

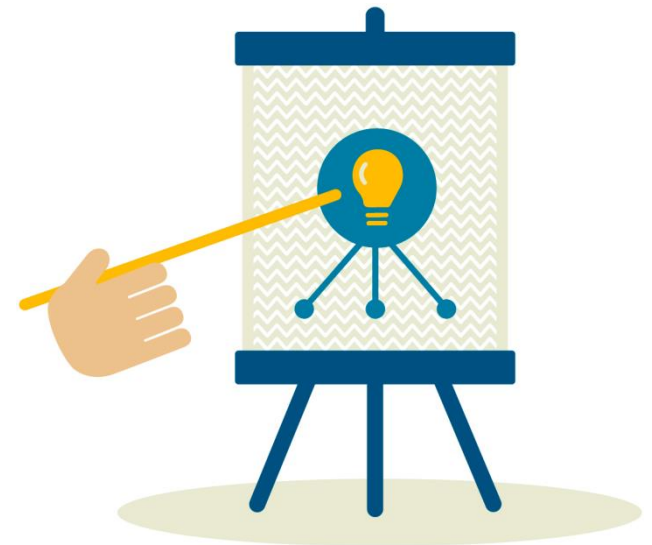
# Risk-based verifications and sampling

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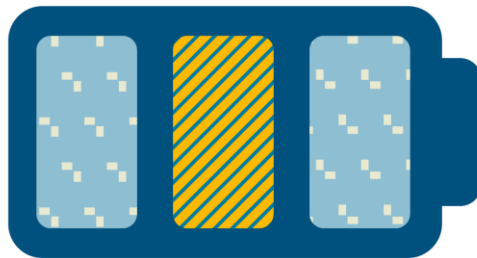
# Content

1. Terminology
2. Regulatory framework and guidance 2014-2020
3. HIT risk assessment and sampling



# Terminology

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## Sampling

- Sampling involves the application of control procedures to less than 100 % of items within a class of transactions or budget lines, such that all sampling units have a chance of selection (Definition based on ISA 530 No. 5)
- Routinely applied by certified auditors, Second Level Control, EC Auditors, etc.
- Was used in some ETC FLC systems (on-the-spot, administrative).
- Usually done if it is impossible, unnecessary or not practical to control all expenditure items.

## Risk

- Potential error source

## Risk assessment

- Aimed at obtaining a better understanding of potential error sources related to the project, the beneficiary, the type of expenditure, etc.
- Sampling methodologies often include risk assessments as a basis for planning the sampling methodology.

# Risk-based approach to control (1)

**Pick the riskiest!**

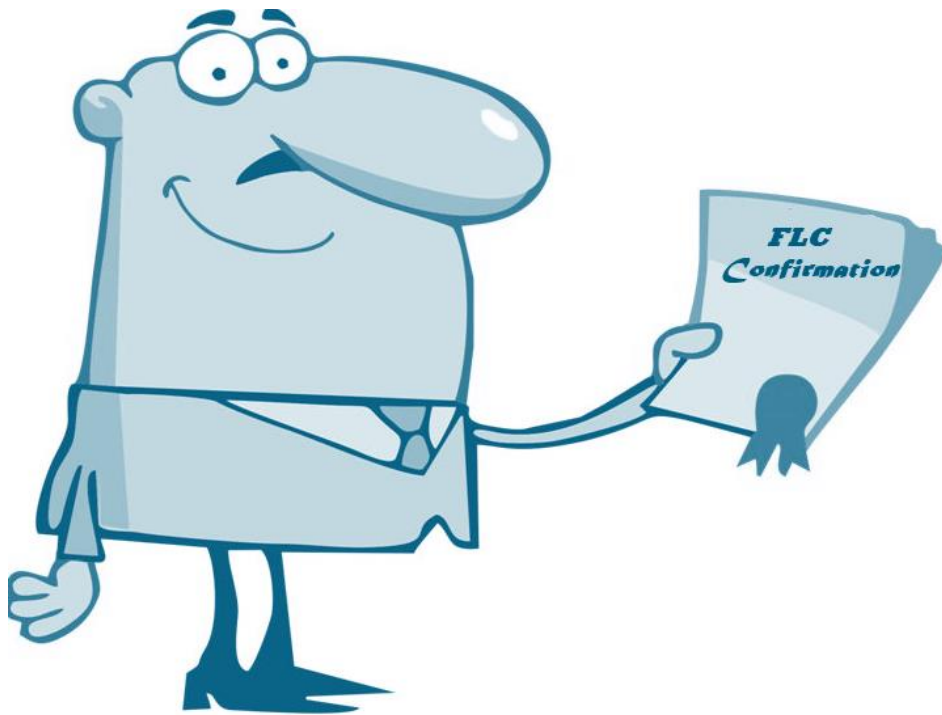


- **Decrease control work** for low-risk control areas, where certainty is high that more controls will not result in the discovery of material errors, such as:
  - ✓ Items of low value (e.g. bus tickets, pens, paper, etc.);
  - ✓ Standard internal processes for which it is already known that they function well (e.g. payment processes, deduction of VAT, staff cost budget line, etc.)

# Risk-based approach to control (2)

- **Increase control work** for control areas where the risk of material errors is high, even if difficult to control.
- **More thorough controls:** Spend more time, pay more attention to details, etc.
  - ✓ Infringement of public procurement rules,
  - ✓ Double funding,
  - ✓ Lack of existence and reality,
  - ✓ Fraudulent external expertise arrangements,
  - ✓ etc.

# Risk-based approach is not new to controllers



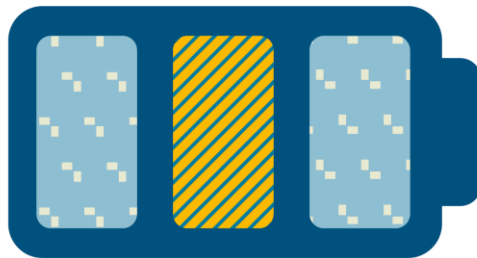
## Controllers ...

- Are very aware of potential risks (especially experienced controllers)
- Have good feelings about the quality of the reports they control
- Many adapt their work programmes over time to the quality of reports (although not always explicitly so)



# Regulatory framework and guidance 2014-2020

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# Intensity

## On the spot verifications

Art 125.5, Reg. [1303/2013](#): on-the-spot verifications may be carried out on a sample basis

## Administrative verifications

Guidance on management verifications: where justified, verification of a sample of expenditure items is allowed.

# Methodology – Recommendations (1)

## On-the-spot verifications (p. 13 of guidelines)

- MA keeps records of the operations selected; description of the sampling method and reviews the sampling method annually
- Risk-based selection is complemented by a random sample
- Risks e.g.: complexity of operation, amount of public support, risks discovered during management verifications, etc.
- Sample, e.g.: high value operations, problems/irregularities or unusual transactions have been previously identified

# Methodology – Recommendations (2)

## Administrative verifications (p. 12)

- Methodology established ex-ante (by the MA)
- Sampling based on risk factors (e.g. value of items, type of beneficiary, past experience)
- Risk-based selection is complemented by a random sample

# Debate

## Pros and Cons of sampling

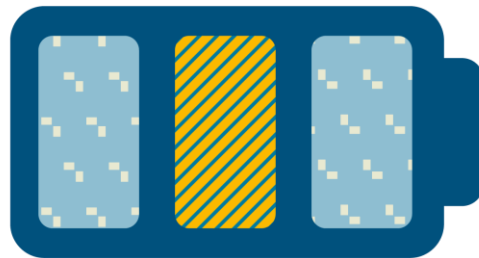
Why should we sample? Why not?

What are the risks?

What are the benefits?

# HIT risk assessment and sampling methodology

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# HIT Sampling methodology for administrative verifications

- ✓ In line with EC Guidance on Management Verifications
- ✓ Sampling based on risk assessments and done per budget line
- ✓ Sampling items, e.g.:
  - Staff costs: monthly payments to employees
  - Office and administration: monthly electricity costs
  - Travel and accommodation: business trip reports

# Risk (inherent + control risk)



Inherent  
Risk

Control  
Risk

- **Inherent Risk** - Typical for this type of beneficiary, project or report
- **Control Risk** - Related to the quality of internal accounting and controls of the beneficiary.

*Assessment requires experience with the quality of the expenditure reported by the beneficiary.*

**-> No sampling of the first report!**



# Inherent risk

- Inexperienced beneficiary
- Beneficiary with poor track record, known issues
- Beneficiary with other EU or non-EU grants
- Large partnership
- Large partner budget
- Private partner
- Person responsible for preparation of the financial report has changed recently
- Large public procurements
- Few tangible outputs (based on networking, meetings, etc.)
- Others (e.g. programme- or country-specific risks)

# Control Risk

## Assess the quality of the partner report:

1. Quality of expenditure when originally reported (e.g. good, medium, bad)
2. Number of clarification rounds with beneficiary
3. Quality of expenditure after clarifications

**Recommended to do this per budget line!**

Draw conclusions for the next report.

# HIT Sampling methodology for administrative verifications

Sampling not recommended for:

1. The first partner report
2. Public procurements
3. Budget lines where quality of previous report was not sufficient
4. Simplified cost options

# Sampling (Example)

## A combination of:

- **Simple random sampling:** The suggested minimum sample size per budget line is **at least 10%** of the total value of declared expenditure for the budget line **AND at least 2 items**.
- **Key-item sampling:** In addition included are:
  - All items that exceed 25% of the total value of the budget line.
  - Any risky item (e.g. based on type of beneficiary) and unusual or suspicious items.

**It can be necessary to expand this sample until controllers have a good feeling about the reliability of information!**

# Exercise: Developing own sampling method

- Define some risk factors for inherent risk (typical for specific project partners, project types, etc.)
- Define some aspects of 'quality of partner reports' for control risk (good, medium, bad reports - examples of criteria)
- Develop sampling methodology consisting e.g. random sample minimum size (e.g. 10%) plus key item sample (e.g. all risky and suspicious items)
- Determine what should never be sampled

Note: Methodology needs to be reviewed (e.g. every year) and adapted if necessary!

# Extending controls after the initial sample

- In case that material errors are found in the sample tested -> extend the testing **to determine whether the errors have a common feature** (i.e. type of transaction, location, product, period of time)
- Either:
  - No common feature(s): extend the verifications to 100% of the application for reimbursement, or
  - Common feature(s): project the error in the sample to the unchecked population.
- The total error is calculated by adding the errors from the risk based sample to the projected error from the random sample.

# Cooperation works

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All materials will be available on:

**[www.interact-eu.net](http://www.interact-eu.net)**