

**Summary of the results of the audit of the use of financial assistance within
the programme “PHARE 2001 Social and Economic Cohesion (SSG) – Development
of Small and Medium-Sized Enterprises” from the Investment Grant Fund (FDI)
by small and medium-sized enterprises**

2.1. Overall assessment of the audited activity

1. The Supreme Chamber of Control positively assesses the performance of tasks with regard to management of the Investment Grant Fund (FDI) by Regional Financing Authorities (RIFs), although not all resources from the budget have been used for the reasons that are beyond control of these institutions. The NIK has detected some irregularities, they do not, however, have impact on the audited activity. These irregularities are of formal nature and they relate to, for example, delays in concluding and settling grant agreements or procedural errors regarding evaluation of application forms.
2. The NIK positively assesses the use of resources obtained from grants by small and medium-sized enterprises. Only some isolated cases of irregularities and minor irregularities have been found regarding errors in development of applications or settlements. The expected objectives of the programme have been obtained, and they are reflected by a growth in employment and in sales of goods and services.

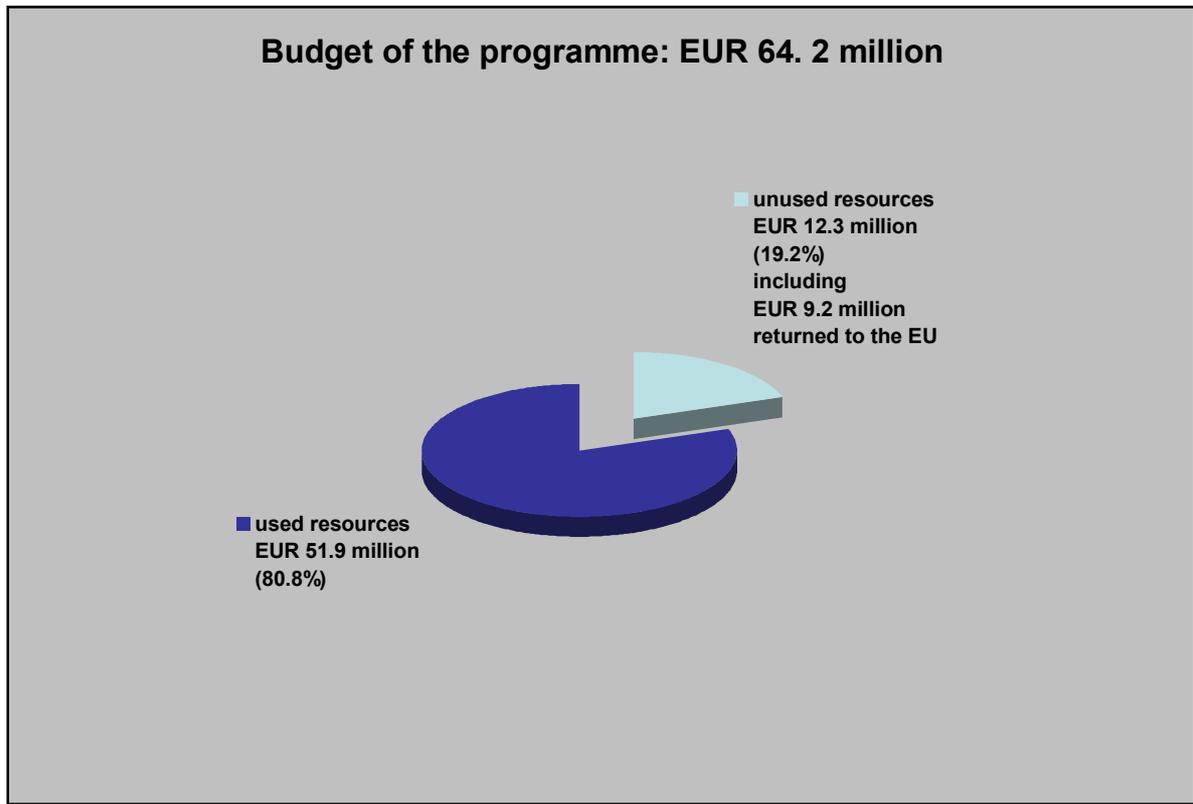
2.2. Synthesis of audit results

2.2.1. Polish Agency for Enterprise Development (PARP)

The Polish Agency for Enterprise Development (PARP) properly performed the tasks of the authority implementing the FDI programme at the national level. Both the resources from the budget of the European Union and the resources for co-financing of the programme from the state budget were transferred to Regional Financing Authorities (RIF). The PARP developed reliable reports on the programme implementation and submitted them to the PHARE Programme Authorizing Officer (PAO) at the Ministry of Economy and Labour (MGIŁ) and made required financial settlements.

However, the implementation of the FDI programme ended with a failure to use EUR 12.3 million, i.e. 19.2% of the national limit of the FDI budget (EUR 64.2 million).

Unused resources of the Investment Grant Fund (FDI)



The main reasons for not using the limit of the resources include lower than forecast eligible costs of the investments found during final settlements with beneficiaries and termination of agreements that were not implemented. Although the agreements concluded used up almost 100% of the programme budget (EUR 64.12 million), some beneficiaries resigned from implementation of agreements. It mainly resulted from the launch of the FDI programme within PHARE 2002, which provided grants for up to 50% of the value of investments, whereas the FDI 2001 envisaged co-financing up to 25%. Unused resources were freed after the deadline for concluding contracts (30 April 2004)¹, and therefore they could not be contracted anew. Unused resources from the single-purpose provision of the state budget were returned and resources from the European Union in the amount of EUR 9.2 million (75% of unused FDI finances), despite actions taken, were lost, i.e. returned to the account of the European Commission (for the details see: Pronouncement, page 26-27).

¹ For the PARP, the deadline for contracting was 15 February 2004, i.e. on the day when last agreements with the RIFs were concluded. After this date, the amounts designated for assistance to SMEs could not be changed.

2.2.2. Regional Financing Authorities (RIFs)

1. The audited RIFs appropriately performed their tasks regarding publication of information about opportunities to obtain assistance measures by entrepreneurs within the programme on the Internet. It has been found, however, that applicants did not always take advantage of the assistance of the RIFs during development of grant applications, which, according to the NIK, could be a reason for rejecting applications at the stage of administrative evaluation by Evaluation Commissions². The average rate of applications rejected at the stage of administrative check and eligibility criteria, i.e. for formal reasons³, in relation to all rejected applications stood at 94% in the audited RIFs (for details see: Pronouncement, page 30-31).

2. The Supreme Chamber of Control positively assesses the activities of the audited RIFs regarding the procedures for reception and evaluation of grant applications. In the audited entities, the Evaluation Commissions were appointed in an appropriate manner. However, in as many as three audited RIFs (out of five) the same persons accepted and evaluated applications and simultaneously were responsible for control, settlement and payment of grants, which violated the requirement of division of responsibilities with regard to contracting and implementing that had been set out in the agreements concluded with the Polish Agency for Enterprise Development (description: Pronouncement, page 28).

“Guidelines for Applicants for Investment Grants”⁴ (hereinafter referred to as “the Guidelines for Applicants”) lay down a 15-day period, counted from the date of the submission of the application, for evaluating and sending a list of recommended applications to the PARP, which, however, was frequently not complied with, especially with regard to the first period, i.e. 28 July 2003⁵. Delays, from a few to 46

² The verification of grant applications covered three stages: administrative compliance regarding formal requirements of applications and eligibility criteria of the enterprise and the applicant, followed by technical and financial evaluation of applications. The employees of RIFs could not make evaluations of the correctness of the development of applications as applications were submitted in sealed envelopes, and they were evaluated at the Opening Session by the Evaluation Commission.

³ The most frequent reasons for rejection of applications include: lack of signature on the copy of the document, bank code given in writing, lack of required annexes, lack of initials on all pages of the application, etc.

⁴ “The Guidelines for Applicants” were approved by the European Commission Representation on 19 May 2003 and published on the PARP website on 27 May 2003.

⁵ The dates set out on the basis of “Financial Memorandum of the Polish National Programme 2001 PL0008”, signed on 20 December 2001 between the Government of the Republic of Poland and the European Commission

days (description: Pronouncement, page 27), have been found in all audited RIFs. The RIFs explained that the delays had resulted from the large numbers of applications and a short period between the first and the second date for their submission (28 July and 18 August 2003).

Evaluation Commissions made evaluations of applications on the basis of the regulations determined by the PARP in “the Guidelines for Applicants” and the agreements concluded between the PARP and the RIFs. It has been established, however, that the RIFs did not apply strict evaluation criteria, which resulted in rejection of some applications for formal reasons (e.g. lack of stamps). Alternatively, beneficiaries had to provide additional explanations. The applied procedures did not allow the RIFs to fill in incomplete applications and made them reject all applications that did not fulfil administrative and eligibility criteria⁶. Verification of some applications through additional explanations by beneficiaries has been assessed by the NIK as an irregularity that may create corruption prone mechanisms because of unequal treatment of applicants, which was proved by the number of applications rejected at the stage of formal evaluation – 90% of all rejected applications (Pronouncement, page 30). It has been established that Evaluation Commissions appealed for such explanations and the percentage of explanations provided stood at 5%.

3. There have been few errors detected in the evaluation of applications. In one RIF (Warsaw), the Evaluation Commission accepted applications submitted by beneficiaries with regard to whom it was impossible to state, on the basis of applications and statements attached to them, whether they were small or medium-sized enterprises⁷, although the valid register document of the applicant showed that over 25% of the shares were owned by another enterprise (description: Pronouncement, page 28). The fulfilment of this criterion was verified only through a statement of the applicant and the valid register document of the applicant (issued not

are the following: in 2003 – 28 July, 18 August, 13 October, 15 December, and in 2004 – 16 February and 15 March (originally 19 April).

⁶ A possibility to fill in incomplete applications was introduced during the implementation of the FDI PHARE 2002 programme. Changes in the procedures of the FDI programme introduced in the PHARE SSG 2002 and 2003 are presented in Annex 2 to the Pronouncement.

⁷ It refers to 3 applicants, i.e. 10% of the audited sample of 30 applications. The criteria of a small and medium-sized enterprise have been set out in Article 54 and 55 of the Act of 19 November 1999 – Economic Activity Law (Journal of Laws No 101, item 1178 with amendments).

earlier than 6 months before submitting the grant application)⁸. The RIFs explained this irregularity indicating inability to verify the submitted statements. The NIK has established, however, that the Commission appealed to some applicants for providing additional explanations regarding shareholders.

It has been also found that in one RIF (Warsaw) the Evaluation Commission accepted 4 application forms (13.3% of the audited sample) of entrepreneurs whose financial position was weak, which was incompliant with the requirements set out in “the Guidelines for Applicants”. The Commission awarded them with such a number of points that included them into the list of applications recommended for grants, whereas their applications should have been rejected at the stage of administrative evaluation (description: Pronouncement, page 29).

In two RIFs, the Evaluation Commissions accepted applications although they contained errors and irregularities in their contents or in attached documents – 10% of the audited sample (description: Pronouncement, page 29-30).

4. The NIK has not detected significant irregularities with regard to signing agreements with beneficiaries by the RIFs, with regard to down payments and final settlements of grants.

However, the NIK has assessed as an irregularity the failure to keep by the PARP the deadline to sign agreements within 41 days from the day of the submission of applications. This deadline proved unfeasible in the light of the possibility, adopted by the PARP, to wait for free resources from other programmes or from unused resources. Delays in signing agreements, from a few to a few hundred days, occurred in all audited RIFs (description: Pronouncement, page 36). Prolonged periods for signing agreements constituted serious reasons for resigning from these agreements by some applicants (three cases in the Wrocław Regional Development Agency S.A.).

Moreover, it has been found that in all audited contracting entities there were delays regarding final payments lasting from a few to 150 days, although payments should have been made within 60 days after submission of applications. Beneficiaries did not appeal for interests (for details see: Pronouncement, page 34).

The agreements between the PARP and the RIFs set out a 5% minimum ratio for direct monitoring and a 10% ratio for telephone and mail contacts regarding

⁸ In the PHARE SSG 2002 and 2003, it is required to submit additional statement on fulfilling the criteria of SME before signing grant agreements (see Annex 2 to the Pronouncement).

implemented agreements, the compliance with which, however, varied from 44 documented monitoring activities, including 20 visits and 24 telephone conversations (27%) by the Foundation of Small and Medium-Sized Enterprises in Warsaw to 167 monitoring visits (96.5% per 173 agreements concluded) by the Regional Development Agency S.A. in Konin (description: Pronouncement, page 34). It should be noted that the method for monitoring based on telephone conversations has been assessed by the NIK as a method which does not provide for appropriate supervision of implementation of agreements by beneficiaries⁹.

5. The failure to use the limit of the FDI budget referred to all audited RIFs. The ratio of unused resources stood at the level from 10.8% of the programme budget (EUR 4,121,514) in the Toruń Regional Development Agency S.A., i.e. EUR 444,978, to 25.2% of the programme budget (EUR 2,810,663) in the Zachodniopomorska Regional Development Agency S.A. in Szczecin, i.e. EUR 707,528 (description: Pronouncement, page 32-33).

Although the RIFs did not use all resources, many entrepreneurs were not recommended for grants in the last period (15 March 2004), even though they submitted applications correctly and in due time, or they were qualified for assistance, yet agreements with them were not concluded because of lack of finances. The number of recommended applications varied from 12 in the Zachodniopomorska Regional Development Agency S.A. in Szczecin to 58 in the Foundation of Small and Medium-Sized Enterprises in Warsaw (description: Pronouncement, page 33). In the opinion of the NIK, one of the reasons for freeing resources after the deadline set for completion of contracting was a long period between the date of concluding agreements and their final settlement, which lasted up to over ten months. The activities of the RIFs that led to prolongation of the period for agreement settlement or that allowed beneficiaries to submit corrected final settlements for many times, in spite of being compliant with the procedure set out by the PARP, resulted in delayed creation of “savings” that therefore could not be used.

The NIK has positively assessed the execution of returns of resources under terminated or inappropriately implemented agreements by the RIFs. Only in four cases

⁹ In the PHARE SSG 2002 FDI programme, the limit of obligatory monitoring activities has been increased to 15% of the agreements settled over the year, including at least 5% monitoring visits (see Annex 2 to the Pronouncement).

irregularities have been detected with regard to recovery of these receivables (description: Pronouncement, page 36-37).

6. Correctness of developed reports and settlements between the RIFs and the PARP have been assessed positively. The irregularities disclosed referred only to short delays in submission of reports and delays in return of resources or payments of interests in the accounts of the RIFs (two cases – description: Pronouncement, page 37). The audited RIFs generally properly managed the resources from the state budget transferred by the PARP on the basis of the annual agreement on grants designated for covering the RIF's operating expenses such as, e.g., promotion, counselling, control and administrative services, and the irregularities detected were rare (details: Pronouncement, page 38-39).

2.2.3. Beneficiaries of the FDI programme – small and medium-sized enterprises

1. In 22 out of 29 audited small and medium-sized entrepreneurs¹⁰ no irregularities have been found. The irregularities detected in the seven remaining beneficiaries were related to:
 - A failure to inform the public opinion about the financial contribution of the European Community to the investments co-financed from the PHARE resources, which is incompliant with Article 6 of “General terms and conditions” which constitute annex to the grant agreement. These irregularities have been found in 6 enterprises (information about assistance obtained was absent from the enterprise's website – 5 cases; information on the assistance obtained was absent from the enterprise's internal documentation – 1 case) (description: Pronouncement, page 40);
 - A failure to use some of the equipment purchased with the use of money from the grant (description: Pronouncement, page 40);
 - Using some of the equipment outside the region, which is incompliant with the rules of “the Guidelines for Applicants” (description: Pronouncement, page 40);
 - Violation of Article 28, paragraph 1 of the Act of 29 September 1994 on accounting¹¹ regarding remission write-offs of the value of equipment which was

¹⁰ The audit covered 29 beneficiaries who had received assistance measures in the framework of the FDI in the amount from EUR 40,000 to EUR 50,000, that is the maximum amount available (non-statistical sampling).

¹¹ Journal of Laws of 2002 No 76, item 694 with amendments.

recorded in the books as tangible assets under construction (description: Pronouncement, page 41);

- Submission of an incorrect statement on lack of liabilities under taxes and payments to the Social Insurance Institution (ZUS) (description: Pronouncement, page 31);
 - A failure to meet the obligation stemming from Article 4, paragraph 3 of the grant agreement regarding a bank account in zloty, which required the beneficiary to return the down payment and, consequently, resulted in a loss of the grant in the amount of PLN 2,809 (as a result of exchange rate differences during the second payment) (description: Pronouncement, page 41).
2. Furthermore, in four cases beneficiaries stated that they had compared three offers¹², although the comparisons clearly indicated that the selection of the supplier had been in fact made without any comparisons. In reports to the RIFs, offers from various periods of the investment realization were presented or offers other than those collected for comparison. Since neither the PARP nor the RIFs established a methodology for comparing offers by beneficiaries¹³, the NIK has not found irregularities in such cases, although it has voiced some objections with regard to the ways of using public resources by beneficiaries (description: Pronouncement, page 41-42).
3. The majority of the audited small and medium-sized enterprises achieved the effects of the programme contained in agreements. It has been established that the investments were realized in accordance with agreements and they mostly resulted in a growth of turnover and the expected growth of employment. In 28 out of 29 audited enterprises, a growth in income from sales of goods or services has been observed. In 25 enterprises a growth in employment occurred. Only in one enterprise a reduction in

¹² “Guidelines for Applicants”, item 2.2.1. and the annex to the grant agreement (sample report) obliged beneficiaries to present to the RIFs a comparison of at least three offers from potential suppliers or contractors together with a justification of their choice provided that the amount of the grant exceeded EUR 5,000. Such a comparison, together with a justification, should be attached to the Technical Report on the implementation of the project, which is submitted with the payment application. This requirement resulted directly from the provisions of “Practical manual for procedures of concluding agreements within PHARE, ISPA and SAPARD” published in November 2000.

¹³ The issue has been regulated, as in the PHARE SSG 2002 FDI a rule has been introduced providing that all offers must be valid as at the date of the comparison and they must contain a description of the item, its price and the period of the offer validity (see Annex 2 to the Pronouncement).

employment has been found although it was assumed otherwise in the grant agreement.

4. The findings of the audit show that in all audited enterprises the final share of the grant in zloty was lower, which should be attributed to exchange rate differences that took place in the period between the date on which the agreement was concluded and the date of the settlement of the investment, although the amount calculated in euro was compliant with the agreement. It resulted in a lower share of the grant in the value of the realized investments (see: Pronouncement, page 35-36).

2.2.4. Identification of barriers in the access of small and medium-sized enterprises to assistance within the FDI PHARE 2001 SSG programme

During the audit, an anonymous questionnaire was conducted among the employees of the RIFs dealing with servicing the FDI programme containing the following questions: What kind of problems regarding the implemented programme were identified during its implementation?; What is your opinion on the cooperation between the RIFs and the Implementing Authorities, i.e. the PARP and the PAO (Ministry of the Economy and Labour)?; Is there a need to introduce changes in the system for the FDI implementation from the perspective of the implementation of the next edition of assistance programmes in the SME sector?

The audited small and medium-sized entrepreneurs (29) were asked an open question regarding their opinion on the cooperation with the Implementing Authorities (the RIFs and the PARP), problems in the implementation of the programme and potential aspects that should be improved in the programme implementation process.

The results of the questionnaire conducted among the employees of the RIFs show that in all audited entities the main problems covered: too large number of applications, too formalized and unclear procedures resulting in rejections of a significant number of applications at the stage of formal evaluation, too short periods for evaluation (15 days) and for submitting loan agreements (30 days), numerous annexes to agreements that prolonged the period of their implementation (details: Pronouncement, page 38).

In their questionnaire, entrepreneurs indicated too formalized and unclear procedures and the long period for waiting for evaluation of applications and signing agreements as the main

problems (details: Pronouncement, page 39). Entrepreneurs appealed for simplification and clarification of procedures related to submission of applications and settlements.

2.3. Financial results of the audit

The results of the audit allowed for establishing financial irregularities in the amount of PLN 1,159,284, including:

- Amounts spent in a breach of “the Guidelines for Applicants” and the terms and conditions of the agreements:
 - a) PLN 77,046 – Evaluation Commission of the Wrocław Regional Development Agency S.A. recommended the applications of three entrepreneurs although they were incomplete and should have been rejected at the stage of administrative evaluation (details: Pronouncement, page 29),
 - b) PLN 528,720 – Evaluation Commission of the Foundation of Small and Medium-Sized Enterprises in Warsaw accepted the applications of four entrepreneurs whose financial position was very weak, which was incompliant with the requirements of “the Guidelines for Applicants” (details: Pronouncement, page 29),
 - c) PLN 153,954 – the value of the equipment purchased by MOTO BUDREX Sp. z o.o., a company from Bydgoszcz, that was used outside the region in which the company had obtained the grant, which was incompliant with the rules contained in “the Guidelines for Applicants” and the terms and conditions of the agreement (details: Pronouncement, page 40-41);
- Amounts spent uneconomically:
 - a) PLN 8,550 – MOTO BUDREX Sp. z o.o., a company from Bydgoszcz, did not use the acquired equipment before the audit (details: Pronouncement, page 40);
- Unreliable data in financial and accounting records or in reports:
 - a) PLN 3,700 – including PLN 3,200 of inflated operating expenses of the Wrocław Regional Development Agency S.A. because of unreliable data included in the reports for the PARP, and PLN 500 of understated operating expenses because of an error in the number of grants paid included in the report for the PARP (details: Pronouncement, page 38-39),
 - b) PLN 39,983 – MOTO BUDREX Sp. z o.o., a company from Bydgoszcz, remitted the value of tangible assets under construction which was incompliant

with Article 28, paragraph 1 of the Act of 29 September 1994 on accounting¹⁴ (details: Pronouncement, page 41);

- Other financial irregularities:
 - a) PLN 210,936 – value of final payments made by the Wrocław Regional Development Agency S.A. 60 days after the date for submission of correct applications, which was non-compliant with the terms and conditions of the agreements (details: Pronouncement, page 34),
 - b) PLN 3,934 – amount of interest rates in the account of the Wrocław Regional Development Agency S.A. returned to the PARP on 13 December 2004 instead of on 15 January 2004 (details: Pronouncement, page 37),
 - c) PLN 2,809 – amount resulting from a failure to comply by POL AQUA S.A., a company from Piaseczno, with the obligation referred to in Article 4, paragraph 3 of the grant agreement on running a bank account in zloty (details: Pronouncement, page 41),
 - d) PLN 1,962 PLN – amount of expenditures on food for the employees of the RIF in Warsaw which was by mistake included into operating expenses directly related to the programme servicing (details: Pronouncement, page 38-39);
- Saved financial benefits:
 - a) PLN 106,435 – value of the agreement terminated by the Regional Development Agency S.A. in Konin after it was established that the beneficiary had obtained a grant before. The down payment in the amount of EUR 24,686 was not returned as the beneficiary appealed to court.
 - b) PLN 21,255 – value of machines and equipment purchased by MOTO BUDREX Sp. z o.o., a company from Bydgoszcz, which were stored outside the Kujawsko-Pomorskie Voivodship (Region) before the end of the audit and which are to be moved to the area of the region to which the grant applied (details: Pronouncement, page 40-41).

2.4. Final remarks and conclusions

The results of the audit show that there is a necessity to take actions aimed at full utilization of the resources designated for small and medium-sized enterprises as public aid aimed to

¹⁴ Journal of Laws of 2002, No 76, item 694 with amendments.

adjust the level of Poland's economy to this of the other states of the European Union. In the opinion of the NIK, the Minister of Economy and the PARP should strive after introduction of systemic solutions with regard to developing methods for minimizing amounts unused due to limitations of deadlines, which make it impossible to use resources from savings at the stage of settlements and from terminated agreements.

This objective should be achieved through minimizing procedural barriers that limit access of entrepreneurs to this type of public aid and that hamper settlements of used resources. Changes to the procedures for the implementation of the Investment Grant Fund (FDI) introduced in PHARE 2002 and PHARE 2003 have commenced the process that should bring the desired effects¹⁵. The reasons for unfavourable phenomena that were identified during the implementation of the FDI 2002 programme should be eliminated in the framework of the programmes financed from EU resources directed to entrepreneurs that are being implemented now.

¹⁵ The list of changes in the procedures of the PHARE SSG FDI programme in its next editions are presented in Annex 2 to the Pronouncement.