An introduction to the EU audit process

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Introduction

Brian Pack's recent study on red tape in the farming sector in Scotland recommended that all farmers and land managers take the time to understand the EU audit process.

This guide provides an outline of the process to help the industry understand the consequences and impact of audits for individual farmers, Scottish Government funding and Scottish agriculture as a whole.

Purpose and objectives

The audit process covers all area of EU-funded expenditure and not just the Common Agricultural Policy (CAP). It exists to protect taxpayers from inaccurate, illegal or fraudulent claims across the wide range of EU expenditure.

Overview

In short, when an audit takes place, a small team of auditors comes to Scotland for a few days.

They question us – the Rural Payments and Inspections Division (RPID) – on our processes, review our guidance and scheme rules, check our records, and visit some farms to assess eligibility and compliance. The auditors then leave and write-up their findings.

Afterwards, there is an exchange of correspondence and a series of meetings to confirm and agree the findings. The whole process from start to finish can take several years to complete.

The auditors are effectively checking whether our administrative checks and on-the-spot inspections were sufficient to ensure:

- the farmer was eligible for the money he got
- the farmer had complied with all the scheme rules and funding conditions
- the amount the farmer got was correct

The auditors are also checking:

- that any overpayments are recovered
- the appropriate penalties are applied in the case of farmers breaching scheme rules
- that any non-compliance or fraud is followed-up and reported
- the accuracy of record keeping and accounting

- the overall extent of farmers claiming (and us paying) money that is not fully in accordance with the scheme and EU regulations

The different types of audit

In practice, there a number of audits looking at our processes and controls, all of which, either directly or indirectly, can bring about disallowance [1].

European Court of Auditors

The European Court of Auditors audits the accounts of the European Commission annually. It reviews a sample of CAP payments made to farmers across Europe to assess compliance with the various rules and regulations, and to determine the overall level of errors or irregularities in the European Commission's accounts.

The audit findings are addressed to the European Commission. However, where an overpayment or irregularity is found during a European Court of Auditors visit to a particular farm, we are expected to recover any overpayment from the farmer and apply penalties in accordance with the European Commission regulations.

European Commission audits

European Commission audits are subject specific and we are audited across the full range of schemes or measures funded under the CAP.

We are typically subject to two or three European Commission audits per year.

The main focus is on our control systems, but audits often include visits to a small number of farms, mainly to assess the quality of our on-the-spot inspections, the general eligibility of claims, and the way in which we confirm eligibility and compliance.

For area-based schemes, the selection of cases for re-inspection is done using our aerial photography, which can readily highlight potential issues with land eligibility. This approach increases the risk of auditors finding overpayments.

The outcome of a European Commission audit can result in recommendations for changes to processes and potentially disallowance. The most frequent issues are the over-declaration of land and, in the area of cross compliance, ear-tagging failures, out-of-date livestock registers, and delays in notifying movements.

As with a European Court of Auditors audit, in the case of any specific overpayment found during the audit, we are expected to recover the overpayment from the farmer and apply penalties.

Annual Certification Audit

The Annual Certification Audit is undertaken by Audit Scotland, essentially on behalf of the European Commission.

This audit is of the EU CAP accounts that we have to prepare annually for direct farm payments and rural development expenditure.

Until 2014, this audit was essentially a financial one. However, from 2015, Audit Scotland also has to give an opinion on the 'legality and regularity' of the expenditure. This will involve a number of on-the-spot checks to assess the eligibility of the expenditure and the accuracy of the claim and payment.

The outcome of the Annual Certification Audit is reported to the European Commission and any financial errors detected in the sample are applied across the population as a whole, effectively as a form of disallowance.

As with the other categories of audit above, there is an expectation that where an overpayment is found during a visit to a particular farm, we will recover the overpayment from the farmer and apply penalties, potentially over several years where the breach has been ongoing.

National audits

The EU also requires that we have adequate internal audit arrangements. The Scottish Government therefore audits our systems and processes, including farm visits to assess the quality of inspections.

The output of this work is essentially for our management team, although the other auditors mentioned can draw on these findings to inform or reinforce their own work.

Furthermore, in addition to its role in the Annual Certification Audit, Audit Scotland also has a role in certifying the Scottish Government's domestic accounts. As one of the larger grant-giving parts of the government, we are subject to annual scrutiny by Audit Scotland.

Disallowance

[1] Disallowance, or financial correction, is the term used where the European Commission believes that our controls contain weaknesses or where there is evidence of widespread non-compliance that results in overpayments or irregularities.

The European Commission normally proposes disallowance as a fixed percentage of the total overall expenditure, with the gravity and number of weaknesses determining the level.

For weaknesses of a minor administrative nature, disallowance is normally two per cent of the total EU expenditure subject to audit.

For weaknesses in key controls, disallowance is normally five per cent or more.

Key controls include:

- inspections (timing, selection and conduct)
- eligibility checks
- land parcel identification system
- livestock database
- calculation of the aid due
- sanctioning and recovery of non-compliance

To put the risk in perspective, five per cent of the area-based payments in Scotland equates to approximately a €30 million per annum loss of revenue to the Scottish Government.

This is why we have to be rigorous in our approach to administrative checks, inspections, the application of sanctions, and the recovery of payments.

Implications for the farming industry of disallowance

Disallowance has no direct impact on farmers, since we cannot apply pro-rata reductions to farmers' payments.

However, there is an indirect impact, in that any reduction in the money received from the EU reduces the money available to fund the national element of rural development expenditure. Disallowance can lead to a gross reduction in overall Scottish Rural Development Programme (SRDP) funding.

It is important therefore for us and the farming industry to do all we can to avoid disallowance. We must ensure our controls are robust and are used in accordance with EU regulations. And farmers must ensure they understand the scheme rules and regulations, and comply with these and with the commitments contained in rural development contracts.

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