

## Importance of cooperation among EU Supreme Audit Institutions highlighted in Riga, Latvia. Project management and audit perspective in EU

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### Introduction

I have had opportunity to participate in the Contact Committee meeting of EU Supreme audit institutions as part of Latvian presidency in the EU council. The cooperation platform of the Supreme Audit Institutions of the EU and the European Court of Auditors – the Contact Committee – was held in Riga, Latvia on June 18 and 19, 2015. The meeting was attended by the Heads of the Supreme Audit Institutions of the EU Member States and five candidate countries, representatives



from the European Commission and the European Investment Bank, and the President of the European Court of Auditors, Mr.

Vítor Caldeira. The European Organization of Supreme Audit Institutions (EUROSAI) was represented at the meeting as an observer. The meeting is organized by the State Audit Office of the Republic of Latvia.

Mūrniece during Contact Committee opening speech pointed to the logo of Latvian Presidency of the EU Council making symbolic links with millstone: “Mill is used for grinding grain to get pure top quality flour. Only from such we can bake a good bread. Supreme audit institutions work is to help the countries build a perfect system of governance in public administration”.

Ms Ināra Mūrniece expressed her utmost respect for the successful cooperation within Contact Committee members. She stressed that such international cooperation also builds public trust in audit authorities.





“This is a time to assess the progress of our work, to agree on how to proceed and outline our future goals. I really hope that these two days of intense work together will be successful and productive” with warmly congratulations to her colleagues – leaders and representatives of the Supreme Audit Institutions said Auditor General of the Republic of Latvia Ms Elita Krūmiņa.

In her address to participants of the Contact Committee Auditor General Ms. E.Krūmiņa marked the main topics that will be the center of discussions during this meeting. The topics discussed at the Contact Committee meeting will be: the European Fund for Strategic Investments; preventing and combatting irregularities and fraud in cooperation with law enforcement bodies; and the Multiannual Financial Framework within previous raised discussion on the banking union in the EU.

During the Contact Committee meeting participants examine the most topical issues concerning the performance of external audits, consider possible means for facilitating further cooperation, and exchange professional knowledge and experience including on the audit of EU funded projects and other EU-related issues.

It promotes the exchange of information, thus allowing the members to initiate and coordinate common audits and other activities in order to improve the quality of external audits and accountability.



While discussing how to prevent and combat project irregularities and fraud in cooperation with law enforcement bodies, the Supreme Audit Institutions shared their examples of best practice so that corruption and systematic discrepancies in the use of financial resources in the public sector can be reduced in the most effective possible way. As these topics are timely and important for the whole European Union, the common vision of the Contact Committee and the solutions proposed will have particular added value.



During the meeting Supreme Audit Institution member discussed and evaluated an accomplishment progress of nine working groups' activities within Contact Committee framework.

**Contact committee work on Audit findings in EU financed projects**  
***Just few “lessons learnt” from 2004 – 2006 planning period:***

- ✓ Management and control system mostly fails to ensure achievement of planned objectives and development, and thus – sustainability and impact of the EU co-financed projects
- ✓ Instead, the system focuses on maintenance of procured assets prescribed by the EU regulations (*durability*)



***“Post-project” monitoring by Intermediate Bodies is ineffective:***

- ✓ scrupulous monitoring of beneficiaries before the final payment to the beneficiary is made, while
- ✓ after the final payment, the beneficiary may fail to ensure further development, may even decrease performance below the level before receiving the EU support
- ✓ In most of cases only insolvency is considered as the reason for declaring the expenditure as ineligible, however -

- ✓ recovery of budget funds (EU and national) usually fails - Intermediate Bodies are at the bottom of the list of creditors

### **European regional development fund 2007 – 2013**

- ✓ No “lessons learnt” from 2004 - 2006
- ✓ Only 20% of the ERDF co-financed projects achieved planned results, other projects revealed no results or partly achieved results
- ✓ 17% from supported beneficiaries (mostly – SMEs) are already closed or face severe difficulties
- ✓ *Neto* turnover of every third beneficiary has decreased after the receipt of the ERDF support



### **Why the beneficiaries (Project implementers) fail?**

National legal framework generally fails to require achievement of results

- ✓ Project selection procedures permit selection of projects without any potential for development, and fail to prefer projects with higher potential and lower support intensity
- ✓ National legal framework generally fails to clearly authorise Intermediate Bodies to perform certain actions in case the results are not achieved
- ✓ Insufficient “top – down” communication – beneficiaries are mostly not aware that the results defined in their own project applications **MUST** be achieved

**BENEFICIARIES ARE NOT MOTIVATED**

*neither by «carrot», nor «whip»*

## **Some of Recommendations what was proposed during international meeting in Riga**

Choice between development and social support / support to survival

- ✓ Definition of adequate goals and policies for their achievement thus avoiding:
  - resource consuming and senseless monitoring of beneficiaries by Intermediate Bodies, trying to verify achievement of results, nobody is interested in
  - unjustified expectations by public believing that EU funds contribute to development
- ✓ Establishment of an adequate legal framework requiring achievement of results<sup>1</sup>
- ✓ Similar treatment for the EU and national budget expenditure (*much stringent requirements for the EU expenditure compared to that from the national budgets*)

### **Accountability of «budget users»**

Close co-operation with law enforcement agencies (SAI must do more, as they formally should)

- ✓ Strengthening of legal framework requiring accountability
  - *From 2014 – within 6 months after finalization of audit, the supervising institution of audited entity must assess accountability of certain officials and decide on the measures to be taken*
- ✓ Additional powers for SAI to be applied in cases where the public service is not willing to react (debated in the other parallel session)

### **Risks to the financial management of the EU budget (see Figure 1. Next page)**

- ⚠ The budget may not be spent as agreed by the budgetary authority and in accordance with the rules (legality and regularity – negative ECA DAS opinion)
- ⚠ The accounts may not show the correct budget spending (reliability of accounts – generally not a problem)
- ⚠ The budget may not be spent wisely, with sound financial management principles (economy, efficiency and effectiveness)
- ⚠ EU spending may not add value and the expected benefits may not arise

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<sup>1</sup> This includes clarification of terminology (“innovative” technologies, increased “added value” of products)



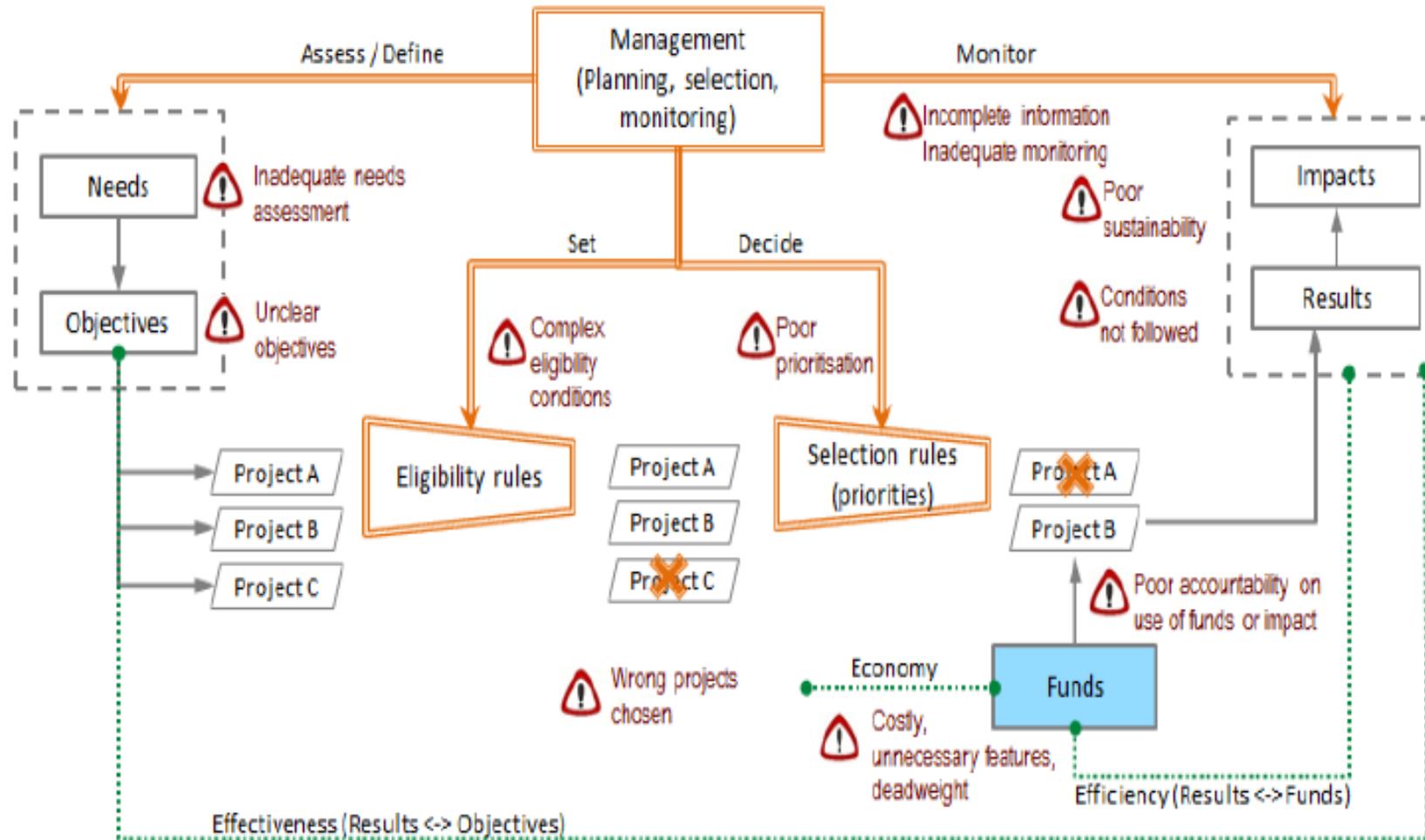


Figure 1. **European Court of Auditors perspective on Project impact factors. Based on audit findings**

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## **Results of Supreme Audit Institutions working group on Project management issues within EU public funding framework**

In 2013, the Contact Committee of the heads of Supreme Audit Institutions (SAIs) of the Member States of the European Union and the European Court of Auditors mandated the Working Group on Structural Funds to continue its review of issues relating to Structural Funds, more specifically, to carry out a parallel audit on the 'Analysis (of types) of errors in EU and national public procurement within the structural funds programmes'.

The Working Group consisted of nine SAIs, while a further five SAIs and the European Court of Auditors acted as observers. The parallel audit was carried out in order to understand the reasons why beneficiaries fail to comply with public procurement rules. The comparison of the national results was intended to reveal differences or similar causes in the Member States. Most SAIs based their audit on errors already detected by their national management and control system.

One of the most frequent types of errors within the Structural Funds programmes occurs in the field of public procurement. As a result, financial corrections are made and project implementation is often seriously hampered. Improper application of EU public procurement rules can lead to financial corrections of even 100 per cent of the respective contract value.

When analysing the different amounts of detected errors and the corresponding irregular expenditure in the Member States, the Working Group had to take into account several conditions which had a significant impact on the findings. It was often challenging for national authorities to provide information on the number of projects under (partly) public procurement and on the types of errors detected by the authorities. Such data was often not available through the administrative systems used by the national authorities to support the management and control of their programmes. That is one of the reasons why several SAIs limited the audit scope to some OPs (SAIs of Italy, Germany, Poland and Portugal<sup>10</sup>) or took a sample within one OP (SAIs of the Netherlands (ESF) and Poland).

The findings presented by the SAI of the Czech Republic are only one part of an investment audit and cover a sample within one OP. Another factor to be accounted for is the diversity of the audited OPs and the management and control systems in the Member States. For example in some OPs, many projects are funded – one German ESF OP funded 40 000 projects in the years 2010-2012 – while others funded a limited number of projects – the Maltese ESF OP funded 165 projects in the same period.

To help readers better understand the results presented below, the Working Group points out the following differences:

- ✓ Since the description of errors given in the COCOF guidelines is rather ambiguous and vague, uniform application of the categories cannot be ensured.
- ✓ Some detected errors fitted into more than one description of the types of errors and were classified accordingly. As a result, the total amount of errors was increased.
- ✓ ESF projects often include considerably less or more simplified public procurement procedures than ERDF projects.
- ✓ While some ERDF OPs are designed to support infrastructure projects with major projects and a lot of (mostly extensive) public procurement procedures, others promote micro, small and medium-sized enterprises (SME) with smaller projects and small-scale public procurement procedures. Regarding the volume of infrastructure OPs, most of its public procurement procedures exceed EU thresholds.
- ✓ Sometimes staff of the management and control systems was well experienced in public procurement procedures, however, other staff was less experienced.
- ✓ The types of beneficiaries largely differ. They range from public bodies to SMEs, to small non-profit organisations and other different types of beneficiaries. Therefore, their knowledge of and experience with public procurement rules varies significantly.
- ✓ Not every error identified was reported by the authorities of the management and control systems and especially their Intermediate Bodies. Where the responsible authorities found minor (mostly formal) errors during their checks and the beneficiaries corrected these errors before the expenditure had been declared to the EC, they recorded it in the project files only.

### **Conclusions and recommendations from working group**

Although this parallel audit was not designed to provide a full and accurate picture of the situation, the findings suggest a rather large number of errors in public procurement under Structural Funds. It has to be taken into account that presumably a high number of cases has not even been detected or recorded.

- ✓ Most authorities of the management and control systems and especially their Intermediate Bodies do not register and report all and any error detected.
- ✓ Working group recommends that the responsible national authorities take steps to ensure that errors found are recorded and reported.
- ✓ Most national authorities do not systematically record the types of errors in public procurement procedures. They place focus on individual errors only.
- ✓ Working group recommends that national authorities systematically record the types of errors detected in public procurement procedures. This is the only way to provide a full picture of these errors and tackle them effectively.

Errors in public procurement were more wide-spread in procedures below the EU thresholds than above the EU thresholds. However, average financial impact of errors was higher in procedures above the EU thresholds than below the EU thresholds.

Both in European Social Fund (ESF) projects and European Regional Development Fund (ERDF) projects above the EU thresholds the highest error rates belonged to category 12 (incorrect application of certain ancillary elements). The category featured a broad array of irregularities and seemed to function as a “miscellaneous clause” for errors that do not fit properly into any of the other categories. Below the EU thresholds, the COCOF guidelines neither provide a similar category nor sufficiently suitable categories.

- ⚠ National authorities are advised to decide on the treatment of errors that do not fit into the categories of the COCOF guidelines.
- ⚠ Although most authorities already seek to prevent errors in public procurement procedures, we recommend that national authorities take more targeted action to reduce the most common errors in public procurement procedures and those with the highest financial impact.
- ⚠ According to the authorities, errors are not often committed intentionally. It was noted that, in a few cases, the most expensive (and presumably preferred) supplier was chosen although cost was one of the award criteria. Furthermore, the proposal of the preferred supplier was handed in early whereas only weeks afterwards - perhaps only after selection of the preferred party - other parties were asked to hand in a proposal as well. However, in most of the studied cases, it is difficult for authorities to determine whether or not beneficiaries have made mistakes intentionally. Other reasons frequently cited include interpretation differences. In such cases the rules are known, but authorities and beneficiaries have different opinions as to whether or not their conduct is in compliance with these rules. Such differences in interpretation often relate to the amount of evidence required to justify the award to a certain supplier.

**According to the audit findings “lack of knowledge” is the most common reason for errors in public procurement, followed by “interpretation difficulties”.**

Working group recommends that the Member States request the EC to further clarify the legal framework and reduce the administrative burden for the contracting authorities and the bidders, but this should not result in limitation of the equal access, fair competition and efficient use of public funds.

**Working group recommends that Member States take the following steps in order to prevent or reduce errors in the area of public procurement in projects:**

- ⚠ They should keep public procurement rules as simple as possible and should avoid major and frequent amendments. All necessary steps should be undertaken in order to fully and properly implement the new EU Directives on public procurement at a national level from the very beginning when they take effect on 18 April 2016. This should be supported by electronic tools to manage public procurement procedures. Furthermore, they should continue to clarify the legal framework and reduce the administrative burden for the contracting authorities and the bidders.
- ⚠ With regard to the staff of the national authorities, some Member States should improve their knowledge in the field of public procurement in order to be able to advise beneficiaries better (make them aware of the rules in force) and prevent errors. The staff should be encouraged or obliged to participate in special training on public procurement.
- ⚠ Although most authorities stated that they already sought to support beneficiaries, the Member States need to improve their communication policy and provide better information (see also Key Requirement 3 - being one of the key elements of the management and control system 'Adequate information and strategy to provide guidance to beneficiaries')<sup>2</sup>. It might also be helpful to provide support to inexperienced beneficiaries from the application to the completion of the project. They should try to ensure that beneficiaries exert due diligence at all stages of public procurement, including in particular planning and preparation of the procurement, selection procedure as well as implementation of the contract.
- ⚠ Taking these steps to improve the "knowledge" may prevent other reasons for errors; such as "errors made intentionally" by pointing out the consequences for the breach of public procurement rules, "interpretation difficulties" and errors related to "human failure".

**During Contact Committee meeting in Riga SAI's accept resolution on further developments in the field:**

They recommend the Member States to request the European Commission to further clarify the legal framework and reduce the administrative burden for the contracting authorities and the bidders, but without resulting in limitation of the equal

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<sup>2</sup> COCOFC 08/0019/00-EN Guidance on a common methodology for the assessment of management and control systems in the Member States (2007-2013 programming period), final version of 23 April 2008.

access, fair competition and efficient use of public funds. Further to that, we recommend Member States to take the following steps in order to prevent or reduce errors in the area of public procurement:

- ⚠ They should keep public procurement rules as simple as possible and not change them too radically or too frequently.
- ⚠ Some Member States should improve the knowledge of the staff of the national authorities in the field of public procurement in order that they are equipped to support beneficiaries and prevent errors.
- ⚠ Member States should improve their communication policy and provide better information to beneficiaries. They should try to ensure that beneficiaries exert due diligence at all stages of public procurement.

### **Importance of Contact Committee and Latvian presidency in the EU council**

The Contact Committee is a forum of the Heads of the Supreme Audit Institutions (SAIs) of the EU Member States and the European Court of Auditors (ECA) that aims to contribute to the improvement of EU financial management and good governance within the EU Member States for the benefit of all EU citizens.

During the Contact Committee meeting participants examine the most topical issues concerning the performance of external audits, consider possible means for facilitating further cooperation, and exchange professional knowledge and experience including on the audit of EU funds and other EU-related issues. It promotes the exchange of information, thus allowing the members to initiate and coordinate common audits and other activities in order to improve the quality of external audits and accountability.

The presidency of the Council of the European Union (EU) rotates among the EU Member States every six months and the country holding the presidency drives forward the Council's work. The EU Council is an essential decision maker which together with the European Parliament (EP) adopts legislation and coordinates EU policies.

Presidency is an opportunity for each Member State, regardless of its size or the length of the membership, to influence the EU agenda and guide the EU endeavours. Latvia for the first time is assuming this task from 1 January 2015 to 30 June 2015 taking it over from Italy and afterwards handing over the reins of the presidency to Luxembourg.

*\*Information and pictures from Latvian EU presidency press centre and State Audit Office of The Republic of Latvia were used in this report, as well as information from presented papers and presentations during Contact Committee meetings.*

## About the Author



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**Emils Pulmanis** is a member of the board of the Professional Association of Project Managers in Latvia and development project manager at State Audit Office of the Republic of Latvia. He has gained a BSc. in engineer economics, a professional master's degree in project management (MSc.proj.mgmt) and currently is a PhD candidate with a specialization in project management. He has elaborated and directed a number of domestic and foreign financial instruments co-financed projects. He was a National coordinator for a European Commission-funded program – the European Union's financial instruments PHARE program in Latvia. Over the past seven years he has worked in the public administration project control and monitoring field. He was a financial instrument expert for the Ministry of Welfare and the European Economic Area and Norwegian Financial Mechanism implementation authority as well as an expert for the Swiss – Latvian cooperation program as a NGO grant scheme project evaluation expert. He has gained international and professional project management experience in Germany, the United States and Taiwan. In addition to his professional work, he is also a lecturer at the University of Latvia for the professional master study program in Project management. He has authored more than 25 scientific publications and is actively involved in social activities as a member of various NGO's.

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