



AUDIT CERTIFICATE GUIDANCE NOTES
ETEN PROGRAMME

GUIDANCE NOTES FOR CONTRACTORS AND CERTIFYING ENTITIES

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**Information Society
and Media**

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1. INTRODUCTION

These guidance notes have been compiled to guide participants and certifying entities in the preparation of audit certificates under the European Commission's eTEN Programme.

The objective of these guidance notes is to give an overview of the requirements and contractual provisions which are of importance in claiming costs for reimbursement and hence in the certification of financial statements. In the event the concentration of information in this document should lead to inconsistencies, the stipulations of the eTEN grant agreement and its annexes will prevail.

This document has been composed on the basis of the contractual provisions for market validation and support action projects. The principles for deployment projects are, however, similar, so that the guidance notes may also be used for this type of project. Where the contractual provisions in the deployment grant agreement are different from those mentioned below, this will be indicated.

2. CONTRACTUAL REQUIREMENTS

Article 4.2 (b) of Annex II to the grant agreement¹ states:

“Each *beneficiary* or *member* receiving for this *project* a total Community financial contribution equivalent to EUR 150.000 or more shall request an external auditor to certify its financial statements. Each *beneficiary* or *member* which will receive a *pre-financing* or intermediary payments cumulatively exceeding EUR 750.000 per financial year shall provide the corresponding financial statement in the format specified in Part E, Forms E-1/A and E-1/B, certified by an external auditor. (...)

Such audit certificates shall be provided at the time of submission of Forms E-1 and E-2, as applicable.”

This implies essentially that participants, in most cases² at the end of the project – i.e. with the last cost claim - will have to deliver an audit certificate in case the total request for Community financing exceeds EUR 150.000. This audit certificate has to cover the total project duration and not just the last reporting period.

¹ The provisions referred to in this section 2 of the guidance notes are those in the market validation and support action grant agreement. In the deployment grant agreement, a similar provision is contained in Article 4.2 (c) of Annex II to the grant agreement. Please note, however, that the contract provisions in this type of grant agreement are slightly different with regard to the requirement of an audit certificate in cases of pre-financing or intermediary payments cumulatively exceeding EUR 750.000 per financial year. The deployment grant agreement requires that in such cases, the audit certificate shall be submitted together with the interim Milestone payment request of the participants as specified in Article 4.2 (b) of Annex II to the deployment grant agreement.

² Unless at interim stage EUR 750.000 is requested.

Furthermore the grant agreement states in the same article:

“Each *beneficiary* or *member* is free to choose any external auditor, including its habitual external auditor, provided that it meets the following cumulative professional requirements: (i) the external auditor must be independent from the *beneficiary* or *member*; (ii) the external auditor must be qualified to carry out statutory audit of accounting documents in accordance with the 8th Council directive 84/253/EC of 10 April 1984 or similar national regulations. Where a *beneficiary* or *member* is a public body, it may opt for a competent public officer provided that the relevant national authorities have established its legal capacity to certify such document.”

This implies that all participants, whether public or private, will have to deliver an audit certificate and there are no exemptions related to the type of organisation. A participant may choose its usual external auditor but is not obliged to do so. In any case the auditor must be independent meaning that the auditor can carry out his/her work without direction or interference of any kind of the participant concerned. A preliminary condition is that the auditor (external or competent public officer) was not involved in any way in drawing up the cost claim.

The legal capacity of the competent public officer to carry out audits of that specific public body is established by the relevant national authorities. This is usually done by a letter of notification to the Project Officer of the project within the eTEN unit in the Directorate-General Information Society and Media of the Commission and subsequent letter of confirmation. Reference should be made to this notification in the certificate. As an alternative this letter could be attached to the audit certificate itself³.

The services provided by an external auditor to the participant are considered as subcontracting arrangements⁴ and are therefore subject to the requirement of selection of the bid offering the best value for money (see Articles 5.2 and 14.3 of Annex II to the grant agreement). Where the participant uses its usual external auditor then it is presumed that the contractor already has an agreement with the auditor and is not obliged to find new bids.

Article 4.2 (b) of Annex II to the grant agreement further indicates that :

“Certification by external auditors does not affect the liability of *beneficiaries* or *members* according to this grant agreement nor the rights of the Community arising out of Article 17 of this Annex.”

³ It should be noted, however, that in this case the participant bears the risk that the Commission does not accept the argumentation put forward in the letter of notification and as a result does not accept the audit certificate.

⁴ The costs of the certification itself is an eligible cost under the “other specific costs” category (see section 3.5)

An audit certificate is in fact a project deliverable which is presented to the Commission through the co-ordinator. As a project deliverable the European Anti Fraud Office (OLAF) and the Court of Auditors may have access to the certificates. Each contractor will remain responsible to the Commission for the costs it has claimed. The auditor has a contractual relation solely with the contractor – and not with the Commission. The Commission will not intervene in any dispute between the auditor and the contractor.

3. BASIC PRINCIPLES

3.1. Scope of the audit certificate

The auditors should essentially establish whether the costs claimed are eligible, actually incurred during the project and recorded in the books of account of the participant. The audit is a financial audit and should not reflect on the efficiency, effectiveness and economy in the allocation of resources by the participant and should not cover the achievement of technical results and/or project objectives. The eligibility criteria of the grant agreement (see in particular Articles 13 to 16 of Annex II to the grant agreement) always override normal accounting practices.

For the establishment of an audit certificate the auditors have to carry out a compliance audit and not a normal statutory audit. The minimal requirement is to arrive at reasonable assurance⁵.

3.2. Eligibility of costs

The general principles on the eligibility of costs are indicated in Article 13 of Annex II to the grant agreement. Article 14 and 15 of Annex II to the grant agreement indicate the different categories of costs. Under 'Direct costs' there are nine categories as follows: personnel, durable equipment, subcontracting, travel and subsistence, consumables, computing, protection of knowledge, other specific costs and administrative and financial co-ordination. The latter is an eligible cost category for the co-ordinator. 'Indirect costs' are either based on actual costs (if the participant uses the full cost system) or a flat-rate amount of 20% of the direct costs is to be applied (if the participant uses the additional cost system, see Article 15 of Annex II to the grant agreement).

3.3. Contractual relations between the participant and the auditor and auditor's liability

Although participants remain responsible towards the Commission for the costs they have claimed, auditors must be aware that they have a professional liability for the correctness of their certificates. It is advisable that the participant signs a task assignment agreement with the auditor prior to the start of the audit work. This task assignment could include:

⁵ As provided in the International Auditing standards 'Reasonable Assurance' means 'A high, but not absolute, level of assurance, expressed positively in the auditor's report as reasonable assurance, that the information subject to audit is free of material misstatement.'

- The requirement for auditors to document their audit procedures in accordance with generally accepted auditing standards;
- Reporting requirements for both the auditor and the participant in case a qualified opinion is submitted by the auditor (see also below);
- The obligation for the auditor to provide proof of his qualifications to carry out statutory financial audits and to provide copy of his registration with the competent authority of the country of legal residence of the participant.

In addition, it might be considered to foresee in the task assignment the possibility for the Commission to verify the working papers of the auditor on request.

3.4. Qualified opinions

The participant and the auditor are expected to clear any questions on factual data or detailed calculations prior to submission of the cost claim, and the accompanying audit certificate, to the Commission. It is also recommended that the participant takes into account the auditor's preliminary comments and suggestions in order to avoid a qualified opinion or to reduce the scope of the qualifications.

However, persisting disagreement on matters of principle of interpretation of contractual provisions can exceptionally lead to a qualification by the auditor.

Auditors need to substantiate such qualifications in the audit certificate. In doing so they must highlight the assumptions made by the participant and not accepted by the auditor (this can be done in the section "Qualifications" foreseen in the model audit certificate). They must also provide calculations demonstrating the impact of each of the assumptions rejected by the auditor on the amount of costs declared. For this purpose, the model audit certificate contains a table which clearly sets out the amounts declared, with a breakdown whereby distinction is made between costs for which the auditor expressed a qualification and the accepted costs.

The Commission will examine the explanations and calculations provided by the auditor in order to determine the amount of the costs that can be accepted. Qualifications by the auditors will normally lead to a rejection by the Commission of those costs for which a qualification has been expressed. In exceptional cases, however, the Commission might come to the conclusion that the costs can be accepted in spite of the auditor's qualifications.

In case of qualifications, it might therefore also be useful to attach to the audit certificate a report on the contradictory discussion between the auditor and the participant listing arguments and counter arguments of both parties. This report should be signed by both parties and, as detailed above, should be limited to matters of principle or interpretations of contractual conditions.

3.5. Reimbursement of costs of an audit certificate

According to Article 14.8 of Annex II to the grant agreement, the cost of certification of financial statements is an eligible cost under the “other specific costs” category. For deployment projects, the costs of certification are also acceptable under the “other specific costs” category, although this is not explicitly mentioned in the deployment grant agreement (see Article 14.8 of Annex II to the deployment grant agreement).

The costs will be reimbursed according to the funding percentage set out in the grant agreement.

3.6. Form of an audit certificate

It is recommended that the external auditor or competent public officer follows, to the extent possible, the model audit certificate in Annex I to these guidance notes. This model is not binding. However, deviations may result in additional information and clarification being requested by the Commission and the subsequent risk of rejection of the certificate. Both the audit certificate and its Appendix I (Summarised data of eligible costs declared to the Commission by the participant) must be signed (signature and stamp) and dated by the external auditor or the competent public officer.

The audit certificate should be established in the language foreseen for project deliverables in Article 4.1 of the grant agreement (usually English). The audit certificate is to be submitted in two originals and one electronic copy through the coordinator.

4. PRACTICAL HINTS FOR PARTICIPANTS

In order to avoid delays in the submission of audit certificates, participants should select and contract the auditor well before the financial statement is due. As a first step it is essential that the auditor fully understands the requirements of the audit certificate and that the auditor is provided with a complete set of the documents necessary for the audit certification (see below).

The auditor will then establish an audit plan/audit strategy which normally includes familiarisation with the contractual provisions. An indicative model for an audit programme is provided in Annex II of these guidance notes. In the execution of the audit programme the auditor may need access to further detailed information and participants should ensure that relevant staff is available to provide any explanations/additional information that may be needed.

At an early stage of contact with the auditor, the participant will need to communicate a number of essential parameters that will determine the certification process. These include:

- The cost reporting model used. If an AC cost reporting model is used, indirect costs do not need to be examined as a flat-rate is applied. If an FC cost reporting model is used, the indirect costs will need to be certified.
- The number of staff involved in the project. The major cost of a project is normally personnel costs. Certification of these costs may imply a verification of the time spent by staff on the project, the calculation of the hourly personnel rates, the calculation of the productive hours and, for example, an examination of the employment contract. In addition, for participants using the AC cost reporting model, the temporary nature of the contract or the dependence on external funding will need to be verified (see Article 14.1 (c) of Annex II to the grant agreement).
- The usual accounting rules, for example, whether travel costs are usually considered to be direct or indirect costs (see Article 14.4 of Annex II to the grant agreement: 'Travel and subsistence costs shall be established on the basis of the usual rules of the participants').

The following documents serve as a basis for certification. The list refers to principal documents and does not include the audit evidence which must be obtained from the accounting system of the participant. The list is therefore not exhaustive.

- Grant agreement signed between the participant and the Commission
- The Annexes to the grant agreement, i.e. Annex I 'Description of Work' and Annex II 'General Conditions' (in particular, part C of Annex II setting out the provisions for reimbursement of costs) and Annex III (Specific conditions)
- The table of indicative breakdown of costs and financing plan for the project
- Periodic reports, which normally contain information about the progress of work and e.g. resources employed
- The financial statements in the formats specified in the contract
- Communications between the Commission and the participant, or co-ordinator, with respect to the financial statements
- Proposed model for an audit certificate (see Annex I)
- Indicative model of an audit programme (see Annex II)

In Annex III a list of frequent errors in eTEN financial statements is provided.

In case you need further information you can contact the Commission's project officer of your project.

AUDIT CERTIFICATE

I/We..... [*name(s) of auditor(s)*].....of.....[*name of audit firm*].....(copy of document of approval by the competent authorities attached herewith) hereby certify that :

I/We have conducted a financial audit of the financial statement(s) presented to the Commission, and summarised in Appendix I to this audit certificate, under grant agreement [*grant agreement reference*] by.....[*name of company/organisation audited*].... in respect of the project.....[*reference number and acronym of project*] for the total project duration.⁶

The audit was carried out in accordance with generally accepted auditing standards respecting ethical rules and on the basis of the relevant provisions of the above-referenced grant agreement and its Annexes. The above-mentioned financial statements were examined and such test of the supporting documentation and accounting records deemed necessary were carried out in order to obtain reasonable assurance⁷ that [subject to the qualifications mentioned below]:

- Only eligible costs are claimed in accordance with the financial provisions of the grant agreement,
- the costs claimed are related to the project,
- the costs claimed are actual costs recorded in the official accounts of [*name of the participant*],
- the costs claimed have been incurred during the duration of the project or as otherwise specified in the grant agreement,
- the actual hours worked by the persons directly undertaking the work for the project and charged to the grant agreement are supported by time records maintained in accordance with the relevant article of Annex II to the grant agreement.

[Qualifications:]

Signature & date

Audit Company's Stamp

⁶ Note that this does not apply if the participant receives a prefinancing or intermediary payments cumulatively exceeding EUR 750.000 per financial year.

⁷ As provided in the International Auditing standards "Reasonable Assurance" means "A high, but not absolute, level of assurance, expressed positively in the auditor's report as reasonable assurance, that the information subject to audit is free of material misstatement."

Appendix I to the audit certificate

**Summarised data of eligible costs declared to the Commission by the participant
..... for the period(s).....to**

Cost categories	Costs declared (Euro/currency...)		
	Unqualified	Qualified	Total
Direct costs ⁸			
1. Personnel			
2. Durable equipment			
3. Subcontracting			
4. Travel and subsistence			
5. Consumables			
6. Computing			
7. Protection of knowledge			
8. Other specific costs			
Indirect costs			
9. Overheads			
Total			

The total cost incurred by the contractor for the audit certificate[s] relating to the [first][and] [specify cost claim] [and] [final] cost claim is Euro..... [amount to be specified.]

Signature & date

Audit Company's Stamp

⁸ For certification of financial statements of the co-ordinator, an additional cost category for "administrative and financial co-ordination costs" might need to be inserted.

ANNEX II : INDICATIVE MODEL OF AN AUDIT PROGRAMME

This model audit programme is designed as a guideline to cover the main areas in need of attention during a complete audit. The prime objective of each audit will always be to verify that the costs incurred in performing eTEN grant agreements, have been claimed in compliance with the contractual rules defined in each specific grant agreement under audit.

1. Ensure availability and access to the following documents:

- Grant agreement signed between the participant and the Commission
- The Annexes to the grant agreement, i.e. Annex I 'Description of Work' and Annex II 'General Conditions' (in particular, part C of Annex II setting out the provisions for reimbursement of costs) and Annex III (Specific conditions)
- The table of indicative breakdown of costs and financing plan for the project
- Periodic reports, which normally contain information about the progress of work and e.g. resources employed
- The financial statements in the formats specified in the contract
- Communications between the Commission and the participant, or co-ordinator, with respect to the financial statements
- Proposed model for an audit certificate
- List of frequent errors in financial statements

2. Review the grant agreement to be audited.

3. Establish which cost reporting model is applicable

4. Review costs claimed

- Direct costs - personnel
 - ✓ Reconcile the charged working time with supporting documents (time records)
 - ✓ Verify that the hourly labour rates have been correctly calculated, i.e. gross remuneration plus all related charges, divided by productive hours (indicator: 1.680 p.a.); verify that the number of chargeable hours used for the calculation of the hourly rate is reasonable and in line with the participant's normal practice. Ensure that the actual number of productive hours performed does not exceed the number of productive hours applied in this calculation.
 - ✓ Verify that the amounts charged correspond with the amounts (gross remuneration plus employer's portion of social charges) actually paid and are recorded in the official books of the participant (NB: provisions are non eligible costs).

- ✓ Substantive testing of underlying documents regarding costs charged to the financial statement such as personnel files, labour grant agreements, salary information, progress reports as well as minutes of meetings, publications concerning the project
- ✓ Conclude on the eligibility of the labour costs claimed, and calculate the audit adjustment, if necessary.
- Direct costs - other
 - ✓ Reconcile the claimed costs with the supporting documentation.
 - ✓ Verify compliance of the claimed costs with the terms of the grant agreement (Articles 13 and 14 of Annex II to the grant agreement)
 - ✓ Ensure that the rules on subcontracting have been complied with (see Article 5 of Annex II)
 - ✓ Ensure that no VAT is included.
 - ✓ Conclude on the eligibility of the costs claimed, and calculate the audit adjustment, if necessary
- Indirect costs
 - ✓ Verify that overheads have been claimed in line with the applicable cost reporting model.
 - ✓ Review system of overhead apportionment, calculation method and allocation to grant agreements.
 - ✓ Agree the figures considered for the calculation of overheads with the profit and loss accounts and review the accounting records.
 - ✓ Verify compliance with the terms of the grant agreement regarding the costs charged.
 - ✓ Verify that the number of chargeable hours used for the distribution of overheads is reasonable and in line with the participant's normal practice. If overheads are distributed over salaries, verify that the percentage has been correctly calculated.
 - ✓ Conclude on the eligibility of the overheads claimed, and calculate the audit adjustment.
 - ✓ Ensure that costs accounted for in the overhead calculation do not include ineligible costs which do not meet the eligibility criteria as set out by Articles II.13 and II.15 of Annex II.

5. Complete and sign two copies of the Audit Certificate and submit to the participant.

ANNEX III : LIST OF FREQUENT ERRORS IN FINANCIAL STATEMENTS

This list of frequent errors is based on the experience gained in eTEN projects.

Non-substantiation of working time

The working time to be charged to the grant agreement must be recorded throughout the duration of the project as foreseen in Article 14.1 (a) of Annex II to the grant agreement. The person in charge of the work designated by the participant or the duly authorised financial officer of the participant must certify the records at least once a month. An estimation of hours worked is not sufficient. There must be a system that allows the time of anyone working on the project to be recorded and audited. Good practice suggests that the link between the project and the time record is clearly established and that the type of work performed is indicated.

Budgeted versus actual costs

A further problem observed is the use of budgeted personnel and overhead rates. At the time of submitting financial statements actual costs must be reported and the participant has amongst others to certify that “costs are actually incurred”.

Use of average personnel rates

Only the costs of the actual hours worked may be charged to the grant agreement. Many participants however generally base cost claims on average personnel rates. Average employment costs are allowed provided this corresponds to the normal practices of the participant concerned and such costs do not differ significantly from the actual costs. Moreover such practices must be regarded as acceptable by the Commission (see Article 14.1 (b) of Annex II to the grant agreement). Thus it needs to be verified whether the average personnel rate reflects the actual costs incurred in the specific project. Participants should be aware that the acceptance of average rates by national authorities is of limited value in this respect as cost claims need to comply with the specific financial provisions of the eTEN grant agreement.

The calculation of hourly personnel rate

A further problem concerns the calculation of the hourly personnel rate. The hourly personnel rate is to be calculated as ‘the actual costs (gross remuneration and the employer’s portion of social charges) divided by the number of productive hours’. Audit evidence indicates that in general a plausible number of productive hours are in the order of 1680 hours per year. If in the calculation of the hourly personnel rate a significantly lower number of productive hours is used a solid justification should be on file.

Personnel Costs for participants using the AC cost reporting model

The conditions for personnel costs related to participants using the AC model are more specific and refer to “a temporary contract for Community projects, or a contract which depends upon external funding additional to the normal recurring funding of the participant” (see Article 14.1 (c) of Annex II to the grant agreement).

Indirect costs

The principal errors in the calculation of overhead are as such:

- Cost items which do not meet the eligibility criteria as set out by Articles 13 and 15 of Annex II in terms of “necessary for the project” are included in the claimed overhead costs. Prominent examples are marketing costs, non-productive hours of staff or non-chargeable activities.
- use of budgeted rates
- non-eligible cost items like notional costs
- unbalanced apportionment of overheads

VAT

It has been observed that VAT has been included as part of, for example, the ‘travel and subsistence’ or ‘consumables’ costs claimed. The grant agreement in general excludes ‘indirect taxes and duties, including VAT’ as an eligible cost (see Article 13.4 of Annex II to the grant agreement).

Lack of prior agreement in case of subcontracting

For the subcontracting of elements of the work, the grant agreement requires, under certain conditions, the prior approval of the Commission, unless Annex I to the grant agreement already contains sufficiently detailed data with regard to the subcontracting (see Article 5.2 of Annex II to the grant agreement). It is observed that in some cases the subcontracting of tasks is neither specified in Annex I nor covered by the required prior written approval of the Commission.

Substantiation of costs claimed

The participant is obliged to keep appropriate supporting documentation to justify the costs claimed on file.

In order to substantiate costs, for example durable equipment and travel supporting invoices, tickets etc. must be filed so that there is a proper audit trail