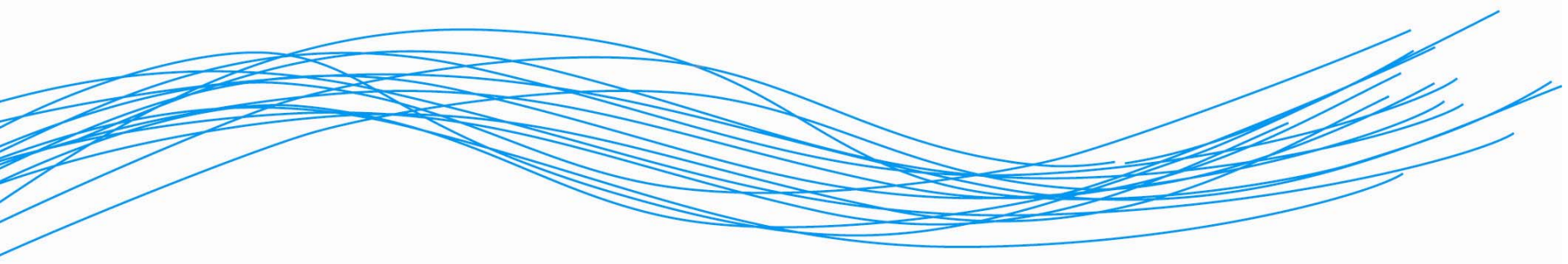


Cost Reporting in FP7

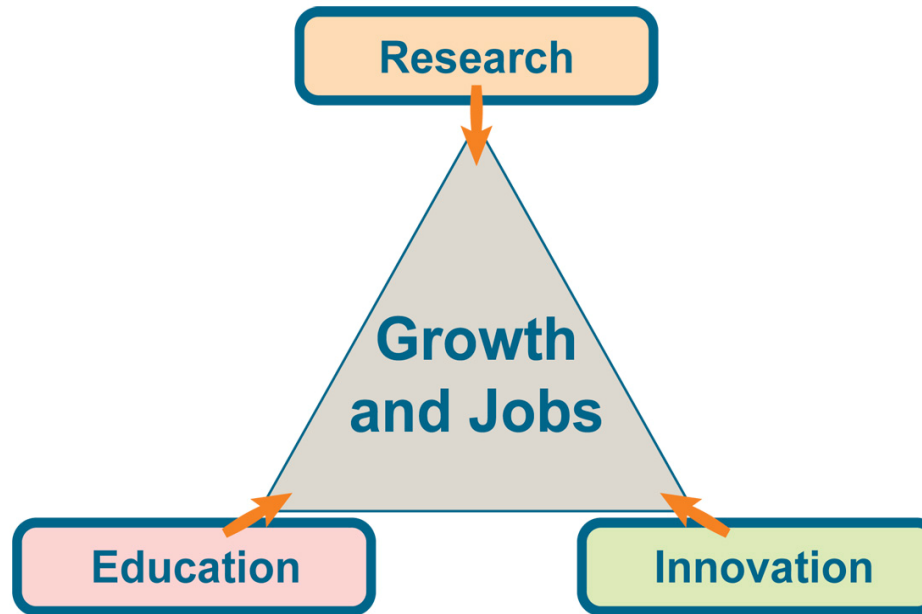
Hot spots from an auditors' perspective



FFG
Vienna
30/09/2010

European Commission
RTD.A.4 External Audits
René Sieron

Research policy is part of the Lisbon strategy

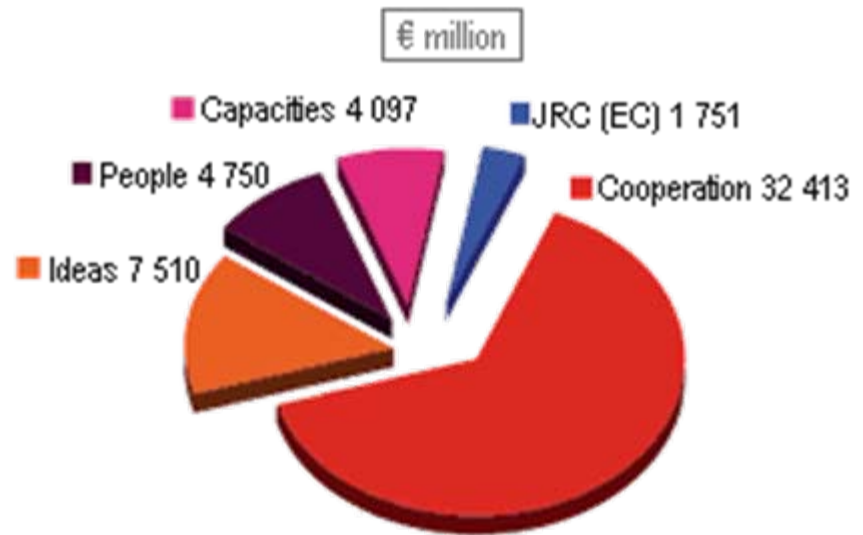


“Science and Technology” contributes to the **Lisbon** objectives: economic **growth**, **employment** creation, **environmental** protection, **social** challenges: fight **poverty**, improve human **health** and **quality** of life

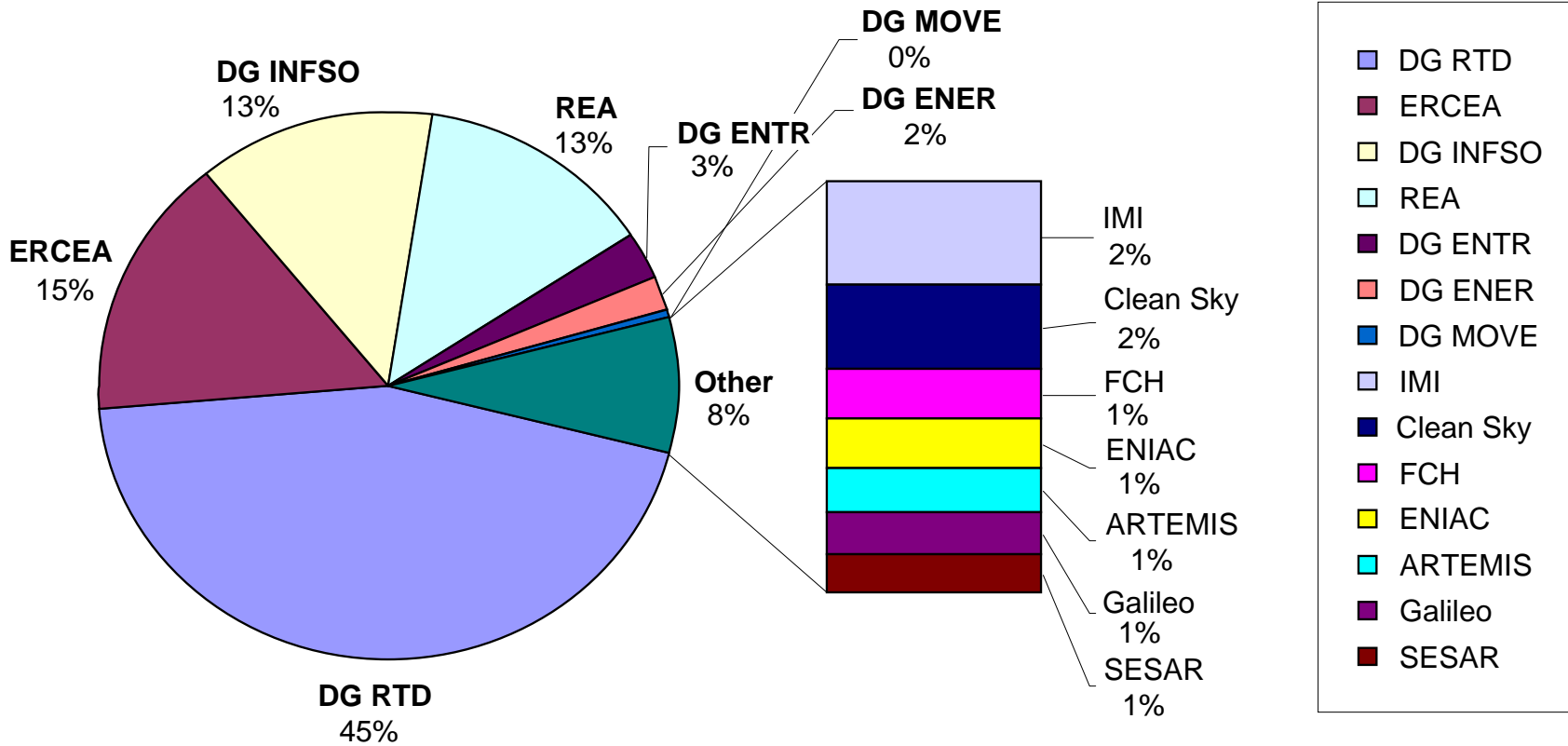
FP7 budget

Specific Programmes

- Cooperation
- Ideas
- People
- Capacities
- Nuclear Research



FP7 budget



FP6 → FP7

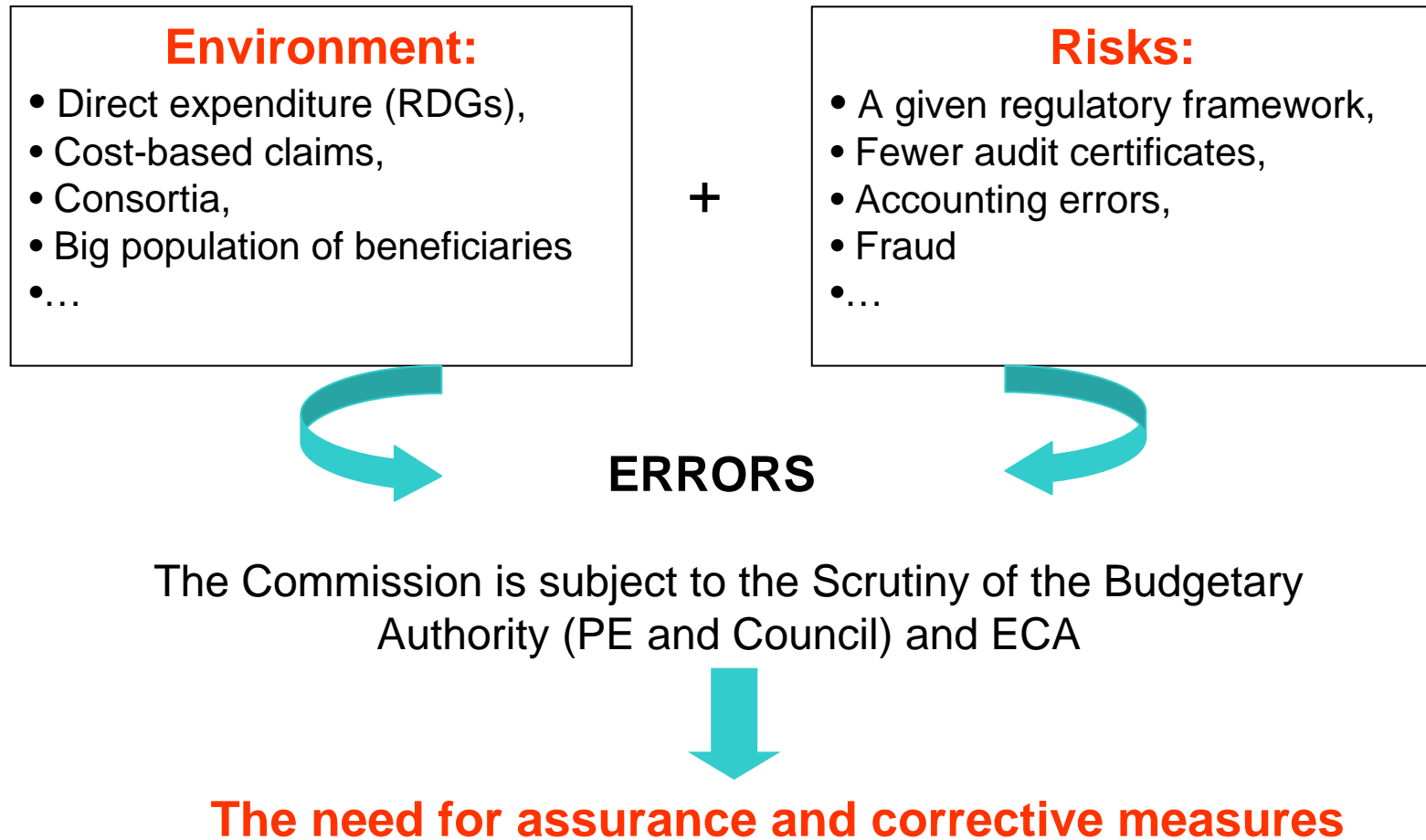
	FP6		FP7	Impact
% EU budget	3.5% (2006)	→	5.1% (2009)	Higher profile
Total allocation	17.5 billion €	→	53.2 billion €	Cost-effectiveness Auditing resources Audit coverage
Time line	5	→	7	Multi-annual strategy
Managing entities	4 research DGs	→	5 research DGs + 2 EAs + JTI's + Art.185	Enhanced co-ordination necessary

more money = more audits = more co-ordination

Error rates per Commission service (x6)
+
Multiple samples (x6 xN)
+
Many common beneficiaries
+
All sampling items must be audited
=

Need for stronger **co-ordination** across Commission services

- **co-ordination** of audit planning
- **cost-effectiveness** of audits
- **common audit approaches** across the Commission service
- **common interpretation of eligibility issues**
- **sufficient audit coverage for different parts of budget**

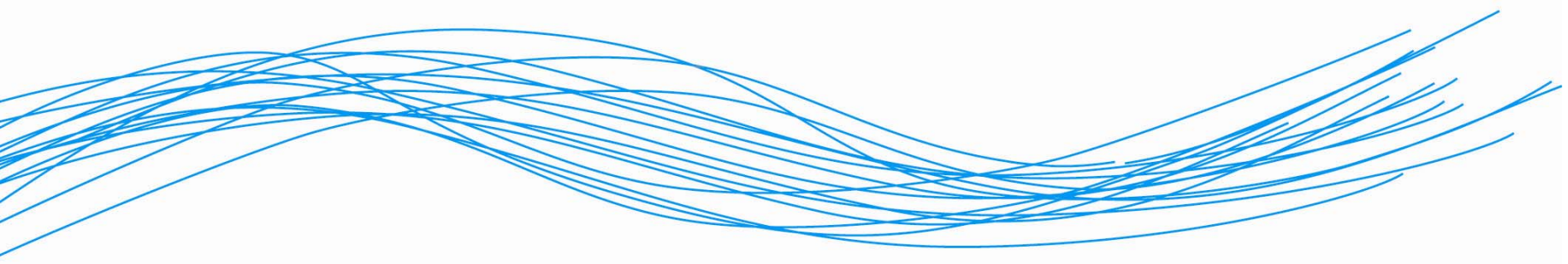


Why is the inherent risk important?  DG declaration of assurance

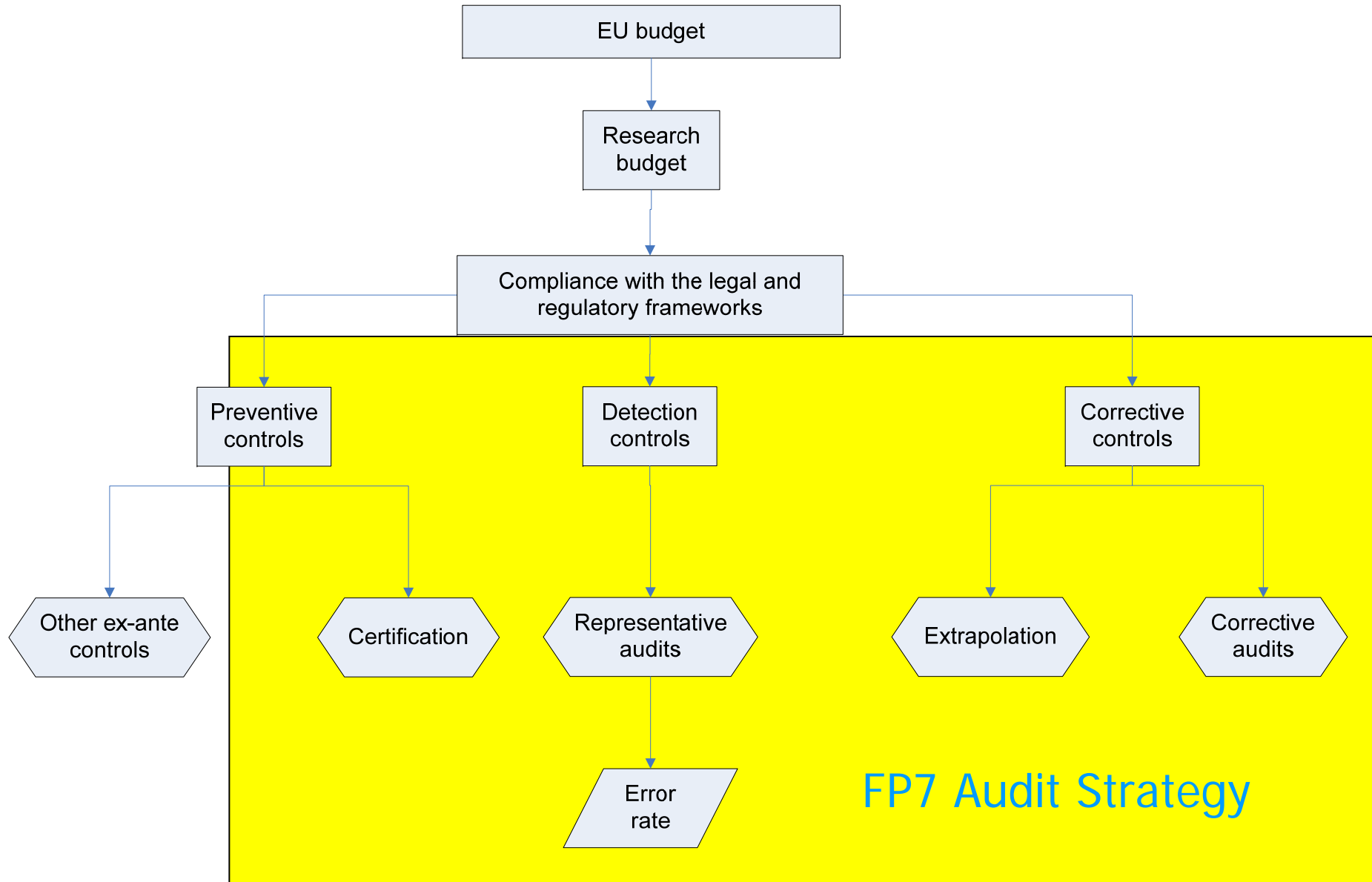
***I, the undersigned, Mr Robert-Jan Smits, Director-General of DG Research,
in my capacity as authorising officer by delegation
declare that the information contained in this report
gives a true and fair view [1]....
State that I have reasonable assurance...***

[1]= in this context means a reliable, complete and correct view on the state of affairs in the service.

Audit tools



Where do audits fit in ?



Audits on-the-spot

Ex post Audits by EC auditors (RTD-A.04)

- Approx. **30%** of audits
- Own resource audits
- Specific audits (follow-up, audit on request...)

Ex post Audits by Contracted audit firms (RTD-A.05)

- Approx. **70%** of audits
- Batch audits
- Supervision of the audit process by EC services

in-house or outsourced

Types of audit:

- Regular audits in line with the audit strategy
- Fusion audits
- Coal and steel audits
- Third countries audits
- Audits on Request
- Follow-up audits
- Technical audits & reviews

- Audits by the European Court of Auditors

Audit tools - certification



- **Certificate on the methodology for personnel and indirect costs (CoM)**
- **Certificate on the methodology for average personnel costs (CoMav)**
- **Certificate on the Financial Statements**



By Mr. Peter Härtwich

Purpose & Type of audits (1)

	Selection	Purpose
<p>Representative audits</p>	<ul style="list-style-type: none"> •Monetary Unit Sampling (MUS) methodology (95% confidence level, 2% expected error rate, 5% materiality threshold) •Cost statements as sampling unit •Samples from the whole population of each RDG/EA •Possibility of multiple samples 	<ul style="list-style-type: none"> •Determine the amount of error present in the population <p style="text-align: center;">↓</p> <p style="text-align: center;">Representative error rate</p> <ul style="list-style-type: none"> •Contribute to the Declaration of Assurance •<u>Corrective</u> as well as <u>representative</u>

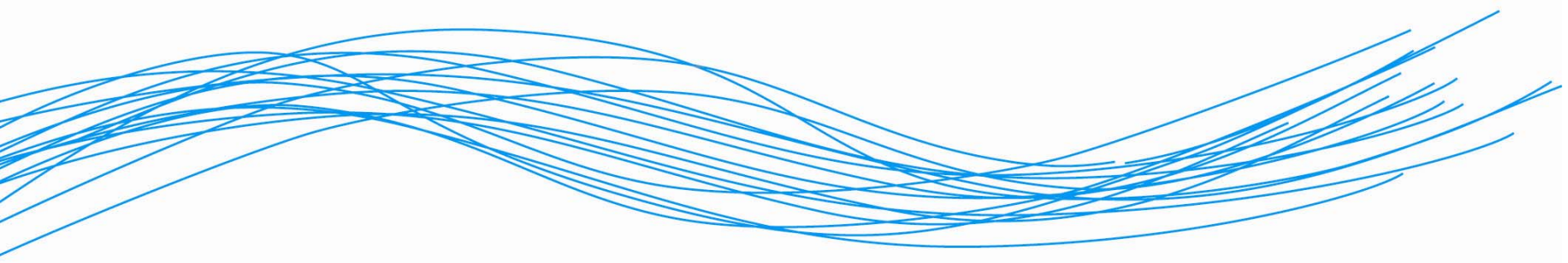
Purpose & Type of audits (2)

	Selection	Purpose
Corrective audits	<ul style="list-style-type: none"> • Focus on top beneficiaries (50% of the budget) • Specific risk profiles • Flexible in view of peculiarities present in the populations of different RDGs/EAs 	<ul style="list-style-type: none"> • Wide audit coverage • Identify and correct errors in a cost-efficient way • ‘Clean’ min. 50% of budget from systematic material errors • Long-term prevention of issues found (‘fixing the future’) • Fraud detection and prevention
Other types (system, scientific/technical ...)	<ul style="list-style-type: none"> • On request or pre-selected 	<ul style="list-style-type: none"> • Verify compliance with certified methodologies • Identify and correct systemic problems • Provide additional assurance on specific parts of the budget • Complement scientific audits

technical audit (TA) & technical review (TR)

- **TA** performed at beneficiary level, to assess the technical performance of beneficiary(ies) within specific work package(s) of the project
- **TR** performed at project level by Project Officers and/or external experts to give external advice to the Commission
- **TA** always done on the spot (up to 5 years after project end)
- **TR**: can be done remotely or on the spot
- **TA & TR**: Optional for all FP7 projects

Results



Participation of Austria in FPs

FP5 (421 beneficiaries)		
	Number of Contracts	Sum of EC Contribution
Total	794	183.979.437
FP6 (740 beneficiaries)		
Instrument/Project Funding Scheme	Number of Contracts	Sum of EC Contribution
Grand Total	1262	260.675.177
CA	159	20.894.387
CRAFT	87	9.501.416
IP	249	90.378.401
NOE	68	15.562.911
RTN	54	16.812.455
SSA	161	9.535.535
STREP	347	73.557.332
FP7(501 beneficiaries)		
Instrument/Project Funding Scheme	Number of Contracts	Sum of EC Contribution
Grand Total	720	195.514.053
CP	450	154.051.755
CP-CSA	36	9.119.518
CSA	221	27.959.584
NOE	4	2.344.686

FP5-FP7:

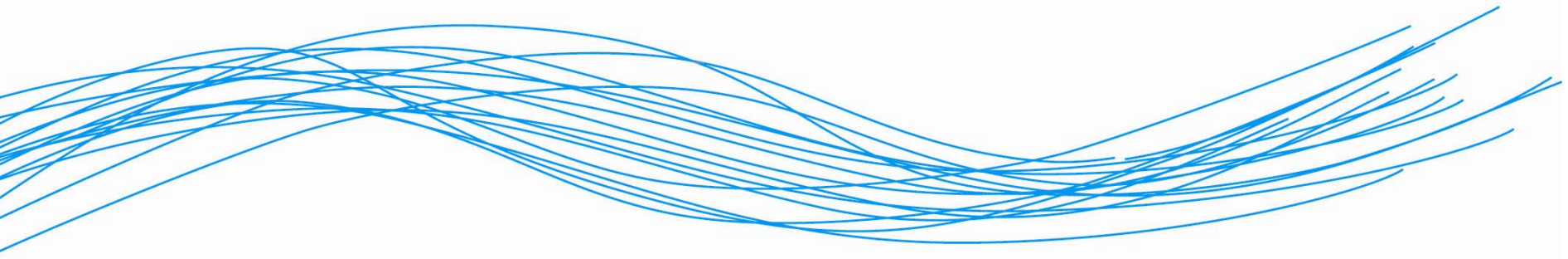
52 Austrian contractors have been audited

<i>Framework Programme</i>	<i>Sum of Audited costs</i>	<i>Sum of Adjustments</i>	<i>%</i>
FP5 Total (14 auditees)	4.613.152	163.291	3,5%
FP6 Total (28 auditees)	55.719.432	484.995	0,9%
FP7 Total (10 auditees)	1.850.848	-87.168	-4,7%
Grand Total	62.183.433	561.118	0,9%



RTD audits FP 6	No. of adjustments	% no. of negative adjustments	% of the total adjustment amount	% of the total costs accepted by Financial Officers
Adjustment to costs previously reported	88	3,8%	2,0%	0,2%
Audit certificates	3	0,1%	0,0%	0,0%
Consumables and computing	182	7,8%	2,7%	6,2%
Durable equipment	87	3,7%	3,1%	2,5%
Management of the Consortium	9	0,4%	0,1%	0,2%
Other costs	388	16,6%	8,3%	10,3%
Personnel	420	18,0%	46,6%	41,6%
Protection of knowledge	0	0,0%	0,0%	0,1%
R & T Development / Innovation / Training	7	0,3%	0,3%	0,2%
Subcontracting	90	3,9%	16,4%	13,7%
Total indirect costs	672	28,8%	14,5%	18,6%
Travel and subsistence	378	16,2%	1,3%	3,1%
Various others	13	0,6%	4,8%	3,3%
Grand Total	2337	100%	100%	100%

Frequent findings



Eligibility criteria

- Costs = **actual costs** <-> not budgeted nor estimated costs
- Costs = **economic** <-> non-excessive, not reckless, no profit
- Costs = **necessary to carry out** the project
- Costs = **charged in accordance** with the usual accounting principles (not made « on purpose »)
- Costs = **incurred and recorded** in the books **during the duration** of the project

Frequent findings (2)

- Direct costs = Directly attributable to the project
- Indirect costs = Attributable to more than one activity
- Problem: consideration under more than one cost category



Link all costs claimed to the project

Personnel costs

- Calculation of productive hours
- Budgeted costs
- Insufficient evidence of working times (time recording)
- Specific Issues: **e.g.** bonus payments, In-house services, third-party contributions
- SME/owner-managers

Personnel costs

Average costs can reflect actual costs
(if based on those)

but

Often deviation of costs charged from actual
costs incurred

Time recording



Basic Principles

Art II.15.1 of the FP7 model Grant Agreement:

*“...only the costs of the **actual** hours worked by the persons **directly carrying out work** under the project can be charged.”*

FP7 Guide to Financial Issues

- *Employees have **to record** their time on a daily, weekly, or monthly basis using a paper or a computer-based system*
- *The **time-records have to be authorised** by the project manager or other supervisor*
- *The complete time recording system should **enable reconciliation** of total hours in cases where personnel work on several projects*

HOWEVER...

Time sheets are not mandatory

A time-recording system is mandatory

A reliable time-recording system is mandatory

The reliability is assessed by the auditor independently

Additional evidences can be requested

Additional evidences can be requested always

Additional evidences are requested in the interest of the contractor

Example of daily full time-recording (per person)

Due to the fact that different activities have different reimbursement rates, work on EC projects is to be recorded not only differentiating by individual EC project but also by activities

The level of detail of this section is to be defined by the beneficiary. The Commission requests at least time-records by main activities

Absences are necessary to verify the accuracy of the annual productive hours used to calculate the hourly rates

Date	Mon 02/02	Tue 03/02	Wed 04/02
EC-Projects			
R&D Activities			
Project x		3	4
Project y		5	5
Demonstration			
Project x			
Project y			
Management			
Project x			
Project y			
Other Activities			
Project x			
Project y			
Other research projects and Internal activities			
Teaching			
Training			
National Projects			
(...)			
Absences			
Annual Leave			
Special Leave	8		
Illness			
Total hours	8	8	9

Other direct costs

- Ineligibility of direct taxes (i.e. identifiable VAT)
- Necessity and plausibility of purchases (not reckless)
- « Entertainment » costs
- Separation of direct and indirect cost items
- Double classification of a cost (e.g. travel)
- Internal invoicing
- Interests incurred on project funds



subsistence costs and accommodation related to project travel on the basis of flat rates per country

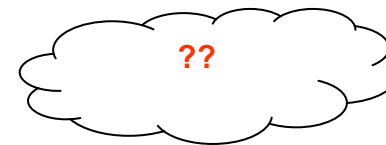
Indirect costs

- Industry, Trade:

$$\begin{array}{rccccccc} \text{Product} & & + & \text{indirect costs} & & = & \text{price} \\ 1 & & + & 0,2 & & = & 1,2 \end{array}$$

- Research:

$$\begin{array}{rccccccc} \text{Project work} & + & \text{indirect costs} & & = & \text{cost} \\ 1 & + & 2 & & = & 3 \end{array}$$



Indirect costs

- “...Indirect costs are all those eligible costs
- which cannot be identified by the beneficiary as being directly attributed to the project,
 - but which can be identified and justified by its accounting system
 - as being incurred in direct relationship with the eligible direct costs attributed to the project...”

Indirect costs

- Inclusion of ineligible cost items (cost of sales, teaching, research funded by other resources, provisions, cost of capital, ...)
- Unfair or unrepresentative allocation keys



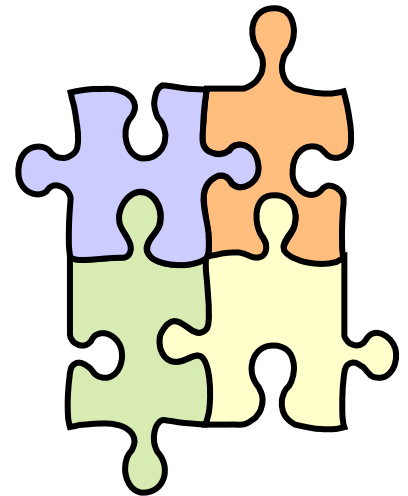
Recourse to published financial data of the beneficiary to retrace indirect costs claimed

(e.g. balance sheets, profit & loss statements)

Subcontracting

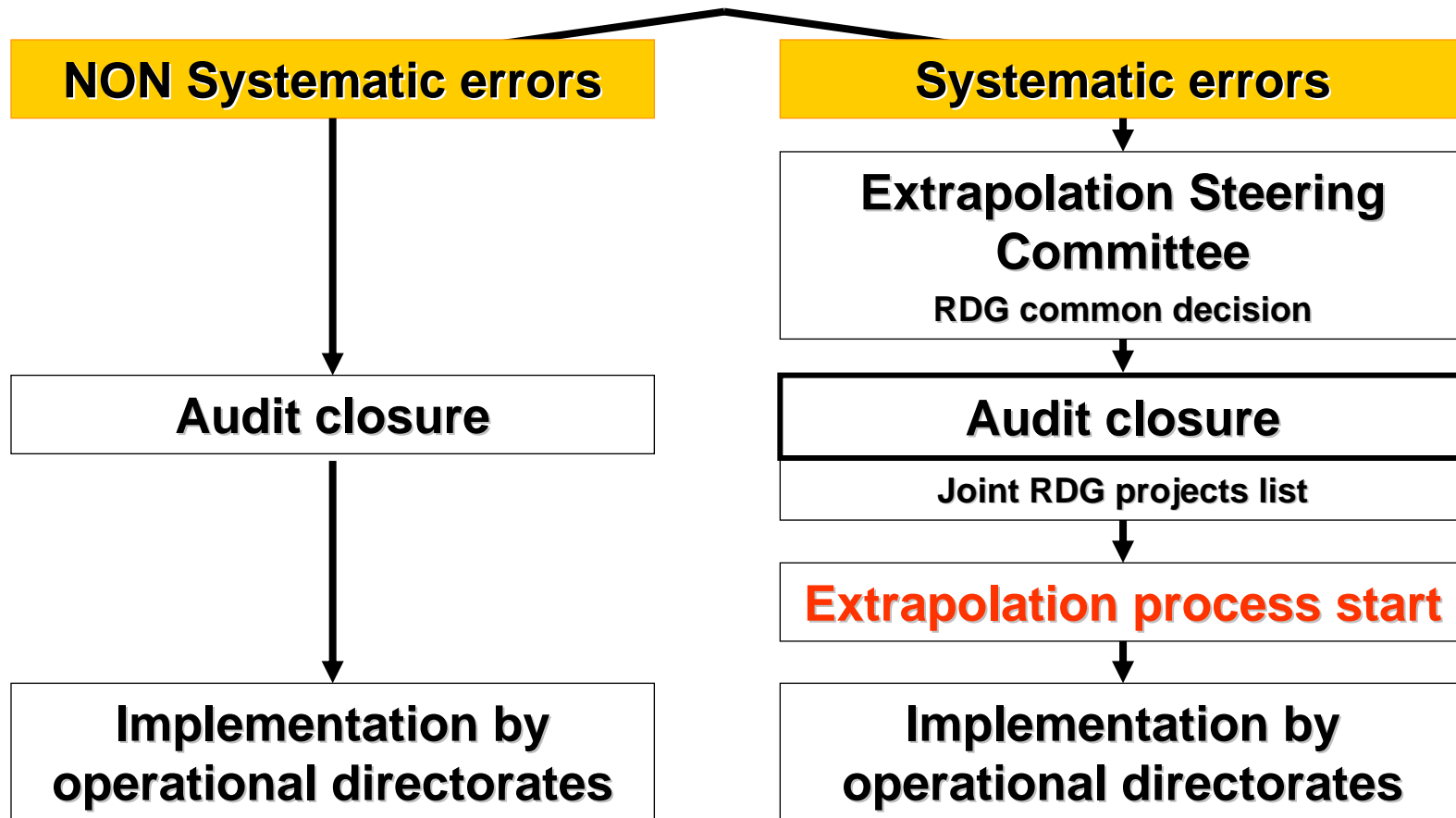
- Prior approval in the contract or by project management of the Commission
- Audit process: Verification at subcontractor in case of significant amounts (foreseen in subcontracting provisions)
- Procedures « best value for money »
- Ineligibility of VAT on subcontracts
- Subcontractors vs third parties contribution

Implementation of Audit Results



Implementation of Audit Results (1)

- Financial adjustments administered by the operational EC service managing your project
- Possibility of liquidated damages
- Consideration of serious audit findings (i.e. high adjustments) for future project & contract negotiations



- **Extrapolation** when contractor is not complying with his contractual obligation in a **systematic** way
- **Assumption:**
 - All currently open and closed contracts under the same FP are affected and might need to be adjusted
- **Impact:**
 - Contractor will be asked to review all financial statements issued under the same FP and, where necessary, to recalculate costs claimed
 - possible adjustments through flat rates correction



Extrapolation procedure

- Common decision of all Research DGs which are concerned
- Letter of Closure of the Audit indicating procedures to be followed, including a list of contracts subject to extrapolation
- 90 days delay to respond
- Follow-up audits

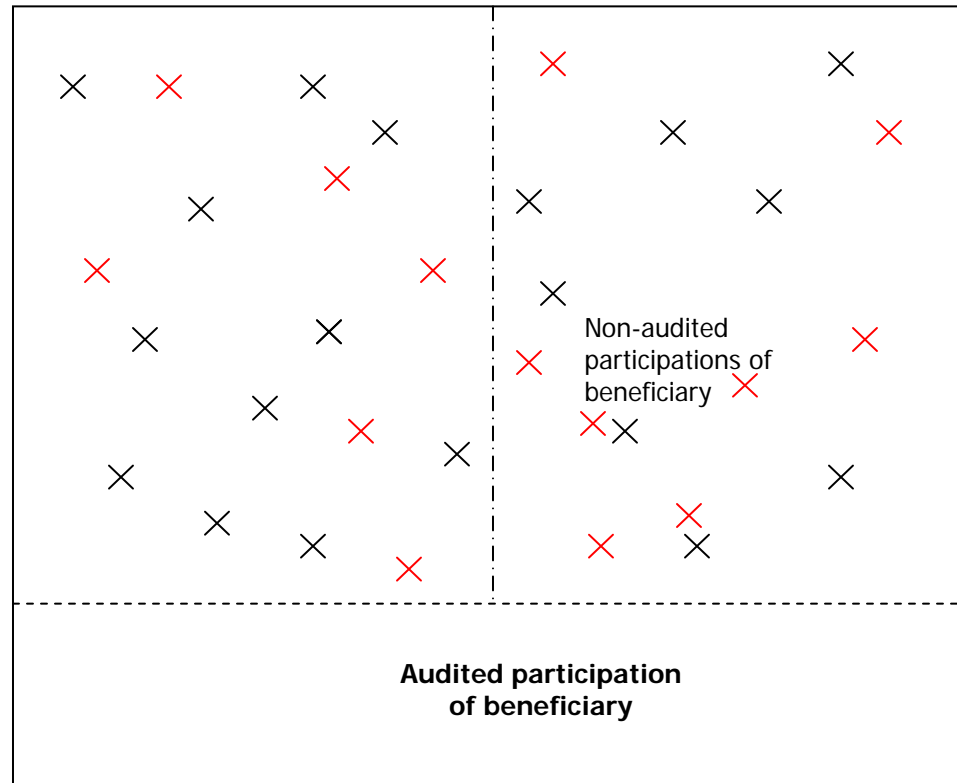
Representative error rate

Measures the amount of all errors present in the population



Corrective measures, step 1: The effect of auditing





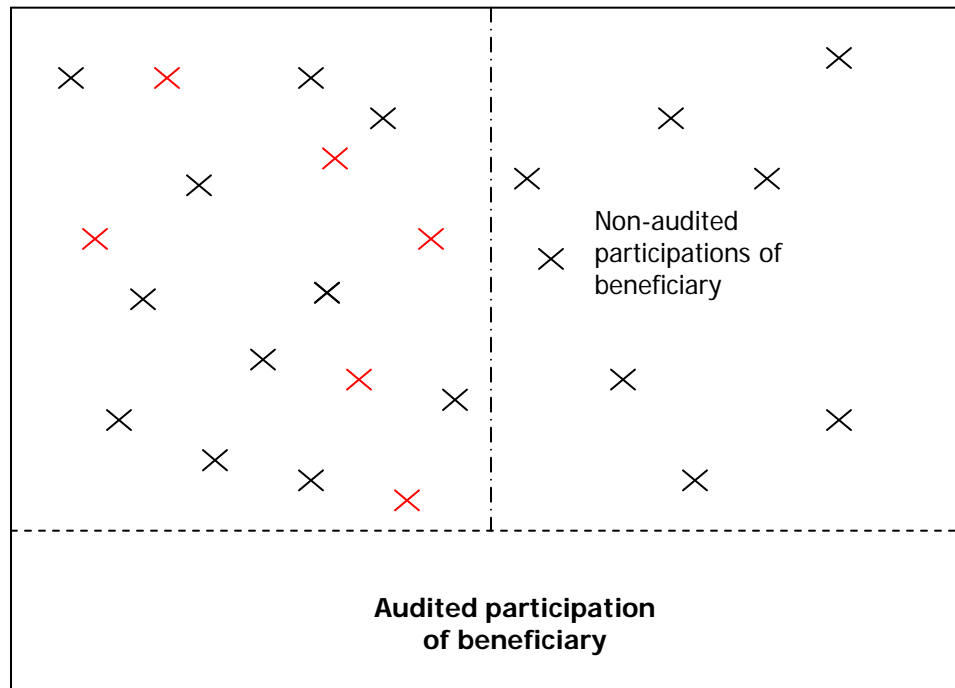
All errors removed from the audited portion of the budget

Corrective measures, step 2: The effect of extrapolation



Residual error rate

Measures the amount of error left in the population after corrections

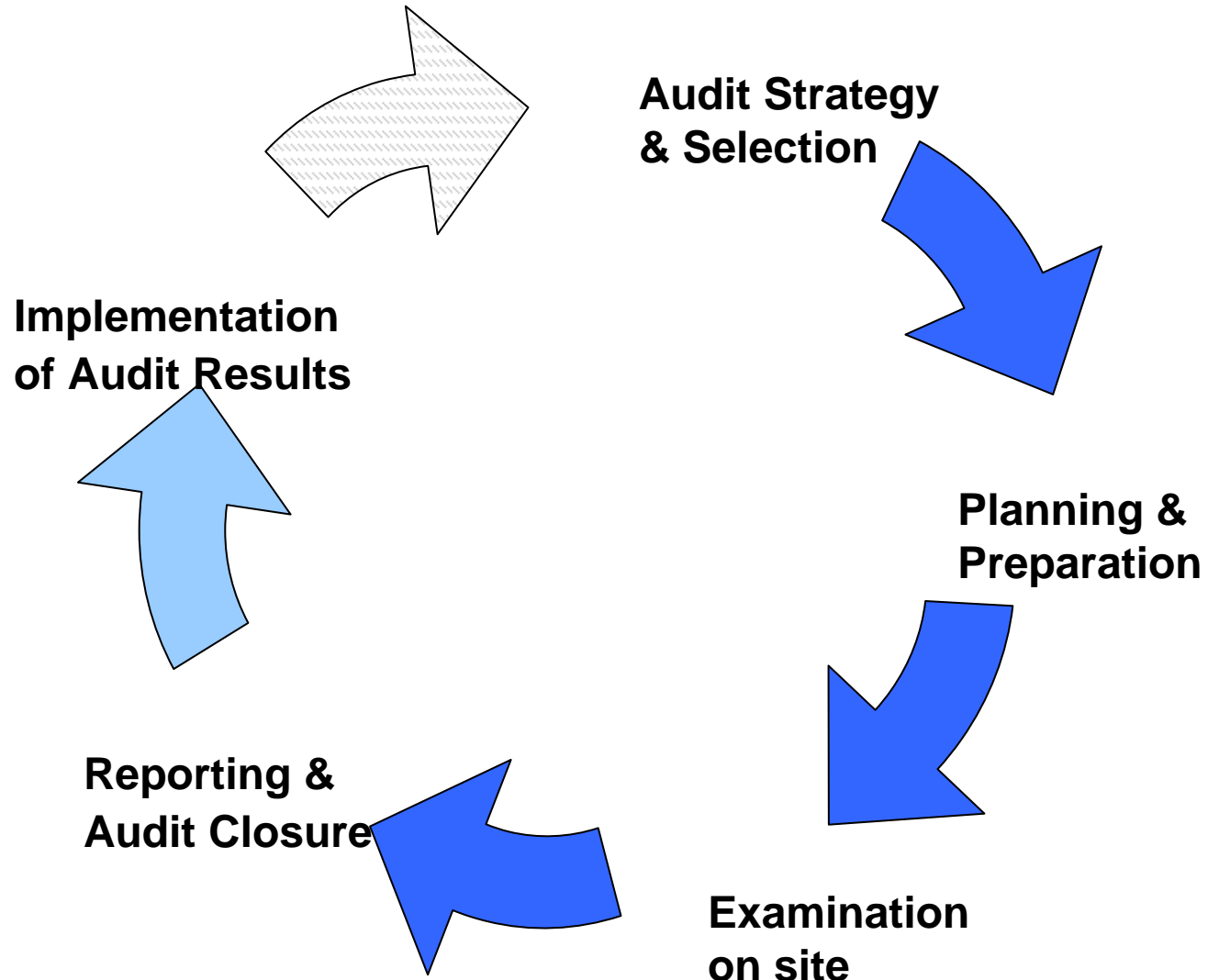


Irregularities and Fraud

- Sources of potential irregularities or fraud:
 - Operational services
 - On-the-spot audit
 - Whistleblower
- Analysis by RTD.A.4 (the OLAF team)
 - Collecting evidence
 - Transmission to OLAF
- Fraud mechanisms:
 - Intentional misuse of funds
 - Falsification of documents (time records, audit certificates, reports, etc.)
 - Double funding
 - Plagiarism



Audit Cycle



Timeline

Audit Strategy & Selection



Planning & Preparation



Examination on site



Reporting & Audit Closure



Implementation of Audit Results

***Audit on-the-spot* – Preparation**

- Selection of Contracts
- Input audit file
- Contacts with contractor
- Formal Announcement (LoA)
- Logistics



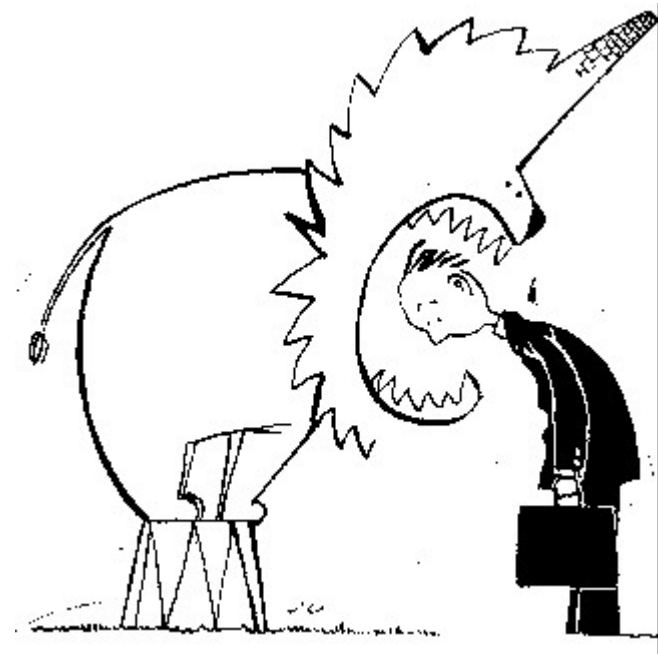
Planning & Preparation: Information request

- Letter of Announcement (LoA), detailing the audited project(s) and audit scope, includes precise list of information to be provided by the auditee
 - prior to the audit examination on site
 - **during** on-site verification
- Most relevant information in the preparation are the **project accounts** matching the costs claimed in the financial statements

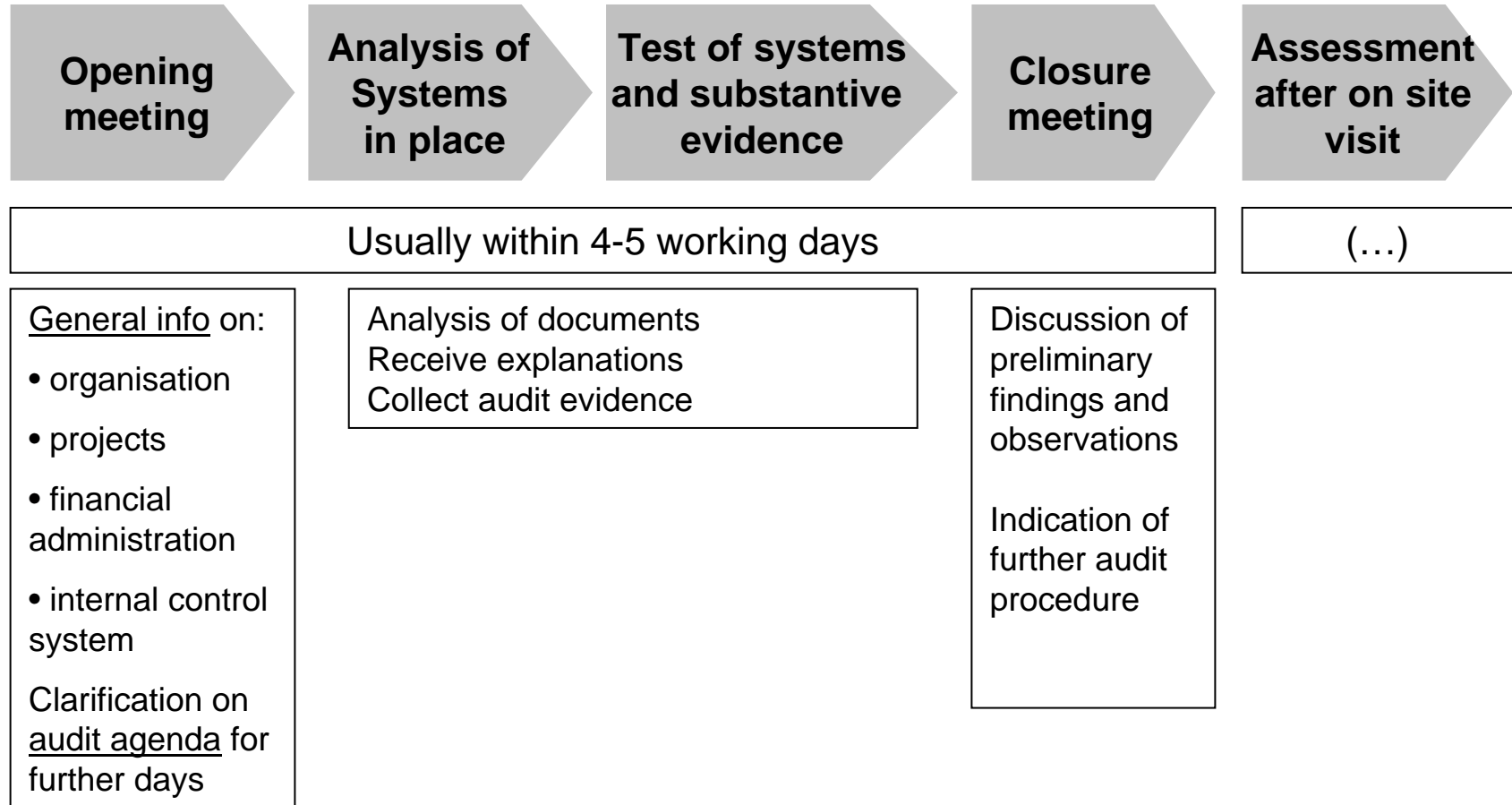
How to handle an audit(or) on site:

be CPF:

- competent
- polite
- firm

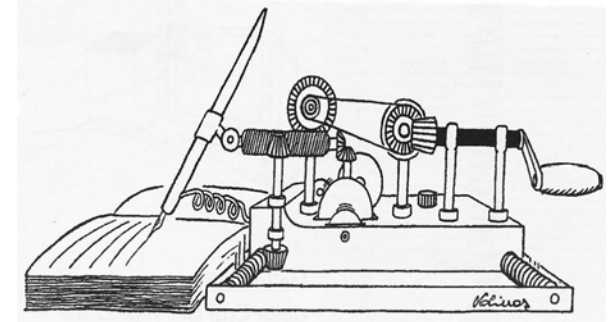


Examination on site



Follow-up & finalisation

- Draft audit report
- Quality control
 - Coherence
 - Completeness
 - Correctness
 - Compliance with the Audit Handbook
- Audit Steering Committee
- Contradictory procedure (30 days for the auditee to react)
- Final audit report
- Letter of conclusion (LoC)



END OF THE AUDIT

FURTHER INFORMATION



Guide to Financial Issues relating to FP7 Indirect Actions



http://cordis.europa.eu/fp7/how_en.html#financial

FURTHER INFORMATION

EC Financial Officer to your project



FURTHER INFORMATION



Guidance on FP7

http://ec.europa.eu/research/fp7/index_en.cfm



Practical Guide to FP7 funding opportunities

http://cordis.europa.eu/eu-funding-guide/home_en.html



And in case of doubts, contact also: **RESEARCH HELPDESK**

<http://ec.europa.eu/research/enquiries>

