Interreg NWE Risk Based Management Verifications

National Control Methodology

1.1 Legal and programme basis

In accordance with Regulation (EU) 2021/1060 Article 74 1. (a*) "the managing authority shall carry out management verifications to verify that the co-financed products and services have been delivered, that the operation complies with applicable law, the programme and the conditions for support of the operation and:*

(i) Where costs are to be reimbursed pursuant to point (a) of Article 53 (1) that the amount of expenditure claimed by the beneficiaries in relation to these costs has been paid and that beneficiaries maintain separate accounting records or use appropriate accounting codes for all transactions relating to the operation:

(ii) Where costs are to be reimbursed pursuant to points (b), (c) and (d) of Article 52 (1) that the conditions for reimbursement of the expenditure to the beneficiary have been met."

Article 74 2. adds that the *"Management verification referred to in point (a) of the first subparagraph of paragraph 1 shall be risk-based and proportionate to the risks identified ex ante and in writing."*

Looking at the specific Interreg Regulation, Regulation (EU) 2021/1059 Article 46 3. states that *"Member States may decide that management verifications referred to in point (a) of Article 74 (1) of Regulation (EU) 2021/1060 are to be done through the identification by each Member State of a body or person responsible for this verification on its territory."*

In the Interreg NWE programme the NTF (NWE Task Force) has been set up prior to the Monitoring Committee to take the decisions for the Interreg VI B programme. In its meeting on 8 December 2021 the NTF decided to give the mandate to the JS to develop such risk-based methodology to be applied for all approved projects and partners on behalf of all participating Member States. This harmonised approach was clearly favoured by all countries in the NWE programme.

1.2 Process

To reach the goal of an effective, efficient and risk-based management verification system the programme has decided to structure the process the following way:

- External analysis of the reported corrections by FLCs and JS of the VB programme on all information submitted to the programme until early November 2021.
- Development of the new NWE programme taking into consideration previous analysis made during the annual summary feedback to the EC as well as Second Level Audits.
- Programme decisions on extrapolations of the sample and on the spot checks,
- Exchanges with other programmes through working groups on Interact level
- Development of a first draft methodology
- Peer review of the methodology (including controllers and national approbation bodies) end January 2022
- Final approval by the Member States in March 2022

The system to be established needed to be easily understandable while taking into consideration the real risks that the NWE programme faces, without creating additional administrative burden for the involved controllers.

1.3 Risk assessment

The overall basis of the risk assessment is the project partner claim and the individual corrections made per claim as they were reported in the NWE VB database eMS.
Even though guidance documents on EC level suggested making a risk assessment by project, Interreg projects include different partners from different Member States that work together. These partners have different levels of risk depending on the work they implement, and their expenditure claimed. Therefore, the programme has decided to stick to the same basis as the audits of operations. It was clearly necessary to check if there were risks elements present in some partners but not in others.

There was a conscious decision to not use any “soft” risks in the analysis like “project working well” or “staff changes” when developing this methodology. These rather soft criteria tend to include a lot of preconceived judgements and are not based on factual elements. Therefore, it would be impossible to establish a harmonised system that would treat all beneficiaries from different Member States equally. Furthermore, establishing a technical solution to draw the sample on the basis of such criteria was deemed too complex.

1.3.1 Population for the risk assessment

Early November 2021 the NWE programme used the data submitted from 2017-2021 established in the VB programme to run a comprehensive risk assessment. The data included a list of all corrections made by the controllers to each individual invoice reported by the project partner as well as the reason for correction. The following elements were evaluated:

- Are private partners riskier than public ones?
- Are project partners riskier than lead partners?
- Is there a different risk level per specific objective?

- Is there a difference between different report numbers?
- Which are the riskiest cost categories?
- Which errors are the most common ones?
- Is there a difference between centralised and decentralised systems?
- Is the size of the partner budget a source of risk?

The basis of the analysis was ca. 26,000 individual corrections made by the FLCs on €402,526,232.09 declared by 2,428 partners in 112 projects.
The programme furthermore requested the external service provider for some scenario suggestions on how to incorporate the conclusions of the risk assessment into concrete system proposals.

1.3.2 Feedback received

Before diving further into the feedback, it is important to stress how interesting such an analysis has been.

Only 649 organisations out of 2,428 have been subject to a correction by the controller, meaning that 73% of the project partners declared expenditure has not led to any corrections. The total error rate was calculated at 2.1%, the average amount corrected by the FLC per single correction is €328. 96% of the corrections made by the controller are below €2,000.

All these elements clearly show that, overall, the programme can be considered a low error environment, with most of the expenditure presented by project partners not being subject to any correction. Having had constantly low error rates in second level audits in the past two programming periods supports this argument.

- ***Are private partners riskier than public ones?***
  467 private partners and 552 public ones have declared costs in the programme. Controllers rejected 2.6% for private partners and 1.7% for public partners.
  The number of errors and the amount rejected is higher for private partners than for public ones, the main errors being in "staff" and "external expertise and services" cost categories.
  After further discussions with the external provider, it was decided however that this difference was not significant enough to implement a specific sampling approach for private partners. The programme suggested to tackle these findings through a specific seminar for private project partners that would focus on the points raised during the presentation.

- ***Are project partner riskier than lead partner?***
  At first glance the answer is yes: in total there has been more expenditure rejected (€7,487,645 were rejected for the project partners vs €1,165,249 for the lead partners). There were also more individual rejections made on the project partners. This does however make sense as the programme has a 2,316/112 ratio project/lead partner.

Knowing that there are 20 times more project partner than lead partner, we can conclude that this difference is normal and does not require a specific sampling approach.

- ***<u>Is there a different risk level per specific objective?</u>***

Priorities 1 and 2 are subject to more corrections than priority 3 not only in individual corrections (8,728 and 11,377 to 6,221) but also in amounts (€3,238,468 and €3,869,616 compared to €1,492,432). Amounts rejected compared to claimed were all similar with 2.6% (P1), 2.2% (P2) and 1.8% (P3). All these amounts did not stress any significant specificity or risk according to the providers.

- ***<u>Is there a difference between different report numbers?</u>***

While the amount rejected compared to what was claimed is the highest in period 1 (usually reports 1.1 and 1.2) with 3.1%, the amounts corrected in later periods are higher. This makes sense with amounts in general being lower at the beginning, partners needing to understand fully what is requested from them. Procurement findings for example that are higher in total value are mostly only coming up during the later implementation of the project. A further analysis that was made per project report showed that there did not seem to be a direct correlation between error rates and report number. It was therefore deemed not necessary to set any requirements for this risk.

- ***<u>Which are the riskiest cost categories?</u>***

59% of all declared errors were made in the staff cost category, while all other cost categories have all similar amounts that are significantly lower (around 5% -13%). The amounts rejected by the controllers were also 47% in staff and 25% in external expertise and services. The highest corrections on average were made in the category infrastructure and works.
What was pointed out was the specificity of the travel and accommodation cost category. Taking into consideration what was claimed vs. what was rejected by the FLC, travel and accommodation leads with 4.9% before 3.4% in external expertise and services and 2.9% in equipment. The rejection rate for staff is only at 2% of what was claimed by the project partners. This highlights however that with future simplified cost options being based on staff, it will be very important to prevent errors at partner level rather than to correct them.

- ***<u>Which error types are the most common ones?</u>***

The most common type of error made by partners is miscalculation of staff costs (12,021) followed by other (7,903) and incomplete audit trail (1,872). Lack of audit trail generated the highest total amount of corrections by the FLCs whereas costs declared twice and public procurement represent the highest average amounts.

- ***<u>Is there a difference between centralised and decentralised control systems?</u>***

There seems to be no correlation between the FLC system and the risk of errors (amounts rejected by the FLC at 2.3% for the decentralised system and 2.1% for the centralised one).

- ***Is the size of the partner budget a source of risk?***

There does not seem to be any correlation between the budget size and the risks of errors according to the analysis made, therefore there is no statistical ground to say bigger projects or bigger partners are a greater risk for the programme.

1.4 Changes implemented in the NWE Programme

During the transition from VB to VIB the programme decided to make the following changes to improve what the programme felt were the biggest sources of errors:

1.4.1 Simplification of the claiming of staff costs

The programme has changed its way for claiming staff costs from the VB programme to IVB programme. Options have been reduced to one method being the fixed percentage and a possible standard scale of unit cost is under discussion with the Member States, which would cover staff costs for company owners.

1.4.2 Extended use of simplified cost options

In the previous programme a preparation cost lump sum as well as a flat rate for administration costs were used for simplified costs options. For the VIB programme it was decided to keep those previously existing SCOs and to further extend the use of simplified cost options. The programme will use the following:

- Preparation cost lump sum of €50,000 TEC
- Administration cost flat rate of 15% of all declared direct staff costs
- Travel and accommodation flat rate of 6% (BE, DE, FR, LU, NL partners) or 8% (IE partners) of all declared direct staff
- 40% of all direct staff costs for all other costs

Considering the risk shown by the analysis on the costs cut under travel and accommodation, the flat rate will lead to a significant reduction of work on FLC as well as the reduction of documentation work and errors for partners.

However, since all three flat rates that could be used in the future will be based on staff it shows the importance of further reducing errors under this budget category.

1.4.3 Specific focus on prevention and trainings

Independently from the system chosen for the risk-based sampling the programme will have to invest in training and guidance for the project partners to ensure that:

- The list of expenditure contains the same information from partner to partner. Should the list of expenditure be deemed wrongly filled in by the partner, the JS officers would only be able to revert the checks after the control was already done. Only a standardised way can guarantee a harmonised way of those controls taking place.
- All the documents needed for the verification have been uploaded
- Staff costs are clearly explained to project partners and will not lead to more errors in other categories

1.5 VI B Control system

Taking into considerations all risks analysed, the programme came to the following conclusion:

In line with the suggestions made by the external provider and taking into consideration the feasibility as well as the simplicity of the suggested approach the programme will implement the following:

- In a first step single expenditure items (key items) representing more than 10% of the amount claimed in a costs category that is based on direct costs (staff, external expertise and services, equipment and infrastructure and works) should be selected.

- In a second step, a random verification of 10 further items per cost category covering a minimum of 10% of the number of total items claimed should be made. This means that any partner having 100 items per cost category will have 10 of those items checked in addition to the key items. A partner having 230 lines of expenditure, would have 23 items checked.

- For all project partners using the 40% flat rate mentioned under 1.4.2 controllers should check 50% of the amount claimed in the staff cost category.

1.5.1 Administrative verifications

The basis of the administrative verifications is every partner progress report (activity + financial report) submitted by the project partner to the controller. All cost categories with direct costs (staff costs, external expertise and services, equipment and infrastructure and works) will be individually, randomly sampled as stated above:

- Selection of key items representing more than 10% of the amount claimed in a cost category
- Verification of 10 additional items covering a minimum of 10 % of the number of total items claimed.

- For all project partners using the 40% flat rate, controllers should check 50% of the staff cost expenditure reported.

1.5.2 Extension of the verifications and additional checks by the FLC

In case the controller finds deficiencies in the sampled population the sample will have to be extended. We suggest extending to 15 additional items in the cost category covering more than 70% of the expenditure claimed. Should no further deficiencies be presented the verification can be stopped. Should further deficiencies be detected, a 100% verification shall take place.

Independently from the question of how to extrapolate after errors were found, the controller will always be able to add additional items to the verification that are considered risky or suspicious. This addition will however have to be duly justified, as this methodology was established to create a harmonised approach over the entire NWE programme area and is supposed to reduce the burden on the beneficiaries.

1.5.3 On-the-spot verifications

The controllers will only have to do physical on the spot verifications for projects that include investments in the approved application form (project description – workplan – work packages – tab investment). The experience of the IVB and VB NWE programmes has shown that there is limited added value in doing a mandatory on the spot check at partners claiming mainly staff costs and external expertise. Contractual documents can be very well controlled remotely.
The on-the-spot check should take place in the second half of the implementation of the project to guarantee that investments have started their physical implementation and communication requirements have been taken onboard. The check can take place at the same time as the normal administrative verifications of another claim.

For all other project partners, we suggest for the controller to have a simple, non mandatory, online interview at the start of the project in order to get clarifications on the main points of attention (e.g. audit trail, double financing).

1.6 Technical aspects

The initial sample as well as the extension should be drawn by the controller through a push of a button in the database based on the information submitted in the list of expenditure by the project partner.

Jems should identify the controlled items and would ideally make a difference between the original sample, the extension of the sample and the expenditure added by the controller. All items added based on the professional judgment of the controller will have to be added manually and justified.

1.7 Updating the Methodology

The methodology established in section 1.5 shall be subject to a yearly review. The revision time should be February/March after the accounts for the previous year have been established. Errors found during second level audits will be analysed during this revision and the methodology should be adapted if the analysis shows that the reason for the error is a faulty methodology and not an individual mistake by the FLC.

Earlier updates can be made if the programme is made aware that immediate adjustments are required.

The MC will have to be informed of all changes and will have to approve the updated methodology.