



HM TREASURY

# Consolidated statement on the use of EU funds in the UK:

for the year ended 31 March 2009

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Consolidated statement on the use of  
EU funds in the UK:  
for the year ended 31 March 2009

Presented to the House of Commons by  
Command of Her Majesty

Ordered by the House of  
Commons to be printed on  
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# 1

## Commentary

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### Background

**1.1** As part of ongoing work to improve the accountability of European Union (EU) funds, the then Economic Secretary to the Treasury announced to the House of Commons on 20 November 2006 that HM Treasury would prepare an annual Consolidated Statement on the use of EU funds in the United Kingdom (the Statement) and invited the Comptroller and Auditor General to undertake the external audit of this Statement. This Statement covers the period 1 April 2008 to 31 March 2009.

**1.2** The preparation, audit and publication of the Statement helps promote the sound management of EU funds by strengthening Parliamentary scrutiny of the UK's management of those funds and by assisting in the detection of any weaknesses in control systems, which can then be tackled more quickly and effectively. The Government hopes that in conducting their audit work the European Commission and the European Court of Auditors will be able to take the Statement into account as well as the assurance provided by the Comptroller and Auditor General in the audit opinion and Report. Similar initiatives are underway in other Member States, such as Denmark and Sweden.

### Respective responsibilities of the UK Parliament and Devolved Administrations

**1.3** In accordance with the devolution settlement, relations with the European Union are the responsibility of the Parliament and Government of the United Kingdom, as a Member State. Responsibility for implementing EU obligations relating to devolved matters lies with the Devolved Administrations. The proper administration of EU Funds in Northern Ireland, Scotland and Wales is a matter for the relevant Devolved Administration. This Statement is prepared without prejudice to the devolution of responsibilities.

### Preparation of the Statement

**1.4** HM Treasury has assumed responsibility for developing the format of the Statement and for collating the financial data provided by Managing Authorities<sup>1</sup> included in the Statement. Managing Authorities, however, remain accountable for the propriety of the reported spending, which is disclosed in their annual financial statements and is subject to external audit. The Statement therefore brings together financial information relating to the use of EU funds by the UK but does not replace individual accountabilities.

**1.5** This is the third such Statement and, along with the accompanying Report of the Comptroller and Auditor General, it honours the Government's commitment to present an annual statement of the UK's receipt and use of EU funds. The purpose of the Statement is to bring together financial information in respect of EU sponsored projects in the UK. It supports greater scrutiny of the UK's management of EU funds and of the financial relationship between the UK and the EU.

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<sup>1</sup> For the purposes of this Statement, the Managing Authorities comprise the Westminster Departments managing EU funds and the Devolved Administrations.

**1.6** The format of this third Statement builds on earlier Statements. HM Treasury is continuing work with Managing Authorities to develop the format and content with the aim of improving the reporting and disclosure of the use of EU funds.

**1.7** The Economic Secretary to the Treasury's announcement in November 2006 referred to the preparation of a Statement in accordance with International Financial Reporting Standards (IFRS).<sup>2</sup> The UK Government moved its financial reporting on to an IFRS basis on 1 April 2009. In future, therefore, this Statement will be prepared on an IFRS basis.

## **Boundary of the Statement**

### **EU funding of UK expenditure**

**1.8** The Statement shows expenditure on co-managed EU schemes in the UK and the corresponding income from the EU. The main schemes in which the EU and UK share management responsibility include the disbursement of Common Agricultural Policy Funds and the Structural Funds, where the UK pays beneficiaries on behalf of the EU.

**1.9** The Statement excludes:

- amounts received from the EU where UK central government is the beneficiary;
- amounts in respect of commercial contracts awarded to UK central government bodies by the EU;
- financial support for twinning projects<sup>3</sup> where EU funding is transferred to other Member States or to mandated bodies for their part in the project. The transactions are not reported as income and expenditure of the relevant Managing Authority; and
- the purchase of Intervention stocks<sup>4</sup> with UK funds which are accounted for in the financial statements of the Department for Environment, Food and Rural Affairs (DEFRA).

## **Member States' contributions to the EU**

**1.10** Member States' contributions to the Budget of the European Communities are made on the basis of the financing system set out in the Own Resources Decision which was agreed by all Member States and incorporated into UK law by virtue of the EC (Finance) Act 2001. The contributions relate to calendar years and are formula based using factors that are in many cases subject to periodic revision over a number of years as better information becomes available. UK contributions to the EU are included in the Government's Consolidated Fund Account, which is published separately (HC929, 2008-09). These contributions are not, therefore, included in this Statement.

## **Timing of expenditure and the related EU funding**

**1.11** Managing Authorities are required to account for expenditure on EU-funded schemes and the related funding from the EU on an accruals basis under UK GAAP (International Financial

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<sup>2</sup> IFRS includes pronouncements by or endorsed by the International Accounting Standards Board (IASB), including the Framework for the Preparation and Presentation of Financial Statements, the accounting standards – international accounting statements (IAS) and international financial reporting standards (IFRS) – and interpretations thereof issued by the Standards Interpretations Committee (SIC) or its successor, the International Financial Reporting Interpretations Committee (IFRIC).

<sup>3</sup> Twinning projects are EU funded projects that support the capacity building in new Member States or the Candidate Countries. They are delivered by the public sector, usually by central government. These are funded through pre-accession funds.

<sup>4</sup> Intervention stocks are stocks held by paying agencies in the European Union as a result of intervention buying of commodities subject to market support. Intervention stocks may be released onto the internal markets if internal prices exceed intervention prices; otherwise, they may be sold on the world market.

Reporting Standards from 1 April 2009). There is normally a time lag between payment to beneficiaries and settlement of claims by the EU. The UK Exchequer therefore has to bear the cost of the programme until EU funding is received. Expenditure is recognised as it is incurred, with a matching debtor from the EU. The debtor is extinguished when the EU approves the subsequent claim and the release of funds to the UK.

**1.12** The final settlement of claims by the EU may give rise to adjustments following the closure process or disallowances (see paragraphs 18 to 21 below). The European Commission may make such adjustments several years after funds have been paid out by Managing Authorities to recipients. The Statement includes provision for possible future adjustments and discloses contingent liabilities where the position is less certain.

**1.13** Such an arrangement does not easily lend itself to a 'traditional' presentation of the primary statements of an income and expenditure statement, a balance sheet and cash flow statement. Each of these might contain a combination of EU funds and expenditure supported, temporarily, by the UK Exchequer. Primary statements have nevertheless been developed supported by notes to aid understanding of the figures. HM Treasury will continue to improve these primary statements through feedback from users and contributors to the Statement.

## **Expenditure on EU funded schemes in 2008-09**

**1.14** The Statement shows that gross expenditure on EU-supported Schemes in 2008-09 was £4.18 billion, a reduction of some £0.2 billion compared with the previous year. This reduction was mainly due to lower expenditure on schemes supported by the European Regional Development Fund and the European Social Fund. After allowing for foreign exchange variations and adjustments to claims, the amount reimbursable by the EU is £3.83 billion, the balance being met by the UK Exchequer.

**1.15** There was a reduction in temporary funding of EU-supported schemes by the UK Exchequer. At the year end, temporary funding amounted to £218 million, compared with £231 million at the end of the previous year.

**1.16** In recognition of likely future funding adjustments, Managing Authorities made net new provisions totalling £288 million against claims for reimbursement from the EU, including substantial provisions against disallowances of payments under the Common Agricultural Policy and European Regional Development Fund. These include provisions made by Managing Authorities in their financial statements for 2009-10, which have been recognised as adjusting post balance sheet events in this Statement. After allowing for the use of £142 million provisions following the crystallisation of adjustments, total provisions at 31 March 2009 amounted to £601 million, some £147 million higher than the corresponding figure at the end of the previous financial year.

## **Financial corrections announced since 31 March 2009**

**1.17** Since the end of the reporting period, the EU has announced a number of planned financial corrections and revisions to previous proposals. Material corrections and revisions are set out below.

### **Common Agricultural Policy Funds**

#### **Environment, Food and Rural Affairs**

**1.18** On 30 September 2009, the Commission issued a report imposing financial corrections totalling £3.3 million, primarily in respect of expenditure incurred between 28 August 2005 and 28 August 2007 on the England Rural Development Programme. The disallowance, representing 5 per cent of expenditure claimed, was imposed because of deficiencies in the system for

checking beneficiaries' entitlement to subsidy, in particular, cross checks on the declared number of animals.

**1.19** On 5 January 2010, the Commission issued a report proposing a £28 million correction in respect of expenditure on the Fruit and Vegetable Scheme incurred by the Department between 8 November 2005 and 15 October 2008. A provision has been made in the Statement for the proposed correction, which is subject to conciliation.

**1.20** On 15 July 2010, The Commission issued a decision confirming disallowances totalling £158 million in respect of the Single Farm Payment Scheme between 2005 and 2008. The Department had previously made provision for these disallowances. European Commission recovery of sums due will be reflected in future Statements.

### **Northern Ireland Executive**

**1.21** On 5 January 2010, the Commission notified the Executive of a proposed 5 per cent financial correction amounting to £31 million in respect of expenditure incurred in 2004, 2005 and 2006 on the Single Farm Payment Scheme and land-based Pillar II schemes. The proposed financial correction was confirmed in the Commission's decision of 15 July 2010. The Commission also notified the Executive on 5 January 2010 of a similar flat rate correction amounting to £31 million in relation to expenditure incurred in 2007 and 2008. This proposal is subject to conciliation. The proposed disallowances flow from perceived deficiencies in controls over the expenditure, for example with farm maps and on-the-spot inspections. A provision has been made in the Statement for the proposed corrections.

### **Other Funds**

#### **Northern Ireland Executive**

**1.22** In 2008 the Commission announced a potential financial correction against the Northern Ireland Single Programme Document (NISPD) and the Special Support Programme for Peace and Reconciliation in Northern Ireland and the Border Counties of Ireland (PEACE I) Programmes (1995-99). Negotiations progressed during 2009 to bring the matter to a conclusion. Initial discussions reduced the correction to £34 million and subsequent negotiations led to revised closure proposals in December 2009 reducing the correction to £25 million. A provision has been made in the Statement for this amount. In March 2010, the Department of Finance and Personnel paid £9.9 million to the EU, in relation to the £25 million financial corrections. The amount paid was the total financial corrections less £15.1 million that had been due from the Commission in respect of the PEACE and NI Single Programmes.

### **Management of EU funded schemes**

#### **(a) Common Agricultural Policy Funds**

**1.23** As required by Regulation 885/06 each paying agency has an internal audit service independent of the other arms of the entity that reports directly to the agency's director. The Internal Audit Services are required to verify that the procedures adopted by the agency are adequate to ensure compliance with Community rules and that accounts are accurate, complete and timely.

**1.24** Verifications may be limited to selected measures and samples of transactions provided that an audit plan ensures that all significant areas, including the departments responsible for authorisation, are covered over a period not exceeding five years.

**1.25** The work of internal audit is performed in accordance with internationally accepted standards, recorded in working papers and result in reports and recommendations, which are addressed to the agency's senior management.

**1.26** The Certifying Body for the Agricultural Funds reports on whether the annual accounts of the Paying Agencies are in all material respects true, complete and accurate and that internal control procedures have operated satisfactorily. The Certifying Body reports have confirmed that internal audit in all the UK paying agencies is operating to a high standard.

### **(b) Structural Funds**

**1.27** The Managing Authorities responsible for the control of structural fund expenditure ensure that all systems are subject to regular examination by internal audit.

**1.28** Management use internal audit results to strengthen procedures during the implementation of programmes. At the closure of programmes, internal audit provide reasonable assurance as to the accuracy, completeness and regularity of expenditure certified to the Commission.

**1.29** Recent internal audit work within Managing Authorities has generally reported a positive picture with most having a satisfactory level of assurance that systems operate adequately. Where this was not the case, action plans were agreed to address weaknesses.

### **Future developments**

**1.30** For the 2008-09 Statement HM Treasury has continued to work closely with Managing Authorities and the National Audit Office to agree how underlying transactions should be reported in the Statement. This has improved the quality of the data used to produce the Statement.

**1.31** These initiatives will continue for the 2009-10 Statement. The priorities are to agree a consistent approach to recognising underlying transactions and how these should be recorded in the accounts of Managing Authorities and in the Statement. HM Treasury will also review the form and content of the Statement on the adoption of International Financial Reporting Standards. It will also work on refining the governance structures for the Statement and the provision of data.

**1.32** The on-going work to develop better guidance on the accounting requirements for the Statement continues. HM Treasury has also developed clearer and more comprehensive guidance on the recognition and measurement of EU funding and is examining the scope for lower level guidance to ensure that underlying processes are consistent across Managing Authorities.

### **External audit**

**1.33** The Statement is subject to external audit by the Comptroller and Auditor General. His audit opinion and report to the House of Commons is published with the Statement.

A handwritten signature in black ink, appearing to read 'Nick Ray', with a long horizontal flourish extending to the right.

Sir Nicholas Macpherson  
Permanent Secretary HM Treasury  
12 January 2011

# 2

## Statement of the Responsibilities of HM Treasury's Accounting Officer

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### Statement of the Responsibilities of HM Treasury's Accounting Officer in relation to the Consolidated Statement on the Use of EU Funds in the UK

**2.1** Following the announcement made by the then Economic Secretary to the House of Commons on 20 November 2006, HM Treasury has prepared a Consolidated Statement on the use of EU Funds in the UK for the financial year 2008-09. The Statement is prepared on an accruals basis and includes an expenditure statement, a balance sheet and a cash flow statement intended to give a true and fair view of expenditure on EU supported programmes by UK central government sector entities and the related funding due from the EU.

**2.2** HM Treasury's Accounting Officer has overall responsibility for the preparation of the Statement, which consolidates the EU Funds accounted for by the individual central government sector entities disclosed at Note 2. Responsibility for the recording and regularity of underlying transactions rests with the Accounting Officers of the individual entities that account for the receipt and payment of EU monies.

**2.3** In preparing the Statement, HM Treasury's Accounting Officer has, so far as is relevant to this Statement:

- observed the requirements of the Government Financial Reporting Manual (FRM);
- applied suitable accounting policies on a consistent basis;
- made judgements and estimates on a reasonable and consistent basis; and
- stated whether applicable accounting standards have been followed and disclosed and explained any material departures in the accounts.

**2.4** Responsibility for the preparation of the returns of expenditure, receipts and other relevant accounting information for the public sector entity accountable for the payment of EU Funds rests with the Accounting Officers of the relevant entity. These Officers are responsible for preparing data capture returns for that body in accordance with the requirements set by the Treasury. In discharging his responsibilities for the preparation of the Statement, HM Treasury's Accounting Officer relies upon the returns provided by those Officers.

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## Independent auditor's report to the Economic Secretary to the Treasury

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I have audited the Consolidated Statement on the use of EU funds in the UK for the year ended 31 March 2009. These comprise the Expenditure Account, the Balance Sheet, the Cash Flow Statement and the related Notes. These financial statements have been prepared under the accounting policies set out within them.

### **Respective responsibilities of the Treasury, other Accounting Officers and auditor**

HM Treasury's Accounting Officer has overall responsibility for the preparation of this Statement which consolidates the EU Funds accounted for by the individual central government entities detailed in Note 2. Responsibility for the recording and regularity of underlying transactions rests with the Accounting Officers of the individual entities that account for the receipt and payment of EU monies. These responsibilities are set out in the Statement of Responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the accounting policies outlined in them. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

In addition, I report to you if I have not received all the information and explanations I require for my audit, or if information required by HM Treasury's Financial Reporting Manual, insofar as it is applicable, is not disclosed.

I read the Commentary, published with the Consolidated Statement, and consider whether it is consistent with the audited financial statements. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

### **Basis of audit opinions**

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements. It also includes an assessment of the significant estimates and judgements made by HM Treasury and other Accounting Officers in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Statement, consistently applied and adequately disclosed.

I planned my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, and that in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. However, the evidence available to me was limited due to a failure to maintain adequate

accounting records and supporting evidence for Temporary UK Funding of £217,994,000 in the Balance Sheet and Receipts from the EU (£361,182,000 of the £4,687,084,000 balance included in the Cash Flow Statement) and the corresponding 2007-08 figures.

In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements.

### **Qualified Opinion Arising from Disagreement on Consistency of Application of Accounting Policies, Disagreement on Accounting Policies for Foreign Currency Transactions and Limitations in Audit Scope**

- The financial statements do not comply with the Financial Reporting Framework as:
  - accounting policies have not been applied consistently to similar transactions and events across all UK Managing Authorities; and
  - the statements do not account for foreign currency transactions carried out by the Rural Payments Agency in accordance with Financial Reporting Standard (FRS) 23 *The Effects of Changes in Foreign Exchange Rates*.
- This has led to consequential material misstatement of:
  - debtors, creditors and related transactions between entities, including the corresponding 2007-08 figures;
  - the 2007-08 figures for EU funding, cash balances and provisions for financial corrections; and
  - recognised exchange gains and losses in scheme expenditure and gains arising on the revaluation of the European Commission debtor.

I am unable to quantify the impacts on the financial statements because the Managing Authorities have not maintained the records or obtained the information required to comply with the financial reporting framework in these respects. My audit opinion has been modified because of the effects of the misstated 2007-08 figures on the comparability of the current period's figures and the corresponding figures.

Except for the financial effects arising as a result of the failure to apply consistent accounting policies or to properly apply FRS 23 and any adjustments which might have been determined to be necessary had I been able to obtain sufficient appropriate audit evidence over Temporary UK Funding and Receipts from the EU and the corresponding 2007-08 figures, **in my opinion:**

- the financial statements give a true and fair view of the state of affairs of the use of EU funding in the UK as at 31 March 2009, and of the expenditures and cash flows for the year then ended; and
- the financial statements have been properly prepared in accordance with HM Treasury's Financial Reporting Manual, insofar as it is applicable to the Consolidated Statement.
- In respect of the limitation on my work relating to Temporary UK Funding and reported Receipts from the EU:
  - I have not obtained all the information and explanations that I considered necessary for the purposes of my audit; and
  - proper accounting records have not been maintained.

- **In my opinion**, information which comprises the Commentary, published with the Consolidated Statement, is consistent with the financial statements.

### **Qualified opinion on Regularity**

Where the European Commission determines that its scheme regulations have not been complied with, it may impose a disallowance penalty. In the year to 31 March 2009 and in the period prior to the Accounting Officer signing the Consolidated Statement, £398million of disallowance penalties were confirmed. I have concluded that this expenditure has not been applied to the purposes intended by Parliament because it represents a crystallised loss to UK funds.

**In my opinion**, except for £398 million of confirmed disallowance penalties, in all material respects, the expenditure and funding have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

### **Report**

Further details are set out in my report on pages 15 to 22.

Amyas CE Morse  
Comptroller and Auditor General  
14 January 2011

National Audit Office  
157-197 Buckingham Palace Road  
Victoria  
London SW1W 9SP

# 4

## Report by the Comptroller and Auditor General

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### Introduction

1. This report relates to the 2008-09 UK Consolidated Statement on the use of European Union (EU) Funds, and is the third annual statement produced by the Government. There is no statutory requirement to produce such a Consolidated Statement and it is therefore prepared on a voluntary basis, to help to detect weaknesses in controls and to promote sound management of EU funds. HM Treasury's Accounting Officer has overall responsibility for the preparation of this Statement. The arrangements for accounting for the use of EU funds are explained in the Commentary to the Statement. Funding from the EU and expenditure made from these funds are accounted for by the UK authorities who receive and include them in their audited statutory accounts. The Accounting Officers of these authorities are responsible for the recording and regularity of the underlying transactions.
2. I have audited this Statement to give my opinion on whether it presents a true and fair view and whether the underlying transactions conform to the authorities which govern them. In forming my opinion I have considered, in accordance with International Standards on Auditing, the results of specified audit procedures carried out by the auditors of the underlying statutory accounts. This report summarises the results of my audit.

### The European legislative framework

3. The Treaty establishing the European Community provides the basic legal framework for the Budget of the EU. The Budget includes a number of separate funds, including the European Agricultural Guarantee Fund (EAGF), the European Agricultural Fund for Rural Development (EAFRD), the European Regional Development Fund (ERDF) and the European Social Fund (ESF). These are governed by secondary legislation made by the Council of the EU (the Council) and the European Commission (the Commission) which has overall responsibility for implementing the budget. The Council regulations and decisions define the eligibility criteria which final beneficiaries have to meet to be entitled to EU funds. They also specify certain control processes which must be implemented by Member States. Within the Member States, national authorities are responsible for overseeing the implementation of EU funded schemes in accordance with EU legislation. This includes determining whether final beneficiaries have met the eligibility criteria before payment is made. The national authorities also have a financial reporting responsibility to the Commission.
4. If the UK authorities, in common with other Member States, fail to meet certain procedural and other requirements in EU regulations and decisions, the Commission may determine that conditions have not been met and levy a financial correction on the Member State. Where this occurs, the Commission makes a reduction in EU funding made to the Member State for expenditure on programmes. While my audit provides an opinion on the regularity of payments of EU funds by UK authorities to final beneficiaries, only the Commission is able to determine whether any financial correction is due. Any such shortfall in funding for UK expenditure is made good by the UK taxpayer. I consider that any expenditure met by the UK taxpayer in these circumstances is outside the intentions of Parliament and therefore irregular in the context of that part of my audit opinion.

5. These financial corrections are normally made some considerable time after the payments to final beneficiaries under the relevant programme. They normally result from inspections and audits by the EU authorities, sometimes as part of the formal closure of a scheme or multi-year programme. Hence, it can be several years before financial corrections are implemented. Paragraphs 28 to 33 set out the results of my audit of regularity.

## **The purpose of the Consolidated Statement**

6. The purpose of the Consolidated Statement is clearly defined in the then Economic Secretary's announcement to the House of Commons on 20 November 2006, where he stated that *"the Government intend...to prepare and lay before Parliament an annual consolidated statement on the UK's use of EU funds...which would be audited by the National Audit Office... These arrangements would enhance audit and Parliamentary scrutiny of our own use of EU funds, help detect any irregularities and thus improve financial management."* The Consolidated Statement adds transparency by providing a single perspective on how the UK is managing EU funds and the liabilities that arise as a consequence – principally the probable future financial corrections that the UK expects the Commission to impose on the UK.

## **Responsibilities for the preparation of the Consolidated Statement and audit**

7. HM Treasury's Accounting Officer has overall responsibility for the preparation of this Statement, which consolidates the EU funds accounted for by the individual central government authorities detailed at Note 2 to the Statement.

8. HM Treasury has taken steps in the production of this, the third annual Consolidated Statement, to further refine the definition of what is included in the Statement and what is not. As set out in the accounting policy in Note 1.3 to the accounts, the 2008-09 Statement now excludes transactions and balances from EU schemes where the UK authority is the final beneficiary, as these are managed by the Commission, not the UK government. The Statement should therefore only recognise transactions and balances from EU schemes where the UK government is in effect the managing authority on behalf of the EU and distributes the funds to others. This has required HM Treasury to restate some of the figures previously presented in the 2007-08 Consolidated Statement, following this refinement of its accounting policy.

9. HM Treasury has asked me to provide an audit opinion on this Consolidated Statement. My audit is designed to form a view on the truth and fairness of the financial statements and to conclude whether, in all material respects, the expenditure and funding have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them. This includes checks on whether payments are for the correct amounts and paid to eligible beneficiaries who satisfy the scheme criteria. Where the conditions are not met, I consider the element of the transaction which is not in compliance with the regulations to be 'irregular'

## **Progress in the preparation and audit of the Consolidated Statement**

10. Significant progress has been made in the preparation and audit of this annual statement since 2006. There is now a clearer sense of what funds are classed as managed by the UK Government, as opposed to being managed by the Commission. Some good progress has been made in securing improved consistency of accounting policies across the component authorities. This has been most notable in relation to provisions for future liabilities, where there is now much greater commonality in determining when to raise a provision for potential future financial corrections and when to recognise that the provisions have crystallised into actual losses to the UK Exchequer.

11. The Consolidated Statement now reflects more fully the objectives originally envisaged. Nonetheless, there are material issues at the core of producing the Statement that HM Treasury

and the UK authorities have still to resolve. I have therefore qualified my audit opinion on the 2008-09 Consolidated Statement. My comments on the potential for further improvements to the Consolidated Statement are discussed at paragraphs 34 to 38.

## **Qualified True and Fair Opinion arising from Disagreement on Consistency of Application of Accounting Policies, Disagreement on Accounting Policies for Foreign Currency Transactions and Limitations in Audit Scope**

**12.** Under International Standards on Auditing (UK & Ireland), I am required to give my opinion on whether the Consolidated Statement presents a true and fair view of the use of EU funds in the UK. I have qualified my opinion for the reasons set out below.

### **Application of Accounting Policies**

**13.** The accounting policies for EU funds are set out in HM Treasury's Financial Reporting Manual (FReM), which has been adopted by the UK government as the basis for producing its accounts. With the exception of Financial Reporting Standard 23 'The effects of changes in foreign exchange rate' (see paragraphs 15 to 18 below), authorities which received EU funding complied, in all material respects, with the FReM in producing their own financial statements and their interpretation of the guidance was within an acceptable range of professional judgement. For the purposes of this Consolidated Statement, however, accounting treatments and estimates have not always been consistent between Managing Authorities.

**14.** As a result of the inconsistent applications of accounting treatments and estimates, I have been unable to confirm that the debtors, creditors and related expenditure entries have been compiled on a consistent basis and are materially accurate.

### **Accounting Policy for foreign currency transactions**

**15.** I qualified my "true and fair" opinion on the 2008-09 financial statements of the Department for Environment, Food and Rural Affairs (DEFRA) and the Rural Payments Agency (RPA) over a disagreement about the accounting treatment for foreign exchange rate gains and losses.

**16.** Both DEFRA and the RPA are required to produce accounts in accordance with the FReM, which interprets UK General Accepted Accounting Practice for use in the public sector. The FReM requires entities to apply Financial Reporting Standard 23 'The effects of changes in foreign exchange rate' and Financial Reporting Standards 25, 26 and 29 relating to financial instruments in full from 2008-09 onwards.

**17.** The RPA has significant exposure to exchange rate risk as it pays out European Commission scheme funds (the most significant of which is the Single Payment Scheme) to English farmers in Sterling – but is reimbursed in Euros. To manage this risk, RPA uses a forward exchange contract to hedge its Single Payment Scheme-related Euro income.

**18.** I do not consider that the RPA's application of FRS 23 conformed to the Standard. In particular, the RPA did not apply the spot exchange rate on recognition of foreign currency transactions in respect of reimbursement from the Commission. The approach adopted by the RPA did not reflect the full volatility of exchange rates experienced in 2009. The effect of the RPA's treatment was to omit material gains/losses arising on retranslation of claims during the year. The full application of FRS 23 as stipulated in the Standard would have had a material impact on the valuation of the European Commission debtor, recognised foreign exchange gains in losses in scheme expenditure, and gains arising on the revaluation of the European Commission debtor. DEFRA and the RPA acknowledge that their 2008-09 accounts (and their figures included in this Consolidated Statement) did not comply in full with FRS 23.

## Limitation in Audit Scope arising from unauditable balancing figures

- 19.** The Consolidated Statement relies upon two balancing figures to complete the Balance Sheet ('Temporary UK Finding') and the Cash Flow Statement ('Receipts from the EU').
- 20.** The Consolidated Statement is unusual in that it is not drawn up from a single ledger that supports the production of a trial balance, but from a series of returns made by component authorities. The Managing Authority returns are comprised of summary EU-related financial data extracted from the ledgers which support their statutory accounts.
- 21.** Most Managing Authorities do not maintain EU-related debit and credit entries in a ledger separate from other activity. This introduces an inherent risk that the figures extracted from their accounting data are incomplete. To ensure that the Managing Authority returns balance, there is a built-in balancing figure in each one – Temporary UK Funding.
- 22. Temporary UK Funding** in the Balance Sheet is intended to represent the amount of UK funds given to Managing Authorities to finance EU Scheme activities ahead of claiming and receiving funds from the European Commission. The underlying accounts and accounting records of the UK Managing Authorities do not, however, record the level of Temporary UK Funding. It is therefore not a figure for which I can draw specific assurance from the audits of the underlying statutory accounts.
- 23.** If I could be assured that all of the other components of the Balance Sheet were materially correct, I could make the same judgement about Temporary UK Funding. I have not, however, been able to gain full assurance concerning the identification of debtor and creditor balances and related transactions between entities. I could therefore not verify the figure for Temporary UK Funding (£217,994,000 in the Balance Sheet).
- 24. Receipts from the EU** is a figure that should be easily identifiable from the underlying statutory accounting data of the Managing Authorities, but the absence of a specific ledger for EU transactions means that HM Treasury has adjusted the receipts figure to make the Cash Flow Statement work. I have no assurance that this adjustment is a valid correction and I could therefore not verify £361,182,000 of the reported Receipts from the EU (£4,687,084,000 in the Cash Flow Statement).
- 25.** I am content that, with the exception of adjustments which may have been required to the balance sheet, expenditure statement and cash flow statement as a result of the matters in paragraphs 13 to 24 above, the accounts present a true and fair view of the EU-funded activities of the UK central government.

## Qualified True and Fair Opinion on 2007-08 figures

- 26.** My audit opinion on the 2007-08 Consolidated Statement was qualified for reasons similar to, but not confined to, the reasons I have set out in respect of my opinion on the 2008-09 Statement. My opinion on the 2007-08 Statement highlighted that:

The financial statements are not based upon bookkeeping in a single ledger that supports the production of a trial balance. The process of data capture is vulnerable to the risks of inconsistencies among the UK government bodies involved.

As a result, there is uncertainty over the completeness and reliability of data concerning transactions and balances relating to the use of EU funds in the UK. In my opinion, accounting policies have not been consistently applied across the component entities in relation to the identification of debtor and creditor balances and related transactions between entities, the treatment of EU funding, the compilation of cash balances and the recognition of provisions for financial corrections.

Accordingly, these consolidated financial statements contain material misstatement, the quantification of which is dependent on professional judgement in the interpretation of those policies. As a direct consequence of the uncertainties surrounding the reliability of the balance sheet, I could not verify the figures for Temporary UK Funding (£182,839,000 in the balance sheet) or Other Receipts Direct from the EU (£108,530,000 in the cash flow statement).

**27.** The qualification of my opinion due to the inconsistent application of accounting policies was broader in 2007-08, since it also included the treatment of EU funding; the compilation of cash balances; and provisions for financial corrections. These qualification matters are unresolved, in that HM Treasury's subsequent restatements of the 2007-08 figures do not remove my concerns about the comparative figures - which are also disclosed as part of the 2008-09 Statement – being materially misstated. I am required by International Standard on Auditing (ISA) 710 to draw this matter to attention because it limits the understanding that can be gained by comparing the figures presented for the financial years 2008-09 and 2007-08.

### **Regularity of payments to final beneficiaries**

**28.** My audit included the examination, on a test basis, of evidence that payments by UK government bodies to final beneficiaries in 2008-09, in all material respects, conformed with the authorities which govern them. As a result of the audit, I have been able to confirm that payments generally complied with these requirements. I noted a number of procedural and administrative matters which, whilst not providing evidence that payments to final beneficiaries were subject to material irregularity, give rise to the risk of the Commission imposing financial corrections in the future if it believes that its scheme regulations have not been followed.

### **Qualified Regularity Opinion**

**29.** Where the Commission determines that its scheme regulations have not been complied with, it may propose a financial correction. The Commission makes an initial assessment of the consequences of the weaknesses found. It then discusses its findings with the UK authorities before deciding on the actual level of the correction to be applied. The correction is then made by restricting the level of future funding made available to the UK, with the resulting cost being met by the UK taxpayer.

**30.** When the UK authorities become aware that a financial correction may be necessary, either from their own knowledge or from notification by the Commission, they provide for these amounts in their statutory accounts. Provisions for potential financial corrections of £601 million have been included in the 2008-09 Consolidated Statement. These provisions, relating predominantly to likely corrections by the Commission relating to expenditure and control systems up to 31 March 2009, represent a probable outflow of economic benefit but I do not consider these transactions to be irregular at that point. Once the Commission has determined

the final correction, this represents a crystallised loss to UK funds which I then consider to be irregular.

**31.** During the financial year 2008-09, financial corrections relating to prior years totalling £137 million crystallised (**Table 1**), as a result of decisions confirmed by the Commission. Most of the £137 million disallowance that was confirmed in 2008-09 was incurred by DEFRA. I consider that these amounts are material in the context of the Consolidated Statement for 2008-09. I have qualified my regularity opinion on the Statement on the grounds that the loss to UK funds from these corrections falls outside of Parliament’s intentions in relation to the proper administration of European funding.

**32.** A further £261 million of corrections has crystallised since the end of 2008-09 and prior to the Accounting Officer signing the Consolidated Statement (**Table 2**). Although these decisions occurred after the balance sheet date, they relate to conditions existing at that date and I consider these losses are also irregular in respect of my opinion on the Consolidated Statement for 2008-09. HM Treasury has provided further information on these corrections in the Commentary on the Consolidated Statement. The total of crystallised disallowances in 2008-09 and since that relate to events up to 31 March 2009 is therefore £398 million.

**33.** I also qualified my “regularity” opinion on the 2008-09 and 2009-10 DEFRA accounts because of the payment of material disallowance penalties imposed by the Commission.

**Table 1: UK financial corrections confirmed by the Commission in 2008-09**

Department	Amount £m	Funds affected
Department for Environment, Food and Rural Affairs	92	Agriculture and Natural Resources
Department for Communities and Local Government	24	European Regional Development Fund
Wales	12	European Regional Development Fund
Scotland	9	European Regional Development Fund
	<b>137</b>	

**Table 2: UK financial corrections confirmed by the Commission since 31 March 2009**

Department	Amount £m	Funds affected
Department for Environment, Food and Rural Affairs	161	Agriculture and Natural Resources (Single Payment Scheme)
Department for Environment, Food and Rural Affairs	32	Agriculture and Natural Resources (Other)
Northern Ireland	43 <sup>1</sup>	Agriculture and Natural Resources (Single Payment Scheme)
Northern Ireland	25	European Regional Development Fund
	<b>261</b>	

## Improving the Consolidated Statement

**34.** This Statement represents the third annual Consolidated Statement of the use of EU funds in the UK, compiled from pre-existing audited accounts for the 2008-09 financial year. In producing the Statement, HM Treasury has again made a number of significant adjustments to the data received from UK authorities.

**35.** HM Treasury continues to improve its processes for capturing data and preparing the Consolidated Statement and is working closely with the UK authorities to address the data quality and consistency issues highlighted in this report. In partnership with those authorities,

<sup>1</sup> Plus an additional £11 million accounted for in DEFRA’s Resource Accounts, dating back to SPS 2005, included in DEFRA figures shown.

HM Treasury is also developing its accounting guidance to help to improve the consistency of reporting of EU funding transactions across Central Government. This work should lead to continued improvements for future years.

**36.** The first two annual Statements have already led to increased scrutiny of the use of EU funds in the UK. The annual publication of this Statement will help to ensure that this continues. The audit of the Consolidated Statement should help to detect weaknesses in the UK's management of EU funds so that they may be addressed and so that management control systems may be improved.

**37.** The preparation of the 2008-09 Consolidated Statement has been subject to delay. Competing priorities meant that the Statement was not ready for certification and laying by the parliamentary summer recess, which led to further unavoidable post balance sheet events. Material financial corrections either proposed or confirmed by the Commission after the certification of the statutory accounts of Managing Authorities have been a major factor. When these announcements occur, they are significant post-balance sheet events that require adjustments to be made to the Consolidated Statement. In such circumstances, HM Treasury's Accounting Officer needs to have processes in place for the Accounting Officers of Managing Authorities to give their consent for HM Treasury to adjust figures that have been presented in the underlying statutory accounts and in the data returns to HM Treasury for the Statement.

**38.** The situation described gives rise to a risk of HM Treasury reporting matters to Parliament in the Consolidated Statement before the Managing Authorities do – for example, recognising disallowance provisions in the Statement that a Managing Authority would not report before publishing its statutory accounts for the following financial year. Securing agreement on the treatment of post-balance sheet events for the 2008-09 Consolidated Statement was not possible until the 2009-10 accounts of a key Managing Authority were completed and certified in August 2010. In my view, the resolution of this issue, enabling the HM Treasury Accounting Officer to make material adjustments to the figures within the Statement, is key to securing timelier completion and publication of the Consolidated Statement.

## **Conclusion**

**39.** My report has identified a number of significant accounting and other issues which need to be addressed in order to ensure that the annual Consolidated Statement represents a true and fair view of the use of EU funds in the UK. HM Treasury has made further incremental improvements to its processes for preparing the annual Consolidated Statement and, with the agreement of the other UK authorities, is addressing the remaining issues through further work to align the detailed accounting policies and related accounting treatments across government.

**40.** The most important gain from the production of the Consolidated Statement has been the overview that it presents of the level of financial corrections imposed by the Commission. The confirmed losses totalling £398 million set out in this report and the provisions for further losses of £601 million detailed in Note 15 to the Statement represent huge past costs and potential future costs to the taxpayer of implementing EU schemes in the UK. The Agriculture and Natural Resources schemes currently account for the bulk of the losses and provisions. In October 2009, I published "A Second Progress Update on the Administration of the Single Payment Scheme by the Rural Payments Agency" (HC 880, 2008-2009). That report set out my recommendations for addressing the major underlying problems leading to the costly administration of the scheme and the mounting financial corrections proposed by the Commission.

**41.** Note 15 to this 2008-09 Consolidated Statement shows that there is also a total of £221 million of provisions for other EU schemes – principally the European Regional Development Fund. This represents an increase of £113 million on the equivalent figure at 31 March 2008

and indicates that the issue of needing to improve controls over EU funds is one that extends beyond the administration of the Single Payment Scheme.

Amyas CE Morse  
Comptroller and Auditor General  
14 January 2011

National Audit Office  
157-197 Buckingham Palace Road  
Victoria  
London SW1W 9SP

# 5

## Financial accounts

### Expenditure Account

For the year ended 31 March 2009

	Note	2008-09 £000	2007-08 Restated (Note 6) £000
Gross expenditure on EU supported projects	2	4,178,769	4,365,853
Provisions created in year	3	(442,112)	(108,280)
Provisions released in year	3	154,069	43,198
Expenditure net of provisions		3,890,726	4,300,771
Foreign exchange gains/(losses)	3, 5	(41,167)	24,400
Withdrawn from EU claim	3	(40,929)	(31,437)
Net expenditure reimbursable by the EU	3	<b>3,808,630</b>	<b>4,293,734</b>

### Explanatory Note

The Expenditure Statement shows the EU funded element of amounts paid out by UK Central Government bodies on projects supported wholly or partially by the EU on which the UK anticipates EU funding at the point the payment is made.

Gross expenditure on EU supported projects is recognised in the period in which it becomes payable by UK Central Government to the recipient under the rules of the relevant scheme. The amount shown in the Account represents the amount paid and payable in sterling during the period to beneficiaries.

Net expenditure represents the amount receivable from the EU in respect of amounts paid or payable by the UK on EU supported projects, after taking account of provisions for disallowances and foreign exchange gains or losses.

## Balance Sheet

As at 31 March 2009

		2008-09	2007-08
	Note	£000	Restated (Note 16) £000
<b>Assets</b>			
Advances to beneficiaries	7	203,439	230,462
EU funds receivable	8	2,258,505	2,378,620
Other assets	9	20,025	8,833
		<b>2,481,969</b>	<b>2,617,915</b>
<b>Liabilities</b>			
EU funds paid on account	10	1,231,811	866,960
Amounts payable to beneficiaries	11	1,009,718	1,483,802
Repayable to EU	12	13,455	36,414
Provision for disallowances	15	600,527	454,140
Other liabilities	13	8,991	-
		<b>2,864,502</b>	<b>2,841,316</b>
<b>Net Assets/(Liabilities)</b>		<b>(382,533)</b>	<b>(223,401)</b>
Financed By			
Temporary UK funding	14	217,994	230,739
Less Possible permanent UK funding: Disallowances Provision	15	<b>(600,527)</b>	<b>(454,140)</b>
		<b>(382,533)</b>	<b>(223,401)</b>



Sir Nicholas Macpherson  
Permanent Secretary HM Treasury  
12 January 2011

### Explanatory Note

The Consolidated Statement shows the flow of funds from the EU to the UK and from UK Government to beneficiaries. The balance sheet shows those assets and liabilities that stem from such cash flows, e.g. where the UK has paid a claim from a beneficiary and is awaiting reimbursement from the EU. The disallowances provision relates to amounts paid out by the UK for which it believes it probable that the EU will apply financial corrections and not fully reimburse the UK.

Temporary UK funding is the working capital provided by the UK Exchequer that will in due course be funded by the EU. Possible permanent UK funding is the element of temporary UK funding for which it is probable that the EU will apply financial corrections. Possible permanent UK Funding represents the funding that will be met by the UK Exchequer if provisions in respect of EU disallowances crystallise. Possible permanent UK funding will always equal provisions.

As the Consolidated Statement shows funding flows there are no reserves, as there is no trading gain or loss, and there is no taxpayers' equity.

## Cash flow statement

For the year ended 31 March 2009

		2008-09	2007-08
	Note	£000	Restated £000
<b>Gross EU expenditure</b>	2	(4,178,769)	(4,365,853)
Movement in working capital			
(Increase)/decrease in advances to beneficiaries		27,023	60,891
Increase/(decrease) in amounts payable to beneficiaries		(474,084)	(338,729)
Increase/(decrease) in amounts repayable to the EU		(22,959)	(58,112)
<b>Net cash outflows</b>		<b>(4,648,789)</b>	<b>(4,701,803)</b>
Receipts from EU		4,687,084	5,574,085
Increase/(decrease) in temporary UK funding	14	(12,745)	(797,095)
Permanent UK funding			
Realised foreign exchange gains	5a	(25,550)	(75,187)
<b>Net cash inflows</b>		<b>4,648,789</b>	<b>4,701,803</b>

### Explanatory Note

The cash flow statement balances the cash outflows from the UK government with cash inflows from the EU.

The cash outflows only include that cash paid out on which the UK anticipates EU receipts and is therefore shown net of disallowance provisions and foreign exchange losses.

## Notes to the Statement

### 1. Accounting policies

1.1 The principal accounting policies adopted in the preparation of the Consolidated Statement (the Statement) are set out below.

#### *Basis of preparation*

1.2 The Statement has been prepared so as to give a true and fair view by consolidating the relevant transactions and balances as recorded by the Managing Authorities in their financial statements prepared in accordance with the Financial Reporting Manual (FRoM). The Statement is prepared under the historical cost convention.

#### *Boundary of the Statement*

1.3 The Statement shows the expenditure incurred by the UK on EU sponsored projects and the income due from the EU in respect of such projects, where the UK acts as an agent in distributing funds in respect of EU supported projects and programmes to the final beneficiary. The boundary of the Statement excludes:

- amounts received from the EU where UK central government is the final beneficiary;
- income and expenditure stemming from commercial contracts awarded to UK central government bodies by the EU;
- twinning funds held by UK central government bodies for the benefit of other member states; and
- amounts recorded in the Expenditure Statement as withdrawn from EU claim or subject to a disallowance, which fall outside the boundary of this Statement as the expenditure will be funded by the UK Exchequer. Where the EU propose a financial correction against the UK, the UK will have submitted a claim in respect of the project subject to the potential correction. As such, the proposed correction will be recognised as a contingent liability or a provision as per the accounting policy in this Statement. Where possible the UK Exchequer will endeavour to recover withdrawn or disallowed expenditure from the final beneficiary but the recovery of such amounts and any outstanding balances will not be recorded in the Statement as they fall outside the boundary.

#### *Expenditure recognition*

1.4 Gross expenditure on EU supported projects is recognised in the period in which it becomes payable by UK Central Government to the recipient under the rules of the relevant scheme. The amount shown in these accounts represents the amount paid and payable in sterling during the period to bodies outside the Central Government boundary. Net EU Expenditure represents the amount receivable from the EU (converted into sterling after disallowances and foreign exchange gains or losses) in respect of amounts paid or payable by the UK on EU supported projects.

#### *Income Recognition*

1.5 Income is recognised by the UK for funding it expects to receive from the EU in respect of expenditure incurred on EU supported projects. Income has not been separately recorded in the Statement as it will always equal the expenditure incurred. Where provisions for disallowances have been made they reduce the level of expenditure reclaimable from the EU and thus the level of EU income.

### *Foreign currency translation*

**1.6** The Commission makes payments in Euros, with the Managing Authority recognising the receivable in Sterling in line with the requirements of FRS23 The Effects of Changes in Foreign Exchange Rates. Foreign exchange gains and losses are realised where there are variations in exchange rates between the date EU income is recognised by the Managing Authority and the date payment is received from the EU. Such gains and losses are recognised in the Expenditure Statement. Unrealised gains and losses arising from the revaluation of assets and liabilities at the exchange rate current at the balance sheet date are reported in the Statement of Recognised Gains and Losses. Any hedging mechanisms used to mitigate the impact of foreign exchange losses are not included in this statement as they do not impact on the amounts paid out on EU projects or the funding provided by the EU.

### *Disallowances provision and contingent liabilities*

**1.7** Probable disallowances arising from financial corrections are recognised, and contingent liabilities disclosed, in accordance with the requirements of Financial Reporting Standard (FRS) 12, Provisions, Contingent Liabilities and Assets. A provision is recognised where there is a past event – for example an ineligible payment or a failure to comply with the regulations governing a scheme – which will probably lead to the EU disallowing expenditure and not reimbursing the UK. Managing Authorities are responsible for estimating the value of any provisions required. Contingent liabilities are disclosed where there is a past event but it is not probable that it will lead to the EU disallowing expenditure.

### *EU Funding Withdrawn*

**1.8** Managing Authorities can apply self corrections which result in amounts being withdrawn from an EU claim. Self corrections occur where, due to an irregularity in a claim, the Managing Authority chooses not to claim the expenditure from the EU. This is a member state function and such self corrections are not provisions for the purposes of this statement. The withdrawal of the claim removes the relevant amount from the boundary of this statement through the Expenditure Account as the self correction is funded by the UK Exchequer pending recovery from the UK beneficiary.

### *Restatements*

**1.9** There have been a number of reasons for the restating of balances for 2007-08 within this 2008-09 Consolidated Statement. First, the accounting policy covering the accounting boundary has been modified to exclude amounts related to activities where the government is the final beneficiary of the funds from the EU. This has resulted in a restatement of comparatives for 2007-08 where the expenditure has decreased by £20.7 million. Second, a change to the format of the Expenditure Account has meant that released provisions have resulted in an increase in the Net Expenditure of £43.2 million. Finally, there have been restatements by various managing authorities as they have identified corrections and adjustments to prior year figures. More detail on the impact on the Expenditure Accounts is disclosed in Note 6 and the impact on the Balance Sheet in Note 16.

## 2. Analysis of Gross expenditure by UK Central Government Departments and Devolved Administrations on EU supported projects

	Agricultural Funding	Financial Instrument for Fisheries Guidance	European Social Fund	European Regional Development Fund	European Guidance and Guarantee Fund	Other (Note 4)	Total	2007-08 Restated
	£000	£000	£000	£000	£000	£000	£000	£000
<b>England</b>								
Asset Recovery Agency	-	-	-	-	-	-	-	83
Communities and Local Government	-	-	-	383,167	-	-	383,167	476,045
Culture, Media and Sport	-	-	-	-	-	-	-	4,133
Environment, Food and Rural Affairs	1,962,980	6,101	-	-	8,958	9,336	1,987,375	1,846,383
Forestry Commission	12,345	-	-	-	-	-	12,345	12,480
Home Office	-	-	-	-	-	19,328	19,328	7,200
Innovation, University and Skills	-	-	166,416	-	-	-	166,416	301,641
Transport	-	-	-	-	-	24,603	24,603	23,804
Work and Pensions	-	-	109,208	-	-	-	109,208	282,098
<b>Scotland</b>								
Scottish Executive	505,372	6,637	39,114	64,100	-	-	615,223	643,390
<b>Wales</b>								
Welsh Assembly Government	273,869	2,169	88,744	117,941	14,132	-	496,855	463,792
<b>Northern Ireland</b>								
Northern Ireland Executive	275,443	3,856	17,275	45,377	10,185	12,113	364,249	304,804
<b>Gross expenditure</b>	<b>3,030,009</b>	<b>18,763</b>	<b>420,757</b>	<b>610,585</b>	<b>33,275</b>	<b>65,380</b>	<b>4,178,769</b>	<b>4,365,853</b>

### 3. Analysis of Net expenditure by UK Central Government Departments and Devolved Administrations on EU supported projects

	Agricultural Funding	Financial Instrument for Fisheries Guidance	European Social Fund	European Regional Development Fund	European Guidance and Guarantee Fund	Other	Total	2007-08 Restated
	£000	£000	£000	£000	£000	(Note 4) £000	£000	£000
<b>Gross expenditure in the United Kingdom</b>	<b>3,030,009</b>	<b>18,763</b>	<b>420,757</b>	<b>610,585</b>	<b>33,275</b>	<b>65,380</b>	<b>4,178,769</b>	<b>4,365,853</b>
Communities and Local Government	-	-	-	(120,017)	-	-	(120,017)	(92,715)
Environment, Food and Rural Affairs	(221,668)	-	-	-	-	-	(221,668)	(4,423)
Home Office	-	-	-	-	-	(5,427)	(5,427)	(642)
Scottish Executive	-	-	(16,707)	(2,293)	-	-	(19,000)	(10,500)
Northern Ireland Executive	(51,000)	-	-	(25,000)	-	-	(76,000)	-
<b>Total disallowances provided for</b>	<b>(272,668)</b>	<b>-</b>	<b>(16,707)</b>	<b>(147,310)</b>	<b>-</b>	<b>(5,427)</b>	<b>(442,112)</b>	<b>(108,280)</b>
Communities and Local Government	-	-	-	55,827	-	-	55,827	-
Environment, Food and Rural Affairs	92,631	-	-	-	-	-	92,631	27,400
Home Office	-	-	-	-	-	3,045	3,045	-
Scottish Executive	-	-	-	2,566	-	-	2,566	8,200
Welsh Assembly Government	-	-	-	-	-	-	-	7,598
<b>Total disallowances released</b>	<b>92,631</b>	<b>-</b>	<b>-</b>	<b>58,393</b>	<b>-</b>	<b>3,045</b>	<b>154,069</b>	<b>43,198</b>
Communities and Local Government	-	-	-	(4,020)	-	-	(4,020)	15,988
Environment, Food and Rural Affairs	(40,581)	-	-	-	-	-	(40,581)	9,416
Transport	-	-	-	-	-	-	-	69
Work and Pensions	-	-	1,743	-	-	-	1,743	1,551
Welsh Assembly Government	-	1	-	1,481	-	-	1,482	(4,077)
Northern Ireland Executive	-	720	(4,796)	2,168	1,189	928	209	1,453
<b>Total foreign exchange gains/(losses)</b>	<b>(40,581)</b>	<b>721</b>	<b>(3,053)</b>	<b>(371)</b>	<b>1,189</b>	<b>928</b>	<b>(41,167)</b>	<b>24,400</b>
Communities and Local Government	-	-	-	-	-	-	-	(11,204)
Forestry Commission	(168)	-	-	-	-	-	(168)	(195)
Transport	-	-	-	-	-	-	-	(8)
Work and Pensions	-	-	(40,761)	-	-	-	(40,761)	(16,290)
Northern Ireland Executive	-	-	-	-	-	-	-	(3,740)
<b>Total withdrawn from EU claim</b>	<b>(168)</b>	<b>-</b>	<b>(40,761)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(40,929)</b>	<b>(31,437)</b>
<b>Net expenditure reimbursable by EU</b>	<b>2,809,223</b>	<b>19,484</b>	<b>360,236</b>	<b>521,297</b>	<b>34,464</b>	<b>63,926</b>	<b>3,808,630</b>	<b>4,293,734</b>

## 4. Other Projects

The following projects are included in the 'Other' category in Note 2.

Department or Devolved Administration	Project	2008-09 £000	2007-08 Restated £000
Culture, Media and Sport	Director General Research Framework		588
	Technology Projects		269
Environment, Food and Rural Affairs	Transmissible Spongiform Encephalopathy (TSE) Monitoring and Bovine Spongiform Encephalopathy (BSE) Eradication	3,560	13,066
	Scrapie Eradication	600	1,783
	EU Aid	30	73
	Bee Health	83	
	Other Fund disease	794	
	European Fisheries Fund	1,247	
	EU Data Collection	3,022	41
Home Office	EU Solidarity Mechanism	19,328	7,200
Innovation, Universities and Skills (now Department for Business Innovation and Skills)	Science Programmes		206
	Marie Curie Actions		243
	EURATools		16
Asset Recovery Agency	Camden Asset Recovery Inter-Agency Network		83
Transport	Trans European Network	24,603	14,075
Northern Ireland Executive	Trans European Network	12,113	-
<b>Total</b>		<b>65,380</b>	<b>37,643</b>

## 5. Analysis of foreign exchange gains and losses

	2008-09 £000	2007-08 £000
<b>(a) realised gains / (losses)</b>		
Environment, Food and Rural Affairs	(28,435)	9,416
Communities and Local Government	18,222	27,352
Work and Pensions	36,216	35,859
Northern Ireland Executive	(453)	2,491
Transport	-	69
	<b>25,550</b>	<b>75,187</b>
<b>(b) unrealised gains / (losses)</b>		
Environment, Food and Rural Affairs	(12,146)	-
Communities and Local Government	(22,242)	(11,364)
Work and Pensions	(34,473)	(34,308)
Welsh Assembly Government	1,482	(4,077)
Northern Ireland Executive	662	(1,038)
	<b>(66,717)</b>	<b>(50,787)</b>
<b>Total foreign exchange rate gains / (losses)</b>	<b>(41,167)</b>	<b>24,400</b>

## 6. Expenditure Account – restated amounts

	Original £000	Restated £000	Difference £000
Gross expenditure incurred by the Ministry of Justice, Government Equality Office and The National Archives determined to be outside the scope of the Statement Release of provisions reported in Note 12a but omitted from the Expenditure Account	20,717	-	(20,717)
Gross expenditure incurred by the Department for Innovation, Universities and Skills – correction of understatement	296,587	301,641	5,054
Other expenditure	3,948,895	3,948,895	-
<b>Net expenditure reimbursable by EU</b>	<b>4,266,199</b>	<b>4,293,734</b>	<b>27,535</b>

## 7. Advances to beneficiaries

These are amounts paid out by the UK to non Central Government bodies responsible for delivering EU supported programmes and projects in advance of claims.

	2008-09 £000	2007-08 Restated £000
Communities and Local Government	125,430	-
Innovation, Universities and Skills	36,366	72,267
Environment, Food and Rural Affairs	11,570	26,835
Work and Pensions	27,133	88,237
Scottish Executive	382	21,603
Welsh Assembly Government	-	21,345
Northern Ireland Executive	2,558	175
<b>Total</b>	<b>203,439</b>	<b>230,462</b>

## 8. Analysis of EU funds receivable

These are amounts reimbursable by the EU in respect of expenditure incurred by the UK following the receipt of claims from beneficiaries.

	2008-09 £000	2007-08 Restated £000
Communities and Local Government	397,812	356,366
Innovation, Universities and Skills	99,445	80,078
Environment, Food and Rural Affairs	894,416	1,044,708
Forestry Commission	549	1,359
Home Office	9,653	4,644
Transport	-	20
Work and Pensions	461,918	606,693
Scottish Executive	131,542	113,707
Welsh Assembly Government	96,870	30,661
Northern Ireland Executive	166,300	140,384
<b>Total</b>	<b>2,258,505</b>	<b>2,378,620</b>

## 9. Other assets

	2008-09 £000	2007-08 Restated £000
Welsh Assembly Government	20,025	8,833
	<b>20,025</b>	<b>8,833</b>

## 10. EU funds paid on account

These are amounts paid by the EU in advance of formal claims from the UK. The contractual terms of EU funding for projects and programmes often provide for such payments on account to allow projects to proceed.

	2008-09	2007-08
	£000	Restated £000
Communities and Local Government	496,428	346,972
Innovation, Universities and Skills	16,637	53,422
Environment, Food and Rural Affairs	107,084	40,075
Home Office	9,091	2,509
Work and Pensions	524,999	375,825
Scottish Executive	15,100	42,898
Welsh Assembly Government	53,454	2,875
Northern Ireland Executive	9,018	2,384
<b>Total</b>	<b>1,231,811</b>	<b>866,960</b>

## 11. Amounts payable to beneficiaries

These are amounts payable to organisations and individuals in respect of EU programmes and projects and are recognised when valid claims are approved but not yet settled.

	2008-09	2007-08
	£000	Restated £000
Communities and Local Government	23,635	122,963
Innovation, Universities and Skills	16,633	56,165
Environment, Food and Rural Affairs	547,928	754,671
Home Office	4,281	-
Transport	7,499	151
Work and Pensions	247,845	400,518
Scottish Executive	39,988	50,143
Welsh Assembly Government	92,419	68,372
Northern Ireland Executive	29,490	30,819
<b>Total</b>	<b>1,009,718</b>	<b>1,483,802</b>

## 12. Amounts repayable to EU

These include amounts to be repaid to the EU resulting from direct action taken by the UK to identify overpayments on programmes.

	2008-09	2007-08
	£000	Restated £000
Innovation, Universities and Skills	-	121
Forestry Commission	7	2
Work and Pensions	-	34,571
Welsh Assembly Government	13,448	1,720
<b>Total</b>	<b>13,455</b>	<b>36,414</b>

## 13. Other liabilities

	2008-09	2007-08
	£000	£000
Welsh Assembly Government	2,311	-
Northern Ireland Executive	6,680	-
	<b>8,991</b>	<b>-</b>

## 14. Analysis of temporary UK funding

	2008-09	2007-08	Movement
	£000	Restated £000	£000
Communities and Local Government	(3,179)	113,569	(116,748)
Innovation, Universities and Skills	(102,541)	(42,637)	(59,904)
Environment, Food and Rural Affairs	(250,974)	(276,797)	25,823
Forestry Commission	(542)	(1,357)	815
Home Office	3,719	(2,135)	5,854
Transport	7,499	131	7,368
Work and Pensions	283,793	115,984	167,809
Scottish Executive	(76,836)	(42,269)	(34,567)
Welsh Assembly Government	44,737	12,128	32,609
Northern Ireland Executive	(123,670)	(107,356)	(16,314)
	<b>(217,994)</b>	<b>(230,739)</b>	<b>12,745</b>

## 15. Provision – future financial corrections (disallowances)

The EU may disallow claims for reimbursement by imposing financial corrections where the conditions of the relevant scheme have not been met. In such circumstances the EU reduces the amount paid to the UK.

	2008-09	2007-08
	£000	Restated £000
As at 1 April 2008 (restated)	454,140	401,067
Created during the year	442,112	120,197
Released in year	(154,069)	(43,198)
Utilised	(141,656)	(23,926)
<b>As at 31 March 2009</b>	<b>600,527</b>	<b>454,140</b>

### 15a Analysis of provisions for disallowances

	2008-09	2007-08
	£000	Restated £000
<b>Department or Devolved Administration</b>		
Communities and Local Government	113,365	72,915
Environment, Food and Rural Affairs	379,209	345,831
Home Office	1,988	642
Scottish Executive	29,500	22,370
Welsh Assembly Government	-	11,917
Northern Ireland Executive	76,465	465
<b>Totals</b>	<b>600,527</b>	<b>454,140</b>

**15.1** Establishing the boundary between EU and UK funded expenditure can be a difficult process. The UK Exchequer provides funding to projects in anticipation of such projects being fully funded by the EU. However, failure to meet certain EU rules attaching to EU funding can result in the EU disallowing claims. Although it is standard procedure to recover grants that are found ineligible, this is not always possible and can lead to the UK Exchequer bearing the full or partial cost of a project to which a disallowance has been applied.

**15.2** The disallowance provisions consolidated in this Statement include those recognised by the relevant Departments and Devolved Administrations in their own financial statements. The amounts include adjustments made after the end of the reporting period and included in Departments' financial statements for 2009-10 as set out in Note 18.

## Communities and Local Government

**15.3** Following consideration of potential ineligible grant payments in respect of European Regional Development Fund (ERDF) programme expenditure, CLG have reported additional net new provisions amounting to £64 million. After allowing for the use of existing provisions, there was a net increase of £40 million in the balance at the year end. This included a post balance sheet adjustment of £39 million (see Note 18).

## Environment, Food and Rural Affairs

**15.4** The Department for Environment, Food and Rural Affairs reported provisions for 2008-09 amounting to £250 million in financial statements, relating to CAP funding (£246 million) and Financial Instrument for Fisheries Guidance (FIG) funding (£4 million). Following consideration of likely future disallowances, additional net provisions amounting to £129 million were made in the Department's 2009-10 financial statements. These have been reflected in this Statement as a post balance-sheet adjustment. After allowing for the use of existing provisions, there was a net increase of £34 million in the position at 31 March 2009 in the EU Statement.

## Home Office

**15.5** The Home Office provisions, which amounted to £2 million, relate to three funds forming part of the European Solidarity Mechanism, the European Refugee Fund, the European Integration Fund, and the European Returns Fund. Following a comprehensive review of potential liabilities, the Department made new provisions amounting to £2.4 million (net) in 2008-09.

## Scottish Executive

**15.6** The Scottish Executive made new provisions of £16.7 million (ESF) and £2.3 million (ERDF). The provisions relate to ongoing Commission and European Court of Auditor audit missions which have identified potential irregularities in the delivery of the Structural Fund programmes. Proposed disallowances are subject to the contradictory procedure. Council Regulation 1083/2006 Article 100 provides further details.

## Northern Ireland Executive

**15.7** The Northern Ireland Department of Agriculture and Rural Development reported in its financial statements for 2008-09 that the EU was proposing financial corrections in respect of 2004, 2005 and 2006. The disallowance was put on hold pending completion of the conciliation process. The Commission has since announced that the disallowance for those years was £31 million and that a further £31 million disallowances are proposed for 2007 and 2008. As some £11 million had already been provided, the Department expensed £51 million in its financial statements for 2009-10, and a corresponding provision has been recognised in this Statement.

**15.8** The Northern Ireland Department of Finance and Personnel disclosed no contingent liabilities relating to EU funding in its financial statements for 2008-09. Since those accounts were issued, the Executive has accepted European Commission proposals to disallow £25 million expenditure in relation to the Northern Ireland Single Programme Document and the Special Support Programme for Peace and Reconciliation in Northern Ireland and the Border Counties of Ireland. In the Department's financial statements for 2009-10, this amount has been recorded as an expense, with £9.9 million paid to the EU. This amount paid was the total financial corrections less £15.1 million that had been due from the Commission in respect of the PEACE and NI Single Programmes.

## 16. Balance Sheet: restated amounts

	Original £000	Restated £000	Difference £000
Advances to beneficiaries – correction of overstatement and elimination of intra-government balances	242,591	230,462	(12,129)
EU funds receivable – elimination of intra-government balances and restatement due to revaluation at year end exchange rate	2,412,861	2,378,620	(34,241)
Other assets – correction of omission	-	8,833	8,833
Total assets	2,655,452	2,617,915	(37,537)
EU funds paid on account – mainly correction of amounts paid on account	(946,027)	(866,960)	79,067
Amounts payable to beneficiaries – elimination of intra-government balances, correction of overstatement and revaluation at year end exchange rate	(1,490,293)	(1,483,802)	6,491
Repayable to EU –restatement of amounts previously netted off asset balances and reclassification of creditor as a provision	(36,293)	(36,414)	(121)
Provision for disallowances – adjustment reflects use of provision in 2007-08 which was not reflected in the Statement and reclassification of creditor as a provision	(441,757)	(454,140)	(12,383)
Total liabilities	(2,914,370)	(2,841,316)	73,054
Net liabilities	(258,918)	(223,401)	35,517
Financed by			
Temporary UK funding	(182,839)	(230,739)	(47,900)
Disallowances provision	441,757	454,140	12,383
	258,918	223,401	(35,517)

## 17. Contingent Liabilities

**17.1** Contingent liabilities are disclosed following the requirements of Financial Reporting Standard 12. The disclosures below reflect those disclosed in the resource accounts of the relevant department and devolved administration, updated as necessary for subsequent developments.

### Communities and Local Government

**17.2** The Department reported contingent liabilities totalling £215 million in respect of the 2000-06 European Regional Development Fund programme in its financial statements for 2008-09. It subsequently carried out a full review of the programme and, after making provision for potential disallowances, it has reduced contingent liabilities to £36 million.

### Environment, Food and Rural Affairs

**17.3** DEFRA is in ongoing discussions with the Commission regarding perceived non-compliance with EAFRD and EAGF regulations. Any future disallowance stemming from these discussions will depend on the assessed severity of any breach and on subsequent clarification negotiations with the Commission in accordance its clearance accounts procedures. The Department has made full provision for potential disallowances and is currently reporting no contingent liabilities.

### Work and Pensions

**17.4** DWP has a potential liability in respect of ineligible claims for ESF programmes operated during 2000-06 as a result of adverse opinions on the closure statements produced by the ESF Audit Authority. The Department's accounts reported an estimated liability of £38 million and its latest estimate of the potential liability is £35 million.

## Scottish Executive

**17.5** Closure of the European Structural Fund Programmes may result in the reduction in the funds recoverable from the European Commission, the financial effects of which are unquantifiable.

Possible disallowance arising from Commission audits of agricultural funding for the period 2005-07. The disallowance is not quantifiable.

## 18. Post balance sheet events

**18.1** The Statement was authorised for issue by the Accounting Officer on 12 January 2011.

**18.2** The Statement has been adjusted to take account of events after the end of the reporting period affecting the recovery of income from the European Commission. The principal adjustments include additional net provisions of £129 million for the Department for Environment, Food and Rural Affairs, £76 million for the Northern Ireland Executive and £39 million for Communities and Local Government. These additional provisions were reflected in the organisations' financial statements for 2009-10.



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If you require this information in another language, format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

Tel: 020 7270 4558

Fax: 020 7270 4861

E-mail: [public.enquiries@hm-treasury.gov.uk](mailto:public.enquiries@hm-treasury.gov.uk)

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