

MEMO

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Subject Guidance for Member States on Management Verifications
(Programming Period 2014 – 2020)

Background

Management verifications are part of the internal control system of any well managed organization. They are the normal day to day controls made by management within an organization to ensure that the processes for which it is responsible are being properly carried out.

The guidance covers the regulatory requirements, general principles and purpose of verifications, the bodies responsible for carrying them out, the timing, scope and intensity of the verifications, the organisation of the on-the-spot verifications, the requirement to document the work and outsourcing. Given management verifications are a responsibility of the MA, their importance cannot be underestimated and MAs should address such responsibility by putting in place good elements of control systems as their proper implementation contribute to the prevention and detection of fraud.

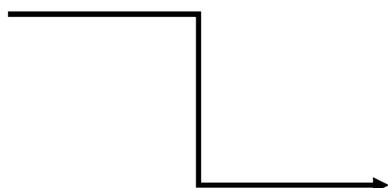
Legal Basis

Article 125 (4)(a) CPR requires that the MA is to verify that the co-financed products and services have been delivered and that expenditure declared by the beneficiaries has been paid and that it complies with applicable law, the operational programme and the conditions for support of the operation. Pursuant to this, the verifications shall include administrative verifications in respect of each application for reimbursement by beneficiaries and on-the-spot verifications of operations.

Main Issues

Verifications made by management within an organisation should ensure that the processes for which it is responsible are being properly carried out and are in compliance with the relevant rules and regulations. Each MA is fully responsible to plan, administer and assess its internal capacities to identify the number and value of operations which can be appropriately managed.

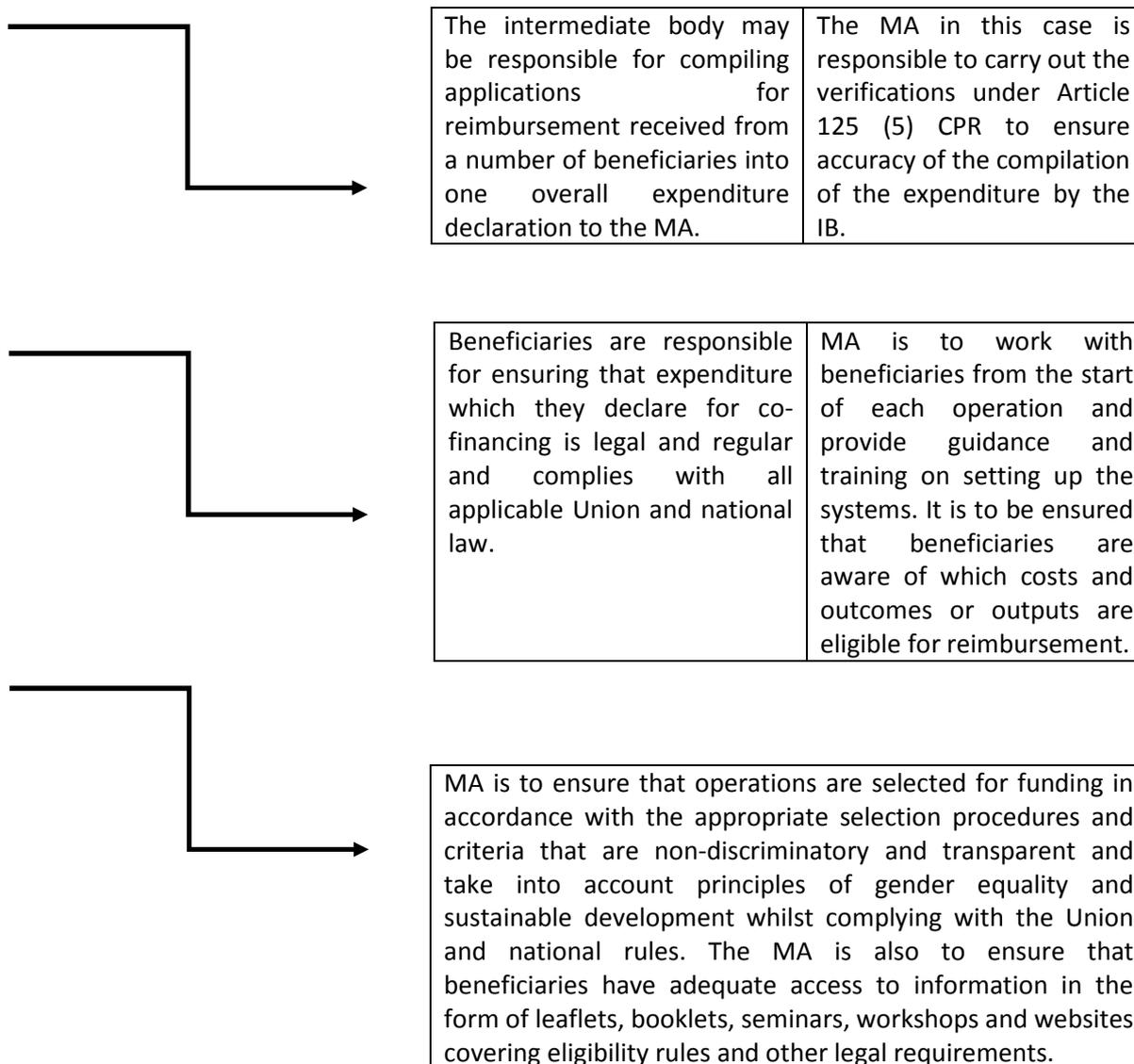
Under Article 125 CPR, the MA is responsible for managing and implementing operational programmes in accordance with the principle of sound financial management in line with the illustration below:



1. Draw up a management declaration on accounts covering expenditure incurred and presented to the Commission for reimbursement;
2. Draw up the annual summary of the final audit reports and of controls carried out;
3. Verify that the co-financed products and services are delivered and that the expenditure declared by the beneficiaries for operations has been paid and that it complies with applicable law, the operational programme and conditions for support of the operation;
4. Ensure an adequate audit trail;
5. Establish a system to record and store in computerized form data on operation, including individual participants data, where applicable;
6. Put in place effective and proportionate anti-fraud measures taking into account the risks identified;
7. Ensure that beneficiaries involved in the implementation of operations maintain either a separate accounting system or an adequate accounting code for all transactions;

Though the MA has the overall responsibility for the above mentioned tasks, some or all tasks may be delegated to IBs given that the MA ensures they are properly carried out. To have this assurance the MA may prepare guidance notes, checklists, perform quality checks and receive audit reports incorporating reviews of the verifications. The MA shall also carry out checks at IB level including a sample of beneficiary's applications for reimbursement so as to assess how the verifications have been performed.

The illustrations below focus on the coordination of tasks between the IB, MA and beneficiary:



While designing management verifications, the MA is to consider fraud risks and hence, management and staff should have sufficient knowledge to identify red flags while verifications shall always be carried out with professional scepticism. The MA should provide staff with training and guidance on the skills required. Where suspected fraud is detected, the MA should inform the relevant national authority (which would then notify the Commission) or refer the case directly to the judicial authorities. It is recommended by the Commission that the MA adopts a proactive, structured and targeted approach to manage the risk of fraud.

Methodology and scope of Article 125 (5) management verifications

Verifications comprise two key elements namely **administrative verifications (desk-based verifications)** and **on-the-spot verifications** of operations. All applications for reimbursement shall be subject to administrative verifications based on an examination of the claim and relevant

supporting documentation such as invoices, delivery notes, bank statements, progress reports and timesheets. When operations are implemented through simplified cost options, the amount of supporting documents might be reduced. If during on-the-spot verifications, a material amount of irregularities is detected in expenditure which has already been included in a request for payment submitted to the Commission, then the responsible authority should carry out a quantitative and qualitative assessment of the irregularities detected in order to assess the risk that irregularities exist also in the operations not sampled. Corrective measures should also be taken to strengthen verifications before the request for payment to the Commission.

The methodology used by the MA for carrying out verifications should be set out in the manual of procedures identifying which points are checked in the administrative verifications and in the on-the-spot verifications.

The timing of management verifications depends on the controls being carried out:

- Verifications during project selection - MA to ensure that applicants have the capacity to fulfil a number of conditions before the approval decision is taken
- Administrative verifications during project implementation – management verifications to be carried out **before** the related expenditure is declared to the next level above;
- On the spot verifications during project implementation – to be planned in advance and undertaken when the operation is well under way, both in terms of physical and financial progress; the nature, specific characteristics of an operation, risk level and the extent of administrative verifications will often influence the timing of on-the-spot verifications;
- On the spot verifications after operation implementation – required during the operational phase to ensure that conditions continue to be observed in cases where ongoing conditions are imposed such as retention of ownership or number of new employees;

MA is recommended to set internal deadlines for the completion of all management verifications in order to enable both CA to certify the accounts, MA to issue the management declaration and AA to draw up the audit opinion. **No expenditure shall be included in the accounts submitted to the Commission if the planned management verifications are not fully completed and the expenditure is not confirmed as legal and regular.**

Intensity of management verifications

<p><i>Administrative verifications</i> must be carried out in respect of all intermediate and final applications for reimbursement by beneficiaries.</p> <p>Such verifications should comprise a review of the supporting documents such as invoices, proofs of payment, timesheets, proofs of delivery to each application for reimbursement. Selection of the expenditure items is to be verified within each application for reimbursement and this is to be done on a sample of transactions taking into account risk factors (value of items, type of beneficiary, past experience) and complemented by a random sample to ensure that all items have probability to be selected.</p>	<p>On the spot verifications are carried out in order to check the reality of the operation, delivery of the product or service in full compliance with the terms and conditions of the agreement, physical progress and respect for Union rules on publicity. Such verifications can also be used to check that the beneficiary is providing accurate information regarding the physical and financial implementation of the operation.</p>
<p>The sampling methodology used shall be established ex-ante by the MA and it is recommended to establish parameters that can be used to project the errors in the unchecked population.</p>	<p>On the spot verifications may be carried out on a sample basis. Where sampling is used, the MA shall keep records describing and justifying the sampling method and a record of operations selected for verification.</p> <p>No operation shall be excluded from the possibility of being subject to an on-the-spot verification. The intensity, frequency and coverage of on-the-spot verifications is dependent on the complexity of the operation, the amount of public support to an operation, the level of risk identified by management verifications and audits of the AA. The sample could focus on high value operations, operations where problems have been identified previously or where particular transactions have been identified during administrative verifications that appear unusual and require further examination.</p>

Documenting management verifications

All management verifications shall be documented in the project's file and results are to be available to all concerned staff and bodies. The records should state the work performed, the date when the work was carried out, details of the application for reimbursement reviewed, amount of expenditure tested, the results of the verifications, a full description of irregularities detected and corrective measures taken. Checklists should be in place to record each of the actions performed together with the results. Photographs of billboards, copies of promotional brochures, training course materials and diplomas may be used to provide evidence of the verification of compliance with publicity requirements.

Outsourcing management verifications

In situations where due to the high volume or technical complexity of the operations to be verified, the MA finds that it does not have sufficient staff or expertise to carry out the verifications, outsourcing of some or all the elements of the verifications to external firms may be appropriate. Before a decision to outsource management verifications, it is essential that the scope of the work to be carried out and a wording of the opinion are set out clearly in the terms of reference. The MA is recommended to implement procedures ensuring timely processing of reports by external firms and additional staff by may be involved to assess the quality of the outsourced work.

Auditors' certificates

The terms of agreements for individual form of support may include a requirement for beneficiaries to provide an auditor's certificate with applications for reimbursement they submit. Such certificates usually cover basic requirements such as confirmation that the expenditure has been paid within the eligible period, that it relates to items approved under the agreement, that the terms of the agreement for individual forms of support have been compiled with and that adequate supporting documentation, including accounting records, exist. To rely on such certificates, the MA is to provide guidance for use by the auditors on the scope of the work to be done and the report / certificate to be presented. In order to ensure quality and reliability of auditors' certificates, the MA is to review a number of auditors' certificates. Reference to IFAC 4400 which establishes standards and provides guidance on the auditor's professional responsibilities can also be made.

Segregation of Duties

Adequate segregation of duties shall be ensured when the MA (or the IB) is responsible for selection and approval of operations, management verifications and payments. This may be achieved by for example using a separate department within the same organisation, independent of the department where the beneficiary is located, to carry out the management verifications. It is to be noted that the objectives of management verifications are different from those of audits carried out under the responsibility of the AA (which are carried ex post) and have the aim of ensuring effective internal controls. Although management verifications and audits under the responsibility of the AA shall be separated, exchange of information between the MA, CA and AA services is desirable.

Specific areas concerning management verifications

Public Procurement Verifications in relation to public procurement should aim to ensure that Union public procurement rules and related national rules are complied with and that the principles of equal treatment, non-discrimination, transparency, free movement and competition have been respected throughout the entire process. At award of funding stage, it should be ensured that beneficiaries are aware of their obligations in this area and that staff received relevant training. The intensity of management verifications should be determined by the MA according to the value and type of contracts. Where the MA considers there is a risk, it should verify ex-ante such elements as a preventive measure and also check that cost-estimates are up to date.

Particular attention should be paid to checking the appropriateness of the procurement method being used; the interdependence between the different contract phases and financing plans and the availability of national co-financing. For high value contracts or where beneficiaries are presumed to be inexperienced in the area of public procurement, the MA is recommended to ensure, prior to advertising the contract, that the quality of the tender documents have been verified either by their own experts or by an external expert. Particular attention should be given to verifying that the specifications are well-defined as regards technical, economic and financial capabilities and that appropriate selection and award criteria are to be used. In order to properly verify that tender selection and award procedures have been carried out in accordance with EU and national procurement rules, the MA should obtain and review the tender evaluation reports prepared by evaluation committees.

Particular areas of the tender evaluation and award procedures which Commission audits have been identified as being problematic include: no separation between the selection phase and award phase and confusion of selection criteria and award criteria; selection criteria incorrectly used during the award phase; criteria not being published in the tender notice or tender specifications; use of discriminatory technical specifications or national permits requested at tendering stage; inadequate documentation of decisions taken by the evaluation committee; too dissuasive selection criteria not linked to the subject matter of the contract;

During contract implementation stage most problematic areas include supplementary or complementary works awarded directly without being re-tendered and substantial amendment of essential conditions of the contract at implementation stage;

Examples of the most common issues identified in the past by the Commission in the area of public procurement include: additional works (direct award); unlawful award criteria; splitting of a project to avoid tender procedures on EU level; unlawful selection criteria; too restrictive time limits for tendering; direct award of contract; non-compliance with advertising procedures; weaknesses in tender clarification; failure to provide an adequate audit trail; unjustified use of negotiated and accelerated procedures; deficiencies in the case of contract value calculation; deficiencies in respecting the established delivery deadline; works started before the tender procedure was completed;

Environment management verifications should verify that the beneficiary has complied with the applicable directives by checking whether the relevant consents have been obtained from the competent national authorities in accordance with the procedures. The competent national authorities are responsible for ensuring that EU environmental legislation is correctly applied and for taking appropriate steps if this is not the case. The MA should ensure that it has access to appropriate in-house or external expertise to assist it in identifying all relevant environmental issues related to the particular type of operation being approved together with verifying continuing compliance of operations with environmental rules.

State aid MS needs to comply with the rules on state aid when any aid is granted by a MS or through State resources which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods in so far as it affects trade between MS. In practical terms, the management verifications on state aid should complement the checks carried out during the selection of operation process – verifying whether the operation includes state aid, identifying the legal basis and using aide memoirs to ensure that all relevant provisions are tested. Further complementary tests should be carried out in respect of de minimis rules, block exemptions and notified aid.

Financial Instruments management verifications in relation to financial instruments should aim to ensure the compliance with applicable rules and regulations, the sound financial management of ESIF, the safeguarding of assets and the reliable financial monitoring and reporting by the bodies that implement the funds or the financial instrument. Examples of the most common issues identified in the past by the Commission in this area include management costs not based on evidence, failure to provide an adequate audit trail, inadequate management verifications, missing compulsory elements in the funding agreement and audits of operation not performed because of limitation to scope.

Revenue-generating operations where cash flows can be expected after operation completion, the MA should examine whether the cash inflows will be directly paid by the users or whether they can be classified as ‘other cash inflows’ such as private or public contributions or other financial gains.

Durability of operations pursuant to Art 71 CPR, the MA must ensure that an operation retains the contribution from ESIF only if that operation does not, within five years from the final payment to the beneficiary or the period applicable to state aid, undergo a substantial modification.

Equality and non-discrimination management verifications should check that operations respect and promote gender equality whilst also preventing any discrimination based on sex, racial or ethnic origin, religion or belief, disability, age or sexual orientation during the various stages of implementation.

Youth Employment Initiative the specific requirements to verify consist in checking whether payments are eligible for the YEI (age group, status, place of residence) and that the beneficiary ensured that those taking part in an operation are specifically informed of the YEI support provided. *(the Youth Employment Initiative was launched to provide extra support to young*

people aged below 25 and living in regions where youth unemployment was higher than 25% in 2012)

Simplified Cost Options For unit costs and lump sums the management verifications will check whether the conditions for reimbursement set in the agreement between the beneficiary and MA have been met and that the agreed methodology has been correctly applied. In case of flat rate financing, the verification should also check whether costs have been correctly allocated to a given category, there is no double declaration of the same cost item and the flat rate has been correctly applied.

Indicators the verifications should ensure that the data related to indicators and target values at investment priority, priority or programme level is timely, complete and reliable. The verifications should check key requirements concerning data collection, storage and quality. The lack of data quality and the reliability of the monitoring system is subject to suspension of payments. Hence, the MA is to ensure data quality through checking their completeness and consistency. On the spot verifications should verify the correctness of data communicated by beneficiaries in relation to the indicators.

Examples of Best Practices

Use of ARACHNE Risk Scoring Tool – enriched with data from publicly available sources in order to identify the most risky projects, beneficiaries, contracts and contractors. This programme enables and aids the MA in identifying most risky projects, contracts, contractors and beneficiaries and helps to gear its administrative capacity to the most risky cases while planning on-the-spot visits.

In order to ensure a consistent methodology when carrying out management verifications, guidance notes may be prepared at MA level but where necessary tailored at IB level to meet specific requirements.

The MA could establish appropriate criteria to assess the operational, technical and administrative capacity of applicants. Criteria may vary depending on the type of operations but may include an assessment of the financial standing of the applicant, the qualifications and experience of its staff and its administrative and operational structure.

All documentation is to be submitted with the beneficiary's application for reimbursement so as to reduce the volume of documentation to be submitted by beneficiaries. It is also recommended to verify compliance with national and union rules including public procurement procedures during administrative verifications. As best practice, it is recommended to verify all contracts above the EU thresholds and a sample of contracts below the EU threshold which are sampled using a risk based approach.

For on-the-spot verification of measures that include construction works best practice is to carry out additional checks on the quantity and quality of the material used. Normally both the contractor and the engineer are responsible for ensuring that the investment complies with the conditions laid out in the technical specifications. Yet, additional checks by the MA or an independent expert contracted by the MA to help prevent damages during and after construction.

A system for recording and storing in computerized form data on each operation for and from verifications carried out should be maintained for each programme. Records are to be kept in computerised monitoring information systems in MS.

For contracts exceeding the thresholds in the EU public procurement directives, the MA may send an observer to tender evaluation and a report setting out the observer's conclusions regarding the evaluation is then prepared. Some MS have also established an independent public procurement verification unit empowered to carry out checks of all stages of tender procedures, up to contract signature stage.

It is essential to ensure a sound verification on state aid, based on specific checklists for each measure that will be used as an aide memoire and an audit trail of the checks carried out.

Regarding revenue generating activities, the MA should give indications about the methodology to be applied by the beneficiaries for the forecast of future net revenue.

As part of its verifications and after the completion of operations, the MA should check compliance with durability of projects, including on-the-spot verifications on a sample basis.

