



INTERACT Point Managing Transition and External Cooperation

Financial Management of Territorial Cooperation Programmes

15-16 May 2008, Bucharest – DAY 2

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Financial control in INTERREG

**Control, correction and closure**

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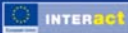
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What is control?

**Control is a process which aims at:**

1. Providing a firm understanding, knowledge or certainty of action
2. Adjusting actions to requirements
3. Prevention of unwanted results from ongoing actions

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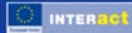
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### What is the purpose of Control in INTERREG?



- Provide security that ERDF funds are used properly (liability)
- Help programme delivery
- Avoid or correct irregularities quickly (managing a problem instead of a crisis)

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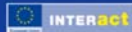
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### Financial Control in INTERREG – Tips



#### Keep it simple

- Ensure dialogue between control bodies and with projects
- Avoid the 'double management' trap
- Provide as much information as possible
- Try to get some agreement on common standards for the programme
- Try not to ask the EC for clarification

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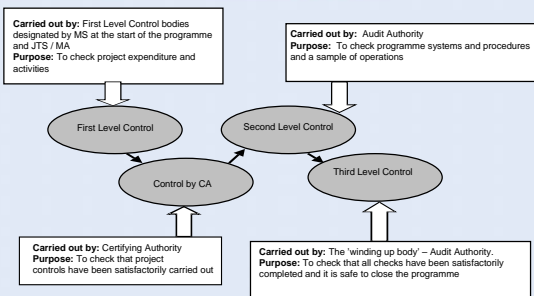
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### Financial control structure in Territorial Cooperation programmes 2007 – 2013



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Other control bodies 

- Co-financing organisations
- Member States
- **Commission Audit Service**
- **Court of Auditors**
- **OLAF**

} Checks are rare –  
but always possible

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First Level Control 2007 – 2013 

**Art 16 EC 1080/2006**

*"In order to validate the expenditure, **each Member State** shall set up a control system making it possible to verify the **delivery** of the products and services co-financed, the **soundness** of the expenditure declared for operations or parts of operations implemented on its territory, and the **compliance** of such expenditure and of related operations, or parts of those operations, with Community rules and its national rules."*

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First Level Control 2007 – 2013 

**Art 16 EC 1080/2006**

*"(...) each MS shall **designate the controllers** responsible for verifying the legality and regularity of the expenditure declared by each beneficiary participating in the operation.*

*Each MS shall ensure that the expenditure can be validated by the controllers within a period of **3 months**"*

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- MS are responsible for designation of first level controllers
- Preferably a list of first level controllers (name, address, contact details, etc.) should be provided by the time Art. 71 declaration is submitted to EC
- MS assign a first level controller to programme/project
- MS may decide to designate a single controller for the whole programme area
- Internal FLC will not be possible

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**First Level Control includes:**

- **Formal check** that expenditure has been calculated and documented in the proper way and is eligible (First Level Controller)
- **Activity check** that all expenditure relates to approved and relevant activities (First Level Controller / MA / JTS)
- In some cases '**on-the-spot**' checks (First Level Controller / JTS / MA / MS)

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- **Compliance with EC and national rules on:**
  - Eligibility / eligibility time-wise
  - State aid
  - Public procurement
  - Publicity and information
  - Protection of the environment
  - Equal opportunities
- **Is there a sufficient audit trail?**
- **Is there evidence of activities and deliverables?**
- **Is there a correct reflection of project progress and financial information in report**

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**First Level Control with Lead Partner Principle**

**Securing the audit trail**

- Who keeps documents?
- Do all project partners know the requirements?
- Is the audit trail secured down to all beneficiaries?
- LP's role in First Level Control

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**The Lead Partner Principle**

**Lead Partner Principle:**

- Primarily concerned with project content
- Lead Partner does also have a control role however
- Requires clarity about control and audit responsibilities
- Requires that Lead Partners provide accurate and reliable information to all partners and the programme bodies assist them in this process

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**Control procedures in 2007- 2013**

1	2	3	4	5
PARTNER	LP	MA	MS	CA
PARTNER				
LP				
All project partners (including LP) draw up statement of expenditure and have it checked by nationally designated first level controllers.	LP checks that all claims have been certified by the approved controllers. Draws up an aggregate project claim (calculations may also be checked by LP controller)	MA (possibly delegated to JTS) checks certification again. Also checks reports to ensure the project is being delivered in accordance with the approved application.	MS responsibility to set up a system (possibly delegated to MA/JTS) including on the spot checks of a sample of operations checking administrative, financial, technical and physical aspects as appropriate.	CA checks a sample of the project claims to confirm that the work that has been done provides a sound basis for making the programme claim.

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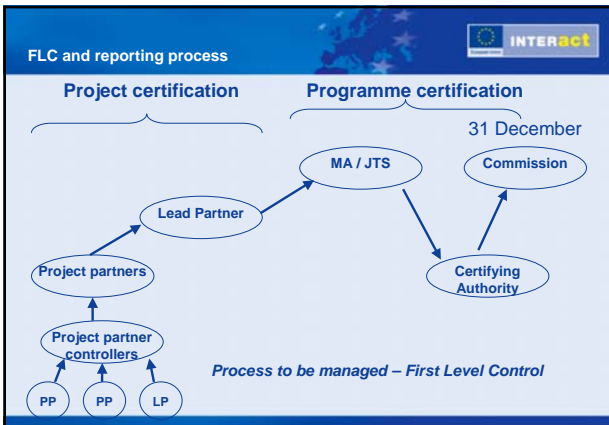
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**Reporting questions**

**Key issues to decide on when developing a financial control system:**

- How long will it take the appointed controllers to control expenditure?
  - 'Each Member State shall ensure that the expenditure can be validated by the controllers within a period of three months'
- When does the programme need to set the reporting deadline (if used)?
  - Depends on how long it takes the programme to process reports and claims in time to the get the expenditure included in the claim to the Commission
- What will happen to partners that cannot have certified statements ready in time?

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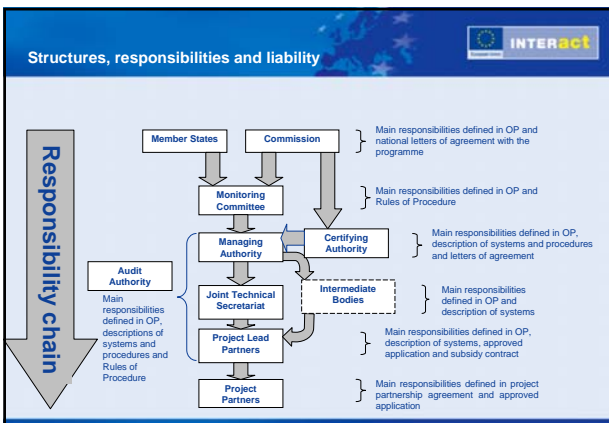
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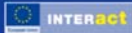
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Structures, Responsibilities and Liability



- Liability passed down to project partner level
- Burden of confirming that responsibilities have been fulfilled rests with FLC
- Subsequent control is really a check of the quality of FLC
- FLC used to be often outside formal programme structures (and information flows). Not any more!

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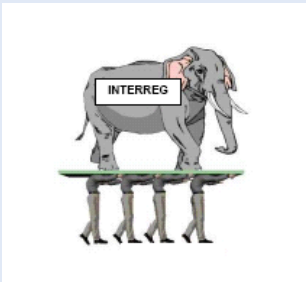
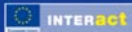
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The whole system of INTERREG rests on the shoulders of First Level Control



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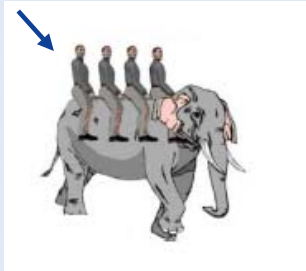
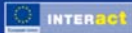
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Second and Third Level Control



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The purpose of First Level Control 

**Art 13 EC 1828/2006**

*“The verifications to be carried out by the managing authority...shall cover administrative, financial, technical and physical aspects of operations, as appropriate.”*

➤ Everything

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The purpose of First Level Control 

**Art 13 EC 1828/2006**

*“Verifications shall ensure that the expenditure declared is **real**, that the products or services have been delivered in **accordance** with the approval decision, that the applications for reimbursement by the beneficiary are **correct** and that the operations and expenditure **comply** with Community and national rules.”*

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The purpose of First Level Control 

**Art 13 EC 1828/2006**

*“They shall include procedures to **avoid double financing** of expenditure with other Community or national schemes and with other programming periods.”*

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The purpose of First Level Control 

**Art 13 EC 1828/2006**

*“Verifications shall include the following procedures:*

- (a) **Administrative** verifications in respect of each application for reimbursement by beneficiaries;*
- (b) **On-the-spot** verifications of individual operations.”*

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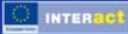
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First Level Control – how it will work? 

**Art 16 EC 1080/2006**

*“(…) each MS shall **designate the controllers** responsible for verifying the legality and regularity of the expenditure declared by each beneficiary participating in the operation.*

*Each MS shall ensure that the expenditure can be validated by the controllers within a period of **3 months**”*

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Characteristics of First Level Control 

- Covers 100% of the expenditure claimed
- Takes place every time project makes a payment claim
- Takes place at the beneficiary (partner) level
- Expenditure which has not been certified by FLC cannot be included in programme payment claim to EC

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First Level Control – findings 

Amount of expenditure eventually rejected during FLC varies enormously:

- Between 3% and 25%
- Proportionality?

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First Level Control – Check of activities 

- Check of activities almost always carried out at least in part by the programme – JTS / MA
- Need to be aware of potential conflicts between management and control functions

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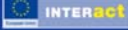
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On the spot checks 

- Every programme has to make its **own decision** on the nature of on-the-spot checks
- These checks can reveal **project weaknesses** with project management and control systems that have gone unnoticed
- To make on-site checks as effective as possible, programmes can send projects a **checklist** informing them what information should be available

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**Challenges for the First Level Control** 

**Proof of existence depends very much on the project output**

- Investment projects
- 'Soft' projects e.g. networks



*(...) the only projects which should be approved are those which present a clear work programme with, for each activity, an identifiable product which makes it possible to check afterwards whether or not the event occurred*

- conference papers
- a website
- implementation document
- a report on the activities undertaken

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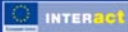
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**On the spot checks** 

- Programmes doing visits normally check more than proof of existence
- Should these checks be part of formal procedures?
  - If not how should the results be used?
- Do they justify the expenditure?
- The 'sleep well at night' effect

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**IIIB NSR checklist** 

**What is checked during on-the-spot checks?**

1. **Time line:** Delays? How long? Reasons and implications? Action to be taken?
2. Is **spending** on target as in original plan (ERDF)? Amount claimed to date? Difference? Expected final amount claimed? Reasons for difference? Implications? Action to be taken?
3. Are **outputs** as in original plan? What has been achieved to date? Has it been checked? Quality? Reasons for difference and implications? Action to be taken?
4. **Project management system:** Are systems to ensure effective implementation in place? Are procedures for monitoring and controlling expenditure effective? Implications and actions to be taken?
5. **Partnership:** What role each partner plays in the implementation? Are there problems in partnership? Implications and actions to be taken?
6. **Discrepancies** between payments claimed and activities carried out
7. Are **project goals** shifting during implementation?
8. Are there significant **changes of budget**?

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**Common problems spotted by the First Level Control**

- Reporting non-eligible expenditure
- Project partners' budgets are exceeded
- Budget lines are exceeded
- Costs are reported under wrong budget lines
- Costs do not correspond to the activity report
- Changes in the partnership
- Wrong exchange rate used
- Failure to comply with procurement rules
- Failure to comply with publicity rules
- Lack of adequate evidence for costs
- Lump sums charged instead of real costs
- VAT
- And in your experience...?

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**Irregularities**

## Case Study 3 First Level Control

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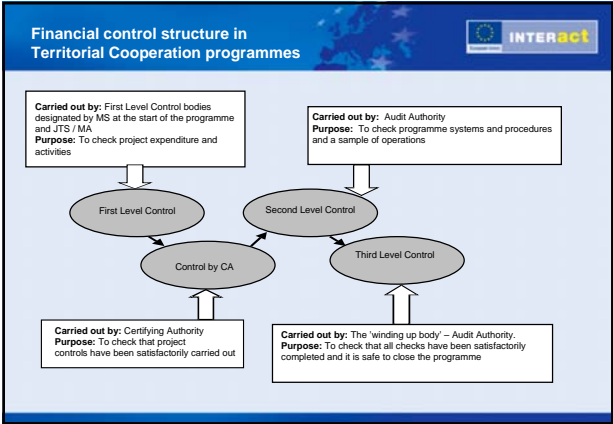
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**Control by Certifying Authority** 

- After processing by JTS / MA, payment claims are forwarded to CA
- CA certifies the legality and regularity of expenditure declared to the EC (interim and final)
- CA functionally independent of MA and AA
- CA ensures the reliability of the MA's work
- MA informs CA of the procedures operated to:
  - Verify the delivery of products and services cofinanced and the reality of expenditure claimed
  - Ensure compliance with the applicable rules
  - Maintain the audit trail
- Guidance documents available on the control by CA

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**Managing Authority vs Certifying Authority**  
(based on CDRR-06-0004-00) 

Certifying Authority	Managing Authority (or JTS)
1. Core function: certifying expenditure declared to the Commission 2. Ensuring the reliability of the MA's work 3. Claims to the Commission 4. Accounting records on programme level	5. Approves individual project claims 6. Main contact to project LPs 7. Verifies that products and services are delivered 8. <b>On-the-spot verifications of operations</b> 9. Ensures there is system for recording and storing project accounting records 10. Ensures that project documents and procedures meet requirements for adequate audit trail

- Clear separation of functions and independence essential
- There should be no duplication of control – satisfactory results of e.g. systems controls of the MA can lead to limiting of CA's actual control work

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**Second Level Control** 

**A two-step process:**

- Systems audit to ensure effective functioning of programme systems
- Audit of sample of operations to verify expenditure declared

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**Second Level Control carried out by Audit Authority** 

- Regulations establish new body – Audit Authority – for overseeing programme audit requirements
- Within 3 months of OP approval each MS involved will nominate a representative to a “Group of Auditors” per programme, which will assist the AA
- AA can be authorised to operate for the whole programme, without a group of auditors

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**Audit Authority** 

- Formal programme body with tasks set out in the regulations
- Responsible for systems checks and sample checks on operations (current Art 10)
- Ensures audits meet international audit standards and are carried out on an appropriate sample
- Presents Audit Strategy for the programme to EC within 9 months of OP adoption
- Writes Annual Control Report with Opinion on the operation of management and control systems
- Preparing and submitting the 'winding up declaration'

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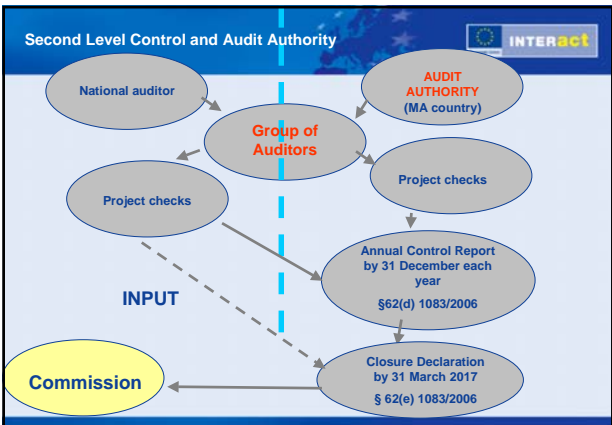
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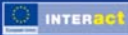
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AA (= Audit Authority)	AA + GoA (=Group of Auditors)
<ul style="list-style-type: none"> <li>- Systems check</li>   <li>- Integrated reports</li> <li>- Reports to EC</li> </ul>	<ul style="list-style-type: none"> <li>- Audit strategy</li> <li>- Selection of sample of operations</li> <li>- Carrying out checks</li> <li>- Partial (national) reports</li> </ul>

*AA is a coordinating body for the MSs, contact point with the EC and usually SLC body in the MA Member State*

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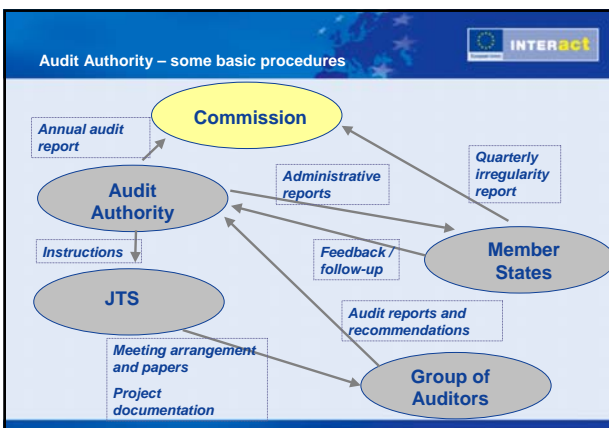
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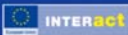
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- Issues to address when setting up Audit Authority**
- Independence
  - Staffing and work flows?
  - Budget? And who will pay for it?
  - Sub-contracting or designating a public body?
  - Coordination with FLC?
  - Role in follow-up of problems identified?
  - Advisory / Training function?
- Answers will depend on the size of the programme and the attitude of participating MS*

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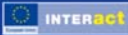
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**Control system – Timing** 

- There can be no repeat of long delays in setting in place control and audit systems
- Vital to be in place early to accompany programme development and implementation
- Payments will not be made without proper systems in place

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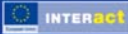
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**Second Level control – content** 

- Verify effectiveness of the management and control systems
- Identify corrective measures to eliminate risks in the systems
- Prevent and take actions against irregularities
- Recover amounts lost as a result of irregularities or negligence
- Verify the presence of a suitable audit trail
- Verify selectively declarations of expenditure at various levels
- Verify the correctness of accounting records at final beneficiaries
- Facilitate the identification of possible risks in the execution of operations
- Verify that the national co-financing has been made available

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**What information will Second Level Control provide?** 

- Are the problems encountered of systemic character?
- If so, what is the scope of operations affected?
- What are the causes of the problems?
- What corrective and preventive action is required?

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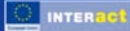
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Selection of a sample for the SLC  
2007 – 2013



- **Representative random statistical sample**
- Not 5% of programme funds but enough to ensure at least **60% confidence level**
- Systems and procedures checks must continue **throughout programme lifetime**
- AA must give **opinion** on:
  - Effectiveness of systems
  - Accuracy of expenditure declaration
  - This is the first time that "SLC body" must express formal opinion on the audit results

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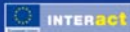
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Second Level Control – common problems 1/2



- Commission Reg. (EC) No 1260/1999 and Commission Reg. (EC) No 1685/2000 amended by Commission Reg. (EC) No 448/2004 were **unknown**
- Procurement rules were unknown
- **Documentation not available to demonstrate a clear link between work actually executed and the declared expenditure**
- The **EU emblem** was missing on (all) publications and the relevant papers had already been distributed
- **No documents** and evidence for the co-financing were available
- The project partner had changed address without informing the programme
- The project title was missing from some invoices

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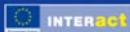
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Second Level Control – common problems 2/2



- Financial departments are decentralised and the book-keeping system could not be checked
- **Payments were without invoices, only bank account statements**
- One invoice was included twice
- There was one invoice with a partial payment where an advance had been paid prior to service completion
- Invoices from one sub-partner were paid *after* payments were received from the EU
- Personnel costs include overheads without a comprehensible calculation
- Exchange rate - invoices contained two different exchange rates
- **The financial report was not signed by the first level controller**

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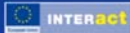
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Second Level Control – Questions & Challenges



1. National controllers are not appointed or appointed too late to fix problems
2. International audit firms are appointed but resources are very limited
3. National controllers are overworked – the control work is delayed and systemic errors are not found until it is too late
4. Roles and responsibilities are unclear e.g. the controller delivers his / her report, what happens next?
5. Project control is not given priority e.g. the task is forgotten or given to people without a background in audit or experience in the field
6. The findings are politically inconvenient – lack of support from MS
7. Eligibility rules vary between countries e.g. if common rules are not in place or are being challenged, control of adherence to the rules is difficult

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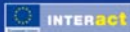
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Second Level Control now and in the future – SUMMARY



2000-2006	2007-2013
MSS shall organize SLC checks carried out by SLC group	AA is a formal body to carry out SLC audit AA is set up at the start of the programme
MSS develop and audit strategy for the whole programming period specifying: • Objectives of the audit work • Who will carry the audit work • How to ensure Art.10, Art 15 requirements are fulfilled	AA presents <b>audit strategy</b> (within 9 months after OP approval)
MSS inform the Commission of the organisation of management and control systems within 3 months of the approval " <b>Art 5 Declaration</b> " (it includes the provisions for the audit of management and control systems)	AA approves the <b>description of management and control systems</b> (within 12 months after OP approval)
MSS submit <b>annual Art 13 report</b> on the execution of the sample checks (by 30 June) It also includes updates of the Art 5 declaration	AA submits <b>annual control report</b> by 31 December
Not specified who submits closure declaration. Must be a body independent of the management and control system	AA issues <b>annual audit opinion</b> AA submits the <b>closure declaration</b>

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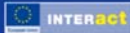
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Lessons from INTERREG III



Second Level Control:

- Lack of systems audits means that systemic problems have gone undetected
- Project sample checks often started too late (and well past the date when constructive improvements could have been recommended to other projects)
- Annual reports to the Commission very rarely report irregularities
- Annual reports not good enough at identifying improvements

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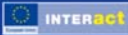
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Second Level Control – conclusions... 

The SLC findings suggest the weakness of the first level control in place in many cases

Are they rare cases or part of a general pattern?

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Irregularities 

Problems detected by First Level Control

- Must be resolved before project closure
- If final project payment retention is big enough, should not be a problem

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Irregularities 

Problems detected by Second Level Control / higher level control body

- May happen after closure and final payment to project
- May require recovery procedure

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**Irregularities** 

**What is an irregularity:**

*"... any infringement of a provision of Community law resulting from an act or omission by an economic operator which has, or would have, the effect of prejudicing the general budget of the Communities by charging an unjustified item of expenditure to the Community budget" (Art 1 (EC) No 2168/2005)*

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**Irregularities** 

**How do we handle irregularities:**

- Below the €10.000 threshold – the programme can deal with the irregularity directly
- Above the €10.000 threshold – the irregularity must be reported to OLAF

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**Irregularities under the reporting threshold 2007 – 2013** 

- MS shall keep accounts of amounts below €10.000 threshold
- MS shall keep accounts of amounts recovered or withdrawn following cancellation of the contribution to an operation
- MS shall repay the recovered amounts to the general budget of the EC

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2007 – 2013  
MS do not need to report irregularities if:



- Irregularity is due to **bankruptcy** of the beneficiary
- Beneficiary voluntarily **informed** MA and CA about it regardless if payment to beneficiary has already been made or not
- MA and CA **corrected it before payment** was made to beneficiary and before inclusion of the irregular expenditure in a statement of expenditure submitted to the Commission

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Irregularities and recoveries in 2007 – 2013



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    graph TD
      A[Certifying Authority initiates recovery] --> B[Lead Partner repays funds]
      B --> C[Lead Partner recovers funds from partner]
      C --> D[If unsuccessful, partner Member State pays funds to Certifying Authority]
      D --> E[Certifying Authority repays Lead Partner]
  
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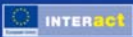
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MS responsibilities: Recoveries and dealing with irregularities in 2007 – 2013



- **Detecting** and correcting irregularities (Art 17 ERDF)
- **Recovering** amounts unduly paid – reimbursing to the CA any irrecoverable amounts unduly paid to partners on the MS's territory
- **Reporting** to the Commission each quarter any irregularities which have been the subject of a primary administrative or judicial finding
  - A report must also be submitted if there are no irregularities
- **Following up** in each quarterly report on actions taken as a result of previously reported irregularities

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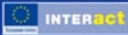
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Recoveries 2007 – 2013 

- Requires strong procedures with deadlines for e.g. how long the Lead Partner should use on attempting to recover funds
- MS need to be kept informed from the beginning
- Implementing Reg. (Art 28) contains useful definitions of what to report
- All irregularities need to be subject of an administrative or judicial report

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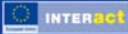
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Recovery procedure 

**Recovery procedures** set out how to deal with irregularities at various stages in the project lifecycle including:

- A clear definition of who does what, when and how
- Deadlines defining when a MS should take over
- The completion of a standard form to inform the National Authority of an irregularity

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Programme life cycle 

	Start Up	Implementation		Closure
<b>Programme</b>	<ul style="list-style-type: none"> <li>• Bodies</li> <li>• Systems</li> <li>• Tools</li> <li>• Documentation</li> <li>• Allocation</li> </ul>	<ul style="list-style-type: none"> <li>• Funds management and payments</li> </ul>	<ul style="list-style-type: none"> <li>• First and Second level control</li> <li>• Eligibility</li> <li>• Irregularities</li> </ul>	<ul style="list-style-type: none"> <li>• Closure statement</li> <li>• Errors</li> <li>• Eligibility</li> </ul>
<b>Project</b>	<ul style="list-style-type: none"> <li>• Budget plans</li> <li>• Application</li> <li>• Contracting</li> <li>• Partnership Agreements</li> </ul>	<ul style="list-style-type: none"> <li>• Management of spending</li> </ul>	<ul style="list-style-type: none"> <li>• Monitoring</li> <li>• First level control</li> <li>• Reporting</li> </ul>	<ul style="list-style-type: none"> <li>• Final payments</li> </ul>

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**Effective closure depends on:**

- Outputs of operational controls
- Cooperation between controller, MS and the programme bodies
- Swift completion of processes

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**First Level Control**

As part of the final report, the project submits a compiled report in which the project auditor:

- Concludes on the audit of each project partner and the entire partnership
- Declares any qualifications
- Declares whether or not the project fulfils the requirements of Art 4 (EC 438/2001)

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**Eligibility after Closure – in the short term:**

- Invoices coming in after closure of project activities but relating to activities in the eligible period
- Costs incurred after 31 of December 2008 and purely linked to programme closure e.g. TA, staff, audit costs (fixed price), printing costs of the final report, winding-up body are eligible and can be covered by the new programme's TA budget

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**Eligibility after closure 2/2**

**Eligibility after Closure – in the longer term:**

- Filing requirements are not adhered to – accounting evidence is lost
- Project specific requirements are not adhered to e.g. material investments are sold

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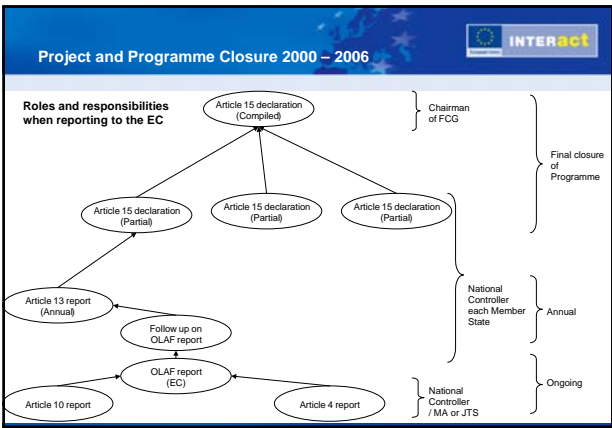
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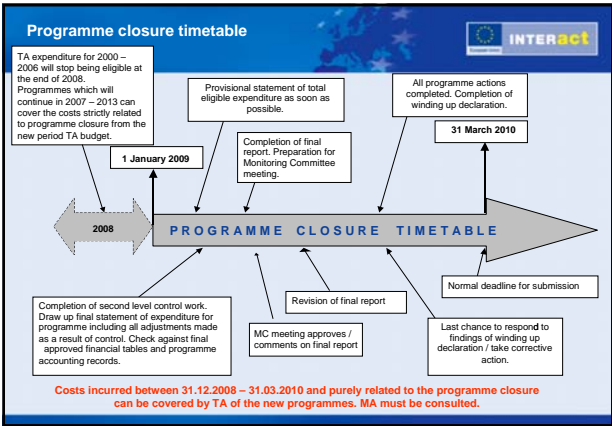
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Retention of 5% programme funds by the Commission 

- Last 5% of programme funds is retained
- Programmes' decision: how much to retain from projects (5% or e.g. 20%). NB It has changed now!
- The remaining funds will be paid as soon as a programme receives final payment from the Commission

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Closure of the Managing and Paying Authorities 

**Final 'official' task** is to draw up the final report, statement of expenditure and request for payment.

**Procedures for drawing up these documents must ensure that:**

- Amount claimed reconciles with programme accounting systems
- There is adequate supporting documentation
- Procedures followed give reasonable assurance that only eligible expenditure is included
- All control and audit issues have been resolved

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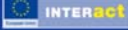
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The closing procedure – where is the firm ground? 

**The financial tables:**

- Changes were possible until the end of 2006
- The deadline for submission of a request for changes was 31 December 2006
- The post-2006 tables form the basis for the closing procedure (2% flexibility limit)

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The closing procedure – Commission requirements 

**The closing documents:**

- Audited statement of accounts and an application for the final tranche
- A final report
- A declaration on winding-up the assistance

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Winding up declaration – what is checked?  
2000 – 2006 

**A repeat check of controls at other levels, focusing in particular on:**

- The independence of the Art. 10 (EC 438/2001) body
- Sampling method used for the Art. 10 checks
- How the final statement was drawn up
- Nature and quality of the audit work carried out
- The implementation of audit recommendations and correction of errors

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Winding up declaration 2000 – 2006 

**Essential that work starts as soon as possible in 2008/2009**  
so corrective action can be taken.

All errors should have been **‘treated satisfactorily’**. Meaning:

- Reported to relevant bodies
- Amounts concerned deducted from statement of expenditure
- Recovery procedures launched when necessary
- Systemic errors corrected

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Opinion on "winding up" 

**Two negative results possible:**

- **No opinion:** For example, Art. 10 checks have been inadequate or serious management failures have not been addressed
- **Qualified opinion:** For example, sampling technique is weak, there is no formal procedure for identifying and treating systemic problems.

**Both delay the final payment and request to quantify the extent of the problems (how much money to deduct)**

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Frequency of irregularities – low or high? 

**Low / high frequency of irregularities and errors**

- Used to make a decision on the overall reliability of management and control systems
- Different importance of errors, e.g.
  - Formal vs. substantive
  - Financial impact
  - Systemic

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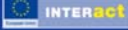
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Frequency of irregularities – max 2% is acceptable 2000 – 2006 

**2% error rate is the limit:**

- Based mainly on the findings of the Article 10 checks
- Taking account of the findings of other checks

**Qualified opinion unless MA and PA can take effective corrective action**

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**Most important to avoid systemic problems, since they:**

- Could lead to cut in funding for all measures / priorities where these systems / procedures are in place if corrective action cannot be taken

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**Thanks for coming!**

**Please let us know what you thought**

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