

DISTURBING FACTORS IN THE AUDIT OF PROJECTS WITH EUROPEAN FUNDS

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Abstract:

The present paper presents the results of a study based on a theoretical research upon the concepts used in the audit of projects funded through structural funds, as well as an enquiry based research which intercepted various practical aspects regarding the used procedures and techniques, and moreover the difficulties encountered during the implementation of the audit, considering the specific aspects that must be followed in order to issue opinions on the certification of eligible expenses and more.

This study aimed to shape an image regarding the project audit (to clarify the characteristics of this type of audit), given the existing discussions on the definition of the project audit concept, as well as the identification of irregularities that may occur during the project implementation with the help of the audit reports elaborated by the independent auditors.

The purpose of this paper is to surprise the importance of a performing project audit, the paper itself representing a guide for the beneficiaries of grants, as well as for those who conduct such an audit for a better communication between the beneficiary and the auditor, the latter being one of the main disturbing factors.

Keywords: *audit, project, irregularities, European funds, accountancy, eligible expenses.*

JEL classification: M4

1. The concept of audit in terms of the European funds-granted projects

The term audit knows several meanings given the objectives aimed during the mission. In projects, the audit is defined as a re-examination and evaluation of the project with its various forms and objectives and typical problems encountered when conducting this audit and evaluation process.

In general, the audit consists of the collection and evaluation of certain evidence regarding the information, in order to determine and report the degree of conformity of the respective information with a series of re-established criteria. The audit must be performed by a competent and independent person, a characteristic also met in the project audit (Loebbecke, A., 2003). The competent and independent person who performs the audit, called auditor, must know the evidence types and quantities, analysed in order to get to the right conclusion, while proving an attitude of independence; for this reason, its moral and professional quality represents one of the factors that influence the quality of the performed audit.

The audit objectives, exerted within the European Commission on structural funds, are represented by the establishment of the efficiency of management and control systems (the continuous and proper functioning of the internal control system), the existence of an audit trail on the control-submitted operational programs (the existence of sufficient documentation), the profitability of co-financed operational programs, the eligibility of expenses and the observance of community policies, as well as the

correctness of payments performed through European funds or national co-financing (Cuenca J.L., 2002).

The European Commission considers that the main bodies implied in the audit of structural funds-financed projects are: The European Audit Court (the external public audit of the European Commission), supreme audit institutions of the member states (the Audit Court by the Audit Authority, the external public audit), the audit services from the member states (the bodies with attributions in the performance of the internal public audit); the individual audit of the final beneficiaries (the independent financial audit)(Lesconi M., Breuer A., Breuer B., 2012). More responsibility therefore lies for each Member State preserve the audit trail and conduct the necessary controls and checks , so the Managing Authority must make the “site visit” of the project, the Audit Authority must make the “control checks” on projects, the Certificate Authority must make the “follow up checks” (Smail R., 2007) and the independent financial audit must make the “conformity checks”.

The project audit is very important for the beneficiary and also for the Managing Authority, because the audit report should comprise the expression of an authorized opinion upon the objectives assumed under the Financing Contract (Avram V., Togoe G.D., 2013).

Analyzing the elements presented in the above mentioned definition, we consider that an important stage is the collection and evaluation of evidence, as well as the procedures used during the audit mission. The international audit standards require the use of specific procedures in order to obtain evidence, such as: inspecting, observing, requesting information and confirmation, calculating and analysing facts (documents), analytic procedures, corresponding to the requirements (Rusovici, A., Cojan, FI., Rusu, Gh., 2000). As regards the procedures used in the project audit, they are similar to the ones used in the financial audit, i.e. each represents a careful investigation of the audited subject/object, their results being different.

The audit standards relevant for the project audit are: ISRS 4400 „Missions for procedures regarding the financial information”, ISA 500 „Audit evidence”, as well as ISA 520 „Analytic procedures”, being known and applied by all auditors that belonged to the target group within the performed research. In some papers we can find also ISA 315 „Identifying and assessing the risks of material misstatement through understanding the entity and its environment” in which it carries out its activity, offering to professional auditors the basic elements that may be used in the process of evaluating the audit risk Contract (Avram V., Togoe G.D., 2013).

According to the legal stipulations of the European funds, the financial independent and authorized auditor verifies if all expenses declared by the beneficiary (the part contracted with the management authority) in the temporary or final grant/refund application are real, accurately registered and eligible according to the stipulations of the financing contract and issues an expense evaluation report according to the standard format provided by the financer, or in the absence of such a format, in accordance with the legal stipulations within the audit.

Some authors (Botez D., 2012) consider the grant expenditure verification by an auditor a specific professional intervention in relation to Structural Funds project.

Performing an analysis of the audit companies within the project auditing, we can observe that the following services are included in the package, mainly, the conformity of the grant applications submitted with the conditions of the financing contract (if the grant was spent according to the terms and conditions of the financing contract), the conformity of the beneficiary’s accounting records with the regulations regarding the registrations and with the accounting regulations from the financing contract (in our opinion, in the instructions, in the implementation and work procedures

manuals), the verification of information in the refund application, if they reconcile with the accounting system and with the beneficiary's registrations, with the authenticity and the authorization of the initial budget and if the performed expenses were stipulated in the budget. Here we can add certain services specific to the performance audit such as: identifying in time the problems that may occur during the project implementation, improving the project performances, speeding up the results, identifying the mistakes, fixing and avoiding them in the future, or reconfirming the interest and the engagement in the project. From this statement we can see the different ways of understanding the concept of audit projects, if the certain auditors carry out only an audit of expense conformity performed with the legal and the financing contract stipulations, other auditors include in the provided services activities specific to the financial audit, while others include activities corresponding to the performance audit.

Professionals know, however, that the audit mission is part of the broader category of insurance, i.e. missions that provide beneficiaries with a certain degree of assurance on the information they shall draw up and publish them. Professional intervention of structural funds is not part of the category of insurance, so it is improper to call the audit mission. (Botez D., 2012)

Other authors consider that the audit of this type of projects should be limited at the requirement expressly stipulated under financing contracts and supposes a series of activities, such as: the analysis and verification of the nature, legality, accuracy and eligibility of expenses, the verification of using the amounts received in advance; the audit of third parties' accounts, the comparison of the expenses with specially assigned accounts and the project budget, the verification of project incomes (inclusively of the advances received from the financier, interests to the advances and other incomes generated by the project), etc. (Avram V., Togoe G.D., 2013).

Following a research conducted among the audit specialists, which have performed at least one audit mission, the activities developed during the audit mission, in the opinion of 94% of the respondents, supposes the verification of the project expenditures according to the financing contract and the technical specifications, as appropriate, only one project auditor emphasizes the fact that a project audit also supposes a technical audit. In this context, we considered it necessary to outline the audit typology to which the project audit approaches, in the view of the practitioners, thus to the question as to whether the project audit can be limited to a project financial audit, 50% of the respondents answered affirmatively and 50% negatively, and to the question as to whether the project audit can be limited to a project performance audit, 25% of the respondents answered affirmatively and 75% negatively.

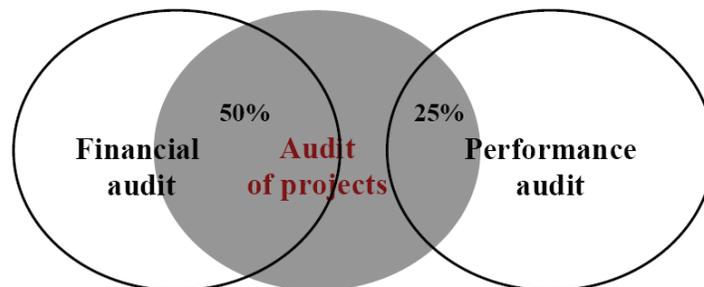


Fig.1. Defining the concept of project audit considering the audit typology

We consider that the independent financial auditors engaged in the development of audit missions of projects financed through structural funds perform a conformity financial audit on the expenses requested for refund contained in the grant application

and its annexes, the audit report containing opinions on the eligible expenses, in terms of reality, legality and accuracy.

2. The role of audit in detecting the irregularities specific to EU financed projects

The irregularity, according to the applied national legislation (the stipulations of the Government Ordinance no. 40/2008, amending and supplementing the Government Ordinance no. 79/2003 on the control and recovery of community funds, as well as of the misused co-financing funds), represents any discrepancy from the legality, regularity and consistency with the national and/or European law as well as with the stipulations of the contracts or of other legal engagements, that affect the general budget of the European Community and/or the budget managed by it, as well as the budgets from which arises the related co-financing through an undue expense.

Given the typology of irregularities (depending on the criteria such as causality, impact, frequency) we can exemplify the following types of irregularities, encountered in the implementation of projects financed through structural funds:

- *irregularities in the accounting records*: the existence in the project accounting of incorrect, forged records or even the omission of accounting records, or the lack of accounting documents; undisclosed;

- *wrong documentation*: incomplete or missing documents, insufficient certificates, groundless, false or forged financing applications, incomplete or missing, incorrect, forged supporting documents, unfounded, false or forged certificates, or other wrong documents;

- *ineligibilities*: ineligible beneficiary or partner, ineligible financing measure, ineligible activity or ineligible expense;

- *irregularities committed by the beneficiary/contractor*: incorrect identity, inexistent beneficiary/contractor, inadequate description of the beneficiary/partners, beneficiary/contractor without the required quality or other irregularities committed by the beneficiary/contractor related to the assumed commitments;

- *irregularities related to the financing right*: compliance of dates, accumulation of incompatible financing, control refusal, payment refusal, lack or incompatibility of the contract or the funding order, more different applications (pre-financing or refund) with the same object, non-compliance of other regulations/contractual conditions, breach of regulations on public acquisitions;

- *further irregularities on the financing right*, and measures not implemented or completed (activities in the project, measures established by the managements authority or by other competent authorities), actions developed with complying the rules, false statements, unjustified expenses, expenses outside the period of the contract or the funding order, infringements of the co-financing system, undeclared income or corruption documents.

When we speak about irregularities, we speak about the risks that the auditor has regard: whether the risk is a fraud risk, whether the risk is related to recent significant evolutions of economic and accounting nature, imposing a special attention; the complexity of transactions, whether the risk involves significant transactions with affiliated parties (Avram V., Togoe G.D., 2013).

In the view of the auditor practitioners which responded to the questionnaire of the project audit research, the main categories of irregularities identified after performing the audit mission were the following: the lack of supporting documents, inconsistencies between the interim and final financial reports, inconsistency of eligible expenses, failure to comply headings, problems regarding the internal control of the

beneficiary due to insufficient intern implemented control procedures, lack of separate accounting records of expenses on separate budget lines of the project due to the use of less performance software, the transparency of the organization and development of auctions or the existence of incomplete acquisition documents.

In the last European Anti-Fraud Office (OLAF) report published in July 2012, for the period 1 January to 31 December 2011, the most frequent fraud cases are concerned with offences, such as (http://ec.europa.eu/anti_fraud/documents/reports-olaf/2011/olaf_report_2011_en.pdf, 2012):

- forgery of expense settlement documents;
- fund misappropriation;
- overestimation of assets;
- simulation of tenders, forged tenders;
- illegal subcontracting of works awarded at the tender.

3. Factors that influence the quality of the performed audit on the projects financed through European funds

As regards the multitude of factors that limit the project audit, the time and money represent the two most frequent and obvious factors that limit the depth of the research and the detailing degree of the presentation in the audit report. Another factor is represented by the anxiety caused by any research, in general, determining the involved persons to have a defensive attitude. If the report is not drafted in a constructive tone, the team morale will suffer. Often, the audit of the technical aspects cannot be very deep, because the person researching does not have the necessary technical skills. In this case, a technical audit is required. The moments, in which the audit is developed, differ, in general, the later it is performed, the lower its immediate value, for the project, but it will have a higher value for the organization.

In the opinion of some authors, the success of an audit mission of a project financed from European funds supposes first of all the familiarization of the auditor with the audited activities of the entity (Avram V., Togoe G.D., 2013), so “lack of knowledge” can be consider a factors that influence the quality of the performed audit.

Given the definition of the project audit, we consider the project accounting as an important information source in the audit mission, thus in the conducted research, the comments on the phrase „accounting, information source in the project audit”, we can mention the following:

- the auditor verifies if the expenses declared by the beneficiary in the interim and final refund applications are real, properly recorded and eligible according to the stipulations of the financing contract and issues an expense verification report according to the standard format provided by the management authorities, and the beneficiary must provide the independent and authorized technical auditor with all the documents and required information and ensure all proper conditions for the verification of the expenses;
- the economic and financial effects of the project implementation are outlined in accounting often as tangible and intangible assets, in order to be monitored later;
- the project audit is performed with information provided by the project accounting;
- the documents that are the basis of determining the performance of the financial operations within the project and which reflect the developed activities are the financial-accounting documents;

- the verified aspects are corroborated with the information recorder in accounting, fairly and truly reflecting the financial operations within the project, thus constituting an important information source;

- even if the verified expenses are recorded in the financial report or the expense record, the accounting represents the basis of the audit mission;

- the evidence used by the auditor for the performed expenses are mainly based on the accounting documents, the accounting records and the financial statements elaborated in the beneficiary’s accounting.

The role of the financial project management, in general and of the project accounting, especially in a quality audit can be observed also in the categories of financial documents elaborated during the project implementation applied by the auditor in order to accomplish the audit mission, among these (in order of frequency) we mention: the refund application, the financial report, the expense record, the progress report and sometimes the pre-financing application.

In the view of the auditor practitioners which responded to the questionnaire of the project audit research, the important factors in a performance (quality) project audit, (in order of importance) are the following: the quality of the audit team members, the correct elaboration of the documents by the applicant, the access to the project documents, the compliance of audit standards and communication with the beneficiary.

4. Conclusions regarding the problems encountered by the auditors in the audit mission

In conclusion, we would like to present the problems identified after the research conducted among the practitioners of the project audit, thus the main problems the auditors have confronted with in the audit mission, and the solutions identified by them in solving these problems, were the following:

Table 1. *Problems and solutions identified in the project audit mission*

Problem	Solutions
Limiting the verification works due to the delay of the submission of the documentation necessary for the audit mission;	Reconciliation of terms with the beneficiaries;
Access to information sources;	Discussing the matter with the management factors;
Poor communication, misunderstanding of terms;	Explanation of terms;
Poor communication due to the lack of supporting documents;	Repeated requests of documents, explanation of the work methodology and of the contractual terms; Setting the deadlines with the beneficiary.
Changing the terms of reference for the development of the audit process;	No solution was found, the contracting authority rejects the audit report and does not issue the money instalment from the grant, being a compromise that puts to a test the continuation of the audit contract.
Implementing complex rules;	The continuous professional training and permanent information.
Great amount of information sources	Clear division of responsibilities within the audit team.

(Source: Table created by the authors based on the questionnaire information processing)

Considering the above mentioned (from the point of view of the financier, but especially considering the objective of the audit mission), the project audit is necessary in the conditions in which the management authorities do not intensify the control measures, having a very important role in the fight against fraud, in the conditions in which certain irregularities can be depicted in the structural funds management. Also, even if the opinions

regarding the definition of project audit differ, we can state our proposals in order to improve these activities:

- computerizing the verification procedures capable of issuing opinions considering the purpose of the project audit mission, an example being the programs existing for the financial audit of the financial statements;
- the existence of some clearer stipulations in the financing guides regarding the purpose of the project audit and the applied standards;
- setting some common instructions regarding the format of the audit report;
- the organization by the management authorities of some auditor training sessions;
- the auditor should allocate sufficient time, at the stage of planning in order to understand the project operation, the object for which financing is allotted, the budget limits, the indicators that should be performed after the project implementation.
- Setting in the service providing contract closed between the auditor and the beneficiary of some terms regarding the submission of the applied documents;
- Stability regarding the decisions of the management authorities on the rules applicable to the financial management, accounting and project auditing.

In this context, we consider opportune to present proposes of the Chamber of Financial Auditors of Romania (CAFR) about the ways of cooperation with the management of the structural funds:

- participation with its own specialists in training/specialization of personnel management bodies or those specific areas on the intermediate of the nature required audit of projects financed;
- creating special guides, such as to improve the quality of the work carried out by the auditors;
- monitoring the work of auditors who have conducted missions in the framework of EC-funded projects, in order to identify the aspects that influence the quality of audit work, along with some proactive steps for counselling, training and subsequent monitoring;
- active participation in working groups/committees that there is or will be created in the institutions involved in the supervision and management of EU funds;
- active cooperation with the authority, to clarify any aspects of their non-refundable financing at all stages of a project.

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