



ISSN 2029–2236 (print)
ISSN 2029–2244 (online)
SOCIALINIŲ MOKSLŲ STUDIJOS
SOCIAL SCIENCES STUDIES
2010, 1(5), p. 237–252.

REGULATION OF THE CONTROL SYSTEM FOR EUROPEAN UNION FINANCIAL SUPPORT IN LITHUANIA, 2004–2006

Jaroslavas Buinauskas

Mykolas Romeris University, Faculty of Economics and Finance Management,
Department of Finance and Taxes
Ateities 20, LT-08303 Vilnius, Lithuania
Phone (+370 5) 2714 521
E-mail fmk@mruni.eu

Received 29 August, 2009; accepted 15 March, 2010

Abstract. *Lithuania's joining of the European Union (EU) opened up the possibility to receive financial support from the EU Cohesion and Structural funds. Establishing a proper system for the management and control of EU financial support has become one of the most important tasks for the Lithuanian Government. Since non-eligible funds must be returned to the European Commission's account, the control system for EU financial support requires special attention.*

Since Lithuania entered the European Union, EU financial support has been included in the national budget. Since the budget of the Republic of Lithuania is subject to public financial control, EU financial support must come under public scrutiny as well.

A control system for EU financial support was created during the 2004–2006 programming period. However, when defining the activities of the control subjects, insufficient powers were provided to ensure their effective work in the supervision of European Union funds.

Keywords: *European Union financial support, budgetary relations, public financial policy, finance control system.*

Introduction

Lithuania's joining of the European Union opened up the possibility to use financial support provided by the European Union Cohesion and Structural Funds. Prior to membership in the EU, Lithuania received support from SAPARD, PHARE and ISPA funds, which were allocated for future member states to help them prepare for membership and to introduce them to EU financial support policy.¹

Receiving support from EU Cohesion and Structural Funds entails the particular challenge of successfully using EU financial assistance.

Lithuanian legislation concerning EU financial support establishes that unused or improperly utilized EU funds must be returned. Therefore, one of the main tasks for the Lithuanian Government is the creation of a control system that would ensure the successful use of EU financial support and the security of EU financial interests in Lithuania.

This control system is defined by EU regulations and decisions that are of direct legal application, laws adopted by the Seimas (Lithuanian parliament), decisions of the Government and other legislation. It should be noted that the European Community Treaty provides no specific financial control model for the Member States, only a common set of obligations.

To harmonize national legislation with EU legislation, Lithuania adopted whole series of new laws and amendments to existing legislation pertaining to EU financial support, its management, control and the distribution of functions between different institutions. This was done during the 2004–2006 financial programming period. However, not all legislation concerning the control of EU financial support was properly prepared; therefore, the successful operation of an integrated control system guaranteeing the proper functioning of EU financial aid solutions may not be assured.

The issue in question has not been extensively analysed in Lithuania, and the specific literature on the control of EU financial support is sparse. For the most part, only the control and auditing principles have been analysed.² In fact, there are only a few books on the management of EU financial support³ and none of them are concerned with examining the EU financial support system. I have therefore selected this particular issue to analyse from both, the practical and the theoretical vantage points. An analysis of the legal regulation of the control system of the 2004–2006 programmes is particularly

1 Vilpišauskas, R. *Europos Sąjungos vidaus rinka ir Lietuva* [The European Union's internal market and Lithuania]. Vilnius: Eugrimas, 2003, p. 60.

2 Arens, A. A. *Auditing and assurance services: an integrated approach*. Beasley Upper Saddle River: Prentice Hall, 2006; *Handbook of International Auditing, Assurance, and Ethics pronouncements*. New York: IFAC, 2005; Lakis, V. *Audito sistema: raida ir problemos. Monografija* [Auditing system: development and issues. Monograph]. Vilnius: Vilniaus universiteto leidykla, 2007; Weirich, T. R.; Pearson, T. C.; Reinstein, A. *Accounting & auditing research: tools and strategies*. London: Thomson, 2005.

3 *Europos Sąjungos parama: Lietuvos galimybės* [European Union structural funds: opportunities for Lithuanian]. Vilnius: Versus Aureus, 2006; Stoškutė, A. *ES struktūriniai fondai – Lietuva* [EU structural funds – Lithuania]. Vilnius: VŠĮ „Vertimo, dokumentacijos ir informacijos centras“, 2004; Bernotaitė, K. *Peculiarities of the legal regulation and implementation of European Union structural funds in Lithuania*. Vilnius: Mykolo Romerio universitetas, 2008.

relevant, because this support has been used till the end of 2008; with a detailed analysis of the control system, it should be possible to identify which aspects of legal regulation should be improved. In addition, a comprehensive analysis of the control system should determine the direction for the improvement of legal regulation.

For the description of control system for EU financial support and the analysis of the gaps in the regulation thereof, the following sources were used: normative documents, internet sources, as well as publications by the Lithuanian and foreign authors.

1. The Position of EU Financial Support Control in the System of Public Financial Control

Prior to analysing the regulation of EU financial support, the concept of control and the position of control in the Lithuanian legal system have to be identified.

‘Control’ is one of the constituents of ‘management’ which in turn arises from the purposes of state and authority.⁴ Control plays a certain role in state management. This role is determined by the purpose of control—the process of supervision (monitoring). Therefore, control is one of the final stages in state management and its aim is to assess the level of achievement of the set goals; following such an assessment, the existing goals and tasks can be modified or new ones can be set. The management cycle could not function without the element of control. Thus, we may conclude that control, as an element of management, is the process of monitoring the management object. Its main purpose is to assess the validity, effectiveness of the decisions made and the results of their implementation, to identify deviations in such implementation, and to try to eliminate deficiencies and correct the existing situation.

In the field of public finances, ‘control’ is distinctive in that it is carried out by all public institutions, regardless of their main tasks and fields of activity.

Public finances is the object of public finances control.⁵ In this case, it is very important to define the concept of public finances. In the narrow sense, public finances can be considered as the state (or municipality) budget, its formation use. In the Republic of Lithuania, this particular field is regulated by the Law on Budget Composition and detailed legislative acts passed on the basis of this law. Moreover, control of public finances may be understood as the state (or municipal) budget, its formation and control over its use. In a broad sense, in addition to the state (or municipal) budget, a number of other elements that constitute the entire national assets of the society have to be considered. In addition to the formation and use of the state (or municipal) budget, these elements include natural resources, industrial-economic activity, their distribution and use. In a broad sense, the control of public finances is the control over the formation, composition and use of state assets.

4 Stepašin, S. V.; Stoliarov, N. S.; Šochin, S. O., et al. *Gosudarstvenyj finansovyj kontrol* [State financial control]. Sankt Peterburg, 2004, p. 74.

5 *Ibid.*, p. 83.

Since Lithuania became a member of the European Union, EU financial support has been included in the special programs of the national budget. The budget of the Republic of Lithuania is the object of public finances control; thus, the control of EU financial support is one of the types of public finances control.

2. Aspects of the Control System for EU Financial Support during 2004–2006 from the View of Public Finances Control

EU financial support can be analysed by employing the method of system analysis. It can be analysed as a holistic phenomenon interacting with other phenomena or it can be viewed as a specific control system composed of individual and mutually interacting elements. Having chosen the latter approach, I will attempt to identify aspects of the control system for EU financial support.

The following are the main regulations of the European Commission providing for control systems during the 2004–2006 period: 2 March 2001 European Council (EC) Regulation No. 438/2001 laying down detailed rules for the implementation of Council Regulation No 1260/1999 as regards the management and control systems for assistance granted under the Structural Funds ('the regulation on structural funds') and 29 July 2002 European Council Regulation No. 1386/2002 laying down detailed rules for the implementation of Council Regulation No 1164/94 as regards the management and control systems for assistance granted from the Cohesion Fund and the procedure for making financial corrections ('regulation on Cohesion Fund'). Hence, two separate regulations provide for control systems of the Cohesion and Structural Funds.

Based on the above-mentioned regulations, the Government of the Republic of Lithuania issued two Decrees: Decree No. 649 dated 31 May 2001 'Regarding placing of responsibility on public institutions for implementation of support from the European Union structural funds' ('the rules on management of Structural Funds approved by the Lithuanian Government'), and Decree No. 1026 dated 24 August 2001 'Regarding administration of support from the European Union Cohesion fund in Lithuania' ('the rules on management of Cohesion Funds approved by the Lithuanian Government'). These two decrees and several subsequent amendments to these decrees laid responsibility on public institutions administering the support received from the EU Cohesion and Structural Funds.

In the regulation on structural funds, the system of management and control is based on reliable financial practice; consequently, the rules on management of Structural Funds approved the Lithuanian Government provide for the function of an intermediate institution that assesses the implementing institution's applications for payment presented to the state treasury (paragraph 9.11). Meanwhile, the rules on management of Cohesion Fund as approved by the Lithuanian Government do not provide for financial control functions attributed to an intermediate institution.

Based on these decrees, we may conclude that institutions responsible for the control of EU Cohesion and Structural Funds may be divided into:

1. Institutions directly responsible for the management of EU financial support and for carrying out control functions;
2. Internal Audit services of institutions which are responsible for internal audits of EU funds management and control systems and performance of spot checks⁶;
3. External control subjects.

The implementing, intermediate, and payment institutions carry out control functions as provided for in the aforementioned decrees, and fulfil functions of EU financial support management. Thus, they can be considered as institutions directly liable for the management of EU financial support and for carrying out the control functions.

Regulation of the control functions of institutions directly responsible for management of EU financial support. One aspect of the EU financial support control system for the years 2004–2006 is inspections on the spot, as regulated by Article 4 of the Regulation on Cohesion and Structural Funds, the rules on management of Cohesion Funds (paragraph 14.10) and on the management of Structural Funds (paragraph 11.8.) approved by the Lithuanian Government. The implementing institutions must carry out inspections of separate fields of activity during the period of project implementation. Such inspections have to be formalized on the spot, and thus they are called on-the-spot checks. Regulations distinguish two types of checks—physical and administrative. In case of physical checks on the spot, representatives of the implementing institution have to inspect the place where the project is being implemented and evaluate how the project financed by the EU funds is implemented in practice. Administrative checks entail the review of project documentation and processes performed by entities implementing the project or the end beneficiaries. The proper performance of this function can prevent the improper use of funds, such as the well-known case of embezzlement of SAPARD funds in Lithuania.

A payment institution carries out the function of managing payment documents. However, more detailed inspections of payment documents are also carried out by implementing institutions. Therefore, when presenting declarations of expenditures to the European Commission, the payment institution has to make sure that these inspections are in order.

The regulation of the activities of internal audit services acting as subjects of EU financial support control. Internal audit services are a separate element of control, which performs sample checks and audits the management and control system. This is another specific feature of the EU finance support control system, which differentiates this control system from the public finances control system. By the 1 August 2005 Order No. 1K-266 of the Minister of Finances ‘Regarding the approval of sample methods for performing sample checks on the European Union structural funds allocated for implementing the measure of single programming document for 2004–2006’, sample methods of sample checks and internal audit of management and control systems were approved. Based on these methods, internal audit services must audit the effectiveness of existing management and control systems, and by the method of selection and on the basis of risk

6 Also called a Sample Check.

analysis, review expense declarations drafted in various levels.⁷ On the whole, internal audit services have to make sure that management and control systems operate properly and expenses are justified.

The Law on Internal Control and Internal Audit is the main document regulating the activities of internal audit services. According to this law, one of the main tasks is to assess the administration and use of funds received from the European Union and foreign institutions and funds. Article 9 of the regulation on the EU Cohesion Funds and Article 10 of the regulation on Structural Funds provide for the obligation to perform sample checks and internal audits of the management and control system. These provisions have been incorporated into the rules on the management of Cohesion and Structural funds approved by the Lithuanian Government.

The control of public finances is characteristic in its requirement for independence. This attribute differentiates it from other kinds of activities in both, the theoretical and the practical sense; in addition to separating the competences of individual subjects, it creates new special subjects of control that perform only the function of control.⁸ In Lithuania, this provision is included into the Law on Internal Control and Internal Audit, which provides that the head of the internal audit service or internal auditors may not be involved in the performance of any managerial function in a public legal entity, an entity subordinate to it or falling within its area of regulation.⁹ Therefore, internal audit services carry out the functions of control only.

It should be noted that according to the rules on the management of Cohesion Funds approved by the Lithuanian Government, internal audit services are attributed to the intermediate institutions. In the case of structural funds, internal audit services were considered to be intermediate institutions until 18 April 2005, when the rules on management of Structural Funds were amended and internal audit services were redefined as individual institutions. Internal audit services have functional independence from intermediate institutions, because the functions of the latter in branch ministries are carried out by one or more departments. Thus, they can be considered as individual institutions performing audit.

One reason for this gap in the regulation may be the lack of experience in managing EU financial support at the time when the rules on the management of Cohesion Funds were approved. Regulations provided for management, payment, intermediate and implementing institutions, and consequently, internal audit services were not considered as individual institutions, and the principles of public finances control were not considered.

Regulation of the activities of external subjects of EU financial support control. Some theories on public finances control differentiate between internal and external

7 See also: Minister of Finance of the Republic of Lithuania. 1 August 2005 Order No. 1K-226 'The European Union structural funds allocated to Lithuania for 2004-2006 Single Programming Document measures to implement activities on a selective checks on model validation techniques'

8 Stepašin, S. V.; Stoliarov, N. S.; Šochin, S. O., *et al.*, *supra* note 4, p. 76.

9 Law on Internal Control and Internal Audit. *Official Gazette*. 2002, No. IX-1253.

subjects of public finances control,¹⁰ whereas others also distinguish state subjects of public finances support.¹¹ In the author's opinion, internal subjects of control in the control system for EU financial support could be classified into institutions directly responsible for the management of EU financial support and those carrying out control functions and internal audit services.

The National Audit Office of Lithuania—the state subject of public finances support—is one of the main subjects of public finances control in Lithuania. It should also be noted that independent private audit companies, which carry out independent assessment of projects funded by EU funds, also play an important role. The EU Audit Chamber and other EU organizations and institutions in charge of EU financial support control are among the external EU control subjects.

Chapter XII of the Constitution of the Republic of Lithuania provides that the National Audit Office supervises the lawfulness of the possession and use of state property and the execution of the state budget.¹² Considering the fact that on 1 May 2004 Lithuania became a member of the EU and EU financial support was included in the special programs of the national budget, the National Audit Office is one of the most important subjects of EU financial support control.

Article 9 Paragraph 1 Item 6 of the Law on the National Audit Office provides that the National Audit Office audit respective fund management institutions and beneficiaries and assess how funds of the EU allocated for the Republic of Lithuania are used and how programmes in which Lithuania participates are implemented.¹³

According to Article 38 Paragraph 1 Item F of the 21 June 1999 Council (EC) Regulation No. 1260/1999 laying down general provisions on the Structural Funds, member states are primarily responsible for the control of support funds and, upon the conclusion of a programme, must submit to the European Commission a declaration drawn up by a person or department independent of the designated managing authority. Therefore, the Parliament of the Republic of Lithuania has commissioned the National Audit Office to carry out audits of EU financial support. The National Audit Office has to assess the project financed by EU funds prior to submitting the application for the last payment of support to the European Commission. This provision means that the function of final auditing of projects financed by the Cohesion and Structural Funds has been delegated to the National Audit Office.

This section reviewed the regulation of the control system for EU financial support during the 2004–2006 period based on the legislative acts of the EU and the Republic of Lithuania. Lithuania has adopted many legislative acts on the bases of EU legal sources; they aim at creating a unified control system encompassing all management stages and preventing the improper use of EU Cohesion and Structural Funds.

10 Stepašin, S. V.; Stoliarov, N. S.; Šochin, S. O., *et al.*, *supra* note 4, p. 110.

11 Mackevičius, J. *Auditas teorija, praktika perspektyvos* [Audit theory, practice and perspectives]. Vilnius: Lietuvos mokslas, 2001, p. 41.

12 *Lietuvos Respublikos Konstitucija* [Constitution of Republic of Lithuania]. Vilnius: Teisinės informacijos centras prie Teisingumo ministerijos, 1996.

13 Law on State control of Republic of Lithuania. *Official Gazette*. 2001, No. 112-4070.

3. Problems with the Legal Regulation of the EU Financial Support Control System, 2004–2006

In negotiations with the EU, Lithuania pledged to be able to fully apply the EU *acquis* in the area of finances control by 1 May 2004. As a result, seeking to apply the *acquis* (the total body of Community law, *Acquis communautaire*)¹⁴ requirements effectively, institutions were strengthened, administrative capabilities of respective personnel were enhanced, and new legislative acts were adopted or the old ones amended. At present, the control of EU financial support funds is a constituent part of public finances control. Seeking to properly regulate the control of EU Cohesion and Structural funds in the 2004–2006 period, many legislative acts were adopted which, in my opinion, fail to properly define the control system.

According to the rules on management of the Cohesion and Structural funds approved by the Lithuanian Government, internal audit services of intermediate institutions, which in my opinion do not belong to the intermediate institutions, are responsible for sample checks of Cohesion Funds (15 percent) and Structural Funds (5 percent) and internal audits of management and control systems.

In fact, no proper legal basis for the above-mentioned checks and internal audits has been created, because the limits of the competence of internal audit services are not specifically defined; internal audits can be performed only in public legal entities that are subordinate to the ministry and fall within the area of regulation.

The Law on Internal Control and Internal Audit provides that the objective of internal audit is to contribute to achieving the objectives of a public legal entity, its subordinate public legal entities or those within its area of regulation, through a systematic and comprehensive assessment and evaluation of risk management and internal control.¹⁵ According to the sample methodology on internal audit approved by the Minister of Finance, the entity subjected to the audit is defined as a public legal entity, its division(s), its subordinate public legal entity and/or one falling within its area of regulation.¹⁶ Hence, the field of competence of internal audit services is public legal entities wherein internal audit services are established, public legal entities subordinate to such public legal entities or those within its area of regulation.

It should be noted that internal audit services is a structural subdivision of the public administration subject (in this case—ministries) which, according to the theory of public law, can carry out only those functions that it has been granted by laws and legislative supplements. The competence of internal audit services is strictly regulated by legislation, and therefore, the functions of performing sample checks and internal audit of management and control systems, as specified in the rules on the management

14 Vilpišauskas R., *supra* note 1, p. 11.

15 Law on Internal Control and Internal Audit. *Official Gazette*. 2002, No. 123-5540.

16 Order of Minister of Finance on the Model of the internal audit methodology, internal auditors' professional code of conduct and internal audit needs assessment analysis of the outline approval. *Official Gazette*. 2001, No. 43-1982.

of Cohesion and Structural Funds approved by the Lithuanian Government, cannot be properly fulfilled.

In the context of EU financial support, the role of internal audit services is crucial. Their limited competence is a relevant problem in controlling EU Cohesion and Structural Funds. For example, having allocated EU support for transportation sector following the procedure for provision of limited support, 39 municipalities were assigned to implement projects. None of these public legal entities belong to the competence of internal audit service of the Ministry of Communications and Transportation, because the municipalities and one budgetary institution concerned are neither subordinate to the Ministry of Communications and Transportation nor to public legal entities falling within the area of the Ministry's regulation. The same could happen with other intermediate institutions, because when allocating EU structural funds, they would grant those funds to public legal entities subordinate to them and falling within the area of their regulation as well as that of other institutions. Therefore, internal audit services are not entitled to perform internal audits in entities implementing projects which are not subordinate to the branch ministries and do not fall within their area of regulation. Therefore, five percent sample checks and internal audits of management and control system cannot be adequately carried out.

To eliminate the above-mentioned drawback, intermediate institutions usually include a certain provision in the agreements with entities implementing projects upon the allocation of funds. Based on this provision, entities implementing a project have to submit themselves to the internal audit services of ministries carrying out sample checks and internal audits of management and control systems. Ministries are subjects of public administration, and thus employees of their internal audit services (public servants) must fulfil only functions they have been granted by legislative acts. Provisions of concluded agreements do not grant subjects of public administration the right to take more actions than prescribed by laws; thus, employees of internal audit services have no power to perform internal audits in public legal entities that are not subordinate to ministries and do not fall within their area of regulation.

Because of contradictory legislation, the proper functioning of a control system for EU financial support in 2004–2006 has become problematic. If obligations regarding sample checks and internal audit of management and control systems are performed improperly, the European Commission may suspend the provision of EU Structural Funds support to Lithuania. To rectify this problem, amendments are needed for the Law on Internal Audit and Internal Control that would specify the limits of competence of internal audit services. The Law on Local Self-Government should also be amended to include the provision that the central governing institutions—in this case, the internal audit services of ministries—be granted the right to control EU financial support.

Another problem related to the activities of internal audit services concerns private legal entities. *Internal audit services have no right to perform obligatory checks* not only in the public legal entities subordinate to ministries and falling within their area of regulation; they also have no right to do so in the *private legal entities*.

The Law on Internal Control and Internal Audit provides that the purpose of the law is to establish a basic legal framework, objectives, and procedures for the functioning of internal control, including financial control, and internal audit in a public legal entity that manages, uses, and disposes of state and municipal assets ('the public legal entity'), as well as the competence of the head of a public legal entity.¹⁷ In accordance with the Law on Management, Use and Disposal of State and Municipal Assets, the managers of assets are state or municipal institutions, the Bank of Lithuania, state or municipal enterprises, offices and organizations.¹⁸

It may be concluded that under the Law on Internal Control and Internal Audit, state and municipal institutions, offices, enterprises and organizations are the public legal entities which manage, use, and dispose of state and municipal assets. Thus, the law specifies in detail which legal entities under the provisions of the Law on Internal Control and Internal Audit are to be attributed to the public legal entities.

It should be noted, however, that neither private nor public limited liability companies are included in the regulation by the Law on Internal Control and Internal Audit. Even if a company is established by a public institution, under the provisions of the Law on Companies, the state has only rights as a shareholder, while the assets belong to (i.e., are managed, used and disposed of by) the respective private or public limited liability company under the right of ownership. We may therefore conclude that the control system for EU financial support cannot function properly, because private limited liability companies are the main entities implementing projects that receive this financial support. In my opinion, internal audit services of ministries have no right to carry out the functions prescribed to them by the decrees of the Lithuanian Government—the functions related to sample checks of EU Cohesion and Structural Funds and internal audits of management and control systems in the entities that implement those projects, the ultimate beneficiaries of this funding.

Considering these two problems in the regulation of the EU financial support control system—the contradictions between the Law on Internal Control and Internal Audit and the rules on the management of Cohesion and Structural funds approved by the Lithuanian Government and the duties and obligations specified by the EU regulations—Lithuania may face significant financial consequences. Namely, it may have to return a fraction of the EU financial support to the European Commission. To avoid such consequences, the Ministry of Finances of the Republic of Lithuania must initiate amendments that would clearly define who can perform checks on EU funds and in which legal entities.

Based on the analysis of the concept of public finance control, control is one of the constituent components of management. Since management is related to making binding decisions, control should also be treated as a management activity—making decisions that would be obligatory and binding on the controlled entities. According to the theory of public finances control, one characteristic of control is that its 'subjects are entitled

17 Law on Internal Control and Internal Audit. *Official Gazette*. 2002, No. 123-5540.

18 Law on the management, use and disposal of municipal assets of the Respublic of Lithuania. *Official Gazette*. 1998, No. 54-1492.

to give the objects of control binding orders regarding the identified drawbacks¹⁹. As a matter of fact, having signed financing agreements with entities implementing particular projects, the use of EU structural funds (implementation of projects) has intensified, and internal audit services of some ministries already carry out sample checks and internal audits of management and control systems. Upon performing these checks, internal audit services provide recommendations. However, there are problems with ensuring that these recommendations are followed.

In addition to the public legal entities falling within the regulation area of ministries (intermediate institutions), financing from EU Cohesion and Structural Funds is also granted to public legal entities that do not fall within the area of regulation (e.g. municipalities) and private legal entities.

Article 120 of the Constitution provides that municipalities may act freely and independently within their competence defined by the Constitution and other laws. Furthermore, the Law on Local Self-Government specifies that ‘local self-government is an administrative unit of the territory of the State, defined by law, the community of which has the right to self-governance guaranteed by the Constitution and implemented through a municipal council elected by the permanent residents of that administrative unit of the territory of the State and through an executive institution as well as other institutions and establishments of a municipality, which are formed by the latter and accountable to it’.²⁰ Thus, the head (minister) of an intermediate institution cannot influence in any way the decisions made by municipalities, and cannot carry out his/her functions concerning the implementation of the recommendations of internal audit services as specified by the Law on Internal Control and Internal Audit. The same problem arises in case of private legal entities—a head of an intermediate institution cannot ensure that the entities implementing the project make decisions on the timely implementation of recommendations. As a result, it is likely that if ministers are not granted the powers to ensure the implementation of the recommendations of internal audit services, the entities implementing these projects may fail to create a system for the management and control of EU Cohesion and Structural Funds and consequently, the projects financed by EU funds may be implemented in breach of the rules on implementation as prescribed by EU legislative acts.

Rule 1 Paragraph 3 of 10 March 2004 European Commission (EC) regulation No. 448/2004 laying down detailed rules for the implementation of Council Regulation (EC) No. 1260/1999 as regards the eligibility of expenditure of operations co-financed by the Structural Funds, and Article 39 of 6 January 2003 European Commission (EC) regulation No. 16/2003 laying down special detailed rules for implementing Council Regulation (EC) No 1164/94 as regards eligibility of expenditure in the context of measures part-financed by the Cohesion Fund regulate the conclusion of subcontracts. These Articles specify that all subcontractors must provide the audit and inspection bodies with all

19 Stepašin, S. V.; Stoliarov, N. S.; Šochin, S. O., *et al.*, *supra* note 4, p. 76.

20 Law of Republic of Lithuania on municipalities. *Official Gazette*. 1994, No. 55-1049.

necessary information about their subcontracting work.²¹ Another problem in regulating the control system of EU financial support in Lithuania is that not all Lithuanian legislative acts have been adjusted to the provisions of EU regulations. In conclusion, based on the above-mentioned provisions, institutions—both, auditing and controlling EU financial support—have the right to receive all necessary information directly from the subcontractor. This provision does not mention the contractors; however, provided it is possible to request information directly from the subcontractor, it is likely that this provision also implies the receipt of information and data from the general contractor. It should be noted, however, that this right has not been granted by Lithuanian legislative acts either to institutions performing audit of EU Cohesion and Structural Funds or to the institutions undertaking control thereof (except for the State Control and Financial Crime Investigation Service). This may lead to a situation where, seeking to financing by EU Cohesion and Structural Funds, contractors and subcontractors could conclude mutual agreements on participation in particular public tenders. The number of cases of improper use of funds and inadequate quality of works and services may increase, unless institutions carrying out the audit and control functions are granted the right to request documents from contractors and subcontractors. To create a properly functioning control system for EU financial support, provisions of EU regulations regarding control over contractors and subcontractors have to be incorporated into the Law on Internal Control and Internal Audit, the Law on Budgetary Institutions, and other laws and legislative supplements.

In summary, during the 2004–2006 programming period, Lithuania has not developed an effective control system for EU financial support that would be consistent with the EU *acquis* and the basic principles of the theory of public finance control.

Conclusions

The creation of a proper system for the management and control of European Union financial support in Lithuania has become one of the most important priorities for the state. Of particular concern is the control of EU financial support, because improperly used funds have to be refunded to the European Commission. On the basis of legislative acts regulating the control system for EU financial support and in conjunction with theoretical considerations, the author proposes the following conclusions:

1. As a constituent element of management, control is the process of monitoring the object of management. The purpose of this process is to assess the validity, effectiveness of the decisions made and the results of their execution, to identify shortcomings in their implementation, and to attempt to eliminate the unwelcome factors and correct the existing situation. In the sector of public finances, control is undertaken by all public institutions. The object of public finances control is the state (municipal) budget, its formation and use. Since joining the European Union, EU financial support has been

21 The European Commission 10 March 2004 Regulation (EC) No. 448/2004.

included in the special programmes of Lithuania's state budget. Therefore, the control of EU financial support is one of the constituent components of public finances control.

2. The control system for EU financial support consists of separate elements interacting with each other. These elements serve to distinguish this system from other types of public finances control. Certain aspects of EU financial support control are determined by the EU fund management system and institutions carrying out the functions of control. Distinct attributes include the internal audits of management and control systems and sample checks performed by internal audit services, which have to cover at least 5 percent of all Structural funds and 15 percent of all Cohesion funds, and have to be based on the selective entirety of approved types of activity. Another attribute is that physical and administrative checks are performed and formalized on the spot by the implementing institution.

3. Independence is the core principle of public finances control; therefore, institutions responsible for sample checks and internal audits of management and control systems have to be functionally independent from institutions making decisions. According to the rules on the management of Cohesion Funds approved by the Lithuanian Government, internal audit services are considered to be the intermediate institutions. Such distribution of functions fails to ensure the main principle of EU financial support management—namely, separation between management functions and control functions. Because of such inadequate regulation, the European Commission may suspend financing of Cohesion Fund projects.

4. Because of improperly defined limits of their competence, internal audit services of the ministries managing EU financial support cannot carry out the functions delegated to them by the decrees of the Lithuanian Government. Internal audit services can carry out checks in subordinate public legal entities or those falling within their area of regulation. However, EU support is usually granted to municipalities and other public legal entities not subordinate to ministries and not within their area of regulation. Because of these legal contradictions, Lithuania may face significant financial consequences. To prevent this, we may suggest that the Ministry of Finance should reconsider the limits of competence defined for the subjects of financial control.

5. When carrying out obligatory assessments of EU financial support, internal audit services present recommendations; the responsibility for the implementation of these recommendations falls on the head of a public legal entity (in this case, the ministers of relevant ministries). Financing from EU Cohesion and Structural Funds is granted to both, public legal entities within a ministry's area of regulation (intermediate institutions) and public legal entities outside this area of regulation (municipalities), as well as private legal entities. According to the Law on Local Self-Government, municipal administrations are functionally independent from central authorities. Moreover, private legal entities are independent from central authority in the management of their enterprises. Heads (ministers) of intermediate institutions have no right to issue mandatory orders to public legal entities not within their area of regulation, nor to private entities; as a result, they cannot guarantee that the identified drawbacks are eliminated when implementing the recommendations made by internal audit services.

6. EU regulations provide that subcontractors must provide audit and inspection bodies all necessary information about their subcontracting work while executing any subcontract. It should be noted, however, that this right has not been granted by Lithuanian legislative acts either to the institutions performing audit of EU Cohesion and Structural Funds or to the institutions undertaking the duties of control. Thus, we may conclude that not all Lithuanian legislative acts are in harmony with EU regulations. To create a properly functioning system of the EU financial support control, we suggest that the provisions of EU regulations on the control over contractors and subcontractors be incorporated into the legislative acts of the Republic of Lithuania.

References

- Brožaitis, H.; Linartas, R.; Nekrošius, V. *Europos Sąjungos regioninės plėtros pasekmių įvertinimas Lietuvos viešajai administracijai* [The European Union's regional development impact assessment for Lithuanian public administration]. Vilnius: Eugrimas, 2002.
- Campbell, L. *International Auditing. A comparative survey of professional requirements in Australia, Canada, France, West Germany, Japan, the Netherlands, the UK and the USA*. Macmillan, 1985.
- Council 21 June 1999 Regulation (EC), No. 1260/1999 laying down general provisions on the Structural Funds. *Official Journal of the European Communities*. 1999, No. L161.
- Decision of Government of Republic of Lithuania on the responsibilities for the European Union's structural funds implementation in Lithuania distribution between state institutions. *Official Gazette*. 2001, No. 48-1676.
- Decision of parliament of Republic of Lithuania on the order of the Republic of Lithuanian National Audit Office to carry out European Union financial assistance audits, *Official Gazette*. 2003, No 70-3171.
- European Commission's 10 March 2004 Regulation (EC), No. 448/2004. *Official Journal of the European Communities*, 2004, No. L72.
- European Commission's 6 January 2003 Regulation (EC), No. 16/2003. *Official Journal of the European Communities*, 2003, No. L2.
- Katkus, A. *Valstybės ekonominė kontrolė* [State economic control]. Vilnius, 1997.
- Law on Internal Control and Internal Audit. *Official Gazette*. 2002, No. 123-5540.
- Law on municipal organization of Republic of Lithuania. *Official Gazette*. 1994, No. 55-1049.
- Law on Municipal asset management, use and disposal of Republic of Lithuania. *Official Gazette*. 1998, No. 54-1492.
- Law on State control of Republic of Lithuania. *Official Gazette*. 2001, No. 112-4070.
- Lietuvos Respublikos Konstitucija* [Constitution of Republic of Lithuania]. Vilnius: Teisinės informacijos centras prie Teisingumo ministerijos, 1996.
- Nakrošis, V. *Europos Sąjungos regioninė politika ir struktūrinių fondų valdymas* [The European Union's regional policy and structural funds management]. Vilnius: Eugrimas, 2003.
- Mackevičius, J. *Auditas teorija, praktika perspektyvos* [Audit theory, practice and perspectives]. Vilnius: Lietuvos mokslas, 2001.
- Order of Minister of Finance on the Model of the internal audit methodology, internal auditors' professional code of conduct and internal audit needs assessment analysis of the

- outline approval. *Official Gazette*. 2001, No. 43-1982.
- Order of Minister of finance on the European Union structural funds allocated to Lithuania for 2004-2006 Single Programming Document measures to implement activities on a selective checks on the model validation methods. *Official Gazette*. 2005, No. 96-3615.
- Regulation (EC), No. 438/2001 laying down detailed rules for implementing Council Regulation (EC). 1260/1999 as regards the Structural Funds management and control systems.
- Regulation (EC), No. 1386/2002 laying down detailed rules for implementing Council Regulation (EC). 1164/1994 as regards the Cohesion Fund management and control systems and procedures for making financial corrections.
- Stamp, E.; Moonitz, M. *International auditing standards*. Prentice Hall. International, 1978.
- Stepašin, S. V.; Stoliarov, N. S.; Šochin, S. O., et al. *Gosudarstvennyj finansovyj kontrol* [State financial control]. Sankt Peterburg, 2004.
- Vilpišauskas, R. *Europos Sąjungos vidaus rinka ir Lietuva* [The European Union's internal market and Lithuania]. Vilnius: Eugrimas, 2003.
- Vitkus, G. *Europos Sąjunga enciklopedinis žinynas* [European Union Encyclopedic catalog]. Vilnius, 2008.

EUROPOS SAJUNGOS FINANSINĖS PARAMOS KONTROLĖS SISTEMOS REGULIAVIMAS LIETUVOJE 2004–2006 METAIS

Jaroslavas Buinauskas

Mykolo Romerio universitetas, Lietuva

Santrauka. *Lietuvai įstojus į Europos Sąjungą bei gaunant paramą iš Europos Sąjungos Sanglaudos ir struktūrinių fondų ypač svarbiu uždaviniu tapo veiksmingos Europos Sąjungos finansinės paramos kontrolės sistemos, kuri sudarytų sąlygas užtikrinti Bendrijos finansinių interesų saugumą Lietuvoje, sukūrimas.*

Viešųjų finansų srityje kontrolę vykdo visos valstybinės institucijos. Viešųjų finansų kontrolės objektas yra valstybės (savivaldybės) biudžetas, jo formavimo ir naudojimo sritys. Europos Sąjungos finansinė parama buvo įtraukta į Lietuvos Respublikos biudžeto specialiąsias programas. Lietuvos Respublikos biudžetas yra viešųjų finansų kontrolės objektas, todėl Europos Sąjungos finansinės paramos kontrolė yra viena iš viešųjų finansų kontrolės rūšių.

Europos Sąjungos finansinės paramos kontrolė – kontrolės sistema, susidedanti iš atskirų elementų, veikiančių tarpusavyje, kurie padeda ją išskirti kaip vieną iš specifinių viešųjų finansų kontrolės rūšių. Europos Sąjungos finansinės paramos kontrolės ypatumus suponuoja Europos Sąjungos lėšų valdymo sistema bei kontrolės funkcijas vykdančios institucijos. Išskirtiniai jos bruožai 2004–2006 m. programavimo laikotarpiu yra vidaus audito tarnybų atliekami valdymo ir kontrolės sistemos vidaus auditai bei atrankiniai patikrinimai, kurie turi apimti ne mažiau nei 5 procentus visų struktūrinių ir 15 procentų visų Sanglaudos fondo tinkamų išlaidų bei remtis atrankine patvirtintų veiklos rūšių visuma.

Lietuvos Respublikoje buvo sukurta Europos Sąjungos finansinės paramos kontrolės sistema 2004–2006 m. programavimo laikotarpiui, tačiau reglamentuojant kontrolės subjektų veiklą nebuvo suteikta pakankamai įgaliojimų, reikalingų užtikrinti sklandų jų darbą kontroliuojant Europos Sąjungos lėšų panaudojimą, t. y. vidaus audito padaliniai buvo pavaldūs tarpinių institucijų vadovams, todėl sunkiai buvo užtikrinamas jų nepriklausomumas. Taip pat nebuvo parengta teisinė bazė, sukurianti galimybes vidaus audito padaliniams atlikti patikrinimus ne ministerijų kompetencijai pavaldžiuose ar valdymo sričiai priskirtuose viešuosiuose juridiniuose asmenyse bei privačiuose juridiniuose asmenyse, nors parama tokiems juridiniams asmenims buvo skiriama, taip pat nei Europos Sąjungos Sanglaudos ir struktūrinių fondų audita, nei kontrolės funkcijas atliekančioms įstaigoms teisės aktais nebuvo suteikta teisė iš rangovų ir subrangovų gauti visą auditui atlikti reikalingą medžiagą.

Reikšminiai žodžiai: *Europos Sąjungos finansinė parama, biudžetiniai santykiai, finansinė valstybės politika, finansinės kontrolės sistema.*

Jaroslavas Buinauskas, Mykolo Romerio universiteto Ekonomikos ir finansų valdymo fakulteto Finansų ir mokesčių katedros doktorantas. Mokslinių tyrimų kryptys: finansų kontrolė, biudžetiniai santykiai, finansinė valstybės politika.

Jaroslavas Buinauskas, Mykolas Romeris University, Faculty of Economics and Finance Management, Department of Finance and Tax, doctoral student. Research interests: financial control, budgetary relations, public financial policy.