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Investigation of Irregularities in the Administration and Management of European Structural Funds - the case of Romania

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Abstract

The European Union as a whole is a donor of external financial assistance to third countries through structural instruments having as unique receiver the Member States with a lower level of development than the European Union average and as the main objective the accelerated support for economic development and the promotion of cross- Member States and increasing economic competitiveness. In this paper we aim to identify and analyse the particularities regarding the conformity of the projects funded by non-reimbursable funds with the national and international legislation, by stopping us from investigating the irregularities carried out by the Romanian organisms with responsibilities in identifying, monitoring and reporting. The analysis has as its starting point the first exercise of Romania's access to the European Structural Funds for the period 2007-2013, and it consist in highlight the regulated procedures, instruments and competences that Romania has at its disposal in order to ensure a healthy financial management.

Keywords: *European structural funds; responsibility; verification; suspicion; irregularity.*

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1. Introduction

The EU's non-reimbursable financial assistance is implemented through projects and implemented decentralized at the level of each Member State, focusing on certain priorities set out in the strategic programming documents.

As regards the management of the European Structural Funds, the division of responsibilities between the European Commission and the Member States is guided by respect for the principles of proportionality, partnership and shared management. The objectives of the Structural Funds are pursued in the framework of close cooperation ("partnership") between the European Commission and each Member State on the design, implementation, monitoring and evaluation of operational programs.

The distribution of responsibilities between the European Commission and the Member States for the management of the Structural Funds is governed by respect for the principles of partnership, proportionality and shared management, such is:

- the Commission and the Member States utilise in order to implement the funds, financial and administrative resources that must be proportionate to the total amount of expenditure related to an operational program;
- the European Union budget allocated to the Structural Funds is implemented under shared management between the Member States and the European Commission under the conditions of sound financial management.

In this context, we considered it appropriate to realize a study on the procedures for investigating irregularities in the implementation of programs financed by European funds in the framework of the control and verification actions realized by the attributed structures and the importance of recording, monitoring and reporting irregularities in the management sound financial framework referred to in the partnership concluded at the level of the European Union.

Our study has the character of a theoretical documentation which mainly focused on the applicable legislation in the field in Romania, with an empirical research component, in order to highlight the way to identify the fraud indicators following the external audit missions made by the Court of Accounts of Romania through the Audit Authority.

2. Theoretical Background

The possibility for Member States to support their accelerated economic development or the promotion of economic and employment competitiveness is influenced by a number of factors such as: the competence of the institutional structures involved at national level in the management of these instruments, the financial capacity of the potential beneficiaries from a Member State as regards the financial resources for the implementation of projects financed by structural instruments, their level of information.

The European Commission respond for the good implementation of the entire budget of the European Union. In order to fulfil this responsibility, the European Commission verifies the existence and correct functioning of the management and control systems in the Member States and may suspend / discontinue the payment deadlines or may suspend payments totally / partially to Member States under the different operational programs or any other financial corrections necessary if the national management and control systems fail to function properly in accordance with the principles of sound financial management.

The financial corrections consist in the partial or total cancellation of the Community contribution to an operational program if, after deploying the necessary verifications, the European Commission concludes that:

- there is an important deficiency in both program management and control system, which jeopardizes the Community contribution already paid to the program;
- identifies irregularities in the expenditure covered by a certified statement of expenditure, irregularities which have not been corrected by the Member State prior to the opening of the specific correction procedure.

3. Argument of the paper

Therefore, the tasks of the European Commission are of strategic nature, consisting in the permanent analysis of the national systems of management and supervision of the efficiency of measures financed by structural funds.

On the other hand, institutions with attributions in the field of European funds that each State must have are the following:

1. Managing Authority for the management of the operational program.

2. Certification Authority for certify their expenses and requests for payment before being sent to the European Commission; for several operational programs, the same authority may be designated.

3. Audit Authority: an independent structure, needed to formulate a functional point of view on the compliance of the operations carried out with the regulations and rules applicable to each program; for several operational programs, the same authority may be designated.

One or more organisms responsible for the management of the Structural Funds and their relations with the Commission may be designated as intermediaries; each Member State must establish the rules governing its relations.

4. Arguments to support the thesis

The Managing Authority within each Member State must ensure that operations and projects funded under the different operational programs are well-managed financially throughout the duration of the project.

As regards the certification of expenditures realized in the funded operations/projects, the verifications carried out by the Managing Authority are supplemented by the specific verifications of the Certifying Authority, prior to the transmission of the expenditure and payment documents to the European Commission.

In turn, the European Commission wants every state to respect the principle of good management of financial funds and operational program through conditionality that exist in pre-financing, interim and final payments.

Except for pre-financing, Structural Funds operate in the system of reimbursement of eligible expenditure actually incurred by Member States. When making payments to the Member State, the Commission requests certification of this expenditure to ensure that all expenditure incurred by each state involved in the operational programs is eligible expenditure taking into account European rules and that fund management systems at Member State level, works properly so that the information provided by these systems is accurate and real.

Practically, this conditionality contributes to making the Member State responsible for the use of structural fund resources.

5. Identification, recording, monitoring and reporting of irregularities in the case of projects funded by non-reimbursable funds in Romania

A general regulation on uniform controls, administrative measures and sanctions for infringements of Community law was adopted in 1995 for the financial protection of the European community, which states that "Any violation of a provision of Community law as a result of an act or omission by an economic agent which may or may be prejudicial to the general budget of the Communities or the budgets managed by them, either by diminishing or losing revenue accruing from own resources collected directly on behalf of the Communities or through unjustified expenditure." [1]

From the point of view of the Romanian legislation, there is an irregularity "any deviation from legality, regularity and compliance with the national and/or European provisions, as well as with the provisions of the contracts or other legal commitments concluded on the basis of these provisions, an action or inaction of the beneficiary or of the authority competent for the management of European funds, which has, or would be, prejudiced the European Union budget / the budgets of the international public donors and/or the national public funds related to them through an amount unduly paid." [2]

The competent Romanian authorities are required to develop control/investigation activities in order to establish/establish the existence of an irregularity in accordance with the applicable legislation and the activity of establishing the budgetary receivables resulting from irregularities - "the amounts to be recovered following the finding of an irregularity in obtaining and using European funds and/or national public funds related to them". [2]

To this end, authorities managing European funds should designate an *irregularity officer* to develop the activity of registering, monitoring and reporting irregularities.

5.1. Suspicion of irregularity/fraud

Authorities managing Community funds and their co-financing in order to identify and report irregularities are required to verify complaints from within and outside the Authority regarding possible irregularities or frauds.

Sources of reporting on possible irregularities in the management of Community funds may be: verifications carried out at the level of the Managing Authority, control notes/reports of internal control structures,

internal audit reports, control/audit acts drawn up by the representatives of the European Union, issued by the Anti-Fraud Department (DLAF) and the inspection report issued by the European Anti-Fraud Office; audit reports issued by the Audit Authority/external audit structures; on-site verification reports issued by the Certifying and Paying Authority; internal or external referrals of whistleblowing, which means "making a good-faith complaint about any act that involves a violation of law, professional ethics or principles" good governance, efficiency, effectiveness, economy and transparency." [3]

If the notification "does not meet the conditions for identifying the program, payment scheme, transaction and / or beneficiary to which it refers, it is ranked." [2]

The notifications will be established as confirmed irregularities, only following investigations under OUG 66/2011, through the control structure, as a result of which the irregularities will be ascertained and the corresponding budgetary receivables will be established.

The activity of finding irregularities and establishing budgetary receivables resulting from irregularities, namely establishing the financial corrections, as well as settling the appeals against the issued debt securities, is carried out by the control compartment.

Depending on the frequency of occurrence, irregularities may be systematic or individual, and depending on the causality they may be unintentional irregularities and intentional irregularities (fraud).

5.2. Identification, recording, monitoring and reporting of irregularities

Unintentional irregularity is any action/inaction of a person belonging to one of the institutions involved in the management of European non-reimbursable funds, representing the unintentional non-compliance with the legal provisions in force.

These are basically errors that may be due to negligence in document preparation, management and reporting, or errors resulting from the unclear or inadequate definition of the control environment or financial management system.

Intentionally irregularity (fraud) is "any intentional action or inaction related to the obtaining or use of Community funds and/or national public funds related to them" [2], consisting in the submission of false or incorrect or incomplete documents or statements or failure to transmit the information or misapplication of the regulatory framework for obtaining a

benefit, incriminated by the Criminal Code, the legislation in force in the field of prevention, detection and sanctioning of corruption acts or by other special laws. Intentionally fraudulent (fraud) is a crime "committed in connection with the obtaining or use of European funds and/or national public funds affiliated with them, incriminated by the Penal Code or other special laws". [2]

In accordance with the applicable law for the organization of the activity and the functioning of the Romanian Court of Accounts, only the Audit Authority is the national authority competent to develop external public audit, on the basis of the Community and national legislation, on the non-reimbursable funds granted to Romania by the European Union.

The European Commission may request the Audit Authority to develop a sample-based verification of the Community funds expenditure that the responsible authorities have declared to be incurred, particularly in cases where "the problems discovered appear to be systematic and present risks for other operations under the operational program".[1]

The audit activity is carried out on the basis of the accepted International Standards for Auditing and of the Community and national legislation applicable to the structural funds granted to Romania by the European Union. Also, the audit engagement for the Structural and Cohesion Funds of the Audit Authority is considered in the audit engagement.

The report, based on adequate, appropriate and reliable audit evidence to support the conclusion regarding the legality and regularity of the audited expenditure, the analysis of identified errors and deficiencies, including the findings and recommendations made, will be forwarded to the Managing Authority by management letter in order to receive the point of view of audited entities. Subsequently, the final audit report will be prepared, reviewed, endorsed and approved and transmitted to audited entities.

Measures taken by audited entities to implement auditors' recommendations will be monitored on the basis of reports submitted by audited entities at the set implementation deadlines and verified in the next follow-up mission.

As a result of the audit engagement, for deployment of the activity of registering, monitoring and reporting the irregularities, the irregularity officer shall draw up the Event of Irregularity, in case of unintentional irregularities or Suspicion of fraud, in case of intentional irregularities and its transmission to control structures, within the time limit provided by the law.

Both Suspicion of Irregularity and Suspicion of Fraud are formalized documents, the preparation of which is done in strict compliance with the model provided by the national legislation.

In addition to identification data related to the program/fund/priority axis, project, intermediary organism, beneficiary, number and the date of the contract/agreement/decision/financing order, the "regulated format" [4] necessarily includes information, accompanied with a detailed description of:

- Source/date of the first information that led to the conclusion that there is a suspicion of irregularity or fraud;
- How to discover a possible irregularity: on-the-spot checks, audit missions, control missions, whistleblowing system;
- Type of suspected irregularity: intentional/unintended, individual or systemic irregularity;
- Description of suspected irregularity, including how it is produced: overpayment/payment of ineligible expenditure/legal breach of procurement/breach due to negligent work procedures or due to unclear or insufficient definition of legal norms/procedures;
- Type of expenditure: personnel, materials, etc.;
- The amount suspected of being unduly paid;

The Irregularity/Fraud Form must be accompanied by the document that is the source of the first information that led to the conclusion that there is a suspicion of irregularity/fraud.

5.3. Case study on identifying fraud indicators in the case of projects funded by non-reimbursable funds in Romania

As mentioned above, the external audit missions are performed on the basis of the provisions of Law no. 94/1992 by the Audit Authority of the Court of Accounts of Romania, which realize the verification, based on a representative sample, of the expenditure declared by the authorities responsible for managing and implementing the Community funds.

As mentioned above, external audit missions have been regulated since 1992 by Law no. 94 and are carried out by the Court of Accounts of Romania through the Audit Authority which carries out the verification of the expenditures incurred and declared by the authorities responsible for the management and implementation of the Community funds.

The effective execution of the audit involves the application of audit procedures, the collection of sufficient, appropriate and reliable audit evidence to support the conclusion regarding the legality and regularity of the audited expenditure; analyzing the errors and deficiencies identified.

The mission ends with an Audit Report that includes centralizers of the findings and recommendations formulated and are sent to the Managing

Authority by management letter to receive the point of view of audited entities. Subsequently, the final audit report is elaborated, revised, endorsed and approved and also sent to the audited entities.

In case of serious deficiencies or suspicion of fraud, the Audit Authority may recommend to the Managing Authority to verify all operations realized within a project in order to identify the fraud indicators and to establish appropriate financial corrections.

Fraud indicators are described in Romanian law in 16 fraud systems, common and recurrent, the structure and content of which are based on instructions for professionals regarding fraud and fraud prevention from the Association of Certified Fraud Examiners. These are the following: 1. Corruption - bribe and illegal commissions; 2. Notification of conflicts of interest; 3. Practices of secret cooperation; 4. Discrepancies; 5. Manipulation of specifications; 6. Disclosure of auction data; 7. Manipulating offers; 8. Unjustified attributions to a single bidder; 9. Fragmenting purchases; 10. Combining of contracts; 11. Incorrect costing; 12. Manipulation of prices; 13. Non-fulfilment of contract specifications; 14. False or doubles invoices or excessive prices; 15. Fictitious service providers; 16. Substitution of the product. [4]

Case study : At the request of the European Commission, the Audit Authority initiated the verification action in order to obtain audit evidence that is sufficient, relevant and reliable to demonstrate that the operations within a project for which, between 01.01 - 31.12.20NN, have been declared to the European Commission expenditure are fair, legal and regulatory.

Deficiencies found by the Audit Authority:

1. Non-compliance of the provisions and rules in the field of procurement in the case of awarding 2 contracts for equipment supply concluded by one of the beneficiaries;

2. When awarding procurement contracts, the beneficiary has imposed in the documentation for tenderers restrictive criteria such as to prevent tenderers from taking part in the procurement procedure.

Taking into account the provisions of the Applicant's Guide, it is noted that rigorous financial management was not ensured in terms of efficient use of funds and an optimal cost-effectiveness in the conduct of procurement procedures.

The main **recommendations** formulated to remedy the identified deficiencies:

1. Laying down the measures stipulated by OUG no. 66/2011, for the purpose of applying a 25% correction of the value of the two awarded contracts without conducting an adequate competitive procedure, recovery of the claim and related accessories and its deduction from the expenditure

declared to the Certifying and Paying Authority for the deduction of expenditure declared as CE.

2. In view of the irregularity of the project acquisitions in the context of the verification made, the AM POS DRU must ensure the verification of all acquisitions under the project and apply financial corrections in the event of non-observance of the procurement rules.

As a result of the audit mission, in order to realize the activity of registration, monitoring and reporting of irregularities, the irregularity officer makes **the suspicion of fraud** and sends it to the control structures within the term stipulated by the law.

The control mission shall be completed by drawing up a debt instrument, namely the **Notice of finding irregularities and establishing financial corrections**. This is done when the irregularities found make it necessary to apply the financial corrections provided by the legislation in force for the verified public procurement contracts.

Conclusions of the verification activity:

Contract no. 1: Acquisition of computer applications

For the application of unlawful qualification and selection criteria, OUG no. 66/2011 applying a 10% correction of the value of the contract affected by the offense.

The Beneficiary has breached the provisions regarding the stages and the operations to be performed for the award of the procurement contracts, namely the obligation to sign the procurement contract with the bidder in accordance with the provisions of the tender offer and the documentation for the bidders.

Fraud indicators fall under the description of the System of Secret Cooperation Practices [4] and are:

1. Abnormal bidding configuration (technical offers are identical in terms of the products offered and their technical characteristics);

2. Apparent links between bidders and joint shareholders, given that the two bidders have the same shareholding and address for the registered office.

Contract no. 2: Acquisition of computer equipment

From the analysis of the specification included in the tender documentation, of the tenders submitted by the tenderers and of the HG provisions no. 875/2011, approving the Methodological Norms for the application of the provisions of OUG no. 66 of 2011, fraud indicators have been identified, which fall under the **Manipulation of Specifications** category. [4]

Identified fraud indicators:

1. Technical specifications are too restrictive and can be used to exclude other qualified bidders to justify purchases from a single source and to avoid any competition;

2. There are similarities between the specifications and the products or services of the winning contractor.

For each individual contract a financial correction value was also established, which will be reflected in the debtor's budget claim. The amount owed to the authority responsible for managing European funds is broken down into the following destinations:

- 1) the budget of the European Union;
- 2) the state budget of Romania;
- 3) VAT recovered from the state budget.

6. Conclusions

The responsibility for the implementation of operational programs therefore lies with the beneficiary Member States of the non-reimbursable funds. In order to ensure sound financial management of operational programs, they also have the responsibility to investigate irregularities and take the necessary corrective measures when there is a significant modification with an impact on the nature of the operations or on the conditions for the implementation of those operations or programs.

In order to manage and administrate European Structural Funds more efficiently, Romania needs to identify the most appropriate working structures and modalities, being a model that effectively responds to the needs and characteristics of its own administration. Prevention measures are also necessary to defending the financial interests of European Member States by ensuring that they recover the funds that have been misused as a result of irregularities.

The correct allocation and use of funds through the implementation of efficient control procedures and of a good management, the correct and timely implementation of the recommendations resulting from the control and auditing actions lead to good financial management and, implicitly, to reduce the risks of irregularities and fraud or at least to diminishes their complexity and impact.

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