

# Legal and financial aspects of accounting for grants provided to NGOs by local government units in the light of the requirements laid down in the EU directives

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## **Abstract:**

**Aim:** The cooperation between non-governmental organizations and public administrative bodies exemplifies the implementation of the principle of subsidiarity, according to which their actions should be limited to the minimum necessary. In accordance with the competition principle applicable in the EU Member States, every activity on the part of public authority in relation to selected undertakings is an unlawful public aid which distorts free competition. The cooperation of local government units with NGOs is an element of implementing their own tasks. When outsourcing the implementation of tasks to non-profit organizations, domestic legal regulations make it possible to circumvent public procurement law. The aim of the paper is to assess whether local government units in outsourcing some of their own tasks to NGOs may in fact be violating the basic principles of the European Union, and whether or not in their accounting for the implementation of tasks local governments observe the principle of sound financial management, in other words, whether it is in compliance with the principles of economy, efficiency and effectiveness in terms of spending public resources.

**Research methodology:** Realizing the aim set, an overview of European and domestic legal acts was carried out, as well as the analysis of reports on public task performance by non-profit organizations with the reports providing the basis for accounting for earmarked grants in two local government units. The analysis of the data contained in the reports was conducted using comparative and indicator-based method.

**Findings:** The analysis of legal determinants shows that it cannot be ruled out that local governments may violate the principle of the free market competition by providing public benefit organizations with earmarked grants. Examining the financial aspect of accounting for grants provided to NGOs, the conclusion to be made is that the practical implementation of the principle of purpose and economy in spending grant resources is not entirely observed. The relationship between the best effect and the costs incurred is not analyzed.

**Originality of the paper:** Highlighting the self-understood in the EU law principles of public spending, reiterated in the Polish legislation, but not sufficiently discussed nor emphasized in Polish literature, including the principles within the scope of grants provided to NGOs.

**Research implications:** The results of the study may find their application in good practices of accounting for earmarked public grants provided to NGOs.

*Key words:* non-governmental organizations, EU directives, local government units.

JEL: L31, H7

## 1. Introduction

The cooperation between non-governmental organizations and public administrative bodies exemplifies the implementation of the principle of subsidiarity, according to which public administrative bodies are expected to take actions only in such areas in which private and non-state individuals and lower authorities cannot achieve the objective of such actions effectively. Actions of public administrative bodies shall be limited to the minimum necessary. In accordance with the competition principle applicable in the EU Member States, every activity on the part of public authority in relation to selected undertakings is an unlawful public aid which distorts free competition. With respect to local government units, cooperation with non-governmental organizations is an element serving the implementation of the units' own tasks (Article 7(1) point 19 of the Act of 8 March 1990, and Article 4(1) point 22 of the Act of 5 June 1998).

The general framework of the cooperation between local government units and non-profit organizations is governed by the Act of 24 April 2003 on Public Benefit and Volunteer Work, (UDPP), as well as by implementing acts of this act<sup>1</sup>. When outsourcing the implementation of tasks to non-profit organizations, the regulation cited makes it possible to circumvent public procurement law. Beneficiaries of grants provided for the implementation of tasks may encompass the following organizations: non-governmental organizations and other entities listed in Article 3(3) of UDPP. Local government units outsource their tasks predominantly to sport clubs and associations. The scope of work which may be outsourced to non-profit organizations is laid down in Article 7 of UDPP. Local government units most frequently outsource their tasks within the following areas:

- social aid,
- maintaining and promoting national tradition, cultivating Polishness and developing national, civil and cultural awareness,

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<sup>1</sup> During the period spanning the study that was the Ordinance of the Minister of Labor and Social Policy of 15 December 2010 on the model form of tender and framework agreement as regards the implementation of a public task, and the model form of the report on the completed task.

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- activity supporting the development of local communities,
- education and upbringing,
- culture, art, protection of cultural goods and national heritage,
- supporting and promoting physical culture.

Outsourcing public tasks may be in the following forms:

- entrusting the performance of public tasks, plus providing grants for financing the tasks,
- supporting the performance of public tasks, plus providing grants for financing the tasks.

Non-profit organizations carry out tasks that are contracted out to them on the basis of an agreement for supporting the public task implementation (Article 16 of UDPP), which specifies the scope of the public task and the terms and conditions of its performance. The responsibility of the public authority outsourcing a particular task involves handing over the grant for the task execution, as well as monitoring and assessing projects that are being carried out. The agreement must be concluded in writing and for a term that does not exceed five years. The agreements that local government units mainly conclude are those which span several months and do not go beyond the current fiscal year. Contractors for public tasks are required to identify the funds received for the agreement implementation in their accounting records. According to Article 17 of UDPP, a public body which contracts out public tasks may, but does not have to, control and evaluate the task implementation, in particular:

- “the degree of completion of the task;
- effectiveness, reliability and quality of the task;
- regularity of the use of public resources received for the task performance;
- keeping records relating to the task performed”.

The contractors are required to draft a report on the execution of the task and the use of the grant received, and to submit the report to public administration bodies.

The aim of the paper is to assess whether local government units in outsourcing some of their own tasks to NGOs may in fact be violating the basic principles of the European Union, and whether or not in their accounting for the implementation of tasks local governments observe the principle of sound financial management, in other words, whether it is in compliance with the principles of economy, efficiency and effectiveness in terms of spending appropriations (Article 30 of Regulation (EU, EURATOM) No 966/2012 of 25 October 2012).

For the purpose of this paper, non-profit organizations' reports on their performance of public tasks for two local government units were investigated. The present study covered those organizations which received the largest grants for the longest timeframe, and which implemented the greatest number of tasks over the years 2014-2015.

## **2. The principles of public aid according to the EU regulation**

Pursuant to Article 107(1) of the Treaty on the Functioning of the European Union (TFEU), we deal with a public aid (whatever its form, e.g. a loan on preferential terms, surety that is not on purely market terms, partial tax write-off, or providing a grant) if such aid falls within the following scope:

- it pertains to an undertaking, or rather an entrepreneur, within the meaning of EU competition law,
- it comes from state resources,
- it is granted on terms that are more favorable than market terms,
- its character is selective,
- there is risk that the aid may distort or distorts competition and affects trade between the Member States

One should bear in mind that the Union legislation defines certain terms differently than the Polish legislation, for instance, the terms which are crucial for the study presented herein, and it interprets differently some provisions, namely<sup>2</sup>:

- entrepreneur (in Polish legislation, an undertaking) is every entity involved in economic activity irrespective of its legal form, sources of its financing and economic objectives (it need not be profit-oriented), and as such it may be an association or a budget unit;
- economic activity consists in offering goods and services on the market regardless of whether its nature is that of profit-making, nor does it have to be conducted in a way that is organized, continuous and for hire or reward. Some small NGOs established in order to satisfy occasional needs of small town and rural population operate from one project to another, with the project

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<sup>2</sup> Article 49 of TFEU states that freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings. The concept of "undertaking" was defined more precisely in part VI. 1.1 of the Decision of Commission of 2 March 2005. On the issue of the aid scheme implemented by Italy aimed at restructuring institutions engaged in occupations education, Official Journal of 8 March 2006, No. L 81/25.

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being organized once a year. In light of the provisions of Article 2 of the Act of 2 July 2004 they do not conduct an economic activity; however, in light of the EU legislation they do so. The same applies to sport associations and clubs which provide free of charge services;

- undertakings may conduct simultaneously both a commercial and non-commercial activity. The rules on the internal market, competition and, in particular, on state aid do not apply to the latter type. In Poland such diverse services may be rendered, for instance, by public benefit entities (Article 9(1) of UDPP<sup>3</sup>);
- an economic activity consisting in providing services, is, pursuant to Article 57 of TFEU, normally conducted for remuneration; however, it follows from the Commission Decision of 2 March 2005 on the aid scheme implemented in Italy for the reform of the training institutions that this is not a necessary requirement. The Commission stated that activities performed normally with the intention to fulfill social functions in an institution which is non-profit-oriented, being engaged neither in production nor in trade, were excluded from the application of the EU rules on competition and the internal market. However, it cannot be ruled out that an activity, which is on the whole oriented toward achieving social aims, may not gain profit in the form of other benefits in the sector. Thus, non-profit entities can successfully compete against companies which are profit oriented and as such may become undertakings within the meaning of Article 107 of TFEU. Another observation made by the Commission suggests that considering a natural evolution of economic activity, it is possible to transfer to undertakings certain tasks traditionally regarded as falling within the sovereign powers of States, which implies that non-profit entities involved in the sector of social economics and benefiting from state aid will increasingly more frequently run counter to the principle of free market;
- public funding can be direct, e.g. it comes from resources of a local government unit, but also indirect, e.g. in the situation where aid is given to a cultural event organized by a local association, or a match is played by a local sport club, if in the latter case tickets are sold at prices that are lower than those at non-funded events;

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<sup>3</sup> Article 9 of the Act states, however, that one may not combine economic activity with public benefit activity for hire or reward within the same area of the entity's activity.

- for an entrepreneur, any reduction of his burdens, for instance, through funding some costs or exempting them from e.g. taxes or local fee constitutes a benefit,
- selective funding means providing aid to a selected group of entrepreneurs or a selected group of goods, e.g. for a public-benefit organization;
- examining the impact of the provision of services and goods on the EU internal market is problematic in that the European Commission quite frequently states its opinion on this issue with the Commission's decisions being not that clear. In the Notice from the Commission on a simplified procedure for the treatment of certain types of State aid, the Commission concluded that in order for the measure at stake to be considered as not having any effect on intra-community trade, the following features are required to be demonstrated:
  - 1) that the aid does not lead to investments being attracted in the region concerned,
  - 2) that the goods/services produced by the beneficiary are purely local and/or have a limited attraction zone,
  - 3) that there is no more than a marginal effect on consumers from neighboring Member States,
  - 4) that the market share of the beneficiary is minimal.

According to the criteria mentioned, most services provided by public benefit organizations will rather not affect the intra-community market, although in the fast-developing regions where non-profit organizations are also very active such impact will be difficult to rule out;

- a public undertaking, according to Article 106 (2) of TFEU, entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules on competition. The concept of public undertaking was further defined in Article 2 of the Commission Directive on the transparency of financial relations between public undertakings as well as on financial transparency within certain undertakings, which states that an inherent feature of the public undertaking is a dominant influence on the part of the public authorities (direct or indirect), including local governments by virtue of holding the major part of the undertaking's subscribed capital or of controlling the majority of the votes attaching to shares issued by the undertakings and of being in the capacity of appointing more than half of the members of the undertaking's administrative, managerial or supervisory body. Such municipal companies, for instance, are public undertakings, of which some, e.g. those involved in supplying water to a local community, carry out their activity under

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the conditions of a natural monopoly. In Polish environment, public tasks are performed by central and local government administration (voivodship, poviast and commune), as well as entities which are granted special or exclusive rights by the government, e.g. energy sector, postal services, but also activities performed by public benefit organizations;

- public benefit services are not defined unambiguously in Union law. Their definition was derived from relating them to the services of general economic interest, and they, pursuant to Article 14 of TFEU, are the services which are of special importance for the shared values of the EU, and which support social and economic cohesion of the Union. The Community and Member States ensure the provision of these services although the market may not have sufficient incentives to provide such services. They allow social needs to be met, with their provision being in the general interest of the society, and thus the basis for their distinction is their public utility. The so called network services, e.g. energy, transport sector, are in the first place classified as this type of services;
- the following (Article 106(2) of TFEU) has been considered, among other things, to be in line with the internal market rule: social aid for individual consumers, aid to repair the damage caused by natural disasters or exceptional occurrences. In paragraph 3 of this article, it is stated that what may be considered to be compatible with the internal market, and as such also with the rule on competition, is aid aimed at promoting the economic development of regions, some economic activities, support for projects important for the European Community and aid to promote culture and heritage conservation. In the Commission Regulation, which considers some forms of aid to be compatible with the internal market, under Articles 107 and 108 of TFEU new categories of aid covered by the block exemption have been indicated, namely: social aid for transport for the population from the outermost regions, aid for broadband network, innovations, sport infrastructure and multifunctional recreational infrastructure, as well as local infrastructure. The block exemption provides assurance that public funding of at least one area listed in the Act on Public Benefit and Voluntary Work (Article 4(1) point 16 of UDPP) – culture, art, protection of cultural goods and heritage – does not violate the Community rules on the free market;
- The Court of Justice has held that grants for public benefit services will not confer an economic advantage on the entity, and thus they will not constitute public aid within the meaning of Article 106 of TFEU if they meet the following four criteria cumulatively:

- a) The beneficiary must actually have public service obligations to discharge and the obligations must be clearly defined,
- b) The parameters which provide the basis for calculating the remuneration for services rendered (the grant) should be defined in advance in an objective and transparent way so as to avoid the situation in which an undertaking which receives aid is granted the advantage of being favored in comparison to entrepreneurs who do not receive such aid,
- c) The grant that is received in relation to public services rendered should not exceed what is necessary to cover all or some costs incurred in discharging the public service obligation, taking into account the relevant receipts and reasonable profit the undertaking may be expecting for providing the service,
- d) In the case “the undertaking which is to discharge public service obligations is not chosen pursuant to a public procurement procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs which a typical undertaking, well run and adequately provided with means of transport so as to be able to meet the necessary public service requirements, would have incurred in discharging those obligations, taking into account the relevant receipts and a reasonable profit for discharging the obligations” (Judgment of the ECJ of 24 July 2003). It was thus emphasized that the basis for making the decision on entrusting an undertaking with the provision of public benefit service should be an adequate economic analysis.

Considering the above, it may not be ruled out that in entrusting public tasks or in aiding the performance of those tasks by providing public benefit organizations with a public grant local governments violate one of the fundamentals of the European Union, which is the competition on the common market. Entrusting outside undertakings with local governments’ tasks may lead to favoring unfairly undertakings which implement those tasks over other undertakings running an economic activity.

### **3. Relevant EU Directives in terms of accounting for grants provided to public benefit organizations**

Public finance units, to which local government units clearly belong, are obligated to observe mainly two Directives of the European Parliament and Council, and these are as follows:

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- a) Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States;
- b) Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC.

The former is a set of rules, procedures and institutions that constitute the basis for general government to conduct budgetary policies, in particular it defines the following:

- “systems of budgetary accounting and statistical reporting;
- rules and procedures governing the preparations of forecasts for budgetary planning;
- country-specific numerical fiscal rules, which contribute to the consistency of Member States’ conduct of fiscal policy with their respective obligations under the TFEU expressed in terms of a summary indicator of budgetary performance, such as the government budget deficit, borrowing, debt, or a major component thereof;
- budgetary procedures comprising procedural rules to underpin the budget process at all stages;
- medium-term budgetary frameworks as a specific set of national budgetary procedures that extend the horizon for fiscal policy-making beyond the annual budgetary calendar, including the setting of policy priorities and of medium-term budgetary objectives;
- arrangements for independent monitoring and analysis, to enhance the transparency of elements of the budget process;
- mechanisms and rules that regulate fiscal relationships between public authorities across sub-sectors of general government”<sup>4</sup>.

The Directive on the budgetary framework is one of the six legal acts adopted by the EU to strengthen the implementation of the main principle governing the Member States’ economic policy, which is defined synthetically as avoiding excessive deficit and is enshrined in Article 126 of TFEU. In implementing the provisions of the legal acts for the stabilization of public finances,

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<sup>4</sup> <http://orka2.sejm.gov.pl/BASleksykon.nsf/dokument.xsp?id=7C99CAE5BD46235EC1257A7100329AB3> [17.06.2018].

in 2009 Poland, for instance, amended the Act of 27 August of 2009 on Public Finances. Instruments for multiannual financing plan were implemented (Multiannual Financial Plan of the State – WFPF, Multiannual Financial Forecast – WPF). Moreover, the variation of the organizational and legal forms of the units of the public finance sector was reduced, the duties of internal audit were strengthened and management control was implemented. In addition, activity-based budget was established in government units. Prudential standards were strengthened in the state budget and in the budgets of local governments. The rules were changed on the management of non-recoverable European funds and other funds from foreign sources. Those changes were aimed at increasing the effectiveness in public spending. Articles 221 and 252 of the Act on Public Finances apply directly to the object of this study. The articles state that a local government unit may contract out its tasks to a non-governmental organization and provide an earmarked grant for this purpose. The agreement must define the following: a detailed scope and aim of the task as well as a precise timeframe within which it will be carried out, the grant amount, the arrangement for paying the grant and the timeframe for using the grant (not later than by 31 December), the arrangement for controlling the use of the grant, the timeframe and manner of accounting for the grant and the deadline for the return of the unused amount (not later than on the 15<sup>th</sup> day following the day on which the task was completed). In order to allow one to control the use of the grant, beneficiaries must keep a separated accounts for those appropriations. The authorizing officer of public funds is obligated to account for the grant within a physical and financial scope within 30 days following the accounting. If it is ascertained that the grant has been misused (in whole or in part), or it was collected for an excessive amount, the authorizing officer specifies, by way of a decision, the amount to be recovered plus statutory interests. In addition, Article 254 of the Act on Public Finances lays down the rules on financial management, indicating, among other things, that outsourcing tasks by local government units should proceed in a public procurement procedure with the exception when tasks are contracted out to NGOs. With respect to the latter, outsourcing and providing grants proceeds pursuant to the provisions of UDPP.

The aim of the second of the directives mentioned is to reduce the reporting burden of small units and to introduce a new financial statement and payment issued to government administration by undertakings in extractive and forestry sectors. The Directive on annual financial statements, consolidated financial statements and related reports of certain types of undertakings was implemented into the Polish environment by the Act of 23 July 2015 on amendment of the

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Accounting Act and some other acts. The act implemented the EU recommendations, but it did not extend the simplification of financial statements for small and microenterprises to public benefit organizations. Consequently, pursuant to Article 2(5) of Accounting Act of 29 September 1994, these organizations still ought to keep full accounting, balance sheet and profit and loss accounts, as well as provide additional information according to Annex 1 of the Act, which is a synthesized version of the full report. The micro and small undertakings meanwhile may in addition simplify the rules on keeping accounts, e.g. they do not have to value assets and liabilities according to the prudent valuation principle, or to fair value.

#### **4. Interpretation problems regarding the provisions of the Act on Public Benefit and Voluntary Work in terms of accounting for outsourced tasks**

What underpins the performance of tasks entrusted to NGOs, are the already mentioned agreements concluded with those organizations. Legislator included a model form of the framework agreement in Annex No 2 of the Ordinance of the Minister of Labor and Social Policy of 15 December 2010 on the model form of tender and of framework agreement as regards the implementation of a public task, as well as the model form of the report on implementation of this task.

The framework agreement lays down the usual elements, such as the party to the agreement and its subject matter, implementation timeframe, the elements required pursuant to Article 151 of the Act on Public Finances and elements that are specific to the agreement on aid to/entrustment of the implementation of a public task. The provisions which are specific from the point of view of monitoring and final accounting for the task entrusted are presented in Table 1 and they refer to the following obligation on the part of the contractor:

- keeping the total cost of task at the level set out in the tender (the contractor may relocate funds between other sources of financing), with this cost consisting of the following items: funds from sources other than the grant that is to be accounted for, including the beneficiary's own resources, grants received from other public administration bodies, from other entities and payments made by individual recipients of the task and the contractor's personal and in-kind contribution.
- keeping the share of the grant in the total cost of the task at the level declared in the tender, while the outsourcing party may allow for this share to be increased by a portion indicated,

- to bear costs according to the estimate given; possible divergences in terms of specific items of the estimate may not exceed the percentage defined by the party providing the grant.

In the entities under study an earmarked grant was provided only by way of support for carrying out a public task, yet while adopting entirely different model forms of agreements. One local government unit adopted its own model form which met all the requirements provided for in the Act on Public Finances, but the model form did not include one provision resulting from the model form of the framework agreement. The second of the units examined for all practical purposes adopted the model form of the framework agreement (cf. Table 1).

**Table 1. The comparison between the provisions included in the model form of agreements on aid to/entrustment of public task implementation and the solutions adopted by the local government units examined**

| According to Annex No. 2  | Applied in entity No. 1   | Applied in entity No. 2  |
|---|---------------------------|--|
| Section 3 paragraph 6. The amount of appropriations from the sources referred to in paragraph 4 point 1, point 2 letter b and point 2 letter c, may change, provided their total does not change.   | The provision was omitted | The provision included in the model form was adopted   |
| Section 5 paragraph 1 The percentage share of the grant in the total cost of the public task does not exceed<br>.....   | The provision was omitted | The provision included in the model form was adopted   |
| Section 5 paragraph 2. Contractor/contractors is/are required to keep at the same level the percentage share of the grant in the total cost of the public task, referred to in section 3 paragraph 5.   | The provision was omitted | The provision included in the model form was adopted   |
| Section 11 paragraph 4. If a particular financial cost from the grant showed in the report on the implementation of the public task fails to be equal to the cost set forth in the relevant item of the estimate, then it is deemed to be compatible with the estimate if it did not increase by more than .....% | The provision was omitted | The provision included in the model form was adopted, but it was broken down into two paragraphs, and the requirement was written in the present tense (if it does not increase by more than .....%) |
| Section 11 paragraph 5. The obligation referred to in Section 5 paragraph 1 is deemed to be met if the grant percentage share, referred to in Section 5 paragraph 2, in the total cost of the implementation of the public task does not increase by more than .....%.  | The provision was omitted | The provision included in the model form was adopted   |

Source: self-reported data based on the Ordinance of the Minister of Labor and Social Policy of 15 December 2010 on the model form of tender and framework agreement as regards the implementation of a public task, and the model form of the report on the completed task.

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Other sources than the grant for funding the public task were found only in the agreements concluded by one of the local governments investigated. Among those sources, the most frequent ones included the tenderer's own resources and possibly the personal contribution of the organizers of the task. The share of the grant in the total cost of the task ranged between 2.12% and 44.4%. The second local government unit covered by the study employed a model form of the agreement that was not in line with that included in the ordinance, with the grants, virtually in all the agreements, making up 100% of all the costs of the task. The first of the outsourcing party defined the permissible extent to which the grant share could increase in the total cost of task up to 5%, while the volatility in terms of the specific items of the estimate up to 10%.

The analysis of the provisions included in the model form of the framework agreement within the scope of the contractor's obligations allows one to conclude that the provisions specified in it allowing for the costs to diverge as compared to the tender/plan were only apparent. The relevant numerical example confirming this observation is presented in Table 2. The example shows that for the obligations included in section 3 paragraph 6 to be fulfilled – the sum of all the costs must stay the same, the contractor may not use the flexibility that is afforded to the share of the grant in the total cost of the task. With the same amount of the grant and of the total costs, the contractor may possibly relocate the amounts between various sources of funding. As already mentioned, for the local government unit using its own model form of the agreement the only source of financing tasks were virtually exclusively grants. In this case, for the contractor to be able to meet its obligations the post-completion estimate of costs must be the copy of the estimate included in the tender. A similar situation is encountered when it comes to tolerances allowed for the items of the estimate.

**Table 2. Illustrative calculations**

| <b>Components of the total cost of the task</b>       | <b>Tender</b> | <b>Report</b> | <b>Permissible change</b> |
|---|---------------|---------------|---------------------------|
| Grant   | 2000          | 2000          | 2000                      |
| Own resources   | 4750          | 4570          | 4570                      |
| Personal contribution                                 | 250           | 100           | 430                       |
| Total costs of the public task                        | 7000          | 6670          | 7000                      |
|   |               |               |                           |
| The share of the grant in the total costs of the task | 28.57%        | 29.99%        | 28.57%                    |

|                       |        |  |  |
|-----------------------|--------|--|--|
| permissible change 5% | 30.00% |  |  |
|-----------------------|--------|--|--|

Source: self-reported data.

In the light of the above observation, all the tasks contracted out by the local government unit which applied the model form of the agreement were carried out in breach of the contractual provisions despite the fact that the agreement had a framework character and could be adjusted to the specific rules adopted by the local government. This way of proceeding legitimized the commentaries to the Act on Public Benefit and Voluntary Work (cf. e.g. Blicharz 2012) where it was noted that the contradictory provisions set forth in the framework agreement made the strict provision of section 3 paragraph 6a more flexible.

### **5. The most frequent irregularities in accounting for the tasks contracted out to public benefit organizations**

The basis for the physical and financial accounting for the performance of the task entrusted is a report which the contractor is required to submit pursuant to Article 18 of the act. The model form of the report is laid down in the same ordinance in which the model form of the framework agreement is presented (Ordinance of the Minister of Labor and Social Policy of 15 December 2010).

The outsourcing party may require the submission of partial reports and a final report. The deadline for submitting the final report, as set forth in the agreement, is on the 30<sup>th</sup> day following the completion of the public task. The reporting period is the fiscal year. The structure of the report results from the content and order adopted in the tender for the task implementation. Thus, the report should include the following components:

- a) a detailed description of how the task will be carried out and of the objectives and results to be achieved;
- b) a breakdown of the total costs needed for the task implementation (expenditures incurred) and the sources of their funding.

While controlling the implementation of the tasks entrusted, the outsourcing party, apart from verifying the reports submitted by the organization, may examine the contractor's accounting books specific for every grant, other documents and information sets containing task-related data, and he may carry out an on-site verification during the period spanning the task implementation. Moreover, the outsourcing party may require that explanations be made orally or in writing and the

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relevant data be delivered. In the units examined, accounting for the performance of the public task was conducted only on the basis of the report submitted.

For the purpose of this study, the analysis of the reports, accepted by the local government units, as the basis of accounting for the grant provided, was conducted using a questionnaire. The questionnaire encompassed 41 questions broken down into the following four groups: formal evaluation of the report, substantive evaluation, evaluation of the implementation of expenditures and evaluation of additional material. The cumulative results are included in Table 3.

In the reports examined numerous errors were found in all the four areas of evaluation. The error was omitted which consisted in failing to observe the provision on keeping the task total costs at the same level, which is referred to in point 3 of the article,. The unit which used the recommended model form of the agreement made errors which in their number exceeded by 60% those made in the unit employing the agreement that was inconsistent with the model agreement and in which all the contractor's obligations relating to the cost structure were omitted. The simplified and less demanding agreement for aid provided to a public task certainly made the accounting for the grant easier, yet at the same time it limited substantially the extent to which the implementation of expenditures could be controlled. The most numerous errors pertained to the evaluation of the expenditure implementation. The vast majority of the errors included the following: the discrepancy between the amount spent according to the sources of funding and those adopted in the agreement, and an insufficient or incorrect recording of the expenditures incurred. During the implementation of 4,6% of tasks in the unit which defined the permissible divergence of the grant share in the total cost of the task excessive amounts were collected, which should otherwise have been recovered to the outsourcing party. In each unit about 12-13% of accounts examined were not fully documented (not all invoices confirming the expenditures were enclosed, or those enclosed were not correct, e.g. dated before the implementation timeframe, pertaining to different tasks), or the expenditures were confirmed by documents which did not meet the requirements applicable to accounting evidence, e.g. they were not verified by the person responsible for book keeping in the organization, or the amounts included in accounting evidence exceeded substantially the average costs of similar services, e.g. transport. At this point one should note that neither organizers' own contribution nor voluntaries' work (with one exception) were in

any way documented, e.g. by concluding contracts with voluntaries, or making payments for the work performed.

**Table 3. The comparison of errors found in the final report according to the local government units under study**

| No.       | Evaluation elements  | Percentage of negative responses                         |                                     |
|-----------|--|--|-------------------------------------|
|           |  | The unit applying the recommended model of the agreement | The unit applying its own agreement |
| <b>A.</b> | <b>Formal evaluation</b>   | <b>11.9%</b>   | <b>15.2%</b>                        |
| 1.        | Was the report drafted according to the current model form?  | 0.0%   | 0.0%                                |
| 2.        | Was the report signed by authorized persons?   | 13.3%  | 16.7%                               |
| 3.        | Does the report bear the organization's stamp?   | 6.7%   | 8.3%                                |
| 4.        | Is the date of the report submission on the form?  | 6.7%   | 16.7%                               |
| 5.        | Was the report submitted within the set deadline?  | 33.3%  | 0.0%                                |
| 6.        | Does the report contain the correct title of the task?   | 6.7%   | 16.7%                               |
| 7.        | Is the deadline set for the task implementation correctly defined in the report?   | 13.3%  | 25.0%                               |
| 8.        | Is the number of the agreement correctly stated in the report?   | 6.7%   | 0.0%                                |
| 9.        | Does the report contain the correct date on which the agreement was concluded?   | 0.0%   | 0.0%                                |
| 10.       | Is the person contracting out the task correctly stated?   | 13.3%  | 0.0%                                |
| 11.       | Is the contractor correctly stated ?   | 0.0%   | 16.7%                               |
| <b>B.</b> | <b>Substantie evaluation</b>   | <b>26.2%</b>   | <b>30.4%</b>                        |
| 1.        | Is there information on the measurement of the objectives to be achieved? (part I. 1)  | 18.2%  | 20.8%                               |
| 2.        | Were the planned objectives achieved to the extent specified in the tender? (part I. 1)  | 0.0%   | 4.2%                                |
| 3.        | Were the reasons for the deviations from the implementation of the objectives explained ?(part I.1)  | 0.0%   | 4.2%                                |
| 4.        | Was the description of the task implementation that was included consistent with the agreement/annex – updating the schedule and estimates? (part I.1)                                 | 9.1%   | 16.7%                               |
| 5.        | Did the description of the task implementation contain information on the activities performed together with their brief description? (part I.1)                                       | 12.1%  | 0.0%                                |
| 6.        | Did the description of the task include the deadlines for the performance of the activities? (part I.1)  | 6.1%   | 4.2%                                |
| 7.        | Did the description of the task implementation contain information on the entity which performed activities within the scope of the public task that was to be implemented? (part I.2) | 6.1%   | 0.0%                                |
| 8.        | Does the report describe how the manner of funding the investments related to the implementation of the task affected the performance of the task? (part I.3)                          | 24.2%  | 25.0%                               |

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|  |   |               |               |
|--|---|---------------|---------------|
| 9.   | Was the description of the outcomes achieved included? (part I. 4)  | 12.1%         | 12.5%         |
| 10.  | Was the scale of actions performed within the framework of the activity shown in numerical terms? (part I.5)  | 3.0%          | 8.3%          |
| 11.  | Does the scale of activities specified in the report correspond to the assumptions included in the agreement? (part I. 5)   | 9.1%          | 4.2%          |
| <b>C. Evaluation of the expenditure implementation</b>   |   |               |               |
|  |   | <b>51.6%</b>  | <b>49.4%</b>  |
| 1.   | Is the type of costs consistent with the estimate constituting the annex of the agreement? (part II.1)  | 3.1%          | 10.5%         |
| 2.   | Did the total cost change? (part II.1)  | 1.5%          | 0.0%          |
| 3.   | Was the amount of the grant defined in compliance with the agreement?   | 0.0%          | 2.6%          |
| 4.   | Did the organization define its own contribution in compliance with the tender?   | 10.8%         | 7.9%          |
| 5.   | Did the total sum comprising the organization's own contribution, other public sources and other sources change?  | 1.5%          | 0.0%          |
| 6.   | Was the table correctly filled in concerning the accounting by the type of costs, and was it checked whether it was consistent with the amounts from the invoices? (part II. 1) | 6.2%          | 13.2%         |
| 7.   | Are the costs covered by the grant for specific items consistent with the estimate?   | 4.6%          | 7.9%          |
| 8.   | Does the increase referred to in point 6 exceed 10%?  | 1.5%          | n.d.          |
| 9.   | Was the table concerned with accounting by the source of funding correctly filled in? (part II.2)   | 3.1%          | 0.0%          |
| 10.  | Is the grant share compliant with the agreement?  | 10.8%         | 2.6%          |
| 11.  | Does the increase referred to in question 9 exceed 5%?  | 3.1%          | n.d.          |
| 12.  | Was the limit from question 7 and/or 10 exceeded in total; that is, was the grant collected for an excessive amount?  | 6.2%          | n.d.          |
| 13.  | Was the information included on the revenues obtained while performing the agreement, and on bank interest on the appropriations collected in the bank account? (part II. 3)    | 9.2%          | 13.2%         |
| 14.  | Are the accounting documents dated within the timeframe of the task implementation? (part II. 4)  | 6.2%          | 2.6%          |
| 15.  | Were all the elements included in the invoices given correctly? (part II. 4)  | 0.0%          | 0.0%          |
| 16.  | Was the list of invoices prepared correctly? (part II. 4)   | 12.3%         | 13.2%         |
| <b>D. Substantive evaluation of additional documents</b> |   |               |               |
|  |   | <b>10.3%</b>  | <b>3.8%</b>   |
| 1.   | Was the report accompanied by other documents which were required?  | 38.5%         | 33.3%         |
| 2.   | Were additional materials documenting the implementation of the task enclosed?  | 23.1%         | 0.0%          |
| 3.   | Do the enclosed documents confirm a sound implementation of the task?   | 38.5%         | 66.7%         |
| <b>Total</b>   |   | <b>100.0%</b> | <b>100.0%</b> |

Source: self-reported data.

In the substantive evaluation of the report on the implementation of the public task what is noticeable is the fact that the objectives of the tasks financed by public funds and formulated in the tender and accounted for in the report are general and non-measurable, which makes it impossible to check whether or not the appropriations were spent in a focused way e.g. development of physical fitness among youth, promoting national tradition. Clearly the SMART method in setting up goals has not been employed (specific, measurable, achievable, relevant and timed objective). It has to be stressed that in indicating the attractiveness of an objective one cannot disregard the financial dimension making it necessary to define economic benefits that can be achieved through the implementation of a particular task, e.g. expenditure savings (assessment of the effectiveness/productivity of public spending). Whether a particular objective is realistic should be analyzed not only in terms of keeping to the agreed timeline of the task implementation (the entire task as well as individual activities making up the task), but also in terms of the sources which the contractor has at hand. Hence, in the tender for the implementation of a public task, constituting an annex to the agreement, legislator provided for the information on the tenderer's personal and material contribution, including, for instance, information on the skills of persons to be employed to carry out the task, voluntaries' skills, available premises, equipment, materials. In none of the tasks examined were such data provided. The feasibility of accounting for the task was assessed by the outsourcing party on the basis of the previous cooperation with the public benefit organization.

What is further noticeable is that neither the outsourcing party nor the contractor appreciate the informative quality of additional documents attached to the report. For the unit which contacts out a task and does not make an on-site verification, what can become an information source instead is, for instance, an attendance list, posters promoting the project, press clips, evaluation questionnaires.

## **6. Conclusions**

The aim of the article was to assess whether local government units in their outsourcing some of their own tasks to non-governmental organizations may in fact be violating the basic principles of the European Union, and whether or not in their accounting for the implementation of tasks local governments observe the principle of sound financial management, in other words, whether it complies with the principles of economy, efficiency and effectiveness in terms of public spending.

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While realizing the aim outlined in the paper, a review of European and national legal acts was conducted, as well as an analysis was carried out of reports on the implementation of public tasks by non-profit organizations, with the reports providing the basis for accounting for the appropriations in two local government units. In the study, the reports of those organizations were adopted which used those appropriations throughout the longest period of time, received the largest amounts and carried out the highest number of tasks over the years 2014-2015.

The analysis of the legal framework shows that one cannot rule out that local governments may violate the principle of the free market competition when entrusting public tasks or in aiding their implementation by providing public benefit organizations with earmarked grants. The Polish state granted special rights to non-governmental organizations and other entities listed in Article 3 paragraph 3 of UDPP, pursuant to Article 106 of TFEU. The European Commission has, however, noted on numerous occasions that Member States by granting special or exclusive rights to individual undertakings, as well as by financing through public sources services in general economic interest violate the EU fundamentals – its principles. In the regulation on *de minimis* (small) aid, it was laid down that a given appropriation does not affect trade, nor does it distort competition and as such it does not constitute a public aid if the total *de minimis* aid granted to an undertaking does not exceed EUR 200 000 over the period of three years, that is over PLN 200 thousand per year. The study carried out in the selected local government units shows that the amounts most frequently used in funding are within the range between a few and several dozen thousand zlotys, although there are also some exceeding this amount.

Examining the financial aspect of accounting for grants provided to NGOs by local government units, the conclusion to be made is that the implementation of the principle of purpose and economy in spending the grant resources is not entirely observed. There are accountings in which appropriations were spent not on what was stated in the tender. In accounting for the total costs of a public task more emphasis is being put on meeting the formal requirements rather than those in terms of effectiveness of spending. The relationship between the best effect and the costs incurred is not analyzed. Tenders for the implementation of a public task include no measurable objectives, which rules out the evaluation of the grant already at the stage of conducting the tender for carrying out public tasks.

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