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Audit of European Structural and Investment Funds, a Component of the Management and Control System

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Abstract: *The European Commission (EC) has established through European regulations that at each Member State an independent body, generically called the Audit Authority (AA), who will ensure the external public audit function for each operational program financed by the European grants. Each Member State was free to set up its audit authority, subject to the above-mentioned conditions.*

The Romanian Audit Authority was set up at the level of the Romanian Court of Accounts, being established by national law as a body without juridical personality, operationally independent from the rest of the public audit activity. This audit body performs the external audit function for all operational programs financed by the European grants.

The present article aims to present the Romanian Audit Authority, its institutional and organizational capacity to fulfil the legal requirements of the European legislation and the extent to which its results can provide a reasonable assurance to the European Commission that the management and control system (MCS) functions in way to prevent, detect and correct deficiencies and financial sanctions. One of the challenges of the audit is whether its recommendations can prevent malfunctions in the MCS, and in the event of irregularities, the managing authority (MA) and the certifying authority (CA) can correct them in time before the European Commission is declared expenditure. It will also present the procedure established by the legal framework on how audit recommendations are implemented by the other entities within the management and control system.

Although it is part of the Court of Auditors, the Audit Authority has its own working procedures, which must reflect the requirements of European regulations and guidelines, and the results of its verifications are communicated to the European Institutions. The manner in which the EC uses the audit reports will also be the subject of this article.

Keywords: *management, audit, irregularities, recommendations.*

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1. Introduction

In the framework of Regulation (EU) No 1303/2013 laying down common provisions on the European grants, for each operational program approved by the EC, the national authorities have the obligation to set up an audit authority as part of the MCS.

The European Commission has allowed by regulation the audit authority to be a public institution at national, regional or local level, or private entity functionally independent of the other components of the MCS, namely the MA and the CA.

At the level of each member state of the European Union, the application of the legal requirements of the Regulation (EU) No 1303/2013, supposed the organization of the external audit function for the European funds in different structures from the central or local public administration, respecting the conditions of independence. As an example, the situation in several countries of the EU regarding the location of audit authorities is the following:

• In Lithuania, it is organized in the Court of Accounts - Supreme Audit Institution;

• In Poland and Portugal, it is organized at the level of the Ministry of Finance, within the General Inspectorates of Finance;

• In France, it is organized as an inter-ministerial commission, under the direct subordination of the Prime Minister made up of representatives from several line ministries;

• In Hungary, it is organized as a central agency coordinated by the Ministry of Economy.

In Romania, the Audit Authority was set up at the level of Romanian Court of Accounts and performs the audit activity for all operational programs financed by the European grants.

The EC has the obligation to cooperate with the national audit authorities to ensure the methodological coordination of the audit plans and methods used. At the same time, it was necessary to develop an immediate exchange with the audit authorities of the results of the audits carried out on the functioning of the MCS for each operational program. To this end, the European Commission has issued a series of guidelines that reflect how the audit body should assess the MCS, the methods of sampling audit operations, and how to perform the audit of the accounts. Where a EU country established more than one audit body, as in the case of Italy and Germany, is a condition to designate a coordinating audit body.

The European Commission, the audit body and any coordinating audit body have the obligation to meet at least once a year to discuss about the audit activity from audit strategy and the conclusions from the audit reports. One of the most important topic is to exchange opinions on issues related to improving the functionality of the MCS.

2. Theoretical Background

The Audit Authority was established in Romanian Court of Accounts on the basis of Law no. 200/23.06.2005 regarding the approval of Government Emergency Ordinance no. 22/2005 for completing the Law no. 94/1992, as a body without legal personality, but operationally independent of it.

Thus, it was regulated that it is the only national authority competent to carry out external public audit, in accordance with national and European legislation, on the European funds granted by the European Union to Romania.

The most important requirement of the European regulations for the functioning of this authority is its independence from the other components of the MCS. The MA and the CA are organized in the structure of some ministries subordinated to the Government of Romania, according to the legal provisions of H.G. no. 398/2015. The AA is an operationally independent body vis-à-vis the MA and the CA, as it functions within the Romanian Court of Accounts, the supreme audit institution exercising public audit over the administration and use of the public financial resources. As a result, there is no subordination between the institutions included in the MCS of the operational programs under the authority of the Government and the Audit body.

For the 2014-2020 programming period, in accordance with the provisions of Regulation (EU) No. 1303/2013, as well as with the requirements of the Financial Regulation no. 966/2012, the tasks of the Audit Authority are the following:

• assess the compliance by the MA and the CA with the key requirements for the internal control environment, risk management, control and management activities and monitoring (Annex XIII to Regulation (EU) 1303/2013 - designation audit);

• checks on a representative sample, established as a general rule, on the basis of statistical sampling methods, if the expenditure declared by the national authorities responsible for the management and implementation of operational program financed from European grants, is legal and compliant with the regulatory requirements (the audit of operations);

• audit the proper functioning of the MCS established for the implementation of the operational program (system audit);

• provide reasonable assurance about the amounts declared in the accounts, regarding the completeness, accuracy and veracity of this amounts (auditing of accounts);

• examine the statements in the management statement and the contents of the annual summary drawn up by the management authority;

• to issue the annual audit report stating the most important results of the audits carried out, including the results of the deficiencies found in the MCS and the proposed measures to correct the deficiencies identified;

• annually issues an independent opinion on the authenticity and fairness of the image provided by the accounts, on the legality and regularity of the amounts declared for which the European Commission has been reimbursed and declared in the AC accounts on the capacity of the MCS set up at the level of an operational program to function properly, and whether the audit activity casts doubt on the statements included in the management declaration and in the annual summary;

• send the audit opinion and the annual control report for the previous accounting year, to the European Commission;

• looks at how the audited entities implement the recommendations made following previous audit work carried out by the Audit Authority in order to complete the specific sections of the annual control report in accordance with the model report in Annex IX of the Implementing Regulation application 207/2015 (follow-up audit).

In accordance with the European legislation, the Audit Authority is also required to establish and to the develop an audit strategy for conducting audits, within eight months of the approval of an operational program. The audit strategy is a document setting out the purpose, objectives, audit methodology, sampling methods for audits of operations and auditing of accounts, planning of the audit work to be performed by the Audit Authority for the current accounting year and the next two accounting years and the need to update it annually from 2016 to 2024 inclusive.

According to the requirements of Regulation (EU) no. 1303/2013, the audit strategy must present:

• the body conducting the audits, with specific reference to cross-border cooperation programs, if it does so with its own resources or is used by the Audit Authority of the partner countries. It may also be decided to outsource the audit in the countries participating in the implementation of the operational program (cross border program).

• the audit methodology to be used to carry out audit engagements;

• the method of sampling for operations audits, with the Commission imposing statistical sampling methods and, in exceptional cases, applying non-statistical methods;

• indicative planning of audits and controls to ensure that the main bodies of the program are audited and those audits are spread equally over the current accounting year and the next two accounting years.

The main attributions of the Audit Authority deriving from the European regulations were provided by Law no. 94/1992.

The Audit Authority is headed by a president and two vice-presidents appointed by the Romanian Parliament for a term of nine years and cannot be renewed. At each vice-president level, there are two specialized departments, consisting of 3 or 4 services, and at the level of the president under his direct coordination there is a methodological direction. The number of posts allocated to the Audit Authority is 308, distributed according to the organization chart in the following structure:

A. Audit Department for Large Infrastructure Projects, with 48 positions at central level, where four services are organized:

a) Audit service for multimodal transport projects;

b) Audit service for transport projects for the TEN-T network and the subway;

c) Audit Service for Environmental and Energy Projects - Service 1;

d) Audit Service for Environmental and Energy Projects - Service 2

B. The Directorate for the Audit of Funds for Agriculture, Rural Development and Fisheries with 28 posts, at central level, where three services are organized:

a) Audit Service of the EAGF;

b) Audit Service of the EARDF;

c) Audit Service of the EFD;

C. Audit Directorate for the ERDF with 36 posts at central level, with three services:

a) Audit Service for ROP;

b) Audit Service for POSCCE, POC, OPAT and Internal Affairs;

c) Audit Service of European Territorial Cooperation Programs

D. Audit Directorate for the European Social Fund and other funds, with 32 posts at central level, with three services:

a) Audit Service of the European Social Fund - Service 1;

b) Audit Service of the European Social Fund - Service 2;

c) Audit Service of the European Social Fund and other funds

E. Coordination, methodology, synthesis, audit quality assessment and staff training, with 27 posts at central level, with two services:

a) Synthesis, methodology and audit quality evaluation service;

b) Coordination, strategic development and staff training.

At the territorial level, the Audit Authority has created 8 territorial structures per development region with a total of 137 posts, which are organized as Regional Audit Directorates. Regional Audit Directorates are located within the Alba County Councils, Călăraşi, Ilfov, Dolj, Galati, Timiş, Neamţ and Cluj.

The Statute of the external public auditor of the Court of Accounts of Romania stipulates, among other things, the general conditions for staff recruitment, aspects regarding the development of the external public auditor's career and the continuous improvement of the professional training, but also the rights and obligations of the external public auditor its incompatibilities).

Personnel employed by the Audit Authority must meet the following conditions:

• Have superior training in economics, law or other specialty (eg technical - engineers);

• Have at least 5 years of experience in the specific field of graduate studies;

• Have at least 2 years of experience in one of the areas of control/audit and/or management of community funds;

• Know English;

• Have computer skills.

Auditors of the Audit Authority shall be subject to the requirements of the Code of Ethical and Professional Conduct, put in place in the Romanian Court of Accounts, which establishes the ethical and professional conduct norms as well as the fundamental ethical principles and values to be observed by the staff of the Audit Authority. The ethical principles governing the professional responsibilities of the auditor are: independence, integrity, professional competence, confidentiality, professional conduct and objectivity.

3. Argument of the paper

According to the Regulation on the organization and carrying out of the audit activities of the Romanian Court of Accounts, as well as the valorisation of acts resulting from these activities, published in the Official Gazette of Chapter VII, the procedure for capitalizing the audit reports issued by the Audit Authority is presented in detail.

Audit reports are required to be submitted to the audited entities, in our case to the managing authorities and the certifying authority, respectively the National Procurement Agency, which for the old programming period was part of the MCS for each operational program. Where appropriate, these audit reports may also be forwarded to other interested national bodies, such as the National Anti-Corruption Directorate and the General Prosecutor's Office when there are evidence of fraud, or other authorities of the Romanian State at their express request, such as Parliament Romania, the President of Romania, etc. At the same time internationally, audit reports are made available to the services from the EC, ECA or even the OLAF when there are evidence of fraud.

For identified deficiencies, the Audit Authority recommends that the authorities in the MCS take action to resolve them and the latter are required to carry them out. When irregularities with a financial impact have been identified for non-compliance with Community and/or national regulations, the Audit Authority makes recommendations for the application, in accordance with Community and/or national legislation, of financial corrections or measures to ensure the removal of irregularities/recovery unjustified expenditure, as follows:

1. financial corrections in the case of:

a. non-compliance with the legislation on the implementation of public procurement procedures;

b. systemic deficiencies - when they characterize the entire MCS of the operational program, and which could have consequences for the expenditures made from the funds that finance an operational program and will be declared to the European Commission;

2. Interruption/suspension of payments until correction/removal of system failures;

3. Recovery of ineligible/unlawful expenses, in the case of payments without legal documents, which do not express reality and have consequences for the execution of the works, compliance with the terms of reference, non-compliance with the specifications, tenders, contracts and/or technical design and execution documentation, etc.

The management authorities, notified by the Audit Authority through its reports, according to the Government Emergency Ordinance no. 66/2011, are obliged to carry out their own verifications through the specialized control and antifraud structures to issue the record of determining the receivables to be recovered, which is a debt claim. They are then required to communicate to the Audit Authority the results of their own verifications. If the Audit Authority identifies possible fraud indices, they are communicated for resolution, under the law, to competent bodies with fraud investigation.

The Audit Authority is required, in accordance with the provisions of the European legislation, to monitor how the audited entities implement the recommendations in their audit reports, based on the implementation timetable established with the management authorities. The timetable for implementing the recommendations has to be set in line with the deadlines set by the national legislative framework. Quarterly or whenever needed, entities responsible for implementing audit recommendations shall communicate the state of play on the state of implementation to the audit authority. Verifying how recommendations have been implemented can be done as a distinct task or as a specific objective in the current system or operations audit missions. The follow-up mission is done periodically after a set timeframe based on the complexity and scope of implementation of the recommendations from the previous audits.

4. Arguments to support the thesis

If the recommendations are not implemented or are partially implemented, the management of the audited authorities will also transmit the evidence/documents as well as the reasons that led to the non-fulfilment of the recommendations. In the follow-up missions to the implementation of the recommendations, the evidence, documents and reasons presented will be analysed to ensure that the data and documents on obtaining and using national and European public funds related to them were real and accurate. This analysis may result in the findings of the Audit Authority being maintained, reconsidered or revised as appropriate. The results of these checks are recorded by the audit team in a follow-up report on how to implement the recommendations, which will also be communicated to the audited entities and the EC.

The overall objective of the audit is to conclude for each operational program whether the accounts (financial statements) give a fair and clear picture if the expenditure presented to the Commission for reimbursement

is legal and compliant with national and European legal provisions and if existing control systems way to prevent, detect and correct errors.

The audit opinion is based on the results of audits conducted in accordance with international auditing standards on:

• the proper functioning of the operational program MCS;

• the legality and regularity of the expenditure declared on the basis of a representative sample of operations, as a general rule, by a method of statistical sampling;

• the completeness, accuracy and veracity of the data presented in the accounts drawn up at the level of the CA;

• the level of implementation of the recommendations made during the previous audit missions;

• the correctness of the statements made in the management statement and in the annual summary.

The European Commission, which is the principal recipient of the audit reports and opinions issued by the audit body, after carrying out its own analyses and audit missions in the Member State, may decide that:

A. Payments to the Member State can continue if the accounts (financial statements) give a fair and clear picture if the costs presented to the Commission for reimbursement are legal and comply with national and European legal provisions and if the management systems function properly.

B. Payments may be suspended, suspended or even directly applied to financial corrections for all or some of them at the level of the priorities or operational programs in those Member States if one or more of the following conditions are met:

- there is a significant deficiency in the functioning of MCS of the operational program, which jeopardizes the financial contribution of the European Union and for which no corrective measures have been implemented,

- the expenditure included in the payment request sent to the European Commission is affected by irregularities with a financial impact and having serious financial impact which have not been corrected,

- there is a important deficiency in the quality and reliability on the information from monitoring system, regarding the specific indicators,

- no measures are taken to meet ex ante conditionality,

- there is evidence that results from a performance analysis for a part of the operational program, that has seriously failed to achieve the targets related to that priority on financial and output indicators, and key implementation indicators set out in the performance framework.

The European Commission will decide to lift the interruption or suspension of partial or total payments when the national bodies has implemented the necessary steps to remedy the situation.

5. Arguments to argue the thesis

The situation in several countries of the European Union regarding the location of audit authorities has led to a series of debates. As presented, each Member State has different forms of organization, the only condition being that independence must be ensured. The fact that in Romania the AA is part of Romanian Court of Accounts and fulfils the audit activity for all operational programs is not agreed in certain economic and political environments. Another divergence concerns the preventive part, and it is argued at certain times that the audit authority checks ex-post after spending has been executed, with many financial sanctions being applied. Fund beneficiaries support the idea that those situations that lead to financial corrections must be presented, and many of them are due to factors independent of them, such as the non-harmonized framework with European directives and the case law of the European Commission.

6. Dismantling the arguments against

The main argument that support the form of organization chosen by Romania, namely that the Audit Authority is part of the Court of Accounts, ensure its total independence. The prevention function is an attribute of entities to organize their internal managerial control according to national standards.

The European Commission supports the organizational structure chosen by Romania, the recent intentions to amend the law on the Court of Accounts led to a series of warnings on the blocking of the funds granted.

7. Conclusions

The Audit Authority in Romania, established at the level of the Romanian Court of Accounts, fulfilled the most important requirement stipulated by the European regulations for its functioning, namely its independence from the other components of the MCS. There is no report of subordination between the MA and the CA under the authority of the Government and the Audit Authority of the Court of Auditors.

Continuing to ensure independence Parliament appoints the leadership of the Audit Authority for a 9-year mandate to talk about a certain stability in time from a decisional point of view. By comparison, the leadership of some ministries or government agencies is secured at most for

4 years, but reality has shown us in recent years that we are talking only for 2 years. From an organizational point of view, the Audit Authority covers all development regions, thus ensuring the auditing of all regional intermediary bodies such as Regional Development Agencies and a sufficient number of fund beneficiaries. As a human resource, the recruitment criteria ensure the recruitment of staff with specific experience in audit activity, control and implementation of European grants. The principles governing the work of auditors are in line with international auditing standards on professional conduct, professional competence, confidentiality and objectivity.

Considering the audit obligations established by the European regulations, the fact that the Audit Authority has been involved in the designation audit provides the part of the prevention that has been recently insisted on in the Romanian media. The designation audit gives you the opportunity to analyse institutional building on all its management components before the actual operational program runs and to issue recommendations on those areas where the risks are high that the management and control system does not work properly, declared to the European Commission to contain a number of irregularities with financial impact. Subsequently, in the framework of the first system audits, it is possible to adjust some aspects that seemed to fit in the design but later in practice created a series of bottlenecks in the implementation of the projects.

Considering audit recommendations, the MA and CA should attach particular importance to these decisions in view of the decisions that the European Commission can take to suspend payments or to apply financial corrections with a major impact on the implementation of the national budget. Such a European Commission procedure involves at least 6 months of European funds being blocked, and all commitments under the funding contracts will be borne by the state budget.

National regulatory acts have created the appropriate legal framework for the MA and the CA to carry out their own verifications and to undertake legal measures to recover budget receivables or to correct deficiencies resulting from the functioning of the MCS. When the conclusions of its own checks are in contradiction with audit recommendations, it is necessary to re-examine the Audit Authority so that the final conclusions are in line with reality and the European Commission is properly informed.

If we take into account that the audit term comes from the Latin auditum = listening, we can conclude that we have to listen to the audited entities and then give an independent opinion based on real facts.

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