

Summary of the results of the audit “Functioning of the internal financial control system of the Structural Funds”

2.1. Overall assessment of the audited activity

The system for management and control of the Structural Funds in Poland meets the requirements set out by the European Commission and it basically assures detection of irregularities in the utilization of these resources. However, the procedures for management and financial control adopted within operational programmes were too extensive and they introduced duties that were not required by the community law. This, in practice, resulted in delays in utilization of the Structural Funds at the level of final beneficiaries, Implementing Authorities, Intermediary Authorities and Managing Authorities, which is assessed negatively by the NIK. Expenditures in the three audited sectoral operational programmes¹, about refunds of which the Managing Authorities applied by the end of 2005, stood at EUR 75.8 million, which constitutes 8.3% of the allocation² for 2004, and 2% of the allocation for the years 2004 – 2006. In the opinion of the NIK, a low level of the utilization of the Structural Funds within operational programmes, in particular the Sectoral Operational Programme “Transport”, poses a risk of losing some finances from the allocation for 2004.

The audit findings indicate the following reasons for such a situation:

- delays in development of legal acts, guidelines and procedures for implementation of the programmes and a necessity for their multiple amending,
- creation of a too complex system, which hampered due and prompt development and verification of payment and refund applications. The solutions that had been adopted resulted in dispersed responsibility, prolongation and repetition of activities in the process of multi-level verification of applications,
- unclear procedures and guidelines which created difficulties in development and settlement of projects by beneficiaries,
- failure to implement the IT system for monitoring and financial control (SIMIK), although PLN 12.6 million were spent on this purpose,
- inappropriate organization of works, staff rotations, insufficiently qualified personnel and insufficient number of employees in some institutions.

Furthermore, the NIK negatively assesses the establishment of a too complicated system for notifying of irregularities and its functioning. It has been established that the tasks regarding internal audit, control over implementation of the operational programmes, securing and archiving documentation and division of duties related to making, verifying and confirming

¹ The audit covered the following Sectoral Operational Programmes: “Transport” (SPO Transport), “Increase in Competitiveness of Enterprises” (SPO WKP) and “Human Resources Development” (SPO RZL). The audit covered the period from 1 May 2004 to 31 July 2005, whereas its findings were updated, when possible, as at the day of the completion of the audit in the entity.

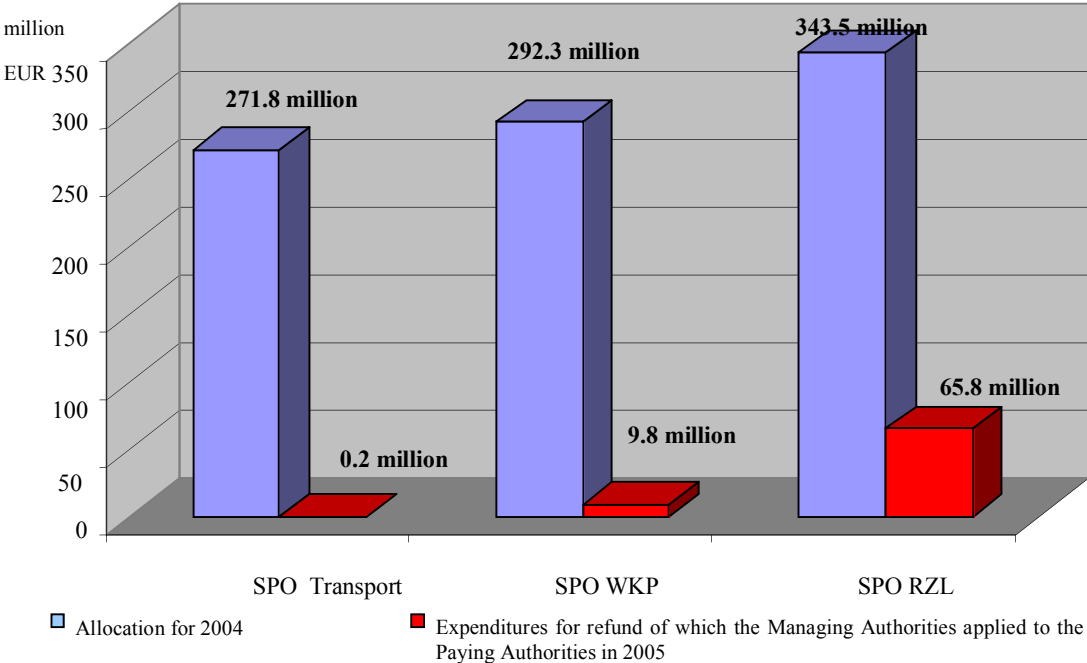
² The amount of the structural funds designated by the European Commission for the implementation of the programmes in a programming period.

financial operations were generally performed in an appropriate manner, and minor errors and irregularities found at the preliminary stage of the implementation were removed.

2.2. Synthesis of audit results

2.2.1. The allocation for Poland for the years 2004 – 2006 for operational programmes subject to audit stands at EUR 3,884.5 million³. By the end of December 2005, the Managing Authorities applied to the Paying Authorities for a refund of resources at the total value of EUR 75.8 million⁴. The risk of a failure to make use of EU finances mainly refers to the Sectoral Operational Programme “Transport” (SPO Transport) and the Sectoral Operational Programme “Increase in Competitiveness of Enterprises” (SPO WKP), which are co-financed from the ERDF.

Figure 1. Expenditure from the allocation for 2004 as at 31 December 2005



So far, the level of the utilization of ERDF funds reveals a serious threat of losing part of the allocation for 2004. To prevent this, Poland, in compliance with the n+2 principle⁵, should transmit, by the end of 2006, applications at the amount of EUR 554.2 million to the European Commission. The utilization of finances from the ESF is better. At the end of 2005,

³ Including: SPO RZL – EUR 1,470 million, SPO WKP – EUR 1,251.1 million, SPO Transport – EUR 1,163.4 million.

⁴ Including: SPO RZL – EUR 65.8 million, SPO WKP – EUR 9.8 million, SPO Transport – EUR 0.2 million.

⁵ Pursuant to Article 31 of the Council Regulation (EC) No 1260/1999 laying down the general regulations regarding the Structural Funds (Official Journal of the EU No L 161 with amendments) if a Commission commitment included in the community budget in the given year (the n year) has not been settled by a payment application transmitted to the EC by the Paying Authority of the member state by the end of the n+2 year, the difference between the amount of the commitment and the amount of payment applications shall be automatically decommitted.

the Managing Authority applied to the Paying Authority for a refund of EUR 65.8 million, i.e. 19% of the allocation from the ESF for 2004 (Pronouncement, page 23-24).

The low level of the expenditure of funds resulted from, for example, excessively complicated and extended procedures which hampered and delayed the implementation of the programmes. Furthermore, legal acts, guidelines and procedures necessary for the implementation of the operational programmes were issued by the Managing Authorities with a delay, and they were not appropriately developed, which was reflected in their frequent corrections and amendments. The delay at the first stage of the implementation resulted also from the development of drafts of basic documents, such as application forms, contracts with beneficiaries and reports on implementation, via executive documents⁶.

2.2.2. Out of 46 audited institutions involved in the implementation of the operational programmes, 30 entities were obliged to develop procedures for management and control, and to present them to competent institutions for approval⁷. Both the development of these projects and the process of their arrangement were lengthy and lasted from one to thirteen months. Although the implementation of the programmes began in 2004, by December 2005 four institutions failed to meet this obligation in an appropriate manner. The audit has also disclosed that the adopted procedures required numerous changes, which hampered the implementation of the programmes (Pronouncement, page 26).

The procedures regarding development and verification of payment and refund applications were too complicated, time-consuming and inflexible. Repeated activities in the process of multi-level verification of SPO WKP and SPO RZL applications prolonged this process, and resulted in dispersed responsibility for appropriate performance of particular tasks. The solutions adopted by the competent Managing Authorities and Paying Authorities regarding verification of refund applications with regard to contents on the basis of lists of expenditures only, without access to source documents, did not allow the Managing Authorities for their appropriate verification (Pronouncement, page 28).

The NIK has found that “System for notifying of irregularities regarding utilization of the Structural Funds”⁸, approved by the Ministry of Finance, was extended and too complicated (too many forms and addressees of notifications of irregularities exceeding EU regulations were introduced), and with regard to amounts of irregularities, it was partially incompliant with Article 12 of the Regulation No 1681/94⁹. As a result, some institutions adopted

⁶ During the audit of the preparedness of the public administration for obtaining and making use of the Structural Funds, carried out in the 4th quarter of 2003 (pronouncement of March 2004, KAP-41005/03, No 12/2004/P/03/065/KAP), the NIK observed a necessity to accelerate adjusting works related to implementation of the operational programmes and to develop effective mechanisms for coordination of the process of utilization of the Funds.

⁷ The obligation did not apply to Regional Financing Authorities (RIFs).

⁸ The document was developed by the Interdepartmental Working Group on preventing irregularities with regard to utilization of EU funds and, having been accepted by all Managing Authorities of the operational programmes, it was approved in July 2004 by the Governmental Plenipotentiary for Combating Fraud against the Republic of Poland and the European Union at the Ministry of Finance.

⁹ The Commission Regulation (EC) No 1681/94 of 11 July 1994 on irregularities and the recovery of sums wrongly paid in relation to the financing of the structural policy and organization of the information system in this area (Official Journal of the EU No L 178).

procedures that prolonged the process of notification and it consequently added to unreliable¹⁰ and delayed transmission of notifications of irregularities to authorized entities or a lack of them (Pronouncement, page 32-33).

2.2.3. At each level of the implementation of the sectoral operational programmes, there were irregularities regarding development and verification of payment applications and refund applications. The NIK positively assesses the ability of the entities involved in the implementation of the programmes to detect errors made in the process of development of payment applications. The audit has disclosed, however, that these errors resulted, to a large extent, from unclear procedures and guidelines. This added to inappropriate development of payment applications by beneficiaries which, in turn, prolonged the verification process (over 70% of applications required corrections). Besides, 15 out of 21 Implementing Authorities made formal and factual errors in refund applications at the total amount of PLN 148 million, i.e. 50.8% of the value of the applications subject to audit (Pronouncement, page 28).

Furthermore, the SPO WKP Managing Authority and the SPO RZL Managing Authority negligently developed 4 out of 5 applications filed to the Paying Authorities related to refunds of expenditures from the ERDF and the ESF at the total value of EUR 3.7 million (35.3% of the value of the applications filed), which delayed the activities of the Paying Authorities by 14 to 75 days. The audit has also showed that in 5 refund applications transmitted by these Managing Authorities¹¹ the amounts were inflated by total EUR 2,400, which resulted in an incorrect development of payment applications to the EC by the Paying Authorities (Pronouncement, page 30-31).

2.2.4. The findings of the audit show that the audited institutions (excluding the SPO Transport Managing Authority) carried out 1,274 audits and monitoring visits altogether. With regard to irregularities disclosed during verification of payment applications and the said audits, 185 pronouncements on irregularities were developed. In 9 out of 45 audited institutions, negligence in the obligation to send required notifications of irregularities has been found. Moreover, reports on irregularities were submitted to the EC after the required deadlines set out in the European regulations (with delays from 3 to 90 days). Additionally, the Minister of Finance did not submit to the EC the required reports on the SPO WKP and the SPO Transport for the period from the 4th quarter of 2004 to the 2nd quarter 2005 (Pronouncement, page 31-35).

2.2.5. In all audited institutions, the division of duties regarding performance, verification and approval of financial operations on the Structural Funds was compliant with financial control standards. However, in two Regional Labour Offices (WUP) the procedures for replacing

¹⁰ As a result of conversion of all sums of irregularities not exceeding EUR 4,000, in accordance with the appropriate exchange rate, the NIK auditors have not disclosed cases where the Ministry of Finance would be obliged to report to the EC.

¹¹ It applies to the SPO WKP Managing Authority and the SPO RZL Managing Authority. In the audited period, no indirect payment applications were submitted to the EC within the SPO Transport.

employees involved in the implementation of the programmes were not established (Pronouncement, page 35).

2.2.6. The findings of the audit show that only 1 out of 46 audited institutions did not meet the obligation to develop procedures for protecting and archiving documentation related to the programmes implemented. In one case, the procedures were incompliant with the European requirements regarding the period for documentation storage. The audit has also disclosed that in 2 entities there were cases of disobeying these procedures (Pronouncement, page 36).

2.2.7. Minor irregularities and irregularities have been detected with regard to audit implementation in 7 out of 22 entities¹². They were related to delays in establishing organizationally and functionally independent internal audit units (from 60 to 180 days)¹³ and delays in employing internal auditors (from 30 to 120 days)¹⁴. In two entities, the procedures did not cover the tasks of Regional Labour Offices regarding the implementation of the operational programmes. Moreover, two Regional Labour Offices developed audit plans without making a thorough risk analysis. In the audited period, audit units of 21 entities carried out 37 audit tasks altogether. Only one Regional Labour Office did not carry out any audit tasks (Pronouncement, page 37).

2.2.8. The activities of the Ministry of Finance regarding the establishment of the SIMIK system and its functioning proved ineffective. The introduction of the system started in 2002 and the deadline for the completion of works was frequently rescheduled. The software was delivered in December 2004, however by the end of the audit the SIMIK system was not introduced for the audited operational programmes, although PLN 12,629,900 altogether had been spent on this purpose. The lack of the system resulted in additional costs incurred by the institutions involved in the implementation of the operational programmes. For example, the Polish Agency for Enterprise Development (PARP) developed a substitute system in order to provide current monitoring of co-financing applications submitted by beneficiaries, which cost PLN 394,000 (Pronouncement, page 41).

2.2.9. The down payment from the Structural Funds transferred by the EC in 2004 for covering the Community contribution in the amount of EUR 1,354.8 million¹⁵, including EUR 349.6 million from the audited operational programmes, was temporarily transferred to the state budget account instead of being directly transferred to a separate bank account¹⁶. The NIK observes that, pursuant to Article 30d, paragraph 1 of the Act of 26 November 1998 on

¹² With regard to 6 institutions (i.e. the Ministry of Economy and Labour (MGIŁP), the Ministry of Finance (MF), the Ministry of Infrastructure (MI), the Ministry of Science and Information Society Technologies (MNIł), the Ministry of National Education and Sports (MENiS) and the Polish Agency for Enterprise Development (PARP)), the obligation stemmed from the Act on public finance which was in force at the time (Article 35d), for the remaining 16 institutions, i.e. Regional Labour Offices, it was laid down in agreements on financing.

¹³ The Regional Labour Offices in Toruń, Kielce, Kraków and Szczecin.

¹⁴ The Regional Labour Offices in Białystok, Toruń, Kielce, Szczecin and Warsaw.

¹⁵ Out of which: ZPORR – EUR 475 million, SPO RZL – EUR 235.2 million, SPO WKP – EUR 200.2 million, SPO Transport – EUR 186.1 million, SPO RiPR – EUR 32.3 million.

¹⁶ Before the decision on transferring the down payment to the state budget account was taken, the Director General of the EC Budget was notified of this by the Undersecretary of the State at the Ministry of Finance in a letter of 27 April 2004.

public finance¹⁷ which was in force at the time, finances from the Structural Funds should be accumulated in separate bank accounts and they could be spent up to the amount collected in these accounts. Whereas, pursuant to Article 32, paragraph 2 of the Council Regulation No 1260/1999 “throughout the lifetime of assistance, the Paying Authority shall use the payment on account to pay the Community contribution to expenditure relating to this assistance”. Furthermore, the records on the EU finances were kept at the Ministry of Finance in such a manner that did not provide for permanence of records as required by Article 23 of the Act on accounting¹⁸ (Pronouncement, page 42).

2.2.10. In the audited entities, there were 1,500 people employed altogether performing tasks related to the implementation of the Structural Funds. About 96% of the employees had a university degree, and over 25% had additional post-graduate education in the field of European integration. Almost 93% of the employees had knowledge of foreign languages. In the audited period, over 4,200 trainings were organized, however not all of them proved effective. The NIK has observed considerable staff rotation (almost 17%), as well as little experience of the employees in servicing assistance programmes (84% - below three years, 22% - below one year), which, according to the NIK, resulted in the irregularities disclosed during the audit (Pronouncement, page 38).

2.2.11. Financial results of the audit: PLN 231.9 million¹⁹ (Pronouncement, page 28 and the following).

2.3. Final remarks and conclusions

According to the NIK, delays in the implementation of the operational programmes in 2004 and 2005 will result in a considerable accumulation of payments to be made in the following years (in 2005 only 14% of the expenditure plan of the audited operational programmes were implemented). This may hamper the works of the institutions concerned which will not be able to promptly and diligently perform their duties with regard to, for example, verification of payments made by beneficiaries. This may, in turn, pose a risk of refunding expenditures that are not eligible for assistance from the Structural Funds, and, as a consequence, a necessity to return finances to the EU budget if such irregularities are detected by the European Commission or the European Court of Auditors.

Therefore, the management and coordination by the Managing Authorities of the activities taken by the entities involved in the implementation of the operational programmes must be

¹⁷ Journal of Laws of 2003, No 15, item 148 with amendments. Since 1 January 2006, Article 201, paragraph 1 of the Act on public finance of 30 June 2005 has been in force (Journal of Laws No 249, item 2104).

¹⁸ Journal of Laws of 2002, No 76, item 694 with amendments.

¹⁹ Out of which: PLN 118,029,800 – amount of expenditures for 2005 that were not realized by the PARP; PLN 89,173,100 – value of the applications sent by the Implementing Authorities after the deadline; PLN 18,739,200 – value of incorrectly developed applications; PLN 5,846,000 – applications considered after the deadline; PLN 58,500 – amount of irregularities regarding utilization of resources detected by the Implementing Authorities; PLN 9,200 – amount of ERDF and ESF refund applications inflated by the Managing Authorities. As a result of the NIK’s audit, PLN 57,000 were recovered.

improved. It is necessary to introduce essential systemic changes that would eliminate unjustified delays at the stage of payment realization, especially in view of the fact that the expenditure planned for 2006 is 2.5 times higher than for 2005. Activities of the Managing Authorities should aim at simplifying the existing implementation system, for example through elimination of the procedures that result in overlapping activities at various stages. This should add to a clear division of responsibilities for appropriate performance of tasks. Too complicated and unstable procedures, as well as redundant and unclear requirements make the process of project development, selection and implementation as well as refunds of expenditures difficult for beneficiaries. The findings of the NIK's audits reveal a tendency to burden the institutions involved in the implementation of the Structural Funds with additional duties that are not required by the Community legislation. Difficulties in prompt performance of particular tasks result also from the differences between management and implementation procedures adopted in Poland regarding both particular operational programmes and measures within them. This made institutions implementing more than one operational programme or measure develop numerous separate procedure manuals, the complexity of which depends on the Managing Authority.

Lack of appropriate coordination and clear division of competence with regard to management of the Structural Funds adds to delays in the implementation of the operational programmes. The findings of the audit show that both the Managing Authority (Ministry of Regional Development – MRR) and the Paying Authority (Ministry of Finance – MF) consider themselves the institutions responsible for the implementation system on behalf of Poland.

The NIK has frequently indicated problems with staff rotation and adjustment of the organizational structure to performance of tasks related to servicing EU finances found in the audited institutions, which adversely affected the use of the Funds²⁰. A prerequisite for improvement in the utilization of the Structural Funds is a significant strengthening of institutional capacity of the entities involved in the implementation of the programmes, in particular through providing an adequate number of employees and proper remunerations for them, so that to prevent undesired staff rotation.

The adoption and implementation by the government of the activities set out in “Repair programme improving absorption of the Structural Funds in the framework of the National Development Plan 2004 – 2006” which aim at, for example, simplification of the rules for verification of payment applications that should eliminate repetition of the same activities at various implementation stages, is to improve the level of the Structural Funds utilization. However, achievement of the main goal of “the Repair Programme” will require coordinated and intensive activities on the part of all entities that implement the programmes.

²⁰ For example, during the audit carried out in the 3rd and 4th quarter of 2004 regarding the preparedness of the public administration for obtaining and making use of the Cohesion Fund (Pronouncement on the results of the audit of June 2005, No 133/2005/P/04/004/KAP).

In reference to the abovementioned assessments and comments, the NIK appeals for:

- 1) undertaking activities aimed at improving the coordination of management of the operational programmes by the Prime Minister;
- 2) accelerating the implementation of the SPO Transport, the SPO WKP and the SPO RZL by the Minister of Regional Development, so that to avoid losses in the funds from the allocation for 2004 – 2006;
- 3) analyzing and simplifying the procedures by the Minister of Regional Development and the Minister of Finance, so that to eliminate delays in the implementation of the operational programmes;
- 4) considering, by the Minister of Regional Development, an introduction of unified rules and procedures for management and control for all operational programmes;
- 5) reliable and prompt notifying, by the institutions involved in the implementation of the operational programmes, of irregularities or lack of them;
- 6) appropriate and prompt development and verification of payment applications and refund applications by beneficiaries and the institutions involved in the implementation of the operational programmes;
- 7) introduction, by the Minister of Regional Development and the Minister of Finance, of rules for carrying out comprehensive verification of payment applications by the institutions that dispose of complete financial documentation;
- 8) immediate implementation by the Ministry of Finance of the IT system for monitoring and financial control – SIMIK;
- 9) providing appropriate personnel in the institutions involved in the implementation of the Structural Funds and appropriate remuneration for them, so that to reduce staff rotation.