



EUROPEAN COMMISSION

Directorate General
Regional Policy
Audit
The Director

Brussels,
REGIO/J2/REGIO/D(2012) 1075934

Subject: ERDF and Cohesion Fund – Complementary EPM 'To obtain assurance on the functioning of the management and control systems through the audit of Operational Programmes / areas and horizontal themes (2010-2012)'

Final conclusions on audit mission of 15-19 November 2010 (mission n° 2010/BG/REGIO/J2/933/1)

Ref.: Your letter PB-3-2280 of 26 July 2011 (Ares(2011)816255)
Our letter of 10 February 2012 (Ares(2012)153747)
Your letter PB-3-696 of 1 June 2012 (Ares(2012)672552)

Your Excellency

I am writing to inform you that Directorate-General of Regional Policy has concluded the audit carried out on the Regional Development Operational Programme (2007BG161PO001) and on the Transport Operational Programme (2007BG161PO004).

Following the analysis of the information provided in the Member State's letters above-mentioned, you will find in annex I our conclusions in this regard.

I would like to draw your attention to Finding 5. This finding relates to the compliance of operations with the requirements of Article 57 of Council Regulation (EC) N° 1083/2006. Although this finding has been closed in the context of our audit, the audit authority is nonetheless requested to verify this issue in its future audit work. The managing authority is also requested to cover this issue in its future ex-post management verifications.

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As the irregular expenditure detected during the audit, as presented in annex II, has been accepted by the national authorities and as they have agreed to make the required financial corrections, no further action will be taken by the Commission. The audit is therefore **closed**. Details of the financial corrections accepted by Member State are set out in annex II.

I would like to remind you that under Article 90(1) of Council Regulation (EC) N° 1083/2006, the competent bodies and authorities are required to keep available all relevant documents for a period of three years following the closure of an operational programme as defined in Article 89(3) of the Regulation or three years following the year in which partial closure takes place, in case of documents regarding expenditure and audits on operations referred to in 90(2) of the Regulation.

Yours faithfully

A large, dark, rectangular redacted area covering the signature of Lena Andersson Pench.

Lena Andersson Pench

Enclosures: Annex I - Commission's conclusions
 Annex II - Summary of financial corrections accepted by Member State

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ANNEX I – COMMISSION’S CONCLUSIONS

1. FINDINGS IN RELATION TO THE REGIONAL DEVELOPMENT OPERATIONAL PROGRAMME (2007BG161PO001)

General findings 1, 4 and 5

Finding n°1: Lack of an effective procedure for assessing the financial capacity of applicants to implement and maintain the project

The assessment of the financial capacity of beneficiaries, as performed by the managing authority prior to the signature of the grant contracts, was not sufficient. This was evidenced by the fact that beneficiaries often have problems with ensuring payments to contractors in a timely manner.

The managing authority should ensure an effective procedure for assessing the financial capacity of the applicants to implement and maintain the operation.

In addition, the managing authority should ensure that reimbursement of payment claims submitted by beneficiaries is made in a timely manner.

Member State reply

The managing authority informed the Commission that the recommendation is being implemented. The evaluation of the financial capacity of applicants is carried out at the technical/financial stage. Detailed criteria for evaluation of the economical standing of the candidate are included in the evaluation.

The reply also stated that the beneficiaries (e.g. municipalities) have the possibility to apply for resources from the Fund for local authorities and governments. This enables them to ensure sufficient financial resources are available for the implementation, completion and maintenance of the operations co-financed from the ERDF.

Commission position

Actions undertaken by the Member State in order to address the deficiency identified during the audit were considered adequate. Nevertheless, since at the time of drafting the reply to the Commission's audit report the implementation of all corrective measures was not finalised, the national authorities were requested to submit confirmation on completion of all the corrective measures mentioned.

Member State second reply

The managing authority informed the Commission that the recommendation has been implemented. The eighth version of the Manual on the Management and Implementation of the Regional Development OP was approved on 14 February 2012. The Guidelines for applicants expressly indicate the documents required for the verification of the economic and financial capacity of applicants, their qualifications etc. To ensure the sustainability

of planned investments at the stage of submission of project proposals applicants have to submit a decision of the municipal council confirming that the necessary co-financing will be made available.

Additionally, in order to ensure the timely reimbursement of the amounts indicated in payment requests, the Procedures Manual stipulate the maximum length of the period for verification of the payment requests, which the managing authority receives from beneficiaries, depending on their type, their completeness and compliance with applicable technical requirements.

Commission position

The corrective measures have been implemented. The finding is **closed**.

Finding n°4: Unsatisfactory quality of management verifications in the area of public procurement

Findings presented in relation to the three operations audited under the Regional Development OP indicated weaknesses in the quality of the work carried out by the managing authority during its management verifications in the area of public procurement.

The managing authority was requested to ensure that a detailed analysis of all public procurement findings identified during audits was carried out. The nature of the irregularities should be examined with a view to improving the checklists used and the quality of the verifications carried out by the controllers.

As the deficiencies identified by DG Regional Policy audit are of a systemic nature, the managing authority was requested to review its own verification reports in order to identify any deficiencies and, where relevant, to carry out additional checks.

In addition, the staff involved in the execution of public procurement verifications should have been provided with relevant trainings.

Member State reply

The managing authority stated in its reply that the recommendation is being implemented. The reply also referred to a financial correction of BGN 3 569 000 imposed as a result of re-performed management verifications in the area of public procurement. Re-performance of the management checks have been carried out as requested in the Commission audit report, in relation to expenditure certified in 2010.

The managing authority has developed more detailed checklists for the on-the-spot checks as well as for ex-ante and ex-post controls, which are included in the procedures manual. The administrative capacity of the managing authority was improved.

Commission position

The Commission recognised the efforts of the managing authority and corrective actions taken in order to eliminate deficiencies in the area of public procurement verifications.

Nevertheless, the Commission requested the managing authority to provide a summary analysis of the results of the re-performed public procurement verifications together with a list of all financial corrections implemented as a result of these re-performance checks.

Member State second reply

The managing authority has carried out follow-up checks to verify the legality of all contracts concluded in 2010 and 2011 under which expenditure had been certified. The amount of certified expenditure in relation to which follow-up checks were carried out stood at BGN 151 482 844 in 2010 and BGN 109 000 811 in 2011. This resulted in registering irregularities and imposing financial corrections in the amount of BGN 11 103 290 in 2010 and BGN 2 345 779 in 2011.

Information about the checks conducted by the managing authority to verify the legality of the awarded public procurement contracts under all projects where expenditure has been declared to the European Commission and the respective amounts of detected errors in expenditure and imposed financial corrections was reported at project level.

Commission position

The corrective action has been implemented. The analysis of the re-performed public procurement verifications together with a list of all financial corrections implemented as a result of these re-performance checks has been provided. The finding is **closed**.

Finding n°5: Lack of clear long-term strategy for the maintenance of the operations financed from the social infrastructure measure

During the audit, DG Regional Policy auditors were informed of the adoption of the National Strategy for the 'Deinstitutionalisation of Children in Bulgaria'. Under this plan, closure of 130 existing institutions is envisaged.

The managing authority has approved co-financing under the Regional Development OP for a number of investments for homes for children which are due to close. These operations consisted mainly of the renovation or partial renovation of the related infrastructure.

The closure of these ERDF co-financed operations within five years of completion of this renovation work would breach Article 57 of Regulation (EC) No 1083/2006 which requires that an operation should not, within five years from its completion, undergo a substantial modification.

In the case of operations co-financed from the social infrastructure measures which fall under the scope of the reform referred to above this minimum requirement of five years will therefore not be respected.

The managing authority was requested to scrutinise the operations under the social infrastructure measure in order to identify all cases of non-compliance with Regulation (EC) No 1083/2006 in respect of the durability of operations.

Member State reply

The managing authority referred to a letter sent by the Minister of EU funds to DG Regional Policy dated 21 March 2011 with a possible option to convert the existing social infrastructure falling under the deinstitutionalisation reform into homes for people with disabilities, elderly people and homeless people from the minorities.

Commission position

The information requested was not provided. The managing authority was reminded to implement the corrective action specified in the audit report.

Member State second reply

The managing authority informed that in line with the reform of the social services system, three institutions for children with mental disabilities situated in Karnobat, Vidin and Razgrad will be closed. The buildings housing the respective institutions have been renovated under the Regional Development OP.

To ensure compliance with the principle of sustainability, a committee consulted specialist institutions in order to appraise the possibility of converting the buildings into social services centres for elderly people with mental disabilities thereby ensuring their continued unaltered use. According to the report of this committee, a partial internal conversion will allow the buildings to be adapted and used as centres of social services to the elderly. The interventions require adequate funding and may be financed from the operational programmes for the period 2014-2020. It should be noted that the three homes for mentally disabled children in the municipalities of Karnobat, Vidin and Razgrad will be effectively closed in mid-2014 at the earliest when the construction of the family-type accommodation centres is expected to be completed and the children relocated.

Commission position

The Member State reply did not provide sufficient assurances that the Article 57 of Regulation (EC) No 1083/2006 which requires that an operation does not, within five years from its completion, undergo a substantial modification, will be respected.

The managing authority is therefore requested to include the projects falling under the 'Deinstitutionalisation of Children in Bulgaria' plan within the scope of its ex-post management verifications and carry out a detailed analysis of their respect of requirements under Article 57 of Regulation (EC) No 1083/2006.

The finding is **closed** within the scope of this audit mission.

However, the audit authority is requested to follow-up this issue in its future audit work and during the closure of the programme.

Findings 10 and 11 relate to the Beneficiary: Sliven Municipality - BG161PO001-1.1.01-0219

Finding n°10: No final payment to the contractor

Although, the handover certificate for the works was issued in October 2008, the final payment of BGN 416 730 (EUR 213 071) had not been made to the contractor. The beneficiary did not provide any explanation as to why the contractor's final invoice has not been paid. In addition, interim payments to the contractor were made with substantial delays.

The managing authority was requested to provide an explanation why, after a period of more than two years, the beneficiary has still not paid the final invoice to the contractor.

Member State reply

The managing authority argued that it is not part of the contract for works and in the absence of the invoice issued by the contractor it has no legal basis for intervening.

Commission position

The Commission did not accept the response of the managing authority. The fact that the managing authority is not a part of the contract agreement between the beneficiary and the contractor does not prevent the managing authority from following up this issue. Pursuant to the Article 60 of the Regulation 1083/2006, the managing authority is responsible for implementation of the operational programme in accordance with the principle of sound financial management. This imposes on the managing authority the obligation of verifying that the co-financed products and services are delivered and that the expenditure declared by the beneficiary has actually been incurred and complies with the applicable rules.

Member State second reply

The managing authority informed that on 15 August 2011, the beneficiary Sliven municipality remitted to the contractor the amount of BGN 375 131, which represents a part of the final payment due under the invoice from October 2008. The amount of BGN 41 599 which covers the cost of the additional works and which represents the own contribution of the beneficiary remains outstanding while detailed checks are in progress in relation to all works contracts.

Commission position

The final payment to the contractor has been made. The finding is closed.

Finding n°11: Delay in the implementation of the second project component – Community house for disabled children and adults

According to the grant agreement dated 22 May 2009 the deadline for implementation of the operation was 15 months after the date of its signature. On 17 August 2010 the duration of the grant agreement was extended to 24 months (i.e. until 22 May 2011). As at the date of the audit (15 November 2010) the tender notice for this component was still not published.

According to the beneficiary the main reason for the delay was due to uncertainties regarding the overall legality of the award of the framework contract.

Considering the overall delay in implementation of this project component and the implications of the 'Deinstitutionalisation of Children in Bulgaria' reform the managing authority was requested to reassess the appropriateness of co-financing this element of the operation.

Member State reply

The managing authority referred to a financial correction of 25% of the works contract value and to the specific reasons for delay in the implementation of this contract.

Commission position

The reply of the managing authority did not address the merit of the finding, namely the need to reassess the appropriateness of co-financing the Home for children and adults with disabilities part of the project given the implications of the 'Deinstitutionalisation of Children in Bulgaria' reform.

The Bulgarian authorities were also reminded of the requirements of Article 57 of Regulation (EC) No 1083/2006. This article requires that an operation does not, within five years from its completion, undergo a substantial modification. This would be important if following the completion of a co-financed project a decision was subsequently taken to close the project or to substantially change its functions.

Member State second reply

The managing authority stated that the contract was in line with the 'Deinstitutionalisation of Children in Bulgaria' reform. Two social institutions, the Sveti Stilian Detepazitel Day Care Centre for children and adults with mental disabilities and the Sliven Home for Elderly People, will undergo exterior and interior renovation and will be fitted out under the project. The contract does not envisage interventions on homes for children with mental disabilities which are an element of the process of deinstitutionalising children with disabilities in Bulgaria.

Under the contract an access ramp and a lift will be installed at the Sveti Stilian Detepazitel Day Care Centre for children with mental disabilities, which will improve access for children with special educational needs. The exterior of the building will also be renovated. In addition, special equipment for physical, psychological and speech therapy will be purchased, including aids facilitating socialisation, tuition and the process

of learning. With a view to expanding the range of available social services a greenhouse for growing flowers will be built so as to allow older disabled children and adults to acquire floriculture skills. The development of specialist community-based social services will ensure an effective alternative to specialist institutions and, in the case at hand, will also build on the outcomes of project 'Deinstitutionalisation of children at risk through building dedicated family-type residential centres in Sliven Municipality'.

Commission position

The managing authority explained that the facility will not be influenced by the 'Deinstitutionalisation of Children in Bulgaria' reform. The finding is therefore closed.

Finding 12 relates to the Beneficiary: Karnobat Municipality BG161PO001-1.1.01-0128

Finding n°12: Public procurement irregularities identified (irregular prolongation of contract)

In the tender notice of 5 June 2009, the duration of the works constituted one of the award criteria and was set at maximum of 8 months¹. The tender documentation² also contained a reference to an 8 months period for completion of the works. The shorter the period proposed by tenderers, the higher the score awarded to them in the evaluation.

The contract was awarded to a company which proposed an implementation period of 6 months. The works started in August 2009. Works were suspended for the period January – April 2010 due to bad weather conditions. There was no formal amendment to the contract. The document certifying completion of the works is dated 7 September 2010, almost 13 months after commencement of the contract.

The prolongation of the contract represents an irregular modification of the terms of the tender resulting in an infringement of the public procurement law, namely a breach of the equal treatment and transparency principles (Article 2 of the Bulgarian Public Procurement Law).

A financial correction of BGN 51 030 (EUR 26 090) corresponding to 10% of the value of the works contracts awarded under the operation was proposed due to non-compliance with the public procurement law. The rate of the financial correction proposed was based on irregularity type n° 23 of the Guidelines for determining financial corrections to be made to expenditure co-financed by the Structural Funds or the Cohesion Fund for non-compliance with the rules on public procurement (COCOF 07/0037/03).

¹ Tender notice: Chapter II – subject of the procurement notice, section II. 3) – duration of the contract / final deadline for completion.

² Tender dossier: Section II – general conditions containing full description of the subject of public procurement

The managing authority was requested to confirm that it accepts this financial correction and that it agrees to implement the correction by deducting the amount concerned from the next expenditure declaration.

Member State reply

The managing authority disagreed with the Commission finding and argued that formally there was no contract modification. The works have been suspended due to the weather conditions. These weather conditions represented circumstances falling outside the responsibilities of the contracting parties. The managing authority stated that the contract remained formally unchanged. This opinion was confirmed also by the opinion of the public procurement agency. In addition, the national authorities provided a report from the meteorological agency which stated that the temperatures were exceptionally low. The average of the reported minimum temperatures was -3.5°C for January, $+0.1^{\circ}\text{C}$ for February and $+1.4^{\circ}\text{C}$ for March.

Commission position

The managing authority argued that the temperatures in the winter of 2010, namely from 6 January 2010 to 6 April 2010 were exceptionally low. This view was contested because temperature extremes are characteristic for Bulgaria. Moreover, the temperatures reported for January and March were only non-significantly lower than the long-term averages for the Karnobat area. The temperatures reported for February are higher than the long-term averages.

In any case, by January 2010, the works should have been approaching completion given the six month completion period stipulated in the contract.

The actual duration of the works was of almost 13 months, i.e. more than double the contractually agreed duration of the works of 6 months. The actual duration of the works after the deduction of the winter months, was still 10 months.

The statement that the contract remained formally unchanged is irrelevant in relation to the competition being factually distorted by the unfair advantage given to the contractor who was granted the contract based on a short proposed implementation period which was subsequently neither respected nor penalised.

The managing authority was requested to confirm that it accepts the financial correction of EUR 26 090 and that it agrees to implement the correction by deducting the amount concerned from the next expenditure declaration.

Member State second reply

The managing authority informed that the draft contract formed a part of the tender documentation. All interested parties that submitted tenders were aware of the clauses set out therein and had stated their agreement with them. Moreover, the clauses of the model contract and the one signed with the contractor were identical, i.e. no significant modifications were made.

The protocol dated 6 January 2010, which ascertains the condition of construction works in progress upon their suspension indicates that works were suspended due to exceedingly low temperatures which compromised the contractor's ability to comply with the relevant technological requirements. The protocol ascertaining the condition of construction works upon their resumption indicates that works were resumed on 6 April 2010 when weather conditions improved sufficiently.

The possibility to suspend/resume works is envisaged in the signed contract, which stipulates: 'where works are suspended on an order of the contracting authority or another local or central government body; or when suspension is objectively warranted by circumstances for which the contractor may not be held liable, the contract period shall be adjusted accordingly'. The contract does not stipulate a requirement for contract modification hence no annex was signed.

The managing authority reiterated that the cited provisions were identical to those specified in the model contract included in the tender dossier and that all interested parties were familiar with them. This means that the contracting authority acted in compliance with the principles of publicity, transparency and equal treatment of applicants underlying the Public Procurement Act.

On 14 May 2010 a statement ascertaining that works are fit for handover was drawn up. The protocol further ascertained that all works have been carried out in full and in accordance with the approved technical specifications. Following their completion, construction debris was removed and the site was cleaned and restored to its prior condition.

A report issued by the National Meteorology and Hydrology Institute under the jurisdiction of the Bulgarian Academy of Sciences, which indicates the minimum air temperatures measured in Karnobat in the period between 6 January 2010 – 6 April 2010, has been annexed to the documentation.

An annex to the final report dated 31 January 2011, which was drawn up by the beneficiary of the infrastructure project, indicates that construction works were completed on 14 May 2010.

According to the report on implementation drawn up by the beneficiary and the updated works schedule construction and renovation works and the purchase and installation of equipment were undertaken as two separate activities (Activities No. 4 and 5).

The commencement and completion dates for Activity 4 *Construction Works* were 17 August 2009 and 14 May 2010, respectively. The three-month delay was documented and occurred due to low temperatures that did not allow the contractor to comply with the relevant technological requirements. The commencement and completion dates for Activity 5 *Purchase and Installation of Equipment* were 16 August 2010 and 21 August 2010, respectively. This means that no delay in implementation has occurred.

In view of the facts of the case the extension of the project implementation period was lawful and did not constitute an infringement of the Public Procurement Act, including the principles of equal treatment and transparency laid down therein.

Commission position

The Commission accepts the managing authority's explanation that the contract includes a suspension clause in the event of bad weather. This suspension clause was included in the model contract in the tender dossier. Therefore, this finding is closed.

ANNEX II – SUMMARY OF FINANCIAL CORRECTIONS ACCEPTED BY MEMBER STATE

Finding Nº	Amount of irregular expenditure in € (Basis for calculation of financial correction)	% Rate of assistance	% Financial correction	Amount of financial correction agreed by Member State in €	Date of letter of acceptance by Member State (Ares nº)
9	895 468	85%	25%	190 287	26 July 2011 (Ares(2011) 816255)
TOTAL	895 468			190 287	