The Agenda 2000 reforms did not only establish a clearer division of competences and tasks between the European level and the Member States it also inserted stricter provisions on financial management. New instruments such as the performance reserve or the n+2 rule increase the pressure for effective financial management even further.

In that light, the seminar objectives were twofold. Firstly, the new relevant provisions of Council regulation 1260/1999 and Commission regulation 438/2001 with view to e.g. the paying authority, revenue generating investment and combating fraud were presented and explained. Secondly practitioners presented examples of Member States applying the new rules covering e.g. financial management structures, 5% controls as well as new approaches to financial engineering. With around 70 participants coming from 11 Member States and 7 applicant countries, it became clear that the subject of financial management is of great interest and practitioners experience a considerable need for training.

The seminar was opened by a panel discussion on the division of responsibilities for the financial management of Structural funds after enlargement. The panelists, Dr. Heinz Schrumpf from the Rheinisch-Westfälisches Institut für Wirtschaftsforschung, Essen (D), and Mr Jan Maarten de Vet, Netherlands Economic Institute, Rotterdam (NL), reviewed the relationship between European, national and subnational level as well as the actual financial management system.

Unlike common belief, the most urgent problem cohesion policy will be facing after enlargement will not be the funding available for the new Member States, but according to Mr. Schrumpf: (1) the regional concept of Structural Funds, (2) the redistribution of funds between the eligible areas.

As regards the first challenge, Mr. Schrumpf pointed out that, if the present concept of Structural Funds will be applied to the applicant countries, all regions within the new accession countries would be eligible for Objective 1 support. Thus, practically one coherent territory of Objective 1 regions would exist. This not only leads the regional eligibility concept ad absurdum. But it also does not meet the needs of the applicant countries. A regionalised concept of cohesion policy does not respond adequately to the problems of the new Member States. Whereas this challenge is more based on economic rationale, the second challenge identified by Mr Schrumpf is of a more political nature. The distribution of funds would be considerably altered if the current system is extended without adaptation. Due to a simple statistical change and not the fact that the regions in reality are
better off, a number of regions currently benefiting from Structural Funds support would not be eligible for the next programming period anymore.

The solution to both challenges is to be found in changing the very concept of Structural Funds. Instead of following a regional policy approach, the Cohesion Fund approach is more favourable for both new and old Member States. Not only are the management requirements for the Cohesion Fund less demanding it also solves the re-distribution problem because eligibility is determined at central level. Although funds would still be re-distributed, it would be less severe for the present beneficiaries. Moreover, funds are not distributed following the rigid regional division (NUTS)

The second panellist, Mr. De Vet, focused on the question how to achieve effective financial management of Structural Funds after enlargement. Responsibility for financial management rests with the Member States. Consequently, they are responsible for creating a structure in line with the legal requirements laid down in the various Council and Commission regulations. The three pillars of every financial management structure are: the management authority, the paying authority, and implementing bodies. Further to Article 32.2 and 34 of Council regulation 1260/1999 the tasks of the management authority include: responsibility for managing assistance under Structural Funds, insuring proper financial management and accounting systems in place, implementing internal controls, assembly of data and progress reports for monitoring and evaluation purposes, providing information on expenditure using financial tables, submission of proposals for reallocation of funds and adjustments to programme complements. The paying authority forms a counter part to the management authority. Its main responsibilities include: submit certified payment requests to the Commission, channel payment to the final beneficiaries, recover sums paid undue, and ensure that adequate checks are taken at the management authority level. The role of implementing bodies include: monitor financial progress, verify the eligibility of expenditure, submit payment requests, and submit reports to the management authority. The tasks of the implementing bodies are somewhat less specified because they depend very much on the management authority delegating tasks to them.

According to Mr. De Vet there are three main indicators for efficient management, namely structures, human resources and system & tools. Structures relate to the clear allocation of responsibilities, competences and tasks to institutions, including coordination arrangements between, as well as within, institutions. Human resources refer to the ability to detail responsibilities, competences, and tasks not only at institutional level but also at the level of individual employees. And finally, tools relate to the availability of procedures, forms, guidance, manuals. etc.

Further to Mr De Vet, the most important aspect for an efficient management is the clear division of responsibilities and tasks. This should be done by using existing experience both at the level of an institution as well as at the level of individual staff members.

Mr. Nicholas Martyn, head of unit, DG Regional Policy, European Commission focused his presentation on the paying authorities and their role in financial control of the Structural Funds.
As laid down in Council regulation 1260/1999 and Commission regulation 438/2001, the paying authority is responsible for ensuring the correctness of the money flow. Its tasks include: Compilation of expenditure declarations, applications for interim and final payments to the Commission, certification of expenditure declarations, ensuring that the final beneficiary is paid as soon as possible, reporting on recoveries, and supply of expenditure forecasts. Certification has to be performed by a person or department independent from those departments and persons involved in management tasks. But not only have the Paying and the Management Authority to be separated, also the tasks of compiling expenditure and certifying them have to be separated.

How can the paying authority obtain assurance about the correctness of payments made. Mr Martyn presented several ways, including: checks of expenditure declarations, selective in depth checks, double keying, validation and reasonableness check (by system), additional information (incl. Audit reports). Furthermore the paying authority has the right to conduct audit itself. The information which has to be submitted to the European Commission by the management authority should cover the following aspects: breakdown of expenditure, details of supporting documents, who checked / authorised the declaration, evidence of management checks, evidence of physical monitoring, existence of audit trail, and audit reports.

In implementing the above system, the European Commission has observed the following problems: Inadequate separation of functions, insufficient staff both in terms of quality and in terms of quantity, as well as lack of powers transferred to the institutions concerned.

Representing the Regional Policy DG of the European Commission, Mr Johannes Wachter elaborated on a special case in the co-financing rules namely, the reduction of the Rate of Assistance for revenue-generating Investments as laid down in Article 29.4 of Regulation 1260/1999. Outlining the fundamental goals put down in Regulation 1260/1999 he especially stressed the aim to strengthen the leverage effect of Community resources while reducing the amount of Structural Funds support to a minimum. To this end, projects generating net revenue are not eligible for the full maximum amount of EC assistance (i.e. 75% Structural Funds share for Objective 1 areas, 50% for Objective 2).

The speaker concluded the presentation by offering simplified guidelines of how to apply article 29.4. He suggested a method of how to calculate the rate of assistance without conflicting the Regulation and specified this method for the special case of investments in infrastructure project that generate substantial net revenue (i.e. over of total initial investment).

The proposed calculation method works as follows: In order to calculate which amount of Structural Funds support a particular measure is eligible for, it must be determined if the infrastructure investment concerned creates net revenue over its calculation reference period by applying a discounted cash flow analysis. If the investment is revenue-generating, the rate of assistance is determined according to the first subparagraph of Article 29.4. The subparagraph, Mr Wachter pointed out, is correctly interpreted by first deducting the
expected net revenue from the total initial investment cost and then apply the normal rate of assistance of the measure concerned (the 75% respectively 50% margin) to the difference deducted in the preceding step. As an additional condition, the final result must not create an undue advantage for the recipient of aid, i.e. the project shall not be over-financed. This is secured by a ceiling set out in Article 29(3).

To calculate the rate of assistance for projects with a substantial net revenue the same calculation method should be applied. One must, however, respect different ceilings, namely those laid down in Article 29.4 (a). This means the contribution may not exceed 40% of the total eligible costs for Objective 1 areas (plus 10% in Member States covered by the cohesion fund), respectively 25% in areas covered by Objective 2. Again different ceilings apply for investments into firms (Article 29.4 (b)) for which the special maximum rates account to 35% (Objective 1) respectively 15% (Objective 2) (plus 10% for non-direct aid only for productive investments. Further, maximum aid rates determined by State Aid rules must be respected.

Apart from these very specific comments of how to apply Article 29.4 of the Regulation, Mr Wachter made some general statements on when to apply it. The Regulations aims at investment projects only (while for cases or receipts from projects that are no investments the eligibility rule No 2, Regulation 1685/2000 applies). The expected net revenue is calculated ex ante for the economic lifetime of the project, respectively a calculation reference period. The calculations are generally carried out by national authorities, only for large-scale projects the Commission itself is involved. The Commission representative pointed out that once this expected revenue has been determined, no later modifications are possible in the light of real developments. Answering a question from the floor, Mr WACHTER explained that net revenue cannot be calculated as national co-financing of a particular project since this would run counter to the central objective of Regulation 1260/1999 to increase the leverage of Structural Funds resources.

Combating Fraud in EU Cohesion Policy: Instruments and Achievements Structures, tasks, achievements of the were presented by Mr Oliver Baum, European Anti-Fraud Office (OLAF) The office was established in 1999 as successor to the 'Co-ordination of fraud prevention' task force (UCLAF) of the Secretariat-General of the Commission. Despite being part of the European Commission under the responsibility of the Commissioner in charge of the budget, the office has an individual independent status to pursue its investigative functions. OLAF thus enjoys investigative independence to detect and monitor fraud in e.g. the customs field, misappropriations of subsidies and tax evasion concerning the Community, and to fight corruption or any other illegal activity related to the finances of the Community. On behalf of the Commission OLAF carries out all powers of investigation that derive from Community legislation and agreements with third countries. The office can “conduct internal investigations in all the institutions, bodies, offices and agencies established by or on the basis of the EC and Euratom Treaties” (Regulation No 1073/99, paragraph 7) and is entrusted “to conduct on-the-spot checks and inspections in the Member States” (ibid., paragraph 9). Essential for the effective execution of the office's investigative responsibilities is the close co-operation with national partners (investigation services, police, legal and administrative services, etc.) not only because the latter collect the
traditional own resources of the Community but also because they implement almost 80% of the Community budget.

OLAF, DG Audit and the operational DGs share responsibilities for monitoring the system and irregularity communications at the Community level while the Member States hold the primary responsibility for dealing with irregularities detected and for making financial corrections. In the framework for the communication and follow-up of detected irregularities concerning Structural Funds (Regulation (EC) 1681/94), OLAF is the lead authority. This means that the authorities dealing with Structural Funds in the Member States supply OLAF with communications referring to details of detected irregularities (with a financial impact exceeding EUR 4 000) and provide the office with updates on such cases. Mr BAUM commented that the ESF was relatively susceptible to irregularities. Moreover, he mentioned that an electronic communication registry (which exist for the Common Agricultural Policy) has not yet been set up for Structural Funds.

The Director General of OLAF conducts the implementation of the office's (internal and external) investigation functions and is designated by the Commission for a five-year period following a favourable opinion by the Supervisory Committee (consisting of five outside persons independent from the Community institutions) in co-operation with the European Parliament and Council. The Director General is legally obliged not to seek nor to take instructions from any government or other institution. To consolidate this independence, the Supervisory Committee undertakes regular controls of the investigative functions. Either on its own initiative or following a request by the Director General. The Committee delivers opinions to the Director, yet without interfering with the conduct of investigations in progress.

One of OLAF’s roles is to provide information and guidance on the implementing provisions of Regulation (EC) 1681/94, which deals with the communication of irregularities detected by the Member States to the Community level. A central aspect of its guidance for Member States is to define an irregularity. The office does this by referring to Article 1(2) of Council Regulation (EC, Euratom) No 2988/95 which defines an irregularity as “any infringement of a provision of Community law resulting from an act or by an economic operator, which has or would have, the effect of prejudicing the general budget ... by an unjustified item of expenditure”. Generally, the distinction between fraud and an irregularity is that the former is an intentional act and a criminal offence, while the latter is any infringement of Community law resulting from an act or omission.

Turning to case studies of how financial management of Structural Funds is handled in particular Member States, the Swedish Business Development Agency NUTEK was presented by Ms Barbro Nordgren and Ms Christina Johansson. NUTEK is the central co-ordinating body for all Structural Funds in Sweden. The agency holds responsibilities as paying authority (for one programme), as secretariat for monitoring committees, as evaluation body and for the preparation of reports and forecasts for the government. The speakers outlined the present functioning of Swedish Structural Funds financial management, they presented the experiences in setting up the relevant institutions during the first programming period (1995-99) after the Sweden’s accession to the EU, and they...
commented on the Commission's role in establishing a financial management system in Sweden.

Central to the Swedish approach is a strong decentralisation concerning regional decision-making and implementation, complemented by centralised payments which are delivered at the national level. Accordingly, for Objective 1 and 2 as well as for Interreg IIA and Urban projects the management authority is normally part of the county administrative board, which in a number of cases also functions as paying authority. The Swedish ESF Council functions as management authority for Objective 3 and Equal, the Swedish National Labour Market Board (AMS) as paying authority. Four further bodies function as managing or paying authorities. Altogether, two ministries (industry and agriculture, both without direct involvement into the implementation), six authorities (agencies and boards), and six County Administrative Boards (providing for eleven paying authorities) constitute Sweden's financial management system.

As the two speakers concluded, the strongly decentralised system offered great advantages although, at the same time, it demands a lot of co-ordination. NUTEK provides this co-ordination for both, the managing and paying authorities of the different Structural Funds programmes, and is also responsible for providing training and information. On the one hand, regular meetings with the Swedish authorities provide a platform for the exchange of experiences and a common interpretation of rules, on the other hand, NUTEK acts as the connecting link between the regional level, the Commission and OLAF.

Evaluating Sweden's performance in setting up a financial management system, the speakers pointed out that certain difficulties derived from insufficient preparations and policy differences between the Swedish and the EU system (i.e. differences in control and follow-up on programme and project level – especially insufficient expertise and staffing; differences in focus and programme length) – although creating new structures for the implementation of the Community Structural Funds had a certain impact on Swedish national regional policy. Further, drawing conclusions on the first programming period positive aspects that could be identified were: the regional commitment to decisions and implementation as well as the structures providing opportunities for good follow up and for the co-ordination for the co-financing of projects. Sweden faced in particular three problems during the 1995-99 programming period, namely: the extensive organisation, the different systems and routines, and the unclear division of responsibilities between the many different bodies involved. Providing an outlook on the important aspects for an effective implementation of the new Structural Funds regulations, Ms Nordgren and Ms Johansson mentioned the need for coherent interpretation of the regulations, effective co-ordination of the bodies involved, and adequate training of authorities. With view to the latter issue they stressed that experience has shown that especially the creation of human resources was a timely process and that most programmes were thus handled better at the end of a programming period than in the beginning.

Finally, commenting on the role the Commission played, Ms Nordgren and Ms Johansson emphasised that the institution's critique and support were helpful in increasing the efficiency of their country's financial management. However, co-operation with the
Commission could be more efficient if co-ordination between the Commission DG’s was improved. The Commission evaluated very positively that Sweden set up a manual for the handling of financial management in form of a handbook and a DATA base (compatible for the management the ERDF) which provides a generalised computer system accessible by all relevant bodies.

The head of the EDRF Financial Unit (Department of Finance), Mr Dermot Byrne, elaborated on the financial control system in Ireland. In contrast to the Swedish system, Ireland's financial control is operating in centralised structures which serves better the preconditions of the rather small state. Remarkable about the Irish approach is that the national regional policy share in the National Development Plan (NDP) and the Community Support Framework (CSF) is much higher than required by the Regulation. Mr BRYNE explained that it is broader in scope than the previous NDPs meaning that the programme severs not only to draw down EU aid (as previously) but it is designed to address the state's total development needs.

The speaker illustrated the structure of the actual control and auditing system. While the internal control is a system of ex-ante controls established by the management, the audit function means an ex-post independent examination of both, financial records and of the correct functioning of the internal control system. Thus, the internal control is concerned with authorisation, segregation of duties, accounting, and written procedures, whereas the audit function covers a system-based audit and the 5% verification. The Irish control system builds on a cascade of system-based audit performed by internal audit units or contracted internal audit functions; on each level (from the management and paying authority, the implementing body down to the final beneficiary) these internal audits take place. For the 2000-2006 period the 5% verification of transactions is carried out by the functionally independent Financial Control Unit (FCU) (mainly at the final beneficiary/recipient level). The FCU also examines the audit trail, respectively the transactions and systems at all levels in the cascade and monitor progress on systems audits by internal audit units.

The speaker presented the Irish approach to risk assessment required for the 5% controls. Further to the Commission audit manual, he first distinguished between inherent risk, control risk, detection risk of a project or measure. The next step is to quantify potential risk by assessing a risk factor score to each element of funding (giving scores from 1 to 5 for high/medium/low risks). Scores are given for certain key risk factors (such as complexity of regulations, competence and experience of staff, etc.). On this basis a total risk score can be calculated which relates to a risk adjusted monetary value. Mr Byrne stressed that this system of risk assessment did not serve to determine the risk inherent in a particular project but achieve relative assessment to evaluate which projects are more risky than others. …

Problems Ireland faced in applying Regulation 438/2001, include adequate information and guidance for management and paying authorities as well as implementing bodies. Likewise, a clear definition, allocation and separation of functions was not easy to achieve. In contrast to the Swedish experience, IRL opted not to develop a comprehensive manual because the rules applying to the various bodies involved differed too much. Furthermore, Mr Byrne raised concerns that the implementation of the ‘n + 2’ rule could create problems since he
thought it likely that the time window for the implementation would not be met by many projects. The money withdrawn by the Commission in such cases would have to be covered for by the national budget.

On the basis of previous experience in managing the funds, the speaker drew the following conclusions: a Member State must ensure to prevent/detect irregularities itself since it then remains entitled to re-allocate funds; manuals are an important tool for passing on information to all authorities involved; responsibilities at all levels should be clearly allocated/segregated; a sound risk assessment should take place in audit planning and sampling; EU regulations/guidelines should be distributed to responsible at all levels; adequate monitoring/cost control should be ensured.

Ms. Sheila Maxwell from the Welsh European Funding Office, presented the Welsh approach to financial engineering. The speaker presented as the central element of financial engineering the concept of self-reliance through a system of financing.

Mrs. Maxwell identified several positive aspects of venture capital. The dearth of financing for many SMEs that want to start an own enterprise, invest in or expand its current business is a recurring problem in the EU. The problem becomes more acute when the financial risk involved is high. Lack of funding hinders development as positive net present value opportunities are foregone due to limited finance.

In Wales the regional government subsumes the role of the managing and paying authorities for the Structural Funds. Through a system of venture capital several aims are achieved. First, shifts financing from grants to loans. This ensures that the responsibility of the receiver of the loan is taken. Thus the financing is partly provided by a private body, which also allows some distribution of risk for the government. Secondly, through the private co-financing also the expertise of professional venture capitalists is provided. External experts evaluating the project application are recruited on a limited contract basis. Thirdly, through the loan structure the funding is not merely distributed but invested providing future possibilities of financing for similar projects after repayment. This leads to increased leverage effect of the Structural Funds support.

Financial support can take three forms. The funds can provide loans like a normal bank but due to the higher risk involved should charge higher interest rates. It is also possible to provide firms with equity varying with the growth stage of the business. The last method is a combination of the two previous methods and is called Mezzanine. It involves a mixture of debt and equity finance. Support can also take the form of management support. This can be done through various methods including executive monitoring, consultancy and turnaround of specialists.

Mrs. Maxwell summarised the experience of the Welsh office with this venture capital programme. The contribution of the private sector should be above 30%. Moreover, funds should be large and cover a wide target population so that economic viability is ensured. Also the focus should be on areas of market deficiency so that negative economic side effects produced by market failures can be dealt with.