

28 September 2006

Screening report

Turkey

Chapter 32 – Financial control

Date of screening meetings:

Explanatory meeting: 18 May 2006

Bilateral meeting: 30 June 2006

I. CHAPTER CONTENT

This chapter contains four main policy areas, namely public internal financial control (PIFC), external audit (EA), the protection of the EU's financial interests and the protection of the Euro against counterfeiting.

With regard to the first two areas, there is no Community legislation requiring transposition into national law. Rather, the screening concerns the commitment of the candidate country to adopt international control and internal audit standards and EU best practices. For this purpose, the candidate country should discuss with the Commission and adopt a PIFC Policy Paper with a short and long term action plan having realistic deadlines.

PIFC is a comprehensive concept to support the candidate country in upgrading its internal control systems. PIFC and EA essentially relate to the entire public budget, in particular central government income and expenditure, including foreign funds. However, the more specific rules for managing and controlling EU funds are treated under the relevant other accession negotiation chapters.

The PIFC concept is based on three principles, 1) managerial accountability carried by sound financial management and control (FMC) systems, 2) decentralised and functionally independent internal audit (IA) and 3) centralised harmonisation of the FMC and IA systems.

Regarding **external audit**, the candidate country is expected to apply the norms defined by the International Organisation of Supreme Audit Institutions – INTOSAI, in particular its Lima Declaration, which foresees supreme audit institutions that are functionally, institutionally and financially independent.

The other relevant policy area under this chapter concerns the **protection of EU financial interests**. First, it comprises operational cooperation of Member States, which must have the capacity to cooperate effectively with the European Commission and to communicate all suspected cases of irregularities and fraud. They must ensure the protection of EU funds at an (at least) equivalent level to the protection of national funds. Member States are also obliged to assist and co-operate on-the-spot checks carried out by EC services. While some of this *acquis* applies directly to Member States and thus does not need to be transposed, effective co-operation and coordination structures and capacities in the candidate country need to be set up. In order to facilitate the required cooperation by future Member States, the nomination of national anti-fraud cooperation services – AFCOS – as a single contact point with OLAF is considered very useful.

Furthermore, this part of the chapter also includes the convention on the protection of the EU's financial interests ("PIF-Convention") and its three protocols, including the harmonisation of penal law and the reinforcement of cooperation.

Finally, this part of the chapter comprises the non-penal aspects of the **protection of the Euro against counterfeiting** (first pillar aspects), such as the prohibition of metals or tokens similar to Euro coins, the obligation for financial institutions to withdraw counterfeit notes and coins and effective anti-counterfeiting bodies and procedures.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the information provided by Turkey and the discussion at the screening meeting. Turkey indicated that it can accept the relevant standards and *acquis* regarding Internal Financial control.

II.a. Public Internal Financial Control (PIFC) and External Audit

In 2002, Turkey adopted a PIFC Policy Paper outlining the future development of its public internal control systems. On the basis of the conclusions of this paper, the PFMC Law 5018 was adopted and came into force on 1 January 2006. This law aims to ensure harmonisation with international standards and EU best practice: an effective, economic and efficient collection and utilisation of public resources in line with policies and objectives of the government, as well as accountability and fiscal transparency. The law covers the social security institutions, the central government including general and special budget administrations, as well as local administrations.

The law contains the concepts of managerial responsibility and accountability (establish and supervise financial management and control (FMC) systems, establish functionally independent internal audit, clearly defined duties, authorities and responsibilities of personnel as well as appropriate monitoring and reporting, including internal control assurance declaration and public disclosure). The segregation of the duties between the authorising officer, the accounting officer and the ex ante financial controller is addressed.

The internal control system includes strategic planning, performance programming, budget allocation, implementation, ex ante financial control, accountability reports, audit and evaluation as well as accountability to parliament and local councils.

Furthermore the law prescribes the establishment of a decentralised and functionally independent internal audit system as well as central harmonisation of the FMC and internal audit systems. Central harmonisation of FMC is performed by the Directorate General for Budget and Fiscal Control in the Ministry of Finance and the central harmonisation of internal audit is carried out by the inter-ministerial Internal Audit Co-ordination Board.

In April 2005 Turkey established change management teams and a Steering Committee to manage the change process in co-ordination with the Ministry of Finance. Secondary legislation relating to the implementation of the new PIFC system has been largely drafted and approved.

Turkey announced that it will update its 2002 PIFC Policy Paper to take into account recent developments and to correct previous deficiencies. The updated paper will be based on a thorough gap analysis showing discrepancies between present internal control and internal audit systems and the international internal control standards. The scope of the paper will be widened (in a section on Control Environment) to cover all existing inspection and control services including the role of the Board of Treasury Controllers in the control of Community funds, explaining their roles and responsibilities in relation to the three principles of PIFC. The paper will also devote attention to the following items: the management capacities of the IA Co-ordination Board and the suggestions by the Commission to create a permanently functioning Central Harmonisation Unit (CHU) for Internal Audit; the underlying principles of sound financial management of revolving funds and other non-budgetary state income and expenditure if they exist; the exact role and responsibilities of the ex ante financial control and of the recently established Strategic Development Units in line ministries in their relation to the CHUs.

Turkey commits itself to take into account comments by DG Budget of the European Commission before primary and secondary PIFC related legislation is finalised, in line with the 2001 Memorandum of Understanding on the Administrative Co-operation between the Ministry of Finance and DG Budget. To this end all PIFC related policy papers, acts or draft

legislation or regulation will be sent to DG Budget for comments, allowing for at least two weeks of scrutiny.

With regard to **external audit**, Turkey considers that the Turkish Court of Accounts (TCA) can be characterised as operationally and financially independent. It drafts its own budget which is presented directly to the Parliament. It holds both an audit function for revenues, expenditures, assets and liabilities of all public administrations, as well as a judicial function to take a final decision on the compliance of accounts and transactions. The follow-up of its reports is ensured by Parliament. The TCA has a three-year strategy paper and action plan as well as annual audit plans. Currently there is a draft TCA Law to be adopted by Parliament to extend the scope of organisations falling under the audit responsibility of the TCA and to bring the TCA in line with international standards.

II.b. Protection of EU Financial Interests and Protection of the Euro

Article 280 TEU requires Member States to protect the **Communities' financial interests** in the same way as national financial interests. Turkey still has to formally align its legislation to this requirement. The same applies for the immediate communication of irregularities and fraud in the Common Agricultural Policy, Structural Funds and Cohesion Fund.

Regarding cooperation for on-the-spot checks by EU investigators, Turkey stated that it intends to fully support such activities. However, no formal rules are in place yet, which ensure that EC inspectors as well as information and evidence produced by them are treated like national ones. The same applies for the obligation to safeguard evidence, to actively cooperate with and participate in EC inspection missions, and to support such missions, if requested, vis-à-vis economic operators.

Turkish penal law already punishes the principal offences of fraud, corruption and money laundering. However, Turkish penal law lacks a criminal law protection against the misappropriation of funds and clear requirements with regard to the liability of heads of business as well as legal persons for criminal acts against the EU's financial interests. Currently, there are no plans for further alignment.

Within the system of decentralised implementation of EU pre-accession funds, Turkey is subject to provisions requiring the regular communication of suspected irregularities and fraud. Turkey stated that it plans to establish a central anti-fraud cooperation service (AFCOS) for the Commission's Anti-Fraud Office by 2008. In a recent letter Turkey, through its delegation to the EU, has indicated that the Prime Ministry Inspection Board (PIMB) will be the contact point for OLAF with responsibilities to deal with all EU related investigations until the formation of the Turkish AFCOS by 2008.

With regard to the **protection of the Euro against counterfeiting**, Turkey stated that its law provides for a definition of such acts referring to both notes and coins. Four law enforcement agencies, the Turkish Central Bank (CBRT), as well as a directorate in the under-secretariat of treasury are cooperating in the fight against counterfeiting. A "counterfeit banknote monitoring system" has been established with contributions from the CBRT, National Police and Gendarmerie, the latter being the immediate addressee of findings. Information about counterfeiting is to be forwarded to the National Bank by the prosecutors for analysis. A similar system against counterfeit coins is currently being implemented in the Mint. Turkish law does not provide for communication of cases or transmission of counterfeits to the ECB.

Withdrawal and reporting of counterfeit Euronotes is compulsory under the Turkish criminal code, which sentences failure to report a crime or failure of a public officer to report a crime. Cooperation with the Member States, the Commission and the ECB takes place in terms of exchange of information (via Interpol, Europol, Liaison Officers and channels agreed by bilateral agreements).

Regarding counterfeit and sale of medals and tokens similar to Euro coins, there is no legislation in place.

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY

As regards the relevant international standards and the *acquis* under this chapter, Turkey's level of alignment is at a satisfactory level. While an updated PIFC strategy paper is under preparation, important legislation has been adopted. Turkey is aware of the need for further development and implementation, which can be achieved within the medium term.

III.a. Public Internal Financial Control (PIFC) and External Audit

In the recent past, Turkey has made considerable efforts to align its **public internal control** systems with international standards. To that extent it has adopted a PIFC Policy Paper and relevant legislation. Turkey is presently in the process of PIFC implementation. Although this progress is most welcome, there are certain areas that have to be dealt with in the short term, before further progress can be made. The PIFC Policy Paper needs to be updated and cover important areas like the scope of PIFC application, the relationships between internal audit and inspection, the link between the internal control of public budget and of Community funds, and the precise definition of *ex ante* financial control and the establishment of a permanent Central Harmonisation Unit (CHU) for Internal Audit. The immediate establishment of decentralised internal audit units is of high importance, so that the training of public internal auditors can offer the perspective of job opportunities.

In relation to its implementation capacity, the government has adopted several regulations following the implementation of the Public Financial Management and Control Law. The most relevant are the procedures and principles relating to internal control and *ex ante* control, the financial services in line ministries (called the Strategy Development Units), the Internal Audit Co-ordination Board and the training and certification of internal auditors. These regulations provide for the legal basis for activating the PIFC implementation capacity.

The adopted regulation on "Working Procedures and Principles of Strategy Development Units" establishes units in each branch of public administration for carrying out the functions of financial services. One important regulation on "Working Procedures and Principles of the Internal Auditors and Other Issues" and a decree on "Procedures and Principles for the Appointment of Internal Auditors", have recently been adopted. These regulations are important for the establishment and functioning of decentralised internal audit units and for the appointment of public internal auditors. Furthermore, training activities have already started for management officers, officers in financial services including accounting and *ex ante* control and for internal auditors.

The implementation capacity of the Central Harmonisation Units for Financial Management and Control and Internal Audit will have to be kept at levels in such a way that they can carry out their responsibilities adequately and timely.

Turkey has been accredited for the Decentralized Implementation System of Community assistance since 2003. The implementation of the system, which may have an impact on the global situation of PIFC in Turkey, has recently shown some severe shortcomings, which are currently being addressed by the government.

With regard to **external audit**, the present draft TCA Law, which has been presented to Parliament for approval, is increasingly consistent with the INTOSAI standards.

III.b. Protection of EU Financial Interests and Protection of the Euro

Turkey needs to nominate and establish the service responsible for the coordination and cooperation with the Commission in the fight against fraud and the protection of the EU financial interests. As the final decision regarding this AFCOS will not be adopted until 2008, Turkey has, for the meantime, appointed the PMIB as provisional contact point for OLAF.

In order to comply with the requirements of the **PIF-Convention** and its protocols, Turkey's criminal law identifies certain offences. However, Turkey must still undertake further efforts to align its provisions with the Convention and the Protocols:

- The penal law protection against the misappropriation of funds should be completed.
- The existing fraud and corruption provisions should be assessed as to whether a further amendment of national law is required in the light of jurisprudence.
- More information is needed in order to determine whether the Turkish criminal law provides for concepts to ensure that heads of businesses or legal persons can be held liable for such offences. Turkey will have to provide for a penal liability of heads of businesses and a liability of legal persons for criminal acts.
- The jurisdiction granted to Turkish courts should also be aligned in detail with the requirements of the PIF-Convention and its protocols.

With respect to the **protection of the Euro against counterfeiting** Turkey has sufficient expertise in relation to analysis and classification of counterfeited notes and coins. There is also an adequate level of police capacity incorporating four law enforcement bodies. However, progress needs to be achieved with regard to centralisation of information and communication to the competent Community institutions and bodies.

Turkey needs to provide specific sanctions for financial institutions failing to withdraw counterfeits from circulation and hand them over to the competent national authorities. Finally, Turkey needs to introduce sanctions against medals and tokens similar to euro coins.