2017 Annual Report
German Supreme Audit Institution, Bundesrechnungshof
Abridged version

Preface

The present volume contains those audit findings developed by the German SAI that are relevant for the granting of discharge by the two Houses of the German Parliament to the Federal Government for FY 2016. This is the annual report on federal financial management.

1 The German SAI's annual report volumes I and II – basis for the annual decision about granting discharge to the Federal Government

The German SAI audits the entire financial management of the Federal Government including federal off-budget funds and industrial or trading funds. We highlight the results of our audit work in the annual report on federal financial management. This report provides an essential basis for the decision which the two Houses of the German Parliament take each year about granting discharge to the Federal Government.

In our annual report, we especially state

- whether the amounts posted in the budget and capital accounts tally with the amounts stated in the underlying accounting records and whether the audited revenues and expenditures are properly backed up by vouchers;
- major cases where the audited entities have not complied with the applicable financial management regulations and principles;
- the key results generated by our audits of the management of federal government shareholdings in enterprises and
- what recommendations for improvement we have developed.

As a result, the annual report deals with the Federal Government's revenues and expenditures, assets and liabilities. Furthermore, the annual report may address all programmes that may have a financial impact on the federal budget even if they have not yet resulted in receipts or issues.

We combine the reporting about the results of our audit work with an analysis of trends in federal public finance. Previously, the annual report also included explanations of the key items and trends of the departmental budgets that form part of the overall federal budget (analyses of departmental budgets). We are considering the option of publishing the analyses of departmental budgets separately after the budget deliberations in the future, thus furnishing more timely information to a wider circle of stakeholders.

We issue our annual report in two volumes:

- The present volume (principal volume) covers the general audit findings on the annual federal accounts and trends in public finance. This report covers the findings on the budget and capital accounts, the trends in federal public finance and on cross-departmental and government-wide issues. In addition, it sets out the audit findings on individual budgets.
- In a supplementary report (addendum) issued in the following spring, we report on additional audit findings of current interest. We use this possibility to report on current audit findings that have become available only after submission of the principal volume as input for the discharge procedure.

The President of the German SAI communicates the principal volume (autumn report) to the two Houses of Parliament and the Federal Government. At the same time, he presents it to the public. The autumn report is also available on our website.

The Lower House of German Parliament (Bundestag) refers our annual report to its Budget Committee. The Budget Committee communicates the report to its sub-committee, the Public Accounts Committee.

2 Audit findings promote compliance and performance in government operations

The annual report sets out those of our audit findings and our pertinent recommendations which the executive branch has so far not taken up. They are discussed intensively in the Public Accounts Committee (PAC). The Committee usually invites the responsible policy-makers to attend the deliberations. In the vast majority of all cases (more than 90 per cent) the PAC endorses our findings and recommendations. In these cases, the PAC adopts resolutions requesting the Federal Government to implement our recommendations and to ensure that government operations provide good value for money and comply with applicable regulations.

The Budget Committee prepares the annual decision about granting discharge, taking into account the results of the deliberations of the PAC on our annual report. Based on this, the two Houses of Parliament decide on granting discharge of the Federal Government. They normally call upon the Federal Government to pay due regard to the resolution of the Budget Committee on our audit findings when preparing the budget estimates and implementing the federal departmental budgets.

We monitor the implementation of the Committee resolutions over the course of several years and follow up on whether the Federal Government has duly implemented the recommendations developed. During this period, the respective federal government departments have to answer to the PAC. Furthermore, the results may serve as input for the budget deliberations, thus having a bearing on the appropriation of funds for the following financial year.

In many cases, the audited bodies directly implement our recommendations. As a rule, reporting to the two Houses of Parliament is not needed in such cases.

3 The quality of audit findings is ensured by a structured procedure and the involvement of audited bodies.

We are independent in the choice of what we audit and the design of our audit exercises. As a rule, we accede to audit requests of Parliament and its committees.

In our audit work, we apply the criteria of performance, regularity and compliance as set forth in Art 114.2 German Constitution. Furthermore, we check whether the audited bodies have used funds in an efficient way and whether their programmes actually accomplished the objectives set. When auditing regularity and compliance, we check whether the audited bodies adhere to applicable standards and principles.

As a matter of principle, we communicate our audit findings to the auditees and request them to comment on our findings, giving them the chance to explain the circumstances or to justify their actions. On this basis, we decide on the final wording of our audit findings.

By means of an implementation status query and follow-up audits, we keep an eye on any remedial action taken or improvements made by the audited bodies in response to our audit findings. We also verify compliance by the audited bodies with the requirements imposed by Parliament.

Our work is carried out in line with clear principles and free from any bias. We continuously reconsider our methods and adapt them where necessary. We do not evaluate policy decisions. However, we may audit and report on whether the assumptions underlying these decisions are accurate and whether a measure based on them has achieved the intended effect.

4 The German SAI and the Federal Performance Commissioner advise Federal Government and Parliament

On the basis of audit findings, we may provide advice especially to the two Houses of Parliament, the Federal Government and individual federal government departments. We summarise our audit findings and recommendations pursuant to Art. 88.2 Federal Budget Code. The reports addressed to Parliament are thoroughly deliberated at committee level, especially in the Budget Committee and the PAC, its sub-committee. During these deliberations, decisions are also taken about the way in which our recommendations are to be implemented.

Furthermore, we may at any time inform the two Houses of Parliament and the Federal Government of matters of particular importance (Art. 99 sentence 1 Federal Budget Code). We have to be consulted or notified in many cases such as the promulgation of grant funding guidelines by the federal ministries or changes of federal government shareholdings in companies incorporated under private law.

By tradition, the President of the German SAI holds the ex officio position of Federal Performance Commissioner. One of the Federal Commissioner's principal functions is to provide advice to Government and Parliament on the impact legal provisions may have on government performance. For this purpose, federal government departments have to involve the Commissioner at an early stage in drafting bills, delegated legislation and administrative regulations. In discharging his functions, the Federal Commissioner mainly relies on the audit findings and lessons learnt of the German SAI.

5 The German SAI strengthens and supports public accountability by publishing audit results

Once our annual report or special reports prepared in accordance with Article 99 Federal Budget Code are forwarded to Parliament, they are also published on the internet. In addition to that, we may publish or grant access to any other report and preliminary audit report where appropriate. We make use of this option unless rights relating to data privacy, business interests or the public interest may be infringed. This ensures transparency of government activities not only for Parliament but also for citizens and the media. Annual reports, preliminary audit reports and other reports that have been made public so far are available on our website, please click at the button: "Publications"

6 German SAI's rights to collect audit evidence at non-federal entities have been solidly enshrined in the Constitution and significantly extended

Along with legislation on the reform of the fiscal relations between the federal and regional governments, the two Houses of Parliament amended Art. 114.2 German Constitution. For the first time, this amendment explicitly gives us a constitutional right to collect audit evidence at non-federal entities where these manage federal funds. This may be entities of the federal states, local authorities or entities incorporated under private or public law. This has settled a dispute about the extent of our right to collect audit evidence, i.e. to carry out field work.

We have already responded to the significantly extended audit access. We have set up a project audit unit that will examine federal grants given under the Act to Promote Investments of Financially Weak Local Authorities.

In this endeavour, we benefitted from our reorganisation that took effect on 1 January 2017. With a sweeping reform of our structural organisation, we realigned our audit divisions to better address key policy areas. Our field offices, that previously were separate entities, have become organisational units of our Institution. Thus, we abolished one hierarchy level and integrated the staff of our field offices directly into our audit divisions and audit units. By setting up the project audit unit, we may now respond more quickly and in a better targeted manner to new and complex administrative challenges emerging.

2017 Annual Report

General part

1 Findings on the Federal Government’s budget and capital accounts for FY 2016

We audited the budget and capital accounts of the Federal Government for FY 2016. In doing so, we did not find any variances significant for the discharge procedure between the figures stated in the accounts and in the underlying records. Government expenditures totalled €317.4 billion and thus were €0.5 billion higher than estimated in the budget. The remittance to the reserve "Asylum seekers and refugees" excluded, expenditures amounted to €310.9 billion. The revenues were €0.5 billion higher than budgeted. No net borrowing was required to balance the federal budget. The constitutional debt rule was complied with. Excess and extra-budgetary expenditure totalled €2.1 billion. Commitments totalled €156.1 billion. At year-end 2016, the Federal Government and the off-budget federal entities had assumed guarantees of €478.0 billion. Including off-budget federal entities, the Federal Government’s net worth was €252billion. Liabilities (including contingent liabilities for public service retirement and health care benefits) amounted to €1.866 billion.

1.1 Status of discharge procedure

Both Houses of Parliament granted discharge to the Federal Government for FY 2015. The respective resolutions were based on the 2015 annual accounts and our 2016 annual report on federal financial management. The *Bundestag* (Lower House of Parliament) has not yet put the granting of discharge to the Federal Government on its agenda.

1.2 Information pursuant to Art. 97.2.1 Federal Budget Code

Rather than as an aggregated annual account, the Federal Ministry of Finance has presented the budget and capital accounts separately since FY 2009. We audited compliance of these accounts. We did not find any deviations significant for the discharge procedure between the amounts stated in the accounts and those in the underlying records.

On the basis of samples we checked the extent to which federal budget revenues and expenditures were properly supported by vouchers. We used an arithmetical statistical method. For this purpose we took a random sample of 1,926 of the individual accounting entries recorded in the Federal Government's accounting system. We found major errors in 1.39 per cent of the audited accounting entries. From this we conclude that the proportion of payments not properly supported by vouchers in the total number of individual accounting entries recorded in the Federal Government's financial management system was likely to be of the same magnitude.

1.3 2016 budget implementation

The 2016 Budget Act of 21 December 2015 provided for revenues and expenditures of €316.9 billion without any net borrowing. One budget item was a withdrawal from the "Asylum seekers and refugees" reserve in the amount of €6.1 billion.

In order to facilitate additional public investments in the educational infrastructure, the Federal Government increased the resources of the Municipal Infrastructure Fund by €3.5 billion. This allocation of resources required a supplementary budget, which also provided for an adjustment of interest expenditure to current market rate levels, resulting in the reduction of the respective budget estimate by

€3.5 billion. As a result, the 2016 federal budget with a target total of €316.9 billion was balanced without new borrowing.

As in the previous financial year, the 2016 Budget Act provided for any surplus in budget execution to be remitted to the "Asylum seekers and refugees" reserve. Furthermore, any profits of the German central bank in excess of the budgeted profits of €0.7 billion were to be allocated to the reserve. Based on these provisions, further €6.5 billion were allocated to the reserve on the closing of the 2016 budget. The withdrawal proposed for FY 2016 of €6.1 billion from the reserve was not necessary. Accordingly, the amount of the reserve at the end of FY 2016 exceeded the figure planned by €12.6 billion.

The Federal Budget Code does not contain any provisions about estimating such a reserve. In view of the funding shortage arising in connection with the refugee crisis, using a foreseeable funding surplus in implementing the current year's budget for the purpose of accumulating a reserve in favour of future budgets is reasonable for a transitional period. However, continuously forming reserves for funding expenditures in subsequent financial years would significantly interfere with the principle of annual budgeting. Therefore, this instrument should be given up as appropriate. In future financial years, any surpluses should be used again for repaying debts of the Investment and Redemption Fund (IRF).

1.4 Budget implementation and supplementary budgets

In budget implementation, total expenditure and total revenue amounted to €317.4 billion, i.e. €0.5 billion more than estimated in the supplementary budget. No net borrowing was required to balance the 2016 federal budget. Total expenditure also encompasses allocations to the reserve for asylum seekers and refugees. Due to a revenue surplus of €6.2 billion and seigniorage amounting to €0.3 billion, it was possible to remit an aggregate amount of €6.5 billion to the reserve.

Compared to the supplementary budget, items with significant underspending were especially interest expenditure, the programme for investing in the future and warranties.

However, the result of budget execution with respect to interest expenditure does not reflect the financing terms because it includes revenue of €6 billion from the sale of bonds at a premium. With dropping market interest rates, the Federal Government was able to generate additional revenues by issuing additional bonds on identical terms at a price above par. However, due to the higher interest rates, its interest expenditure will increase. Given that the bond premiums are recognised fully in the year of issue, this might give the impression of using discretionary scope.

Revenue (excluding seigniorage) increased by €0.5 billion compared to the amounts included in the supplementary budget. Tax revenue increased by €0.9 billion. Other revenues exceeded the budget targets by €5.8 billion. In deviation from previous planning, it was possible not to withdraw €6.1 billion from the reserve for asylum seekers and refugees.

In principle, revenues and expenditures have to be balanced without obtaining proceeds from borrowing. FY 2016 is the first year in which the new debt rule applies after the expiry of a transition stage stipulated in the Constitution. The debt rule is to ensure long-term sustainability of the federal and regional government budgets.
The new debt rule was complied with both in drawing up the 2016 budget and the supplementary budget.

Net borrowing as defined by the debt rule amounted to €-1.0 billion which means that a surplus has been achieved. While the federal budget was balanced without net borrowing, the off-budget federal entities recorded a surplus. This results in a structural surplus of €0.8 billion. Thus, the debt rule providing for a standard limit on structural net borrowing of 0.35 per cent of GDP was complied with also in budget implementation.

1.5 Details of revenues and borrowing powers

As a rule, the portion of the profit of the German central bank that exceeds the relevant federal budget estimate is to be paid into the Investment and Redemption Fund. The estimate for the central bank's profit had been €2.5 billion. The actual profit totalled €3.2 billion. In compliance with a provision of the 2016 Budget Act and in deviation from the general rule, the portion of the central bank's profit that exceeded the estimate in the federal budget in the amount of €0.7 billion was transferred to the reserve for asylum seekers and refugees. As already in the previous year, the amount was not used to retire debts of the Investment and Redemption Fund.

Since FY 2013, the budget account has included a "summary of the losses of federal revenue". Apart from the remitted claims, temporary and permanent respites, settlements, changes in contracts and waivers for other reasons are disclosed. In FY 2016, losses of revenue totalled €3.6 billion.

The 2016 Budget Act did not provide for any borrowing powers to fund expenditure. Furthermore, no residual borrowing authorisation from the previous year was available. Likewise, no residual borrowing authorisation from FY 2016 is available for the 2017 federal budget.

1.6 Excess and extraordinary budget expenditure

In FY 2016, the Federal Government incurred excess expenditures of €1.9 billion and extra-budgetary expenditures of €0.2 billion. The aggregate amount of €2.1 billion is equivalent to 0.7 per cent of the total budget target. It exceeds the previous year's figure of €0.3 billion by €1.8 billion. All excess and extra-budgetary expenditures were set off by under-implementation of other budget appropriations.

1.7 Unexpended balances

The amount in which the federal government level recognises unexpended balances from the past financial year is usually not yet known when the budget account is drawn up. We can therefore only present an overview of the past FY's (2016) expenditure authorisations that are eligible for carry-forward and report on the unexpended balances recognised in the previous year (2015).

At the end of FY 2015, €11.8 billion were eligible for carry-forward to the 2016 budget. Unexpended balances of some €9.8 billion were actually carried over to FY 2016, i.e. €0.5 billion more than at the end of FY 2015.

At the close of FY 2016, unexpended balances of €16.7 billion were available. As a matter of principle, this amount is available for recognising unexpended balances in 2017. It is €4.9 billion higher than at the close of FY 2015.

A special feature of expenditure authorisations which come under devolved budget management is that, as a matter of principle, the use of unimplemented appropriations need not be matched by commensurate savings in the relevant ministry's own departmental budget. They are available without any time limit. Departments and agencies formed unexpended balances of €2.3 billion of the expenditure authorisations eligible for carry-forward to FY 2016, which amounted to €2.4 billion. According to this, government departments wish to draw on more than 94 per cent of the unused expenditure authorisations in future years. In view of Parliament's power to control spending, we expect all ministries to observe the requirements when assessing their specific needs. They have to apply a rigorous standard when recognising unexpended balances. This is particularly true in an environment of significantly increasing expenditure authorisations that are eligible for carry-forward. Of the expenditure authorisations that are eligible for carry-forward into 2017, €2.8 billion come under a flexible financial management regime, i.e. €431 million or 18 per cent more than in the previous year.

1.8 Commitment authorisations

The 2016 federal budget included commitment authorisations of €71.4 billion, i.e. €4.4 billion more than in the previous year. Actual commitments made under these authorisations totalled €41.0 billion. The utilisation ratio was 57 per cent; last year's utilisation ratio was 67 per cent. In addition, the federal government departments entered into other commitments amounting to €4.2 billion due to other legal requirements or for ongoing activities. Thus, the utilisation ratio for FY 2016 is lower than in the previous year. Almost half of the available resources had not been used. We expect all federal government departments to carefully assess if current commitment authorisations actually comply with the requirements for inclusion in the budget and to budget such authorisations only in the amounts necessary for fulfilling the tasks and for making payments when due.

As of 31 December 2016, payments of €156.1 billion were still to be made under commitments entered into. Of the total amount of commitments entered into until 2016, €43.6 billion have been allocated to FY 2017 and €34.4 billion to FY 2018.

1.9 Guarantees

Guarantees are instruments by which the Federal Government supports projects meriting assistance in terms of public interest. They also back up the Federal Government's financial commitments vis-à-vis international financial institutions. The 2016 Budget Act had authorised the Federal Ministry of Finance to grant guarantees up to an amount of €486.4 billion. Thus, the guarantee ceiling increased by €9.5 billion compared to the previous year's figure. By the end of FY 2016, the

Federal Government had provided guarantees in the amount of €359.1 billion.

Under the Act on the Assumption of Guarantees in Connection with a European Stabilisation Mechanism, the Federal Ministry of Finance was authorised to assume guarantees of €211 billion for financing operations carried out by the European Financial Stability Facility. By year-end 2016, the Ministry had used €85.9 billion under this authority.

In 2016, federal revenues from guarantee fee payments and from honouring federal guarantees amounted to €2.6 billion. This contrasted with federal expenditures of €0.8 billion on compensation payments for defaults, debt restructuring and other expenditures in connection with honouring guarantees.

1.10 Funds under devolved financial management

Expenditure authorisations may be budgeted as funds for devolved financial management, if this serves to put budget funds to economical use. In contrast to other budget funds, they remain available for the specified purposes in future years without any time limit. If budget funds are brought under the devolved management regime, the amounts concerned need to be posted as expenditure and are thus stated in the budget account. However, they need not have been disbursed to third parties. This diminishes the desirable clarity of the accounts whose presentation is required by the German Constitution and Parliament’s ability to oversee spending.

By the end of 2016, the funds under devolved financial management on federal cash accounts totalled €1,639 million. Such funds were spread over ten departmental budgets. Compared to the previous year’s €1,223 million, their aggregate balance increased by €417 million, equivalent to 34.1 per cent. A major item with a rapid growth of funds under devolved financial management is departmental budget 30 (Federal Ministry of Education and Research).

1.11 Capital account

Administrative regulations issued with respect to Arts. 73, 75, 76, 80 and 86 Federal Budget Code are applicable to the Federal Government's accounting system. However, not all major assets have been fully recognised. As in previous years, the Federal Ministry of Finance notes that the values of such assets have not yet been determined. These include federal real estate with infrastructure assets and tangible movable assets. Moreover, assets that have already been recorded do not adequately reflect the true financial position.

The valuated federal assets including those of the off-budget federal entities totalled €252 billion at year-end 2016. Liabilities (including provisions) totalled €1,866 billion. These encompass credit market liabilities (including borrowing to maintain liquidity) amounting to €1,116 billion.

We acknowledge the Federal Ministry's efforts of the past few years to enhance data quality; to produce more meaningful and insightful capital accounts; and to include all items not yet disclosed. By doing so, they complied with the demands raised by the Bundesrechnungshof for many years. However, our findings show that current accounting procedures, the process of closing the accounts as well as the rendition of the overall account are error-prone and inefficient. We support the Federal Finance Ministry's efforts to further complement and improve the capital account.

1.12 Off-budget federal funds

The budget account presents 25 federal off-budget funds and trading funds.

Between 2009 and 2011, the Federal Government used the Investment and Redemption Fund for financing additional steps to boost economic growth. As from 2012, the bodies responsible started to settle and liquidate the Fund. In derogation from the IRF Establishment Act, the portion of the central bank's profit exceeding the amount estimated as revenue in the federal budget (€0.7 billion) was transferred to the reserve for asylum seekers and refugees. Differing from the years 2009 and 2014, in 2016 the Investment and Redemption Fund thus did not participate in the profits transferred by the German central bank. Likewise, the 2016 federal budget surpluses were not used to redeem liabilities of the IRF but served to fund the reserve for asylum seekers and refugees. This means that the original goal of repaying the debts incurred by the IRF for counteracting the financial and economic crisis in a more favourable period of the economic cycle was abandoned at least in the medium term. The Legislator's original intention to redeem the debts within a reasonable period has become a distant prospect.

The Financial Market Stabilisation Fund set up to respond to the financial crisis was designed to help financial institutions to overcome liquidity shortages and to strengthen their equity capital base. The Fund is managed by the Federal Agency for Financial Market Stabilisation. At year-end 2015, the Fund was closed so that no new programmes can be taken.

The deficit accumulated since the establishment of the Fund totalled €22.5 billion on 31 December 2016. The loss will be carried forward until the Fund is wound up. Any loss remaining after the Fund's winding-up will be shared by the Federal Government and the German states in the proportion 65:35, with the states bearing losses only up to the amount of €7.7 billion.

Another off-budget federal entity, the Energy and Climate Fund (ECF), is to provide the resources for programmes promoting an environmentally friendly, sustainable and affordable energy supply and climate change mitigation. To fund programme expenditure, the proceeds from auctions of tradable emissions allowances are to be allocated to the Fund (CO_2 emissions trading). Since the amendment of the law on establishing the Energy and Climate Fund in 2014, the Fund is eligible to receive federal grants pursuant to the applicable budget act. In 2016, such grants totalled €713 million. Total expenditure of the Energy and Climate Fund was €1.6 billion.

Giving annual federal grants means abandoning the original goal of financing the ECF's expenditure solely from climate change levies. Instead, the ECF is partly funded from the general budget and the amounts of such financing are likely to increase significantly in future years. An efficient, transparent and coordinated use of resources could be better achieved by estimating all resources in the federal budget. Furthermore, parliamentary oversight would be facilitated if all federal revenues and expenditures were disclosed in the budget account. Against this background we do not perceive any need for maintaining the ECF.

The Reconstruction Aid Fund was established in July 2013. The off-budget fund serves to channel disaster relief to victims of floods from 18 May to 4 July 2013 and compensate for damage not covered by insurance.

When setting up the Fund in 2013, the Federal Government allocated €8 billion to the Fund. €1.5 billion were designed for restoring federal infrastructure affected by the flood, €6.5 billion for eliminating flood damages in the German states.

The actual cash outflow was lower than anticipated. Up to year-end 2016, only €3.0 billion of the Fund's total resources were called, of which €773 million in 2016.

The Federal Government has already exercised the option to reallocate unneeded Fund resources of €1.217 billion to the federal budget.

In case the federal states do not fully use the portion of funds earmarked for them, the Federal Government may remit up to €1 billion from the Fund to the federal budget before the final account of the Fund resources is drawn up.

In order to help level out differences among the various federal states' economic structure, financial assistance from the Municipal Investments Promotion Fund shall be granted to promote major investments of financially weak local governments and associations of local governments. Up to 90 per cent of such projects may be covered from federal grants to financially weak local governments.

Initially, the Municipal Fund was endowed with a one-off amount of €3.5 billion. By virtue of legislation for restructuring the federal fiscal equalisation system as from 2020 and amending budgetary law, the endowment was increased to €7.0 billion by a second allocation of €3.5 billion. This amending legislation also provided for an option to grant financial assistance to financially weak municipalities for nationally significant investments in the field of educational infrastructure. Furthermore, the funding period was extended. The second allocation and thus the increase of the total endowment was authorised by the 2016 Supplementary Budget Act before the Constitution was amended. The said Act came into force in the beginning of 2017.

In FY 2016, the Municipal Fund resources of €146.2 million were claimed. Based on the actual volume in FY 2016, i.e. €3.5 billion, the disbursement rate was 4.2 per cent. The unused budget funds were allocated to a reserve. To observe the principle of annuality, we recommend that expenditure should only be budgeted when they meet the formal requirements for inclusion in the budget.

In the case of the Municipal Fund, we also hold that it does not meet the strict criteria to be applied to the establishment and maintenance of off-budget federal entities. There are no apparent advantages over estimation in the federal budget. Given that the volume of the Municipal Fund has meanwhile been doubled to €7.0 billion, that there has been an extension of the funding areas and that the possible duration of grant-funding has partly been extended by four years, this financial support should be directly included in the federal budget and not budgeted in an off-budget federal entity.

2 Trends in federal public finance – Challenges and options for action for the 19th legislative period

2.0

Due to the general elections, the 2018 draft budget will not be deliberated on and adopted in Parliament (principle of discontinuity). However, it describes the financial point of departure and the action required in the new legislative period. From a fiscal point of view, the framework conditions remain favourable. For the fourth time in a row, the Federal Government is able to submit a draft budget balanced in revenues and expenditures without net borrowing. This is possible due to a stable economic trend with a high rate of employment, low unemployment and expected increases in tax revenues and low interest rates. The medium-term financial plan up to 2021 also provides for no new borrowing. Nevertheless, considerable fiscal challenges lie ahead in the medium and long term. These include the demographic change reflected above all in increased grants to the statutory pension insurance scheme and the growing need for investments in infrastructure. It remains to be seen whether, in the long run, the eternity burdens of the interim and final storage of nuclear waste will require additional funding from the federal budget. The fiscal burden on Germany stemming from the reception and integration of asylum-seekers and refugees continues to be disproportionately high in comparison to most other European Union states. The Federal Government increasingly supports the mission performance of the federal states and the municipalities. This leads to an interlocking of tasks, operational and funding responsibilities which makes control and audit by the Federal Government difficult. A positive aspect is that we have been given access rights to audit evidence at entities outside the federal government level where such entities manage federal funds. Following our proposal, Parliament has also implemented the necessary control and audit mandate of the federal administration with respect to financial assistance.

2.1 Key budgetary figures up to 2021

The key figures set out in the FY 2018 draft budget and the medium-term financial plan up to 2021 are based on the Federal Government’s assumption of a favourable economic trend based on the spring 2017 projection for the German economy. The draft budget calls for expenditure to rise to €337.5 billion in FY 2018, which means an increase by €8.4 billion, equivalent to 2.6 per cent over the 2017 target figure. Once again, we found significant increases of expenditure under some departmental budgets. Expenditure policy thus remains expansive. Tax revenues are projected to grow by €7.8 billion, equivalent to 2.6 per cent, to €308.8 billion. To balance the 2018 budget, €8.2 billion are to be withdrawn from the “asylum reserve” formed in FY 2015. As in the annual budgets since 2014, no net borrowing has been planned.

Since 2007, new off-budget federal entities such as the Energy and Climate Fund and the Municipal Investments Promotion Fund have been set up. The existence of such subsidiary budgets may impair such budgetary principles as unity, completeness, clarity, current-year principle and annuality. We therefore reiterate our recommendation not to rely on alternative funding channels in the form of subsidiary budgets. The required resources are to be estimated in the core budget as expenditures or commitment authorisations.

According to the medium-term financial plan, expenditures will rise to €356.8 billion up to 2021. The revenue budget is to continue to increase to up to €341.6 billion. No new borrowing for balancing the budget has been scheduled for the financial planning period. Compared to the previous financial plan, expenditure will rise above all in the defence budget. Estimates of social expenditure are lower. Nevertheless, they will continue to increase during the financial planning period. Financial burdens will be alleviated by additional toll revenues estimated as from 2019, the withdrawals from reserves scheduled for the 2018 and 2019 budgets and the partial reversal of the general revenue shortfall included in the previous financial plan.

2.2 Fiscal challenges

The figures of the 2018 draft budget and the financial plan up to 2021 include a number of fiscal risks that may impair the medium and long-term sustainability of the federal budget. This includes the rising expenditure in connection with demographic change and the maintenance and modernisation of infrastructure. Additional burdens arise for the interim and final storage of radioactive waste, the need to cope with the influx of refugees and the modified funding arrangements between the Federal Government and the federal states. At the European level, additional burdens may emerge due to the Brexit and potential impact of the sovereign debt crisis.

The fiscal burden on Germany stemming from the reception and integration of asylum-seekers and refugees continues to be disproportionately high in comparison to most other European Union states. According to the 2018 draft budget, the Federal Government will allocate €21 billion to this purpose. Further burdens in the range of tens of billions of euros have to be expected in the medium term. A considerable portion of this will be distributed to state and municipal budgets through VAT.

The restructuring of the financial relationships between the Federal Government and the federal states will result in additional burdens for the federal budget in the annual amount of €10 billion as from 2020. The aggregate financial support of the Federal Government to states and municipalities will total more than €76 billion in 2018. Compared to that, little progress is being made in the separation of tasks. At least, a decision has been made that the federal motorways will be taken over by a company controlled by the Federal Government. However, considerable challenges will have to be overcome before this reorganisation can become operationally effective. With regard to subsidised housing, the relevant tasks and funding responsibilities will be ultimately assumed by the federal states as from 2020.

We recommend that our proposals and ideas for a greater separation of tasks and funding responsibilities will be pursued further in the new legislative period. The objective must be to achieve greater transparency in federal cooperation and to enhance financial self-reliance of the different levels of government. A positive aspect is that we have been given access to audit evidence at entities outside the federal administration where such entities manage federal funds. Following our proposal, Parliament has also implemented the necessary steering and control rights of the federal administration. This enables the Federal Government to adequately control compliance and performance above all of mixed funding resources.

Even though the Federal Government's fiscal situation appears favourable, greater emphasis should be placed on the structural consolidation of the federal budget in the face of current and potential challenges. Since the savings potential in the expenditure budget appears limited, the focus should be on the revenue budget in order to prepare for meeting the fiscal challenges and, where appropriate, for sustainably financing tax relief. A critical review of existing tax relief to be carried out at regular intervals could open up considerable fiscal leeway. There is a high consolidation potential inherent in the subsidies in the taxation of energy. The comparably low tax rate on diesel fuel should also be questioned. Another pending issue is the reform of the reduced VAT rate which we have demanded for years.

2.3 Compliance with the debt restriction rule

The new constitutional debt restriction rule has been effective since FY 2011. According to this rule, the Federal Government may not exceed a borrowing limit of 0.35 per cent of gross domestic product (GDP) in times of normal economic growth. According to the 2018 draft budget and the financial plan up to 2021, borrowing relevant for the debt rule will remain below the ceiling set. The Federal Government's draft budget anticipates a revenue deficit of €8.5 billion that is to be set off by the withdrawal of €8.2 billion from the "asylum reserve" and by seigniorage (€0.3 billion). The "asylum reserve" of €18.7 billion formed from the revenue surpluses of the 2015 and 2016 budgets would decline to €3.8 billion as a result of the withdrawals planned under the 2017 and 2018 budgets. According to the medium-term financial plan, the remaining amount is to be used to balance the budget in FY 2019. In our opinion, continuously forming reserves to fund expenditures in subsequent budgets seriously encroaches upon the principle of annual budgeting. Furthermore, the recognition of allocations to and withdrawals from reserves as revenue and expenditure, respectively, likely does not comply with the EU fiscal rules. Therefore, this instrument should be given up as soon as possible.

The planned safety margin to the limit of structural net borrowing is appropriate under fiscal aspects in order to be able to cope with adverse fiscal developments and new challenges while complying with the debt rule. Thus, the foreseeable outflow of resources from the off-budget federal entities is already included in the calculation of the relevant limit for structural net borrowing.

2.4 Top-down approach and decision made in March 2017 on benchmark figures

Since 2012, the Federal Government has drawn up its budget proposal by means of the top-down procedure. In this regard, it sets binding benchmark figures regarding revenues and expenditures of all budget accounts in order to implement the new debt restriction rule. In March 2017, the Federal Cabinet adopted the financial benchmark figures for the FY 2018 draft budget and the medium-term financial plan up to 2021. According to the tax revenue estimate as of May 2017, revenue forecasts for the period up to 2020 improved by €11.4 billion as compared to the benchmark figures adopted. This is attributable to more favourable forecasts of economic trends. On the other hand, the results of the negotiations at federal government and states level about their financial relations need to be taken into account in the medium-term financial plan as from 2020. On balance, the planning figures for the period 2018-2021 improved by a total amount of €17.2 billion compared to the decision about the benchmark figures.

Since 2016, the Federal Government has underpinned budget preparation by means of spending reviews, i.e. relevant analyses of revenues and expenditures. Two final reports supplemented by recommendations are available for the two issue areas "Housing" and "Promotion programmes for energy transition and climate change mitigation", which were selected in the last budget preparation procedure. Since the saving of budget funds is not the first priority in such analyses, the fiscal impact of the recommendations is limited. With regard to an efficient and effective use of budget funds, we consider it appropriate to do periodical analyses in the course of budget preparation. We appreciate that the Federal Government plans to include in its analysis for the 2017-2018 cycle two issues of current interest in political and economic terms, i.e. the issues of "Procurement of standardised bulk goods" and "Humanitarian aid and transitional aid including the interfaces crisis prevention, crisis response, stabilisation and development cooperation".

2.5 Trend and structure of expenditures

Pursuant to the 2018 draft budget, social security expenditure is to increase by €3.3 billion to reach €173.8 billion. Notwithstanding the relatively minor increase of 1.9 per cent, social security expenditures form by far the largest expenditure item in the federal budget. This is due to the large funding provided by the Federal Government to the statutory pension insurance and health insurance schemes, financial support of the labour market and migration-related expenses. In addition, the Federal Government has increasingly paid social expenditure which, according to the constitutional assignment of tasks, should be primarily borne by the states and local authorities. This mainly concerns social assistance benefits. According to the financial plan, the share of social expenditure in the total budget will increase even further – from 51.5 per cent (2018) to 52.2 per cent (2021). For the first time since 2013, the 2018 draft budget anticipates an increase of interest expenditure in 2018. Compared to the proportion of social expenditure, the share of investments remains at a low level.

As stated in the 2018 draft budget, expenditures for supporting the various retirement benefit schemes (statutory pension insurance, retirement benefit programme for farmers and for federal employees, benefits under special pension schemes in Eastern Germany and retirement benefits for former civil servants of the then government-run railway, postal and telecommunications services) amount to more than one third of total expenditures. The biggest items in this expenditure category are grants to the statutory pension insurance scheme totalling €93.7 billion. According to the financial plan, they are expected to increase to reach €103.3 billion in 2021. This increase is due to the demographic trend and enhanced benefits (such as the maternal pension supplements and a new provision under which employees may retire early at the age of 63 without a reduction of their pension claim) and the Act extending pension legislation to Eastern Germany.

The favourable labour market situation has had a positive impact both on the federal budget and on the Federal Employment Agency’s budget. For the financial planning period, the Federal Government expects only a slight increase of labour market expenditure from €37.1 billion in 2017 to €38.3 billion. This is contingent upon the smooth integration in the first labour market of refugees entitled to protection. Based on the stable labour market situation that is currently expected, the Federal Employment Agency is likely to accumulate budget reserves: Up to 2021, the reserve is expected to increase to about €29 billion.

The federal grants channelled via the Health Fund to the statutory health insurance scheme remain high at €14.5 billion annually. Despite an increase of expenditure by 4.3 per cent in 2016, the scheme’s financial situation is comfortable since rising expenditure has been largely set off by higher contribution revenues. At year-end 2016, the financial cushion in the statutory health insurance scheme totalled €25 billion. In some areas of health care, expenditure is increasing last but not least due to demographic trends. Without cost cutting programmes, it is likely that the funding need and the burden on the federal budget will increase in the medium term.

Where interest expenditure is concerned, the federal budget continues to benefit from historically favourable refinancing terms. Nevertheless, the Federal Government does not expect future interest expenditure to continue to decline as in recent years. According to the 2018 draft budget, interest expenditure is to increase slightly from €18.5 billion in 2017 to €20.8 billion. One of the reasons for this is that revenues from bond premiums as in recent years are no longer expected. In the subsequent years of the financial planning period, interest expenditure is to increase only moderately. Compared to previous financial planning, the budget estimates for interest expenditure have been considerably reduced: In the period 2014-2020, these reductions will total €109 billion. The interest expenditure to tax revenue ratio is to remain slightly above 6 per cent. This is equal to the 1977 level, although the debt-to-GDP ratio is three times as high. The risk of changing interest rates is not inconsiderable in the light of average annual gross borrowing of €175 billion. However, any growth of interest expenditure would be mitigated by an extension of the lock-down period for interest rates.

2.6 Trend and structure of revenues

Tax revenues are by far the most important source of revenue for the Federal Government. According to the May 2017 tax revenue forecast, a further increase of tax revenues is expected for all public budgets.

The Federal Government's tax revenues are to rise by more than 3 per cent annually to €341.6 billion in 2021. The tax-to-GDP ratio will also increase. It is forecast to rise to 23.3 per cent of GDP at the end of the financial planning period and will thus be 0.8 percentage points higher than the actual figure in 2016 (22.5 per cent). However, due to ceding shares of VAT revenue to the states and local authorities, the Federal Government benefits ever less from this development. While its share in the total tax revenues of general government was 43.3 per cent in 2011, it has been declining ever since. The introduction of the financial transaction tax at the European level remains still uncertain.

Under the vertical financial equalisation scheme, the Federal Government gives large grants to the States. The decline attributable to the digressive scheme applicable until 2019 to the supplementary federal grants for special needs will not continue. As a result of the restructuring of the financial relations between the Federal Government and the States, the federal supplementary grants will be increased as from 2020. There will be two new types of grant: the grant to supplement municipal tax revenues and the research promotion equalisation grants. Additional expenditure items are financial reconstruction aid for the federal city states of Bremen and the Saarland. The financial volume of grants from federal tax revenues will therefore increase significantly.

In the 2018 draft budget, other revenue is estimated at €30.8 billion – reduced by aggregate losses of revenue of €2.1 billion. The biggest items in this revenue category are the other current revenues of €9.2 billion. These include administrative revenues from fees and charges, e.g. the toll for lorries (trucks), totalling €5.7 billion. The shortfall of the revenues needed to balance the budget is to be set off by a withdrawal of €8.2 billion from the reserve formed in the 2015 budget and by seigniorage of €0.3 billion. Significant proceeds from the sale of capital assets (privatization revenues) are no longer likely to occur.

2.7 Debt and debt service

The accumulated federal debt including the debt of off-budget federal entities, which totalled €1.26 trillion in 2016 is likely to change only insignificantly compared to the previous year’s figure. It has been declining slightly since 2014. The Federal Government’s debt to GDP ratio is declining more strongly and is anticipated to be once more in the range of the ratio as it stood in 2008 before the financial crisis (38.5 per cent of GDP). Nevertheless, the debts of the banking sector assumed by the Federal Government still exist. The extent to which these obligations will permanently increase the debt level can only be determined after the finalization of all financial assistance operations. With an annual average of €175 billion, gross borrowing will remain at a high level in the financial planning period.

2.8 Warranties

The Federal Government’s risk to become liable by virtue of assumed sureties, guaranties and other warranties may become a burden on the federal budget on the medium and long term. According to the 2018 draft budget, the aggregate ceiling for all kinds of warranties is to be €494.2 billion, equal to the previous year’s figure. So far, the ceilings for warranties set by the Budget Act have not been fully utilised. At year-end 2016, €364.7 billion were committed. This is equivalent an utilisation rate of 75.0 per cent.

Apart from the powers granted by the Budget Act to assume warranties, the Federal Government has given guaranties for financial market stabilisation and in favour of the European rescue packages. The latter serve to safeguard the financial assistance given to some states of the euro area. After the closure of the financial assistance programmes for Ireland, Spain, Portugal and Cyprus, the focus is on financial assistance to Greece. Whether these assistance programmes will result in burdens on the federal budget not foreseen so far will depend on the further development of the European sovereign debt crisis and cannot be reliably estimated at this time.

2.9 European fiscal rules and their national implementation

At the European level, Germany has committed itself to limiting its general government deficit (revenue deficit) and its debt level and to comply with binding fiscal rules. The reformed set of rules introduced in response to the European sovereign debt crisis has become increasingly extensive and complex. This trend may adversely affect rather than promoting compliance with the fiscal rules. In 2016, the European Court of Auditors found that, while there were detailed regulations and guidelines for the procedure to be adopted in case of an excessive deficit, there was nevertheless a lack of coherence and transparency in their application. After analysing the European fiscal rules, Germany's central bank also arrived at a critical assessment. It recommended in particular, to strengthen the fiscal rules by giving them a simple and transparent design and to make the assessment of compliance with them more targeted and less policy-driven. This may be achieved by involving an institution other than the EU Commission. We also consider it expedient to underline the seriousness of compliance with the stability goals of the European fiscal policy by a consistent application of the fiscal rules. If EU bodies hesitate for years to respond to the infringement of the rules, this may weaken the confidence in the resilience of the Monetary Union in the face of crisis.

For the structural deficit, the European fiscal compact imposes a medium-term target of 0.5 per cent of GDP. Germany has remained below this benchmark already since 2012. In its stability programme, the Federal Government expects a (structural) revenue surplus of between 0.25 and 0.5 per cent of GDP. Germany is also complying with the European requirements for reducing its debt to GDP ratio. According to the Federal Government's estimate, this ratio is to decline to 57 per cent of GDP by the end of the financial planning period in 2021, once again lower than the benchmark rate of 60 per cent of

GDP. Germany thus is among the financially most stable Member States within the European Union.

Based on the German stability programme, the Council of the European Union concludes that Germany is likely to comply with the Stability and Growth Pact. Based on the European Commission's assessment, it recommended, among other matters, that Germany enhance, at all levels of government, public investment, especially in education, research and innovation, improve the efficiency and investment-friendliness of the tax system and reduce the high burden of charges on low earners. The recommended expansion of public investments basically coincides with our position. Nevertheless, given the existing fiscal challenges, the Federal Government's leeway for action is limited. In no case should the reduction of the still high debt level aimed at under the Stability Programme be jeopardised by expenditure programmes funded by borrowing.

Germany has enshrined the ceiling of 0.5 per cent of GDP for the general government revenue deficit in its national budget legislation. By setting up the Stability Council, a national early warning system for the prevention of fiscal emergencies at federal and state level has been introduced. The Stability Council's position has been strengthened further in the course of restructuring the financial relations between the Federal Government and the federal states. As from 2020, the Stability Council will explicitly monitor compliance with the constitutional debt rule. Furthermore, there is now a legal provision requiring the analyses of the Stability Council to be performed on the basis of a uniform cyclical adjustment method. This enhances comparability and transparency of the analyses carried out by the Stability Council. We find it deplorable that, in the course of the restructuring, it was not possible to confer upon the Stability Council the power to sanction infringements to help better enforce its recommendations.

The Federal Government must have a special interest in the targeted implementation of the budget oversight procedure because, in comparison to the other levels of government, its share in the general government deficit is significantly higher. In view of the expenditure on refugees and the general financial concessions of the Federal Government in connection with the restructuring of the Federal/State financial relations, its leeway for action seems to be largely exhausted. The Federal Government’s priority should now be to secure its long-term fiscal sustainability. If it does not succeed in this, Germany may lose its role as anchor of stability within the European Union.

Departmental audit findings

Federal Ministry of the Interior

3 Generous rules on academic teaching commitments restrict teaching capacities

The Federal University of Public Administration unnecessarily restricted its teaching capacity. The University's approach does not comply with the agreement of the Standing Conference of the Ministers of Education and Cultural Affairs of the Länder (federal states) in the Federal Republic of Germany on the teaching commitments at universities. As a result, this reduces staff available for teaching programmes.

Teaching staff at the Federal University of Public Administration generally have the duty to teach 18 teaching/class contact hours of 45 minutes each per week. The University determined that two weeks each for examinations and committee work without compensation were reasonable for teaching staff. If teaching staff spend additional time on examinations and committee work, they receive a time credit (hours beyond their teaching load). Subsequently, the teachers may deduct these extra hours from their regular teaching commitments. Hours beyond standard teaching load were equivalent to three full-time employees annually and to staff expenditure of approximately €300,000.

This is neither adequate nor efficient. It does also not comply with the agreement of the Standing Conference of the Ministers of Education and Cultural Affairs of the Länder (federal states) in the Federal Republic of Germany on the teaching commitments for professors at universities. Pursuant to this agreement, the time needed for examinations has already been taken into account in the standard teaching load of 18 teaching/class contact hours per week.

In 2014, the Public Accounts Committee of the Budget Committee of the German Parliament had already urged the Federal Ministry of Finance to ensure that the volume of teaching commitments in its Departmental Branch of Financial Administration of the Federal University of Applied Administrative Sciences complied with the agreement. The Federal Ministry of Finance fulfilled that demand in early 2017.

We also hold that the Federal Ministry of the Interior should also take prompt action to refine the rules for its own area of responsibility.

Federal Ministry of the Interior

4 Insufficient monitoring of consultancy work in large-scale IT projects

The Federal Ministry of the Interior did not adequately plan, monitor and control consultancy work in two large-scale IT projects. For instance, the Ministry remunerated the consultants according to the amount of work without evaluating the work done. Since the Federal Ministry of the Interior did not set detailed key performance indicators for the consultants, it should have thoroughly monitored their work.

The Federal Ministry of the Interior intends to update, centralise and enhance the security of the federal IT system by means of the two large-scale projects "Networks of the Federal Government" and "Federal IT Consolidation". For this purpose, the Ministry commissioned consultants. It needs to ensure that deadlines are met, cost limits are complied with and project results are of the required quality.

In 2015 and 2016, the Ministry arranged for being charged according to the amount of work done in 109 out of 110 consultancy contracts. However, these contracts did not specifically define the expected success. As from 2017 until 2022, the Ministry intends to pay more than €230 million for external consultants for the two projects.

The Ministry planned consultancy work only in broad terms. It did not fully determine how much time the consultant needed to carry out what tasks and what the results were. It did also not establish a quality management system for large-scale IT projects which also included consultancy work. The Ministry evaluated the work done by the consultants without consistent criteria. Often, there was a complete lack of evaluation criteria. In many cases, it was ambiguous whether the service provided by the consultants was adequate.

We requested the Federal Ministry of the Interior to efficiently use the working hours of external consultants. We demand that the Ministry continuously plan and monitor consultancy work, especially when consultants are paid according to the amount of work. We expect the Ministry to establish a quality management system and make its application mandatory for large-scale IT projects.

Federal Ministry of Finance

5 IT project costs almost four times the amount budgeted

The Supplementary Pensions Agency for Public Employees carried out an inefficient IT project. The Agency needed more than double the time estimated for implementing a new technical network of hardware and software components. The costs increased by almost four times from €30 million to €115 million. The Federal Ministry of Finance, which exercises oversight of the Agency, is expected to ensure that these shortcomings are not repeated in future IT projects.

A technical network of hardware and software components which enables the development and execution of application programs is referred to as IT platform. The Supplementary Pensions Agency for Employees decided to renew its out-dated IT platform. In 2007, the Agency merged some pre-projects into the "Phoenix" project. This project was expected to cost €30 million and to be concluded by year-end 2009.

In the course of the project, the Agency noted that the new IT platform did not enable it to implement some technical requirements as expected. We attribute this to the fact that the Agency did not adequately define technical requirements before project launch. Thus, the project was extended until year-end 2012. In this period, project costs increased to €115 million. The fact that the Agency studied one IT solution only before, during and at project completion also contributed to this cost increase. The Agency did not take into account available options to ensure an efficient approach.

In light of the serious shortcomings found, the Federal Ministry of Finance will need to provide more vigorous oversight in the case of future projects.

Federal Ministry of Finance

6 Illegal fuel trade causes high fiscal damage

Diesel-like mixtures are illegally traded as fuel, resulting in fuel tax fraud amounting to several millions of euros. Germany serves as a hub for illegal fuel trade in Europe. The Federal Ministry of Finance has underestimated the problem for more than a decade. Up to now, it has not taken adequate steps to combat this type of organised crime.

Designer fuels are mixtures that consist of more than 70 per cent diesel and of other substances. They are mixed in such a way that they have similar characteristics to diesel and thus can be used as fuel. Perpetrators declare them to be industrial oils which are tax-free.

While diesel comes under customs oversight and is taxable, this does not apply to designer fuels. Tax exemption for designer fuels applies only as long as they are not declared or sold as fuel. Otherwise, the fuel tax – such as in the case of diesel – of 43 cents per litre applies. If designer fuels are illegally sold as diesel, the traders commit fuel tax fraud.

Tax fraud in connection with designer fuels has already been known since 2002. The scope of the resulting fiscal damage in Germany can only be estimated but according to the calculations of the Customs Criminological Office it may be an amount in the three-digit million euro range. This type of crime has been increasing for years. As a result, we expect an increasing amount of fiscal damage.

We hold that the actions taken by the Federal Ministry of Finance are not sufficient to sustainably reduce this type of crime.

We demand that the Federal Ministry of Finance take action at national or European level so that designer fuels become subject to customs oversight and that illegal trading in Germany is stopped. Furthermore, we request that, in order to combat this organised type of crime, staffing needs in the customs administration be reviewed and adjusted, where necessary.

Federal Ministry of Economics and Technology

7 Federal Office for Economic Affairs and Export Control has for years ignored risks of its payment-relevant IT systems

The Federal Office for Economic Affairs and Export Control paid a total amount of several hundreds of millions of euros through IT systems operated improperly. In spite of a commitment to the contrary, it did not eliminate weaknesses known since 2014. Weaknesses of the internal control system facilitated accounting and payment errors.

Most managers of federal budget funds are linked to the Federal Government's central accounting system via IT systems. They have to guarantee that controls prescribed by budgetary law are in place to ensure an orderly and secure operation of their IT systems.

Each year, the Federal Office for Economic Affairs and Export Control pays grant funds in the range of hundreds of millions of euros by means of IT systems. As early as in 2014, we found that the operation of two of the Office's IT systems for the disbursement of grants did not comply with the applicable regulations. A follow-up audit carried out in 2017 revealed the continued lack of key procedural documents, e.g. official instructions. Furthermore, the Office had not complied with regulations providing for the separation of functions in the development and maintenance of the systems and in processing.

Sampled vouchers showed such errors as the remittance of grant funds to wrong accounts. The Office argued that this was mainly attributable to individual processing errors and unavoidable in mass procedures. We consider this assessment unconvincing as long as the Office has not defined, documented and implemented structured control programmes such as the cross-checking principle.

The Office must now comply with the provisions of budgetary law and develop adequate internal control systems for its procedures.

Federal Ministry of Labour and Social Affairs

8 Lacking oversight: federal states' accounting errors raise federal expenditure on basic security in old age

The Federal Ministry of Labour and Social Affairs did not check whether serious accounting errors in basic security in old age and in case of reduced earning capacity found in some states can also be found in other states. Furthermore, it does not ensure that the federal states spot-check the work of the authority in charge of providing basic security.

The basic security in old age and in case of reduced earning capacity (basic security) supports people in need who reached the retirement age of the statutory pension fund or who are permanently fully unable to work. The federal states provide the basic security on behalf of the Federal Government. Administrative districts and independent cities but also supra-local basic security authorities are in charge of that task. The Federal Ministry of Labour and Social Affairs needs to supervise how the federal states provide basic security.

The Federal Government fully reimburses the federal states for net expenditure on basic security cash benefits. Net expenditure is gross expenditure minus income.

We found significant shortcomings in net expenditure accounting in selected federal states during our audit. Due to these flawed accounting practices of the federal states, the Federal Government incurred increases in expenditure of approximately €10 million. The Ministry did not check whether the other federal states appropriately accounted for the expenditure even though such a check was obviously needed. It did not adequately carry out its oversight responsibilities vis-à-vis the federal states.

We requested that the Ministry supervise net expenditure accounting consistently and more thoroughly. We expect the Ministry to agree with the federal states that they regularly spot-check the work of the basic security authorities.

Federal Ministry of Labour and Social Affairs

9 Ambiguous regulations on jobseekers’ absences from place of residence– job centres treat entitled individuals inconsistently

After more than six years, the Federal Ministry of Labour and Social Affairs has still not clearly defined how an employable person entitled to benefits needs to be available for job centres. The Ministry failed to put into force new statutory provisions adopted by Parliament in 2011concerning absences. As a consequence, the Ministry tolerates that the job centres apply different criteria to entitled individuals.

Individuals entitled to basic income support for jobseekers (entitled individuals) need to be available for the job centres pursuant to Book II of the Social Security Code. They need to stay close to the job centres to be able to immediately take up any acceptable employment. In 2011, Parliament passed new statutory provisions on temporary absences of entitled individuals. However, the new provisions have not yet come into force because the Federal Ministry of Labour and Social Affairs did not promulgate a statutory instrument (ordinance) to regulate the details.

That is why the job centres have been using the former regulations and various guidances issued by the Federal Employment Agency. These regulations are ambiguous and not easy to understand. Moreover, the guidance of the Agency only applies to some of the job centres. As a result, the job centres do not use consistent criteria for permitting absences.

We request that the Federal Ministry of Labour and Social Affairs put into force the new statutory provisions passed in 2011 as soon as possible and thus harmonise the decisions made by the job centres. The ordinance should consistently and clearly define the area in which entitled individuals may stay as well as the duration of and the requirements for absences.

Federal Ministry of Labour and Social Affairs

10 Long period of entitlement to unemployment benefit II – little support by job centres to self-employed people

For many years, job centres have not made adequate efforts to place self-employed beneficiaries of unemployment benefit II into jobs. As a result, the entitled individuals continued to receive unemployment benefit II.

If self-employed people earn a low income, they are also entitled to unemployment benefit II. In accordance with applicable law, they need to seize every opportunity to end their need for assistance so that they no longer need unemployment benefit II. The job centres need to support the self-employed people and to also place them in dependent employment if necessary (principles of rights and responsibilities).

We found that the job centres did not adequately fulfil their duty so that entitled individuals continued to receive unemployment benefit II. Even if the entitled individual only earned a low income and the self-employment did not offer realistic career prospects, the job centres tolerated this situation. The income of self-employed beneficiaries of unemployment benefit II remained permanently at a low level or even decreased in 80 per cent of the cases reviewed. In many cases, the self-employed people earned a monthly income of less than €450 and received unemployment benefit II for more than four years.

For a continued granting of benefits, it was usually enough for the job centres – in some cases for years – that the self-employed people stated that they expected to be able to increase their income in the future. Documents to prove income were held only by individual job centres. Therefore, we cannot exclude that self-employed people received benefits without fulfilling the respective requirements.

In our opinion, the job centres need to step up their efforts to place self-employed people who have already received unemployment benefit II for some time. For this purpose, the Ministry needs to ensure in its oversight of the Federal Employment Agency (Agency) that the Agency enforces and complies with the applicable law and the respective directions. The responsible federal state authorities which supervise the municipal authorities of basic security benefits for jobseekers are also expected to ensure compliance.

However, if the efforts of the job centres, the authorities of which they are part and the oversight authorities fail to address this situation, we consider a legal provision to be appropriate. The purpose of such provision is to be that job centres place self-employed beneficiaries more speedily so that they no longer receive unemployment benefit II for an unreasonably long period. In line with a proposal of the Agency, self-employed beneficiaries of unemployment benefit II could thus be required after a certain period of time to accept any reasonable employment and to participate in all reasonable integration programmes.

Federal Ministry of Labour and Social Affairs

11 Pension insurance office intends to spend millions on unnecessary pensioners’ certificates

Within the next five years, the German pension insurance office intends to spend €9 million for new pensioners’ certificates. However, the retirees have no need for them. Furthermore, we hold that the production of the certificates without competitive bidding poses a problem.

The 21 million retirees can provide evidence for their status by means of a pensioner’s card. The current pensioners’ certificates adequately serve this purpose and with annual costs of €25,000, they do so also efficiently. The German pension insurance office has so far

- not been able to name any case in which the card was not recognised; and
- only been able to name one proven case in which someone complained about the paper format.

Therefore, we recommend that the German pension insurer does not issue the new pensioners’ certificates. We hold that excess cost of millions of euros could be saved that way.

Federal Employment Agency

12 €55 million paid for vacant places in training programmes

The Federal Employment Agency did not fill all places of pre-vocational training programmes. Between September 2013 and December 2015, the Agency bought places for almost €55 million throughout Germany without filling them.

The Federal Employment Agency (Agency) can provide assistance to young people for making the transition between school and work by means of pre-vocational training programmes. The Agency reimburses the costs incurred by the providers of training programmes. A framework agreement with a term of two years developed by the Agency serves as the basis. As a rule, the young beneficiaries participate in the pre-vocational training programme from autumn until summer of the following year. For being able to respond flexibly to fluctuating numbers of participants during the term, it is possible to have more or fewer participants than the number of places agreed. However, the Agency needs to take and pay for a minimum number independent of whether the places have actually been filled.

We reviewed the capacity utilisation of pre-vocational training programmes. From September 2013 to December 2015, the Agency spent a total of €425.7 million on pre-vocational training programmes throughout Germany. Expenditure of up to €54.5 million (12.8 per cent) for vacant places could have been avoided if the Agencies had made better national plans.

We noted with concern that the Agency purchased more pre-vocational training programmes than needed. Thus, the Agency failed to take action when the training programmes were not filled which resulted in significant cost on vacant places. We demand that in the future the Agency reasonably estimate the places needed for the participants. The Agency needs to increase the number of participants in the pre-vocational training programmes and thus decrease the expenditure on vacant places. The Agency is also expected to adapt the term of the framework agreements to the typical duration of the programme of ten months.

Federal Ministry of Transport and Digital Infrastructure

13 Expenditure on federal waterways' construction projects lacks transparency

The Federal Ministry of Transport and Digital Infrastructure does not adequately account for the expenditure of many federal waterways' construction projects in the federal budget. The Ministry refrained from regularly updating the expected overall project expenditure. As a result, the Ministry makes it difficult for itself and Parliament to manage the funds for important construction projects.

In the 2017 federal budget, the Federal Ministry of Transport and Digital Infrastructure itemised a total of 35 federal waterways' construction projects. The expected total expenditure has been carried forward without changes for many years. For example, the Ministry has estimated expenditure on a construction project to be €493.4 million for years. During the same period, the construction price index for road construction increased by more than 50 per cent. Furthermore, in the case of overall projects with a long duration, the Ministry did not state what components of the project had already been finished and what the trends in expenditure of individual projects were.

According to the justification provided by the Ministry, the Ministry carried forward the expenditure as needed instead of using the construction price index. It intends to break down long-term projects into individual segments.

The Government's bill on the 2018 federal budget includes this breakdown for the first time. We hold that this is only a first step and demand that the expected overall expenditure on the construction projects be updated regularly.

Federal Ministry of Transport and Digital Infrastructure

14 Millions of revenue forgone for use of federal waterways

For more than 17 years, the Federal Ministry of Transport and Digital Infrastructure has failed to increase the most important fees for using the federal waterways. In failing to do so, the Ministry does not comply with its obligation under budgetary law to timely and fully collect revenue. The Ministry does also not adequately respect the principle that fees need to cover the costs and need to be appropriate. By now, lost federal revenue exceeds €19 million annually.

Pursuant to the Federal Budget Code, the law on fees always needs to be kept up to date. The rates need to be adjusted regularly.

As a result of internal studies and reports of outside experts, the Ministry has known for many years that the most important fees for using the federal waterways are far too low. Nevertheless, initiatives to increase the fees have already failed at Ministry level. Repeated requests of the Public Accounts Committee of the Budget Committee of the German Parliament did also not change anything for the better.

The Ministry referred to the work underway for the reform of the law on fees and the development of a special fee regulation. This regulation is designed also to include the use of the federal waterways. The Ministry needs to have the regulation developed by no later than October 2021. Even though an adjustment of the previous rate of fees is still possible, the Ministry does not intend to do so. Thus, the Ministry failed to take action for the federal budget revenues of over €19 million is annually foregone.

We demanded that the rate of fees for using the federal waterways be updated immediately. To wait any longer is neither legally justifiable nor plausible in consideration of the Ministry not having taken action for years.

Federal Ministry of Transport and Digital Infrastructure

15 Cost-effectiveness of the upgrading of a federal motorway not proven – savings potential of €110 million

The Federal Transport Ministry is planning to upgrade federal motorway A 8 to six lanes between the valley of the river Inn and the border. The construction of this 70 kilometres long motorway section will cost €1.2billion. We do not consider it necessary to have the whole motorway section upgraded to six lanes as long as this is not proven to provide good value for money. The Ministry could save at least €110 million.

The Federal Transport Ministry plans to upgrade federal motorway A 8 to six lanes between the valley of the river Inn and the border. The construction cost totals €1.2 billion. The Ministry found that the cost of upgrading is higher than the benefit and that therefore the project provides poor value for money. Nevertheless, it stuck to its plan.

We noted with concern that the Ministry did not take the differing traffic loads on this motorway section into account. We hold that upgrading to six lanes is necessary only from the valley of the river Inn to Chiemsee. The traffic load on the section between Chiemsee and the border only justifies building four lanes with temporary permission of hard shoulder running for the peak traffic loads. The Ministry could thus reduce construction cost by at least €110 million, thus enhancing cost effectiveness.

The Ministry rejects this solution, invoking statutory provisions for the upgrading to six lanes and disadvantages for traffic safety, if only four lanes were built and temporary hard shoulder running was permitted.

We uphold our opinion that a four-lane construction with temporary permission of hard shoulder running will be an environmentally friendly and cost-effective alternative for the section between Chiemsee and the border. The statutory provision does not impede a change of plan. The Federal Trunk Road Upgrading Act requires the Ministry to regularly consider the need for adjusting plans. Given especially the poor value for money provided by upgrading to six lanes, the Ministry is needs to exploit all savings potentials.

We therefore expect the Ministry to assess traffic quality including safety aspects and to calculate and prove the cost-effectiveness of this alternative.

Federal Ministry of Transport and Digital Infrastructure

16 Costly upgrading of a crossing of federal road causes additional costs of €10 million to the Federal Government

Although value for money is not proven, the Federal Transport Ministry insists on expensively upgrading a crossing of federal road B 2 in Weißenburg. This causes excess costs of €10 million to the Federal Government. We had requested the Ministry to study options for optimising the existing crossing in place. That crossing meets all requirements of traffic safety and traffic quality.

The roadworks administration of the Free State of Bavaria intends to expensively upgrade a crossing of federal road B 2 in Weißenburg. To this end, B 2 with two lanes is to be run in a trough beneath a roundabout above. The plan calls for 14 new structures, a groundwater tank and technical service facilities. The construction cost is estimated at €16.6 million.

We held that this solution was clearly too expensive and not cost-effective. We recommended that the Ministry study options for optimising the existing crossing. This may be achieved by widening the crossing roads and by installing a state-of-the-art traffic light system that will safely guide vehicles turning left. This will cost significantly less.

The Federal Transport Ministry has admitted that such optimisation can ensure adequate traffic quality and that costs could be saved. The Ministry estimated the cost of this solution at €3.7 million. Nevertheless, the Ministry continues to pursue the expensive upgrading option. It sought to justify this by the outstanding importance, the high upgrading standard and traffic safety.

We uphold our findings. Optimising the crossing meets all requirements of traffic safety and traffic quality. It avoids additional costs to the Federal Government of more than €10 million. We expect the Ministry to comply with the principles of efficiency and economy in connection with the upgrading of the said crossing. Before deciding, it will have to study the cost-effectiveness of the upgrading options and underpin its decision by proving that it provides good value for money.

Federal Ministry of Defence

17 Federal Armed Forces: efficient fuel supply to ships

Contrary to the promises made by the Federal Ministry of Defence in 2012, the Federal Armed Forces continued to not efficiently supply fuel to their ships. They also tolerated avoidable expenditure on processing fuels and disposing of other liquids.

The Navy requires fuel for operating its ships and boats. As from 2015, we reviewed whether the Navy addressed earlier shortcomings in managing marine fuels. In doing so, we again found several shortcomings.

The Federal Armed Forces could have ensured more competition by stipulating different lots in transport contracts for fuels. Since only one supplier for one lot remained after excluding one offer, the Federal Armed Forces needed to have checked whether the invitation to tender achieved good value for money. It might have been necessary to have the invitation to tender cancelled. Since the Federal Armed Forces did not resort to collective transportation (simultaneous supply of several ships in one port and supply of several locations in a "round trip") and tolerated unnecessary long transportation routes, they incurred avoidable expenditure.

When the Federal Armed Forces were looking for a supplier of waste management services, they inadmissibly restricted competition by requesting an own pier – that is a longer landing place extending into the sea – even though this was unnecessary. The Federal Armed Forces also acted inefficiently when they repeatedly tolerated the contamination of large quantities of fuels.

Therefore, we recommend that:

- the contracts for the transportation of marine fuel and waste management services be terminated as soon as possible;

- the need of the Federal Armed Forces for these services be determined;
- the services be properly put out to tender; and
- attention be paid to an efficient approach when using services.

Federal Ministry of Defence

18 Federal Armed Forces equipment not used as provided for

The German Federal Armed Forces procured transport and storage containers for mobile satellite reception systems and has not used them for that purpose for five years. The containers will likely not be used for transport purposes in the future. In many cases, we have already objected to the Federal Armed Forces procuring equipment without a stated need.

In 2012 and 2013, the German Federal Armed Forces procured 20 transport and storage containers for mobile satellite reception systems for €450,000. These containers have their own power supply, light and heating.

In 2016 and 2017, we found that the Federal Armed Forces did not use the containers at all at some of the locations and at others they did only use them as storage containers. They had never been used for transport purposes. According to the justification provided by the Federal Armed Forces, the transport capacity to the mission areas was limited.

Thus, the Federal Armed Forces procured equipment without justified need as in many cases in the past. The Public Accounts Committee of the Budget Committee of the German Parliament has already repeatedly requested that the Federal Ministry of Defence first analyse its needs in future, while taking into account what is technically feasible.

We expect the Federal Armed Forces not to procure equipment in the future unless there is a real need.

Federal Ministry of Defence

19 Federal Armed Forces Medical Corps: organisation of physiotherapy only gradually improved

In 2013, the Federal Ministry of Defence pledged to ensure transparency in prescribing physiotherapy and to enhance the efficiency of the Federal Armed Forces' own physiotherapy facilities. However, the Federal Armed Forces did not take major action until we reviewed the matter again in 2016.

Military personnel of the Federal Armed Forces are offered physiotherapy under the free medical care scheme. The Federal Armed Forces run their own facilities for that purpose. Military personnel can also be treated by civilian therapists.

The cost for treatments carried out by civilian therapists amounted to €23 million in 2012. This means that the average per-capita expenditure has more than doubled since 2002. We analysed the causes for this trend in health expenditure in 2013. We objected to an excessive prescription of treatments encouraged by a lack of transparency and monitoring. We found that at the Federal Armed Forces' physiotherapy facilities efficient organisation was lacking.

The Federal Ministry of Defence acknowledged the weaknesses. In our 2014 annual report (Bundestag printed paper 18/3300 No. 51), we recorded various actions by which the Federal Armed Forces intended to improve the prescription procedure and enhance the efficiency of their physiotherapy facilities.

In a 2016 implementation status query, we found that the Federal Armed Forces had largely not kept their promises In fact, they had not taken major action until we reviewed the matter. Even though they reduced the number of their own physiotherapy facilities, performance indicators were still lacking. Instead of being used more often, some facilities were used less than before. The annual treatment cost by civilian therapists had further increased and amounted to €25.7 million in 2016 (+11.7 per cent compared to 2012).

We noted with concern that the Federal Armed Forces were reluctant to implement the promised improvements in prescribing physiotherapy. We hold that a period of more than three years for implementing a new prescription form is unacceptable. We expect the Federal Armed Forces to take rigorous action to address the problems stated.

Federal Ministry of Defence

20 No good value for money provided by Armed Forces aircraft maintenance cooperation arrangements

The Federal Ministry of Defence did not assess whether the joint maintenance of some types of helicopters and airplanes carried out by the Federal Armed Forces and companies provided the expected benefits and good value for money. Such cooperation arrangements have existed for more than a decade. The Federal Armed Forces did not reasonably deploy their military personnel in the cooperation arrangements and thus could only develop and maintain the skills needed to a limited extent.

The Federal Armed Forces cooperate with companies in servicing, inspecting, repairing and improving (maintaining) the Tornado and Eurofighter combat aircraft and the UH Tiger and NH 90 helicopters. In these cooperation arrangements, military personnel perform maintenance work under the guidance of companies. By doing so, the Federal Armed Forces seek to identify and remove damage to helicopters and airplanes to a large extent on their own, in particular in missions abroad. Furthermore, they intend to be able to better identify and assess what is needed for operating and further developing the helicopters and airplanes.

Some cooperation arrangements have existed for more than a decade and are of increasing importance for the Federal Armed Forces. Nevertheless, the Federal Armed Forces failed to check whether the cooperation arrangements served to meet their targets. Thus, the Federal Ministry of Defence lacks key data for measuring the performance of cooperation arrangements and for developing them.

The Federal Armed Forces did not define the tasks their personnel were expected to perform in detail in order to build and maintain the skills needed for the maintenance. They did not always provide cooperation arrangements with appropriate military personnel. As a result, the Federal Armed Forces did not fully contribute to the maintenance work and could build and maintain the skills needed to a limited extent only.

The Federal Ministry of Defence admitted that it did not fully check the joint work for their benefits and efficiency. Even though the Ministry announced to have the benefits and efficiency of individual cooperative efforts checked, it had not submitted any results so far. The Ministry confirmed that the cooperation schemes were not always appropriately staffed. However, it did not believe target achievement to be jeopardised.

We expect the Federal Ministry of Defence to promptly develop consistent principles and criteria to measure performance of cooperation arrangements. On this basis, the Federal Armed Forces is expected to check the benefits and efficiency of cooperation arrangements. Moreover, the Federal Ministry of Defence needs to ensure that the Federal Armed Forces organise cooperation arrangements as required and provide adequate staffing.

Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety

21 €50 million to remedy construction defects not transparently disclosed in the federal budget for 24 years

The Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety intends to have construction defects at a Federal Ministry office at Berlin remedied for €50 million by 2024 without transparently disclosing this item in the federal budget. Instead of taking an overall approach to the need for renovation, the Ministry has so far had the defects remedied on a case by case basis. To fund these individual works, the Ministry has drawn on diverse budget titles.

Five years after the move of the government, experts identified serious fire protection shortcomings at the Berlin office of the Federal Ministry for Economic Affairs and Energy. Since the warranty period had already expired, the Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety remedied a number of shortcomings at the expense of the Federal Government. In 2017, the Ministry assessed the overall need for renovation to be €50 million. It intended to have the shortcomings remedied by 2024. At first, the Ministry funded the remedial work from its aggregate budget title for "Construction works for accommodating the Federal Government outside the Parliament district at Berlin". Furthermore, it used funds of the economic stimulus package II. Since the 2011 federal budget, respective funds have also been appropriated from the departmental budget of the Federal Ministry for Economic Affairs and Energy. In line with the principle of reliability and clarity of the budget, however, expenditure on the same purpose is not to be earmarked under diverse budget titles.

The Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety limited budget transparency. Furthermore, we doubted the efficiency of remedying shortcomings on a case by case basis over a period of 24 years.

We demand that the Ministry disclose the overall need for renovation and the capital expenditure appraisal. Large-scale construction works should generally be budgeted individually or explanatory notes should be considered as binding in case of aggregate budget titles in order to respect the right of Parliament to control the budget. Therefore, a specific amount needs to be earmarked for construction works. Subsequent expenditure on construction works also needs to be transparently allocated to these works in the federal budget.

Federal Ministry for Family Affairs, Senior Citizens, Women and Youth

22 Excess grants paid due to major shortcomings in allocating funds to a beneficiary

The Federal Ministry for Family Affairs, Senior Citizens, Women and Youth granted excessive lump sums to a beneficiary for a project. That way, the beneficiary was able to build up inadmissible reserves totalling several millions of euros. Furthermore, the beneficiary did not comply with public procurement law by awarding a service contract for "project controlling" without public invitation to tender. The Ministry did not step in to stop the beneficiary from doing so.

The Federal Ministry for Family Affairs, Senior Citizens, Women and Youth granted more than €12 million to an educational institution in the legal form of an association for a multi-year project aimed at providing advanced training to 4,000 professionals from 2011 to 2015. The training was fully grant-funded and at the same time the association received lump sums per participant day for the training offered. However, the applicable funding rules only permit partial funding and a significantly lower lump sum. The excessive lump sums enabled the association to build up inadmissible reserves of more than €2 million. The reserves were not identified until our audit since the relevant authority did not check the proofs of use funds submitted by the association to ascertain whether the amount of the lump sums was appropriate.

Even though the Ministry demanded the recovery of funds, it waived half of the interest amounting to €80,000. However, such a waiver of the Federal Government may only be used as a "last resort" if interests cannot be deferred or paid in instalments.

The association with its office in northern Germany awarded the service contract for "project controlling" to one of its honorary members of the executive board who lives in the Bonn area. The association did not comply with funding conditions by choosing not to call for public tenders. During the project term, this resulted in expenditure totalling €575,000 for fees and additional significant travel costs. The Ministry did not detect this non-compliance until the end of project run even though this resulted in a major benefit for the honorary member of the association’s executive board. Furthermore, we doubted that the service contract was necessary. In a second, current project part the association managed without a full-time controlling expert on a fee basis even though the number of professionals to receive advanced training now is twice the earlier number.

We requested that the Ministry comply with the funding conditions and lump sums stipulated in its funding rules. If the Ministry charges interests payments, it needs to comply with the budgetary provisions. Furthermore, the Ministry needs to ensure that the beneficiaries comply with public procurement requirements.

Federal Ministry of Education and Research

23 Funding of research institutions – Federal Ministry must review the audit of the use of funds

Each year, the Federal Ministry of Education and Research gives grants in the total amount of €4 billion to non-university research institutions. Although the Ministry must obtain assurance about the expedient and efficient use of these funds, it largely relies on private-sector auditors. The Ministry usually accepts the opinions expressed in general terms by these auditors and makes too little use of its own staff for obtaining a full picture of the use of the funds. For instance, it largely waives field work on the premises of the grant recipients.

We noted with concern that the Ministry does not adequately comply with its obligation to review the use of funds adequately and in line with applicable regulations. The duty to review the use of grant funds is incumbent on the grantor and may not be replaced by a review carried out by third parties. Only the grantor is able to assess, on the basis of its requirements and goals, whether the grant funds have been used in accordance with the specified purposes and in a way providing good value for money.

The Ministry did not agree to our findings, arguing that it did not at all shift the review of the use of funds to third parties but used the private-sector auditors to obtain additional indicators as basis for its own work. It did by no means adopt the private-sector auditors' findings but carried out a review of its own. The Ministry admitted that it might not have adequately documented its work. It intends to better meet its documentation duty in the future.

We are not convinced by the Ministry's statements. We urged the Ministry to carry out its own responsible and transparent assessment of the use of grant funds given to the research institutions. In future, the Ministry should

- no longer automatically adopt the findings developed by the private-sector auditors;
- carry out its own audit work to the extent necessary, focusing on high-risk issues and using all available information for its assessment;
- carry out field work and ensure adequate review quality and
- document the findings in a comprehensive and meaningful way.

General Fiscal Administration

24 Non-compliance with tax-related duties should be sanctioned more consistently

For many years, tax offices have not checked compliance with tax-related duties. In addition, legal uncertainties and lengthy reviews impede the consistent sanctioning of non-compliance with tax-related duties. The Federal Ministry of Finance should take speedy corrective action.

The VAT Act provides for fines to sanction non-compliance with tax-related duties. For instance, traders do not comply with their duties, if they do not issue an invoice or do so belatedly, do not observe retention periods or fully or partly fail to pay VAT to the tax office when due.

As early as in 2008, we found that the tax offices did not check whether non-compliance with tax-related duties was to be sanctioned. The Federal Finance Ministry then promised to press for awareness campaigns to be launched by the federal states at the local tax offices and remove legal uncertainties. During a follow-up audit in 2015, we found that the weaknesses still persisted. Tax office staff rarely paid attention to legal provisions calling for sanctions and actually did not implement these provisions.

Given that the problems with the application of sanctions have been known for years, we find it unacceptable that no sizable improvements have been made in procedures for imposing fines for non-compliance with tax-related duties. The Federal Finance Ministry should therefore urgently press for a consistent implementation of the provisions on fines and arrange for the necessary legislative amendments.

General Fiscal Administration

25 Monitoring system can hardly prevent losses of tax revenue

The Federal Ministry of Finance has so far not succeeded in fully securing VAT payments for goods or services delivered from other EU states. The monitoring system used for this purpose in the last 25 years does not cover most farmers who are subject to flat-rate taxation ('flat-rate farmers'). Losses of tax revenue can therefore hardly be prevented.

Where German traders purchase goods or services from other EU Member States, they owe VAT for these deliveries. In order to secure the tax payments of the traders, the tax administration has for 25 years used a computerised monitoring system by which the deliveries declared by traders in preliminary and final VAT returns are checked against control data from other EU Member States. Such checks have been carried out annually since 1993 and, in addition, at quarterly intervals since 2016.

Using flat-rate farmers as example, we checked as to whether the monitoring system can prevent losses of tax revenue. When devising the monitoring system, the Federal Ministry of Finance expressly selected the flat-rate farmers as a target group.

We found that, as a rule, the monitoring system does not effectively cover flat-rate farmers. It is based on data which the farmers are not compelled to record. As a result, the annual checks cover only a small portion of the flat-rate farmers. The quarterly checks are even fully useless. For the last nearly 25 years, it has hardly been possible to prevent losses of tax revenue for flat-rate farmers. In view of the large number of 181,000 flat-rate farmers, we find this situation unacceptable.

We have urged the Ministry to ensure coverage of the flat-rate farmers by means of the VAT identification letters already in place in the tax offices. This would ensure that all flat-rate farmers are covered by both the annual and quarterly checks under the monitoring system.

General Fiscal Administration

26 Tax offices lack IT support for processing tax returns of large partnerships

As from 2011, tax returns for partnerships are filed electronically. However, the tax offices are unable to electronically receive and process tax returns where the number of partners exceeds the level of 500. The lack of IT support causes high administrative burden and leads to losses of tax revenue.

We noted with concern the lack of IT support. It is no longer acceptable that the tax administration is unable to fully implement the legal provisions because of technical weaknesses. For nine years now, the Federal Government and the federal states have had the time to address the problem.

The lack of IT support ties up valuable human resources in the tax offices. The proper inspection under aspects of tax law thereby loses priority and tax revenue is lost. For instance, it took one tax office more than one year to process the tax return of a large partnership. It had to manually enter 380 pages of hard copy tax returns. The resulting errors caused losses in tax revenue of more than €400,000.

We urged the Federal Finance Ministry to take steps, in conjunction with the federal states, to make sure that the tax offices are provided with the necessary IT support immediately.

General Fiscal Administration

27 Abolish tax privileges of tobacco industry

Tobacco products which the manufacturers give free to their employees are exempt from tobacco tax. This exemption is no longer justified, is contrary to tax equity and questionable in terms of health policy. Since 1989, we have repeatedly recommended that the exemption be abolished. The rejection of our recommendation by the Federal Finance Ministry has resulted in losses of tax revenue in the total amount of €171.7 million.

Cigarettes and cigars are subject to tobacco tax. Tobacco products given free by manufacturers of tobacco products to their employees are exempt from tobacco tax. Nationwide, this benefits about 11,000 employees in the tobacco industry. For instance, an employee receives 600 cigarettes per month (which is equivalent to about 31 packets).

The tax exemption was introduced after the First World War. It was to reduce theft by employees and boost working morale. This motive is now obsolete. Protecting the tobacco industry against theft by their employees or boosting their working morale is not the task of the taxpayer. By using this justification, the entire retail trade could claim tax exemption. Since only a small group benefits from the tax treatment, this is an issue of tax equity. Finally, the tax exemption is questionable in terms of health policy. It contradicts the goals of the Federal Government and WHO, i.e. to reduce the proportion of smokers in the population.

The Federal Finance Ministry has spoken out against abolishing the tax exemption for tobacco products given free by tobacco manufacturers to their employees, arguing that the reasons for the tax exemption were still valid and that the infringement of tax equity was negligible.

The Ministry's opinion is not convincing. We therefore uphold our recommendation to abolish the tax exemption. We have made recommendations to this effect several times since 1989. The Ministry's refusal to act has caused losses of tax revenue in the total amount of €171.7 million.