Funding and Implementation of the Rail Baltic project in Estonia from 2014-2019

How has the implementation, incl. funding, organisation of procurements and management of contracts, of the Rail Baltic project been organised in Estonia?

Report of the National Audit Office to the Riigikogu, Tallinn, 4 December 2019

Ellen Niit

Rongisõit

Rong see sõitis tsuhh-tsuhh-tsuhh,
piilupart oli rongijuht.
Rattad tegid rat-tat-taa,
rat-tat-taa ja tat-tat-taa.

Aga seal,
rongi peal,
kas sa tead, kes olid seal?

Seal olid miisud,
seal olid liisud,
seal olid väiksed kirjud kiisud.
Kiisud sõitsid Türile,
sõitsid külla Jürile.

Seal olid suured mustad kutsud,
seal olid väiksed roosad notsud.
Kutsud sõitsid Torilasse,
notsud sõitsid Porilasse.

Seal olid sarvilised sikud,
sarvilised sikud-sokud.
Sokud sõitsid Karjakülla,
Karjakülla, Marjakülla.

Rong see sõitis tsuhh-tsuhh-tsuhh,
piilupart oli rongijuht.
Rattad tegid rat-tat-taa,
piilupart jäi tukkuma.

Oi-oi-oi, ai-ai-ai,
mis siis sellest rongist sai?!
Rong see sõitis tsuhh-tsuhh-tsuhh,
kuni kraavi läks – karpuhh!!

Oi-oi-oi, ai-ai-ai,
mis siis reisijatest sai?!
Kõik nad läksid uperpalli,
uperpalli, kukerpalli.

Kümme notsut kukkus kraavi,
kümme kutsut laskis traavi,
kiisud jooksid, sabad seljas,
kutsud jooksid, keeled väljas,
sarved segi sikkudel,
sikkudel ja sokkudel.

Kiisud ei saanud Türile,
külla minna Jürile,
kutsud ei saanud Torilasse,
notsud ei saanud Porilasse,
sokud ei saanud Karjakülla,
Karjakülla, Marjakülla.

The poem "Rongisõit" (1957) is published in the audit report with the kind permission of the heirs of Ellen Niit.
The melody of the song based on this poem was composed by Gustav Ernesaks.

Dear readers,

Rail Baltic is the biggest infrastructure project during the history of the independent Estonia both in terms of cost and scale. Approximately a quarter of the total length of the 870-kilometre railway from Tallinn to the border between Lithuania and Poland, which will cost 5.79 billion euros according to initial estimates, will be in the territory of Estonia. The preparation and implementation of the project has been ongoing to a bigger or lesser extent since 1994, somewhat more actively for the last decade.

The planning and management of major projects is always difficult. This is due to the scale of the project as well as the polarising disputes that always go with such projects, numerous unexpected occurrences in the different stages of the project and the mutual amplification of such occurrences. The complexity of the Rail Baltic project is increased by the participation of three states in the project, different interests and a complicated management system where, as indicated by the audit, responsibility can sometimes become muddled.

Contingencies – whether objective or arising for superficial planning – are an organic part of major projects. So, you should always be prepared for contingencies, as they are expected. Not welcome, but unavoidable. As a rule, there are at least three patterns that characterise major projects. The first is that the majority of contingencies that occur during the project are not good for the budget. The second one is that major projects don’t tend to get completed before the planned deadline. They are completed considerably later than initially planned, which means that the benefits of the project are also postponed. And the third pattern is that in the first stage of the project, the leaders of the project are brimming with confidence and certain that the project will be completed by the deadline and it will cost just as much as planned. Even if there are sings that clearly suggest the opposite. But in the initial stage of the project, it is always possible to claim that the increased costs can be covered by cutting the costs of the next stages and the lost time can be made up for by accelerating the next stages. But reality bites in the next stages – they also have some contingencies in store.

Due to the extreme complexity and countless risks of a major project, it’s important that the action plan and funding are planned carefully and in as much detail as reasonable and possible for the entire period of the project. If circumstances change, the project’s action plan and budget have to be reviewed and adjusted. Not for the sake of planning, but to ensure that the project is manageable, and its goals can be achieved by the planned deadline and with the planned costs.

Does the Rail Baltic project differ from other projects? It appears that it doesn’t – delays have occurred in the implementation of activities and the cost forecasts of some activities have increased. For example, the analysis indicated that the activities for which Estonia is responsible have exceeded or are about to exceed the deadlines planned in the funding agreements by more than two years on average. The Ministry of Economic Affairs and Communications insists that every effort will be made to complete the project by 2026 as planned and to find ways of saving money. Although some steps have been taken in this direction, the circumstances identified during the audit indicate that the cost of the activities is likely to exceed the initial forecasts and the completion of the project by the deadline is not realistic – until now, most of the previously set deadlines have not been met.

It was a surprise to the National Audit Office that the Rail Baltic project is only planned by four-year periods. This means that the project documentation does not include an action plan and budget that cover the entire period. The cost specified in the cost-benefit analysis of 2017 is considered in the case of the final price. 433.9 million euros has been spent and is planned to be spent on the development of the Estonian part of the project from 2010 to 2023, which comprises *ca* one-third of the estimated cost of the Estonian part of the Rail Baltic project highlighted in the cost-benefit analysis. A clearer budget forecast has not been prepared for the rest of the project, i.e. an estimated two-thirds of it. The problem is not that the Government has not approved these budget forecasts – they also don't exist as parts of the project documentation.

In the audit, the National Audit Office suggested preparing clearer budget forecasts and funding scenarios of Rail Baltic until the end of the project and present them as annexes to the budget forecast, but the response of the Ministry of Economic Affairs and Communications was surprising. In the opinion of the Ministry, planning the financial side of the project for more than four years is unlawful and possibly also in contravention of the Constitution.

The Ministry adds that the four-year planning period stipulated in the Budget Act is not random, but based on the facts that planning highly specific funding needs and sources for longer periods is difficult because of changes in critical circumstances and that the Constitution does not permit depriving future compositions of the Riigikogu of the opportunity to plan the budget.

There isn't a single legal act, not to speak of the Constitution, that prohibits long-term planning. The preamble to the Constitution still includes the objective to guarantee the preservation of the Estonian people and the Estonian culture through the ages, not just for the four-year period of the state budget. Long-term development plans are still prepared. The Constitution does not obstruct prudential and reasonable behaviour.

The Ministry adds in its letter that the existence of the money by 2024 and thereafter is guaranteed by the fact that in 2017 the Riigikogu assumed the obligation to complete the construction of Rail Baltic irrespective of what the rate of the specific self-financing of Estonia is. As a conclusion, it adds that finding the funds for the establishment of Rail Baltic is within the competence and the obligation of the Riigikogu composition of the respective years. Time will tell whether the Riigikogu has understood the matter in the same manner and obediently finds the money in the future irrespective of how much the Ministry of Economic Affairs and Communications needs for progressing with the project.

The National Audit Office advises the Riigikogu to demand from Ministry of Economic Affairs and Communications a project plan for the entire project period with the obligation to specify it when the circumstances change. We have to agree with the Ministry of Economic Affairs and Communications that planning is difficult, because we don't know how much and on which conditions we can receive support from the European Union in the new funding period from 2021 to 2027. But this doesn't mean we cannot prepare budget forecasts.

Another problem is that we don't have scenarios that could be followed if the implementation of the project ended up costing more than planned or if the European Union funding was lower than the expected 85%. The support of the European Union may decrease if the Member States decide to change the requirements for co-funding the facility or terminate the facility altogether in the negotiations concerning the funding period, or if the decision made upon the assessment of funding applications is to allocate less support than expected. The project may also end up costing more if the activities agreed in the funding agreements cannot be implemented within the agreed scope and schedule and/or with the agreed budget.

If the Ministry of Economic Affairs and Communications proceeds from the fact that the Riigikogu has assumed the obligation and must find the money necessary for funding Rail Baltic no matter how much it costs, then it should present the respective risk scenarios to the Riigikogu.

The risks must be managed and there must be an action plan in place in case the above happens. We must not place ourselves in the situation where the Ülemiste passenger terminal, Pärnu passenger terminal and a couple of viaducts have been built, but there is no railway between them and no money to build it. It would be irresponsible to claim then that the Riigikogu assumed the obligation and must find the money. The scenario where Rail Baltic ends in Riga, coming from the heart of Europe, is also something we don't really want to think about. In this case, the territory between Riga and Helsinki would be an isolated wasteland, a province.

We need extremely strong political will and support to ensure that this will not happen to Estonia. The National Audit Office already emphasised in its overview of 2017 that geopolitical considerations have always been at the centre of the decisions made about Rail Baltic.

We cannot just sit around and hope that nothing will derail the train. The train has to have a driver who understands that they must drive, that they are responsible, and they must see the journey ahead and any risks that may lie in wait.

The joint audit of the Estonian, Latvian and Lithuanian supreme audit institutions of the management of the Rail Baltic project will be completed soon. It will give an idea of what will happen if there are too many drivers pulling at the levers, each of them trying to steer the train in a different direction.

Janar Holm
Auditor General

4 December 2019

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How has the implementation, incl. funding, organisation of procurements and management of contracts, of the Rail Baltic project been organised in Estonia?

Summary of audit results

What did we audit?

The supreme audit institutions of Estonia, Latvia and Lithuania started a joint audit of the Rail Baltic project in 2018 in order to analyse how the funding of the project, the organisation of procurements and the management of contracts has been organised. At the same time, the National Audit Office analysed the implementation of the project in Estonia. The results of the audit carried out in Estonia are presented in this report. The implementation of the entire project is described in the joint audit report of the supreme audit institutions of the three Baltic States, which will be completed by the end of 2019.

Why is this important to taxpayers?

Rail Baltic is the biggest infrastructure project in the history of the independent Republic of Estonia both in terms of cost and scale. The planned total length of the railway from Tallinn to the border between Lithuania and Poland is 870 kilometres, 213 kilometres of which will be in the territory of Estonia. The implementation of the Rail Baltic project costs 5.79 billion euros[1] according to the cost-benefit analysis prepared in 2017. 1.35 billion of this will be spent on the construction of the railway in Estonia, 1.97 billion in Latvia and 2.47 billion in Lithuania.

The three Baltic States entered into an agreement in 2017, with which they assumed the obligation to complete the Rail Baltic railway by 2025 and ensure operation by 2026[2]. Approximately 81% of the cost of the project[3] will be funded by the European Union and the rest by Estonia, Latvia and Lithuania themselves.

[1] Rail Baltica Global Project Cost-Benefit Analysis. Commissioned by RB Rail AS, prepared by Ernst & Young Baltic AS, published 30 April 2017.

[2] Agreement between the Government of the Republic of Latvia, the Government of the Republic of Estonia and the Government of the Republic of Lithuania on the Development of the Rail Baltic/Rail Baltica Railway Connection. Ratified in the Riigikogu on 19 July 2017.

[3] The European Union budget programme (CEF) only co-finances up to 85% from the financial gap of projects with a negative financial net present value. The CBA analysis conducted by EY estimated the financial gap for the RB project to be 94.18%. Nevertheless, the current three CEG Grant Agreements were signed prior to the CBA and the Activities in these GAs are financed by 81% or 85%, depending on the type of Activity. That means that the Commission co-finances approximately 80-82% of the whole RB project.

What did we find and conclude on the basis of the audit?

The audit of the National Audit Office indicated that delays have occurred in the implementation of activities agreed in the Grant Agreements and the cost forecasts of some activities have increased. According to the Ministry of Economic Affairs and Communications, the parties to the project are making every effort to complete the project by its deadline, i.e. 2026. However, the facts identified during the audit indicate that the completion of the project by the deadline is not realistic and the cost of the activities will probably exceed the initial forecasts.

- **The costs of implementation of the activities of the project have increased and their implementation has been delayed.** The audit of the National Audit Office indicated that the projected cost of the activities of the Rail Baltic project for which Estonia is responsible has increased by 31.7 million euros, i.e. 13.9%, when compared to the budget agreed in the three Grant Agreements entered into with the European Union. The European Commission funds the project activities within the scope of the budget agreed in the Grant Agreements and Member States have to cover any extra expenses themselves. At the same time, it's possible to amend the Grant Agreements with the consent of the parties, including extend the deadlines for completion of activities and divide the activities into parts.

  The analysis of the National Audit Office also indicated that the activities for which Estonia is responsible have exceeded or about to exceed the deadlines agreed in the Grant Agreement by more than two years on average. However, if a Member State doesn't manage to use the co-funding at the right time, the European Commission has the right to reclaim the funds. The increasing cost and delays have, among other reasons, been caused by delays in the activities implemented by RB Rail AS (hereinafter RBR) and the specification of the cost forecasts. However, increasing costs and extending deadlines are rather ordinary in the case of major projects[4].

- **The challenge of the state of Estonia upon the implementation of the RB project is to guarantee the existence of funding during the entire project.** In its overview of 2017[5], the National Audit Office advised the state to develop a plan for funding the Rail Baltic project and scenarios for the cases where the rate of EU co-funding proves to be smaller than planned or the project becomes more expensive. This has not been done yet.

  According to the Ministry of Economic Affairs and Communications (MEAC), the funds for the project are planned in the state budget and the state budget strategy, i.e. for five years in advance in total. 433.9 million euros has been spent or is planned to be spent on the development of the Estonian part of the project in the period of 2010-2023. That comprises 32.1% of the estimated cost of the Estonian section of the project. This in turn indicates that a more detailed

[4] Special Report No. 19/2018 of the European Court of Auditors: A European high-speed rail network: not a reality but an ineffective patchwork.

[5] National Audit Office's overview of the agreement for the development of the Rail Baltic rail connection entered into by the governments of Estonia, Lithuania and Latvia National Audit Office, 24 May 2017.

funding forecast, incl. the possible sources of own funding, of at least 67.9% of the project is missing at present.

The audit of the National Audit Office also indicated that the roles and responsibility related to procurements for the Rail Baltic project and the management of contracts have been divided and the procurement and contracting activities have generally been in line with laws and the agreed rules. Although the completion of the project by the deadline and according to the budget does not depend on the activities of Estonian agencies alone, a more efficient approach of the implementers to the project would contribute to the timely and sustainable achievement of the goals.

- **However, there are shortcomings in the organisation of supervision of the Estonian section of the project and the management of risks and changes.** Although most of the activities related to the Rail Baltic project for which Estonia is responsible are carried out by Rail Baltic Estonia OÜ (hereinafter also RBE), the Ministry of Economic Affairs and Communications is still responsible for the timely completion of the activities within the scope of the budget of the respective Grant Agreement.

  However, the MEAC has not established how the activities of RBE are supervised and how the important changes occurring in the project are managed, e.g. a significant extension of the deadline or an increase in costs. According to the MEAC, the steering group of the project was restored at the time of the audit and it has a meeting once a quarter. The main goal of the steering group is to guarantee regular information exchange between the parties of the project and the achievement of agreements at the level of management. Risk management at the Estonian level of the project, as well as in RBE has not been properly developed either.

- **Rail Baltic Estonia OÜ is responsible for the organisation of most procurements and the management of contracts, and it has largely performed its functions well so far.** Internal procedures and guidelines have been established and they have been generally complied with in the organisation of procurements and management of contracts. However, RBE must update and develop its internal processes further as the project progresses and the procurement volumes increase. For example, RBE claims that many agreements and decisions are currently made informally by way of informal communication without documentation of the decisions. This approach worked most of the time, as RBE only employed one project manager until 2019 and there were few activities, but the National Audit Office finds that transparency in carrying out procurements and management of contracts was not fully guaranteed.

Main recommendations

Based on the above, the National Audit Office advises the Ministry of Economic Affairs and Communications to:

- develop a project supervision and change management system in order to make the implementation of the project more efficient, incl. determine the role of the MEAC in the exercise of supervision and management of changes, and the procedure required for the performance of the role;

- analyse possible funding scenarios in cooperation with the Ministry of Finance to reduce the project funding risks and prepare funding forecasts.

Response of the Minister of Economic Affairs and Infrastructure: In the opinion of the Minister of Economic Affairs and Infrastructure, the deadlines agreed for the establishment of the Rail Baltic railway with agreement ratified by the parliaments of the Baltic States are still realistic and the MEAC as well as the other parties to the RB project are constantly working on the completion of the RB railway by 2026. In the opinion of the minister, the roles and responsibility of the Estonian parties of the project are regulated with contracts and the Ministry has planned the funding of the RB railway well in advance whilst complying with all of the obligations and options provided for by law. The minister promised to establish the document of the new management and control system in 2019 and take on board the National Audit Office’s recommendations about roles, supervision, information exchange, change management and risk management.

However, the Minister of Economic Affairs and Infrastructure said that the recommendations made by the National Audit Office for analysing project funding scenarios are questionable from the viewpoint of the state budget planning and preparation principles established by laws and regulations, incl. the principle of universality of the state budget, and compliance with them may breach the principles of materiality and the financial competencies of the Riigikogu.

Comment of the National Audit Office: In the opinion of the National Audit Office, preparing the project’s budget forecast for a longer time does not restrict the financial competence of the Riigikogu. In its overview of 2017, the National Audit Office made the following recommendation about the agreement for the development of the Rail Baltic rail connection made between the governments of Estonia, Lithuania and Latvia: ask the government to submit an analysis and action plan for funding Rail Baltic. The National Audit Office pointed out that the Riigikogu should know the answers to at least the following questions: How big is the financial obligation that will be assumed for the state? How will the project be financed? Has a clear decision-making mechanism been agreed in case the project ends up costing more than planned, is not completed by the deadline or there are changes in funding? The role of the government is to guarantee that the Riigikogu would have all of the information necessary for making decisions. The longer project funding forecast and scenarios recommended in this audit could therefore be the input for the preparation of the state budget and the state’s budget strategy if necessary.

Response of the Minister of Finance: The Minister of Finance finds that it is necessary to develop scenarios for the possibility and impossibility of continuing with the project in the case of different developments, including the reduction or termination of European Union co-funding and if the project becomes more expensive or is delayed. In the opinion of the Minister of Finance, it is highly unlikely that the Baltic States could finance the implementation of the project if the participation rate and volume highlighted in the cost-benefit analysis were considerably larger.

Based on the above, the National Audit Office advises Rail Baltic Estonia OÜ to:

- develop the risk management system for the timely detection and management of risks further in such a manner that it would help mitigate the increasing cost of the project and the delays in the activities;
- document the discussions and decisions concerning the organisation of procurements and management of contracts, the meetings of the working group on risk, the election of members of the procurement committee and the reasons for changing the procurement plan in order to ensure that activities are transparent and can be verified.

Response of the member of the Management Board of Rail Baltic Estonia OÜ: The member of the Management Board of Rail Baltic Estonia OÜ said in their response that the company regularly maps and assesses risks and develops risk management measures. RBE plans to improve the risk management system more regularly in the future. RBE also promised to improve documentation and establish in the procurement procedure the requirements for documenting the reasons of changing the procurement plan, the selection of the procurement type and the decisions made at project meetings. The member of the Management Board promises to record the reason for the selection of committee members in the respective decision in the future and include the relevant requirement in the procurement procedure.

What will we do next?

The National Audit Office deems the improvement of the supervision of the RB project and the preparation of project funding forecasts important components of the success of the project. Therefore, the National Audit Office plans to carry out follow-up activities in 2020 to make sure that the problems have been solved.

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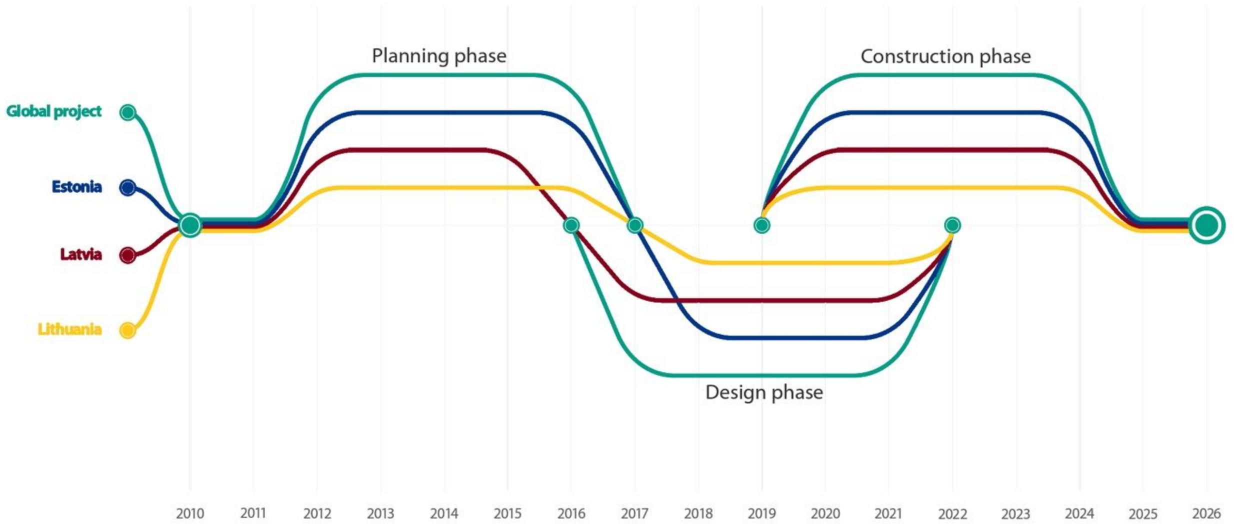
Overview

Characterisation of the Rail Baltic project

1. The Rail Baltic project is a railway project of the three Baltic States[6] co-funded from the Connecting Europe Facility (CEF[7]) of the European Union, which according to the intergovernmental agreement should start operating in 2026 (see also Figure 1).

Figure 1. Schedule of the Rail Baltic project



Source: RB Rail AS

Rail Baltic global project refers to the project of three states. RB Rail AS is the coordinator of the global project.

2. The parameters of the so-called global project were specified[8] in spring 2017, when the parliaments of Estonia, Latvia and Lithuania ratified the intergovernmental agreement. According to the agreement, Rail Baltic is a new fast double-track electrified railway line for passenger and freight transport to be built by way of a project of common interest. The agreed corridor of the railway line runs from Tallinn through Pärnu, Riga, Panevėžys and Kaunas to the border of Lithuania and Poland, and it will have the standard European gauge track width and the maximum project speed of 240 km/h.

3. The project parameters given in the intergovernmental agreement were adjusted upon the preparation of the project guidelines in 2018 considering, among others, that the RB railway must also comply with the requirements of the military mobility facility of the European Union.[9] Therefore, a higher axle load and wider wheelbase of the trains is taken into account upon the establishment of the railway.

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[6] Finland and Poland also participate in the project as observers. A proposition to join as shareholders of RB Rail AS has also been made to both countries.
[7] The Connecting Europe Facility is a key EU funding instrument to promote transport, energy and digital infrastructure projects at the European level.
[8] The indicators were obtained from the AECOM feasibility study of 2011 and the joint declaration of the Baltic prime ministers, see the National Audit Office's 2017 overview of the agreement for the development of the Rail Baltic rail connection entered into by the governments of Estonia, Lithuania and Latvia.
[9] Military Mobility Action Plan of the European Union agreed in 2018: https://ec.europa.eu/transport/sites/transport/files/2018-military_mobility_action_plan.pdf.

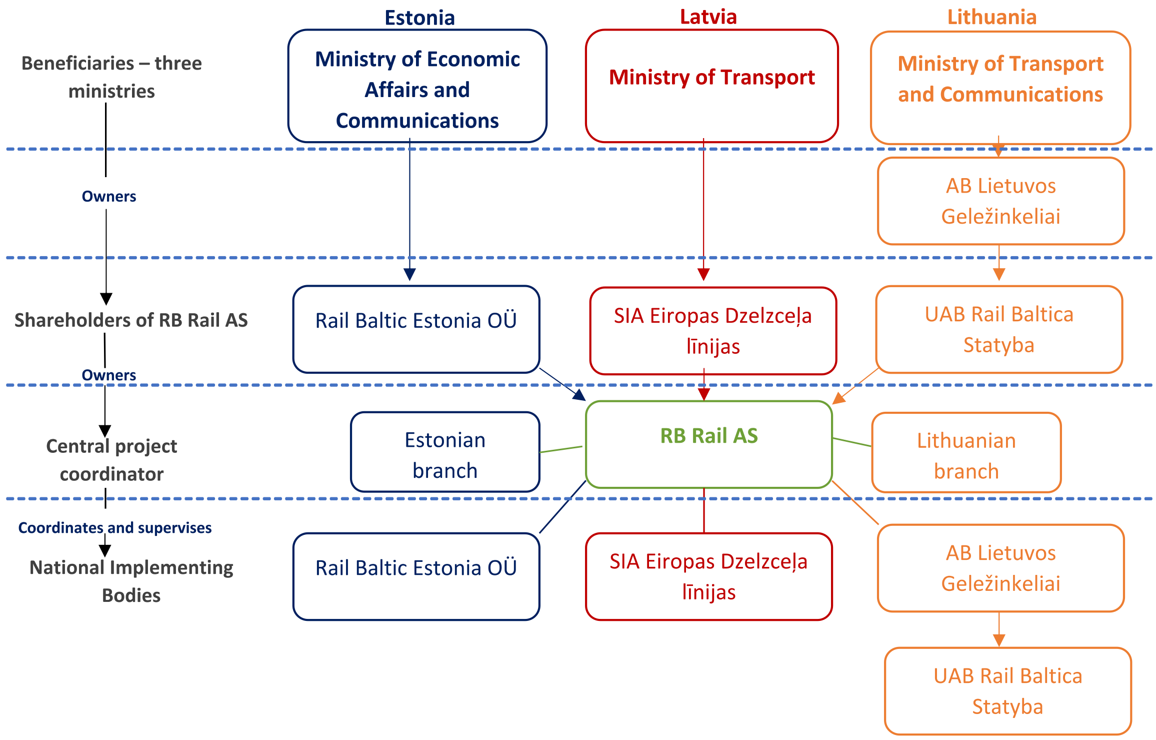
Which agencies carry out the project?

CEF Grant Agreement – the Grant Agreement entered into between RB Rail AS, the ministries responsible for the area of transport of the Baltic States and the Innovation and Networks Executive Agency (INEA) that represents the European Union, which determines the activities required for the implementation of the parts of the project, the time frame, cost, funding and sub-activities of their implementation, which generally mean the carrying out of a procurement contract and award of the public contract.

4. Due to the regulations of the European Union[10], the CEF Grant Agreements and the multilateral agreements made on the basis thereof, the three states participating in the project as the project beneficiaries are responsible for the implementation of the project. The implementation of the Rail Baltic project is the responsibility of the Ministry of Economic Affairs and Communications in Estonia, the Ministry of Transport in Latvia and the Ministry of Transport and Communications in Lithuania (see also Figures 2 and 3).

5. The joint venture RB Rail AS, which operates in Latvia, was established for the implementation of the project and it coordinates the activities of the three states. RB Rail AS is also a project beneficiary according to the CEF Grant Agreements. State owned enterprises have been established in each state[11] for the implementation of the project, which in turn are the founders and shareholders of the joint venture registered in Latvia, each with a share of one-third. RB Rail AS also supervises the activities of the implementing bodies appointed by the project states and makes sure that the activities comply with the conditions established in the Grant Agreements (see also Figures 2 and 3).

Figure 2. Structure of implementation of the Rail Baltic project



Source: National Audit Office

[10] The TEN-T Regulation 1315/2013/EU of the European Parliament and of the Council on Union guidelines for the development of the trans-European transport network and the CEF Regulation, i.e. Regulation (EU) No 1316/2013 of the European Parliament and of the Council establishing the Connecting Europe Facility.
[11] In Lithuania, the shareholder of RB Rail AS is not directly owned by the state, but belongs to Lithuanian Railway (Lietuvos geležinkeliai), see Figure 2.

Which agreements do the project parties proceed from when carrying out procurements and awarding contracts?

6. When carrying out project procurements and awarding contracts, the parties to the Rail Baltic railway project proceed first and foremost from the Contracting Scheme for the Rail Baltic/Rail Baltica, which is an agreement made between the ministries of the three Baltic States, the joint venture and the shareholders on 30 September 2016. This agreement replaces any earlier agreements about the division of roles and responsibilities of the project parties.

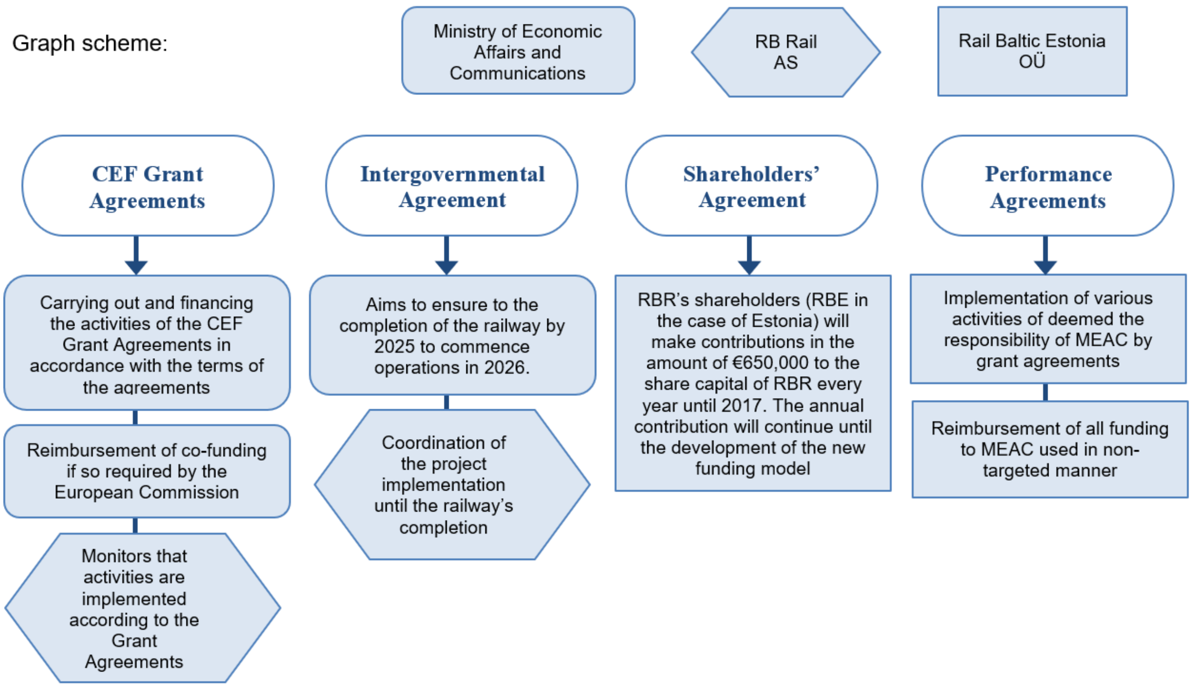
7. The agreement stipulates that the joint venture organises public procurements for studies for the global project, procurement of raw materials, design and construction of the railway sections between the states. In addition to this, the shareholders agreement entered into upon the establishment of the joint venture and the CEF Grant Agreements stipulate that the tasks of RBR include the development of the technical parameters of the railway, supervision of the funding and implementation of the project, risk management and coordination of the implementation of the project (in addition to these tasks, see the responsibility of RBR in Figure 3).

8. The states are responsible for the implementation of the project according to the CEF Grant Agreements. This entails carrying out the studies and analyses required for the completion of the project internally. It also covers the procurements of the technical design of the passenger and freight terminals, depots and other sites required for the operation of the railway and the establishment of these sites as well as the establishment of the track bed, bridges, viaducts and other railway infrastructure, including the organisation of construction procurements.

9. The Ministry of Economic Affairs and Communications has entered into performance agreements[12] with Rail Baltic Estonia OÜ to whom the organisation of the activities required for the implementation of the project have been delegated. Rail Baltic Estonia OÜ is also the implementing body of the activities of the Estonian beneficiary (i.e. the MEAC) according to the CEF Grant Agreements. Therefore, RBE organises procurements for the implementation of the activities for which Estonia is responsible (see also Figure 5), awards contracts and is responsible for the performance of these contracts (see Figure 3).

[12] Contract No 24.5-6/16-040, approved by the Secretary General of the MEAC on 25 October 2016, and Contract No 24.5-6/18-0005/5117, approved by the Secretary General of the MEAC on 11 June 2018. The MEAC, the Ministry of the Environment and the Land Board have also entered into a similar cooperation agreement, which delegates the acquisition of land for RB to the Land Board.

Figure 3. Responsibility of the parties to Rail Baltic project



Source: National Audit Office

How does RBE carry out procurements?

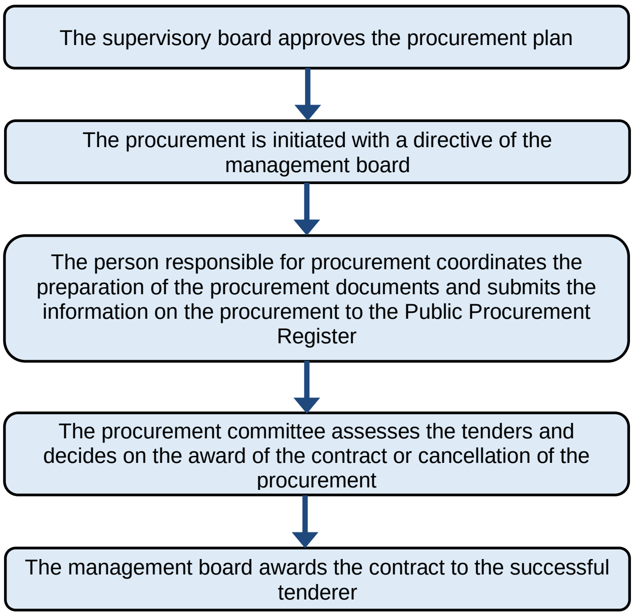
10. Rail Baltic Estonia OÜ uses public funds, i.e. the taxpayers' money, for purchasing the items and services or ordering the construction works it needs for its operations. Thus, Rail Baltic Estonia OÜ is obliged to carry out public procurements and comply with the Public Procurement Act.

11. The purpose of the Public Procurement Act is to guarantee the transparent, practical and economical use of money, equal treatment of persons and efficient use of the existing competition conditions in public procurement. The public procurement procedure guarantees that certain principles are followed upon the organisation of public procurement, and that activities and decisions are transparent and verifiable.

12. The same is also guaranteed by RBR and the RB project implementers in Latvia and Lithuania, who proceed from the law of the EU and their states.

13. Rail Baltic Estonia OÜ carries out procurements according to the procurement procedure approved in the company (see Figure 4).

Figure 4. Organisation of procurement in OÜ Rail Baltic Estonia



Source: National Audit Office

How does the Riigikogu obtain an overview of the expenses incurred in relation to Rail Baltic?

14. In 2017, before the ratification of the intergovernmental Rail Baltic agreement, the National Audit Office prepared an overview for the Riigikogu[13] of the obligations that Estonia has as a result of earlier decisions, including in relation European Union law, and the obligations that will arise upon the ratification of the intergovernmental agreement.

15. The National Audit Office advised to create an additional regulation which would, among others, determine the obligation of the Government to inform the Riigikogu regularly and, in the agreed cases, extraordinarily of the status of the development of the RB project. As a result of this, the Riigikogu added a clause to the Intergovernmental Agreement Ratification Act, which improved the giving of overviews of the project expenses to the Riigikogu.

16. The explanatory memorandum to the 2019 state budget includes a more detailed action plan of the RB project for 2019 and the estimated cost of its implementation. The Ministry of Economic Affairs and Communications has also prepared an overview of the activities of the RB project to the Riigikogu in 2017 and 2018. A more detailed description of the costs of the project and an overview of activities allow the Riigikogu to make more informed budget policy decisions, considering the objectives of the state and the state budget, and the respective legislation, incl. multilateral agreements.

What did the National Audit Office audit this time?

17. In early 2017, the supreme audit institutions of the Baltic States agreed to audit the project together and established by the end of the year that the functioning of the internal control system of the project will be analysed during the first joint audit of the three Baltic States. The audit institutions wanted to make sure before the announcement of the large

[13] National Audit Office's overview of the agreement for the development of the Rail Baltic rail connection entered into by the governments of Estonia, Lithuania and Latvia National Audit Office, 24 May 2017.

construction procurements that the joint venture operating in Latvia as well as the implementing bodies of the Rail Baltic project appointed by the states have established adequate mechanisms to guarantee that the project stays in line with the schedule and the budget.

18. The National Audit Office carried out two audits: the national audit and the joint audit of the supreme audit institutions of Estonia, Latvia and Lithuania about RB Rail AS (hereinafter the Joint Audit).

19. In the national audit, the National Audit Office analysed the funding of the Rail Baltic project and the functioning of the internal control system of RBE upon the organisation of procurements and the management of contracts according to the COSO framework[14]. The National Audit Office assessed whether RBE has established appropriate rules for carrying out procurements and managing contracts, and whether these rules are followed. Compliance with the rules was analysed by the case-study of three completed procurements and performed contracts of RBE (see also Table 1 on page 43).

20. RBE had carried out 12 procurements by December 2018 and the National Audit Office selected three of them for analysis on risk-basis – the ones where the amounts were large, the first procurement failed and/or the completion of the contract was late. The following procurements were reviewed:

- Procurement No 186474 “Preliminary study of the technical and spatial need of maintenance depot of railway infrastructure”;
- Procurement No 183609 “Ordering a risk analysis of the Estonian section of the Rail Baltic project”;
- Procurement No 177780 “Analysis of the technological and spatial needs of the multimodal freight terminal Rail Baltic at Muuga Harbour”.

21. The functioning of the internal control system of the global project and six procurements carried out and contracts awarded by RB Rail AS from 2015 to 2018 were analysed in the Joint Audit.

22. In the first chapter of this report, the National Audit Office describes how the Rail Baltic project is funded, which includes pinpointing the shortcomings in the funding of the project. The National Audit Office also highlights how the agreed schedule and budget have been followed in the implementation of the project from 2014-2019. As the success of the project also depends on how the preparation and construction of the railway have been organised, the second chapter of the report of the National Audit Office describes the functioning of the internal control system of the project’s procurements and contracts (hereinafter the Internal Control System) and highlights the possibilities for improving it. The results of the analysis of the three public procurements of RBE and the contracts awarded are described in the third chapter.

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[14] Committee of Sponsoring Organisations (COSO) of the Treadway Commission. The integrated internal control framework of COSO is the most broadly recognised approach to internal control.

Funding and schedule of the Rail Baltic project

The funding of the Rail Baltic project is planned for four years in advance and a more detailed forecast needs to be developed

Criterion 1: The National Audit Office presumed that the state has analysed the possible funding scenarios of the Rail Baltic project and prepared detailed long-term funding forecasts until the completion of the railway.

How does the European Union support the Rail Baltic project?

23. The funding of the Rail Baltic project depends on the availability and scale of the financial support of the European Union. In addition to the co-funding from the European Union, the states themselves must cover *ca* 15% of the costs of the project with their own funds. The final scale of self-financing will become clear when Grant Agreements are signed and activities are implemented during the project.

24. In the intergovernmental agreement, Estonia, Latvia and Lithuania expressed the principle that the railway will be built if the European Union finances it with at least as much money as before, i.e. to the extent of 85%[15].

Funding application of RB project – RBR represents all of the beneficiary countries on the basis of an authorisation as of CEF Grant Agreement II. This means that all of the states apply for co-funding for the Rail Baltic project jointly.

25. EU aid is granted to the project via the calls for proposals of the CEF, which means that aid is not guaranteed to any project, but depends, among others, on the existence of money in the CEF, and the results of assessment of the funding applications of the RB project and of the competing projects.

26. Funding can be applied for every time when a CEF call for proposals is announced. A Grant Agreement will be entered into if the decision is made to support the project activities indicated in the application, and this means that the states who received co-funding from CEF (the MEAC as the representative of Estonia) and RBR will be obliged to implement the activities highlighted in the agreement.

How much money has been received with the Grant Agreements so far?

27. The co-funding from the EU and the self-financing by the states for the Rail Baltic project is specified most accurately in the CEF Grant Agreements.[16] Three Grant Agreements for the amount of 824 million euros, incl. self-financing of the states, have so far been entered into for the implementation of the RB project with the representative of the European Union, the Innovation and Networks Executive Agency for the Baltic States and RBR in total (see Annex A).

28. According to the CEF Grant Agreements, Estonia can use 234.51 million euros for the implementation of the activities set out in the

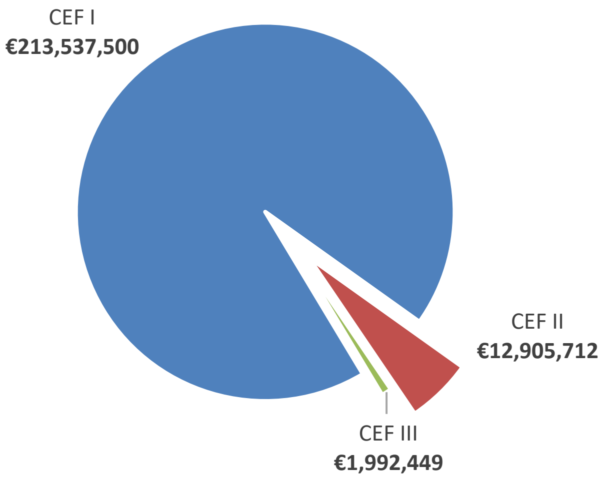
[15] The maximum aid intensity of the European Commission is 85% of the project's need for finances. Considering the expenditure and revenue of the project highlighted in the cost-benefit analysis, this means that the European Union will fund the entire project to the extent of *ca* 81%. See the detailed explanation in the National Audit Office's 2017 overview of the agreement for the development of the Rail Baltic rail connection entered into by the governments of Estonia, Lithuania and Latvia.

[16] Funding has previously been received from the TEN-T facility as well, see Annex B.

agreements until 2023[17]. 228.44 million euros of this is for the implementation of the Estonian section of the project and the rest for financing the activities to be carried out by RB Rail AS. 188.05 million euros of the total amount is European Union aid. The remaining amount is the state's self-financing, which will be covered from the state budget (38.65 million) and in one case from the budget of the City of Tallinn (1.73 million)[18].

29. The sums for the preparation and construction of the Rail Baltic railway are indicated in greater detail in Figure 5.

Figure 5. Sums of CEF Grant Agreements and the main activities for which Estonia is responsible



- Study of measures for mitigation of environmental impact
- Study of security of supply with mineral resources used in construction
- Study of the Muuga freight terminal
- Study of the infrastructure and rolling stock maintenance depot
- Archaeological studies
- Detailed technical design of the Estonian section
- Construction of the Ülemiste and Pärnu passenger terminals
- Stage I of track bed construction

- Solutions for the construction concept and construction logistics
- Feasibility of an additional freight station in the Tallinn region
- Studies of the Ülemiste-Vanasadam tram line and the Pärnu freight terminal
- Construction of the Ülemiste-Vanasadama tram line

- Preparation works for construction of the railway route corridor between Pärnu and the Estonian-Latvian border

Source: National Audit Office on the basis of CEF Grant Agreements

30. The money allocated with the CEF Grant Agreements entered into as of 2019 is not enough for the implementation of the entire project. In order to implement the Rail Baltic project, the MEAC has to apply for EU support from the additional calls for proposals of the 2014-2020 funding period of the EU, as well as from the subsequent EU funding period of 2021-2027. If the RB project is not completed by the agreed-upon deadline or if the money of the 2021-2027 funding period and the contributions made by the states themselves are not enough for the completion of the RB project, it is likely that support must be requested again in the EU funding period after the next.

[17] 2023 is the deadline for use of the funds of the CEF Grant Agreement III, the deadlines for use of the money from Grant Agreements I and II are earlier. See more in Annex A.
[18] The connection of the Tallinn Airport and Ülemiste Terminal with a tram line was financed from the budget of the City of Tallinn.

31. It's not clear yet how much support can be received from the European Union in the new funding period of 2021-2027 and in the subsequent period. The negotiations of the new funding period between the Council of the European Union and the European Parliament were ongoing during the preparation of the audit. According to the explanations of the Ministry of Economic Affairs and Communications, the conditions of the new funding period and the amount that can be obtained for the Rail Baltic project will presumably be clear by autumn 2020[19].

How is the long-term financing of the project by Estonia guaranteed?

32. A detailed and long-term funding forecast of the Rail Baltic project has not been prepared in Estonia as a separate document yet. The total expenditure of the state, incl. the expenses of the RB project, are planned in the state's budget strategy for four years in advance. According to the MEAC, the State Budget Act does not require planning the state's expenditure more accurately for a longer time and the costs of the project are planned in the budget strategy of the state proceeding from the investment plan of RB, which includes the amounts set forth in the CEF Grant Agreements, the expected EU aid in the subsequent funding period and the self-financing by Estonia.

33. The planned start of the use of the Rail Baltic railway is in 2026 and according to the cost-benefit analysis, the biggest expenses will be incurred in 2023 and 2024, i.e. there is no funding forecast for the most expensive period of the project. 28.8 million euros has been allocated for the project in the 2019 state budget and the last state budget strategy for 2020-2023 sets out that 373 million euros, incl. EU aid and self-financing by Estonia, will be spent on the activities of the RB project in this period. 32.1 million euros from the state budget has been used for the development of the project from 2010-2018 according to MEAC (see Annex B).

34. Thus, 433.9 million euros in total has been spent and is planned to be spent on the development of the Estonian part of the project from 2010-2023, which comprises 32.1% of the cost of the Estonian section of the project specified in the cost-benefit analysis. No detailed forecast has been prepared for funding the rest of the project, i.e. 67.9%, incl. for the possible sources of the funds.

35. According to the Ministry of Economic Affairs and Communications, agreements entered into at high levels give the security for the implementation of the project and the existence of funding form the state during the entire project. Above all, it is the intergovernmental agreement with which the Baltic States assumed the obligation to build the railway by 2025 in order to start using it in 2026. The obligation to build the railway has also been assigned to the Baltic States with the TEN-T Regulation[20] and the implementing decision made by the European Commission on the basis of the regulation[21].

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[19] The amounts allocated to specific projects from CEF will become clear on the basis of the project assessment results after the calls for proposals. Thus, nobody can say for sure before the end of the last call for proposals how much money will be allocated to certain projects, as it depends on the competition of the projects applying for co-funding.

[20] See also the 2017 overview of the National Audit Office.

[21] Commission Implementing Decision of 26 October 2018 on the Rail Baltica cross-border project on the North Sea-Baltic Core Network Corridor, Brussels, 26 October

Are there scenarios in case the co-funding by the EU decreases or the cost of implementation of the project increases?

36. The Government of the Republic has not been presented with any scenarios that could be followed if the implementation of the project ended up costing more than planned or if the European Union funding was lower than the expected 85%. The support of the European Union may decrease if the Member States decide to change the requirements for co-funding the facility or terminate the facility altogether in the negotiations concerning the funding period, or if the decision made upon the assessment of funding applications is to allocate less support to the project than expected. The project may also end up costing more if the activities agreed in the Grant Agreements cannot be implemented within the agreed scope and schedule and/or with the agreed budget.

37. The cost-benefit analysis of 2017 includes a forecast of the size of self-financing in the case of different EU co-funding intensity. It sets out the amounts the state would have to pay itself if the EU co-funding drops to 80, 60, 40, 20 or 0 per cent. The Ministry of Economic Affairs and Communications responded to the query of the National Audit Office that it has prepared a project funding forecast for the period from 2019 to 2022 for itself, where the different co-funding intensities have been considered and which is updated twice year – when the state budget strategy is updated and when the state budget is prepared. However, neither the MEAC nor the Ministry of Finance have analysed whether the state has the money to cover the funding of the project in the case of the scenarios highlighted in the forecasts.

38. Funding forecasts in Latvia and Lithuania, where the situation is similar to the one in Estonia, are also covered in the international Joint Audit.

39. According to the explanations of the Ministry of Economic Affairs and Communications, the intergovernmental agreement includes the agreement that if the European Union aid decreases, the governments of the three states must decide together whether and how to proceed with the project. According to the MEAC, it is most likely that the decision made in this case is to build the railway anyway, as the Baltic States are obliged to this with the TEN-T Regulation and the European Commission Implementing Decision made on the basis thereof, but it will be done over a longer period of time.

How does Estonia fund the implementation of the project?

40. The MEAC funds the RB project from the state budget and EU co-funding is also paid into the state budget of Estonia. The pay-outs are made on the basis of the applications submitted by Rail Baltic Estonia OÜ.

41. The MEAC also finances the ineligible activities of RBE from the state budget by making contributions to Rail Baltic Estonia OÜ. Ineligible activities are activities not co-funded by the EU, e.g. the risk analysis procurement that was in the procurement sample of this audit.

42. The MEAC also has to fund a third of the self-financing of the RBR's activities, which will be allocated as share capital contributions via RBE

2018. Accessible at: http://www.railbaltica.org/wp-content/uploads/2018/10/c-2018-6969-rail-baltica.pdf.

to RBR. 7.59 million euros have been paid into the share capital by now, 3.90 million of this to RB Rail AS.

What is the opinion of the National Audit Office?

43. Long-term options of financing the project have not been thought through and a more detailed project funding forecast has not been prepared in the state in case the state doesn't have the money required for the self-financing or if it becomes clear during the implementation of the project that the co-funding received from the EU is not as much as expected. As the implementation of the Rail Baltic project is funded by the CEF according to activities on the basis of applications in the different budget periods of the EU, there is no certainty about the volume in which and the intensity at which it is possible to obtain EU co-funding until the completion of the railway.

44. In the opinion of the National Audit Office, the lack of forecasts may lead to the situation where the implementation of the project may stall because of funding. This in its turn may cause shifts in the project schedule, which will also increase the cost of the project.

45. As the costs of the RB project will increase considerably when the construction of the railway starts, the National Audit Office finds it important to think through a longer funding forecast during the preparation of the 2021-2024 state budget, incl. an action plan in case the EU co-funding is smaller than expected or the cost of the project increases, in order to implement the project without disruptions.

More attention should be given to adherence to the budget and schedule of the project

Criterion 2: The National Audit Office presumed that the Rail Baltic project has been implemented according to the agreed schedule and budget until 2019.

How has the project schedule been adhered to until now?

46. The projected cost of the activities of the three CEF Grant Agreements as of April 2019 according to the Action Status Reports (ASR) submitted to the European Commission[22] is 6.2% or 59.1 million euros more than planned in the agreements[23]. The activities of CEF Grant Agreement I exceeded the budget by 59.3 million euros. According to the reports, the cost of the activities for which Estonia is responsible[24] will increase by an estimated 13.9% or 31.7 million euros in comparison with the costs specified in the agreements.

[22] The action status reports concerning the implementation of the activities specified in the CEF agreements submitted by RBR to the European Commission and the Innovation and Networks Executive Agency (see also Annex C).
[23] The fact that the cost forecast of some activities had decreased has also been taken into account in the calculations. The forecast of the cost of the activities specified in the CEF Grant Agreements covers both EU co-financing and the self-financing by the states.
[24] The state of Estonia, i.e. the MEAC, is responsible to the European Commission for completing these activities on time and according to the budget, although the explanatory memorandum to the project management and control system states that procurements for the implementation of these activities may also be carried out by RBR or RBE (and the Road Administration, the Land Board or Elering on the basis of the authorisation granted by the MEAC).

47. Among the activities for which Estonia is responsible, the projected cost of the activities not yet completed, such as the construction of the Pärnu and Ülemiste passenger terminals, has increased the most. However, the final price of the four activities for which Estonia is responsible that were completed as at the end of 2018 proved to be 149,000 euros less than agreed in the CEF Grant Agreement.

48. According to the MEAC, the construction solutions of the railway and terminals have become more detailed as a result of projects and surveys. This means that the money required for an activity and the increase in market prices could not be precisely assessed when funding was requested from CEF, which is why too little money was requested for some activities.

49. According to the CEF Grant Agreements, it’s impossible to get more money for the implementation of all of the activities of a Grant Agreement than the total amount of the cost of the activities specified in the agreement. This in its turn means that if the activities end up costing more than planned in the agreements, the states must cover the additional costs.

50. However, Grant Agreements can be amended by agreement of the parties, and the activities can be divided into several stages in justified cases, and money for financing the next stages can be requested from the future calls for proposals of CEF. For example, the implementer of said project in Latvia has requested the division of the design and construction activities of the railway intersection in the centre of Riga into several stages and funding of the next stages via future calls for proposals of CEF. The National Audit Office notes that if the European Commission does not agree to such amendment of the agreement, the states will have to cover the cost increase themselves.

51. According to the CEF Grant Agreements, money can be reallocated between the activities of a single agreement. This means that if the implementation of an activity costs less than planned, the remaining money can be used to cover the increase in the cost of another activity.

52. According to the Ministry of Economic Affairs and Communications, it is also possible to change the scope of the activities agreed in CEF Grant Agreement I to some extent. As the forecast of the cost of CEF Grant Agreement I was based on the draft of the county plans and the content of the activities has become considerably more detailed after the preparation of the preliminary design, it is also clear which activities have to be performed and to what extent. This means that, for example, in the first stage of bridge construction, the state may decide to build two more expensive bridges instead of the planned 10 bridges whilst still using all of the money allocated for the activity.

Is the final cost of the implementation of the project known?

53. The forecast of the final cost of the Rail Baltic project becomes more detailed after the completion of each study and activity, and the actual cost will become clear after the performance of the public procurements organised for the implementation of the activities and the contracts awarded as a result of the procurements.

54. For example, the preliminary design of the Estonian section of Rail Baltic was completed in late 2018 and the MEAC specified the budget of the Estonian section of the project on the basis of this.[25] In the opinion of the Ministry of Economic Affairs and Communications, the state of Estonia must pay 7 million euros a year more than planned according to the cost-benefit analysis for the construction of the railway from 2019-2025. The new budget according to the new forecast, which the MEAC also introduced at a cabinet meeting, is *ca* 1.6 billion euros or 18% more than the earlier budget of the preliminary design and the cost-benefit analysis prepared on the basis of the materials of county plans[26].

55. The self-financing by the state of Estonia in the project according to the new forecast is 318 million euros instead of the earlier 269 million euros, i.e. 49 million euros more than initially planned.

Did you know that

the European Court of Auditors highlighted in its audit of 2018 that all of the audited high-speed railway lines ended up costing over 25% more than planned. Costs increased as a result of the failure to meet the deadlines of the projects as well as inadequate preliminary research.

Source: Special Report No 19/2018 of the European Court of Auditors: A European high-speed rail network: not a reality but an ineffective patchwork

56. According to the materials submitted to the cabinet of ministers, the increase in the expected cost of the project arises from the specification of the technical solutions. The most significant differences between the two budget forecasts are related to the construction of local access roads, bridges and tunnels, in the case of which additional roads have been added on the basis of the requests of local governments.

57. The cost forecast of the project also increased as a result of the consideration of the military mobility requirements in all three Baltic States, which in the case of Estonia was 20 million euros. The cost of the works related to the construction of the railway and the forecast of the costs related to land reclamation and crossings with utility lines were also increased. However, the need for mineral materials and the estimated cost of the acquisition of land were reduced in the budget of the preliminary design.

Consolidated procurement – the procurement that is carried out by RB Rail AS on behalf of the other project parties in order to achieve efficiency by way of joint procurements and a lower price as a result of economies of scale. There are plans to carry out a consolidated procurement for construction materials.

58. In the opinion of the MEAC, the budget of the project can be cut by 150 million euros by lowering the requirements for the materials and organising consolidated procurements. During the preparation of the detailed technical designs from 2020-2021, the MEAC plans to consider, for example, lowering the track bed, partial replacement of fences that prevent wild animals from reaching the track with ultrasonic repellents and lowering the quality requirements for gravel ballast, guaranteeing thereby that the agreed general parameters do not change and there will be no conflict with the baseline documents already in effect, such as county plans and the strategic environmental impact assessment.

59. In the memo presented to the cabinet of ministers on 11 October 2018, the Ministry of Economic Affairs and Communications noted that the specification and slight fluctuations of the project budget in the planning and design stages are common in the case of such big projects. According to the Ministry, a more accurate forecast of the entire project and the budget of the Estonian section will become clear after the detailed technical designs of all railway sections are ready, i.e. in 2021 according to the schedule of the Implementing Decision of the European Commission (see point 64).

[25] Press release of Rail Baltic Estonia OÜ of 12 October 2018. See https://rbestonia.ee/pressiteated/valminud-rail-baltica-eelprojekt-tapsustab-eesti-loigu-toomahtusid/.

[26] A preliminary design has not been prepared in Latvia and Lithuania, which means that the forecast of the cost of the Latvian and Lithuanian sections of the project have not been updated.

What is the time schedule of the project like?

60. According to the intergovernmental agreement made in 2017, train traffic on the Rail Baltic railway will start in 2026. Interim deadlines have also been established in the CEF Grant Agreements and the shareholders agreement of RBR[27]. Most of the previously established interim deadlines have been met so far.

61. For example, according to the shareholders agreement, the detailed technical design of the entire railway was supposed to be completed by the end of 2017 (on 30 September 2018 according to the CEF Grant Agreement entered into in 2015). The preliminary design of the entire Rail Baltic, which is the basis for the preparation of the detailed technical design, was completed by late 2018. According to the MEAC, the detailed technical design will be completed by the end of 2021 according to the current schedule.

62. The general schedule of the project[28] was updated for the last time with the Implementing Decision of the European Commission of 26 October 2018[29]. The final deadline of the project was not changed with the Implementing Decision, but new interim deadlines were set. The first new interim deadlines established in the Commission decision were in late 2018. Two of the three activities with a deadline in the end of 2018 had been completed by September 2019: the preliminary design of the entire railway and the infrastructure management study. The environmental assessment, which should have been completed in all three states by now, has not been completed according to the interim reports submitted to the European Commission.

Infrastructure manager – an institution responsible for the efficient traffic management and safety on the railway, which keeps the railway in order, and develops the railway and other infrastructure. Eesti Raudtee AS is the biggest railway infrastructure manager in Estonia. As RB is a cross-border project, the parties must decide whether the project will continue with a cross-Baltic single manager, who can be, for example, RB Rail AS, or whether each state will have its own infrastructure manager. The third option is to create an intermediate system, where the railway section in Lithuania would be managed by Lithuanian Railways and the Estonian and Latvian sections by RB Rail AS or a new company established for this purpose.

63. The next deadline according to the Commission decision was in June 2019, when the states should have reached an agreement about the infrastructure manager, but no agreement was made by this deadline. The detailed technical designs should be finished by the end of 2020 in respect of all railway sections other than the northern and southern sections in Latvia, and the section between Kaunas and the Lithuanian-Polish border. Construction in Estonia, Latvia and Lithuania should also be under way.

64. The acquisition of land should be finished in all three Baltic States and the detailed technical design of the entire Latvian section should be completed by the end of 2021. The construction of the railway and the installation of the railway traffic management system should be completed by the end of 2025.

65. In the opinion of the project parties[30], the most accurate schedule of each project activity is determined in the CEF Grant Agreements (see the activities in Figure 5). According to the CEF Regulation, the European

[27] The shareholders agreement of RB Rail AS made between Rail Baltic Estonia OÜ, UAB Rail Baltica statyba and SIA Eiropas Dzelzceļa līnijas in October 2014.
[28] The overall schedule of the project covers the most important stages, which may include several activities of the CEF Grant Agreements and activities for which co-funding has not yet been requested.
[29] Commission Implementing Decision of 26.10.2018 on the Rail Baltica cross-border project on the North Sea-Baltic Core Network Corridor. Brussels, 26 October 2018. See http://www.railbaltica.org/wp-content/uploads/2018/10/c-2018-6969-rail-baltica.pdf.
[30] Responses of RB Rail AS to the questions of the National Audit Office and the interview with the MEAC.

Commission has the right to reclaim the money from Member States if an activity has not been initiated two years after its planned end.

66. The period during which the co-funding of the European Union can be used is also highlighted in the CEF Grant Agreements. If the project parties are unable to use the money within the given deadline, the Commission will reclaim the unused funds. According to the CEF Regulation, it is possible to request the option to use the CEF grant during a longer period with good reason.

How is adherence to the project deadline monitored?

67. At the request of the European Commission[31], RBR started using a diagram that visualises adherence to the schedule of the global project in 2018 in order to gain a better overview of the project and monitor the activities set out in the CEF Grant Agreements more efficiently. The diagram allows the parties to monitor changes in the schedule and make comparisons between initial plans and the deadlines of the CEF Grant Agreements.

68. RBE confirmed in the interview that each project manager updates the internal schedule if changes occur in the project. Based on this, RBR and the implementing bodies of the states update the diagram of the entire project at least twice a year.

How has the schedule been adhered to until now?

69. The National Audit Office analysed the activities agreed in the CEF Grant Agreements on the basis of the ASRs of the project and found that the implementation of several activities has been delayed. As at the start of 2019[32], the launch of 22 of the 71 activities of the Rail Baltic project and 12 of the 27 Estonian activities[33] agreed in the CEF Grant Agreement had been postponed.

70. The initiation of the entire project as well as the activities for which Estonia is responsible are more than a year behind the deadline on average[34]. The initiation of the activities for which Estonia is responsible is behind schedule the most. The design of the rolling stock maintenance depot was delayed by more than two years and three months. The construction of the track bed and the Ülemiste and Pärnu passenger terminals, which was supposed to start in January 2019, but has been postponed until 2021, is also behind schedule.

71. The actual or projected deadline of 57 of the 71 activities of the entire project and 23 of the 27 Estonian activities had also been postponed. The final deadlines of the activities of the entire project are behind schedule by more than 1,5 years and Estonian activities by more than 2 years. For example, the new deadline of two activities of CEF Grant Agreement I –

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[31] "Towards an Integrated Project Delivery Organisation. A package of Measures." Resolution of 21 June 2018 of the steering group of the project formed in October 2017 for prevention of further delays and more efficient implementation of the project.
[32] The action status reports concerning the implementation of the activities specified in the CEF agreements prepared in April 2019 and submitted by RBR to the European Commission and the Innovation and Networks Executive Agency.
[33] The state of Estonia, i.e. the MEAC, is responsible to the European Commission for completing these activities on time and according to the budget, although the procurements for the implementation of these activities may also be organised by RBR or RBE (and the Road Administration, the Land Board or Elering on the basis of the authorisation granted by the MEAC) according to the management and control system.
[34] The fact that some activities follow the schedule or are ahead of the schedule has also been taken into account in the calculations.

the construction and construction supervision of Ülemiste and Pärnu passenger terminals – is 2025. However, the deadline for using the money of CEF Grant Agreement I is 2020 (see also Annex A).

72. The main reasons why the activities of Estonia and the entire project are late given in the reports are delays in preceding activities. According to the MEAC, the delays in the initiation of the construction of the main route corridor and passenger terminals are mostly the result of delays in design activities.

73. RBE added that the preparation of the activities of RBR – design guidelines and the exploitation plan – have had the biggest impact on the schedule. The first of these determines the design and therefore also the terms and conditions of the construction procurements, and the second the preconditions of building the terminals. The failure of procurements due to the strict qualification requirements and lack of competition is also a problem.

74. The timely implementation of the entire project depends on the implementation of the activities of Estonia, Latvia, Lithuania and RBR at the same time. The project coordinator, RBR, constantly updates the schedule diagram of the global project, as new information and implemented activities have either a positive or negative impact on the schedule. Three possible activity implementation scenarios for a better management of the project had been set out in the schedule diagram as at June 2019. The first of them is the basic scenario, the second one considers the accessibility of EU co-funding and the contributions of the states, and the third also takes into account the forecasts of the updated schedules of the activities.

75. The probable risk highlighted in the schedule in June is that the project will not be completed by the agreed deadline. The earliest time by which the entire Rail Baltic project will be completed according to the scenarios is June 2028. However, no time scenarios have been officially confirmed in the format of a new schedule.

76. According to the Ministry of Economic Affairs and Communications, the parties to the project are making every effort to complete the project by its deadline, i.e. 2026. This means that the stage of construction must be started as fast as possible and from the railway sections and structures the building of which can already start. For example, the Road Administration and RBE have entered into the first contract for the construction of the collectors and road bridges on the crossing of the railway and the Tallinn roundabout as part of the Rail Baltic project.

77. The Supervisory Board of RBR has also asked the Management Board to prepare an acceleration plan, which should determine the activities necessary for completing the project on schedule. This plan was not ready by the publication of the report and the National Audit Office could not review it.

78. As the European Commission has the right to reclaim the money for activities that have not started, the project parties have requested and received the consent to amend CEF Grant Agreement II. Two railway and signalling system installation activities for which Lithuania is responsible have been excluded from the agreement with the amendments, as the parties cannot complete them according to the given schedule.

79. In August 2019 the project parties submitted an application to the EU Innovation and Networks Executive Agency (INEA) for an extension in using the money received on the basis of CEF Grant Agreement I. According to RBR, extension of the activities related to design, construction and land acquisition until 2022 will be requested. According to the Ministry of Economic Affairs and Communications, the project parties will have to start repaying the money requested for uninitiated activities if the INEA refuses to extend the deadlines of CEF Grant Agreement I. This in its turn means that in the next funding round, the Rail Baltic project would have to compete for the money again with other pan-European infrastructure projects.

What is the opinion of the National Audit Office?

80. The audit of the National Audit Office indicated that delays have occurred in the implementation of activities and the cost forecast of some activities have increased. If the activities are not implemented at the right time, the European Commission has the right to reclaim the unused money. Although the activities agreed in the Grant Agreements can be divided into stages (see point 50), this would increase the dependence on future EU co-funding measures, where money must be requested again for the other stages of the same activity.

81. Activities can be divided into stages only by agreement with the INEA. If the INEA refuses to divide the activities into stages, the money for these activities will have to be found from the self-financing by the states. Also, implementing an activity later than planned increases the risk that construction of the railway becomes more expensive, as the people working for the project must be paid for their work for a longer time and it is impossible to forecast how the world market prices, incl. the prices of construction works and materials, will change.

82. In the opinion of the National Audit Office, there are several reasons why the implementation of the project is not going according to the schedule and the budget. On the one hand, this is caused by the complexity of reaching agreements between the states. On the other hand, the National Audit Office found that there is room for development in the activities of the institutions implementing the project and their internal control systems. The efficient functioning of internal control systems contributes to the successful implementation of the project.

83. In the next chapter, the National Audit Office has covered the structure and effectiveness of the internal control of the Estonian part of the project and pointed out the possibilities for its development. The effectiveness of the internal control of the entire project, incl. RB Rail AS, is covered in the report of the international Joint Audit.

84. Recommendations of the National Audit Office to the Minister of Economic Affairs and Infrastructure and the Minister of Finance:

- to develop schedules and funding scenarios regarding the completion of Rail Baltic during the preparation of the state budget strategy for 2021-2024 in case the co-funding by the European Union decreases and in case the project turns out to be more expensive than planned. This makes it possible to consider the impact of the Rail Baltic project on the state budget better during its preparation and guarantee that the money necessary for the implementation of the project is there at the right time;

- to introduce the schedules and funding scenarios to the Government of the Republic and submit them to the Riigikogu as annexes to the state budget strategy or to find another suitable way for introducing the schedules and scenarios to the Riigikogu so they can be considered when budget policy decisions are made.

Response of the Minister of Economic Affairs and Infrastructure: the National Audit Office repeatedly criticises the MEAC and the Ministry of Finance (MF) for planning the funding of the Rail Baltic in detail only in the state budget strategy and the annual budget, i.e. for four years in advance. The National Audit Office finds that the MEAC and the MF should prepare detailed funding scenarios and forecasts for Rail Baltic up to the end of the project and submit them as annexes to the budget strategy. In the opinion of the National Audit Office, this makes it possible "to guarantee that the money necessary for the implementation of the project is there at the right time".

The MEAC explains in response that the recommendations made by the National Audit Office are questionable from the viewpoint of the state budget planning and preparation principles established by laws and regulations, incl. the principle of universality of the state budget, and compliance with them may breach the principles of materiality and the financial competencies of the Riigikogu. Also, complying with the recommendations may not help to guarantee that "the necessary money is there at the right time". Moreover, compliance with the recommendation may create the situation where the support to the Estonian section of the project from the Connecting Europe Facility (CEF) of the European Union will decrease.

The Supreme Court en banc emphasised in its Ruling No 3-4-1-6-12 of 12 July 2012 that "financial competence gives the Riigikogu the right to make choices regarding the state budget and decide on proprietary obligations. Due to the principles of materiality, the financial competence of the Riigikogu binds the Riigikogu to the obligation to make the decisions concerning the state's proprietary obligations and the budget policy."

As stated above, the Riigikogu ratified the agreement for the development of the Rail Baltic / Rail Baltica rail connection entered into between the Government of the Republic of Estonia, the Government of the Republic of Lithuania and the Government of the Republic of Latvia with an act of 19 June 2017 (IGA). In the IGA, the three Baltic States assumed the obligation to establish a railway with a 1,435 mm gauge track and do it with the co-funding from the CEF to the biggest extent possible whilst being prepared to contribute money from the state budgets as well (see articles 11 and 14 of the agreement). By ratifying this agreement, the Riigikogu assumed a proprietary obligation for the state of Estonia to guarantee the funds for the completion of the RB railway in any case (see the reason for ratification given in the explanatory memorandum to the IGA) by reserving themselves the right to extend the completion deadline of the project in cooperation with the other project parties, etc., should the EU funding decrease (see article 14).

The cost of completing the construction of the Rail Baltic railway in Estonia according to the preliminary project of the Estonian section of RB made in October 2018 is *ca* 1.59 billion euros. We will review the construction cost again when the detailed technical design of the railway is completed in 2022 at the latest, and the target is to reduce the costs in such a manner that the main parameters of the railway remain the same as agreed before, and the compliance of the railway with the interoperability specification and the restrictions arising from the established plans (incl. environmental requirements) is guaranteed.

The Riigikogu also assumed a financial obligation of the same scale as the cost of RB when it ratified the foundation agreement of the European Stability mechanism (hereinafter: the ESM) on 30 August 2012. The difference between the financial obligations related to the ESM and the establishment of the Rail Baltic railway lies, among others, in the fact that the costs are spread across several years in the case of Rail Baltic, whilst in the case of the ESM, the state of Estonia was and still is threatened by the obligation to pay *ca* 1.1 billion euros as a lump sum into the ESM upon the materialisation of the risks arising from other countries, which Estonia does not control, and to make this payment from the state budget funds alone (not in combination with EU aid). In the case of the ESM, the Supreme Court deemed it permissible that the Riigikogu assumes such a financial obligation in advance (see Supreme Court en banc Ruling No 3-4-1-6-12 of 12 July 2012). Although the Supreme Court instructed the Riigikogu and the ministries quite a lot in the ruling, it never suggested that when assuming an obligation or due to the general budgeting process, the state should plan how Estonia intends to perform the obligation, including how it intends to finance it.

Moreover, the Supreme Court explain in said ruling that “the Riigikogu has the right to assume proprietary obligations as well as the right to decide on how and with which funds the obligation will be performed. Several manners of performing an obligation may comply with the Constitution. The court’s duty is not to tell the legislator how the Riigikogu should perform the obligations assumed for the state.”

In other words, the Supreme Court said that the financial competency of the Riigikogu consists of different competencies: a) the right to assume a financial obligation; and b) the right and the obligation to decide on how the obligation will be performed. The Supreme Court deems these competencies the core competencies. In the case of RB, the Riigikogu has already assumed the obligation and the current dispute concerns the performance of the obligation.

Pursuant to § 104 clause 11) and § 117 of the Constitution, determining how the performance of the financial obligations assumed for the state is planned in Estonia is within the sole competence of the Riigikogu. The Riigikogu has established the procedure for planning the performance of the obligations assumed for the state, including the long-term planning procedure, in the State Budget Act (SBA), which is a constitutional act (its adoption requires a majority vote in the Riigikogu). The Riigikogu has decided that the state of Estonia plans the performance of the proprietary obligations assumed in the state budget strategy and the annual state budget, and the state budget strategy is prepared for four years according to § 21 of the SBA and the aforementioned regulation of the MF.

Clear principles must also be followed upon the preparation of the state budget, one of which is the principle of universality. This means that the single revenue and expenditure items of the state budget do not depend on each other (see also the comment to § 115 of the Constitution, www.pohiseadus.ee). Thus, the intended use of the state budget revenue has generally not been determined, i.e. the revenue as a whole is meant for financing the expenditure as a whole.

The National Audit Office advises the MEAC and the MF to start preparing spreadsheets, which would indicate the hypothetical scale of the self-financing by Estonia of the establishment of RB after five to seven years and how the state plans to fund such a hypothetical obligation over a budget strategy period, and the National Audit Office thereby advises to submit such "funding scenarios" that exceed the budget strategy period as an annex to the budget strategy prepared for four years.

The Supreme Court emphasised that deciding on how to perform the financial obligations assumed by the Riigikogu, incl. the obligations related to the financing of RB, is within the sole competence of the Riigikogu. The Riigikogu has decided that as a rule, this will be planned for four years in advance. This planning period is not random, but based on the facts that planning highly specific funding needs and sources for longer periods is difficult because of changes in critical circumstances and that the Constitution does not permit depriving future compositions of the Riigikogu of the opportunity to plan the budget. Budget planning also means a more specific planning of the performance of financial obligations, e.g. whether to finance an obligation from the state's tax revenue, a loan or a bond issue. Planning the measures for the implementation of the budget for years in advance on behalf of the future compositions of the Riigikogu is not justified.

Also, such specific planning of the revenue and expenditure of the RB project would be in contravention of the principle of the universality of the state budget (see above). The Supreme Court emphasised that the duty of the court and consequently of the executive and constitutional institutions is not to tell the legislator how the Riigikogu should perform the obligations assumed for the state. The MEAC cannot start telling the Riigikogu with an additional spreadsheet which source could be used to cover the self-financing of the construction of RB in 2025. As this spreadsheet recommended by the National Audit Office could never be binding, it would not have a substantive meaning or oblige anyone to act according to it, or contribute to the goal of guaranteeing the existence of the money in 2025, for example. The recommendation of the National Audit Office is basically a general proposition for amendment of the SBA and the budgeting principles, including the principle of universality, and it is not specific to the RB project.

The guarantee that the money for the establishment of RB exists in 2024 and thereafter is given by the fact that in 2017 the Riigikogu assumed the obligation to complete the construction of Rail Baltic irrespective of what the rate of the specific self-financing of Estonia is. Pursuant to § 21 of the SBA, expenditure is planned in advance more specifically by four-year periods and in detail in the annual state budget. Thus, it is within the competency and the obligation of the Riigikogu composition of the respective years to find the funds for the establishment of RB. The MEAC and the MF have performed all of the obligations stipulated with the Constitution and acts in relation to planning and guaranteeing the funding of RB. The MEAC has also performed the additional obligation assigned by the Riigikogu with the ratification of the IGA and presents a detailed overview of the RB sites of the next year and their costs as an annex to the annual budget and it also informs the Economic Affairs Committee of the Riigikogu about the status of the establishment of RB separately every year.

The MEAC also notes that the total income and expenses of the RB project have been calculated and all of the cost-benefit analyses of RB across all years have been prepared. The possible expenses of RB are thoroughly assessed and planned when the budget strategy is prepared and updated on an annual basis. Similar to other projects with foreign financing, the Grant Agreements already entered into (the CEF Grant Agreements in the given case) are reviewed in the case of RB when the state budget strategy is prepared and the potential budget volumes of the subsequent CEF calls for proposals, the estimated proportion of the RB project in the total volume of grants of the call for proposals and the financing required for the implementation of the Estonian activities are considered. As pursuant to the IGA, the funding of RB is planned, among others, from the CEF in two EU funding periods (2014-2020 and 2021-2027), then we have forecast since 2017 that the costs related to the implementation of RB will be covered also from the next EU budget periods. Submitting specific figures and sources of money for longer than four years is difficult and also impractical, because the changes in the various presumptions as a result of several parallel processes (incl. negotiations between Member States and with the European Parliament, the dependence of the schedule of RB and the investment expenses on the probability of the materialisation of various risks, etc.) change such forecasts. The MEAC and the MF monitor and update these forecasts all the time.

The MEAC also points out that the recommendation of the National Audit Office may reduce the possibilities of getting EU aid for funding RB. Making new official decisions concerning funding alternatives (e.g. by the Riigikogu) would jeopardise getting grants from the CEF. In a situation where the expenses of RB could have largely been covered with other funds in addition to the CEF grant and the required self-financing according to the approved document, the INEA would have no reason to approve applications for the grant, as the existence of financial resources outside the CEF grant would make the allocation of EU grants in the requested amount and at the requested intensity unjustified. The point of EU grants is to finance the achievement of the results of such projects that are necessary in the common interests of the EU, which would otherwise not be achieved due to the lack of financial resources/funding options.

In terms of the schedule of RB, the Baltic States have agreed on the completion deadline of RB in the IGA and the binding deadlines are also set by the implementing decision of the European Commission. The duty of the project implementers is to adhere to said deadlines. The updating of details requires negotiating amendments to and amending of the aforementioned documents by the parties, which is not currently planned, as the parties find that the schedule can be adhered to.

In the case of the schedule of RB, it is important to separately view the final deadline for the completion of RB (or its Estonian section) and the activities to be carried out within the scope of the CEF Grant Agreements entered into by now and the agreed completion deadlines. In the case of CEF Grant Agreement I, there are delays in the initiation of activities as well as the established final deadlines in all of the states involved in the RB project. Considering the type and scope of implementation of the planning and design processes (e.g. the inclusion of local governments and residents etc.), it is not surprising that the circumstance affecting the implementation of the project activities (incl. cost, deadlines) may change to certain extent as new circumstances become evident (e.g. the establishment of spatial plans, the completion of the preliminary design, the completion of the detailed technical design). However, this does not automatically mean that the final deadline of the project will be postponed. It’s important that the changes in circumstances would not bring about the materialisation of possible risks, such as repayment of the funds allocated with the CEF Grant Agreements. The materialisation of this risk was not evident in the case of any of the CEF Grant Agreements in October 2019. Firstly, the project partners are looking for and have found possibilities to ensure that the delay in the full completion of the detailed technical design would not lead to the postponement of the construction deadlines – for this purpose, we will carry out the design works by sections and priority subsections, so that the building permits can be issued and the construction of specific sites can start immediately after the completion of the project documents of the respective site or subsection. Secondly, the duration of the CEF Grant Agreements can be expanded for certain reasons and to a certain extent, activities can be re-planned, etc. by agreement with the INEA considering the achievement of the final objective of the project, which is important from the viewpoint of the common interests of the EU and the states – the completion of a new railway connection. Therefore, an amendment to CEF Grant Agreement I will be signed in November 2019, which among others concerns the extension of the eligibility deadline of the costs required for the implementation of the activities specified in the agreement. We also specified the scale of the activities within the scope of the same amendment, e.g. we divided the construction works of the Pärnu and Ülemiste passenger terminals into stages, which makes it possible to start the works before 2022, but finish them from 2023 by including additional CEF funds.

Comment of the National Audit Office: in the opinion of the National Audit Office, preparing the project’s budget forecast for a longer time does not restrict the financial competence of the Riigikogu. In its overview of 2017, the National Audit Office made the following recommendation about the agreement for the development of the Rail Baltic rail connection made between the governments of Estonia, Lithuania and Latvia: ask the government to submit an analysis and action plan for funding Rail Baltic. The National Audit Office pointed out that the Riigikogu should know the answers to at least the following questions: How big is the financial obligation that will be assumed for the state? How will the project be financed? Has a clear decision-making mechanism been agreed in case the project ends up costing more than planned, is not completed by the deadline or there are changes in funding? The role of the government is to guarantee that the Riigikogu would have all of the information necessary for making decisions. The longer project funding forecast and scenarios recommended in this audit could therefore be the input for the preparation of the state budget and the state's budget strategy if necessary.

Response of the Minister of Finance: in the opinion of the Ministry of Finance, the claim made in point 33 of the report of the National Audit Office that there is no funding forecast for the most expensive period of the project is justified with the lack of national political intent and an international agreement (point 24) for continuing the project in the case of larger self-financing. The Ministry of Finance considers the funding mechanism described in point 25, which does not guarantee continued funding from the EU even if the activities until then have been appropriately completed, a major risk factor. The inadequate project management and delays mentioned throughout the report of the National Audit Office obviously decrease the possibilities of applying for funds successfully. According to the coalition agreement, guaranteeing EU funding to the extent of 81% is the precondition to continuing with the project, but it has not been met according to the description in this point.

According to the explanation given in point 32, the funding forecast for the Rail Baltic (RB) Project is officially not prepared for a longer period (e.g. longer than the period of the state budget strategy, i.e. the SBA), as this is not required by Estonian law. There is no reason to doubt that self-financing to the extent of up to 19% of the construction costs will be found in the state budget in the coming years. The problem presented in point 36 that there are no scenarios that could be implemented if the amounts to be allocated from the budget of Estonia would have to be considerably larger than planned for now, must be regarded as a considerably more serious problem.

In the opinion of the Ministry of Finance, scenarios concerning the possibilities and impossibility of continuing with the project in the case of different visible developments should be prepared before the project is continued. The decrease or termination of EU aid and the increase of the project costs and delays must also be taken into account. Postponing such agreements until the time when the risks have already materialised is not responsible risk management.

The Ministry of Finance finds that if EU support to the implementation of the RB project ends up being smaller than expected, the socioeconomic cost-effectiveness, reasons and track selections of the entire project would have to be thoroughly checked again. The project parties must negotiate and agree on a new, amended schedule for the implementation of the project or suspend the project, because it's highly likely that the Baltic States would be unable to finance the implementation of the project from their budgets if the participation rates and volumes differed significantly from the ones highlighted in the cost-benefit analysis. The opinion of the Ministry of Economic Affairs and Communications that the railway will be built even without European Union support presented in point 39 must be regarded as groundless.

The Ministry of Finance finds that different scenarios must be developed and agreed nationally and between the Baltic States before the biggest expenses are incurred also within the scope of the activities covered by grants until now. The National Audit Office found in point 34 that the amount that has been spent and is planned to be spent on the development of the Estonian section of the project from 2010-2022 is 276.7 million euros, which comprises 20.5% of the cost of the Estonian section specified in the cost-benefit analysis. [The National Audit Office notes that this point of the report was updated according to the state budget strategy for 2020-2023 after the report was sent out for official responses. According to the new calculations, the amount spent and planned to be spent on the development of the Rail Baltic project from 2010-2023 is 433.9 million euros, which comprises 32.1% of the Estonian section of the project highlighted in the cost-benefit analysis.] Actually, the cost of the Estonian section known today is 1.6 billion (point 54), of which the amount spent until now and planned to be spent comprises 17.3%. We consider it probable that the project will become more expensive (as you have also said in the reference to the report to the European Court of Auditors on page 15, which ascertained that the cost of all of the audited lines increased by more than 25%). The cash flow forecasts for the SBS period and a longer period can only be working materials that are based on the presumptions agreed in the Connecting Europe Facility (CEF) Grant Agreements and other related documents, incl. on forecasts based on known circumstances as well as scenarios.

In the opinion of the Ministry of Finance, the audit of the National Audit Office should also have covered the risks of financial corrections or reductions of the actual aid intensity, which may arise from the inadequate national control of the cost-benefit analyses of the project, the failure to carry out procurements properly, the delays that make procurements longer than the eligibility period or for other reasons.

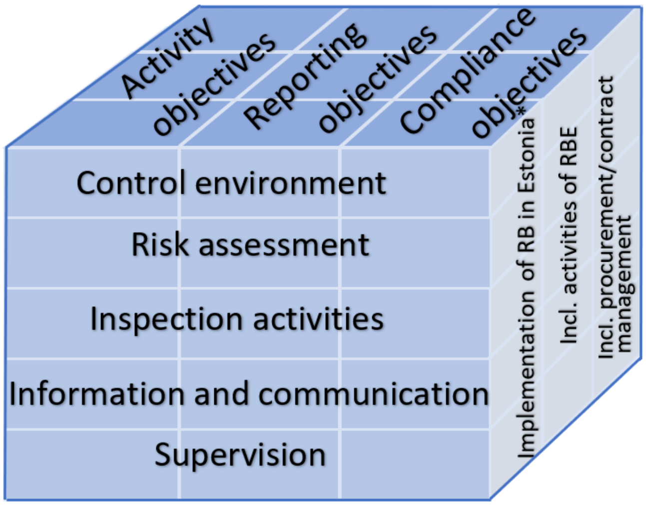
Effectiveness of the internal control system of the Estonian section of the Rail Baltic project in the organisation of procurements and management of contracts

85. According to the COSO model, an internal control system is a set of processes designed and implemented by an organisation’s management. The internal control system must guarantee the achievement of the goals set in the organisation and give the reassurance that reporting is reliable and activities comply with laws and procedures.

86. The internal control system must proceed from the organisation’s goals and start from the establishment of the environment required for the achievement of the goals. The risks of an activity are assessed according to its objectives and measures are set for the identification and management of risks. The rules of information flow must also be set in such a manner that the information gets to the right people at the right time.

87. Supervisory activities are also an important part of the internal control system, the goal of which is the detection of errors and assessment of the functioning of the internal control system. All of these activities are necessary for the efficient functioning of an organisation and their integrated functioning is required for the coordination of national activities, as well as in Rail Baltic Estonia OÜ (see also Figure 6).

Figure 6. Model of internal control system



* The National Audit Office assessed the activities of the MEAC and the RBE in the implementation of the Rail Baltic project in Estonia.

Source: National Audit Office based on the COSO model

88. The National Audit Office assessed the organisation of the implementation of the Estonian section of the Rail Baltic project, incl. how roles and responsibilities are divided between the parties to the project. The National Audit Office analysed the structure of the internal control system of the main implementing body of the RB project in Estonia – RBE – in greater detail and checked its functioning in the organisation of procurements and the management of contracts. The National Audit Office assessed the internal control system of the Estonian section of the RB project according to the COSO framework and used the checklists given in the guideline of the Ministry of Finance[35], which were adapted to the structure of the implementation of the Rail Baltic project.

The roles and responsibility of the project parties have generally been determined

> Criterion 3: The National Audit Office presumed that the implementers of the project, their tasks and the division of responsibility have been clearly determined in Estonia.

How are the activities in Estonia managed?

89. The MEAC has prepared a management and control system for the better coordination of the parties to the Estonian section of the project[36],

[35] Optional guideline for organisation of the internal control systems of local governments, KPMG, December 2018. https://www.rahandusministeerium.ee/sites/default/files/kov_sisekontrollisusteemi_juhend.pdf.
[36] The respective document has been approved by the Ministry of Economic Affairs and Communications with its directive of 5 January 2016.

which also includes the structure of implementation of the project in Estonia and the division of responsibilities in the implementation of Estonian activities according to CEF Grant Agreement I. According to the explanatory memorandum to the approved management and control system, Rail Baltic Estonia OÜ is generally responsible for the implementation of the national activities.

90. It is emphasised in the explanatory memorandum to the management and control system that irrespective of the delegation of tasks to RB Rail AS, the MEAC as the recipient of the co-funding is responsible to the European Commission for the timely implementation of the Estonian activities, the achievement of the results and the purposeful use of the funds specified in the Grant Agreement[37].

91. For example, funds for the design of the main route corridor of the Estonian section have been granted to the state of Estonia, i.e. the MEAC as the beneficiary, with CEF Grant Agreement I, but the Contracting Scheme for the Rail Baltic/Rail Baltica agreement states that designing is a task of RBR, which therefore carries out design procurements and enters into contracts on the basis of the authorisation of the MEAC. Also, building the track bed of the main route corridor of the Estonian section is a responsibility of the state of Estonia, i.e. the MEAC, pursuant to CEF Grant Agreement I, but the necessary procurements are carried out by RBE.

The European Commission found that

the election of the representatives of national implementing bodies (RBE in the case of Estonia) to the Supervisory Board of RB Rail AS may represent a conflict of interest, as the two companies compete for funding. As a result of a compromise of the states and the Commission, it was agreed that only one representative of the national implementing body may be on the Supervisory Board of RBR. The counsellor of the MEAC, who was on the Supervisory Boards of both RBR and RBR, has been only on the Supervisory Board of RBR since 2018.

Source: Towards an Integrated Project Delivery Organisation. A Package of Measures. Resolution of 21 June 2018 of the steering group of the project formed in October 2017 for prevention of further delays and more efficient implementation of the project.

92. In order to make sure that RBR and RBE perform their tasks related to the performance of the CEF Grant Agreements in compliance with the public procurement regulation, in a timely manner and according to the budget, the MEAC must exercise supervision of their activities.

93. According to the main implementing body of the Estonian section of the project, Rail Baltic Estonia OÜ, the activities of the company are supervised by the Supervisory Board. The Supervisory Board has five members appointed by the committee for appointment of the Supervisory Board members of public undertakings[38]. A representative of the MEAC has not been appointed to the Supervisory Board of RBE since 2018.

94. The interview with the MEAC revealed that although the MEAC receives information about the activities of RBE from the working groups established for the implementation of the project and by way of informal communication, not having a representative of the MEAC on the Supervisory Board has considerably reduced the possibilities of the Ministry to supervise the activities of Rail Baltic Estonia OÜ.

95. In addition to this, the National Audit Office found a possible conflict of interest in the exercise of supervision, which lies in the fact that the representative of the MEAC who supervises the implementation of the Estonian section of the project, including the activities of RBE, was an employee of RBE. The National Audit Office informed the management

[37] Only the first CEF Grant Agreement had been entered into at the time the management and control system was approved.
[38] Order for formation of the committee for appointment of the supervisory board members of public undertakings https://www.riigiteataja.ee/akt/326092017004.

of the MEAC about this situation and the MEAC resolved it in September 2019.

What is the opinion of the National Audit Office?

96. In the opinion of the National Audit Office, the obligations and responsibility of the parties to the Estonian section of the project have generally been described in the explanatory memorandum to the management and control system. The role of the MEAC and the exact division of tasks and roles should be specified. The management and control system was being updated during the audit, but the updated version of the document had not been approved yet.

Rail Baltic Estonia OÜ has predominantly established the internal control system of public procurements and contract management

> Criterion 4: The National Audit Office presumed that Rail Baltic Estonia OÜ has prepared the rules and guidelines for the organisation of public procurements and contract management in order to create the preconditions for the functioning of the internal control system.

What is the internal control system of Rail Baltic Estonia OÜ like?

97. According to the articles of association[39], Rail Baltic Estonia OÜ must have an effective internal control system. This is described by the brief memo prepared for the Management Board in RBE[40], according to which an internal control system has been established with rules, procedures and other guidelines effective in the organisation.

98. The National Audit Office analysed during the audit which guidelines and procedures have been established by RBE for procurements and contract management and assessed by the example of three procurements how the developed principles have been implemented in practice. The opinions of the National Audit Office on the effectiveness of the internal control system of RBE are given in the table in Annex D.

99. The audit indicated that the rules and guidelines for procurements and awarding of and management of contracts that are parts of the internal control system have predominantly been developed and established, but certain parts of the internal control system are still under development.

100. For example, the National Audit Office finds that risk management needs to be updated and more attention should also be given to the documentation of decisions. According to RBE, the shortcomings are a result of the fact that since the establishment of RBE, the company has had to organise project procurements, prepare internal procedures and perform the role of the owner of RBR at the same time. This is why some of the procedures are still being developed.

What is the opinion of the National Audit Office?

101. The National Audit Office notes that the MEAC is responsible for the implementation of the Estonian section of the Rail Baltic project, which is why the internal control system of RBE alone is not enough for the successful management of the project, but the MEAC also plays an

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[39] Articles of association of Rail Baltic Estonia OÜ, approved with the resolution of the supervisory board of 28 February 2019, https://rbestonia.ee/wp-content/uploads/2019/03/Rail-Baltic-Estonia-O%C3%9C-p%C3%B5hikiri-2019.pdf.
[40] The brief memo prepared for the management board of RBE in August 2016 on issues concerning the audit committee, internal control and internal audit.

important role in risk and change management and in the exercise of supervision.

102. The parts of the internal control system that require further development are highlighted in the following sub-chapters.

The risk management system must be updated

Criterion 5: The National Audit Office presumed that Rail Baltic Estonia OÜ has developed a risk management system and identified, assessed and implemented measures for reducing the risks of the project.

How are the risks that may threaten the implementation of the project identified?

103. The risks of the entire of Rail Baltic project were listed and assessed in the cost-benefit study prepared in 2017. According to the study, the main risks that affect the project the most are the delays in the start of construction and in the implementation of the railway, the decrease in funding and the changes in the market situation.

104. The risks of the Estonian section of the project were assessed in the risk analysis of the planning and construction phases of the Estonian section of the Rail Baltic project in 2017. The risks arising from the unclear project organisation and division of responsibility, reduction of EU funding and unsuitable procurement strategy were assessed as high. This was followed by the preparation of a risk register in RBE. The assessed risks were divided according to categories and a list of possible risk management measures was prepared. According to RBE, a risk matrix has been created and on the basis of this, the Management Board reports to the Supervisory Board about risk once a year.

105. Irrespective of the work already done, the risk management system in RBE requires further development. A risk register and working group of risks have been established and the members of the group are representatives of the MEAC, the Ministry of Finance, the Consumer Protection and Technical Regulatory Authority and the Land Board. However, it's not clear what the input of the working group to the risk management system is and what the different parties are responsible for. According to the representative of RBE, the risks in the risk register are assessed at the meetings of the working group once a quarter. No minutes are taken of the working group meetings, so it was not impossible for the National Audit Office to see how risks have been assessed.

106. It was also not evident who is responsible for each specific risk, and whether and how the parties carry out risk management activities. There are also risks in the implementation of the project that RBE itself cannot manage, which is why the MEAC and other parties to the project should be included in the risk management process.

107. The National Audit Office notes that documentation is a part of a functioning internal control system, because it makes it possible to exercise supervision and identify any shortcomings[41]. The importance of

[41] Optional guideline for organisation of the internal control systems of local governments, KPMG, December 2018,

documentation is also emphasised in the implementation of quality management systems[42] in the companies, where the achievement of results is proven via documentation.

108. The option to cover the risks of the single procurements and contracts of RBE has been created in the monthly reports prepared by the MEAC and submitted to RBR. In the case of the analysed procurements, it became evident that the reports focused on the problems that had arisen rather than on preventively assessed risks.

109. For example, the monthly reports for June to November 2018 highlighted in the case of the procurement of the study of the Muuga freight terminal that the situation at Muuga port had changed so much during the delays in the study that additional studies must be commissioned. At the same time, the risks that the delay in the performance of the contract may bring about were not highlighted in previous reports.

110. RBE explained that the risks related to single procurements and contracts were not assessed in writing before the announcement of the procurement, but the project manager assessed them as the procurement progresses.

111. The project management procedure of RBE [43] was updated during the audit and the risks related to the implementation of the project will be assessed in each stage of the project planning on the basis of this. The National Audit Office points out that in the future, it's important that the risks related to the project are also known to the MEAC, so the latter can submit correct monthly reports to RBR.

112. According to RBE, their objective is to have risk management in RB Rail AS and RBE function by the same principles. However, this has caused a delay in the selection of the final risk management system of RBE, as the risk management system of RBR is still being developed as well. According to the representative of RBE, the risk management handbook procured by the joint venture RBR and adopted in 2019 will be the basis for the further development of the risk management system. The risk manager, who will be hired by RBE in the end of 2019, will be in charge of the further development of the risk management system. The duties of a risk manager have been performed by the procurement manager until now.

Have the risks materialised?

113. The analysis of the National Audit Office, which covered three procurements and contracts, revealed that different types of risks have become evident in the organisation of procurements and management of contracts, both in the stages of preparation of procurements and management of contracts:

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https://www.rahandusministeerium.ee/sites/default/files/kov_sisekontrollisusteemi_juhend.pdf.

[42] ISO 9001:2015. Quality management systems. Requirements.

[43] For the purposes of Rail Baltic Estonia OÜ, 'project' means the separate sites of the Rail Baltic railway, such as passenger terminal, freight terminal, maintenance depot, etc., and sections of the main route of RB (the main route has been divided in three sections in the Estonian section of RB).

- the risk related to the preparation of the procurement materialised when the initial study of the Muuga freight terminal was disputed and the award of the public contract was delayed because of this;
- the contract management risk materialised when receipt of the works of the Muuga freight terminal and the railway infrastructure was delayed, as the parties related to the study were late with giving their feedback. If the need to include parties upon the receipt of the works had been assessed in advance, the time of receipt of the works could have been planned better;
- the risk arising from the unclear division of responsibility materialised when RBE and RBR failed to agree on who will be responsible for the procurement of the study of the Pärnu freight station. This in its turn caused delays in the project.

114. The materialisation of risks and the resulting need for changes has led to the procurements exceeding their deadlines. For example, the plan was to award the public contract for the study of the Muuga freight terminal in April 2016, but since the initial procurement failed, the contract was only signed in January 2017.

What is the opinion of the National Audit Office?

115. The analysis of the procurements by the National Audit Office indicated that RBE has not encountered many problems due to the failure to manage risks, as there have been few activities until now and the procurement have mostly been for studies. Also, most of the studies and works procured by RBE until now have been ones that do not have an impact on the other activities of the project.

116. As the number of the procurements to be organised will increase in relation to the construction of the railway and the terminals, and the procurements will require more time and work, using the existing risk management practice may mean that the problems and changes will not be responded to on time. This in its turn may cause delays in the project and failure to adhere to the budget.

117. The National Audit Office found that although the risks of the project have been assessed in the cost-benefit analysis as well as in the risk analysis of the planning and construction stage of the Estonian section, the risk management system has still not been fully developed. According to RBE, the risk manager who will be hired in the end of 2019 will start working on the establishment of the system. The National Audit Office also found that it’s unclear how the risks of the Estonian project that are not under the control of RBE are managed.

Change management has predominantly been carried out in Rail Baltic Estonia OÜ, but the roles and procedures should be agreed in greater detail across the project

> Criterion 6: The National Audit Office presumed that the principles of change management have been agreed and they are followed.

Which changes can occur in the implementation of the project?

118. The need to make changes that affect the course of the project, incl. the schedule and budget, may arise in different stages, e.g. if:

- a preliminary survey required for a procurement is late, it must be decided when the next procurement can be organised and the procurement plan must be changed if necessary;
- the price of the submitted tenders exceeds the planned budget and it must be decided whether the service will be ordered for a higher price or a new procurement will be organised;
- the volume and/or complexity of the works under the awarded contract and the resulting cost changes or if the contractor's performance does not meet the expectations of the contracting authority and sanctions must be implemented;
- other situations appear that require changes.

119. It should be clearly determined for all these cases who will decide on the implementation of the changes and how the changes must be documented.

How is the procurement plan changed?

120. The procurement procedure of Rail Baltic Estonia OÜ states that the company's Supervisory Board approves the procurement plan proposed by the Management Board, but it does not specify the information that the Management Board must submit to the Supervisory Board for making the decisions. The procurement plan gives an overview of the procurements planned by the company during a year and is therefore an important tool for the Management Board.

121. According to the articles of association, the approval of the procurement plan is a task of the Supervisory Board via which the Supervisory Board gives orders to the management of the company, and it's therefore important that the information given by the Management Board is up to date and accurate. However, the procurement procedure does not state in which cases the procurement plan can be changed and which information the Management Board must submit to the Supervisory Board in the case of amendments.

122. Analysing the materials submitted to the National Audit Office revealed that the amendment to the procurement plan for 2017 had been approved with a resolution of the Supervisory Board on the basis of the request of the Management Board, but the Management Board did not justify the need to change the procurement plan. The procurement plan for 2018 was approved with Minutes No 26 of the Supervisory Board, but the materials submitted to the Supervisory Board did not highlight the reasons why some of the procurements were postponed.

How are changes managed?

123. In Rail Baltic Estonia OÜ, the project manager informs the Management Board about the need to make changes in procurements and contracts. Until now, it has been done rather informally and it was impossible for the National Audit Office to identify in the case of the reviewed procurements who and on the basis of which information actually made the amendment resolutions, as no minutes were taken of the meetings of the project team with the Management Board. According to Rail Baltic Estonia OÜ, the project manager informed the Management Board about the need for amendments at the meetings held biweekly.

124. An analysis of the internal procedures and procurements of RBE revealed that the clear responsibility of the project manager in decision-making was previously missing in RBE. The interview with RBE showed that in the case of the Muuga procurement, the project manager made the proposition to impose a contractual penalty for a delay and the Management Board made the decision to impose the penalty and determined its amount. At the same time, RBE admitted that the rules for inclusion of the Management Board in such cases do not exist and in the given situation, the project management included the Management Board, because the amount was large and he wanted to get the Management Board's confirmation for imposing the contractual penalty. In the case of other procurements where fines were imposed, the amounts of the fines were smaller and the Management Board was not included.

125. The project management procedure of Rail Baltic Estonia OÜ was updated at the time of the audit and the responsibility of the project manager for change management was specified. Pursuant to the new procedure, the project manager has the right to make changes in the project that have no negative impact on the quality, budget or deadline. Otherwise, the project manager must obtain the Management Board's consent for the implementation of changes. It was impossible for the National Audit Office to analyse the efficiency of the updated procedure, as it was not in effect at the time of the analysed procurements.

126. According to Rail Baltic Estonia OÜ, another significant problem in the management of changes is that there is no official procedure for important decisions reaching the owner, i.e. the MEAC. As the MEAC is responsible for the project, it should at least know about the bigger changes to be made to the project, including any significant changes to the schedule and budget, and make decisions if necessary.

127. Until now, information exchange with the management of the ministry has been inadequate according to RBE. Although information on the status of the projects is presented to the Supervisory Board at the meetings of the Supervisory Board and minutes of the meetings are also sent to the representative of the owner, i.e. the MEAC, it's not certain whether and how the MEAC analyses the received minutes. It's also not known whether the information in the minutes reaches the management of the MEAC, which has to make decisions.

128. The steering group of the project was restored at the time of the audit. The group meets once a quarter and consists of the members of the managements of ministries, boards, public undertakings, RB Rail AS and local government associations. The main goal of the steering group is to guarantee regular information exchange between the parties to the project and the achievement of agreements at the level of management[44].

What is the opinion of the National Audit Office?

129. The audit indicated that change management has largely worked well in Rail Baltic Estonia OÜ so far, although the activities have sometimes been non-formal, i.e. the project manager has communicated with the

[44] Minister of Economic Affairs and Infrastructure Directive No 1.1-1/19-194, signed on 7 November 2019.

Management Board at his own discretion and asked for permission to make changes in the project. The project management procedure of RBE has been updated and the authorities of the project manager have also been specified during the audit.

130. The steering group of the project set up by the MEAC was also re-established during the audit. This should create the prerequisites for the important changes to the project reaching the MEAC, which is responsible for the project. The National Audit Office finds that it's important for the Management Board and the owner to have the information that allows them to decide on the steps required for keeping up with the schedule or find and implement risk management measures at the right time.

131. In the opinion of the National Audit Office, it is also important for a well-functioning internal control system that important information, incl. information concerning deviation from plans, reaches all of the necessary management levels. It's also important to document the process of changes, so that the reasons why the changes were made can be retroactively identified and the transparency of the implementation of the project, the clarity of responsibility and compliance with the Public Procurement Act can be guaranteed. Changes in the activity of the co-called critical path[45] have a particularly big impact on the progress of the project.

132. The National Audit Office notes that the Public Procurement Act includes rules that regulate the cases in which contracts may and may not be amended. The rules are necessary for the prudent use of taxpayers' money.

Supervision of the implementation of the project requires additional activities

> Criterion 7: The National Audit Office presumed that reporting and supervision mechanisms have been established for the Rail Baltic project.

Who supervises the project?

133. The beneficiary of the project, i.e. the MEAC, must supervise Rail Baltic Estonia OÜ. According to the performance agreement, the MEAC has the right to check the compliance of the circumstances that are the conditions for receiving the co-funding and the use of the funds at any time. The MEAC wants to delegate the supervision function partly to the Consumer Protection and Technical Regulatory Authority (CPTRA) with the management and control system.

134. Since the project is co-funded from the European Union budget and the state budget, the Ministry of Finance and the European Commission also have the right to check the implementation of the project. RB Rail AS may also check the activities of RBE to ensure that the project is implemented in compliance with the CEF Grant Agreement.

[45] The activities that are essential for the implementation of the project and on which the subsequent activities of the project depend.

135. The organisation of supervision of the implementation of the project is still being developed. The MEAC supervises the cost statements of RBE according to both the effective and the pending management and control systems. The MEAC explained that it prepares a report about the costs of the project on the basis of the input received from RBE once a month. The same principle also arises from the performance agreement. However, it's not clear how the MEAC checks whether RBE performs the obligations assumed on behalf of the MEAC economically and efficiently.

136. The MEAC explained in the interview that it exercises supervision by checking the eligibility of the activities of the project and participating in working meetings with the representatives of RBE in order to be aware of current issues. The MEAC also admitted that participation in the meetings is cooperation rather than supervision. The MEAC also receives information about the status of the project from the minutes of the Supervisory Board of RBE, which are sent to the MEAC as the owner of RBE.

137. Based on the document of the management and control system that was updated during the audit, but had not been approved yet, the function of the CPTRA will be to carry out preliminary inspection of procurements, but the content or format of these activities have not been agreed in greater detail yet. According to the CPTRA, the inspection will be similar to the inspection of other projects co-funded by the EU. However, the inspection procedures have not been developed yet. According to the MEAC, the CPTRA plans to develop the relevant internal procedure in autumn 2019.

What is the quality of the reports submitted about the activities of RBE?

138. The analysis of procurements by the National Audit Office also revealed that although the format of the monthly, quarterly and annual reports to be submitted to RBR has been established, the status of the activities had not been updated in the report in several instances.

139. The National Audit Office found that in the case of the procurement for the maintenance depot, the non-negotiated procedure without prior publication was covered for the first time in the report for April 2017, although the procurement was announced in January 2017. The deadline for submission of tenders specified in the monthly report was different from the one in the Public Procurement Register, the expected termination date of the contract had not been amended on time and the times of receipt of the results of stages were not correctly indicated.

140. In the case of the study of the Muuga dry port, however, the report filled in in early December 2018 still stated that the procurement should be announced by August 2018 and the contract should be signed in September 2018.

141. According to the multilateral agreements, the MEAC submits reports to RBR irrespective of the fact that the activities are carried out by RBE. According to the MEAC, it receives the information for filling in the reports from the relevant specialists of RBE. RBE does not prepare the report itself as an input for the MEAC. In the opinion of the National Audit Office, the monthly statements are an important source of information to RBR and if important problems are not covered at the right time, it is impossible to respond to them at the right time as well.

What is the opinion of the National Audit Office?

142. The audit of the National Audit Office indicated that the internal control system has largely been developed in the main implementing body of the project, Rail Baltic Estonia OÜ, and the change management procedures were updated during the audit. The risk management system still needs to be finalised, both in RBE and in the entire Estonian section of the project. There are also shortcomings in the organisation of supervision by the MEAC and the procedures of the preliminary inspection of procurements, which will be a function of the Consumer Protection and Technical Regulatory Authority, have not been developed.

143. In the opinion of the National Audit Office, efficient supervision is important for the implementation of the Rail Baltic project, as it would make it possible to identify risks and guarantee the sustainable and appropriate organisation of procurements and management of contracts.

144. In the opinion of the National Audit Office, it is also important to regularly assess the functioning of internal control, incl. supervision. The volume of construction procurements is expected to increase considerably in the next couple of years, which will result in the expansion of the company, which creates the need for assurance that the internal control system, incl. supervision, functions efficiently.

145. **Recommendations of the National Audit Office to the Minister of Economic Affairs and Infrastructure:**

- to carry out special control in RBE when necessary to make sure that the internal control system of RBE is functioning efficiently and contributes to the completion of the Rail Baltic project on time and according to the project;
- to establish, e.g. in the updated management and control system, the exact roles and responsibility of the project parties, also agree in greater detail on the functions of the MEAC in the performance of supervision and management of changes;
- to develop measures for exercising supervision over the activities of Rail Baltic Estonia OÜ, which would, among others, guarantee that the activities of the Rail Baltic project for which Estonia is responsible stay on schedule and on budget.

Response of the Minister of Economic Affairs and Infrastructure: the National Audit Office has advised the Minister of Economic Affairs and Infrastructure to give more attention to the roles and responsibilities of the parties to the RB project, especially RBE OÜ, the supervision of RBE OÜ by the MEAC, the management of changes and the movement of information.

Several agreements that regulate the establishment of RB, such as the Inter-Beneficiary Agreement (IBA) and the Contracting Scheme Agreement (CSA) have been entered into between the implementers of the RB project, including the relevant ministers.

The MEAC established the public undertaking Rail Baltic Estonia OÜ (RBE OÜ) for the implementation of the project and entered into performance agreements with RBE OÜ that are based on the CEF Grant Agreements, which give RBE OÜ clear tasks in the establishment of the

RB railway. These agreements also cover the management and control of the RB project. According to clause 3.3 of the performance agreement, the MEAC has the right to check at any time the compliance of the reports submitted by RBE with cost statements, the compliance of the circumstances on the basis of which grants are received, the targeted use of the grants, and to receive from RBE additional information about the activities related to the performance agreement. Basically, this provision means the right to exercise 'special control'. The reporting obligations arising from the CEF Grant Agreements and the obligations arising from the CSA and the IBA also apply to RBE OÜ as one of the implementers of the project on the basis of the performance agreements.

The Secretary General of the MEAC has also established the project management and control system (MCS) with Directive No 16-0001 of 5 January 2016. This document also consolidates the various performance agreements. Proceeding from the MCS and said agreements and contracts, the project supervision measures, roles and responsibilities have been regulated in a relatively detailed manner, but fragmented between different regulative documents. However, the mechanisms of the supervision and control system are functioning despite this. We therefore agree that the MCS needs to be updated in order to integrate the additional measures and mechanisms agreed after the establishment of the MCS (e.g. the additional obligations and rights arising from the aforementioned cooperation agreements, the IBA and the CSA, which are not regulated by the Grant Agreements).

In November 2019 the MEAC will establish the new version of the MCS, which was prepared during the time of the audit of the National Audit Office. The discussions held during this audit and the recommendations made in the audit report are a valuable input to updating the MCS. The new version of the MCS takes most of the recommendations of the National Audit Office on board in respect of the roles of the parties, supervision and an even more detailed handling and management of risks. The project supervision system as well as change management and the related procedures were and still are in use.

Changes at the level of the project and the activities must be distinguished when changes are managed. Managing changes at the level of the project has been taken to the international level into the framework of the task force of the ministries. At the level of activities, possible changes are considered and decided internally in Estonia according to the level of difficulty of the issue to be resolved either at the level of the steering group of the project or at the level of the Management Boards of the implementing agencies in the case of specific procurements.

- to develop the principles of reporting and information exchange, so that information about the status of activities would move from RBE to the MEAC, incl. to the management where necessary, and the information required for the implementation of activities moves from the MEAC to RBE; and to guarantee that the information in the reports submitted to RBR is correct and up to date;

Response of the Minister of Economic Affairs and Infrastructure: the updated MCS also describes information exchange mechanisms from the preparation and forwarding of reports to regular meetings. We would like to point out that the reporting mechanisms were previously included in the international agreements (IBA, CS, CEF Grant Agreements) as well as in the national agreements (performance agreements of the MEAC with RBE OÜ and the Land Board) and the MCS simply combines their description. The regular information exchange tool for the managements of the project parties is described in the amendments to the MCS in the composition and rules of procedure of the project steering group.

- to develop the decision-making mechanism required for change management so that the management of the MEAC and make the decisions required for the implementation of the project at the right time;

Response of the Minister of Economic Affairs and Infrastructure: the decision-making mechanism required for managing changes in the project is described in greater detail in the updated MCS. The regular information exchange tool for the managements of the project parties (incl. the management of the MEAC at the level of the secretary general) is described in the amendments to the MCS in the composition and rules of procedure of the project steering group. The amendment to the MCS also specifies the requirement to submit the consolidated reports prepared by the MEAC to the management of the MEAC in addition to the joint venture RB Rail AS (in the role of the intergovernmental coordinator).

- to consider the need to have the owner represented in the Supervisory Board of Rail Baltic Estonia OÜ and, if necessary, to nominate its candidate to the committee for appointment of the Supervisory Board members of public undertakings in relation to the fact that the owner is responsible for the performance of the undertaking at the international level, and it would also facilitate carrying out supervision and control.

Response of the Minister of Economic Affairs and Infrastructure: the administrator of the holding in RBE OÜ is the MEAC, whose secretary general is, pursuant to subsection 80^1 (6) of the State Assets Act, a member of the appointments committee established by the Government of the Republic for making propositions related to the appointment of the members of the Supervisory Boards of public undertakings and who looks after the interests of the MEAC as the owner. The MEAC has made the proposition to appoint a representative of the MEAC as the owner to the Supervisory Board of RBE OÜ. The plan is to make said change among the members of the Supervisory Board in 2019.

146. **Recommendations of the National Audit Office to the CEO of Rail Baltic Estonia OÜ:**

- to determine the persons responsible for the processes of the internal control system and their rights and obligations;

Response of the CEO of Rail Baltic Estonia OÜ: the implementation of the internal control system of RBE is guaranteed by the obligation of each RBE employee to proceed from the documents of the management and control system. We will appoint persons on the basis of their positions for the regulations (procurement procedure, code of ethics, project management procedure, risk management system, internal rules of procedure, IT procedure), who will be the contact persons who will explain the respective procedure to the other employees and introduce possibilities for increasing the efficiency of the processes covered in these procedures.

- to update the risk management system, incl. to determine the working principles of the risk management working group and harmonise the risk management system of RBE with the system of RB Rail AS;

Response of the CEO of Rail Baltic Estonia OÜ: the risk manager of RBE receives the main information for risk mapping and assessment from regular meetings (e.g. weekly meetings of the management and project managers) and the reports presented about the project. In addition to the above, the risk management working group is also a format for receipt and provision of information about risks. The perfection of the risk management system is a constant activity, so we will take the above guideline on board and specify the working principles of the working group. Harmonising the risk management systems with RB Rail AS would also be practical.

- to create rules for the documentation of decisions and the materials, opinions, estimates, etc. on which they are based in order to guarantee bigger transparency of risk management, amendments and decision-making;

Response of the CEO of Rail Baltic Estonia OÜ: risks are assessed and management measures are determined in cooperation with project managers. In addition to universal risk mapping, an additional risk plan has been prepared for each project in cooperation with the project manager, which is regularly updated. We will take the aforementioned guideline into account upon the improvement of the risk management system and describe the documentation of risks in greater detail. We will highlight the reasons of the decisions related to project management in the minutes of the project management meetings according to the project management procedure.

- to assess whether the updated process of change management makes it possible to efficiently manage the changes occurring in procurements and contract management, and update the processes if necessary;

Response of the CEO of Rail Baltic Estonia OÜ: we will add regular control of the procedures related to the company's internal procedures, incl. procedures related to change management, to the company's risk management system, during which we will assess the effectiveness of procedures in consideration of the goals set to them, and the respective amendment proposals will be made to the Management Board.

- to systematically assess the functioning of the organisation's internal control system and eliminate any deficiencies identified as a result of the assessment.

Response of the CEO of Rail Baltic Estonia OÜ: we will add regular control of the procedures related to the company's internal procedures, incl. procedures related to change management, to the company's risk management system, during which we will assess the effectiveness of procedures in consideration of the goals set to them, and the respective amendment proposals will be made to the Management Board.

- to assess the problems that have arisen in the organisation of procurements and the performance of contracts, and to update the internal processes on the basis of the analyses.

Response of the CEO of Rail Baltic Estonia OÜ: any non-compliances that have emerged during procurements or the performance of contracts are discussed at project management meetings and the meetings of the risk working group. We will make the amendments that require documentation of the relevant discussions. This creates the grounds for updating the internal control systems.

Examples of organisation of procurements and contract management

Criterion 8: The National Audit Office presumed that the procurements of RBE have been organised according to the laws of the Republic of Estonia and the established guidelines.

How has RBE managed to carry out the procurements of the Rail Baltic project so far?

147. The National Audit Office analysed on the basis of three procurements carried out in Estonia whether Rail Baltic Estonia OÜ has followed the Public Procurement Act, the internal and RBR guidelines and the obligations arising from international agreements when conducting procurements and when awarding and managing public contracts.

148. For this purpose, the National Audit Office gathered the main requirements from all of the above documents and checked whether they had been complied with in the selected three case-study procurements.

What is the opinion of the National Audit Office?

149. The analysis of the National Audit Office revealed that Rail Baltic Estonia OÜ has generally followed the established requirements in the case of the three selected procurements and there were only a few shortcomings (see Table 1).

150. One of the problems that was evident in all three procurements was the non-transparency of the market research. Pursuant to the Public Procurement Act, the information disclosed to the companies and persons that participated in the market research must also be published in the underlying documents of the procurement in order to prevent distortion of competition. Recording the market research in writing makes it possible to check whether the contracting authority has disclosed additional information to market research participants during market research that would give them an advantage in comparison with the persons who proceed only from the information disclosed in the procurement when preparing their tender.

151. RBE confirmed that market research and consultations are carried out in the case of each procurement, but the process of market research is not always recorded in writing. Thus, not recording market research creates the situation where there is no reassurance that everyone participating in the procurement is treated equally and transparency is guaranteed.

152. As a result of the analysis of the procurements, the National Audit Office also found that the election of the members of the procurement committee is not documented in RBE. The procurement committee is appointed pursuant to the procurement procedure of RBE. Depending on the cost of the procurement, the members of the committee are appointed from RBE, RBR and the MEAC, and an observer is appointed from the CPTRA. The lawyer of RBE also participates in the procurement commission as an observer.

153. According to RBE and the MEAC, the members of the procurement committee are elected informally, i.e. their election is not justified or documented, because the background and skills of the possible candidates are already known.

154. The legal analysis revealed that the Management Board can influence the procurement results primarily via the appointment of the members of the procurement committee. As transparency and the equal treatment of participants are important in the case of a public procurement, it is important that the election of the members of the procurement committee is justified and documented. Also, it's important to document the work of the committee, incl. the important opinions of the participants.

155. The National Audit Office also found deficiencies in the assessment and recognition of risks (see from point 103), change management (see from point 118) and reporting (see from point 137).

Table 1. Compliance with requirements for procurements and contract management

Requirements[46]	Maintenance depot[47]	Muuga[48]	Risk analysis[49]	Summary
Has RBE followed its internal guidelines upon the implementation of the activities related to procurements and contracts, incl. guaranteed: ▪ the proper preparation of procurements; ▪ prevention of conflict of interest; ▪ transparency; ▪ clear division of roles and responsibility; ▪ good quality procurement documents; ▪ appropriate award and termination of the public contract;	There were a few deficiencies	There were a few deficiencies	There were a few deficiencies	In general, RBE has followed its internal guidelines upon implementation of the activities related to procurements and contracts. There were deficiencies in the preparation of the terms of reference – all of the information required in the procurement procedure was not highlighted in them. It also became evident that the results of the market research are not recorded in writing and the election of the members of the procurement committee has not be justified in writing. In the case of the maintenance depot procurement, the compliance of the tenders with the tender specifications was not checked, although this is required according to the procurement documents. It was also ascertained that informing the Supervisory Board about the award of public contracts is not always recorded in writing.

46 The requirements for procurements and contract management have been taken from the Public Procurement Act, the internal documents of RBE, the international agreements of the RB project and the public procurement audit guidelines "Public Procurement Audit" (2018) prepared by the supreme audit institution of Portugal, see http://www.tcontas.pt/pt/publicacoes/public_procurement.shtm.
47 Procurement No 186474 "Ordering a preliminary study of the technical and spatial needs of the railway infrastructure maintenance depot".
48 Procurement No 177780 "Analysis of the technological and spatial needs of the Muuga multimodal freight terminal of Rail Baltic".
49 Procurement No 183609 "Ordering a risk analysis of the Estonian section of the Rail Baltic Project".

▪ compliance with the requirements of the PPA?				
Has RBE followed the rules of documenting procurements and contracts, incl. ▪ all of the meetings, decisions and propositions of the procurement committee have been recorded in writing; ▪ the documentation makes it possible to check the selection of the type of procurement, how the procurement was carried out, the selection process and the performance of the contract?	Yes	Yes	Yes	RBE has followed the internal rules of documenting procurements and contracts.
Has the MEAC followed the established rules of information exchange of the global project when carrying out the activities related to the procurements and contracts, incl. have the planned procurements, the status of ongoing procurements, and the identified problems and risks been added to the monthly reports?	There were deficiencies	There were deficiencies	Not an activity recognised in the CEF Grant Agreement, which means there is no reporting obligation	Important data are generally given in monthly reports, but there are deficiencies in the quality of the reports, e.g. the data are sometimes outdated and the problems that have already emerged are recognised instead of risks.
Has RBE followed its internal reporting rules upon the implementation of the activities related to procurements and contracts?	Could not be checked	Could not be checked	Could not be checked	The project management procedure, which includes the internal reporting rules, had not been established yet at the time the selected procurements were carried out. According to the explanations given by RBE, reporting was mostly done at biweekly meetings. When a decision was made at a meeting, it was recorded, but no minutes were taken of the meetings.
Has RBE assessed the risks of the activities related to procurements and contracts and, upon the materialisation of the risks, followed the guidelines on change management and reporting?	There were deficiencies	There were deficiencies	There were deficiencies	No preventive risk assessment has been done (see point 108). Only the obligation to inform the Management Board of the emergence of any risks that may obstruct the achievement of the project's goals was established for change management and reporting, but further action was not regulated. According to the explanations of RBE, information was given at biweekly Management Board meetings, but no minutes were taken of the meetings.
Has the management/Supervisory Board of RBE analysed the impact, reasons and justification of significant changes upon their emergence and taken additional mitigating measures?	Could not be checked	Could not be checked	Could not be checked	According to RBE, there were no changes in the reviewed procurements that would potentially have an impact on the global project. The changes that affect the national activities related to the Rail Baltic project have been highlighted from point 118 onwards.
Has RBE carried out the procurements and the activities related to the contract well, incl.	Yes	Yes	yes	RBE has followed the existing quality control mechanisms when carrying out procurements and performing the contract.

▪ analyses and/or research has been carried out during the planning of procurements; ▪ the documents of the procurement have been specified with important parties; ▪ the Management Board has supervised the activities of the procurement committee; ▪ a certificate has been prepared in the delivery stage of each assignment, where any defects and the deadlines for their elimination have been specified among other aspects; ▪ the received works have been checked by qualified persons?				
Were there delays related to the communication of information and/or decision-making competency upon the solution of the problems that have occurred upon the performance of the contract?	There were delays	There were delays	No	Delays caused by RBE in the acceptance of works were identified in the case of the reviewed procurements. The reason for the delays was that different parties were included in the acceptance of the works and the assessment of their quality, and it took longer than expected.

Source: National Audit Office

156. Recommendation of the National Audit Office to the CEO of Rail Baltic Estonia OÜ:

- to make sure that the market research carried out before the announcement of a procurement are documented;

Response of the CEO of Rail Baltic Estonia OÜ: we will include the requirement to document market research in writing in the procurement procedure.

- to make sure that the election of the members of the procurement committee is justified and documented.

Response of the CEO of Rail Baltic Estonia OÜ: The reason for the selection of procurement committee members will be recorded in the respective decision upon the appointment of the members. We will include the relevant requirement in the procurement procedure.

/digitally signed/

Ines Metsalu-Nurminen
Director of Audit, Audit Department

Recommendations made by National Audit Office and responses of the auditees

The National Audit Office made several recommendations to Minister of Finance, the Minister of Economic Affairs and Infrastructure and the CEO of Rail Baltic Estonia OÜ on the basis of the audit. The Minister of Economic Affairs and Infrastructure sent his response to the recommendations made by the National Audit Office on 6 November 2019, the Minister of Finance on 4 December 2019 and the CEO on 31 October 2019.

The table below gives a summary of the recommendations made and the responses received.

General comments on audit report
Response of the Minister of Economic Affairs and Infrastructure: the three Baltic States have agreed to build the Rail Baltic (RB) railway in such a manner that the use of the railway can start in 2026. The states assumed this obligation with the agreement for the development of the Rail Baltic / Rail Baltica rail connection entered into between the Government of the Republic of Estonia, the Government of the Republic of Lithuania and the Government of the Republic of Latvia (the Intergovernmental Agreement, IGA). The Riigikogu ratified the IGA with an act on 19 June 2017. Commission Implementing Decision (EU) 2018/1723 of 26 October 2018 on the Rail Baltica cross-border project on the North Sea-Baltic Core Network Corridor also states that the project will be completed by 2026. Unlike the National Audit Office, the MEAC finds that the aforementioned deadlines are still realistic and the MEAC and the other parties of the RB project constantly work on completing the RB railway by this time. In the opinion of the minister, the roles and responsibility of the Estonian parties to the project are regulated with contracts between the MEAC and the other parties, and the MEAC has planned the funding of the RB railway well in advance whilst following all of the obligations and options provided for by law.

Recommendations of National Audit Office	Responses of the auditee
Funding of the Rail Baltic project **84. Recommendations of the National Audit Office to the Minister of Economic Affairs and Infrastructure and the Minister of Finance:** ▪ to develop schedules and funding scenarios regarding the completion of Rail Baltic during the preparation of the state budget strategy for 2021-2024 in case the co-funding by the European Union decreases and in case the project turns out to be more expensive than planned. This makes it possible to consider the impact of the Rail Baltic project on the state budget better during its preparation and guarantee that the money necessary for the implementation of the project is there at the right time; ▪ to introduce the schedules and funding scenarios to the Government of the Republic and submit them to the Riigikogu as annexes to the state budget strategy or to find another suitable way for introducing the schedules and scenarios to the Riigikogu so they can be considered when budget policy decisions are made. points 32-45	**Response of the Minister of Economic Affairs and Infrastructure:** the National Audit Office repeatedly criticises the MEAC and the Ministry of Finance (MF) for planning the funding of the Rail Baltic in detail only in the state budget strategy and the annual budget, i.e. for four years in advance. The National Audit Office finds that the MEAC and the MF should prepare detailed funding scenarios and forecasts for Rail Baltic up to the end of the project and submit them as annexes to the budget strategy. In the opinion of the National Audit Office, this makes it possible "to guarantee that the money necessary for the implementation of the project is there at the right time". The MEAC explains in response that the recommendations made by the National Audit Office are questionable from the viewpoint of the state budget planning and preparation principles established by laws and regulations[50], incl. the principle of universality of the state budget, and compliance with them may breach the principles of materiality and the financial competencies of the Riigikogu. Also, complying with the recommendations may not help to guarantee that "the necessary money is there at the right time". Moreover, compliance with the recommendation may create the situation where the support to the Estonian section of the project from the Connecting Europe Facility (CEF) of the European Union will decrease. The Supreme Court en banc emphasised in its Ruling No 3-4-1-6-12 of 12 July 2012 that "financial competence gives the Riigikogu the right to make choices regarding the state budget and decide on proprietary obligations. Due to the principles of materiality, the financial competence of the Riigikogu binds the Riigikogu to the obligation to make the decisions concerning the state's proprietary obligations and the budget policy." As stated above, the Riigikogu ratified the agreement for the development of the Rail Baltic / Rail Baltica rail connection entered into between the Government of the Republic of Estonia, the Government of the Republic of Lithuania and the Government of the Republic of Latvia with an act of 19 June 2017 (IGA). In the IGA, the three Baltic States assumed the obligation to establish a railway with a 1,435 mm gauge track and do it with the co-funding of the CEF to the biggest extent possible whilst being prepared to contribute money from the state budgets as well (see articles 11 and 14 of

[50] See the State Budget Act, the Minister of Finance Regulation No 9 "Procedure for preparation of the state budget strategy and the draft budget of the area of administration of the ministry, and for transfer of the state budget funds" of 4 February 2016.

Recommendations of National Audit Office	Responses of the auditee
	the agreement). By ratifying this agreement, the Riigikogu assumed a proprietary obligation for the state of Estonia to guarantee the funds for the completion of the RB railway in any case (see the reason for ratification given in the explanatory memorandum to the IGA) by reserving themselves the right to extend the completion deadline of the project in cooperation with the other project parties, etc., should the EU funding decrease (see article 14). The cost of completing the construction of the Rail Baltic railway in Estonia according to the preliminary project of the Estonian section of RB made in October 2018 is ca 1.59 billion euros. We will review the construction cost again when the detailed technical design of the railway is completed in 2022 at the latest, and the target is to reduce the costs in such a manner that the main parameters of the railway remain the same as agreed before, and the compliance of the railway with the interoperability specification and the restrictions arising from the established plans (incl. environmental requirements) is guaranteed. The Riigikogu also assumed a financial obligation of the same scale as the cost of RB when it ratified the foundation agreement of the European Stability mechanism (hereinafter: the ESM) on 30 August 2012. The difference between the financial obligations related to the ESM and the establishment of the Rail Baltic railway lies, among others, in the fact that the costs are spread across several years in the case of Rail Baltic, whilst in the case of the ESM, the state of Estonia was and still is threatened by the obligation to pay *ca* 1.1 billion euros as a lump sum into the ESM upon the materialisation of the risks arising from other countries, which Estonia does not control, and to make this payment from the state budget funds alone (not in combination with EU aid). In the case of the ESM, the Supreme Court deemed it permissible that the Riigikogu assumes such a financial obligation in advance (see Supreme Court en banc Ruling No 3-4-1-6-12 of 12 July 2012). Although the Supreme Court instructed the Riigikogu and the ministries quite a lot in the ruling, it never suggested that when assuming an obligation or due to the general budgeting process, the state should plan how Estonia intends to perform the obligation, including how it intends to finance it. Moreover, the Supreme Court explain in said ruling that “the Riigikogu has the right to assume proprietary obligations as well as the right to decide on how and with which funds the obligation will be performed. Several manners of performing an obligation may comply with the Constitution. The court’s duty is not to tell the legislator how the Riigikogu should perform the obligations assumed for the state.” In other words, the Supreme Court said that the financial competency of the Riigikogu consists of different competencies: a) the right to assume a financial obligation; and b) the right and the obligation to decide on how the obligation will be performed. The Supreme Court deems these competencies the core competencies. In the case of RB, the Riigikogu has already assumed the obligation and the current dispute concerns the performance of the obligation. Pursuant to §104 clause 11 and § 117 of the Constitution, determining how the performance of the financial obligations assumed for the state is planned in Estonia is within the sole competence of the Riigikogu. The Riigikogu has established the procedure for planning the performance of the obligations assumed for the state, including the long-term planning procedure, in the State Budget Act (SBA), which is a constitutional act (its adoption requires a majority vote in the Riigikogu). The Riigikogu has decided that the state of Estonia plans the performance of the proprietary obligations assumed in the state budget strategy and the annual state budget, and the state budget strategy is prepared for four years according to § 21 of the SBA and the aforementioned regulation of the MF. Clear principles must also be followed upon the preparation of the state budget, one of which is the principle of universality. This means that the single revenue and expenditure items of the state budget do not depend on each other (see also the comment to § 115 of the Constitution, www.pohiseadus.ee). Thus, the intended use of the state budget revenue has generally not been determined, i.e. the revenue as a whole is meant for financing the expenditure as a whole. The National Audit Office advises the MEAC and the MF to start preparing spreadsheets, which would indicate the hypothetical scale of the self-financing by Estonia of the establishment of RB after five to seven years and how the state plans to fund such a hypothetical obligation over a budget strategy period, and the National Audit Office thereby advises to submit such

Recommendations of National Audit Office	Responses of the auditee
	"funding scenarios" that exceed the budget strategy period as an annex to the budget strategy prepared for four years. The Supreme Court emphasised that deciding on how to perform the financial obligations assumed by the Riigikogu, incl. the obligations related to the financing of RB, is within the sole competence of the Riigikogu. The Riigikogu has decided that as a rule, this will be planned for four years in advance. This planning period is not random but based on the facts that planning highly specific funding needs and sources for longer periods is difficult because of changes in critical circumstances and that the Constitution does not permit depriving future compositions of the Riigikogu of the opportunity to plan the budget. Budget planning also means a more specific planning of the performance of financial obligations, e.g. whether to finance an obligation from the state's tax revenue, a loan or a bond issue. Planning the measures for the implementation of the budget for years in advance on behalf of the future compositions of the Riigikogu is not justified. Also, such specific planning of the revenue and expenditure of the RB project would be in contravention of the principle of the universality of the state budget (see above). The Supreme Court emphasised that the duty of the court and consequently of the executive and constitutional institutions is not to tell the legislator how the Riigikogu should perform the obligations assumed for the state. The MEAC cannot start telling the Riigikogu with an additional spreadsheet which source could be used to cover the self-financing of the construction of RB in 2025. As this spreadsheet recommended by the National Audit Office could never be binding, it would not have a substantive meaning or oblige anyone to act according to it, or contribute to the goal of guaranteeing the existence of the money in 2025, for example. The recommendation of the National Audit Office is basically a general proposition for amendment of the SBA and the budgeting principles, including the principle of universality, and it is not specific to the RB project. The guarantee that the money for the establishment of RB exists in 2024 and thereafter is given by the fact that in 2017 the Riigikogu assumed the obligation to complete the construction of Rail Baltic irrespective of what the rate of the specific self-financing of Estonia is. Pursuant to § 21 of the SBA, expenditure is planned in advance more specifically by four-year periods and in detail in the annual state budget. Thus, it is within the competency and the obligation of the Riigikogu composition of the respective years to find the funds for the establishment of RB. The MEAC and the MF have performed all of the obligations stipulated with the Constitution and acts in relation to planning and guaranteeing the funding of RB. The MEAC has also performed the additional obligation assigned by the Riigikogu with the ratification of the IGA and presents a detailed overview of the RB sites of the next year and their costs as an annex to the annual budget and it also informs the Economic Affairs Committee of the Riigikogu about the status of the establishment of RB separately every year. The MEAC also notes that the total income and expenses of the RB project have been calculated and all of the cost-benefit analyses of RB across all years have been prepared. The possible expenses of RB are thoroughly assessed and planned when the budget strategy is prepared and updated on an annual basis. Similar to other projects with foreign financing, the Grant Agreements already entered into (the CEF Grant Agreements in the given case) are reviewed in the case of RB when the state budget strategy is prepared and the potential budget volumes of the subsequent CEF calls for proposals, the estimated proportion of the RB project in the total volume of grants of the call for proposals and the financing required for the implementation of the Estonian activities are considered. As pursuant to the IGA, the funding of RB is planned, among others, from the CEF in two EU funding periods (2014-2020 and 2021-2027), then we have forecast since 2017 that the costs related to the implementation of RB will be covered also from the next EU budget periods. Submitting specific figures and sources of money for longer than four years is difficult and also impractical, because the changes in the various presumptions as a result of several parallel processes (incl. negotiations between Member States and with the European Parliament, the dependence of the schedule of RB and the investment expenses on the probability of the materialisation of various risks, etc.) change such forecasts. The MEAC and the MF monitor and update these forecasts all the time. The MEAC also points out that the recommendation of the National Audit Office may reduce the possibilities of getting EU aid for funding RB. Making new official decisions concerning funding alternatives (e.g. by the Riigikogu)

Recommendations of National Audit Office	Responses of the auditee
	would jeopardise getting grants from the CEF. In a situation where the expenses of RB could have largely been covered with other funds in addition to the CEF grant and the required self-financing according to the approved document, the INEA would have no reason to approve applications for the grant, as the existence of financial resources outside the CEF grant would make the allocation of EU grants in the requested amount and at the requested intensity unjustified. The point of EU grants is to finance the achievement of the results of such projects that are necessary in the common interests of the EU, which would otherwise not be achieved due to the lack of financial resources/funding options. In terms of the schedule of RB, the Baltic States have agreed on the completion deadline of RB in the IGA and the binding deadlines are also set by the implementing decision of the European Commission. The duty of the project implementers is to adhere to said deadlines. The updating of details requires negotiating amendments to and amending of the aforementioned documents by the parties, which is not currently planned, as the parties find that the schedule can be adhered to. In the case of the schedule of RB, it is important to separately view the final deadline for the completion of RB (or its Estonian section) and the activities to be carried out within the scope of the CEF Grant Agreements entered into by now and the agreed completion deadlines. In the case of CEF Grant Agreement I, there are delays in the initiation of activities as well as the established final deadlines in all of the states involved in the RB project. Considering the type and scope of implementation of the planning and design processes (e.g. the inclusion of local governments and residents etc.), it is not surprising that the circumstance affecting the implementation of the project activities (incl. cost, deadlines) may change to certain extent as new circumstances become evident (e.g. the establishment of spatial plans, the completion of the preliminary design, the completion of the detailed technical design). However, this does not automatically mean that the final deadline of the project will be postponed. It’s important that the changes in circumstances would not bring about the materialisation of possible risks, such as repayment of the funds allocated with the CEF Grant Agreements. The materialisation of this risk was not evident in the case of any of the CEF Grant Agreements in October 2019. Firstly, the project partners are looking for and have found possibilities to ensure that the delay in the full completion of the detailed technical design would not lead to the postponement of the construction deadlines – for this purpose, we will carry out the design works by sections and priority subsections, so that the building permits can be issued and the construction of specific sites can start immediately after the completion of the project documents of the respective site or subsection. Secondly, the duration of the CEF Grant Agreements can be expanded for certain reasons and to a certain extent, activities can be re-planned, etc. by agreement with the INEA considering the achievement of the final objective of the project, which is important from the viewpoint of the common interests of the EU and the states – the completion of a new railway connection. Therefore, an amendment to CEF Grant Agreement I will be signed in November 2019, which among others concerns the extension of the eligibility deadline of the costs required for the implementation of the activities specified in the agreement. We also specified the scale of the activities within the scope of the same amendment, e.g. we divided the construction works of the Pärnu and Ülemiste passenger terminals into stages, which makes it possible to start the works before 2022, but finish them from 2023 by including additional CEF funds. **Comment of the National Audit Office:** in the opinion of the National Audit Office, preparing the project’s budget forecast for a longer time does not restrict the financial competence of the Riigikogu. In its overview of 2017, the National Audit Office made the following recommendation about the agreement for the development of the Rail Baltic rail connection made between the governments of Estonia, Lithuania and Latvia: ask the government to submit an analysis and action plan for funding Rail Baltic. The National Audit Office pointed out that the Riigikogu should know the answers to at least the following questions: How big is the financial obligation that will be assumed for the state? How will the project be financed? Has a clear decision-making mechanism been agreed in case the project ends up costing more than planned, is not completed by the deadline or there are changes in funding? The role of the government is to guarantee that the Riigikogu would have all of the information necessary for making decisions. The longer project funding forecast and scenarios recommended in this audit could

Recommendations of National Audit Office	Responses of the auditee
	therefore be the input for the preparation of the state budget and the state's budget strategy if necessary. **Response of the Minister of Finance:** in the opinion of the Ministry of Finance, the claim made in point 33 of the report of the National Audit Office that there is no funding forecast for the most expensive period of the project is justified with the lack of national political intent and an international agreement (point 24) for continuing the project in the case of larger self-financing. The Ministry of Finance considers the funding mechanism described in point 25, which does not guarantee continued funding from the EU even if the activities until then have been appropriately completed, a major risk factor. The inadequate project management and delays mentioned throughout the report of the National Audit Office obviously decrease the possibilities of applying for funds successfully. According to the coalition agreement, guaranteeing EU funding to the extent of 81% is the precondition to continuing with the project, but it has not been met according to the description in this point. According to the explanation given in point 32, the funding forecast for the Rail Baltic (RB) Project is officially not prepared for a longer period (e.g. longer than the period of the state budget strategy, i.e. the SBS) as this is not required by Estonian law. There is no reason to doubt that self-financing to the extent of up to 19% of the construction costs will be found in the state budget in the coming years. The problem presented in point 36 that there are no scenarios that could be implemented if the amounts to be allocated from the budget of Estonia would have to be considerably larger than planned for now, must be regarded as a considerably more serious problem. In the opinion of the Ministry of Finance, scenarios concerning the possibilities and impossibility of continuing with the project in the case of different visible developments should be prepared before the project is continued. The decrease or termination of EU aid and the increase of the project costs and delays must also be taken into account. Postponing such agreements until the time when the risks have already materialised is not responsible risk management. The Ministry of Finance finds that if EU support to the implementation of the RB project ends up being smaller than expected, the socioeconomic cost-effectiveness, reasons and track selections of the entire project would have to be thoroughly checked again. The project parties must negotiate and agree on a new, amended schedule for the implementation of the project or suspend the project, because it's highly likely that the Baltic States would be unable to finance the implementation of the project from their budgets if the participation rates and volumes differed significantly from the ones highlighted in the cost-benefit analysis. The opinion of the Ministry of Economic Affairs and Communications that the railway will be built even without European Union support presented in point 39 must be regarded as groundless. The Ministry of Finance finds that different scenarios must be developed and agreed nationally and between the Baltic States before the biggest expenses are incurred also within the scope of the activities covered by grants until now. The National Audit Office found in point 34 that the amount that has been spent and is planned to be spent on the development of the Estonian section of the project from 2010–2022 is 276.7 million euros, which comprises 20.5% of the cost of the Estonian section specified in the cost-benefit analysis. [The National Audit Office notes that this point of the report was updated according to the state budget strategy for 2020-2023 after the report was sent out for official responses. According to the new calculations, the amount spent and planned to be spent on the development of the Rail Baltic project from 2010–2023 is 433.9 million euros, which comprises 32.1% of the Estonian section of the project highlighted in the cost-benefit analysis.] Actually, the cost of the Estonian section known today is 1.6 billion (point 54), of which the amount spent until now and planned to be spent comprises 17.3%. We consider it probable that the project will become more expensive (as you have also said in the reference to the report to the European Court of Auditors on page 15, which ascertained that the cost of all of the audited lines increased by more than 25%). The cash flow forecasts for the SBS period and a longer period can only be working materials that are based on the presumptions agreed in the Connecting Europe Facility (CEF) Grant Agreements and other related documents, incl. on forecasts based on known circumstances as well as scenarios. In the opinion of the Ministry of Finance, the audit of the National Audit Office should also have covered the risks of financial corrections or reductions of

<table>
<tr><th>Recommendations of National Audit Office</th><th>Responses of the auditee</th></tr>
<tr><td></td><td>the actual aid intensity, which may arise from the inadequate national control of the cost-benefit analyses of the project, the failure to carry out procurements properly, the delays that make procurements longer than the eligibility period or for other reasons.</td></tr>
<tr><td>Internal control system of the Estonian section of the Rail Baltic project

145. Recommendations of the National Audit Office to the Minister of Economic Affairs and Infrastructure:

■ to carry out special control in RBE when necessary to make sure that the internal control system of RBE is functioning efficiently and contributes to the completion of the Rail Baltic project on time and according to the project;
■ to establish, e.g. in the updated management and control system, the exact roles and responsibility of the project parties, also agree in greater detail on the functions of the MEAC in the performance of supervision and management of changes;
■ to develop measures for exercising supervision over the activities of Rail Baltic Estonia OÜ, which would, among others, guarantee that the activities of the Rail Baltic project for which Estonia is responsible stay on schedule and on budget.
■ to develop the principles of reporting and information exchange, so that information about the status of activities would move from RBE to the MEAC, incl. to the management where necessary, and the information required for the implementation of activities moves from the MEAC to RBE; and to guarantee that the information in the reports submitted to RBR is correct and up to date;
■ to develop the decision-making mechanism required for change management so that the management of the MEAC and make the decisions required for the implementation of the project at the right time;
■ to consider the need to have the owner represented in the Supervisory Board of Rail Baltic Estonia OÜ and, if necessary, to nominate its candidate to the committee for appointment of the Supervisory Board members of public undertakings in relation to the fact that the owner is responsible for the performance of the undertaking at the international level, and it would also facilitate carrying out supervision and control.

points 92-144</td><td>Response of the Minister of Economic Affairs and Infrastructure: the National Audit Office has advised the Minister of Economic Affairs and Infrastructure to give more attention to the roles and responsibilities of the parties to the RB project, especially RBE OÜ, the supervision of RBE OÜ by the MEAC, the management of changes and the movement of information.

Several agreements that regulate the establishment of RB, such as the Inter-Beneficiary Agreement (IBA) and the Contracting Scheme Agreement (CSA) have been entered into between the implementers of the RB project, including the relevant ministers.

The MEAC established the public undertaking Rail Baltic Estonia OÜ (RBE OÜ) for the implementation of the project and entered into performance agreements with RBE OÜ that are based on the CEF Grant Agreements, which give RBE OÜ clear tasks in the establishment of the RB railway. These agreements also cover the management and control of the RB project. According to clause 3.3 of the performance agreement, the MEAC has the right to check at any time the compliance of the reports submitted by RBE with cost statements, the compliance of the circumstances on the basis of which grants are received, the targeted use of the grants, and to receive from RBE additional information about the activities related to the performance agreement. Basically, this provision means the right to exercise ‘special control’. The reporting obligations arising from the CEF Grant Agreements and the obligations arising from the CSA and the IBA also apply to RBE OÜ as one of the implementers of the project on the basis of the performance agreements.

The Secretary General of the MEAC has also established the project management and control system (MCS) with Directive No 16-0001 of 5 January 2016. This document also consolidates the various performance agreements. Proceeding from the MCS and said agreements and contracts, the project supervision measures, roles and responsibilities have been regulated in a relatively detailed manner but fragmented between different regulative documents. However, the mechanisms of the supervision and control system are functioning despite this. We therefore agree that the MCS needs to be updated in order to integrate the additional measures and mechanisms agreed after the establishment of the MCS (e.g. the additional obligations and rights arising from the aforementioned cooperation agreements, the IBA and the CSA, which are not regulated by the Grant Agreements).

In November 2019 the MEAC will establish the new version of the MCS, which was prepared during the time of the audit of the National Audit Office. The discussions held during this audit and the recommendations made in the audit report are a valuable input to updating the MCS. The new version of the MCS takes most of the recommendations of the National Audit Office on board in respect of the roles of the parties, supervision and an even more detailed handling and management of risks. The project supervision system as well as change management and the related procedures were and still are in use.

Changes at the level of the project and the activities must be distinguished when changes are managed. Managing changes at the level of the project has been taken to the international level into the framework of the task force of the ministries. At the level of activities, possible changes are considered and decided internally in Estonia according to the level of difficulty of the issue to be resolved either at the level of the steering group of the project or at the level of the Management Boards of the implementing agencies in the case of specific procurements.

the updated MCS also describes information exchange mechanisms from the preparation and forwarding of reports to regular meetings. We would like to point out that the reporting mechanisms were previously included in the international agreements (IBA, CS, CEF Grant Agreements) as well as in the national agreements (performance agreements of the MEAC with RBE OÜ and the Land Board) and the MCS simply combines their description. The</td></tr>
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Recommendations of National Audit Office	Responses of the auditee
	regular information exchange tool for the managements of the project parties is described in the amendments to the MCS in the composition and rules of procedure of the project steering group. The decision-making mechanism required for managing changes in the project is described in greater detail in the updated MCS. The regular information exchange tool for the managements of the project parties (incl. the management of the MEAC at the level of the secretary general) is described in the amendments to the MCD in the composition and rules of procedure of the project steering group. The amendment to the MCS also specifies the requirement to submit the consolidated reports prepared by the MEAC to the management of the MEAC in addition to the joint venture RB Rail AS (in the role of the intergovernmental coordinator). the administrator of the holding in RBE OÜ is the MEAC, whose secretary general is, pursuant to subsection 80[1] (6) of the State Assets Act, is a member of the appointments committee established by the Government of the Republic for making propositions related to the appointment of the members of the Supervisory Boards of public undertakings and who looks after the interests of the MEAC as the owner. The MEAC has made the proposition to appoint a representative of the MEAC as the owner to the Supervisory Board of RBE OÜ. The plan is to make said change among the members of the Supervisory Board in 2019.
Functioning of the internal control system in Rail Baltic Estonia OÜ **146. Recommendations of the National Audit Office to the CEO of Rail Baltic Estonia OÜ:** ▪ to determine the persons responsible for the processes of the internal control system and their rights and obligations; ▪ to update the risk management system, incl. to determine the working principles of the risk management working group and harmonise the risk management system of RBE with the system of RB Rail AS; ▪ to create rules for the documentation of decisions and the materials, opinions, estimates, etc. on which they are based in order to guarantee bigger transparency of risk management, amendments and decision-making; ▪ to assess whether the updated process of change management makes it possible to efficiently manage the changes occurring in procurements and contract management, and update the processes if necessary; ▪ to systematically assess the functioning of the organisation's internal control system and eliminate any deficiencies identified as a result of the assessment. ▪ to assess the problems that have arisen in the organisation of procurements and the performance of contracts, and to update the internal processes on the basis of the analyses. **points 97-144**	**Response of the CEO of Rail Baltic Estonia OÜ:** the implementation of the internal control system of RBE is guaranteed by the obligation of each RBE employee to proceed from the documents of the management and control system. We will appoint persons on the basis of their positions for the regulations (procurement procedure, code of ethics, project management procedure, risk management system, internal rules of procedure, IT procedure), who will be the contact persons who will explain the respective procedure to the other employees and introduce possibilities for increasing the efficiency of the processes covered in these procedures. The risk manager of RBE regularly maps the risks. We have assessed the risks related to the costs of the project activities increasing and to the schedule of the activities according to all parts of the project in cooperation with the respective project manager. We have prepared a package with risk management measures for each risk. We have planned to regularly observe the implementation of risk management measures in order to manage the risks in the best possible manner. We will improve the risk management system more regularly during the progress of the project. the risk manager of RBE receives the main information for risk mapping and assessment from regular meetings (e.g. weekly meetings of the management and project managers) and the reports presented about the project. In addition to the above, the risk management working group is also a format for receipt and provision of information about risks. The perfection of the risk management system is a constant activity, so we will take the above guideline on board and specify the working principles of the working group. Harmonising the risk management systems with RB Rail AS would also be practical. We will document all of the procurement decisions in the respective documents: the procurement plan, the terms of reference for procurements, the minutes of the procurement committee. We will improve the documentation of the organisation of procurements further according to the recommendations by introducing to the procurement procedure the requirement to document the reasons of the changes made to procurement plans and to document selection of the type of procurement in the terms of reference. In respect of the awarded contracts, we will document the compliance, non-compliance and rejection of the works and the reasons for the implementation of legal remedies in the relevant certificates and notices (certificate of receipt, certificate of rejection of works, notices to the contractor in the case of delays and other non-compliances). We will also introduce to the project management procedure the requirement to cover the issues related to non-compliances at meetings. We will take minutes of the meetings of the risk working group. We will include the respective requirement in the description of the risk management system.

Recommendations of National Audit Office	Responses of the auditee
	The reason for the selection of procurement committee members will be recorded in the respective decision upon the appointment of the members. We will include the respective requirement in the procurement procedure according to the recommendation. risks are assessed and management measures are determined in cooperation with project managers. In addition to universal risk mapping, an additional risk plan has been prepared for each project in cooperation with the project manager, which is regularly updated. We will take the aforementioned guideline into account upon the improvement of the risk management system and describe the documentation of risks in greater detail. We will highlight the reasons of the decisions related to project management in the minutes of the project management meetings according to the project management procedure. we will add regular control of the procedures related to the company's internal procedures, incl. procedures related to change management, to the company's risk management system, during which we will assess the effectiveness of procedures in consideration of the goals set to them, and the respective amendment proposals will be made to the Management Board. any non-compliances that have emerged during procurements or the performance of contracts are discussed at project management meetings and the meetings of the risk working group. We will make the amendments that require documentation of the relevant discussions. This creates the grounds for updating the internal control systems.
Carrying out procurements and contract management **156. Recommendations of the National Audit Office to the CEO of Rail Baltic Estonia OÜ:** ▪ to make sure that the market research carried out before the announcement of a procurement are documented; ▪ to make sure that the election of the members of the procurement committee is justified and documented. **points 149-155**	**Response of the CEO of Rail Baltic Estonia OÜ:** we will include the requirement to document market research in writing in the procurement procedure. The reason for the selection of procurement committee members will be recorded in the respective decision upon the appointment of the members. We will include the relevant requirement in the procurement procedure.

Characteristics of audit

Purpose of audit

The purpose of the audit was to assess whether the internal control systems concerning the procurements and contracts upon the development, funding and management of the Estonian section of Rail Baltic create adequate preconditions for the completion of the railway as agreed and for the project staying on schedule and budget.

The National Audit Office analysed the procurement and contract management practice, division of the roles and responsibilities, risk management and effectiveness of the project supervision functions of the parties involved in the development of the Estonian section of the Rail Baltic project. The National Audit Office commissioned a legal opinion from Law Firm NOVE for analysing the structure of implementation of the Rail Baltic project. The law firm analysed in its opinion how the organisational structure of the implementation of the Rail Baltic project affects the organisation of procurements and contract management.

Assessment criteria

In the opinion of the National Audit Office, the procurement model of Rail Baltic makes it possible to develop the project efficiently and sustainably if a division of roles and responsibilities is established for the organisation of procurements and the procurement model developed for the implementation of the RB project has been developed. Rules have also been established for the management of risks and changes, so that the changes in the global RB project would not exceed the 5% budget reserve specified in the cost-benefit analysis and the final deadline for the start of operation in 2026 specified in the global project is achievable.

In the opinion of the National Audit Office, the of the RB contracting model is efficient and makes it possible to develop the RB project efficiently and sustainably if the contract model sets out the main roles and obligations of all parties and the contracting model corresponds to the global RB project. A procedure for the management of risks and changes has also been prepared for the efficient development of the project, which allows for the project to be implemented with the planned budget and by the deadline specified in the description of the global project.

In the opinion of the National Audit Office, funding of the RB project by the state is guaranteed if the money is planned for the implementation of the RB project in the state budget or the long-term state budget plan. Risks have been managed in respect of the cases were the project ends up costing more than expected or the EU support to the project decreases.

Scope and focus of audit

The audited institutions were the Ministry of Economic Affairs and Communications, the Ministry of Finance, the Consumer Protection and Technical Regulatory Authority and Rail Baltic Estonia OÜ.

The following documents were analysed during the audit:

- legislation, especially the Public Procurement Act;
- state budgets and state budget strategies, and their explanatory memoranda;
- EU Connecting Europe Facility (CEF) Grant Agreements I to III for Rail Baltic Global project;
- expectations of the owners of Rail Baltic Estonia OÜ, 15 December 2016;
- articles of association of Private Limited Company Rail Baltic Estonia;

- Performance Agreement for implementation of the First CEF Grant Agreement, signed on 25 October 2016;
- Performance Agreement for implementation of the Second CEF Grant Agreement, signed by: the MEAC on 11 June 2018 and RBE on 12 June 2018;
- Shareholders Agreement of RB Rail AS;
- Inter-Beneficiary Agreement between RB Rail AS and Ministry of Economic Affairs and Communications of the Republic of Estonia and Ministry of Transport of the Republic of Latvia and Ministry of Transport and Communications of the Republic of Lithuania); 16. June 2016;
- agreement for the development of the Rail Baltic / Rail Baltica rail connection entered into between the Government of the Republic of Estonia, the Government of the Republic of Lithuania and the Government of the Republic of Latvia of 31 January 2017;
- Commission Implementing Decision on the Rail Baltica cross-border project on the North Sea-Baltic Core Network Corridor;
- Estonian management and control system of the Connection Europe Facility project of Rail Baltic, approved on 5 January 2016 with Directive No 16-0001 of the MEAC and the draft of the updated management and control system that is currently being prepared;
- risk analysis of the planning and construction phases of the Estonian section of the Rail Baltic project, final report of the cost-benefit analysis prepared by Ernst & Young AS in September 2017;
- procurement plans of the Consumer Protection and Technical Regulatory Authority and Rail Baltic Estonia OÜ from 2016-2019;
- minutes of the Supervisory Board meetings submitted by Rail Baltic Estonia OÜ;
- project management procedure of Rail Baltic Estonia OÜ; 2018;
- procurement procedure of Rail Baltic Estonia OÜ, approved with Resolution No 2016.12.21-1 of the Supervisory Board of Rail Baltic Estonia OÜ of 21 December 2016, and the procurement procedure approved with Resolution No 2018.02.23-1 of the Supervisory Board of Rail Baltic Estonia OÜ of 23 February 2018.
- common procurement standards and guidelines for Rail Baltica project of RB Rail AS;
- minimum set of requirements for the qualifications of economic operators of RB Rail AS;
- the procurement documents, contract and material related to the performance of the contract of the following procurements;
    - Procurement No 177780 “Analysis of the technological and spatial needs of the multimodal freight terminal Rail Baltic at Muuga Harbour”;
    - Procurement No 186473 “Preliminary study of the technical and spatial need of maintenance depot of railway infrastructure”;
    - Procurement No 183609 “Ordering a risk analysis of the Estonian section of the Rail Baltic project”.

The documents received from RB Rail AS during the joint audit, including the project reports and the schedule of the global project, were also analysed.

Table 1. People interviewed in the course of the audit

Institution	Interviewed	Date of meeting
Rail Baltic Estonia OÜ	Marko Kivila, lawyer Taavi Laja, financial analyst	09.08.2018
Consumer Protection and Technical Regulatory Authority	Jaak Simon, Project Expert of the Transport Department	08.08.2018
Ministry of Economic Affairs and Communications	Kristjan Kaunissaare, Project Manager of Rail Baltica Anti Moppel, Counsellor of the Undersecretary for Transport	14.08.2018
Ministry of Finance	Mari Lahtmets, Counsellor of the Fiscal Policy Department	06.09.2018
Rail Baltic Estonia OÜ	Marko Kivila, lawyer Vaiko Eggert, Project Manager, Procurement Manager, Risk Manager	15.01.2019
Rail Baltic Estonia OÜ	Riia Sillave, member of the Management Board Marko Kivila, lawyer	20.02.2019
Ministry of Economic Affairs and Communications	Kristjan Kaunissaare, Project Manager of Rail Baltica Anti Moppel, Counsellor of the Undersecretary for Transport	28.03.2019

Time of completion of audit

The audit was carried out from August 2018 to July 2019.

Audit team

The audit team consisted of Audit Manager Kaire Kuldpere and auditors Kristiina Visnapuu, Merje Kurm and Silja Einberg

Contact information

Further information on the audit is available from the Communication Unit of the National Audit Office: telephone: +372 640 0704 or +372 640 0777; e-mail: riigikontroll@riigikontroll.ee

An electronic copy of the audit report (PDF) is available online at www.riigikontroll.ee.

The audit report is also available in Estonian.

The number of the audit report in the record management system of the National Audit Office is 2-1/80002/13.

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Previous audits of National Audit Office in the area of Rail Baltic

24 May 2017 – **National Audit Office's overview of the agreement for the development of the Rail Baltic rail connection entered into by the governments of Estonia, Lithuania and Latvia**

All reports are available on the website of the National Audit Office at www.riigikontroll.ee

Annex A. Amounts spent on the basis of the Grant Agreements entered into for the development of the Rail Baltic project and eligibility periods of European Union funds

	CEF I		CEF II		CEF III	
	2015 to 2020		2016 to 2020		2017 to 2023	
	EU co-funding	National funding	EU co-funding	National funding	EU co-funding	National funding
Estonia	175,390,775	38,146,725	10,969,855	1,935,857	1,693,582	298,867
Latvia	237,510,990	54,248,010	492,762	86,958	3,494,732	616,717
Lithuania	23,378,850	4,752,305	118,679,924	20,943,516	94,913,224	16,749,392
RB Rail AS	5,950,000	1,050,000	51,000	9000	10,370,300	1,830,053
TOTAL	**442,230,615**	**98,197,040**	**130,193,541**	**22,975,331**	**110,471,838**	**19,495,029**

Source: CEF Grant Agreements

Note: The eligibility period of CEF Grant Agreement I will extend until 2022 if the project parties and the EU Innovation and Networks Executive Agency (INEA) sign an amendment to the agreement. Other funding agreements may also be amended by agreement of the parties and the INEA in the future, incl. the eligibility periods

Annex B. State budget funds spent on the Rail Baltic project from 2010-2018

Name	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total 2010–2018
Expenses related to the agreements for financing EU TEN-T projects[51]										
Feasibility and cost-benefit analysis (2011, AECOM analysis)	57,600	92,751								**150,351**
Analysis of the establishment of the joint venture			23,688	95,952						**119,640**
Strategic environmental impact assessment				532,500	1,065,000	532,500				**2,130,000**
Communication					108,415	113,028				**221,444**
Preparation of county plans and preliminary design					2,301,232	1,919,011				**4,220,244**
Stage II of archaeological study						900,840				**900,840**
Study of land acquisition compensation measures						67,096				**67,097**
Preparation of terms of reference for security of supply of mineral resources						26,304				**26,304**
Preparation of the terms of reference of the spatial and technological requirements of the Muuga multimodal terminal						22,800				**22,800**
Staff costs (Technical Regulatory Authority)					27,589	37,510				**65,100**
Compensation of the costs of counties concerning the preparation of county plans					12,957					**12,958**
Total expenses related to the agreements for financing EU TEN-T projects	**57,600**	**92,751**	**23,688**	**628,452**	**3,515,195**	**3,619,091**				**7,936,777**
Expenditure from state budget (without aid)										

[51] Project No. 2007-EE-27010-S; Grant Agreement No. C(2008)7494 and Project No. 2012-EE-27001-S; Grant Agreement No. C(2013)5399. The cost includes EU support, self-financing and ineligible VAT.

Preparation of county plans and preliminary design							2,590,912	537,050	811,000	**3,938,962**
Contributions for the formation and increase of the share capital of Rail Baltic Estonia OÜ (incl. payments for the formation and increase of the share capital of RB Rail AS)					890,000	924,000	650,000	1,650,000	1,740,000	**5,854,000**
Total expenditure from state budget (without EU aid)					**890,000**	**924,000**	**3,240,913**	**2,187,050**	**2,551,000**	**9,792,962**
Technical assistance of EU										
Administration of the RB project and participation of the Republic of Estonia in the TEN-T core network						49,540	111,186			**160,726**
Administration of the RB project and participation of Estonia in the TEN-T core network (phase 2)								8,809	155,511	**164,321**
Technical assistance for implementation of the RB project										
Total technical assistance of EU						**49,540**	**111,186**	**8,809**	**155,511**	**325,047**
Costs related to CEF Grant Agreements I, II and III[52]										
Project management and communication							164,523	385,486	458,937	**1,008,947**
Study of the spatial and technological requirements of the Muuga multimodal terminal								232,398	128,642	**361,040**
Establishment of the tram line between RB Ülemiste terminal and Tallinn Airport							1,605,705	9,362,172	484,210	**11,457,087**

[52] Grant Agreement No INEA/CEF/TRAN/M2015/1129482; Grant Agreement No INEA/CEF/TRAN/M2015/1129482 and Grant Agreement No INEA/CEF/TRAN/M2016/1360716.

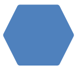
Owner's supervision of the establishment of the tram line between RB Ülemiste terminal and Tallinn Airport							11,550	22,350		**33,900**
Administration of the acquisition of land							46,247	267,697	318,207	**632,152**
Study of mineral construction materials								24,580	48,726	**73,306**
Study of the maintenance depot of the RB infrastructure								61,950	23,099	**85,049**
Design of Pärnu and Ülemiste passenger terminals								502	85,032	**85,534**
Archaeological research								2,490	17,954	**20,444**
Study of security of power supply								76,500		**76,500**
Environmental compensation measures								60,000	66,859	**126,859**
Specification of measures for mitigation of environmental impact									2,496	**2,496**
Research of tram connection to Vanasadam Harbour									102,590	**102,590**
Total costs related to CEF Grant Agreements I, II and III							**1,828,027**	**10,496,125**	**1,736,752**	**14,060,904**
Total expenses related to the RB project	**57,600**	**92,751**	**23,688**	**628,452**	**4,405,195**	**4,592,631**	**5,180,125**	**12,691,984**	**4,443,263**	**32,115,690**

Source: Ministry of Economic Affairs and Communications

Annex C. Reporting scheme of the Rail Baltic project

Key

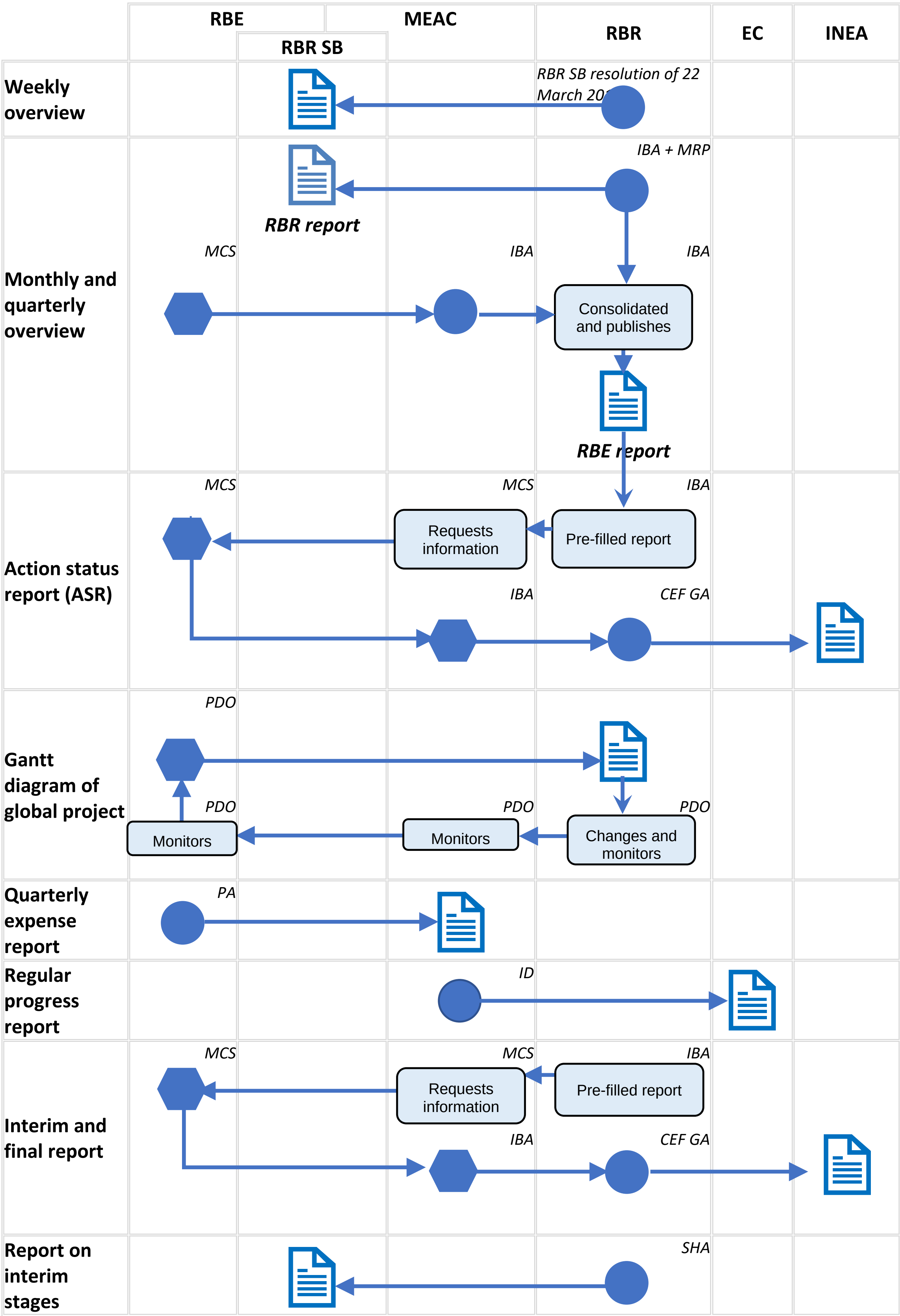
 – report

 – provision of input

 – submission of information

Acronyms:

* RBR SB – supervisory board of RB Rail AS
* EC – European Commission
* INEA – Innovation and Networks Executive Agency; organiser of the use of EU CEF funds
* PDO – resolution of 21 June 2018 of the steering group of the project formed in October 2017 (Towards an Integrated Project Delivery Organisation. A package of Measures)
* MCS – management and control systems
* IBA – RB CEF Inter-Beneficiary Agreement
* MRP – Management Reporting Procedure
* CEF GA – CEF Grant Agreement
* PA – performance agreement between the MEAC and RBE
* ID – Commission Implementing Decision on the Rail Baltic Project of 26 October 2018
* Gantt Diagram – scheme that illustrates the schedule of the global project


RBE
MEAC
RBR SB
RBR
EC
INEA
Weekly overview
RBR SB resolution of 22 March 20
Monthly and quarterly overview
IBA + MRP
RBR report
MCS
IBA
IBA
Consolidated and publishes
RBE report
Action status report (ASR)
MCS
MCS
IBA
Requests information
Pre-filled report
IBA
CEF GA
Gantt diagram of global project
PDO
PDO
PDO
PDO
Monitors
Monitors
Changes and monitors
Quarterly expense report
PA
Regular progress report
ID
Interim and final report
MCS
MCS
IBA
Requests information
Pre-filled report
IBA
CEF GA
Report on interim stages
SHA

Source: National Audit Office

Annex D. Internal control system of Rail Baltic Estonia OÜ

(green)	The internal control role has been developed in the opinion of the National Audit Office
(yellow)	The internal control role can be developed further in the opinion of the National Audit Office
(red)	The internal control role has not been developed in the opinion of the National Audit Office

Internal control role[53]	Explanation
INSPECTION ENVIRONMENT	
The management has guaranteed the implementation of an internal control system in the organisation and is responsible for its effectiveness.	Internal control is regulated in article 3.6.1 of the articles of association. The Management Board manages the company according to the articles of association.
The organisation's processes have been described. The important internal control measures are included in descriptions.	The organisation's processes have been described in different documents, incl. the articles of association, the procurement procedure, the project management procedure. The internal control measures have been described in a memo (see point 59). Rail Baltic Estonia OÜ proceeds first and foremost from the Public Procurement Act (PPA) when it carries out public procurements, the PPA gives clear guidelines that the management company has to follow. Among others, the PPA stipulates the information that must be highlighted in the baseline documents of public procurements, how the procurements must be documented and carried out. Based on the PPA, RBE has developed an internal procurement procedure, which establishes rules from the planning of procurements until the award and amendment of the public contract. Among others, the procurement procedure stipulates the limits of the authorities of the Management Board upon the organisation of procurements and award of contracts. The principles of the formation of procurement committees and the procedure for selected the form of public procurement procedure have also been established in the procurement procedure. In early 2019, RBE established a project management procedure for the management of internal procedures, which specified the responsibility and obligations of the parties to the project. The new procedure sets out, among others, the cases in which the project manager is obliged to inform the Management Board about changes. RBE must also proceed from the general procurement principles of RBR. The document highlights, among others, that the implementers should carry out market research before each procurement if possible and have consultations with companies to make sure that the planned procurement terms do not curb competition unjustifiably. Consultations must be documented in order to avoid giving an advantage to the entrepreneurs who participated in the consultations. According to the document, the necessary experts, especially technical experts, must also be included in the preparation of the procurement.
The rights, obligations and responsibility of the organisation's management and the persons responsible for the process(es) upon the implementation of the internal control system and guaranteeing its efficiency have been determined.	Article 3.6.1 of the articles of association of RBE states that the company has an internal control system, but the procedures do not clarify how the management of the private limited company implements the internal control system or what guarantees its functioning, what are the rights, obligations and responsibility of the persons responsible for the processes upon the implementation and guaranteeing the effectiveness of the internal control system. However, the roles and responsibility of the project manager and project team upon the organisation of procurements and the management of contracts have been highlighted in the new project management procedure.
Unambiguous and clear rules about the decision process have been adopted and published in the case of all decisions.	The roles of the Management Board and the Supervisory Board in decision-making have been determined in the articles of association. The change management principles have been established in the project management procedure.

[53] The internal control roles have been developed on the basis of the "Optional guidelines for organisation of internal control systems of local governments" of the Ministry of Finance.

The descriptions and risks of processes and the measures implemented for reducing the risks have been reviewed in relation to changes in the organisation's environment or changes in its goals.	The project management procedure and the procurement procedure have been updated as the organisation grew. Although the risks of implementation of the RB project's activities should be described in monthly reports, it has not been recorded in the case of changes in the analysed procurements whether the risks were reviewed or risk management measures were taken, as there was no risk register at the time. For example, the first procurement for the Muuga freight terminal failed, but it has not been recorded whether risk management measures were implemented to ensure the success of the subsequent procurement and whether risks were assessed to avoid similar situations in similar procurements.
RISK ASSESSMENT	
Risk management principles have been established in the organisation.	Rail Baltic Estonia OÜ has assessed the risks and an initial risk management system is in use. A comprehensive risk management system is being established, i.e. the working principles of the working group of risk must be specified and owners must be found for risks. The new risk management system should also be compatible with the RBR risk management system.
The organisation regularly (at least once a year) identifies and analyses the risks that jeopardise the achievement of goals and, if necessary, decides on the implementation of risk management measures.	Risks were assessed in the risk analysis prepared in 2017. The analysis of construction logistics that will be commissioned also covers risks. A risk working group has been created and they have met a couple of times, but no minutes have been taken of the meetings and the outcomes have not been recorded.
The internal control system and risk management system have been integrated, i.e. risk assessment and implementation of risk management measures are parts of everyday activities.	The risk management system must be updated. The project manager regularly assesses the risks related to the project, but the results of such assessments are generally not recorded in writing. Risk management measures are used in the everyday work of RBE, e.g. contracts include measures regarding breaches, working groups have been formed (risk, procurement and technical working groups). No procedures for regular risk assessment and use of risk management measures have been developed.
INSPECTION ACTIVITIES	
The bases for planning and carrying out procurements have been established.	Rail Baltic Estonia OÜ has also established a public procurement plan for the implementation of the Rail Baltic project every year, which sets out the public procurements to be carried out during the year, their estimated cost and the person responsible for the procurements.
The procurement plan is approved and published on the website.	The procurement plan is approved by the Supervisory Board of RBE. The procurement plans are publicly accessible on the RBE website.
The persons responsible for procurements and the deadlines of procurements have been determined.	The deadlines and persons are determined in the procurement plan.
Removal and notification principles have been established for the prevention of conflict of interest.	The members of the procurement committee must sign a declaration of no conflict of interest.
The grounds for the formation of procurement committees have been set forth.	The grounds for the formation of a procurement committee have been given in the RBE procurement procedure.
Procurements are documented and retained.	The proceedings of the analysed three procurements have been documented. According to the procurement procedure, the company documents and retains the documents related to procurements (incl. e-mail correspondence) to the extent that makes it possible to check the selection of the type of procurement, the organisation of the procurement and the selection process retroactively and the purposefulness and lawfulness of the company's activities can be assessed.
The errors/problems in procurement are analysed and processes are improved on the basis of such analyses.	There is no written record of whether the errors/problems are analysed. The risk register is still being created.
INFORMATION AND COMMUNICATIONS	
It is guaranteed that important information reaches all necessary management levels, incl. the information that concerns planning the company's activities, management of the risks related to activities and deviation from plans.	The Management Board regularly gives the Supervisory Board an overview of completed activities, further plans and major risks. The project team and the Management Board hold meetings every other week, where the project managers give the Management Board an overview of the

	current status of the activities. The specific content of the meetings is not known, as no minutes are taken.
There are principles for procurement of relevant external information – about the market situation, changes in legislation and the economic environment, etc. Principles have been agreed for improving the quality of procurement and contracts, e.g. for the inclusion of an external expert, ordering analyses and research, or conducting interviews.	According to RBE, market research is carried out before each procurement, but it is not recorded in writing. No market research recorded in writing was carried out before the three analysed procurements. Clause 27 of the procurement procedure of RBE stipulates that the Management Board will include external advisers in the organisation of procurement if necessary. This option has been taken.
A reporting procedure has been established in the organisation. The reporting lines have been established and they are regularly reviewed.	A project management procedure has been established in the company and it describes the rules of reporting related to the project, pursuant to which the project manager: ▪ collects data about the ongoing project from the members of the project team regularly, at least once in two weeks; ▪ submits an interim report to the steering group of the project once a month; ▪ submits an action report to the Management Board once a quarter; ▪ submits information about the project budget to the financial analyst. Risk reporting has not been fully developed yet. The project management procedure was not in effect at the time the procurements analysed by the National Audit Office were carried out. The project management procedure was approved at the time of the audit and the National Audit Office could therefore not analyse whether internal reporting was functioning.
SUPERVISION	
A constant procurement and contract monitoring system is integrated in the organisation's processes	The status of procurements and contracts is monitored with the schedule prepared by RBR. The Supervisory Board of the company also monitors the progress and status of projects via working meetings and Supervisory Board meetings. The MEAC checks the eligibility of the project activities[54].
The effectiveness of the internal control system is regularly assessed. The shortcomings in internal control have been identified and referred to the parties responsible for rectifying them at the right time.	The effectiveness of internal control has been assessed every year since 2016 when the respective work has been ordered from external auditors, who checked, among others, whether RBE has established an internal control system that complies with the requirements of the Public Procurement Act. The auditor did not find any significant conflicts with the PPA.
The professional activities of an internal auditor have been organised in the organisation.	The position of internal auditor has not been created in RBE.
Action plans have been prepared and follow-up operations have been carried out for the correction of deficiencies in internal control and analysis of reasons to check whether the deficiencies have been eliminated in time.	RBE has ordered an inspection and opinion of the effectiveness of its internal control system from an external auditor since 2016. No significant deficiencies were found in the system by the external audit.

Source: National Audit Office

[54] Checks whether activities have been carried out in such a manner that their funding complies with the requirements of the grant agreements, i.e. the activities are eligible.