Develop a common sampling methodology

National Control (FLC) Workshop

14-15 May 2019 I Bergen, Norway
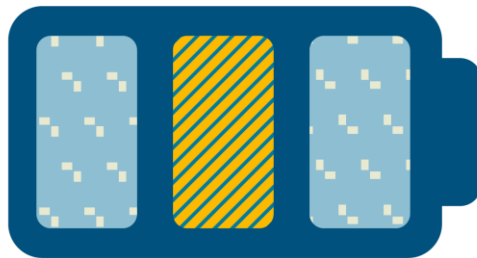
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Risk-based approach to control

Risk-based approach to control

Sampling

- Sampling involves the <u>application of control procedures to less than 100 % of items within a class of transactions or budget lines</u>, 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 Interreg FLC systems (on-the-spot, administrative).

- Usually done if it is impossible, unnecessary or not practical to control all expenditure items.

Risk-based approach to control

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

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

- **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
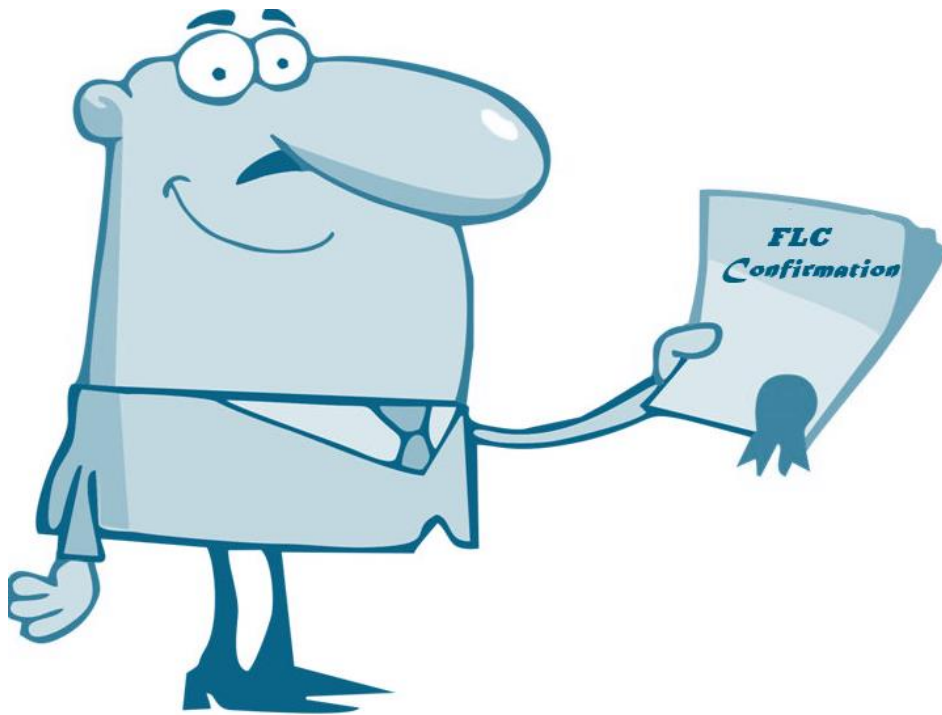
Controllers …

- 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
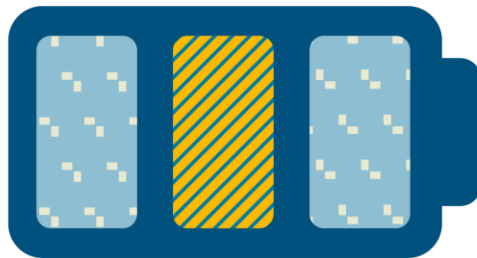
Intensity

On the spot verifications

Art 125.5, Reg. 1303/2013: on-the-spot verifications may be carried out on a sample basis
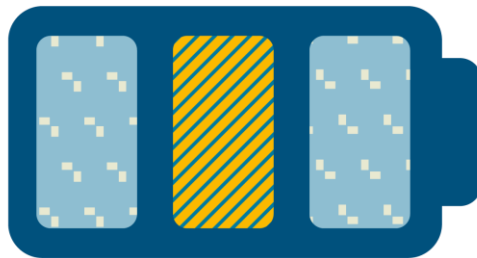
Administrative verifications

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

Methodology – Recommendations

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

HIT Sampling Methodology for Administrative Verifications

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

HIT Sampling methodology for administrative verifications

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!

HIT Sampling methodology for administrative verifications

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)

HIT Sampling methodology for administrative verifications

Control Risk

Assess the quality of the partner report (e.g. good, medium, bad)**:**

1. Quality of expenditure when originally reported

2. Number of clarification rounds with beneficiary

3. Quality of expenditure after clarifications

Recommended to do this per budget line!

Draw conclusions for the <u>next report</u>.

HIT Sampling methodology for administrative verifications

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!

HIT Sampling methodology for administrative verifications

Sampling <u>not</u> recommended for:

1. The first partner report

2. Public procurements

3. Budget lines where quality of previous report was not sufficient
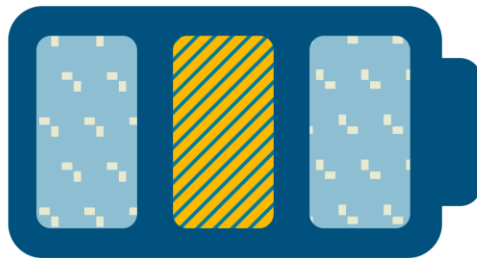
4. Simplified cost options

Developing own sampling methodology

- 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)

- Determine what should never be sampled

Develop sampling methodology consisting e.g. random sample minimum size (e.g. 10%) plus key item sample (e.g. all risky and suspicious items)

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

Group Work

Group Work: Develop own sampling methodology

3 Groups:

1. Define risk factors for **inherent risk** (typical for specific project partners, project types, etc.) E.g., private partners, many partners, large procurements, etc.

2. How would you define '**quality of partner reports**' (good, medium, bad reports)? E.g., number of clarification rounds, error rate per budget line, etc.

3. Determine **what should never be sampled** (if anything). E.g., first report, large procurements, etc.

Cooperation works

All materials will be available on:

www.interact-eu.net

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.