Performance auditing in EU Cohesion Policy: what do we know and what should we know?

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Abstract
Recently, the European Commission has put forward proposals for the next program period of EU Cohesion Policy (EUCP). Part of these proposals is an increased emphasis on performance management. This paper analyses what we know so far on performance management of EU cohesion funds. It will be argued that, despite the frequent use of terms like “sound financial management” and “value-for-money”, which implies the availability of information on all so called three E’s (economy, efficiency and effectiveness), performance auditing so far is largely limited to issues of economy. This is due to the EU’s preoccupation -in budgetary control- with the issue of legality and with irregularities, which link easily to compliance auditing and the issue of economy, but hardly to efficiency and effectiveness (performance auditing). The empirical paragraph of this paper analyses the reports issued by actors on both the European and national (in casu Dutch) level in 2010 and shows that on average 68% of the content of the reports focuses on compliance auditing, instead of performance auditing (32%). Within the share of performance auditing, most attention is paid to output and outcome of the policy concerned (respectively with 12% and 17%); hardly any attention is given to input and costs (with respectively 2% and 1%). This shows that performance auditing still is not in the centre of attention in EUCP and a shift has to be made to really properly account for EUCP.

1. Introduction
For decades, the main aim of EU Cohesion Policy (EUCP) has been to contribute to the economic convergence of regions by reducing economic disparities. Following the introduction of the Lisbon Strategy in 2000 and the refocus of this strategy in 2005, EUCP has increasingly become imbedded into the general economic governance of the European Union (EU). The proposals1 the European Commission has put forward for the next multiannual financial and programming period (2014-2012) clearly show that EUCP is to concentrate on contributing to the objectives of Europe 2020 (the successor of the Lisbon Strategy) of smart, sustainable and inclusive growth. Apart from creating

1 COM(2011) 500 final.
more synergy between the various funds\(^2\) by creating a common strategic and regulatory framework for these funds\(^3\), the main changes to the way EUCP is designed and implemented refer to issues of “results”, “performance”, “conditionalities” and “delivery”.

In the run-up to the new programming period the EC (DG Regional Policy) has started to publish country fact-sheets outlining the progress of individual Member States in meeting their agreed targets under the Europe 2020 Strategy.\(^4\) The fact-sheets give the state of play in various themes under the three headline targets of smart, sustainable and inclusive growth. According to the EC the fact-sheets will be an invaluable support in the negotiations on the next period of EU cohesion funding (2014-2020), as they place each country in a European perspective by measuring performance and comparing to the EU average, as well as the best and the worst performers in the Union.

Following Furubo (2011: 35), in this paper we define performance auditing as an evaluative activity which produces assessments regarding performance or information about performance, of such a reliable degree and with such a freedom from investigatory and reporting constraints, that they can be used in the realm of accountability. Whereas profits (i.e. revenues minus costs) provide firms with a single yardstick to assess performance, performance assessment in the public sector is a far more complicated issue. What counts, eventually, is the extent to which public policies contribute to solving social problems. In the literature on public financial management\(^5\) this idea is often put into a policy-process-chain, which consists of four parts: COSTS (1) \(\rightarrow\) INPUT (2) \(\rightarrow\) OUTPUT (3) \(\rightarrow\) OUTCOMES (4).

In this chain-model “value for money” (hereafter: VFM) refers to the link between element 1 (“money”) and element 4 (“value” in terms of changes in desired outcomes). VFM comprises three different components within the chain:

1. Economy, which links input (2) and costs (1);
2. Efficiency\(^6\), which links output (3) and input (2);
3. Effectiveness, which links outcomes (4) and output (3).

For a number of reasons, this simple chain-model is more complex than it initially looks. First, outcomes are determined not only by (public) outputs, but by other factors (outside of the chain-model) as well. If we take one of the Europe 2020 objectives as an example: employment rates are not only influenced by public sector outputs (legislation regulating labour markets, education, tax rates) but by the actions/outputs of private actors as well. Within the EU context this multi-actor aspect is complemented by the multi-level dimension of EU governance, adding to the overall

\(^2\) European Regional Development Fund (ERDF), European Social Fund (ESF), Cohesion Fund (CF), European Agricultural Fund for Rural Development (EAFRD) and European Maritime and Fisheries Fund (EMFF).

\(^3\) SWD (2012) 61 final (EC staff working document).


\(^6\) There is a certain level of confusion as to how these terms relate to various efficiency concepts within (business) economics. Efficiency is sometimes also referred to as technical efficiency, whereas economy is sometimes referred to as price efficiency. Another concept is that of cost efficiency which links costs (1) and output (3). Yet another term is allocative efficiency which according to some is identical to effectiveness and according to others is identical to VFM. In this paper we will stick to the three Es: economy, efficiency and effectiveness, which together make up VFM.
complexity. Second, linking the elements presupposes that these elements are easily measurable, by one or two indicators. This may be true for the first element (costs), but all other elements have both quantitative and qualitative aspects.

These two problems generally create the risk of what can be labeled *performance audit prolapse*, which pushes performance audit back into the chain. If outcomes cannot be sufficiently linked to outputs, there is a tendency to focus on these outputs instead. If outputs cannot be properly measured because they are mainly qualitative, the tendency is to focus on (processes/throughput indicators and/or) inputs. If inputs cannot be properly measured, performance audits focus on costs. These impossibilities and constraints and the resulting process of degrading can render performance audits quite useless from the overall perspective of accountability that is essential to performance auditing.

In this paper we argue that as such the move away from compliance auditing in the EUCP (aimed at the detection of fraud and errors, i.e. at legal and administrative compliance) towards performance auditing (aimed at assessing the efficiency and/or effectiveness of policies) should be highly welcomed. Despite the frequent use of terms like “sound financial management” and “value-for-money”, up till now auditing in the EUCP has largely dealt with compliance issues and issues of economy, rather than efficiency and effectiveness. The EC itself also mentions in the Fifth Cohesion report: ‘Cohesion Policy needs to cultivate a focus on performance. This has to start from programmes identifying a limited number of policy priorities (concentration) with a clear view of how they will be achieved and how their achievement will contribute to the economic, social and territorial development of the regions, or Member States, concerned. Monitoring and evaluation systems need to be improved across the EU to track performance and to help redirect efforts as necessary to ensure that objectives are attained. This requires a clear strategic vision of what the programme aims to achieve and how success will be recognised and measured (proper target setting). It also requires a greater recourse to rigorous evaluation methods, including counterfactual impact evaluation, cost benefit analysis, beneficiary surveys, as well as a more rigorous use of qualitative methods such as case studies’.

This focus on the issue of economy is due to the EU’s preoccupation - in budgetary control - with the issue of legality and with so-called irregularities, which link easily to the issues of compliance and economy, but hardly to efficiency and effectiveness. As Mendez and Bachtler (2011) argue, the compliance model of audit clearly had the upper hand in the ‘audit explosion’ within the EUCP in the mid-2000s.

The first aim of this paper is to establish empirically whether auditing in the EUCP is indeed still mainly about compliance auditing or not. In addition, in our view it is highly questionable whether the approach to performance auditing and management within the EUCP that has been chosen by the EC, has much value in terms of accountability, as it concentrates on monitoring overall outcomes, without linking these outcomes to outputs, inputs and costs. Where current practice focuses too much on the “correctness” of costs and inputs, the new EC performance auditing paradigm faces a similar risk by focusing solely on overall targets/outcomes. The second aim of the paper is to see

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what kind of information is available in terms of performance and whether this information allows for making valid inferences on the contribution the EUCP makes to Europe 2020 objectives.

This paper is structured as follows. First (section 2), an overview is given of the relatively complicated multi-level governance structure of budgetary control, financial management and compliance and performance auditing in the EUCP. Subsequently (section 3), available data on auditing (both at the EU level and at the Member States’ level) in the field of the EUCP are analyzed (using documents of the EC, the European Court of Auditors (ECA) and of an individual Member State), to see what is currently available in terms of (compliance and performance) auditing. Form this overview it will become clear that much what is done now, is about compliance rather than performance. Finally (section 4), it will be assessed what is needed, in terms of both governance structure and available data, to adequately audit performance in the EUCP.

2. Multi-level governance in EUCP
The budget of the EUCP is substantial, with a growth from €65 billion euro’s in the period ‘88 – ‘93 to approximately €308 billion in the period ’07 –’13. This is the equivalent of the GDP of Belgium and is about the same as France’s expenditure on national education over a five-year period. The EUCP is one of two policy area’s which is characterised by ‘shared management,’ next to Agriculture. Shared management points at the way the management of the policy area is organised; both the EC as the Member States share the obligations for the management of the specific policy area. Regarding the Structural Funds, in the regulation it is explicitly laid down that both the Member States and the EC have specific obligations in the implementation of the Structural Funds. Consequently, budgetary control and audit measures on both the European and national level are involved. This gives the Member States of the European Union, next to the EC, also an enormous responsibility in the management of the EUCP.

When looking at the management of the EUCP, one will find three main levels in which various actors are involved, the supranational level (European level), national level and local or regional level. Various actors have a role on these different levels.

Starting at the supranational level, the EC is the main actor on the European level. The EC as a whole has responsibilities as set out in the Treaty, and these are carried out by the Directorates General (DsG) that are involved in the specific policy field. Regarding the EUCP, these are DG Regional Policy (DG REGIO) and Employment, Social Affairs and Opportunities (DG EMPL). Next to the DsG, a role is set for OLAF, the European Anti-Fraud Office of the European Commission. OLAF has a specific role in the protecting of the financial interests of the European Union, which also applies to the EUCP.

Then on the national level, the management of the EUCP is laid down at a specific ministry or agency (or at more than one within a Member State). This government institution(s) is the primary contact point for the EC concerning the EUCP in the Member State and also for the local authorities within the Member State.

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8 See Council Regulation (EC) 1083/2006 art. 18
11 Art. 274 of the Treaty on European Union and of the Treaty establishing the European Community
Finally, the regional level is the third level in the management of the EUCP. Important to mention is that the starting point of the management within a Member State will always be the national government or agency, which means that the local government or field agency in fact resides under the ministry or national agency.

When looking at the bodies that are responsible for the budgetary control and auditing of the EUCP, one will also find actors on all three levels. On the European level, the ECA ‘checks that EU funds are correctly accounted for and spent in compliance with the rules and legislation, with due consideration for achieving best value for money, irrespective of where the funds are spent.’\(^\text{12}\) To be able to do this, the ECA performs audits on all chapters of the EU budget, which includes the EUCP. For a lot of years, the opinion of the ECA on the EUCP has been that these are affected by material error.\(^\text{13}\) Then on the national level, in some Member States a role is set for the national Supreme Audit Institution (SAI). Finally, on the local or regional level for all operational programmes (OP) a specific audit authority is appointed. This authority, often a national governmental body, is assigned with the auditing of specific projects. In practice, this means that a beneficiary in exceptional instances can be checked or audited by six organisations (ECA, EC, coordinating ministry, national SAI, Management Authority and Audit Authority).

If we take the Netherlands as an example, one can see how complex the system is. The Netherlands is receiving money from the Structural Funds from both the ERDF and ESF, not from the Cohesion Fund. For each fund, one or more Operational Programs are drafted, which gives a specific outline of the goals and actions that are pursued. For ERDF, the country is separated in four (geographical) parts, which all have their own Management Authority (MA). ESF is organised in one OP on a national level with one MA. Next to the five MA’s one Audit Authority (Rijksauditdienst) and one Certifying Authority (Dienst Regelingen EL&I) are appointed for all OP’s, responsible for respectively auditing the programmes and projects, and drawing up, certifying and submitting payment requests. The responsible ministries for all these programmes are the Ministry of Economic Affairs, Agriculture and Innovation (EL&I, for ERDF) and Social Affairs (ESF). In total, for a small country as the Netherlands, this makes a total of nine public authorities. Considering the Netherlands is a quite small unitary state as opposed to large federal states, one can see that the management of the Structural Funds in most Member States is often quite complex, with a lot of different authorities involved.

3. What is known? Data on compliance and performance auditing

Given the complexity of the EUCP management and auditing system, it is now time to look whether the auditing information that is available is focused on performance auditing information (VFM) or rather on compliance management information. The first kind of information consists of the items as mentioned in section two, namely costs, input, output and outcome. This information makes it possible to tell something about the economy, efficiency or effectiveness of the policy. The latter

\(^{12}\) http://eca.europa.eu/portal/page/portal/aboutus/TheCourtsroleandwork/Role

\(^{13}\) See for 2010: European Court of Auditors (2011). Annual report on the implementation of the budget concerning the financial year 2010. Luxembourg, European Court of Auditors.
kind consists of information regarding legality and regularity and often points at general accountability, the focus of the programmes, internal control measures and publicity measures. We have analysed various reports on both Member State level (specifically the Netherlands) and European level (consisting of both documents from the ECA and the EC). We focussed on annual reports concerning the year 2010 and specific reports issued in 2010, concerning the EUCP and its effects. The in total 18 reports we analysed (6 from authorities in the Netherlands, 2 from the ECA and 10 from the EC) dealt with accountability, evaluation or with giving a general overview of activities. In total the reports analysed in this research consisted of 1927 pages. All pages were ranked along one or more of the criteria mentioned above: information connected to compliance issues, performance issues or not belonging to either of these categories. In practice, the last category consists of blank pages, indexes and examples but also of more general background information in the report. This category is left out of the data analysis. The distribution of the information over compliance and performance auditing (the last category consisting of costs, input, output and outcome) leads to the following table and chart.

![Analysis of 2010 EUCP documents on compliance and performance audit (compliance versus costs-input-output-outcome) n = 1760](image)

<table>
<thead>
<tr>
<th></th>
<th>EC</th>
<th>ECA</th>
<th>NL</th>
<th>Average</th>
</tr>
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<tbody>
<tr>
<td>compliance</td>
<td>64%</td>
<td>79%</td>
<td>78%</td>
<td>68%</td>
</tr>
<tr>
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<td>0%</td>
<td>3%</td>
<td>4%</td>
<td>1%</td>
</tr>
<tr>
<td>input</td>
<td>2%</td>
<td>1%</td>
<td>6%</td>
<td>2%</td>
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<tr>
<td>output</td>
<td>12%</td>
<td>13%</td>
<td>11%</td>
<td>12%</td>
</tr>
<tr>
<td>outcome</td>
<td>22%</td>
<td>4%</td>
<td>1%</td>
<td>17%</td>
</tr>
</tbody>
</table>

14 Concerning 3 reports from the EC, 1 from ECA and 5 on Member State level in the Netherlands.
15 Concerning 6 reports from the EC and 1 from ECA.
16 Concerning 1 report from the EC and 1 on Member State level in the Netherlands.
17 The division of the amount of pages on the level is 75% from the EC, 4% from the ECA and 21% from public authorities in the Netherlands.
We analysed the reports issued by the Dutch EFRO OP’s and two reports issued by the Algemene Rekenkamer, the Dutch SAI, concerning European policy. The empirical analysis shows that 78% of the Dutch reports focused on compliance auditing information and only 22% on performance audit. When looking specifically at the part that focuses on performance audit, the attention is specifically going to output (11%, reporting on indicators) and input (6%, reporting on technical assistance). Less attention on the Member State level is going to the costs (4%) and outcome (1%).

It is not surprising that the upmost attention on this level is set at the in- and output, because these are the best possible facts to report on. The Ex-Post Evaluation of Cohesion Policy 2000-2006 gives an interpretation of the problems for performance management on regional level: ‘The context in which cohesion policy was implemented, the often small scale of the funding in relation to the forces it was intended to counteract and the many other factors at work mean that it is unrealistic in most cases to expect to be able to trace a direct link between policy and regional developments. [...] There was also a lack, in many cases, of a clear indication in concrete terms of the objectives of the policy implemented in a form which would enable the success or failure of the measures taken to be properly assessed. Often the aims of the policy were expressed in terms so general (e.g. an improvement in regional competitiveness) to make it difficult, if not impossible, to judge after the event whether they were achieved or not. Though quantitative targets were often set and an indicator system established, as required by the Structural Fund regulations, in many cases neither were linked in a meaningful way to ultimate policy objectives. [...] In most cases, [the targets set] did not play a central role either in the design or in the monitoring of policy and rarely featured in the policy debate. No authorities were held accountable for not meeting the targets set [...]’.\(^{18}\)

When analysing the annual documents from the MA’s it is also clear that a specific format is being used, as has been recommended by the EC. This also shows that the EC is specifically interested in information on general accountability and internal control measures and less on performance audit.

The ECA on the other hand doesn’t issue a lot of information on performance audit on EUCP. It publishes an Annual Report on the implementation of the budget.\(^{19}\) As is being said in paragraph 0.4: ‘The central part of the annual report is the Court’s statement of assurance (the ‘DAS’) on the reliability of the annual accounts of the EU and on the legality and regularity of transactions (referred to in the report as ‘regularity of transactions’).’ This means the focus of the ECA is put on the economy principle, i.e. on aspects like reliability, legality and regularity. This in spite of the fact that the ECA explicitly mentions the principle of sound financial management (which involves efficiency and effectiveness as well) in its Declaration of Assurance.\(^{20}\)

This is confirmed by the data in our research: only 21% of the ECA reports analysed are dealing with performance auditing aspects.

Next to its Annual Report, the ECA also issues special reports on the effectiveness of specific policy areas. Nevertheless, these reports often only cover a limited range of a specific policy fields – such as


\(^{19}\) For the latest report, see European Court of Auditors (2011). Annual report on the implementation of the budget concerning the financial year 2010. Luxembourg, European Court of Auditors. 2011/C 326/01.

\(^{20}\) Ibid.
The EC itself does also publish information on the compliance and performance auditing in the EUCP. The chart shows that the EC reports do have more attention to performance auditing (36%) than the reports from the ECA (21%) and the public authorities in the Netherlands (22%). This might be because the EC has published a lot of evaluation reports in 2010, often concerning the 2000-2006 Cohesion period. Of the ten (large) reports published by the EC on Cohesion Policy in 2010, six concerned evaluation reports, three accountability reports (Annual Activity Reports of DsG REGIO and EMPL and protection of the EU’s financial interests) and one a general overview (Fifth Cohesion report).

In the AAR’s the Director-General of the DG responsible for the specific policy is signing a declaration of assurance to 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 text, signed by all Director-Generals, shows that the focus is put on economy, regarding the words ‘used for their intended purpose’ and ‘legality and regularity’. Therefore, the Dutch Algemene Rekenkamer criticizes the AAR’s of the EC: ‘the transparency in the information offered in the AAR’s [...] on the effectiveness of the EU policy has slightly deteriorated. The reports do not give any information on the effectiveness of the policy in the Member States.’

The results from the research on the documents also show that especially the evaluation reports of the EC put a lot of focus on performance auditing with 38%, against 14% for the accountability reports.

At the same time, the EC especially focuses on outcome (22%) and output (12%) and hardly on input (2%) and costs (0%). This is not surprisingly, because the EC is the authority that has to justify its policy on EC level, where the other authorities in this research have other responsibilities. At the same time, it is surprisingly that the attention of the EC is hardly put at the costs and input phase of the performance audit chain. We would have expected a somewhat higher percentage.

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21 European Court of Auditors (2011). Have the e-Government projects supported by ERDF been effective? Luxembourg. Special report No. 9 2011.
24 Since only this last report is issued in 2010, this is the only special report that is included in the analysis. The ECA mentions another special report on its website that is issued in 2010 on Cohesion, ‘Impact assessments in the EU institutions: do they support decision making?’ Special report No. 3 2010,’ but this report does not cover auditing in EUCP and is therefore excluded.
27 The overview report analysed, the Fifth Cohesion report, consists of a lot of general information that is ranked in the ‘none’ category. The rest of the report does give information on performance audit, therefore this percentage, leading to 60%, is not comparable with the other categories.
4. Conclusion
Based on the data presented in the previous paragraph, we can first of all conclude that the majority of the information in the reports from all levels in the EUCP chain, on average 68%, is focussed on compliance auditing instead of performance auditing. This in spite of the fact that both the EC and the ECA declare in their Assurances of Statement that the resources are spent in accordance with the principle of sound financial management. The data show that this position cannot be validated, as information on performance is largely missing. Actually, this view is supported by reports from the EC itself, stating for instance: ‘A recurrent evaluation finding across all areas of investment was a preoccupation with ‘absorption’, i.e., with spending the money more than focusing on what the programmes were actually designed to achieve. While the former is obviously a pre-condition for success, the latter is ultimately what matters.’

Secondly, the data show that within the information on performance auditing, especially at the EC, the focus is set on outcome and output and hardly any information is given on input and costs. Again, this makes it very hard to make proper inferences on sound financial management and/or VFM within the EUCP. To be able to make such inferences, information on all relevant parts of the chain (costs, input, throughput, output, outcomes) should be available and linked. Even though we did not explicitly gathered quantitative information on such links, it became clear from our analysis that the reports barely deal with efficiency and effectiveness issues.

Thirdly, and related to this issue, we find it disappointing that the ECA publishes so little information on the effectiveness of the EUCP. We found only three reports published in 2010, labelled by the ECA as concerning EUCP, of which one report did not even really cover the policy concerned. Also, the reports that have been published by the ECA on the EUCP during the previous years (appr. 2-3 a year) are so specific in the focus of their evaluation that the conclusions hardly can be generalized to the EUCP-wide level.

Fourth, the role of the institutions should be taken into account when looking at the desired situation with more attention for performance audit. It is clear that on the regional level the focus will be put more on input and output (efficiency) than on the outcome of the policy, because these are better possible to measure on regional level. The outcome of the policy on the other hand, should be more in sight of the EC and possibly the ECA. At the same time, the EC needs information provided by the Member States to be able to give a clear picture on the efficiency and effectiveness of the policy. This asks for better coordination between the levels within EUCP and a clear statement of the EC on the information needed to be able to really give a good supported declaration on the aspect of sound financial management.

Finally we turn to the improvements that are needed in the EUCP regarding performance auditing. The EC does have attention for performance auditing, next to compliance auditing, but given the

dimension of the EUCP with almost one third of the budget of the EU, it needs more focus to be able
to really declare there is sound financial management in the policy field. Also, to be able to give an
overview of the performance of the EUCP on EU level, the EC also needs to point out the importance
of evaluations on effectiveness on national and regional level to the Member States. To start with,
the EC should urge them to give a clear indication at the start of the new programme period of the
objectives of the policy, which makes it possible to properly assess the effects. Also evaluations
should not only be performed on EC level, but it is appropriate when Member States also take their
responsibility and focus more on performance audit. The EC should point this out to the Member
States as well.
Although the subject matter is quite complicated in the public sector, as has been mentioned in the
introduction, it should be taken seriously and needs increasing attention from all actors. Let’s hope
the increased focus on performance audit the EC has put in the new programme period of ‘14 – ‘20
really leads to better audit and performance.
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