

# AUDIT REPORT

Riga

12.12.2014

No 2.4.1-25/2014

## **Parallel regulatory audit on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”**

### **Legal justification of the audit**

1. Pursuant to Article 2 of the State Audit Office Law and the audit engagement No 2.4.1–25/2014 of 16.06.2014 of the Third Audit Department, a regulatory audit was performed on analysis of errors in public procurement within the Structural Funds programmes.
2. The audit was performed within the frameworks of the Working Group on Structural Funds IV of the European Union (hereinafter: the EU) Contact Committee which was mandated to perform parallel regulatory audit on “Analysis (of types) of errors in EU and National public procurement within Structural Funds programmes” (hereinafter: the Parallel Audit) during the time period from April 2014 up to October 2015 in cooperation with 10 supreme audit institutions. The Parallel Audit is headed by representatives of supreme audit institutions of the Netherlands and the Federal Republic of Germany (hereinafter: the Core Group).
3. The audit was performed by the head of the audit team, state auditor-lawyer Baiba Skara and senior state auditor Natalja Mihailova.

### **Aim of the audit**

4. According to the Audit Plan<sup>1</sup> (hereinafter: the Audit Plan) drafted by the Core group, the aim of the Parallel Audit is to analyse errors in EU and National public procurement within the Structural Funds programmes detected during the time period 2010–2013.
5. The aim of the State Audit Office is to evaluate public procurement errors within projects financed by the EU Structural Funds, as detected during the time period 2010–2013 by institutions of the Republic of Latvia which are involved in management of EU funds.

### **Responsibilities of the State Audit Office**

6. The auditors of the State Audit Office are responsible for issuance of audit report based on appropriate, sufficient and reliable audit evidence gathered during the audit.

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<sup>1</sup> Paragraph 11 of the Parallel Audit Plan of 16.05.2014 developed by the Working Group on Structural Funds IV of the EU Contact Committee on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”.

## **Responsibilities of the audited entity**

7. The Ministry of Finance is responsible for ensuring compliance with regulatory enactments and truthfulness of information provided to the auditors.

## **Scope of the audit**

8. Audit is performed in accordance with the international standards on auditing which are recognised in the Republic of Latvia.
9. Pursuant to the Audit Plan approved by the Core group<sup>2</sup>:
  - 9.1. The supreme audit institutions base their audit on errors in public procurement procedures already detected by the managing authority, the certifying authority, the audit authority, as well as other institutions involved in management of EU funds, and if possible the European Commission (hereinafter: EC) and/or the European Court of Auditors<sup>3</sup>, and identify the reasons of these errors;
  - 9.2. Only projects financed by the European Social Fund (hereinafter: the ESF) and the European Regional Development Fund (hereinafter: the ERDF) are subject to the audit, except technical assistance projects.
10. In order to achieve the aims of the Parallel Audit and meet the objectives of the Member States as stipulated in the Audit Plan<sup>4</sup>, following reviews were performed during the audit:
  - 10.1. Assessment of information on public procurement errors as detected by the managing authority, the certifying authority, the audit authority, as well as the responsible and cooperation authorities during the time period 01.01.2010–31.12.2013, by determining types of errors per action programmes and per years;
  - 10.2. Identification of reasons of public procurement errors as detected by audit authority, responsible authority<sup>5</sup> and cooperation authorities<sup>6</sup>, by conducting survey (via questionnaires) of the mentioned authorities and the beneficiaries<sup>7</sup> whose projects had errors;
  - 10.3. On initial procurement reviews<sup>8</sup> conducted by the Procurement Supervision Bureau (Iepirkumu uzraudzības birojs — IUB), responsible authorities and cooperation authorities, by establishing whether during

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<sup>2</sup> Paragraph 11 of the Parallel Audit Plan of 16.05.2014 developed by the Working Group on Structural Funds IV of the EU Contact Committee on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”.

<sup>3</sup> Paragraph 12 of the Parallel Audit Plan of 16.05.2014 developed by the Working Group on Structural Funds IV of the EU Contact Committee on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”.

<sup>4</sup> The Parallel Audit Plan of 16.05.2014 developed by the Working Group on Structural Funds IV of the EU Contact Committee on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”.

<sup>5</sup> The Ministry of Transport

<sup>6</sup> The Central Finance and Contracting Agency, the Investment and Development Agency of Latvia, the State Employment Agency, the Society Integration Foundation, the State Education Development Agency, the State Regional Development Agency.

<sup>7</sup> 26 beneficiaries were included in the sample.

<sup>8</sup> Initial procurement review is a review conducted by the responsible authority, the cooperation authority or the Procurement Supervision Bureau. There are two types of initial procurement reviews — procurement documentation reviews and procurement procedure reviews.

follow-up inspections<sup>9</sup>, conducted by institutions involved in management of EU funds in respect to the projects which were subject to initial reviews, any errors were detected which could have been eliminated during initial reviews;

- 10.4. On preventive measures for elimination of errors as detected by institutions<sup>10</sup> ensuring supervision over the projects of the EU Structural Funds, as well as professional qualification requirements of employees (officials) involved in supervision over the EU Structural Funds and trainings received by the employees in relation to public procurement;
  - 10.5. On errors categorised within the European Union Structural Funds and the Cohesion Fund management information system (hereinafter: the MIS) under the category “other error”, in order to determine whether public procurement errors have been also classified under this category.
11. The audit covers the time period from 01.01.2010 to 31.12.2013.
  12. During the audit for the purpose of data analysis the following information was used from the MIS:
    - 12.1. Data submitted by the managing authority:
      - 12.1.1. On initial procurement reviews by institutions involved in management of the EU funds within projects for which expenditure was declared to the EC during the time period 01.01.2010–31.12.2013;
      - 12.1.2. On errors detected by institutions involved in management of the EU funds within projects for which expenditure was declared to the EC during the time period 01.01.2010–31.12.2013;
    - 12.2. Data obtained by the auditors on errors detected by institutions involved in management of the EU funds during the time period 01.01.2010–31.12.2013 which were classified under the category “other error”.

### **Limitations of audit scope**

13. During the audit it was not possible to analyse the following errors:
  - 13.1. Errors detected by the audit authority in respect to expenditure declared to the EC for the year 2013, as such information was not available during the audit;
  - 13.2. Errors for which the amount of financial corrections was reduced due to contentious appeal and was entered to the MIS with minus sign. During the audit it was impossible to determine when the respective error was entered initially and whether it refers to the audit period, as well as its

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<sup>9</sup> Hereinafter: on-site project reviews, selective checks of certified expenditure by the audit authority, the European Commission audits, payment application reviews, audits of the EU funds management and control system, review of functions delegated by the managing authority, findings by the managing authority during control and audit measures, reviews by the certifying institution.

<sup>10</sup> The managing authority, the certifying authority, the audit authority, the IUB, the responsible authority — the Ministry of Transport and cooperation authorities — the Central Finance and Contracting Agency, the Investment and Development Agency of Latvia, the State Employment Agency, the Society Integration Foundation, the State Education Development Agency, the State Regional Development Agency.

initial amount of financial correction. Following amount of financial corrections was not analysed per each operational programme:

- 13.2.1. Operational Programme 1 “Human Resources and Employment” — EUR 32 864;
  - 13.2.2. Operational Programme 2 “Entrepreneurship and Innovations” — EUR 69 527;
  - 13.2.3. Operational Programme 3 “Infrastructure and Public Services” — EUR 455 840;
- 13.3. Financial corrections for which certain definite amount of irregular expenditure was established, as according to the Guidelines by the managing authority on determination of financial corrections<sup>11</sup> (hereinafter: the Guidelines) for such errors no type of errors is indicated in the MIS. Following amount of financial corrections was not analysed per each operational programme:
- 13.3.1. Operational Programme 1 “Human Resources and Employment” — EUR 548 379 or 44% from the total amount of errors within the programme;
  - 13.3.2. Operational Programme 2 “Entrepreneurship and Innovations” — EUR 82 715 or 3% from the total amount of errors within the programme;
  - 13.3.3. Operational Programme 3 “Infrastructure and Public Services” — EUR 2 088 156 or 15% from the total amount of errors within the programme.
- 13.4. Financial corrections for which the type of error indicated within the MIS was breach of procurement or competition norms, but the indicated paragraph of the Guidelines<sup>12</sup> was not referring to breach of public procurement rules. Following amount of financial corrections was not analysed per each operational programme:
- 13.4.1. Operational Programme 1 “Human Resources and Employment” — EUR 116 648 or 9% from the total amount of errors within the programme;
  - 13.4.2. Operational Programme 3 “Infrastructure and Public Services” — EUR 126 258 or 0.55% from the total amount of errors within the programme.
14. During the audit it was impossible to complete the column “Amount of irregular expenditure” of the Appendix 3, 4, and 6 for errors detected by the managing authority, the audit authority, the responsible and cooperation authorities, since

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<sup>11</sup> The European Commission Guidelines for determining financial corrections to be made to expenditure co-financed by the Structural Funds or the Cohesion Fund for non-compliance with the rules on public procurement (COCOF 07/0037/03-EN); 29.11.2007.

<sup>12</sup> The European Commission Guidelines for determining financial corrections to be made to expenditure co-financed by the Structural Funds or the Cohesion Fund for non-compliance with the rules on public procurement (COCOF 07/0037/03-EN); 29.11.2007.

according to the Audit Plan<sup>13</sup> this column should contain the contractual amount, based on which the proportional financial correction was calculated, but such information is not being accrued.

## Summary

15. In the Republic of Latvia the EU funds administration and control system is established at several levels, which during the audit period enabled detection of public procurement errors in the indicative amount of 1% from the total amount declared to the EC, however:

15.1. There is a risk that the actions of institutions involved in management of the EU funds in clarifying of the principles and legal framework of public procurement, as well as the impact of the detected errors on procurement procedure are insufficient and ineffective, since:

15.1.1. The biggest part of the errors or 57% from the total number of errors detected by institutions involved in management of the EU funds, which were subject to proportional financial corrections during the audit period, in all operational programmes were pertaining to unlawful restrictions for selection of tenderers (for example setting specific requirements that favour a single businessman)<sup>14</sup> or unequal treatment of tenderers in awarding of the contract (for example, unjustified preferential treatment given to one of candidates invited to negotiate)<sup>15</sup>, indicating that the beneficiaries are not completely aware of the procurement procedures;

15.1.2. In 45% of the cases the reasons of errors indicated by the beneficiaries do not correspond to the reasons indicated by the audit authority, the responsible and cooperation authorities; for example, in cases when beneficiaries have not selected any of the six reasons of errors, they have indicated to “other reason of error” and in 50% of cases they described these errors as differences in opinion with the institution which had detected the error;

15.2. The procedure for data entering and classification of errors in the EU funds management information system is inaccurate — information on public procurement errors is entered without specifying the type of error, as well as the EU funds management information system does not aggregate information on procurement contracts in order to enable determining whether the contracts are subject, not fully or not subject to EU Public Procurement Directives and to apply a respective financial correction.

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<sup>13</sup> Table 3a and 4 of the Parallel Audit Plan of 16.05.2014 developed by the Working Group on Structural Funds IV of the EU Contact Committee on “Analysis (of types) of errors in EU and National public procurement within the Structural Funds programmes”.

<sup>14</sup> Paragraph 23 of the European Commission Guidelines for determining financial corrections to be made to expenditure co-financed by the Structural Funds or the Cohesion Fund for non-compliance with the rules on public procurement (COCOF 07/0037/03-EN); 29.11.2007.

<sup>15</sup> Paragraph 24 of the European Commission Guidelines for determining financial corrections to be made to expenditure co-financed by the Structural Funds or the Cohesion Fund for non-compliance with the rules on public procurement (COCOF 07/0037/03-EN); 29.11.2007.

16. At the result of the audit three recommendations were issued to the Ministry of Finance as the managing authority aimed at:
  - 16.1. Ensuring that detailed information is being entered and accumulated within the EU funds management information system on public procurement errors, so that institutions involved in management of the EU funds can analyse this information and perform sufficient actions to eliminate the errors;
  - 16.2. Ensuring that institutions involved in management of the EU funds provide purposeful support to the beneficiaries in respect to procurement procedures and detailed explanation of the substance of the detected errors in order to reduce the number of public procurement errors within projects financed by the EU funds;
  - 16.3. Reduction of the number of unclassified errors by ensuring accurate classification and evaluation of errors according to their type.