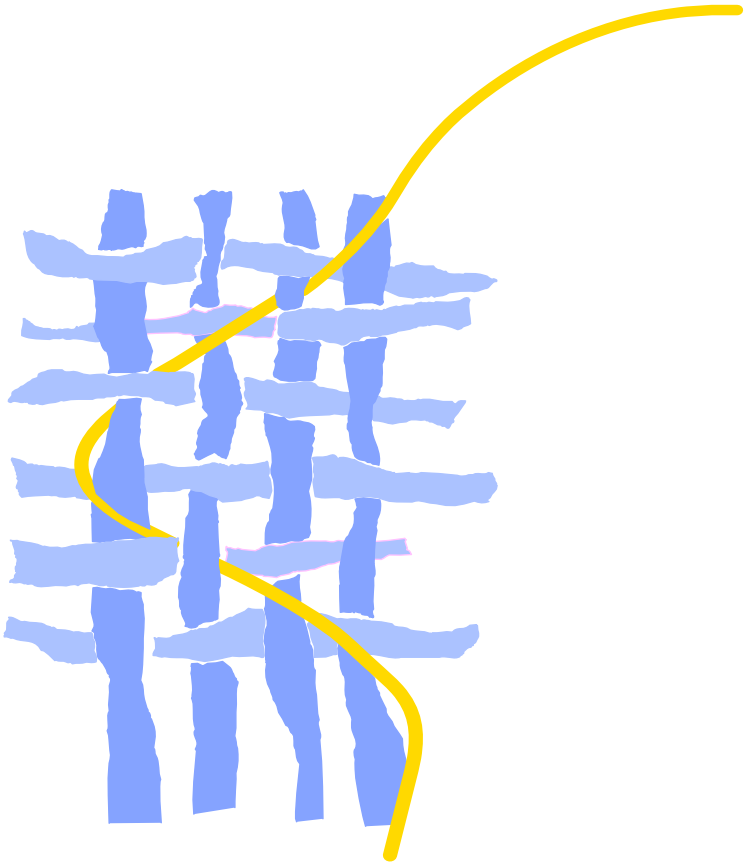
THE EUROPEAN OMBUDSMAN

RESPONSE TO THE PUBLIC CONSULTATION ON REVIEW OF THE FINANCIAL REGULATION



Strasbourg, 17 December 2009

Summary of the Ombudsman's proposals

1. The Charter of Fundamental Rights, to which the Treaty of Lisbon now gives the same legal value as the Treaties, includes the citizens' right to good administration. The Financial Regulation should take account of this new provision by providing guidance to officials as to how they should ensure both sound financial management and good administration. It should, in particular, make clear that the duty of those with financial responsibility is not to eliminate all risk of error, but to pursue, in a transparent way, a long term strategy that aims both to identify and manage financial risks and to promote good administration.

2. Applicants for grants should receive information about the legal remedies available to them.

3. Authorising officers should be able to waive recovery of a sum that has been unduly paid if recovery would be inconsistent with the right to good administration, or if recovery would be oppressive or unfair in the circumstances of the case.

4. The Financial Regulation should, in exceptional cases, provide for *ex gratia* payments, as redress for material loss, serious inconvenience, or severe distress caused by maladministration.

5. The threshold for automatic interest in case of late payment should be reviewed. Creditors who do not benefit from automatic interest should be informed about their right to claim interest.

6. Sub-contractors and staff of contractors should be informed, and given the opportunity to respond, when an EU institution criticises their performance.

Introduction

The European Commission is holding a public consultation on the second review of the Financial Regulation and its implementing rules. According to the consultation document[1], the Commission will present its proposals in mid-2010. The Commission identifies two topics as being of most direct concern to recipients and potential recipients of EU funds. These topics are:

- The award of grants;

- The Commission's handling of financial files.

The Commission states that it would also appreciate contributions relating to other topics covered by the Financial Regulation.

The European Ombudsman has dealt with a large number of complaints to which the provisions of the Financial Regulation and/or the Commission's Implementing Regulation have proved relevant[2]. He has also conducted several own-initiative inquiries into subjects relating to the Financial Regulation. The present response to the consultation is based on the Ombudsman's accumulated 14 years of experience with these cases[3]. It also takes into account the Ombudsman's discussions and meetings with Members and staff of the EU institutions[4], and with organisations which are, or which represent, recipients of EU funds (trade associations, Chambers of Commerce, non-governmental organisations).

The Ombudsman's proposals concern:

- The objectives of the Financial Regulation as regards risk;
- Information about remedies;
- Waiver of recovery of sums unduly paid;
- Interest in case of late payment;
- The rights of sub-contractors and staff;
- *Ex gratia* payments in exceptional cases of maladministration.

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1 http://ec.europa.eu/budget/library/consultations/FRconsult2009/consultation_paper_en.pdf

2 Council Regulation (EC, Euratom) No 1605/2002 of 25 June 2002 on the Financial Regulation applicable to the general budget of the European Communities, 2002 OJ L 357, p.1.; Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No 1605/2002 on the Financial Regulation applicable to the general budget of the Communities 2002 OJ L 357, p.1 (as last amended by Regulation (EC, Euratom) No 478/2007 of 23 April 2007, 2007 OJ L 111, p. 13).

3 An initial database search identified 136 decisions and 10 draft recommendations which mentioned the Financial Regulation. Some of these cases concerned provisions that have already been amended.

4 For convenience, this response uses the term "institution" to refer to all the EU Institutions, bodies, offices and agencies. When referring to an Institution in the sense of Article 7 of the EC Treaty, the term "Institution" is capitalised.

These proposals are relevant to the two topics identified by the Commission, but also have broader application. They are explained in detail below.

This response does not address issues related to the Early Warning System, which is currently the subject of an own-initiative inquiry by the Ombudsman[5].

1 The objectives of the Financial Regulation as regards risk

The EU and its institutions are ultimately financed by European citizens. Citizens in general are entitled to expect the institutions to handle their money wisely and properly and, in particular, to take appropriate measures to avoid the mismanagement or misappropriation of funds. Furthermore, Article 41 of the Charter of Fundamental Rights (to which the Treaty of Lisbon gives the same legal value as the Treaties) provides that *every person has the right to have his or her affairs handled impartially, fairly and within a reasonable time by the institutions, bodies, offices and agencies of the Union*. The right to good administration also applies to financial matters, such as contracts and grants.

The fall of the Santer Commission in 1999 was a traumatic event for the EU institutions, especially the Commission. The search for ways to tackle the problems that had caused it led to many changes, mostly for the better. One consequence, however, was to encourage the view that the ideal level of financial risk in the EU institutions is zero. In this context, it is important not to confuse zero-risk of financial error with the policy of zero-tolerance of fraud. The latter policy should mean that, whenever fraud is detected, criminal and disciplinary measures are pursued. Zero-tolerance in this sense is both valuable and deliverable, but only a very small proportion of the financial errors that occur each year involve fraud[6].

A policy that aims to reduce the level of financial error to zero is doomed to failure, because efforts to avoid errors are subject to diminishing returns: ultimately, zero-risk of error would imply zero activity.

In practice, the philosophy that any error is unacceptable results in slow administration, or even inertia, because it brings forth excessively detailed and complex procedures and because it encourages a state of mind in which officials seek to avoid the personal risk that they will be held responsible for

5 OI/3/2008/FOR. Details of the own-initiative inquiry are available on-line: http://www.ombudsman.europa.eu/cases/initiatives.faces

6 On average, the Court of Auditors reported 3.5 cases of suspected fraud per year to the Anti-Fraud Office (OLAF) in the four years 2004-7: see the Court's Information Note on the 2007 Annual Report on the 2007 EU Budget.

errors. These consequences are especially likely to occur when financial error is wrongly equated with fraud.

The end result of such circumstances is that the institutions find it difficult to respect the right to good administration of persons who have financial dealings with them. The impact on the image of the EU is negative, especially since the burdens are particularly heavy for individuals and SMEs, which find it more difficult to obtain bank credit than large companies and, as a result, may well screen themselves out of competing for EU contracts and grants.

The current review should ensure that, in addition to sound financial management, the Financial Regulation encourages and promotes respect for the right to good administration. In this context, the review also offers an opportunity for the main Institutions that deal with the EU budget (the European Parliament, the Council, the Commission and the Court of Auditors) to communicate to the public the distinction between (i) zero-tolerance of fraud, when it is detected, and (ii) accepting a reasonable and appropriate level of financial risk. This could be facilitated by amending the Financial Regulation to make clear that the duty of those with financial responsibility is not to eliminate all risk of error, but to identify and manage financial risks in a transparent way.

This change would benefit citizens in general, by promoting better functioning of the institutions. It would also benefit citizens, enterprises (especially SMEs) and associations by reducing the administrative burdens that they face in dealing with the EU institutions.

2 Information about remedies

The Ombudsman is pleased to note that, following the 2007 revision[7], the obligations imposed on the EU institutions by Article 149 (3) of the Implementing Regulation include the provision of information to unsuccessful tenderers about the legal remedies available to them.

There is, however, no requirement to inform unsuccessful applicants for grants about remedies.

The European Code of Good Administrative Behaviour states that:

7 Commission Regulation (EC, Euratom) 478/2007 of 23 April 2007 amending Regulation (EC, Euratom) 2342/2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities, 2007 OJ L 111 p.13.

A decision of the institution which may adversely affect the rights or interests of a private person shall contain an indication of the appeal possibilities available for challenging the decision. It shall in particular indicate the nature of the remedies, the bodies before which they can be exercised, as well as the time limits for exercising them. (Article 19)

The Ombudsman notes that recent case-law confirms the admissibility before the Community Courts of an action to annul a decision refusing a grant application[8].

The Ombudsman, therefore, considers that it would be appropriate for the relevant provision of the Implementing Regulation (Article 179) to require that information be given about available legal remedies whenever a grant application is rejected.

3 Waiver of recovery of sums unduly paid

Article 87 of the Implementing Regulation provides that the authorising officer may waive recovery only in the following cases:

a) where the foreseeable cost of recovery would exceed the amount to be recovered and the waiver would not harm the Community's image;

b) where the amount receivable cannot be recovered in view of its age or the insolvency of the debtor;

c) where recovery is inconsistent with the principle of proportionality.

Waiver of recovery of sums due to the EU budget should be an exceptional measure and the provision authorising it should be interpreted and applied restrictively. However, the Ombudsman has dealt with a number of cases where the institution concerned has interpreted and applied Article 87 so narrowly as to be unreasonable. Furthermore, once a waiver has been refused, the institutions appear extraordinarily reluctant to change their position. In one case, for example, the institution concerned had made payments to a citizen, who was the heir of a deceased official. One payment was made mistakenly, and the institution tried to recover the relevant sum several years later. The complainant contested the recovery on the grounds that (i) he had acted in good faith; (ii) the institution only asked for repayment four and a half years after the payment was made; (iii) he had not been aware of the amounts in the relevant bank account because of tragic circumstances, namely, the loss of several members of his family in a short time; and (iv) as a voluntary worker in an

8 Order of the Court of Justice of 5 March 2009 in Case C-183/08 P, *Commission v Provincia di Imperia*, dismissing as manifestly unfounded the Commission's appeal against the decision of the Court of First Instance in Case T-351/05, *Provincia di Imperia v Commission*, [2008] ECR II-241.

NGO, he had no means to reimburse the sum. The Ombudsman agreed with the complainant. The institution, however, rejected a proposal for a friendly solution and it was necessary for the Ombudsman to make a draft recommendation before it agreed to cancel the recovery order[9].

In such cases, the risk to the European Union's reputation for good administration vastly outweighs any possible benefit to the Community budget from recovering the sums involved. In the Ombudsman's view, recovery in such cases would be inconsistent with the principle of proportionality and should therefore be waived in accordance with Article 87 (c) of the Implementing Regulation as it now exists. However, for the avoidance of doubt and to prevent further cases of this kind, the latter provision should be clarified.

As mentioned above, Article 41 of the Charter of Fundamental Rights (right to good administration) provides that every person has the right to have his or her affairs handled impartially, fairly and within a reasonable time (emphasis added). This right should be explicitly mentioned in Article 87 (c) of the Implementing Regulation, so that it would refer to cases "*where recovery is inconsistent with the right to good administration or the principle of proportionality, in particular because it would be oppressive or unfair in the circumstances*."

This change would clearly signal to the institutions the need to take the right to good administration into account, following the entry into force of the Lisbon Treaty.

In order to ensure a consistent approach, it could be useful for the heads of administration of the institutions (who meet regularly) to examine periodically how the revised provision is applied in practice.

4 *Ex gratia* payments in cases of maladministration

When maladministration occurs, an apology and correction of the error normally constitute adequate redress for the complainant. In exceptional cases, where the maladministration has caused the complainant to suffer material loss, serious inconvenience, or severe distress, financial redress may be appropriate.

9 Cases 1617/2005/JF and 902/2007/RT. The Ombudsman's decisions are available on-line at: http://www.ombudsman.europa.eu/cases/decision.faces/en/2910/html.bookmark, http://www.ombudsman.europa.eu/cases/decision.faces/en/3327/html.bookmark

In accordance with Article 3 (5) of his Statute[10], when the European Ombudsman finds maladministration, he seeks a friendly solution, if possible. The Ombudsman has noted that the institutions have been very reluctant to co-operate in the few cases for which he has proposed a friendly solution that would consist of, or include, financial redress. The main reason appears to be the view that such payments imply that the conditions for contractual or non-contractual liability are met. Since these conditions include the illegality of the institution's behaviour, reluctance to accept the Ombudsman's proposals is unsurprising. Furthermore, the institutions may also fear that agreeing to financial redress could be construed as an admission of legal liability, which would expose them to an action for damages.

The Ombudsman considers that the above-mentioned concerns are unjustified. The case-law of the Community courts clearly indicates that a finding of maladministration by the Ombudsman does not necessarily imply that the behaviour of the institution concerned was unlawful. In the Ombudsman's view, it follows from this case-law that financial redress as a solution to maladministration does not depend on the conditions for contractual or non-contractual liability being met. Furthermore, the Ombudsman consistently emphasises that financial redress for maladministration is *ex gratia* and does not involve any admission of legal liability.

Even if they accept the Ombudsman's views on this point, however, institutions may be reluctant to agree to financial redress on the grounds that, unless the conditions for contractual or non-contractual liability are (at least arguably) fulfilled, there is no legal basis for making an *ex gratia* payment.

The Ombudsman, therefore, considers that it would be useful to recognise the possibility of financial redress for maladministration in the Financial Regulation and Implementing Regulation. This could be done through the introduction of a new Article 179b into the Financial Regulation as follows:

> *The implementing rules shall make provision for the authorisation of* ex gratia *payments, in exceptional cases of material loss, serious inconvenience, or severe distress caused by maladministration.*

The corresponding provision of the Implementing Regulation could be a new Article 265b as follows:

10 Decision of the European Parliament 94/262/ECSC, EC, Euratom of 9 March 1994 on the regulations and general conditions governing the performance of the Ombudsman's duties, 1994 OJ L 113 p. 15, as last amended by Decision of the European Parliament 2008/587/EC, Euratom of 18 June 2008, 2008 OJ L 189 p. 25.

1 Each institution shall lay down in its internal rules the conditions and procedure for delegating the power to authorise ex gratia *payments in exceptional cases of material loss, serious inconvenience, or severe distress caused by maladministration.*

2 Each institution shall send to the budgetary authority each year a report on the payments referred to in paragraph 1 involving EUR 5000 or more. In the case of the Commission, that report shall be annexed to the summary of the annual activity reports referred to in Article 60(7) of the Financial Regulation.

As in the case of waiver (section 3 above) and with an eye to ensuring a consistent approach, it could be useful for the heads of administration of the institutions to examine periodically how the new provision is applied in practice.

5 Interest in case of late payment

The problem of late payment by Community institutions has given rise to many complaints to the Ombudsman and has led to own-initiative inquiries, one of which is ongoing[11].

The Ombudsman notes that, following the 2007 revision[12], Article 106 of the Implementing Regulation foresees automatic interest in case of late payment. However, by way of exception, when the interest is lower than or equal to EUR 200, it is paid only if the creditor makes a request within two months. This is a significant improvement compared to the former situation, in which any payment of interest had to be specifically requested by the creditor. However, as the Ombudsman has already pointed out[13], in many cases of excessive delay in paying citizens or small and medium-sized undertakings, the amount of interest due is likely to be less than EUR 200.

The Ombudsman does not exclude the possibility that calculating and paying interest in each and every case of late payment could impose a disproportionate administrative burden on the EU institutions. The Ombudsman is not aware, however, of the legal or other basis on which the threshold of 200

11 OI/1/2009/GG. Details of the own-initiative inquiry are available on-line: http://www.ombudsman.europa.eu/cases/initiatives.faces

12 Commission Regulation (EC, Euratom) 478/2007 of 23 April 2007 amending Regulation (EC, Euratom) 2342/2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities, 2007 OJ L 111 p.13.

13 OI/5/2007/GG http://www.ombudsman.europa.eu/cases/decision.faces/en/3387/html.bookmark See point 1.10.

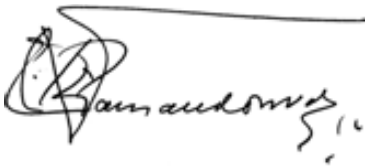
EUR was chosen. Furthermore, that figure seems too high to represent a reasonable compromise between the rights of creditors and the need to avoid unnecessary administrative work. The Ombudsman suggests, therefore, that the Commission review the need for a threshold. In the event that it considers that a threshold should be maintained, detailed evidence should be provided to justify its level. Moreover, in that event, creditors should not be prevented from claiming interest, even if the amount is minimal. In order to enable them to do so, clear information on their rights should be provided.

6 The rights of sub-contractors and staff

The Commission implements many EU programmes by entering into contracts. In many cases, the contractor enters into sub-contracts. The Commission has no contractual responsibilities towards sub-contractors, or the staff employed by contractors and sub-contractors. Moreover, the Financial Regulation and the Implementing Regulation do not confer rights on such persons.

This situation can result in procedural unfairness; in particular where the Commission gives a negative assessment of the performance of a sub-contractor or member of staff. For example, in one case dealt with by the Ombudsman, the Commission insisted on removing the complainant from his position as team leader of a project, even though his employer was happy with his performance and informed him that he was being dismissed only because of the Commission's insistent demands to that effect[14]. In such cases, the person whose performance is negatively assessed by the Commission may not even be informed of the details of the negative assessment, let alone have the opportunity to state his or her point of view.

In the Ombudsman's view this situation is unfair and incompatible with the right to good administration. The Ombudsman, therefore, suggests that the Financial Regulation and/or the Implementing Regulation should make provision for sub-contractors and staff to be informed, and given the opportunity to respond, when an EU institution criticises their performance.



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14 Case 2477/2005/GG. The Ombudsman's decision on the case is available on-line http://www.ombudsman.europa.eu/cases/decision.faces/en/2979/html.bookmark