the research programmes, control efforts will continue on FP6 and intensify on FP7.

#### **4. Declaration of assurance**

*I, the undersigned, Philip LOWE*

*Director-General of DG ENER in 2010*

*In my capacity as authorising officer by delegation*

*Declare that the information contained in this report gives a true and fair view<sup>45</sup>.*

*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 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.*

*However the following reservation should be noted: The residual error rate observed by ex-post controls on grants given under the Sixth Research Framework Programme is higher than the control objective (2%).*

*Done in Brussels, 31 March 2011*

(signed)

Philip LOWE

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<sup>45</sup> True and fair in this context means a reliable, complete and correct view on the state of affairs in the service.

## Annex to Chapter 1: Information on General Objectives in the 2010 Management Plan

<b>General objective</b>	<b><i>Impact indicators</i></b>			
	<i>Indicator</i>	<i>Target (long-term)</i>	<i>Milestones (if any)</i>	<i>Current situation</i>
<p><b>Competitive energy</b></p> <p><i>To provide European citizens and businesses with competitive energy services</i></p>	<p>Degree of energy price convergence in the EU (Measurement unit: price variation ratio between cheapest and most expensive Member State for both household and non-household consumers source: Eurostat and Energy Regulators)</p>	1:2		<p>30/06/2010 (Prices for the first half of 2010 without taxes)</p> <ul style="list-style-type: none"> <li>– Electricity: Household: 1:2.9; Industry 1:2.7</li> <li>– Gas: Household: 1:4.9; Industry: 1: 2.9</li> </ul> <p>31/12/2009 (Prices for the second half of 2009 without taxes)</p> <ul style="list-style-type: none"> <li>– Electricity: Household 1:2.9; Industry: 1:2.6</li> <li>– Gas Household 1:4.6; Industry 1:3.1</li> </ul> <p>31/12/2008</p> <ul style="list-style-type: none"> <li>– Electricity – both categories: 1:3.4</li> <li>– Gas-household 1:3 industry 1:2.3</li> </ul> <p>31/12/2007: 1:3 for households; 1:2.5 for non-households</p>
<p><b>Sustainable energy</b></p> <p><i>To make energy production and consumption more sustainable</i></p>	<p>Energy efficiency and savings. Primary energy savings achieved in 2020 measured against the baseline (%) (Baseline is PRIMES 2007 in 2020, which includes policies to be implemented up to 2006 with an oil price of \$61 per barrel and reference year 2005. Calculated as Gross Inland Consumption minus Final Non-Energy Use Consumption. Source: Eurostat, Commission studies)</p>	20% by 2020		<p>8.5% (2008)</p> <p>8.1% (2007)</p> <p>6.9% (2006)</p> <p>7.1% (2005)</p> <p>[Explanation: When e.g. looking at EU-27 primary energy consumption in 2006, we would save 7% of the projected primary energy consumption for 2020, assuming constant consumption until 2020]</p>

<b>General objective</b>	<b><i>Impact indicators</i></b>			
	<i>Indicator</i>	<i>Target (long-term)</i>	<i>Milestones (if any)</i>	<i>Current situation</i>
	Renewable energy share in final EU energy consumption (%)	20% by 2020	Submission of Member States' national action plans, June 2010  Trajectory contained in Annex 1b of Dir. 2009/28/EC (inc. targets for 2011/2012).	23/27 plans received as at 1/12/2010  31/12/2008: 10.3%  31/12/2007: 9.2%  31/12/2006: 8.74%  31/12/2005: 8.5%
	Share of renewable energy in EU energy consumption for transport (Measurement unit: %; Source: national reports under the renewable energy directive and 2003/30)	10% by 2020	5.75% by 2010	31/12/2008: 3.5%  31/12/2007: 2.6%  31/12/2005: 1%
<b>Secure energy</b>  <i>To create conditions allowing for continuous and secure energy supply for the EU</i>	Number of major energy supply disruptions	0		2010: 1 (Gas disruption originating in Belarus and affecting 2 Member States)  2009: 1 (Gas disruption originating in Russia and affecting 12 Member States)  2008: 0  2007: 0  2006: 1 (Electricity originating in Germany and affecting 7 Member States)
	Number of extra-EU countries supplying at least 3% of the EU market for coal	Increase		31/12/2009: 6  31/12/2008: 6  31/12/2007: 7  31/12/2006: 6

<u>General objective</u>	<u>Impact indicators</u>			
	<u>Indicator</u>	<u>Target (long-term)</u>	<u>Milestones (if any)</u>	<u>Current situation</u>
	Number of extra-EU countries supplying at least 3% of the EU market for gas	Increase		31/12/2009: 5 31/12/2008: 5 31/12/2007: 5 31/12/2006: 4
	Number of extra-EU countries supplying at least 3% of the EU market for oil	Increase		31/12/2009: 9 31/12/2008: 9 31/12/2007: 7 31/12/2006: 7
	Number of extra-EU countries supplying at least 3% of the EU market for uranium. (Source Euratom Supply Agency Annual Report)	Increase		31/12/2009 : 7 (EU27) 31/12/2008: 7 31/12/2007: 6 (EU27) 31/12/2006: 5 (EU25) 31/12/2005: 8 (EU15)