

AUDIT AUTHORITY

ANNUAL CONTROL REPORT



IEGULDĪJUMS TAVĀ NĀKOTNĒ

ESF, ERDF, CF

01.07.2014. – 30.06.2015.

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All the Annexes (Annex 1 to Annex 8) of the Annual Control Report are an integral part of this report.

ABBREVIATIONS

1 OP	Operational Programme “Human Resources and Employment”
2 OP	Operational Programme “Entrepreneurship and Innovations”
3OP	Operational Programme “Infrastructure and Services”
AA	Audit Authority
ACR	Annual Control Report
CA	Certifying Authority
CF	Cohesion Fund
CFCA	Central Finance and Contracting Agency
DG EMPL	Directorate General Employment, Social Affairs and Inclusion
DG REGIO	Directorate General Regional and Urban Policy
EC	European Commission
ERDF	European Regional Development Fund
ESF	European Social Fund
EU	European Union
FEI	Financial Engineering Instruments
IB	Intermediate Body
ISA	International Standards on Auditing
LIDA	Latvian Investment and Development Agency
LVL	Latvian lats
MA	Managing Authority
MCS	Management and control system
MEPRD	Ministry of Environmental Protection and Regional Development
MIS	Management Information System
MoC	Ministry of Culture
MoE	Ministry of Economics
MoESc	Ministry of Education and Science
MoF	Ministry of Finance
MoH	Ministry of Health
MoT	Ministry of Transport
MoW	Ministry of Welfare
MUS	Monetary Unit Sample
OP	Operational Programme
OPs	Operational Programmes: Infrastructure and Services (No 2007LV161PO002), Entrepreneurship and Innovation (No2007LV161PO001) and Human Resources and Employment (No 2007LV051PO001)
PA	Paying Authority
SC	State Chancellery
SEA	State Employment Agency
SEDA	State Education Development Agency
SIF	Society Integration Foundation
SRDA	State Regional Development Agency

SUMMARY

1. Annual Control Report is prepared by the Audit Authority in accordance with Regulation (EC) No 1083/2006 Article 62. (1) (d), (EC) 1828/2006 (Annex VI and VII) and Guidance Note on Annual Control Report and Opinions.

2. In areas where Community budget is managed through shared management arrangements, the ACR and opinions are critical elements that the EC uses in order to assess how the Member States have fulfilled their obligations and responsibilities for using Community budget appropriations.

3. The functions of the Audit Authority under the Operational Programmes: Infrastructure and Services (No 2007LV161PO002), Entrepreneurship and Innovation (No 2007LV161PO001) and Human Resources and Employment (No 2007LV051PO001) are fulfilled by the Ministry of Finance EU Funds Audit Department (*Section 1.1*).

4. Random sample for the audits of operations was selected from the expenditure declared to EC within the period from 1 January to 31 December 2014 (*Section 1.2*).

5. The ACR covers all three Operational Programmes. There is a single Certifying Authority/Paying Authority and a single Audit Authority. Functions of the Managing Authority are delegated to 15 Intermediate bodies (*Section 1.3*).

6. The ACR and the Audit Opinion is prepared based on the results of management and control system audits and audits of operations. More detailed steps of preparation of ACR are described in *Section 1.4*.

7. During the reference period no significant changes in the management and control system were made (*Section 2*).

8. The Single Audit Strategy was updated and communicated to the EC on 11 July 2014 (*Section 3*).

9. As the result of the horizontal management and control system audits performed by the Audit Authority, the Managing Authority is assessed with category 2 - the management and control system of the Managing Authority is determined as working, but some improvements are needed. Deficiencies found have a moderate impact on the functioning of the key requirements/authorities/system. Recommendations have been formulated regarding the closure of 2007-2013 programming period. Certifying Authority is assessed with category 1 – the management and control system within the Certifying Authority works well. Detailed information of the work done regarding the management and control system audits is set out in *Section 4*.

10. Error rate identified by the Audit Authority in accordance with the results of the audits of operations is 0,69% that is below the materiality level, thus the expenditure declared to the EC is within the materiality level and are legal and regular. Results of audits of operations and overall opinion are detailed in *Section 5*.

11. The Audit Authority did not relay on the work of other auditors in preparation of the ACR (*Section 6*).

12. In total the recommendations issued by the Audit Authority have been implemented in accordance with the action plans. There are recommendations that are

not entirely implemented, but do not have an impact on the evaluation of the ACR (*Section 7*).

13. In audit reference period the Audit Authority selected 17 projects for complementary audit of operations in order to ensure the coverage of sample for all priority axes / measures and individually risky projects. Audit approach and results of complementary audit and audited projects are described in *Section 8.1*.

14. In 2015 the Audit Authority audited negative amounts declared during year 2014. (*Section 8.2.*).

15. The Audit Authority performed a horizontal audit regarding the closure of 2007–2013 programming period and in 2016 the Audit Authority is going to audit the preparation of closure of FEI (*Section 8.3*).

16. The work of the Audit Authority and Managing Authority has been assessed by the audits of the EC and the European Court of Auditors. The recommendations are to be implemented in accordance with the action plan (*Section 8.4 and 8.6.*).

17. The Audit Opinion on effective functioning of the management and control system for the reference period from 1 July 2014 to 30 June 2015 and the legality and regularity of the underlying transactions of expenditure declared to the EC in 2014 is based on the results of the management and control system audits and audits of operations. The management and control system has been assessed in category 2 and the error rate of the audits of operations is below the materiality level, thus the Audit Authority concludes to have an unqualified Opinion as it is set out in *Table 14 and Section 8.5*.

1. INTRODUCTION

1.1. Indication of the responsible Audit Authority and other bodies that have been involved in preparing the report

In accordance with the Law on Management of European Union Structural Funds and the Cohesion Fund for 2007–2013 and the Cabinet Regulation No 501 “Procedures for Ensuring the Functions of the Audit Authority in the Management of European Union Structural Funds and the Cohesion Fund” dated 24 July 2012, the Ministry of Finance fulfils the functions of the Audit Authority.

Based on the Regulation of the Ministry of Finance¹ the European Union Funds Audit Department performs functions of the Audit Authority for the Operational Programmes: “Human Resources and Employment” No 2007LV051PO001 (1 OP), “Entrepreneurship and Innovation” No 2007LV161PO001 (2 OP) and “Infrastructure and Services” No 2007LV161PO002 (3 OP).

Functionally and administratively the Head of the Audit Authority is subordinated to the Minister of Finance and has the power to report directly to the Cabinet of Ministers via Minister of Finance as it is set by the Law on Management of European Union Structural Funds and the Cohesion Fund for 2007–2013 that is in force since 13 July 2011.

1.2. Indication of the 12 month reference period from which the random sample was drawn

The random sample was drawn from the expenditure declared to the EC for the period from 1 January 2014 to 31 December 2014 and the actual audit work of audits of operations was carried out between 1 January 2015 and 30 June 2015 in accordance with the Single Audit Strategy updated on 11 July 2014².

1.3. Identification of the operational programmes covered by the report and of its Managing and Certifying authorities. Where the report covers more than one programme or Fund, the information shall be broken down by programme and by Fund

The ACR refers to the single management and control system that has been developed for the implementation of all three OPs and their relevant funds:

¹ Regulation of the Ministry of Finance No 12-16/11 dated 1 October 2014, since 17 November 2015 replaced with Regulation of the Ministry of Finance No 12-16/9

² According to Audit Authority procedure No ARD-4 “Procedure for the Audit Authority to carry out audits of operations of the European Union funds in 2007–2013 programming period” updated on 23 January 2015.

Table 1: Operational Programmes and respective funds

Operational Programme		EU Fund
1 OP	<i>Human Resources and Employment</i>	ESF
2 OP	<i>Entrepreneurship and Innovations</i>	ERDF
3 OP	<i>Infrastructure and Services</i>	CF and ERDF

There is a single Managing Authority in Latvia that has delegated its tasks and functions to the 9 Responsible institutions (8 line Ministries and the State Chancellery) and 6 Co-operation institutions corresponding to the three levels EU fund implementation:

- The Managing Authority in general is responsible for communication with the EC, evaluation of the implementation of OPs and providing methodological support to Responsible institutions, Co-operation institutions and the beneficiaries, as well as supervision over delegated functions;

- Responsible institutions' main tasks include setting up and determining the national legislation for implementation of the activities/subactivities in accordance with the sectorial competences, preparation of reports and financial planning to the Managing Authority on the implementation of the activity/subactivity and project application evaluation of restricted project application calls;

- At the level of Co-operation institutions – the project implementation monitoring and administrative checks (on-the-spot visits, progress report review, payment claim checks), reporting on irregularities, project selection and contracting with beneficiaries.

The State Treasury is performing the Certifying Authority's and Paying Authority's functions for all three OPs including certifying that the statements of expenditure are accurate and reliable, drawing up certified statements of expenditure and applications for payment and ensuring that adequate information from the Managing Authority on the procedures and verifications carried out in relation to expenditure has been received.

The duties and rights of the institutions involved in the management and control system of EU funds are defined in the Law on Management of European Union Structural Funds and the Cohesion Fund.

The information of the institutions involved in the administration of the OPs and EU funds are broken down in *Table 2*:

Table 2: Institutions involved in the management of EU funds

Operational Programme	Function of	Institution
1 OP	Managing Authority	- Ministry of Finance
2 OP	Paying Authority and Certifying Authority	- State Treasury
3 OP		
1 OP	Responsible institutions	<ul style="list-style-type: none"> - Ministry of Finance - Ministry of Economics - Ministry of Education and Science - Ministry of Welfare - Ministry of Environmental Protection and Regional Development - Ministry of Health - State Chancellery
	Co-operation institutions	<ul style="list-style-type: none"> - State Employment Agency - Central Finance and Contracting Agency - State Education Development Agency - Latvian Investment and Development Agency - State Regional Development Agency - Society Integration Foundation
2 OP	Responsible institutions	<ul style="list-style-type: none"> - Ministry of Finance³ - Ministry of Economics - Ministry of Education and Science
	Co-operation institutions	<ul style="list-style-type: none"> - Central Finance and Contracting Agency² - Latvian Investment and Development Agency - State Education Development Agency
3 OP	Responsible institutions	<ul style="list-style-type: none"> - Ministry of Finance² - Ministry of Economics - Ministry of Education and Science - Ministry of Transport - Ministry of Welfare - Ministry of Environmental Protection and Regional Development - Ministry of Health - Ministry of Culture
	Co-operation institutions	<ul style="list-style-type: none"> - Central Finance and Contracting Agency² - State Education Development Agency

³ Technical Assistance project.

		<ul style="list-style-type: none"> - Latvian Investment and Development Agency - State Regional Development Agency
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1.4. Description of the steps taken to prepare the report

The Audit Authority prepares ACR in accordance with Council Regulation No 1083/2006 Article 62 point (1) (d), EC Regulation No 1828/2006 Article 18 point (2) and the Cabinet of Ministers Regulation No 501 “Procedures for Ensuring the Functions of the Audit Authority in the Management of European Union Structural Funds and the Cohesion Fund”. The Audit Authority does not rely on the work of other auditors as its functions are centralized in the Ministry of Finance. The Head of the Audit Authority approves the ACR as authorized by the Ministry of Finance Order No 399 “About the rights of signing the documentation” dated 1 August 2014⁴.

1.4.1. Information used for preparation of the ACR

The following information was used for preparing the ACR:

- 1) the results of the management and control system audits carried out by the Audit Authority over the reference period from 1 July 2014 to 14 December 2015;
- 2) the results of the audit of operations and complimentary sample for the expenditure declared to the EC within the period from 1 January 2014 to 31 December 2014;
- 3) information from follow-up procedures;
- 4) information from the reports of other auditors;
- 5) Statement of the Head of Managing Authority.

1.4.2. Key requirements and assessment criteria

In accordance with the Single Audit Strategy the Audit Authority performs risk assessment in three levels:

1. Risk assessment per OP;
2. Risk assessment per institution;
3. Risk assessment on the horizontal systems.

The management and control system audits are planned in accordance with the risk assessment by listing the institutions in descending order (from highest risk to the lowest). System audits cover all involved institutions every year. Scope of each particular audit is determined based on the risk analysis and previous knowledge.

The results of the management and control system audits and audits of operations are the base for the annual Audit Opinion that is issued by the Audit Authority.

Within the audit reference period from 1 July 2014 to 14 December 2015 the management and control system audits have been performed in every institution that is involved in the management of EU funds (17 in total) assessing all the key requirements that have been defined by the EC assessment criteria at the same time

⁴ Replaced with the Ministry of Finance Order No 192 (30 April 2015) and Order No 215 (22 May 2015).

gaining the assurance on whether the institutions are prepared for the closure of 2007-2013 programming period.

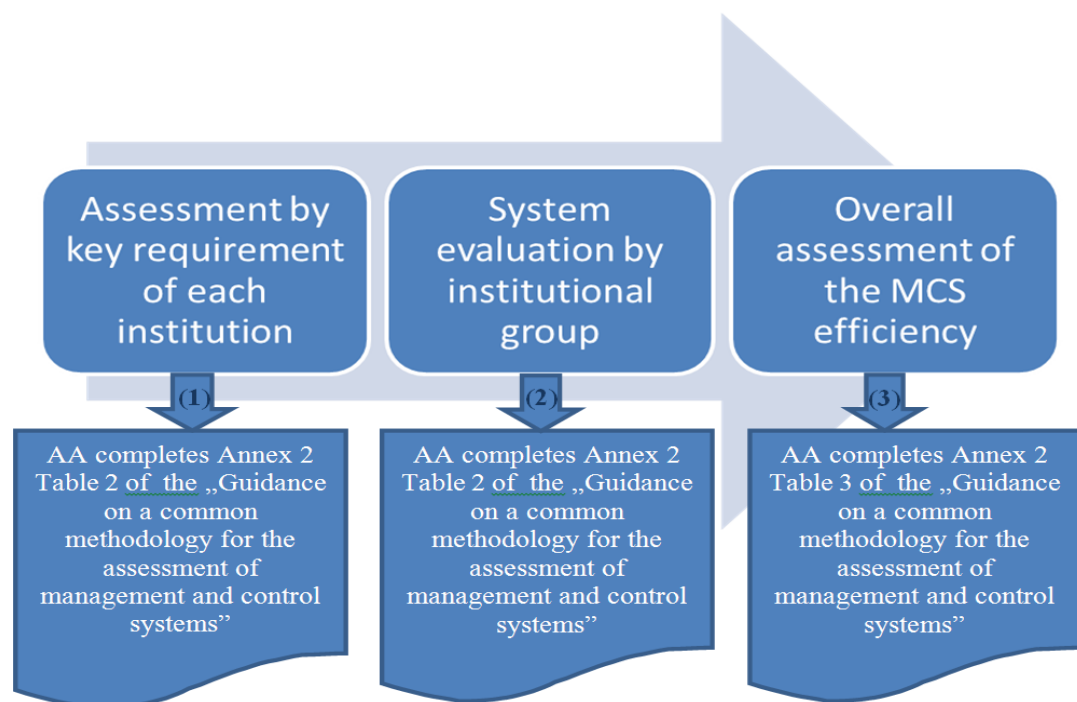
At the planning stage of the management and control system audits the internal control environment of the audited institution is assessed and the main risk factors for each key requirement are determined. In addition, all existing internal controls are identified for the audited institution, whether the controls are in compliance with the EU and national rules and regulations and the controls are sufficient to reduce the risks. The actual controls are tested and results assessed within the course of the audit.

1.4.3. Steps taken to reach overall conclusion and Audit Opinion

The preparation of the ACR is set out in the Audit Authority's procedure No 8 "Procedure on the preparation of the ACR of the European Union funds in the 2007 – 2013 programming period" that has been prepared taking into account the main elements of the management and control systems key requirements and assessment criteria in accordance with Council Regulation No 1083/2006, EC Regulation No 1828/2006 and EC "Guidance note on annual control reports and opinions".

System Audits:

Entire process of the ACR to reach the overall assessment of the management and control system can be set in 3 stages:



Stage 1. The assessment of the key requirements and assessment criteria are determined in the management and control system audits that are performed by the Audit Authority in each institution – Managing Authority, Certifying Authority/Paying Authority, 9 Responsible Institutions and 6 Co-operation

institutions. The audit results are summarized in the audit report and highlighted in the cumulative management and control assessment table. Detailed assessment of each key requirement and assessment criteria per institution audited are provided in *Annex 3*.

Each assessment criteria and key requirement is assessed in 4 categories as defined in the EC “Guidance on a common methodology for the assessment of management and control systems in the Member States (2007-2013 programming period)”, see *Table 3*.

Table 3: Category of the assessment criteria and key requirements

<u>CATEGORY</u>	<u>DESCRIPTION</u>
Category 1.	Works well; only minor improvements needed. There are no deficiencies or only minor deficiencies found. These deficiencies do not have any significant impact on the functioning of the key requirements / authorities / system.
Category 2.	Works, but some improvements are needed. Some deficiencies were found. These deficiencies have a moderate impact on the functioning of the key requirements / authorities / system.
Category 3.	Works partially; substantial improvements are needed. Deficiencies were found that have led or may lead to irregularities. The impact on the effective functioning of the key requirements / authorities / system is significant. Recommendations and/or an action plan have been put in place. The Member State / The European Commission may decide to take corrective action (e.g. interruption or suspension of payments) in order to mitigate the risk of improper use of EU funds.
Category 4.	Essentially does not work. Numerous deficiencies were found which have lead or may lead to irregularities. The impact on the effective functioning of the key requirements / authorities / system is significant – it functions poorly or does not function at all. The deficiencies are systemic and wide-ranging. As a consequence, no assurance can be obtained from the assessment of the key requirements / authorities / system. A formal action plan should be prepared and followed up. The Member State / European Commission take corrective action (e.g. suspension of payments) in order to mitigate the risk of improper use of EU funds.

The assessment of each key requirement cannot be classified more favourably than the worst of the assessment criteria.

Stage 2. The Audit Authority reaches a conclusion by the institution group and institution audited, based upon the results of the categorisation of each key requirement under Stage 1, subject to the following principles:

- 1) Some key requirements are determined as more essential with regard to the regularity of expenditure and the proper functioning of the relevant authority:
 - Managing Authority: key requirement 4 (management verifications).

- Certifying Authority: key requirement 3 (soundly based certification).
- 2) A classification in category 1 (Works well, only minor improvements needed) or 2 (works, but some improvements are needed) of the two essential key requirements mentioned above would have a positive influence on the overall conclusion, while deficiencies in other key requirements may downgrade the assessment for the relevant institution.
 - 3) If the essential key requirements highlighted at point 1 (or the relevant key requirement for each authority) are classified in categories 3 (Works partially, substantial improvements are needed) or 4 (Essentially does not work), the relevant authority cannot be assessed overall in a higher category. In other words, a higher classification of the other less essential key requirements for the authority in question cannot compensate for this deficiency.

The overall assessment of each institution group cannot be higher than the lowest assessment of relevant key requirement. For example, if one of the institutions is assessed according to category 3, overall assessment of Managing Authority cannot be higher than category 3 (category 2 or 1). The conclusion of assessment of each institution/authority is summarized in *Annex 4*.

Stage 3. The Audit Authority concludes on the overall assessment of the management and control system by identifying any mitigating factors/compensating controls that may exist in one authority which effectively reduce the risk in the overall management and control system, in addition the residual risk to regularity is determined as concluded in *Annex 5*.

The overall conclusion by the management and control system provides a basis for determining assurance levels for formulating audit opinions and subsequent action, taking into account the results of audits of operations as provided in detail in *Section 4*.

Audits of operations:

In accordance with the assurance level obtained from system audits, the confidence level is determined for the audits of operations. Before the sample is drawn, the sampling method and parameters of sampling are determined. There is one sample drawn once a year including all three OPs. The detailed testing at the level of Intermediate Bodies and final beneficiaries is performed in order to assess whether the expenditure declared to the EC is legal and regular. As a result of the audit of operations regarding any irregular expenditure found, the Audit Authority evaluates the errors, reports to the auditees and calculates the error rate. More details on sampling methodology applied and the results see in *Section 5*.

The overall opinion is based on the results of the management and control system audits and results of audits of operations, detailed evaluation is set out in *Table 14 of Section 8.5*.

2. CHANGES IN MANAGEMENT AND CONTROL SYSTEM

2.1. Indication of any significant changes in the management and control systems notified to the audit authority as compared with the Management and control description and of the dates from which the changes apply.

For the period from 1 July 2014 to 30 June 2015 the Managing Authority made one update on 29 October 2015 (changes made till 30 June 2015) to the Management and control description. The changes of the management and control system as compared with the Management and control description have been assessed by the Audit Authority for the period from 1 June 2008 to 30 June 2015. In addition, any post events that have occurred after 30 June 2015 have also been taken into account by the Audit Authority when establishing its conclusions and providing its opinion.

Before issuing the Audit Opinion and ACR, the Audit Authority requests from the Managing Authority a management statement, in which the head of the Managing Authority ensures to the Audit Authority that all significant changes in the management and control system have been communicated to the Audit Authority. Last statement signed by the head of the Managing Authority was received on 9 December 2015.

2.1.1. Changes in the period from 1 July 2014 to 31 December 2014

As reported in the ACR 2014 no significant changes have been made in the management and control system for the period stated above as compared with the Management and control description updated by the Managing Authority on 29 October 2014 (changes made till 30 June 2014).

2.1.2. Changes in the period from 1 January 2015 to 30 June 2015, including the events that have occurred after 1 July 2015.

Changes made in the management and control system⁵ are mostly adjustments of resources according to the needs for closure of 2007-2013 and launching of 2014-2020 programming period and are not considered to be significant. Changes are evaluated by the Audit Authority in system audits and follow-up of the implementation of the recommendations.

3. CHANGES TO AUDIT STRATEGY

The initial Single Audit Strategy was prepared and submitted to the EC on 29 September 2008. The acceptance of the Single Audit Strategy from the EC was received by letter No D (2009)6651 on 7 April 2009.

The latest updated Single Audit Strategy was submitted to the EC on 11 July 2014 and the most substantial changes were reported in the ACR 2014.

⁵ Management and control description updated by the Managing Authority on 29 October 2015 (changes made till 30 June 2015) compared with the Management and control description updated by the Managing Authority on 29 October 2014 (changes made till 30 June 2014).

The updated management and control system audit plan for ACR2015 and the audit approach towards closure of 2007-2013 was presented to the EC during the Bilateral Meeting on 30 April 2015.

For ACR2015 instead of the follow-up audits planned in the Single Audit Strategy a single horizontal system audit regarding payment claim verifications was carried out in all co-operation institutions. The follow-up of the implementation of recommendations of all institutions was covered by the performed horizontal audit on preparation for the closure of 2007-2013.

4. SYSTEM AUDITS

4.1. Indication of the responsible audit authority and other bodies that have been involved in preparing the report

During the reference period all system audits solely have been performed by the Audit Authority that is located within the Ministry of Finance in EU Funds Audit Department (more details see in *Section 1.1*).

4.2. Summary list of the audits carried out (bodies audited)

The summary of the management and control system audits carried out during the reference period and not reported in the ACR 2014, indicating the OP, the audit body, the date of the audit carried out, audit scope, principal findings and conclusions, whether there were systemic deficiencies is set out in *Annex 1 and Annex 2*.

The Audit Authority assessed all institutions that are involved in the management of the EU funds performing 2 horizontal system audits *see Annex 1 and Annex 2*.

The horizontal system audits were performed regarding:

1. Assessment of the management and control system and preparation for the closure of 2007-2013 (all institutions) and follow up of implementation of previous recommendations:
 - Ministry of Finance (the Managing Authority);
 - The State Treasury (the Paying Authority and Certifying Authority),
 - All (15) Intermediate bodies:
 - Ministry of Economics;
 - Ministry of Transport;
 - Ministry of Welfare;
 - Ministry of Health;
 - Ministry of Environmental Protection and Regional Development;
 - Ministry of Education and Science;
 - Ministry of Culture;

- State Chancellery;
- Ministry of Finance (Technical Assistance project);
- State Education and Development Agency;
- Latvian Investment and Development Agency;
- State Employment Agency;
- Central Finance and Contracting Agency;
- State Regional Development Agency;
- Social Integration Foundation.

2. Payment claim verifications (all (6) Co-operation institutions and 2 responsible institutions which at the same time perform also the functions of co-operation institutions):

- State Education and Development Agency;
- Latvian Investment and Development Agency;
- State Employment Agency;
- Central Finance and Contracting Agency;
- State Regional Development Agency;
- Ministry of Environmental Protection and Regional Development;
- Social Integration Foundation;
- Ministry of Transport.

4.3. Description of the basis for selection of the audits in the context of the audit strategy

Audits for the reference period were planned according to risk assessment – in total 7 institutions were assessed at high risk and 10 institutions – at low risk. The summary of the risk assessment per OP and per institution for the period from 2014 to 2015 is provided in *Table 4*. The detailed calculations and table of institutions is provided in the Annex 5 of the updated Single Audit Strategy, which was submitted to the EC on 11 July 2014 via SFC2007.

Table 4: Summary of the risk assessment per institution

OP	Institution	Amount of administered EU funding	Total score of risk assessment	Priority
1 OP	MoESc	-	28	Low
	SEDA	236,9 m	34	Low
	MoW	-	19	Low
	SEA	241,7 m	38	High
	MoE	-	27	Low
	LIDA	50,9 m	38	High
	MEPRD	-	28	Low

	SRDA	6,7 m	35	Low
	MoF	-	10	Low
	MoH	-	28	Low
	CFCA	35,1 m	31	Low
	SC	-	19	Low
	SIF	11,8 m	31	Low
2 OP	MoESc	-	26	Low
	SEDA	211 m	32	Low
	MoE	293,5 m	31	Low
	LIDA	168,8 m	36	High
	MoF	-	8	Low
	CFCA	23 m	29	Low
3 OP	MoESc	-	28	Low
	SEDA	298,3 m	34	Low
	MoE	-	27	Low
	LIDA	216,1 m	38	High
	MEPRD	571 m	37	High
	SRDA	310,7 m	38	High
	MoT	1,170 b	41	High
	CFCA	684,9 m	37	High
	MoW	-	19	Low
	MoH	-	28	Low
	MoC	-	19	Low
	MoF	-	10	Low
Managing Authority			39	High
Certifying Authority /			29	Low
Paying Authority			29	Low

In general the Responsible Institutions are line ministries that are competent in setting up the policy for certain area (i.e. Ministry of Health is responsible for the management of health policy in the state). Their functions, amongst other, would include monitoring the implementation at the activity/sub-activity level, set up the project application assessment criteria and the planning documentation, and manage the financial flow of the state budget and EU funds.

Functions of the Co-operation institutions are generally delegated to the state agencies, whose functions would include project application selection process, contracting with beneficiaries, EU fund monitoring at the level of projects, on-the-spot checks, payment request approval, reporting on irregularities, evaluation of the procurement and publicity requirements which is related to the direct financing of final beneficiaries and consequently with higher risk.

The Audit Authority's general approach according to the Single Audit Strategy in system audits is:

- to assess all institutions that are involved in the management of the EU funds;
- to assess key requirements and criteria with highest risks;
- to assess basic horizontal priorities periodically.

4.4. Principal findings and conclusions drawn from the audit work for the management and control systems and their functioning, including the sufficiency of management checks, certification procedures and the audit trail, adequate separation of functions and compliance with Community requirements and policies.



4.4.1. Conclusion reached on the Managing Authority

The Managing Authority of the EU funds for the 2007-2013 programming period is located in the Ministry of Finance and it is responsible for administering the following functions in accordance with Council Regulation No 1083/2006 Article 60:

- ensuring establishment and implementation of computerized information system – Management Information System (MIS);
- evaluations of implementation of the OPs;
- organization of the monitoring committee;
- preparation and submitting of the annual and final reports on implementation to the EC;
- communication to EC regarding information of the major projects.

The rest of the Managing Authority's functions (in regards of implementation, monitoring and control at the Priority/Activity/Project level) are delegated to the Intermediate bodies:

- project application selection process and setting up the assessment criteria for approval of the monitoring committee;
- verifications of the expenditure declared by the beneficiaries and on-the-spot checks;
- ensuring separate accounting system or an adequate accounting code for all transactions relating to the operation;
- setting up procedures to ensure that all documents regarding expenditure to ensure an adequate audit trail;
- assurance provided to the Certifying Authority (partially);

- compliance with the information and publicity requirements.

During the reference period the Audit Authority performed a horizontal system audit in the Managing Authority to evaluate the management and control system and readiness for the closure of 2007-2013 in period from 1 March 2014 to 31 August 2015. Audit report is still under contradictory procedure and will be submitted to the EC via SFC 2007 as soon as final report is approved.

The Managing Authority is assessed in the category 2 – the management and control system within the Managing Authority works, but some improvements are needed regarding the efficiency and quality of supervision of delegated functions:

- ✓ Improvements to ensure sufficient capacity of several Intermediate bodies for timely closure of 2007-2013;
- ✓ Improvements in quality of supervision of delegated tasks, treatment of irregularities and implementation of recommendations;
- ✓ Improvements to ensure reliable data in the Management Information System.
- ✓ Regarding the quality of project evaluation recommendations have been issued in relation to the programming period 2014-2020.

In order to conclude on the overall assessment of the Managing Authority, the Audit Authority audited all high risk key requirements of all Intermediate bodies that are implementing the functions delegated by the Managing Authority. The approach of Audit Authority is that the overall assessment of the Managing Authority cannot be higher than the lowest assessment of the institution of its delegated functions.

As it is summarized in *Annex 3* and *Annex 4* after determining the overall assessment per key requirement for each institution involved in the management and control system, the Managing Authority is assessed in **the category 2** – the management and control system within the Managing Authority is working, but some improvements are needed.

4.4.2. Conclusion reached on the Intermediate bodies

As a result of the two horizontal management and control system audits (see *Annex 3* and *Annex 4*) it is concluded that the management and control system established within the Intermediate bodies is assessed in **the category 2** – is working, but some improvements are needed in order to ensure appropriate scope and timely controls towards the closure of 2007-2013:

- to perform sufficient and timely administrative verifications regarding the payment claim or expenditure;
- to strengthen the capacity to organise timely controls.

Regarding the quality of project evaluation recommendations have been issued in relation to the programming period 2014-2020.

More detailed information on the analysis of the errors and findings in order to identify their systemic nature is provided in *Section 4.5*.

4.4.3. Conclusion reached on the Certifying Authority

During the reference period the Audit Authority performed a horizontal system audit in the Certifying Authority to evaluate the management and control system and readiness for the closure of 2007-2013 in period from 1 August 2014 to 31 March 2015. Audit report is still under contradictory procedure and will be submitted to the EC via SFC 2007 as soon as final report is approved.

The Certifying Authority is assessed in **the category 1** – the management and control system within the Certifying Authority works well.

4.5. Indication of whether any problems identified were considered to be of a systemic character, and of the measures taken, including a quantification of the irregular expenditure and any related financial corrections.

In total as a result of system audits the Audit Authority issued 37 recommendations:

- 37 recommendations provisionally issued in horizontal audit on preparation for the closure of 2007-2013 (draft report under contradictory procedure);
- No recommendations issued in payment claim verification horizontal audit.

Issued recommendations in the time of issuing the Opinion and ACR (see *Table 5*).

Table 5: Issued recommendations

	Recommendations' priority			TOTAL
	High	Medium	Low	
Total recommendations issued (provisional)*, including:	15	12	10	37
Regarding closure of 2007-2013	15	8	10	33
Regarding 2014-2020	-	4	-	4

* included in draft report and are not in force yet

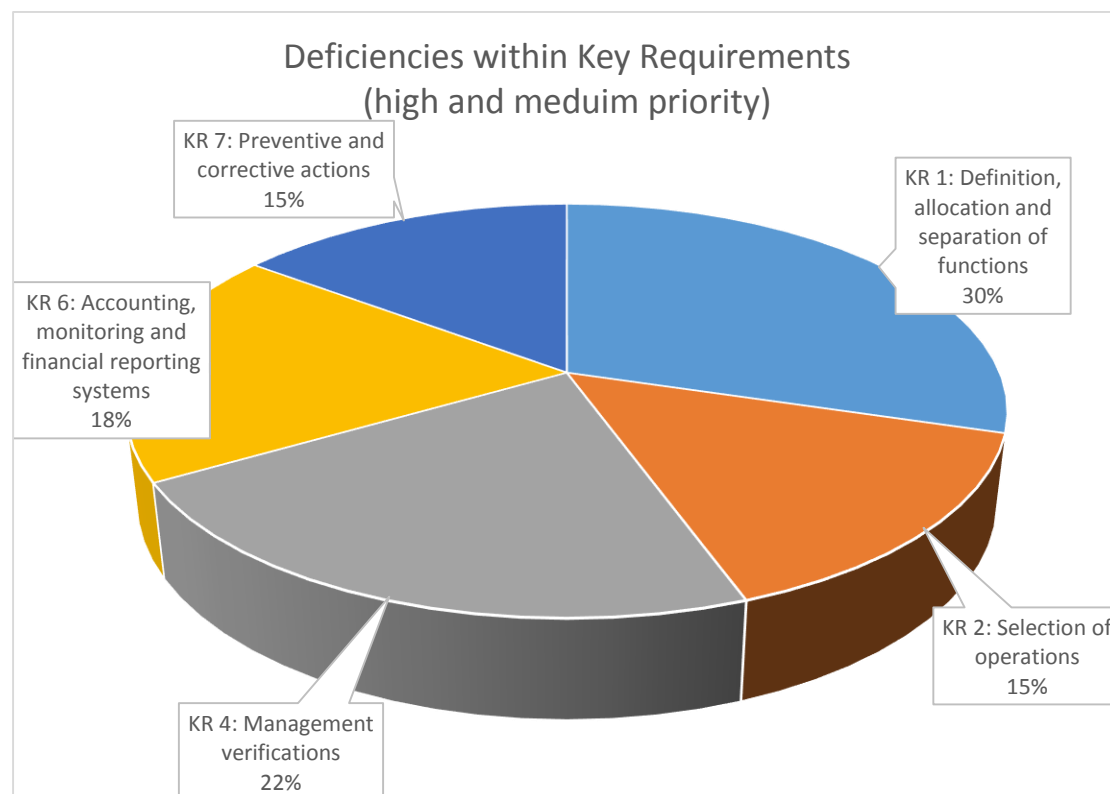
Recommendations are issued in order to ensure timely closure of 2007-2013 and have preventive nature, and do not have an impact on the evaluation of the ACR.

The Audit Authority performed the analysis of the errors and findings in order to identify their systemic nature (we analysed results of both horizontal audits based on draft report which is under contradictory procedure, see also *Annex 2*).

As it is shown in *Chart 1 and Chart 2* 30 % of all (high and medium priority) deficiencies identified by the Audit Authority during the system audits were found within *Key requirement 1 - Definition, allocation and separation of functions*. The Audit Authority identified a capacity risk in regards to management verifications in 3 of 8 Co-operation institutions. As well the 22% of deficiencies found within *Key*

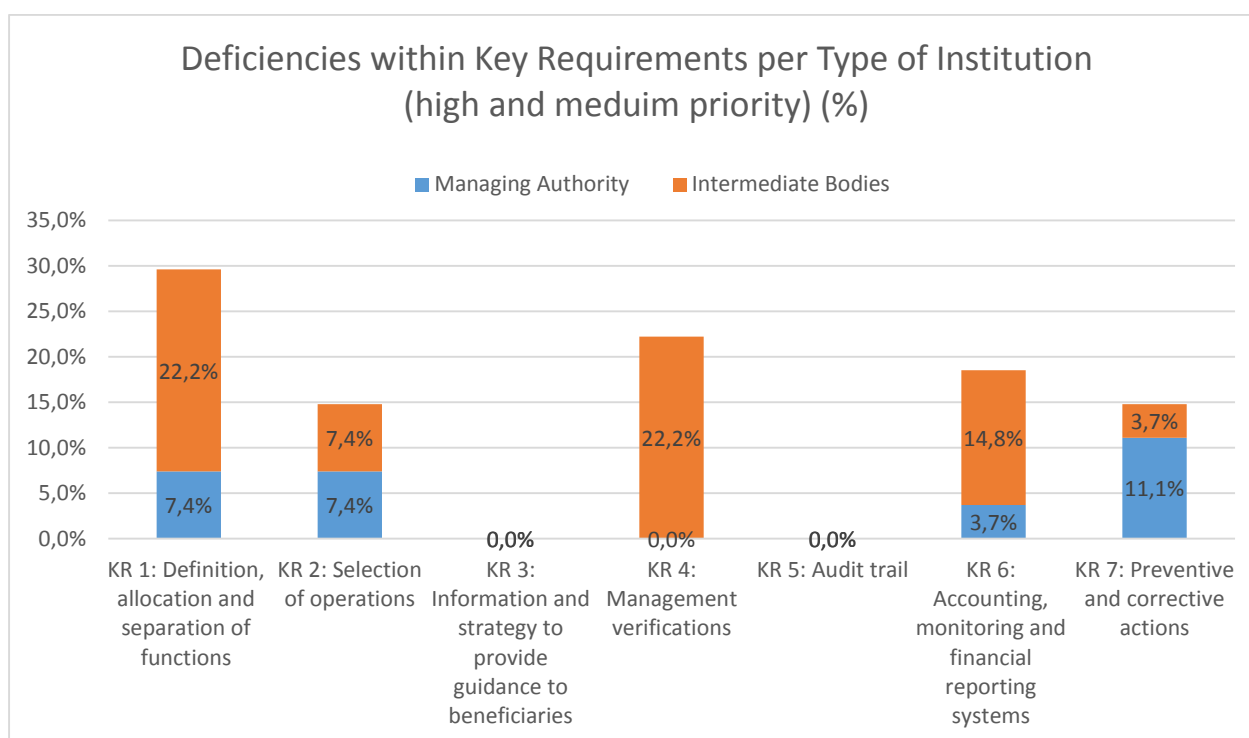
requirement 4 - Adequate management verifications are mainly regarding capacity risk to perform sufficient and timely controls. As current programming period is coming to the end and it is important to have all the resources in place for closure of projects the Audit Authority has indicated the possibility to improve procedures and to allocate resources in the most efficient way.

Chart 1



Deficiencies in other Key Requirements are related to ensure reliable data in the Management Information System, treatment of irregularities and implementation of recommendations, as well the need to improve the quality of project evaluation in the 2014-2020 programming period.

During the horizontal audits no irregular expenditure were found.

Chart 2

5. AUDITS OF OPERATIONS

5.1. Indication of the bodies that carried out the audits of operations, including the audit authority

Audit of operations regarding certified expenditure in calendar year 2014 was carried out by the Audit Authority (*See Section 1.1*).

5.2. Description of the basis for selection of the sample(s). Indication of the materiality level and, in the case of statistical sampling, the confidence level applied

Audit Authority carried out audit of operations in accordance with Audit Strategy updated on 11 July 2014⁶.

Regular audit of operations is performed for expenditure declared to the EC during the period – from 1 January to 31 December 2014 within all three Operational Programmes:

- 1) Operational programme „Human Resources and Employment” (ESF) – 2007LV051PO001;
- 2) Operational programme „Entrepreneurship and Innovations” (ERDF) – 2007LV161PO001;

⁶ According to Audit Authority procedure No ARD-4 “Procedure for the Audit Authority to carry out audits of operations of the European Union funds in 2007–2013 programming period” updated on 23 January 2015.

3) Operational programme „Infrastructure and Services” (CF and ERDF)
– 2007LV161PO002.

Audit of operations is carried out within the reference period from 1 January to 30 June 2015 for the expenditure declared to EC from 1 January to 31 December 2014 (audit No DR-15/3).

For regular audit one population was formed and one selection was done. Population included declared expenditure of 2014 for all three Operational Programmes.

Sampling unit is a project which payment claim/-s covering eligible expenditure approved by Certifying Authority and included in statements of expenditure submitted to the EC during 2014.

Sampling method was determined according to EC's Guidance on sampling methods for audit authorities (COCOF 08-0021-03-EN) for regular audit. General criteria taken into account for determination of sampling method were number of sampling units in population. For expenditure certified in 2014 population consists of 2 463 sampling units and the sampling method used was statistical sampling – Monetary Unit Sampling (MUS) Standard approach.

Sampling selection parameters⁷ that were used are included in *Table 6*.

Table 6: Parameters used for sampling

Parameters	Value
Assurance from the system	Average
Confidence level	70% ⁸
Book value of expenditure declared (BV)	EUR 1 091 491 783,70 ⁹
Size of operations	2 463 units
Materiality level	2%
Tolerable error (TE)	EUR 21 829 835,67
Anticipated error rate	1,30%
Standard deviation of error rates	0,04 ¹⁰
Sampling interval	EUR 32 985 847,30

From total population of 2 463¹¹ units – projects regarding expenditure declared to EC in year 2014, 33 projects were selected, see *Table 7*.

⁷ All parameters determined according to European Commission Guidance on sampling methods for audit authorities (COCOF 08-0021-03-EN).

⁸ In accordance with the Annual Control Report approved on 23 December 2014 where the opinion of management and control system is provided and evaluated with category 2 „Works, but some improvements are needed”, assurance from the system was Average, so that the confidence level was set 70%.

⁹ Amount declared to the EC including negative amounts is EUR 1 038 780 279,18. The value of the population is EUR 1 091 491 783,70 – which consist of expenditure declared to the EC, except negative amounts EUR (-) 58 957 198,21 and amount of EUR 6 245 693,69, that is part of the temporary withdrawals included back in the statements of expenditure.

¹⁰ Based on historical data and taking into account professional judgment.

¹¹ Number of projects that formed population and were used for sampling after quality control. Within quality control negative values were excluded, payment claims merged within project (if for the project more than one payment claim was declared) etc.

Table 7: Expenditure declared during year 2014 and selected units

Population size		Selected sample			Exact verified expenditure		
units	EUR	units	EUR	%	units	EUR	%
Expenditure declared during year 2014							
2 463	1 091 491 783,70	33	179 332 484,33	16,43	33	177 552 092,08	16,27

5.3. Description of the principal results of the audits of operations

Results of audits of operations broken down by Operational Programmes are included in *Table 8*. At the moment of preparation of ACR for 1 project audit draft report is under contradictory procedure, preliminary results are included in *Table 8* and the maximum possible error¹² is taken into account in the projected error rate calculation.

Table 8: Results of audits of operations

	Declared expenditure ¹³ (EUR)	Sample (units - projects)	Audited expenditure (EUR)	Irregular expenditure found within sample (EUR)	Error within sample
Expenditure declared during year 2014	1 091 491 783,70	33¹⁴	177 552 092,08	1 073 057,20	0,60
1 OP (ESF)	73 841 695,80	3 ¹⁵	2 347 641,41	19 520,21 ¹⁶	0,83
2 OP (ERDF)	257 475 408,26	7 ¹⁷	26 613 074,26	0,00	0,00
3 OP (CF and ERDF)	760 174 679,64	23 ¹⁸	148 591 376,41	1 053 536,99	0,71

All irregularities found are taken into account for calculation of the projected error rate. This includes one particular irregularity which had already been detected and acted upon by intermediate body after the sample was drawn by Audit Authority and before particular project audit was launched. The irregular amount has been corrected¹⁹ before submission of the ACR.

According to the second subparagraph of Article 17(4) of EC Regulation No 1828/2006 projected error rate was calculated and compared with the set materiality level – 2%, in order to reach conclusions for the population.

As it is stated above for the population of the year 2014, MUS was used according to the EC's guidelines²⁰. Conclusions were reached in several steps according to internal procedures of the Audit Authority.

¹² Could be reviewed after contradictory procedure

¹³ Expenditure declared to the EC on the basis of which the sample of operations is selected.

¹⁴ Covers 117 payment claims.

¹⁵ Covers 11 payment claims.

¹⁶ Results are under contradictory procedure. This amount is the maximum possible irregular expenditure.

¹⁷ Covers 24 payment claims.

¹⁸ Covers 82 payment claims. CF – 12 projects (47 payment claims), ERDF – 11 projects (35 payment claims).

¹⁹ The irregular expenditures EUR 93 522,83 has been recovered – the amount of subsequent payment claim was reduced.

²⁰ Guidance on sampling methods for audit authorities (COCOF 08-0021-03-EN)

Total projected error rate for the expenditure declared within 2014 is set as 0,69%²¹, which does not exceed materiality level – 2%.

Conclusions reached after the qualitative analysis performed are described in *Section 5.4*. All errors found were classified as systemic and random errors and all were included in calculation of total projected error rate. All errors were projected to the population²². Upper error limit was calculated and set as 0,96%. Further actions taken by the Audit Authority regarding results of regular audits of operations are described in *Section 8.1*.

5.4. Conclusions drawn from the results of the audits of operations with regard to the effectiveness of management and control system

For the reporting period according to Article 16(2) of EC Regulation No 1828/2006 results of regular audits of operations provide reasonable assurance that statements of expenditure submitted to the EC for all 3 Operational Programmes are correct and underlying transactions are legal and regular, except in individual cases when deficiencies were identified in fields highlighted in *Table 9*. As it stated above, the total projected error rate for expenditure declared to the EC in year 2014 is 0,69%, and does not exceed materiality level of 2%.

Table 9: Errors found broken down by operational programs and fields

Field of error	Number of errors			Total
	1 OP	2 OP	3 OP	
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
Systemic errors				
Procurement	0	0	11	11
Eligibility of expenditure	1	0	0	1
Random errors				
Procurement	0	0	1	1
Supervision of project implementation	0	0	8	8
Publicity	0	1	2	3
Eligibility of expenditure	0	0	1	1
Total	1	1	23	25

In addition to the errors indicated in *Table 9*, within audit of operations:

- It was detected that some intermediate bodies have delays of deadlines stated in national legislation regarding of verification and approval of payments. Treatment and further actions related to this issue have not been

²¹ 1) Taking into account EC DG REGIO finding identified during the audit mission No 2013/LV/REGIO/C2/1242/1 concerning potentially unequal treatment of foreign bidders and/or dissuasive effect for foreign bidders (the requirement of registration of experts in Latvia to be demonstrated until the tender submission date) and represented official position of the EC on the issue. Audit Authority during audit of operations identified all similar cases and included all these cases in calculation of the total projected error rate. At the moment of preparation of ACR, financial corrections are proposed except for the individual cases for which assistance from EC DG REGIO was requested and reply received by letter No Ares(2015)3227506 – 31/07/2015. Audit Authority will take the necessary actions regarding these individual cases following the end of the discussion related to the determination of the scope of the affected contracts for which corrections must be applied according to the EC DG REGIO letter No Ares(2015)5588121 – 04/12/2015.

2) For 1 project audit draft report is under contradictory procedure, the maximum possible error is taken into account in the projected error rate calculation

²² Section 2 of the European Commission Updated Guidance for Member States on treatment of errors disclosed in the Annual Control Reports (EGESIF 15-0007-01)

taken as it was included in the scope of the Horizontal audit on preparation for the closure of 2007 -2013 (*see Section 4 and Annex 2*);

- Some insignificant deficiencies related to the construction documentation without financial impact were detected. Audit Authority drew attention of responsible authorities to prevent such kind of deficiencies in the future;
- Audit Authority during the audit identified some cases with potential financial impact outside the sample related to expenditure not yet declared to EC. Audit Authority drew attention of responsible authorities to prevent the risk that ineligible expenditure could be declared to EC in the future. Audit Authority ensures the monitoring of these cases²³.

Detailed qualitative analysis performed on the errors found and their significance is indicated in *Annex 6*.

Further analysis on the systemic errors, their significance and actions taken by the Audit Authority and other institutions is described in the *Section 5.5 and 5.6*.

5.5. Information on the follow-up of irregularities, including revision of previously reported error rates

Recommendations regarding findings and errors detected in the regular audit of operations related to year 2014 and implementation status of those recommendations are summarized in *Annex 7*.

As a result of regular audit of operations in total 18 recommendations²⁴ were issued by the Audit Authority. The implementation status of those recommendations at the moment of preparation of current ACR is:

- 2 – recommendation implemented,
- 1 – not implemented,
- 14 – deadline of implementation of recommendations is not in force yet,
- 1 – under contradictory procedure at the moment of preparation of ACR.

Within the reference period there were no cases of fraud or suspected fraud identified.

According to EC DG REGIO recommendations issued as a result of the audit mission No 2013/LV/REGIO/C2/1242/1²⁵, the Audit Authority recalculated the error rate reported in the ACR 2012, ACR 2013 and ACR 2014. As reported to the EC²⁶ error rates are set²⁷ as: 1,45% for the ACR 2012, 1,86% for the ACR 2013 and 1,06% for the ACR 2014.

²³ In two cases recommendations are issued (*see Annex 7 Point 16 and 17*) and in one case the necessary actions have already been taken

²⁴ 1) In 5 cases recommendations were not issued as the necessary corrective measures had already been taken during the audit. 2) At the moment of preparation of ACR for the individual 5 cases recommendations were not issued *see Section 5.6. Point 3.3*.

²⁵ On 12 November 2014 EC letter was received opening the procedure that may lead to financial correction (audit mission No 2013/LV/REGIO/C2/1242/1).

²⁶ The recalculated error rates sent to the EC on 4 February 2015 (ACR 2013 and ACR 2014) and 11 February 2015 (ACR 2012).

²⁷ Please note that in calculation of the total projected error rate Audit Authority took into account all the contracts affected by irregularity linked to the requirement of registration of experts in Latvia to be demonstrated until the tender submission date without case by case analysis.

Please note that the total projected error rate 1,45% for the ACR 2012 as mentioned above has been recalculated and set as 1,29% due to performed re-evaluation of new circumstances made by Intermediate Body and conclusion that one particular error is considered as being an error with less financial impact.

5.6. Problems which are considered systemic in nature and the measures taken

The Audit Authority performed qualitative evaluation of the deficiencies identified and considered that several of them are with systemic nature. 12 non-compliances were detected, all of them are with financial or with potential financial impact including non-compliances in procurement procedures regarding unequal treatment of foreign bidders and restrictive selection criteria, and incomplete controls carried out by the Intermediate body related to the verifications of the expenditure declared by the beneficiaries.

Breakdown of systemic errors and their financial impact is presented in *Table 10*.

Table 10: Systemic errors

Field of error	1 OP		2 OP		3 OP		Total ineligible expenditure (EUR)	Total ineligible expenditure outside the sample (EUR)
	Number of errors	Ineligible expenditure (EUR)	Number of errors	Ineligible expenditure (EUR)	Number of errors	Ineligible expenditure (EUR)		
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>6</i>	<i>7</i>	<i>8</i>	<i>9</i>
Procurement	0	0,00	0	0,00	11	929 247,94	929 247,94	1 058 275,36
Eligibility of expenditure	1	19 520,21 ²⁸	0	0,00	0	0,00	19 520,21	0,00
Total	1	19 520,21	0	0,00	11	929 247,94	948 768,15	1 058 275,36

As a result of deficiencies detected with systemic character that were found during the audit of operations, there are several actions taken by the Audit Authority and other institutions:

Field of error – Procurement

1. To eliminate different deficiencies in procurement procedures found on the individual project level, recommendations were issued (*see Annex 7*) except at the moment of preparation of ACR for the individual 5 cases (*see Point 3.3 of this paragraph*).
2. Non-compliances regarding restrictive selection criteria:
 - 2.1. Applied requirements (not more than 70% of the total amount of the works to be performed may be transferred to sub-contractors) in procurement documentation and in the national legislation are not in line with the EC public procurement provisions and are considered as restrictive²⁹. As requirements are in accordance with the national Public Procurement Law in force until 31 July 2012, the irregularity is considered as systemic. The finding detected also during the EC DG

²⁸ Results are under contradictory procedure. This amount is the maximum possible irregular expenditure

²⁹ Applied for procurements above EU threshold

- REGIO audit mission No 2014/LV/REGIO/C2/1285/1 and financial correction is proposed³⁰.
- 2.2. Irregularity in procurement procedures found are referable to procurement procedures launched in the period from 2008 till date when amendments to the Public Procurement Law came into force.
 - 2.3. On 22 September 2015 Cabinet of Ministers of the Republic of Latvia took the decision that the ineligible expenditure³¹ are to be recovered from the state budget.
 3. Non-compliances regarding unequal treatment of foreign bidders:
 - 3.1. During the audit mission No 2013/LV/REGIO/C2/1242/1 the EC auditors detected irregularity linked to the requirement for experts to possess a Latvian certificate before submission of the tender.
 - 3.2. According to the EC recommendations provided in the audit report³² Audit Authority has improved procedures to be able to identify this type of procurement problems and re-checked the operations audited for ACR 2012 till ACR 2014, error rate recalculation was made (See *Section 5.5.*).
 - 3.3. At the moment of preparation of Annual control report, financial corrections within audit of operations related to ACR 2015 are proposed, except for the 5 individual cases where assistance from EC DG REGIO was requested and reply received³³. Audit Authority will take the necessary actions regarding those individual cases following the end of the discussion related to the determination of the scope of the affected contracts for which corrections must be applied according to the EC DG REGIO letter No Ares(2015)5588121 – 4 December 2015.
 4. In future reference periods the Audit Authority will follow-up the actions taken, to ensure that systemic errors within procurement are decreasing, procurement control system is improved and working appropriately.
 5. Regarding additional work performed by Audit Authority, public procurement was one of the main issues of the scope of the complementary audit of operations – additional projects were selected and audited (see *Section 8.1.*).

Field of error – Eligibility of expenditure

6. During the audit of one particular project benefited within Sub-activity No 1.3.1.1.1. “Support to training for employed for enhancing competitiveness of enterprises – support to training for employed in partnerships”³⁴ Audit Authority in some individual cases detected potential non-compliance with one of the eligibility criteria set in the Regulations of the Cabinet of Ministers of the Republic of Latvia regarding the implementation of the particular sub-activity:
 - 6.1. After further evaluation it was detected that management verifications regarding one particular eligibility criteria set in above mentioned national regulation are not sufficient which could lead to irregularities with financial impact.

³⁰ Audit mission No 2014/LV/REGIO/C2/1285/1 2 December 2015. final audit report (national language version)

³¹ The expenditure incurred for the contracts affected by irregularity

³² On 12 November 2014 EC letter was received opening the procedure that may lead to financial correction (audit mission No 2013/LV/REGIO/C2/1242/1)

³³ EC DG REGIO letter No Ares(2015)3227506 – 31/07/2015

³⁴ Co-financed by the ESF

- 6.2. Audit Authority did not carry out further verifications for the particular eligibility criteria as it was concluded that this is systemic error.
- 6.3. At the moment of preparation ACR the audit results are under the contradictory procedure, however, the Audit Authority issued recommendations to eliminate deficiencies and evaluate the impact within the whole Sub-activity No 1.3.1.1.1. and has determined the maximum possible irregular expenditure for the calculation of the total projected error rate.
- 6.4. Some of recommended actions are being implemented already – Intermediate body is carrying out verifications to determine the scope of the population affected by the error, the significance of the individual non-compliance and the possible financial implications.

6. COORDINATION BETWEEN AUDIT BODIES AND SUPERVISORY WORK OF THE AUDIT AUTHORITY

6.1. Description of the procedure for co-ordination between different national audit bodies and the audit authority itself

For the ACR 2015 purposes and the Opinion of the Audit Authority as the functions of the Audit Authority are centralized in the Ministry of Finance, the Audit Authority did not rely on the work of internal audit bodies or any other audit body.

6.2. Description of the procedure for supervision applied by the audit authority to other audit bodies

Not applicable.

7. FOLLOW UP OF PREVIOUS YEARS' AUDIT ACTIVITY

Regarding the implementation of recommendations of previous years' system audits it is concluded that institutions that are involved in the management of the EU funds mostly implement the system audit recommendations in accordance with the action plan. However, there are 6 recommendations (medium priority) for Ministry of Transport mainly regarding elimination of specific deficiencies within several projects, and quality of data entered in Management Information System and timely controls that are not entirely implemented yet. As well, 1 recommendation (low priority) for State Regional Development Agency concerning elimination of specific deficiencies within one project that is not entirely implemented yet. For 1 recommendation deadline of implementation is not in force yet.

Regarding implementation of recommendations of audits of operations reported in ACR 2014 – there were 33 open recommendations (*see Annex 8*).

It was reported in the ACR 2014 that results of one audited project within complementary audit of operations was under contradictory procedure at the moment

of preparation of ACR 2014. As a result of contradictory procedure recommendation was not issued (*see Annex 8, Point 31*).

At the moment of preparation of current ACR, there are: 8 recommendations not yet implemented, including 4 – partly implemented concerning to the defects of construction works and in-depth evaluation of the eligibility of expenditure and for 1 deadline of implementation of recommendation is not in force yet.

Recommendations that are not entirely implemented do not have an impact on the evaluation of the ACR.

8. OTHER INFORMATION

8.1. Complementary audits of operations

In addition to the regular audit of operations, the Audit Authority in year 2015 performed one selection and selected 17 projects for complementary audit of operations No PDR-15/10. Following the conditions laid down in the EC's Guidance on sampling methods for audit authorities (COCOF 08-0021-03-EN) section 8.2.1 Audit Authority assessed the sample initially carried out, namely in relation to the results of the risk analysis of each programme and coverage of priority axes audited. As the result of assessment it was concluded that additional work is needed.

Complementary audit No PDR-15/10 has been performed from 27 August 2015 and is still ongoing for some operations (for 11 projects out of 17 projects), in order to reach reasonable assurance whether the results of regular audit of operations and opinion of certain internal control systems remain constant and the expenditure declared to the EC are eligible.

The scope of complementary audit see in *Sections 8.1.1.-8.1.3*.

8.1.1. Representativeness of the audit work

After the assessment of sample of regular audit of operations it was concluded that the coverage of operational programmes and respectful European Union fund – ESF, ERDF, CF as well as priority axes audited during whole programming period 2007-2013 in some OP and priority axes is not representative enough:

- 1 OP “Human Resources and Employment” (ESF) – during regular audit of operations (for declared expenditure 2014) 3 operations and 11 payment claims were audited. During the whole programming period 2007-2013 (regular audits and complementary) 139 operations and 267 payment claims have been audited. After in depth analysis in the light of priority axes/measures it was concluded that for 3 of 1st OP's priority axes/measures the audit work is not representative enough. Depending on the audit work carried out during the whole programming period the complementary sample was selected for each priority axes/measure identified – for more details see *Table 11*. Therefore complementary sample of 7 operations and 24 payment claims was done.

Table 11: Complementary sample per OP: ESF

Priority axes/measure	Name	Audited in Programming period 2007-2013		Complementary sample		State of progress – 18.12.2015
		Payment claims	Operations	Payment claims	Operations	
1.2.2.	Lifelong learning and the development of education and lifelong learning institutions involved in capacity and improve cooperation	11	6	7	2	1 completed 1 audit in progress (discussions on eligibility rules)
1.5.2.	Human Resources Capacity Building	8	7	13	2	2 completed
1.5.3.	Administrative and planning capacity building for planning regions and local municipalities	1	1	4	3	3 completed
Total				24	7	6 completed

- 2 OP “Entrepreneurship and innovations” (ERDF) – similarly to 1 OP “Human Resources and Employment” (ESF) the OP’s priority axes/measures were detected in which the audit work is not representative enough. The analysis resulted in the complementary sample of 2 operations and 5 payment claims – for more details see *Table 12*. Nevertheless after the sampling was accomplished AA received information on the European Court of Auditors mission to Latvia in which they have selected the respective project in the measure No.2.3.2, therefore this project was excluded from the complementary audit work. Therefore the audit work will be carried out for 1 operation and 4 payment claims.

Table 12: Complementary sample per OP: ERDF

Priority axes/measure	Name	Audited in Programming period 2007-2013		Complementary sample		State of progress – 18.12.2015
		Payment claims	Operations	Payment claims	Operations	
2.3.1.	Business Support Activities	7	6	4	1	Audit in progress
Total				4	1	

- 3 OP “Infrastructure and Services” (ERDF, CF) – applying the same criteria as to 1OP and 2OP the priority axes/measures have been detected, as a result 3 operations and 4 payment claims (i.e. 1 operation and 2 payment claims for CF) have been selected – for more details see *Table 13*.

Table 13: Complementary sample per OP: ERDF/CF

Priority axes/measure	Name	Audited in Programming period 2007-2013		Complementary sample		State of progress – 18.12.2015
		Payment claims	Operations	Payment claims	Operations	
3.3.2.	Sustainable transport system	0	0	2	1	Audit in progress
3.4.2.	Tourism	2	1	1	1	Audit in progress (discussions on eligibility and public procurement issues)
3.6.2.	The complex support to local governments on growth	1	1	1	1	Audit in progress (discussions on public procurement issues)
Total				4	3	

As the result of complementary audit (within the completed audits for 6 operations) no errors were identified. For the remaining 5 operations the audits are in progress and the results will be taken into the account in the Final Control Report.

8.1.2. Individually risky units/projects:

During the programming period 2007-2013 the Audit Authority receives information about a variety of possible deficiencies within implementation of the EU funded projects (correspondence between the project administrating institutions and other interested parties, including individual complaints and information from media) as to why the projects were considered as high risk projects.

In total 6 projects were selected for complementary audit No PDR-15/10 –for all projects only risky areas covered³⁵ – for which complaints and EC requests have been received and the deficiencies were not remedied (no appropriate financial corrections and/or payments recovered). Expenditure of the selected projects was declared to the EC till the end of 2014.

The audit for all 6 operations, included in the scope of complementary sample following the issues indicated by the EC and received complaints, are still in progress and the results will be taken into the account in the Final Control Report.

8.1.3. Projects from risky areas identified:

Considering the results of regular audit of operations, it was concluded that most of the errors and deficiencies were found in the field of public procurement. Other risky areas were not detected and therefore additional sampling was not necessary. In addition the complementary audit scope mentioned previously (see

³⁵ Procurements, possible conflict of interests and achievement of project aims

Section 8.1.1. and 8.1.2) covers the public procurement issues therefore no additional sampling was carried out.

8.1.4. Summary

For now (results until 18 December 2015) within the complementary audit no recommendations have been issued. Any issues detected and recommendations issued will be taken into the account in the Final Control Report.

8.2. Audit of negative amounts – recoveries and corrections

The expenditure declared during year 2014 included negative amounts of EUR (58 957 198,21). The amount of negative sampling units is treated as a separate population EUR (13 183 466,93)³⁶. Not considered as negative sampling units amount EUR (45 773 731,28)³⁷.

From the population of 80 units³⁸, 50 negative amounts³⁹ in total of EUR (13 135 209,66) were selected and audited. During the audit⁴⁰ Audit Authority verified whether the amount corrected corresponds to what has been decided by the national authorities or the EC.

Non-compliances were not detected.

Regarding the management and control system audit reported in previous ACR 2014⁴¹, Audit Authority issued a report that was sent to the EC on 3 February 2015 via SFC2007. The Certifying Authority was assessed in the category 1 – the management and control system within the Certifying Authority works well.

During the horizontal system audit on preparation for closure 2007-2013, the assurance was gained regarding the accuracy and regularity of the statement prepared in accordance with the format set in Annex XI of Regulation 1828/2006 that has been sent the EC on 31 March 2015 via SFC2007.

8.3. Closure of 2007–2013 programming period

In 2015 Audit Authority performed a horizontal management and control system audit regarding the closure of 2007–2013 programming period. The audit concluded that the institutions are well prepared for closure although some institutions need to pay attention to their capacity in order to meet deadlines (*see Section 4*). In 2016 Audit Authority is planning to perform a separate management and control system audit regarding preparation for closure of FEI.

³⁶ According to Section 5.5 of the European Commission Guidance on sampling methods for audit authorities (COCOF 08-0021-03-EN)

³⁷ Temporary withdrawals, transfers of operations from one programme to another, clerical errors etc.

³⁸ Negative amounts within 61 projects

³⁹ Within 33 projects

⁴⁰ Audited during audit No DR-15/3

⁴¹ AA carried out audit No SIST-SEI-14/15 in the Certifying Authority

8.4. Audits of the European Commission and the European Court of Auditors

8.4.1. During the reference period final reports for several audits of previous periods have been received:

1. European Court of Auditors letter that closes the audit SPF-6643 (mission 24 to 28 November 2014) carried out in the Management Authority (DAS 2014) in order to assess the payment made on 16 June 2014 within the OP Infrastructure and Services (No 2007LV161PO002) was received on 25 August 2015. No errors with financial impact were found.

2. Final report for the DG REGIO audit mission No 2013/LV/REGIO/C2/1285/1 (12 to 16 May 2014) in order to assess the functioning of management and control system in particular the management verifications as required by article 60(b) of EC Regulation 1083/2006 and articles 13.2 to 13.4 of EC Regulation 1828/2006, with a focus on public procurement (OP Infrastructure and Services (No 2007LV161PO002)) was received on 3 December 2015.

Management and control system (Key requirement 4 Adequate management verifications) was assessed - works, but some improvements are needed (Category 2). In total 5 recommendations were issued. Finding regarding the restrictive selection requirements limiting the works of sub-contractors is thought to be systemic (see also *Section 5.6. Point 2*). Managing Authority identified affected payments and calculated financial corrections regarding the restrictive selection requirements (limitation of sub-contractors). On 22 September 2015 Decision of the Cabinet of Ministers of the Republic of Latvia was taken stating that the affected expenditure are to be recovered from the state budget and are to be withdrawn from the declarations.

8.4.2. Findings of audit missions that are still open:

Regarding the DG REGIO audit mission No 2013/LV/REGIO/C2/1242/1 (25 to 29 November 2013), two findings regarding the imposed financial corrections of public procurement (requirement of public building and certification of experts) are still open. The EC Letter of 30 October 2015 confirms a hearing for the issues and technical meeting (held on 17 December 2015) to take place. (see also *Section 5.6. Point 3*)

8.4.3. During the reference period several audit missions were carried out:

1. DG REGIO audit mission No 2015/LV/REGIO/C2/1454/1 (fact finding visit from 21 to 22 January 2015) was carried out in order to review the work of the Audit Authority for the preparation of the ACR for the 2007-2013 programming period (OP Infrastructure and Services (No 2007LV161PO002) and OP Entrepreneurship and Innovation (No 2007LV161PO001)). On 4 February 2015 Audit Authority recalculated projected error rate of 1.06% and on 26 February 2015 EC Letter was received accepting the Audit Opinion and ACR 2014.

2. European Court of Auditors audit mission (5 to 9 October 2015) was carried out in the Managing Authority (DAS 2015) in order to assess the payment made on 11 March 2015 within the Operational Programme Entrepreneurship and Innovation (No2007LV161PO001). Draft report is not received yet.

3. DG REGIO audit mission No 2015/LV/REGIO/C2/1500 (24 to 27 November 2015) was carried out in order to review the work of the Audit Authority for the preparation of the ACR for the 2007-2013 programming period (OP Infrastructure and Services (No 2007LV161PO002) and OP Entrepreneurship and Innovation (No 2007LV161PO001)). Conclusions of the visit are not received yet.

8.5. The overall level of assurance from the combination of the results of the system audits and audits of operations

The Audit Opinion of the Audit Authority is prepared in accordance to the EC Regulation No 1828/2006 Annex VII and ISA 800 “Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks”.

The Audit Opinion results from the management and control system audits and audits of operations. The relationship between the management and control system audits and audits of operations that is determined by the Audit Authority is set out in *Table 14*.

Table 14: Preparation of the Audit Opinion

MCS audit results	Materiality level		Systemic error where financial correction cannot be prevented	
	Below materiality level < 2%	Above materiality level > 2%	Significant, but not comprehensive	Significant and comprehensive
1	Unqualified opinion	Qualified opinion	-	-
2	Unqualified opinion	Qualified opinion	Qualified opinion	-
3	Qualified opinion	Qualified opinion / Adverse opinion	Qualified opinion / Adverse opinion	Adverse opinion
4	Adverse opinion	Adverse opinion	Adverse opinion	Adverse opinion
Information missing	Disclaimer	Disclaimer	Disclaimer	Disclaimer

The management and control system is assessed in category 2 (*see Section 4 and Annex 5*) and the error rate of the audits of operations is below the materiality level (*see Section 5*), as well based on other information (*see Section 8*) the Audit Authority conclude to issue an Unqualified Opinion.

8.6. Assessment of the Audit Authority

In 2015 the work of Audit Authority was assessed by DG REGIO in two audit missions - see *Section 8.4.3*.

As reported in ACR 2014 an external evaluation (according to International Quality Control Standard) of the Audit Authority was carried out by SIA "Ernst & Young Baltic". Final report was received on 9 December 2014 concluding the Audit Authority's compliance with the International Standards on Auditing. Some recommendations were issued related to improvements of management of Audit Authority and staff training. In 2015 the Audit Authority already implemented most of the *best practice* recommendations issued by SIA "Ernst & Young Baltic". Including an audit IT tool was purchased and installed for all auditors and presently is being adjusted for audits of Audit Authority.

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