Risk-based management verifications methodology

(Version 1 – October 2022)

1. Legal basis and rationale for a programme-wide risk-based methodology for management verifications

In accordance with recital 62 of Regulation (EU) 2021/1060, "*to ensure an appropriate balance between the effective and efficient implementation of the Funds and the related administrative costs and burdens, the frequency, scope and coverage of management verifications should be based on a risk assessment that takes into account factors such as the number, type, size and content of operations implemented, the beneficiaries as well as the level of the risk identified by previous management verifications and audits. Management verifications should be proportionate to the risks resulting from that risk assessment and audits should be proportionate to the level of risk to the budget of the Union*".

Moreover, according to article 74 (2) of the same regulation, *"management verification (…) shall be **risk-based** and **proportionate** to the risks identified ex ante and in writing."*

Finally, in its Reflection note, the EC states that "*each MA is responsible for developing and implementing its methodology in line with the directions in this paper and considering the relevant aspects of the OPs and the specific context in which these are implemented*."

Interreg Europe is a programme financing partners coming from 27 Members States and Norway[1]. Furthermore, the rules and requirements regarding the type of partners, activities and expenditure financed are set at programme level and are therefore the same for all countries. Moreover, in case of audit findings, they are projected across the project partnership and programme as a whole, without any particular reasoning by Partner State. It is thus possible and even necessary to assess the risks at programme level. Therefore, in order to harmonize and guarantee equal treatment, a methodology at programme level was deemed more relevant than having methodologies developed at Partner State level.

This methodology is included in the management and control system description (MCSD) of the programme (as an annex to the MCSD).

2. Process

To reach the goal of an efficient, proportionate, and risk-based management verification methodology the programme has decided to structure the process as follows:

- Exchange with other programmes through participation in the INTERACT HIT working group on risk-based management verifications methodology2.
- Risk assessment specific to Interreg Europe carried out by the JS with the support of the external audit firm contracted for 2014-2020 second level audits: analysis of the errors detected by controllers and

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[1] *Switzerland also participates in the Interreg Europe programme but the Swiss funding received by Swiss partners is not managed by the programme.*

[2] *These discussions led to a paper from Interact HIT working group: **Guidance on the risk-based management verifications for 2021-2027 and HIT methodology***

second level auditors on all expenditure reported to the programme until September 2021 by partners financed under the 2014-2020 programme.

- Presentation and discussion of risk assessment and draft methodology to centralised controllers and national approbation bodies in two online seminars in March 2022.
- Presentation and discussion at INTERACT online workshop in the presence of the European Commission's audit unit on 12 May 2022.
- This approach was developed in close cooperation and harmonization with the NWE programme, who also presented it in the Interact audit authority meeting.
- Collection of feedback from centralised controllers, approbation bodies and MC members.
- Final approval of the methodology by the Monitoring Committee on 06/10/2022.
- Information of the audit authority about the process and the methodology.

3. Risk assessment

The overall basis of the risk assessment is the project partner claims and the errors detected by controllers as they were reported in the programme online system for the period 2014-2020 up to September 2021.

3.1. Data used for the risk assessment

To identify where the risks lie, in September 2021 the Interreg Europe programme used the data from the online monitoring system submitted from 2017-2021. This detailed risk assessment was supported by an external audit firm (Annex 1.1). The data included the list of errors detected by the controllers in the costs reported by the project partners, as well as the errors detected following second level audits.

The following risk criteria were assessed as follows:

- 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? (e.g. Is the risk of errors higher in the first report?)
- Is there a difference depending on the amount reported by partners?
- Which are the riskiest cost categories?
- Which type of errors are the most common ones?

The risk analysis also assessed

- whether desk-based or on-the-spot checks detected more errors
- whether centralised or decentralised control systems detected more errors.

3.2. Results of the risk assessment

The risk assessment for the 2014-2020 programming period confirmed the **low error rate environment** (below 2%) for both first level controls (1.6%) and second level audits (0.23%).

It highlighted that the risks are much more linked to the reported expenditure rather than the type of partner or the topic of projects (see summary of the results below and further detailed in Annex 1). Therefore, a risk assessment at the selection stage based on criteria linked to the type of partners or type of project is not relevant, also considering that the type of activities and budgeted costs in Interreg Europe are similar for all projects.

The risk assessment also highlighted that the risk does not lie in any particular partner report over the duration of a project.

Finally, the assessment concluded that **the risk of errors lies with certain cost categories** (travel & accommodation, external expertise and services, staff costs), and certain type of errors (miscalculation, public procurement, audit trail). On the contrary, the risks are very low for other costs categories (e.g. equipment) and other types of errors (e.g. double-funding).

Risk assessed	Result
Are private partners riskier than public ones?	No statistical impact on error rate
Are project partners riskier than lead partners?	No statistical impact on error rate
Is there a different risk level per specific objective?	No statistical impact on error rate
Is there a difference between different report numbers?	No statistical impact on error rate
Which are the riskiest cost categories?	Staff, travel & accommodation, external expertise
Which type of errors are the most common ones?	Miscalculation, public procurement, audit trail
Is there a difference between desk-based and on-the-spot checks?	Neither type of check detects more errors than the other.
Is there a difference between centralised and decentralised systems?	Neither type of system detects more errors than the other.

4. Mitigation measures implemented in 2021-2027 period decreasing the identified risks

In order to address the main risks faced by the programme over the previous programming periods (staff, travel, external expertise, miscalculation, public procurement, audit trail), several mitigation measures have been implemented for the 2021-2027 period.

4.1 Simplification of the reporting of staff costs

To reduce the risk of miscalculation when reporting staff costs, staff costs calculations options have been reduced to one method being the “fixed percentage" method based on Art. 55 (5) of Regulation (EU) No 2021/1060.

4.2 Extended use of simplified cost options

In the previous programme a preparation cost lump sum as well as a flat rate for office costs were used as simplified costs options (SCOs). For the 2021-2027 programme it was decided to keep those two SCOs and to also offer the possibility to use a flat rate of 15% for travel costs in accordance with Art. 41 (5) of Regulation (EU) No 2021/1059.

This travel costs flat rate (which projects are strongly recommended to use) will lead to a reduction of work for partners and controllers and should also reduce the risk of errors for the cost category “travel costs”.

However, since now two flat rates (office + travel and accommodation flat rates) will be based on the cost category “staff costs”, it is even more important to further reduce errors under this cost category as any error on staff costs would also lead automatically to a correction of the office costs and travel costs flat rates (when the travel costs flat rate is used).

4.3 Specific focus on prevention and trainings

Independently from the system chosen for the risk-based sampling, the programme will provide training and guidance for projects to reduce the risk of errors when reporting costs to the controllers. In particular:

- The programme authorities and national contact points promote the use of the flat rate for travel costs. The use of real costs for reporting travel costs should be limited to exceptional justified cases (e.g. beneficiaries from outermost regions) and the reporting requirements for real costs are clearly explained in the programme manual.
- The staff costs reporting requirements are clearly explained to project partners in the programme manual and in finance seminars for approved projects to reduce the risk of errors in staff costs and related flat rates. The programme also provides templates (e.g. task assignment letter template).
- Public procurement principles and related risks identified by controllers and audits will be clearly explained in programme seminars/webinars organised for approved projects.
- All the documents needed for the verification of costs will be uploaded to the programme Portal by the partners. This will further facilitate the work of controllers and auditors and reduce the risk of errors/findings linked to audit trail.
- Training and guidance may also be provided by Partner States authorities (National contact points, centralised controllers and approbation bodies). These seminars will also allow to further address risks related to public procurement for example.

5. Interreg Europe programme methodology[3]

The external audit firm presented several possible methodologies based on their audit expertise and experience (see Annex 1).

They recommended a minimum sample size of 10 items (used in Horizon 2020) considering the low number of items reported by partners in one report (average of 29 items per report). In order to ensure consistency between reports, it is important that all costs from the list of expenditure are reported similarly from partner to partner. Especially, for every semestrial reports, all staff costs should now be reported by month rather than by semester.

Based on the results of the risk assessment and the recommendations from the external audit firm, the JS developed the following methodology:

- Considering that the risk does not lie in any particular partner report over the duration of a project, at least for the first accounting year, all project partner reports should be checked, through an administrative verification (desk check);
- For each report, the following samples of expenditure are checked by the controller:
    - 10 items checked for the budget category staff costs, selected randomly.
    - 10 items checked for all other items reported under all the other budget categories. Among these 10 items, the following items will be sampled with priority:
        - Items for which a new public procurement is indicated in section “list of contracts”.

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[3] On 6 October 2022, the Monitoring Committee approved this programme methodology as a minimum requirement. In accordance with article 74 (2) of Regulation No 2021/1060 (CPR), Partner States can only apply a stricter approach if a risk-based analysis is carried out by the PS and reveals the need for such stricter approach. This risk analysis has to be specific to Interreg Europe, and the control approach must remain proportionate to its results. If applicable, information on Partner States’ specific methodologies can be found on the programme’s website (under “in my country” section).

- Key items, i.e. expenditure representing more than 5% of the total amount reported in the list of expenditure.

If the 2 above types of items selected with priority represent less than 10 items, the remaining items to reach 10 items are selected randomly.

This methodology is designed to be proportionate to the risks (with a particular focus on staff costs and procurements) and easy to understand and implement for controllers (see also below in section 6 – the sample will be drawn automatically by the Portal).

5.1 Monitoring of joint progress reports by the Joint Secretariat

Once the report has been confirmed by the controller and included in a joint progress report by the lead partner, the monitoring of the joint progress report is done by the Joint Secretariat. The JS officers' checks focus mainly on checking the link between the activities and costs reported, the compliance with the budget flexibility rule and justification for under / overspending, and this for each progress report submitted to the programme. The JS then confirms that the progress report can be considered complete and ready for payment and the Managing Authority signs the payment order. Should an ineligible expenditure be detected through this check, the JS asks the project to correct the concerned partner report and have it recertified and may invite the controller to use their professional judgement to extend the sample of the next progress report if necessary.

5.2 Extension of the verifications by the controller

In addition to the expenditure items included in the sample generated by the Portal, based on his/her professional judgement, the controller can decide to extend the sample to additional items (e.g.in case of doubts about some items or about the partner, in case of suspicion of fraud). In such case, an explanation should be provided in the report.

If the controllers detect any error during their check of the sample, the sample should be extended. Using their professional judgement, the controllers can extend the sample to similar types of expenditure, to the whole cost category concerned or to 100% of the list of expenditure.

5.3 On-the-spot verifications

On-the-spot verifications' main added value is that they facilitate checks on the reality of the equipment or works delivered, the physical implementation of the project and compliance with publicity requirements. On-the-spot-checks may also be useful to verify the good functioning of internal processes, notably in case of doubts about the partner's understanding of requirements, issues with the reporting, or suspicion of fraud for example.

Given the nature of Interreg Europe projects which consists mainly in intangible activities, and the main categories of costs reported by partners (mainly staff and travel costs), on-the-spot verifications have mainly an added value in practice, for projects for which there is a physical implementation to check (i.e., projects with pilot action equipment/or infrastructure).

Furthermore, the above risk-analysis shows that in the context of Interreg Europe, on-the-spot checks did not detect more errors than administrative checks.

Given the above-mentioned points and the fact that Interreg Europe as a whole is a low-risk environment (see section 3.2) it is recommended that controllers carry out on-the-spot checks only for projects with a pilot action which includes reported equipment/infrastructure costs.

This on-the-spot verification should take place once the costs related to the equipment/infrastructure costs have been reported.

Based on their professional judgement, the controller can however decide to carry out an OTSC for a project not reporting pilot equipment/infrastructure costs, if they deem that it has an added value for their check (e.g. in case of suspicion of fraud, issues with the partner reporting / understanding of requirements, doubts about the proper functioning of internal processes, etc.).

5.4 Technical aspects

The sample will be drawn by the Portal based on the items included in the list of expenditure by the project partner.

All supporting documents will be uploaded by the partners to the Portal.

The controller will have the possibility to extend the sample in the Portal if it is justified (also see 5.1). The scope and reason for extension should be documented in the control report.

6. Updating the Methodology

The risks shall be periodically reassessed by the programme based on controller's corrections and audit results. For the first time, this risk re-assessment will take place after the first accounting year cycle.

The methodology will be updated when needed, and based on the revised risk assessment, to reinforce the controls or further reduce them depending on the level of risks.

In case major problems are detected (notably through second level audits, system audits or other checks/audits) or in case of external factors affecting the risks, the methodology will be revised immediately without waiting for the periodic re-assessment of the risks.

The Monitoring Committee will be informed about the re-assessment of the risks and updates of the methodology. The updates of the methodology are presented and approved by the Monitoring Committee. The centralised control bodies and approbation bodies, as well as the Audit Authority will also be informed about these updates.