



European  
Commission

**CERTIFICATES ISSUED BY EXTERNAL AUDITORS**

**GUIDANCE NOTES FOR BENEFICIARIES AND AUDITORS**

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**Disclaimer**

This guide is aimed at assisting beneficiaries and auditors. It is provided for information purposes only and its contents are not intended to replace consultation of any applicable legal sources or the necessary advice of a legal expert, where appropriate. Neither the Commission nor any person acting on its behalf can be held responsible for the use made of these guidance notes.

## Introduction

These guidance notes have been compiled to guide research beneficiaries and external auditors in the preparation of Certificates on the Financial Statements and on the Methodology for calculating personnel costs/indirect costs under the 7th RTD Framework Programme (FP7).

In particular, the document considers the following topics and related issues:

- FP7 model Grant Agreement<sup>1</sup>;
- Guide to Financial Issues Relating to FP7 Indirect Actions<sup>2</sup>;
- Frequently asked questions (FAQs) received by the European Commission from external auditors, beneficiaries and the Commission's operational services<sup>3</sup>.

The objective of these guidance notes is to give an overview of the requirements and provisions which are of importance in claiming costs for reimbursement and hence in the Certification on the Financial Statements and on the Methodology.

The text of this document is valid as of the present date however it may be updated if necessary to reflect developments in the Certificate on the Financial Statements and on the Methodology procedures as they occur.

This document is composed of Part I dealing with the Certificates on the Methodology, Part II covering the Certificates on the Financial Statements and Part III which is a common glossary for both types of Certificates.

This is the fifth update of the Guidance Notes for Beneficiaries and Auditors on FP7 audit certification issues. The main reason for this update is the adoption of the new Financial Regulation<sup>4</sup> which results in the following modifications to the FP7 general model Grant Agreement:

- Art. 6 of the core: **Reduction of the time-limit for payment of pre-financing** to 30 days from the entry into force of the grant agreement
- Art. II.5: **Reduction of the time-limit for payment for interim and final payments** to 90 days from the receipt of the reports.
- Art. II.6 **Abolition of the coordinator's obligation to open and operate an interest-bearing bank account;**

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<sup>1</sup> See in particular Articles II.4 and II.14-II.19 of Annex II (General Conditions, Part B) of the model grant agreement:

[http://ec.europa.eu/research/participants/portal/page/fp7\\_documentation](http://ec.europa.eu/research/participants/portal/page/fp7_documentation)

<sup>2</sup> See in particular Part A, Section 2 of the FP7 Guide to Financial Issues:

[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide_en.pdf)

<sup>3</sup> See the FAQ:

[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Audits/audit\\_certification\\_faq\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Audits/audit_certification_faq_en.pdf)

<sup>4</sup> The Regulation No 966/2012 on the financial rules applicable to the general budget of the Union repealing Council Regulation (EC, Euratom) No 1605/2002 (former Financial Regulation)

- **II.19 Abolition of the coordinator's obligation to declare and reimburse** to the Commission the **interest generated by the pre-financing**.

These changes apply as from 01.01.2013 to both future and existing (on-going) grant agreements. For on-going grant agreements, these new rules will automatically apply as from 1.1.2013 without the need for individual amendments to the grant agreements.

In addition, regarding financial statements (Form C), certificates on financial statements and certificates on the methodology Art. 8 and Art II.4 of the Grant Agreement were also modified with the following implications relevant for the present Guidance Notes:

- For Grant Agreements **signed before 31.12.2012**, the consortia may apply the new electronic-only transmission and signature system, provided they introduce a request for an amendment via the coordinator.
- For Grant Agreements signed **after 01.01.2013** the obligations of electronic-only signature and transmission of the Form C and the electronic-only transmission of the certificates on financial statements and certificates on the methodology have been introduced.

As a consequence, in order to reflect the recent update of the new Financial Regulation and those of the FP7 model Grant Agreements, the following modifications have been introduced in the present "Guidance Notes for Beneficiaries and Auditors":

- The abolition of the obligation to submit the certificates on financial statements in paper form for Grant Agreements signed as from 01.01.2013 (Part II–5 and Part I–4 respectively).
- The abolition of the coordinator's obligation to open and operate an interest-bearing bank account and to declare and reimburse to the Commission the interest generated by the pre-financing as from 01.01.2013 (Part II – 6.4.7);

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## General principles

The Certificates on the Financial Statements (CFS) and on the Methodology for both personnel and indirect costs (CoM) and on the Methodology on average personnel costs (CoMAv) are independent reports of factual findings produced by an external auditor (or in the case of a public body it may be provided by a competent public officer) according to the requirements of Article II.4 of the Grant Agreement.

The purpose of the report of factual findings is to give to the Commission relevant elements necessary to assess whether costs (and, if relevant, the receipts and interests generated by the pre-financing) charged under the project are claimed by the beneficiaries in accordance with the relevant legal and financial provisions of the FP7 model Grant Agreement.

**N.B: The submission of a Certificate on the Financial Statements or on the Methodology does not waive the right of the Commission or the European Court of Auditors to carry out their own audits<sup>5</sup>.**

Notwithstanding the procedures to be carried out, the beneficiary remains at all times responsible and accountable for the accuracy of the Financial Statements. A beneficiary making false declarations or failing to meet its obligations under the Grant Agreement shall be liable to financial penalties according to Article II.25 of the Grant Agreement.

The auditor has a contractual relationship solely with the beneficiary. The auditor does not have a contractual relationship with the Commission and the Commission will not intervene in any dispute between the auditor and the beneficiary.

The Auditor shall undertake that his work has been carried out:

- in accordance with the International Standard on Related Services ('ISRS') 4400 *Engagements to perform Agreed-upon Procedures regarding Financial Information* as promulgated by the International Auditing and Assurance Standards Board (IAASB) of IFAC;
- in compliance with the *Code of Ethics for Professional Accountants* issued by the International Ethics Standards Board for Accountants (IESBA) of IFAC. Although ISRS 4400 provides that independence is not a requirement for agreed-upon procedures engagements, the European Commission requires that the Auditor also complies with the independence requirements of the *Code of Ethics for Professional Accountants*.

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<sup>5</sup> "The Commission may, at any time during the grant agreement and up to 5 five years after the end of the project, arrange for audits to be carried out [...]" (Article II.22 of the FP7 Model Grant Agreement).



# 1. AUDITORS ELIGIBLE TO DELIVER THE CERTIFICATE ON THE FINANCIAL STATEMENTS AND ON THE METHODOLOGY (CoM AND CoMAV)

Each beneficiary is free to choose a qualified external auditor, including its statutory external auditor, provided that the following cumulative requirements are met:

- the external auditor must be **independent** from the beneficiary;
- the external auditor must be **qualified** to carry out statutory audits of accounting documents in accordance with national legislation implementing the Directive on statutory audits of annual accounts and consolidated accounts<sup>6</sup> or any Union/Euratom legislation replacing this Directive. Beneficiaries established in third countries must comply with equivalent national regulations in the same field and the certificate on the financial statements provided will consist of an independent report of factual findings based on procedures specified by the Union/Euratom.

The services provided by the auditors to the beneficiaries follow the requirements related to subcontracts in the framework of FP7 Grant Agreements and are therefore subject to the requirements of best value for money (Article II.7 of the FP7 model Grant Agreement). Beneficiaries shall ensure that the rights of the Commission and the Court of Auditors to carry out audits are extended to cover the auditors.

According to the provisions of Article 27 of the Treaty on the functioning of the European Union, Article 142 of the Financial Regulation and Article 19§10 of the FP7 Rules for Participation, the Court of Auditors has the right to access the records on the premises of any natural or legal person in receipt of payment. Although this would not automatically include the working documents of the auditors, the external auditors might have to provide access to their working papers if the Court of Auditors requests so and when it is necessary to carry out its task. Therefore, the access to working papers should not be required as a matter of course but because there is a genuine concern about the way in which the funds have been spent by the beneficiary. If this access requested by the Court of Auditors would concern working papers subject to a professional secrecy or confidentiality requirements of the national jurisdiction, the auditors concerned are advised to address this issue in a bilateral manner with the Court of Auditors in order to ensure that the auditor can duly respect his professional obligations.

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<sup>6</sup> Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC.

Public bodies, secondary and higher education establishments and research organisations<sup>7</sup> have the choice between an external auditor and a competent public officer. Where a public body opts to use a competent public officer, the auditor's independence is usually defined as independence from the beneficiary "in fact and/or in appearance". A preliminary condition is that this competent public officer was not involved in any way in drawing up the Financial Statements (Form C) and that she/he is not hierarchically dependent from the officer responsible for the Financial Statements. Relevant national authorities must establish the legal capacity of the competent public officer to carry out audits of that specific public body. Although it is not compulsory, based on good practice, it is recommended this be notified by a letter to the relevant research Directorate General and subsequent letter of acknowledgement of receipt from that Directorate General. Reference should be made to this notification in the certificate.

There are no specific independence requirements in relation to the auditors establishing Form E versus the auditors establishing Form D. Either form may be established by one and the same qualified and independent auditor or another one.

The Terms of Reference for the Certificate on the Methodology / on the Financial Statements state that no conflict of interest exists between the auditor and the beneficiary for establishing the certificate. A conflict of interest arises when the auditor's objectivity to establish the certificate is compromised in fact or in appearance when the auditor for instance:

- was involved in the preparation of the Financial Statements (Forms C);
- stands to benefit directly should the certificate be accepted;
- has a close relationship with any person representing the beneficiary;
- is a director, trustee or partner of the beneficiary;
- is in any other situation that compromises his or her independence or ability to establish the certificate impartially.

The Commission stresses that where a beneficiary (in the case of public bodies, research organizations and secondary and higher education establishments) chooses to use its competent public officer (e.g. the internal auditor), the beneficiary must ensure that the competent public officer is fully independent and is sufficiently qualified to perform the related procedures. In many organizations the remit of the internal audit function is not adequate to perform accounting systems tests. In such case, it is essential to have a competent external auditor to perform the tasks.

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<sup>7</sup> Research organisation, as defined by the FP7 Rules for Participation, means a legal entity established as a non-profit organisation which carries out research or technological development as one of its main objectives.

## 2. REIMBURSEMENT OF THE COSTS OF THE CERTIFICATES

The **cost of the Certificate on the Financial Statements** is an eligible cost in the Grant Agreement under the conditions set forth in Articles II.14 and II.4.<sup>8</sup>

The **cost of the Certificate on the Methodology** (CoM and CoMAv) is an eligible cost in any of the financial statements submitted in any FP7 Grant Agreement in which the beneficiary participates after the acceptance of the Certificate on the Methodology by the Commission. The cost of the Certificate on the Methodology, even if it will be used for all FP7 Grant Agreements, can be claimed only once in the lifetime of FP7 unless, due to a change of the methodology, the submission of a new certificate is required.

The FP7 Model Grant Agreement provides that the cost of the Certificate on the Methodology (CoM or CoMAv), which unlike periodic Certificates on the Financial Statements is not linked to a specific project as such, is an eligible cost. In order to avoid that this type of costs disproportionately weigh on the available EU funding of individual projects under which they are submitted, it is important that consortium partners anticipate their intention to provide such certification and identify the estimated costs already at the proposal stage and again at the negotiation stage. As such, this can be foreseen in due time in the project budget.

- If a competent public officer has provided the certificate, then the identifiable direct actual costs (gross remuneration and related charges) will be considered eligible. The total amount charged shall exclude any profit margin.
- The price charged for a certificate is subject to the general eligibility criteria of the Grant Agreement and should consider relevant market prices for similar services. In order to be eligible, the price should in particular be consistent with the principles of economy, efficiency and effectiveness. Excessive or reckless expenditures will be rejected.
- The auditor invoices directly to the beneficiary giving a breakdown of the amount of fees charged and the VAT applied. The amount of VAT is not an eligible cost for reimbursement by the EU/Euratom financial contribution.
- The Commission will not pay the cost of building up the methodology. The eligible cost is limited to the performance of the agreed upon procedure (Annex VII) with the exclusion of any costs relating to consultancy for improvement or refinement of the methodology.
- Costs incurred for the Certificates on the Financial Statements and for the Certificates on the Methodology issued by the external auditors are eligible direct costs charged under the "Management" activity in the "Subcontracting" category.

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<sup>8</sup> For more details on eligibility of costs of the CFS, please consult point 4 of Part II of this document

However the costs for the Certificates on the Financial Statements and for the Certificates on the Methodology established by the Competent Public Officers can be treated as "Other direct costs" under the "Management" activity. Where it is the usual practice of the beneficiary to consider these costs as indirect costs, they cannot be charged as direct eligible costs.

### **3. PRACTICAL HINTS FOR BENEFICIARIES AND ESSENTIAL BACKGROUND DOCUMENTS**

In order to avoid delays in the submission of the certificates, beneficiaries should select and contract the auditor well in advance. The terms of reference attached as Annex VII of the Grant Agreement should form the mandatory basis of the engagement letter to be agreed and **signed** both by the beneficiary and **by the auditor**. As a first step it is essential that the auditor fully understands the requirements of the certificates and that the auditor is provided with a complete set of the documents necessary for the certification.

In addition to the normal supporting documents needed to perform the required testing procedures, the following documents serve as a basis for certification (the list is not exhaustive):

- Grant Agreement signed between the beneficiary and the Commission including possible amendments and its Annexes i.e. Annex I ‘Description of Work’ and Annex II ‘General Conditions’ (in particular, part B of Annex II sets out the financial provisions), Annex III (Infrastructures, SMEs, Civil Society Organisations, Eranet-Plus) and Annex VII – Forms D and E;
- ‘Guide to Financial Issues relating to Indirect Actions of the Seventh Framework Programmes’. As mentioned above these guidelines have been designed to help both beneficiaries and auditors to understand the financial provisions of the FP7 model Grant Agreement;
- The Frequently Asked Questions;
- The present guidance notes.

**PART I: CERTIFICATES ON THE METHODOLOGY**  
**(CoM AND CoMAv)**

## 1. REASONS FOR INTRODUCING THE CERTIFICATION ON THE METHODOLOGY

Experience with past framework programmes shows that most errors were found in the claims for reimbursement of personnel and indirect costs.

The objective of the Certification on the Methodology (CoM and CoMAv) is to promote the use of correct methodologies by beneficiaries when calculating personnel costs and indirect costs, thereby reducing commonly occurring errors. Upon approval of the Commission Services, Certificates on the Methodology should offer beneficiaries an assurance that the approved methodology is in line with the FP7 Grant Agreement requirements.

In view of simplifying and reducing the administrative burden, beneficiaries with approved Methodologies for both personnel and indirect costs (CoM) will not have to submit Certificates on the Financial Statements for interim payments. In addition, the final Certificate on the Financial Statements will be prepared by the auditors by verifying, for actual/average personnel costs and indirect costs, only the compliance with the declared methodology thus adding simplification to the procedures foreseen in Form D. This should also contribute to the reduction of the cost of the certification system as a whole and in particular for beneficiaries participating in several Grant Agreements. As regards other direct costs (such as travel & subsistence, depreciation of equipment, consumables and other costs), since they are not subject of the certification, the certifying auditor/Competent Public Officer will verify their eligibility against the conditions set in the FP7 Grant Agreement.

The ideal target for the provision of this kind of certification is typically beneficiaries of multiple Grant Agreements which have an established methodology for calculating their rates.

As the Certification of the Methodology, once approved, is intended to be valid throughout the whole FP7, it is clear that beneficiaries participating in several Grant Agreements will benefit from this exercise. It is assumed that the methodology used to support the reimbursement of costs claims in the future continues to be the same as the methodology "certified" by the auditor at a certain date unless the beneficiary states otherwise.

## 2. ADVANTAGES OF THE USE OF THE CERTIFICATION ON THE METHODOLOGY

WITHOUT CoM/CoMAv	WITH CoM/CoMAv
Errors in costs claimed are detected when processing payments or during ex-post audits	Early detection and corrections of possible errors in personnel and indirect costs to be claimed
No certainty that the methodology used by the beneficiary to calculate their claims is conforming to the provisions of the Grant Agreement	Early assessment of compliance with the Grant Agreement provisions of methodology applied to calculate personnel and indirect costs
Without CoM, a Certificate on the Financial Statements (hereafter referred to "CFS") to be submitted whenever the amount of the EU/Euratom contribution is equal or superior to EUR 375,000 when cumulated with all previous interim payments for which a CFS has not been submitted (except if the project duration is less than two years; in that case, only at the end of the project)	Waiving of interim CFS (only with CoM)
CFS valid only for the relevant costs claimed	CoM/CoMAv valid throughout all FP7 projects
	With CoM, reduced costs for the whole certification system
	With CoM, simplification of administrative burden both for beneficiaries and EU operational services (less certificates to provide/process)

### 3. SCOPE AND CONTENT OF THE CERTIFICATES ON THE METHODOLOGY

The Certificates on the Methodology (CoM or CoMAv) should be addressed by the auditor (or the competent public officer) to the attention of the beneficiary (not to the attention of the Commission).

The auditor undertakes this engagement in accordance with the terms of references of Form E – Annex VII (hereinafter "ToR") and Parts I and III of the document "Certificates issued by External Auditors, Guidance Notes for Beneficiaries and Auditors" and:

- in accordance with the International Standard on Related Services ('ISRS') 4400 Engagements to perform Agreed-upon Procedures regarding Financial Information as promulgated by the International Auditing and Assurance Standards Board (IAASB) of IFAC;
- in compliance with the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA) of IFAC. Although ISRS 4400 provides that independence is not a requirement for agreed-upon procedures engagements, the European Commission requires that the Auditor also complies with the independence requirements of the Code of Ethics for Professional Accountants.

The auditor performs the procedures specified in 1.9 of the ToR ('Scope of Work – Compulsory Report Format and Procedures to be performed') and uses the evidence obtained from these procedures as the basis for the Report of factual findings.

The work which has to be performed by the auditor will be further detailed in point 6 of these guidance notes.

The Certification on the Methodology (CoM or CoMAv) will consist of one Certificate for the whole Legal Entity, which must account for all the departments and all methodologies in place within the Legal Entity. In no case is a department within a Legal Entity entitled to request a Certificate on the Methodology separately from the Legal Entity. It is important that Legal Entities which may apply the special clause n°30<sup>9</sup> in FP7 Grant Agreements indicate this option in the Certificate on the Methodology which will therefore cover all methodologies applied by the Legal Entity.

The Certificate on the Methodology for both personnel and indirect costs (CoM) may cover the following costs combinations:

- Actual/average personnel costs and actual indirect costs (full analytical accounting or simplified method);
- Actual/average personnel costs and flat-rate<sup>10</sup> for indirect costs.

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<sup>9</sup> When clause n°30 applies, the department/institute which is an integral part of the beneficiary (legal entity) has an analytical accounting system which allows it to identify its actual indirect costs. Therefore the department/institute may declare indirect costs in FP7 Grant Agreements based on its actual indirect costs, despite the fact that the beneficiary (legal entity) has opted for a flat-rate.

<sup>10</sup> When clause n°30 applies, the department/institute may declare indirect costs in FP7 Grant Agreements based on its actual indirect costs, despite the fact that the beneficiary (legal entity) has opted for a flat-rate.



## 4. FORM OF THE CERTIFICATES ON THE METHODOLOGY - ANNEX VII

Use of the reporting format attached as Annex VII (Form E) of the model Grant Agreement by external auditors or competent public officers is compulsory. The reporting format should include the procedures and findings specified in Annex VII. Specific reference should be made to the Grant Agreement under which the cost of the certificate will be claimed.

Nonetheless, under point 1.9, "Scope of Work – Compulsory Report Format and Procedures to be performed", the title should read as follows: "*Independent Report of factual findings on the methodology concerning Grant Agreements financed under the Seventh Research Framework Programme (FP7).*"

The subsequent paragraph referring to a Grant Agreement: "[*title and number of Grant Agreement*]", may be the indication where the cost of the audit certificate is to be claimed and/or the basis on which the certificate on the methodology has been established.

In the section "Statements to be made by the beneficiary and corresponding procedures to be carried out by the Auditor", the "Statements to be made by the beneficiary" have to be filled in by the beneficiary and must be signed (signature and stamp or seal) and dated by the beneficiary while the "Procedures to be carried by the Auditor and factual findings" have to be filled in by the external auditor (or competent public officer) and must be signed (signature and stamp or seal) and dated in order to for the auditor issue an independent report on factual findings on the methodology concerning costs claimed under a Grant Agreement financed under FP7.

The following articles of the FP7 Grant Agreement were modified for Grant Agreements signed from 01.01.2013 on regarding the electronic transmission of reports:

- Art.8 of the core: Introduction of the 2nd paragraph indicating how reports and deliverables should be transmitted to the Commission.
- Art II.4: For Grant Agreements signed after 01.01.2013 the certificates on the methodology will have to be transmitted exclusively electronically to the European Commission as the possibility to submit certificates on the methodology in paper-form has been explicitly abolished. In practice, this implies that certificates on the methodology will have to first be hand-signed on paper and subsequently scanned and sent electronically to the corresponding functional mailbox<sup>11</sup>.

The Certificate on the Methodology should be composed of three separate documents to be found in Annex VII (Form E) of the Model Grant Agreement:

- A list of the minimum terms of reference (sections 1.1 to 1.8) required by the Commission to be included in the engagement letter between the beneficiary and the auditor. The engagement letter must be dated and signed by both parties.
- The model auditor's Report of Factual Findings (section 1.9) to be issued on the auditor's letterhead, dated, stamped and signed by the auditor (or the competent public officer).

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<sup>11</sup> Either "[RTD-FP7-Cost-Methodology-Certification@ec.europa.eu](mailto:RTD-FP7-Cost-Methodology-Certification@ec.europa.eu)" (for CoM submissions) or "[RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu](mailto:RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu)" (for CoMAv submissions)

- A detailed description (table of Annex VII – Form E) including the statements made by the beneficiary and the procedures to be performed by the auditor and the findings expected to result there from. This table has to be dated, stamped and signed on the one hand by the beneficiary for the statements in the left-column and on the other hand by the auditor (or competent public officer) for the procedures and the factual findings.

With respect to the language of the Certificate on the Methodology, Article 4 of the FP7 model Grant Agreement states that: “Any report and deliverable, when appropriate, required by this Grant Agreement shall be in [*insert language*]”. Therefore, the report of factual findings on the methodology should be written in the language indicated in Article 4 of the Grant Agreement.

## 5. SUBMISSION OF THE CERTIFICATE ON THE METHODOLOGY

### 5.1 Steps to be followed

<b>STEPS</b>	<b>Certificate on the Methodology for both personnel and indirect costs (CoM)</b>	<b>Certificate on the Methodology for average personnel costs (CoMAv)</b>
<b>1. Request for eligibility to the EC<sup>12</sup></b>	Beneficiaries who consider to meet the below criteria (point 5.2) may send a request to the EC, only by electronic mail to the functional mailbox : <a href="mailto:RTD-FP7-Cost-Methodology-Certification@ec.europa.eu">RTD-FP7-Cost-Methodology-Certification@ec.europa.eu</a> , containing the Grant Agreement/contract numbers (FP7 and/or FP6) in which they participate.  <b>WHEN:</b> at any time during the lifetime of FP7	No request for eligibility is required.
<b>2. Acceptance/rejection of the request by the EC</b>	Within 30 calendar days (possible extension of time-limit).	
<b>3. Submission of the certificate</b>	Possible only upon acceptance of the request for eligibility (see steps 1 and 2) by EC.  <b>WHEN:</b> at any time during the implementation of FP7 and at the earliest on the start date of the project of the first Grant Agreement signed by the beneficiary under FP7.  It should be noted that the auditors need a sound basis to carry out their procedures (e.g. a pro-forma statement of costs) and that the certified	<b>WHEN:</b> at any time during the implementation of FP7 and at the earliest on the start date of the project of the first Grant Agreement signed by the beneficiary under FP7.  It should be noted that the auditors need a sound basis to carry out their procedures (e.g. a pro-forma statement of costs) and that the certified

<sup>12</sup> European Commission

	<p>methodology must be the one which is used for FP7 projects.</p> <p><b>HOW:</b> This certificate can be introduced only by electronic mail to the following functional mailbox [<a href="mailto:RTD-FP7-Cost-Methodology-Certification@ec.europa.eu">RTD-FP7-Cost-Methodology-Certification@ec.europa.eu</a>]</p> <p><b>IN WHICH FORM:</b> in the form of a report of factual findings as foreseen in the Grant Agreement (Annex VII to the Grant Agreement, Form E).</p>	<p>methodology must be the one which is used for FP7 projects.</p> <p><b>HOW:</b> This certificate can be introduced only by electronic mail to the following functional mailbox [<a href="mailto:RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu">RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu</a>]</p> <p><b>IN WHICH FORM:</b> in the form of a report of factual findings as foreseen in the Grant Agreement (Annex VII to the Grant Agreement, Relevant part of Form E (procedures 0 to 3 related to personnel costs only<sup>13</sup>).</p>
<b>4. Acceptance/rejection of the certificate by the EC</b>	Within 60 calendar days (possible extension of time-limit)	Within 60 calendar days (possible extension of time-limit)

## 5.2 Specific provisions for the Certificate on the Methodology for both personnel and indirect costs (CoM)

### 5.2.1 Criteria for submission of the CoM

The submission of this type of certificate is entirely optional. According to the provisions of the model Grant Agreement (Article II.4.4), the Commission may at its sole discretion accept this submission. The Certificate on the Methodology is reserved to beneficiaries participating in multiple grants.

During the first stages of the implementation of the 7<sup>th</sup> Framework Programme, transitional eligibility criteria based on historical data (FP6) were applied<sup>14</sup> in order to open as soon as possible this option to those eligible beneficiaries.

<sup>13</sup> In the context of a CoMAv, the report on factual findings and table of procedures should not include information on indirect costs since they relate to the average personnel costing methodology only.

<sup>14</sup> Beneficiaries who have participated in at least 8 contracts under FP6 with an EC financial contribution for each of them equal or above 375,000 EUR can submit a request for certification of their methodologies for both personnel and indirect costs, as from their first participations under FP7.

It was agreed that these transitional eligibility criteria should be revised to introduce additional criteria based on the participation in FP7 grant agreements of the beneficiaries. These new criteria indeed permit the FP7 recurrent beneficiaries who are not eligible under the current FP6-based eligibility criteria, such as certain beneficiaries from the new Member States, to be eligible for submission of the Certificate on the Methodology for both personnel and indirect costs.

The Commission has agreed:

- to keep the FP6 eligibility criteria : at least 8 participations in FP6 contracts with an EU/Euratom contribution for each contract equal or above EUR 375,000, and
- to add criteria for the beneficiaries who did not meet the above FP6 criteria but would meet :
  - Either at least 4 participations in FP7 Grant Agreements signed before the 1st January 2010 with an EU/Euratom contribution for each grant agreement equal or above EUR 375,000,
  - Or, at least 8 participations in FP7 Grant Agreements with an EU/Euratom contribution for each grant agreement equal or above EUR 375,000 at any time during the implementation of the FP7.

#### *5.2.2 Consequences of the acceptance and use of the Certificate on the Methodology for both personnel and indirect costs (CoM)*

- **Intermediate CFS for claims of interim payments:** the requirement to submit an intermediate CFS within 60 days after the end of a specific reporting period shall be waived from the date of the notification to the beneficiary of the acceptance of the certificate by the Commission.
- **CFS for the final payment:** beneficiaries for whom cumulatively with previous periods, the EU contribution is equal or superior to EUR 375,000, will only have to submit a CFS for the final payment. However, for average personnel costs and indirect costs, the auditors will only have to focus on checking compliance with the certified methodology and systems, omitting individual calculations.

**Validity of the CoM:** once the certificate is accepted by the Commission, the approved CoM will be valid for all FP7 grant agreements signed by the beneficiary after the date of approval of the CoM. The approved methodology may also be used retroactively for all on-going FP7 grant agreements signed by the beneficiary before the date of approval of the CoM. This retroactive effect will be applicable only to projects, for which the period of submission of the final reports has not elapsed at the time of the notification of the CoM approval (i.e. time-limit for retroactive effect: end date of the project + 60 days).

The certificate is valid for the entire period of FP7 unless the methodology changes or if an audit or other control performed by the Commission services or on its behalf demonstrates a lack of compliance with the certified approved methodology and/or any significant abuse. The beneficiary has to declare to the Commission any changes affecting its methodology, including the date of the change. In the case of a change,

a new certificate on the methodology may be submitted, according to the same procedure as under point 5.1 above. Until the acceptance of this amended methodology, the requirement to provide intermediate CFS will not be waived. A beneficiary that has been making false declarations or has been found to have seriously failed to meet its obligations under this Grant Agreement shall be liable to financial penalties according to Article II.25 of the Grant Agreement.

- The Commission has the right to recover funds unduly paid, as well as to apply liquidated damages, when an inappropriate use of the approved methodology is identified, for example during an on-the-spot audit.
- **The costs for a Certificate on the Methodology for personnel and indirect costs (CoM)** will be eligible provided that the following cumulative requirements are met :
  1. The Commission has accepted in writing (normally e-mail) the request for eligibility of the beneficiary for submitting the Certificate on the Methodology for personnel and indirect costs.
  2. The certificate is submitted in due form (Annex VII – Form E) and the qualified auditor has performed the requested procedures. In other words, the procedures have been fully performed wherever possible by a qualified auditor and the findings duly reported by means of the Form E.
  3. The methodology certified is approved by the Commission. Please note that the auditor's fee is limited to the performance of the agreed-upon-procedures and therefore any cost incurred by the beneficiary in relation to the establishment or adaptation of the methodology (consulting, IT, etc.) is not eligible.
  4. The cost fulfils the conditions of eligibility settled in Article II.14 of the Grant Agreement.

### *5.2.3 Consequences of the rejection by the Commission*

In the case the CoM cannot be accepted, a motivated decision will be communicated to the beneficiary. The beneficiary will be invited to submit another Certificate on the Methodology compliant with the requirements of the Commission. Until the acceptance of the Certificate on the Methodology, the requirement to provide intermediate Certificates on the Financial Statements is not waived.

The costs for rejected certificates will not be eligible according to the above mentioned criteria (under point 5.2.2.).

### *5.2.4 Consequences of withdrawal of a Certificate by the beneficiary*

Costs of certificates formally submitted and subsequently withdrawn by the beneficiary prior to a formal decision of the Commission are not eligible.

## 5.3 Specific provisions for the Certificate on the Methodology on average personnel costs (CoMAv)

### 5.3.1 Abolition of the mandatory certification on average personnel costs

According to Article II.14.1 of the FP7 model Grant Agreement modified by the Commission Decision introducing simplification measures for FP7, beneficiaries may opt to declare average personnel costs. For this purpose, a certificate on the methodology used to calculate the average personnel costs (CoMAv) **may be submitted** to the services of the Commission for approval.

**This implies that beneficiaries are no longer required to submit a Certificate on Average Personnel Costs (CoMAv) for approval as a prior condition for the eligibility of the costs.**

Nevertheless, the CoMAv remains as an option offering beneficiaries the possibility to obtain prior assurance on the compatibility of the methodology in place with the FP7 Grant Agreement provisions. All beneficiaries applying average personnel costs are entitled to submit a CoMAv. Methodologies submitted for approval will be assessed against the new criteria defined in the Commission Decision introducing simplification measures (refer to point 5.4.1). Procedures for the submission and analysis of the CoMAv remain unchanged.

This provision does not stand for SME owners and natural persons who do not receive a salary. For these specific cases, please refer below to point 5.5.

### 5.3.2 Consequences of the acceptance and use of the certificate on the average personnel costs (CoMAv)

- **Intermediate CFS for claims of interim payments:** the Certificate on the average personnel costs does not waive the obligation to provide an intermediate CFS unless a complete Certificate on Methodology on both personnel and indirect costs has been submitted and approved by the Commission.
- **CFS:** Concerning personnel costs, the ex-post audits will only have to focus on checking compliance with the certified methodology and systems, thereby omitting individual calculations.
- **Validity of the CoMAv:** once the certificate is accepted by the Commission, the approved CoMAv will be valid for all FP7 grant agreements signed by the beneficiary after the date of approval of the CoMAv. The approved methodology may also be used retroactively for all on-going FP7 grant agreements signed by the beneficiary before the date of approval of the CoMAv. This retroactive effect will be applicable only to projects, for which the period of submission of the final reports has not elapsed at the time of the notification of the CoMAv approval (i.e. time-limit for retroactive effect: end date of the project + 60 days).

The certificate is valid for the entire period of FP7 unless the methodology changes or if an audit or other control performed by the Commission

services or on its behalf demonstrates a lack of compliance with the certified approved methodology and/or any abuse. The beneficiary has to declare to the Commission any changes affecting its methodology, including the date of the change. In the case of a change, a new certificate on the average personnel costs may be submitted, according to the same procedure as under point 5.1 above. The Commission has the right to recover funds unduly paid, as well as to apply liquidated damages, when an inappropriate use of the approved methodology is identified, for example during an on-the-spot audit. A beneficiary that has been making false declarations or has been found to have seriously failed to meet its obligations under this Grant Agreement shall be liable to financial penalties according to Article II.25 of the Grant Agreement.

**Validity of the CoMAv for natural persons and SME owners who do not receive a salary:** the validity of the certificate already approved by the Commission for natural persons and SME owners is retroactive as of the first day of FP7 provided that the said methodology was in use since the beginning of the project. For further details, please refer to section 5.5 below.

In the case the certificate on average personnel costs refers to both personnel receiving a salary and SME owners and beneficiaries who are natural persons not receiving a salary, the retroactivity of the certificate will be twofold: the retroactivity as of the first day of FP7 is applicable only to costs claimed for SME owners and beneficiaries who are natural persons and do not receive a salary, the validity of the certificate for personnel receiving a salary is addressed under point 5.3.1.

- **The costs for a Certificate on the Methodology for average personnel costs will be eligible provided that the following cumulative requirements are met :**

1. The certificate is submitted in due form (Relevant part of Annex VII – Form E (procedures 1 to 3) and the qualified auditor has performed the requested procedures. In other words, the procedures have been fully performed by a qualified auditor and the findings duly reported by means of the Form E.

2. The methodology certified is approved by the Commission. Please note that the auditor's fee is limited to the performance of the agreed-upon-procedures and therefore any cost incurred by the beneficiary in relation to the establishment or adaptation of the methodology (consulting, IT, etc.) is not eligible.

3. The cost fulfils the conditions of eligibility settled in Article II.14 of the Grant Agreement.

### *5.3.3 Consequences of the rejection by the Commission*

In the case the CoMAv cannot be accepted, a motivated decision will be communicated to the beneficiary explaining the reasons for the rejection and (if applicable) pointing out the issues affecting the eligibility of the costs.



The costs for rejected certificates will not be eligible according to the above mentioned criteria (under point 5.3.1.).

## 5.4 New acceptability criteria for average personnel cost methodologies

### 5.4.1 *New criteria for average personnel costs adopted by Commission Decision C(2011)714*

The new criteria adopted and established in Article II.14.1 of the Grant Agreement as modified by the Commission on 24<sup>th</sup> January 2011, provide for the acceptance of the vast majority of average personnel cost methods used by beneficiaries as their usual cost accounting practice. Those criteria are as follows:

- a) The average personnel cost methodology shall be the one declared by the beneficiary as its usual cost accounting practice; as such it shall be consistently applied to all indirect actions of the beneficiary under the Framework Programmes;
- b) The methodology shall be based on the actual personnel costs of the beneficiary as registered in its statutory accounts, without estimated or budgeted elements;
- c) The methodology shall exclude from the average personnel rates any ineligible cost item and any costs claimed under other costs categories in order to avoid double funding of the same costs;
- d) The number of productive hours used to calculate the average hourly rates shall correspond to the usual management practice of the beneficiary provided that it reflects the actual working standards of the beneficiary, in compliance with applicable national legislation, collective labour agreements and contracts and that it is based on auditable data.

These criteria will apply without prejudice to the other general eligibility criteria set out in FP7 Rules for Participation and the model Grant Agreement (i.e. cost should be incurred during the duration of the project, indicated in the overall budget, etc.). Personnel costs declared to FP7 projects resulting from the application of calculation methods fulfilling the above mentioned criteria are deemed not to differ significantly from the actual costs.

### 5.4.2 *Definition of the new acceptability criteria for average personnel costs*

Criterion a: Usual cost accounting practice declared by the beneficiary

The methodology applied should be the usual cost accounting practice of the beneficiary. The terms "...shall be the one declared by the beneficiary" means that the Commission will consider that by submitting and signing financial statements (Form C) calculated by means of a given methodology, the beneficiary is declaring that such methodology is its usual costs accounting practice. Where necessary this usual cost accounting practice should be adjusted in order to fulfil all the

acceptability criteria. For instance, this would be the case when the usual personnel cost calculation method includes ineligible items which would need to be removed (e.g. indirect taxes).

This criterion does not require the average personnel costs methodology to be equal for all types of employees, departments or cost centres. If, for instance, the usual cost accounting practice includes different calculation methods for permanent personnel and temporary personnel, this is acceptable. However, the overall methodology must be consistently applied in all FP7 participations of the beneficiary and cannot be adapted ad-hoc for particular research actions or specific projects.

#### Criterion b: Based on the statutory accounts

In order to guarantee that the average cost rates used in the methodology are based on actual costs, the calculation method should compute personnel cost rates resulting from the payroll figures registered in the statutory accounts of the entity.

Budgeted or estimated figures are not costs actually incurred and, as such, cannot be accepted as eligible components of the personnel costs. Notwithstanding this, when the actual amount of some element of the personnel costs is not known at the time of the preparation of the financial statements (Form C), beneficiaries are entitled to use the last available financial data or the best possible estimation of the actual costs. In those cases, the costs claimed must be adjusted according to the actual costs incurred as registered in the beneficiary's accounts in the subsequent period or, at the latest, at the time of the submission to the Commission of the final report of the project. The resulting adjustment to the costs already charged should be declared in an additional Form C indicating that it is an adjustment to a previous statement (by ticking out the 'yes' option in the specific box).

#### Criterion c: Excluding ineligible costs and double funding

Cost declared to be ineligible by the Commission, in particular those enumerated in Article II.14.3 of Annex II to Grant Agreement, need to be removed from the personnel rates. If the usual accounting practice includes any element considered ineligible, the personnel rates would need to be adjusted by withdrawing such components from the pool of personnel cost. In case of doubts regarding the eligibility of an item, the question can be raised to the Commission via the network of National Contact Points<sup>15</sup> or the Research Enquiry Service<sup>16</sup>.

The methodology should also prevent double funding of the same costs. As an example, certain methodologies include in the calculation of the

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<sup>15</sup> <http://ec.europa.eu/research/participants/portal/page/nationalcontactpoint>

<sup>16</sup> <http://ec.europa.eu/research/index.cfm?pg=enquiries>

personnel rates cost components which are part of the indirect costs in the beneficiaries' accounts. In such situations, if the beneficiary uses real indirect costs, the methodology should ensure that those items are removed from the pool of costs used to calculate the indirect cost charged to the FP7 projects. In the particular case of beneficiaries applying a flat-rate indirect cost method, the personnel cost cannot include any indirect cost element as these are covered by the flat-rate.

#### Criterion d: Productive time

As a general rule, the number of productive hours should be that applied as the usual practice of the beneficiary. For instance, beneficiaries could use the actual productive hours of each researcher according to the time-records or instead use a standard number of productive hours (generally annual productive hours). When the beneficiary applies a standard number of productive hours, this should be representative of its working standards. Background information used to determine the standard productive hours should be available and verifiable.

An illustrative example could be a case where a beneficiary deducts 7 working days a year as average illness absence of the employees when calculating the annual productive hours. The records substantiating this figure should be available for audit. Besides, if the records on illness absences show that systematically the number of days is lower than 7, this could be a reason for the Commission to re-evaluate the appropriateness of the standard number of annual productive hours.

In the same line please note that the Commission does not consider billable hours (hours that can be directly charged to customer/grantors) as equivalent to productive time. Billable hours are commonly much lower than productive hours, resulting in an overstatement of hourly rates and consequently of personnel cost.

#### *5.4.3 Retroactive application of calculation methods for average personnel costs*

These new criteria are applicable to costs declared in all FP7 projects. Beneficiaries can therefore directly apply their usual average personnel costs calculation method, if compatible with these criteria, for any cost declaration. No amendments to grant agreements are necessary. The new criteria will apply directly to all on-going projects.

However, for **closed grants** (i.e. in principle those for which the last payment has already been made by the Commission and the 2 months period for the Coordinator to change it has elapsed) the beneficiary is not allowed to recalculate costs which were already reported by application of other calculation methods due to the fact that the usual methodology is now acceptable under the criteria described above. For instance, if the beneficiary has charged individual actual costs due to the fact that its average personnel cost methodology was not acceptable by the Commission under the prior criteria, the beneficiary cannot re-calculate at present those costs by using averages, even if its methodology is now acceptable.

For **on-going grants where Forms C have already been paid**, if personnel costs have been submitted based on a certified methodology OR if the beneficiary has claimed actual personnel costs, beneficiaries do not need to submit adjustments referring to periods for which they claimed individual actual costs or average personnel costs on the basis of methodology certified according to the acceptability criteria in force before the 24th January 2011. However, the beneficiary may take the initiative to modify the personnel costs on the grounds that it is in line with its usual accounting practice and with the new criteria. In this case the beneficiary is requested to submit adjustments to all Forms C already paid in all on-going grants. There is no specific need for a CoMAv due to the retroactive validity of the new provisions. If costs need to be corrected, this will be done in the adjusted Form C..

The Commission will also apply these new criteria in all ongoing and future FP7 audits.

#### *5.4.4 Particular cases for already approved CoM (with average personnel costs) and CoMAv*

Following Commission Decision C(2011) 174 of 24/1/2011, the Commission has opted not to continue requiring the submission of the CoMAv for beneficiaries applying average personnel costs. However, in view of the evident preventive value of this certificate, it remains as a voluntary option for these beneficiaries.

During the period of application of the interim acceptability criteria adopted in June 2009, a certain number of beneficiaries have implemented adjustments in their usual methodology in order to obtain its approval by the Commission. All methodologies approved under the former criteria are considered as fulfilling the new criteria.

Thus, those beneficiaries who have obtained the approval of their average personnel costs methodology prior to this decision (under the former criteria) are entitled either to:

- continue applying the approved methodology;

or

- to revert to their usual accounting practice, if different from the approved methodology, in so far as this fulfils the new acceptability criteria.

Beneficiaries opting to revert to their usual accounting practices (and discontinuing the use of the approved certificate on the methodology) are advised to inform the Commission of their decision. If they wish, the beneficiaries are entitled to submit for approval a new Certificate on the Methodology. It is recommended that those beneficiaries inform the Commission on their choice via the functional mailbox:

[RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu](mailto:RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu)

## 5.5 Specific case of natural persons and SME owners who do not receive a salary: Flat-rate financing

### 5.5.1 *New context*

Following a Commission decision of 24/01/2011, Article II.14.1 of Annex II of the Grant Agreement has been modified in order to allow SME owners who do not receive a salary and natural persons beneficiaries in a FP7 Grant Agreement who do not receive a salary, to charge as personnel costs a flat rate based on the allowances used in the People Specific Programme ("Marie Curie" flat-rates).

**Target group:** SME owners and natural persons beneficiaries in a FP7 Grant Agreement who do not receive a salary, including those who are remunerated/compensated by whichever other means such as dividends, service contracts between the company and the owner, etc. *A contrario*, employees of the SME and other natural persons who do receive a salary registered as such in its accounts cannot use this flat rate.

It might however, be possible to use this flat-rate for the cases where the SME owner can show evidence that his/her salary corresponded exclusively to his/her management activity, not to his/her research work.

### 5.5.2 *Retroactive application and calculation of the flat-rate financing*

This form of flat-rate financing shall apply to all grant agreements signed under the Seventh Framework Programmes, including those already signed.

For the calculation of the flat-rate financing, please refer to the FP7 Guide to Financial issues:

[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide_en.pdf)

### *5.5.3 New rules concerning the submission of CoMAv for SME owners/natural persons without a salary*

The submission of a Certificate on Average personnel costs is no longer possible for SME owners and natural persons without a salary. As a transitional measure, the Commission dealt with all certificates submitted up to one month following the date of the decision. Certificates submitted one month after the date of adoption of the Decision were not examined. All SME owners and natural persons having received the approval of their methodology are entitled either to:

- Continue applying the approved methodology
- Apply the flat rate system as described in the FP7 Guide to Financial issues

However, if those beneficiaries choose to apply the flat-rate system they will have to apply it for all cost statements in on-going and future participations in FP7 projects. It is recommended that beneficiaries in this situation inform the Commission on their choice via the functional mailbox:

[RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu](mailto:RTD-FP7-Average-Personnel-Rate-Certification@ec.europa.eu)

Personnel costs submitted prior to the modification of Article II.14.1 of the Grant Agreement by SME owners and natural persons without a salary not having a certificate approved by the Commission will be considered eligible up to the limit of the applicable flat rate. For future cost statements, these beneficiaries will apply the corresponding flat rate and file, where necessary, adjusted Forms C (i.e. in the case that the costs charged in previous periods are different than those resulting from the application of the flat rate).

## 6 PROCEDURES FOR CERTIFICATES ON THE METHODOLOGY ACCORDING TO ANNEX VII - FORM E

### 6.1 How should the beneficiary fill out Form E?

The statements described in the left-hand column of the Form E model represent a "benchmark" methodology. It is expected in practice that there may be some differences between this and the existing systems in place.

The left-hand column of Form E must be filled in by the beneficiary and the auditor has to make factual findings in the right-hand column regarding these statements made by the beneficiary. Thus the statements should reflect the current status of the beneficiary's methodology.

For example, if time recording does not exist, this should be stated clearly by the beneficiary in the left-hand column. As a consequence, the auditor will indeed not be able to perform the procedure foreseen in the right-hand column for time-recording and will have therefore to report this scope limitation in his report under the caption "Exceptions".

It is important to note that such reported exceptions relating to deviations from the benchmark methodology as described in the statements made by the beneficiary are used as a mechanism for the Commission services to prioritise the issues to be examined. **They do not give an indication on whether the methodology will or will not be accepted by the Commission.**

### 6.2 When can the auditor decide to adapt the model findings in the right-hand column and when should he report an exception?

The procedures and factual findings which have been listed in the right-hand column of the Form E model are based on the "benchmark" methodology and attempt to clearly demonstrate that the beneficiary does indeed in practice implement the appropriate methodology for preparing its claims to be compliant with the provisions of the FP7 Grant Agreement.

Any deviations from this "benchmark" methodology, even when reported by the beneficiary, or any errors or exceptions noted by the auditor when performing the procedures will be assessed by the Commission.

Thus the Commission requires a description of the factual findings which effectively highlight any such deviations and errors or exceptions and which have to be reported by the auditor in his report under the caption "Exceptions".

For auditors, different situations require him to report findings as "Exceptions" in his report:

- Scope limitations: the existing system of the beneficiary deviates from the benchmark methodology. It is the responsibility of the beneficiary to report this. As a consequence, the auditor is not able to perform the procedure foreseen in the model Form E. In this case, it is understood that the Commission requires the auditor to report such a situation as an exception.

- Errors or exceptions: the auditor performs the procedure required by the model Form E and the findings raise errors or exceptions. The auditor is to report these errors and exceptions in the report.

### 6.3 Use of the methodology by the beneficiary

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<p>The methodology described below has been in use since <i>[date]</i>.</p> <p>The next planned alteration to the methodology used by the Beneficiary will be from <i>[date]</i></p>	<p><b>Procedure:</b> The Auditor has inspected records and documents which support the date given by the Beneficiary.</p> <p><b>Finding:</b> The dates given by the Beneficiary are consistent with the management information provided by the Beneficiary.</p>

What is the objective of this procedure?

The Commission, for each Form E, is interested in knowing the starting date of the methodology and for how long the methodology has been in use by the beneficiary, principally to ensure that a correspondence can be achieved between the use of the methodology and the relevant cost claims made by the beneficiary.

Which documents should the beneficiary prepare for the auditor?

The typical documents to be provided would include minutes of meetings, internal memos, working documents showing calculations from prior years, etc. The auditor is expected to check their consistency with the data provided by the beneficiary.

What does the Commission understand by 'alterations to the methodology'?

Alterations to the methodology should be understood as major changes, such as a move from average costs to actual costs, changes in cost drivers, changes in the way productive hours are calculated, etc. It is not intended to cover yearly updates to the most recent financial data, or changes in cost structure caused by the evolution of the institution.

If documentation is not available to support the introduction or alterations of the methodology, this should be listed as an exception in the report.

### 6.4 Personnel

#### 6.4.1 Existence of time recording and number of productive hours

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Personnel</b>	
<p>1. Time recording exists, with authorisation, which enables all personnel hours to be allocated to project work, management and administrative time, holidays, etc.</p> <p>The time recording enables the time of employees working on multiple projects to be allocated to those projects, and includes a</p>	<p><b>Procedure:</b> For 10 employees selected at random, the Auditor checked: That the employee had recorded management and administrative tasks separately from project time; That an authorisation check exists which checks, inter alia, double-charging of time; The Auditor obtained the calculation of the productive hours after inspecting all necessary records, national</p>



<p>check to prevent double charging of time.</p> <p>'Productive hours' represent the (average) number of hours made available by the employee in a year after the deduction of holiday, sick leave and other entitlements. This calculation should be provided by the Beneficiary, based on the period(s) corresponding to the Financial Statement (s) or to the last closed financial year (whichever is used by the beneficiary).</p>	<p>legislation, labour agreements, contracts and any other relevant documentation.</p> <p><b>Finding:</b> For the items checked, the time recording includes separation of time as specified above, and an authorisation including a check for double charging of time.</p> <p>For the most recent full calendar year: The average productive hours for the 10 employees was _____.</p> <p>The average productive hours per employee for the organisation as a whole, as recorded by the Beneficiary's time-records was _____.</p> <p>The productive hours calculation corresponds to the usual accounting practice of the beneficiary.</p>
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What is the objective of this procedure?

The Commission needs to confirm that time recording really exists, with the necessary separation of research time (which can be directly charged to the project), and other tasks performed by the employee<sup>17</sup> which are not directly relevant to the project. There is frequently a lack of detail in the time recording at beneficiaries, whereby only the time worked on the project is recorded and thus no conclusions can be drawn about the total productive hours<sup>18</sup>. An example of person-based time recording is available in Annex 3.

**It is recommended that the beneficiary provides a model of time-recording when submitting the Certificate on the Methodology.**

An important aim for the procedure is for the auditor to understand the methodology used to calculate (average) hourly rate(s), and obtain reasonable assurance that it/they represent(s) the beneficiary's usual cost accounting practice.

Why is the Commission interested in the productive hours' calculation?

Through this procedure the Commission intends to obtain information (if available) concerning (i) average productive hours for the 10 researchers<sup>19</sup> sampled<sup>20</sup> and (ii) the average productive hours for the organisation as a whole. This will provide the Commission with useful points of comparison between different beneficiaries, and also enable it to compare 'real' productive hours with those of the organisation as a whole. For the purpose of this procedure, "full calendar year" means "financial year" (12 months

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<sup>17</sup> Employee means researcher or research-related person or person with certain coordinating tasks (when there is a project coordinator).

<sup>18</sup> See Part III, Glossary for the definition of productive time/hours.

<sup>19</sup> Or research-related person or person with certain coordinating tasks (when there is a project coordinator).

<sup>20</sup> The sample should be drawn in the first place from the financial statement or the pro forma financial statement; if such statements do not contain the data for 10 employees, then the sample should be extended to the rest of the employees of the organisation.

period). In order to have comparable data on productive hours, the auditor should ensure that the employees subject to the sample worked during the full calendar year.

#### Why does the beneficiary need a time recording system?

The beneficiary should have in place a system to correctly apportion research-related time where it is spent on multiple projects, so that it is traceable, and the Commission can ensure that over-claiming can be prevented. From a management perspective, it is not possible to accurately apportion costs without a global overview of how research and non-research time is spent.

#### Which documents should the beneficiary prepare for the auditor?

The basic documents will be either paper timesheets filled out by the researchers, or a computer-based data which may be derived from spread-sheets, databases or specifically tailored applications.

The period in question will be the period of the "pro forma"<sup>21</sup> Financial Statement or actual Financial Statement (Form C<sup>22</sup>) or the most recent financial year to calculate productive hours if this is what has been used to calculate the rates claimed<sup>23</sup>. This Financial Statement will be used as a basis for the procedures which the auditor will carry out in the framework of the engagement.

Additional documentation includes relevant legislation on productive time, labour agreements to justify working hours, relevant employment contracts stipulating working arrangements and any other proof that the calculation of productive hours is in accordance with the usual accounting practice of the beneficiary.

#### How should time records normally be approved?

For the time recording data to be reliable, some form of check preventing double counting should exist, normally carried out by a hierarchical superior and using the data compiled from the time sheets. The beneficiary should be able to demonstrate to the auditor how this is done, and show how the system prevents double claiming. Normally this will consist of showing that no more than the total actual productive hours of an individual researcher can be charged.

For paper based systems where aggregation must be carried out manually, the main form of check is the manager/ supervisor's signature on the time-sheet itself.

#### What if the beneficiary only records project time and not all productive time on its time records?

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<sup>21</sup> "Pro forma" means the Financial Statement prepared by the beneficiary covering normally an interim period from the beginning of the project when no actual Financial Statement (Form C) covering a full reporting period for the Grant Agreement is yet available, refer to the definition in Part III, Glossary.

<sup>22</sup> Refer to the definition on Financial Statements in Part III, Glossary.

<sup>23</sup> This relevant period applies to all tests concerning personnel and indirect costs.

If the beneficiary does not require all the time worked (including administrative and management time) to be recorded on the time sheets, it will not be possible to give the average productive hours of the ten employees. This should be described as an exception in Form E.

What are the time-recording requirements in the context of a CoM or a CoMAv?

- In the context of the Certification on the Methodology covering both personnel and indirect costs (CoM), the minimum requirement is a **full time-recording per person** listing all activities (research, administrative, absence, EU/Euratom projects, non EU/Euratom projects, etc.) for all personnel involved in FP7 projects. A model of such a timesheet is available in Annex 3 of the present guide. This requirement is motivated by the fact that the CoM provides the beneficiary with a label of excellence and the benefit of a waiver on the submission of interim CFS.
- In the context of the Certification on the Methodology for average personnel costs (CoMAv), full time-recording per person is highly recommended but not absolutely required to be certified ex-ante provided that all other conditions for the approval of the methodology are fulfilled and that the number of productive hours used to calculate hourly personnel rates is a reasonable standard or an average close to the normal benchmark (e.g. 1680 hours based on 210 workable days and a 8 hour working day. In accordance with the FP7 Guide to Financial Issues which states that an effective time-recording system (a system which certifies the reality of the hours worked) is a requisite for the eligibility of costs, a reliable EU/Euratom project-based time-recording system including time records duly authorised by the project manager or other superior and enabling reconciliation of total hours worked on several EU/Euratom projects during a given period would be considered as a minimum requirement.

*6.4.2 Components of the personnel costs of the beneficiary*

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Personnel</b>	
<p>2. Personnel costs of the employees only include standard salaries, employer's costs, etc. and no special conditions exist for employees on European Union or <i>Euratom</i> projects, unless they are explicitly foreseen in the Grant Agreement.</p>	<p><b>Procedure:</b> The Auditor reconciled the personnel costs used in the average personnel cost calculation to the payroll system and accounting records.</p> <p><b>Finding:</b> The amounts used in the costs calculation and those in the accounting records were the same. The costs consisted of standard salaries and statutory employers' costs, and did not include bonuses and confirmation was obtained from the Beneficiary that no special conditions exist for employees on European Union or <i>Euratom</i> projects</p>

### What is the objective of this procedure?

To reconcile the personnel costs used in the (average) personnel cost calculation to the payroll system and accounting records. The Commission needs to check that the researchers are being paid in accordance with the normal staff remuneration policy of the beneficiary. The personnel costs should represent the normal employment costs<sup>24</sup> of the personnel (social contributions, pension contributions, payments towards sickness and maternity schemes, etc.). In particular, there should normally be no difference when comparing the amount a researcher is paid when working on a non-EU project compared to an EU project. The Commission has experienced cases of researchers receiving bonuses<sup>25</sup> paid out of the EU budget where this had not been specifically permitted by the Commission in writing.

### Which documents should the beneficiary prepare for the auditor?

The period in question will be the period of the "pro forma" Financial Statement or actual Financial Statement (Form C). The documentation for verification of the employment costs should consist of: payroll records and the most recent statutory accounts, or relevant documents and records describing the beneficiary's usual management and accounting practices as regards personnel costs under FP7 indirect actions.

The auditor will have to rely on a written representation by the beneficiary<sup>26</sup> as to the absence of specific bonuses (if none are immediately identifiable from the payroll system) and ineligible costs, in particular those enumerated in Article II.14.3 of Annex II to Model Grant Agreement. The beneficiary should provide all available information concerning national legislation, labour agreements and contracts in support of the personnel cost methodology. For example, if employers are legally required to accrue a holiday pay as part of the normal accounting of personnel costs, this could be brought to the Commission's attention.

### How does the procedure change if the beneficiary calculates hourly rates on an individual basis rather than using average categories?

When the rates are calculated *ad personam* (i.e., using the individual researcher's salary as the basis), the employment costs can also be checked per person for the researchers sampled. If the rates are an average for a category, the aggregated figures extracted from the payroll system and reconciled with the accounting records can be used to perform the check.

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<sup>24</sup> See Part III, Glossary for the definition.

<sup>25</sup> Whilst productivity bonuses or similar which are integrated part of the normal remuneration policy of the entity are commonly accepted, specific bonuses paid only for the participation on EC projects are not eligible.

<sup>26</sup> Included in the model letter of representation.

6.4.3 Correct calculation of hourly rates<sup>27</sup>

<p>3. Hourly rates are correctly calculated using (3a or 3b as appropriate) :</p> <p><b>3a: Actual personnel costs</b> based on one of the following possibilities [choose one]:</p> <ul style="list-style-type: none"> <li>• Actual personnel costs <i>per person</i> divided by actual productive hours <i>per person</i>;</li> <li>• Actual personnel costs <i>per person</i> divided by <i>standard</i> productive hours;</li> </ul> <p><b>3b: For the average costing approach</b>, the Beneficiary should state that:</p> <ul style="list-style-type: none"> <li>• The methodology used to calculate the average personnel hourly rate(s) represent(s) the usual cost accounting practice of the organisation;</li> <li>• Persons are allocated to the appropriate groups in accordance with the described methodology and the Full Time Equivalent (FTE) ratio is applied correctly;</li> <li>• Average personnel costs charged are based on the personnel costs registered in the statutory accounts of the organisation;</li> <li>• The calculation of the average personnel costs excludes ineligible items as defined in Art.II.14.3, Annex II to Grant Agreement or any costs claimed under other cost categories.</li> </ul>	<p><b>Procedure (apply 3a or 3b according to the method of calculation of personnel costs):</b></p> <p><b>3a:</b></p> <ul style="list-style-type: none"> <li>• The Auditor reviewed the calculation and confirmed that hourly rates are calculated as specified by the Beneficiary.</li> <li>• The Auditor multiplied the personnel hourly rate by the total productive hours for e the period of the Financial Statement(s) or to the last closed financial year (whichever is used by the beneficiary) and reconciled the result to the accounting records ('chargeable' personnel costs).</li> </ul> <p><b>3b:</b></p> <ul style="list-style-type: none"> <li>• The auditor reviewed all relevant manuals and/or internal guidance describing the methodology used to calculate average personnel cost;</li> <li>• Obtained a list of all average personnel rates calculated by the beneficiary in accordance with the methodology used;</li> <li>• Obtained a list of all relevant employees (working on EU projects + not working on EU projects) based on which the average personnel rate(s) are calculated;</li> <li>• The auditor reviewed the allocation of employees to the relevant group(s) and verified the correctness of the Full Time Equivalent (FTE).</li> <li>• The auditor performed a numerical reconciliation between the total amount of personnel costs taken into consideration for the calculation of the average personnel rate and the total amount of personnel costs recorded in the statutory accounts;</li> <li>• The auditor reviewed that any ineligible items in particular those enumerated in Article II.14.3 of Annex II to Grant Agreement or any costs claimed under other costs categories are excluded from the average personnel costs calculation</li> </ul>
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<sup>27</sup> Refer to Annex 2 for an example on personnel average system and hourly personnel rate

	<p><b>Finding:</b></p> <p><b>3a:</b></p> <ul style="list-style-type: none"> <li>• No differences arose from the comparisons listed above.</li> <li>• The result of the above reconciliation ('chargeable' personnel costs) in all cases did not exceed the costs recorded in the accounting records.</li> <li>• The Auditor confirms that the rates used were not budgeted or estimated amounts.</li> </ul> <p><b>3b:</b></p> <ul style="list-style-type: none"> <li>• The auditor found no discrepancies between the method described in the relevant documents and the method used by the beneficiary;</li> <li>• No differences arose from the numerical reconciliation.</li> <li>• The Auditor confirms that the rates used for the calculation of the average personnel costs were not based on budgeted or estimated amounts.</li> </ul>
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What is the objective of this procedure?

The objective is to verify that the hourly rate(s) included in the methodology have been correctly calculated from the underlying information. Therefore the auditor needs to fully understand the method used by the Beneficiary to calculate the personnel rates. If applicable, the auditor should obtain the calculation of annual productive hours. Two possibilities are usually allowed:

- a) standard number of productive hours used for all employees; or
- b) actual individual number of productive hours for each employee.

Which documents should the beneficiary prepare for the auditor?

The beneficiary should provide the following documents: relevant accounting records, manuals, internal guidance and any other relevant documents describing the methodology for the calculation of personnel costs.

Which sections have to be filled in?

Depending on whether the beneficiary intends to use actual or average cost calculation he need to fill in either point 3a or point 3b on the side "Statements to be made by the beneficiary".

The auditor has to fill in the corresponding part 3a procedures and 3a findings or 3b procedures and 3b findings, on the side of "Procedures to be carried out by the Auditor and Factual findings".

### How to perform the calculations when rates are calculated on an individual basis?

The auditor should check the accuracy of the extraction of the individual's employment costs and the productive hours (actual or standard), and verify that the division of the costs by the hours to obtain the hourly rate is arithmetically consistent with the rate that is claimed.

The auditor should verify that the rates used were not budgeted or estimated amounts. There may be an exception to this finding for periods in which the annual accounts have not been closed and the actual figures are not available. Procedures by the beneficiary should be foreseen in these cases to ensure that at the time the actual figures are available the costs are adjusted accordingly, these procedures need to be detailed and confirmed by the auditor.

### What are "accounting records" in this context?

For the recalculation of the 'chargeable' personnel costs, the accounting records will normally be the general ledger/ accounting records used to prepare the statutory financial statements (or equivalent). The check is meant simply to demonstrate that the information in the accounting records can be reconciled to the payroll system.

### How to perform the calculations when rates are calculated on an average?

The Commission Decision C(2011)714 adopted new criteria for average personnel costs.

By performing the procedures under 3b, bullets 1-4, the auditor should verify criterion one: the auditor should understand the methodology/ies used to calculate average hourly rate, and obtain reasonable assurance that it/they represent(s) the beneficiary's usual cost accounting practice. The auditor is expected to verify the number of productive hours used for the calculation of the average hourly rate. He should obtain manuals/internal guidance documents describing the methodology used to calculate average hourly rate(s) and establish whether the average hourly rates are based on standard or individual productive hours.

#### ***In the case of standard productive hours:***

- (a) obtain the underlying calculation method;
- (b) obtain a detailed substantiation of the assumptions leading to the assessment of productive and non-productive time;

#### ***In the case of individual(actual) productive hours or average of individual(actual) productive hours:***

- (a) obtain the actual number of productive hours used by the beneficiary for each person in the group (employees working on EU projects + employees not working on EU projects).

Via procedure 3b bullet 5: the auditor should verify criterion two: compare the total amount of personnel costs taken into consideration in the average hourly rate formula(s) and the total amount of personnel costs recorded in the statutory accounts.

Via procedure 3b bullet 6: Verify that the personnel costs taken into consideration in the average hourly rate formula(s) do not include ineligible items or any costs claimed under other cost categories. This procedure is particularly important for methodologies based

on cost centres. Cost centre rates may include elements of indirect costs. The auditor must make sure that costs included in the cost centre rate have not been included in another cost category as well.

## 6.5 Overheads/Indirect Costs<sup>28</sup>

### 6.5.1 Components of overheads/ indirect costs

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Overheads/ Indirect costs</b>	
<p>4. The Beneficiary confirms the following:</p> <p>Indirect costs only include those costs which cannot be allocated to specific projects and support the functioning of the organisation as a whole.</p> <p>The indirect costs do not include costs which relate exclusively to non-research parts of the organisation.</p> <p>If the organisation carries out activities other than research (e.g., manufacturing, education etc.), these indirect costs are transparently separated via cost accounting and do not form part of the claim.</p> <p><i>(This procedure does not apply to beneficiaries using a flat rate to claim indirect costs in accordance with Annex II of the Grant Agreement attached to the grant agreement being reviewed.)</i></p>	<p><b>Procedure:</b> The Auditor obtained the calculation of hourly overhead rates (indirect costs), including a detailed breakdown of the <b>indirect costs to be allocated</b> to research activity;</p> <p><b>Finding:</b> This breakdown did not contain costs relating to direct project activity, such as the cost of research personnel, project consumables and expenses; This breakdown does not contain costs relating to education or manufacturing, or other non-research activities of the Beneficiary; The breakdown of indirect costs used to calculate overhead rates was reconciled to the accounting records.</p>

#### What is the objective of this procedure?

This procedure does not apply if a flat-rate<sup>29</sup> on eligible direct costs is used for the calculation of indirect costs.

The Commission wants to ensure that the costs supported under FP7 have been incurred by the beneficiary in its research activity. The concern is that by including non-research related costs in the indirect cost calculation, the beneficiary ends up having parts of its non-research activity funded out of the FP7 budget. This most frequently occurs in universities, which may have education activities, or companies which have trading businesses where they supply goods and services other than research (e.g. a company that carries out applied research but also sells hardware and software to customers and

<sup>28</sup> Overheads and indirect costs are synonymous in the context of this document.

<sup>29</sup> As stipulated in the Grant Agreement



therefore incurs costs supporting the manufacturing, sales and marketing of these products).

Which documents should the beneficiary prepare for the auditor?

The beneficiary needs to provide a detailed breakdown of the components of the overhead cost, together with a sufficient narrative description of the individual accounting elements (chart of accounts) to enable the auditor to identify the nature of the cost, and to be able to distinguish costs that are wholly relevant to research, mixed, or not relevant to research. In order to ensure completeness of this breakdown, the reconciliation to the accounting records should be provided in order to link the information provided to the annual accounting records of the beneficiary.

What should the beneficiary consider when evaluating the existence of ineligible items in indirect costs?

Final responsibility for the correct calculation of indirect costs, especially for the exclusion of ineligible costs, lies with the beneficiary. This means that the beneficiary must examine each indirect cost component to identify whether it is wholly or partially ineligible.

How can the beneficiary distinguish indirect costs which are related to research from non-research items?

Some cases are clear cut, for example the rent and energy costs of building devoted wholly to the research activity of a beneficiary (research laboratory) can be designated as a research cost that can be 100% allocated across the productive time of the researchers.

Similarly, the trading part of a business (e.g. the manufacturing plant, marketing and sales departments), should be 100% excluded from the indirect cost calculation.

The beneficiary should also describe "mixed-use" cases such as libraries in universities, accounting & personnel departments in trading companies, where the costs will have to be allocated to the different activities using a basis such as the staff to student ratio, or the ratio of research staff to staff working in the business side of the organisation. Beneficiaries should use allocation methods that are easy to compute and understand, and take a conservative approach when allocating "borderline" costs to research. Allocation methods should be described in the Beneficiary's statement.

How is the auditor expected to identify exceptions in the types of costs charged?

The auditor will rely on the detailed breakdown provided by the beneficiary and the detailed description of each cost element. The auditor should identify as exceptions, any items that should normally be charged as direct costs (e.g. direct time of researchers, consumables used on projects, etc.). Identification of "education" or "business" expenses is limited to an analysis of the accounting descriptions e.g. an account clearly designated as relating to (say) sales, or support to teaching staff, should be identified as an exception.

What is meant by "reconciled to the accounts"?

The auditor is not required to perform a sample check of the indirect costs but is required to perform a reconciliation of the data on the basis of the accounting records. The individual cost items should be traceable to the beneficiary's accounting records. If the source of the data is not linked to accounting records but for example to analytical accounting records or management information documents, the beneficiary should provide a reconciliation demonstrating how the figures can be linked to the accounting records.

Procedure 4 as described in this section concerns eligible indirect costs, whereas procedure 5 as described in the next section concerns ineligible overheads/indirect costs. Please note that procedure 5 also deals with allocation methods in the case of shared costs.

*6.5.2 Exclusion of ineligible items (including shared costs) from indirect costs*

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Overheads/ Indirect costs</b>	
<p>5. The accounting system provides for fully traceable elimination of:</p> <ul style="list-style-type: none"> <li>a) identifiable indirect taxes including value added tax,</li> <li>b) duties,</li> <li>c) interest owed,</li> <li>d) provisions for possible future losses or charges,</li> <li>e) exchange losses, cost related to return on capital,</li> <li>f) costs declared or incurred, or reimbursed in respect of another Union/Euratom project,</li> <li>g) debt and debt service charges, excessive or reckless expenditure<sup>3</sup>.</li> </ul> <p>With regard to excessive or reckless expenditure, the Beneficiary confirms that purchases are made according to the principles of best value for money (best price-quality ratio), transparency and equal treatment between The Union/Euratom funded grant agreement and any other agreement or convention that the Beneficiary may have.</p> <p>Where the Beneficiary is allocating shared costs, they should provide a list of allocation methods used (usage records, floor space, activity-based-costing, headcount, etc.) (<i>This procedure does not apply to beneficiaries using a flat rate to claim indirect costs in accordance with Annex II of the Grant Agreement attached to the grant agreement being reviewed.</i>)</p>	<p><b>Procedure:</b></p> <p>The Auditor inspected the accounting records and chart of accounts. The Auditor reviewed the breakdown provided by the Beneficiary in order to check that the ineligible items specified were eliminated; The Auditor also checked (if necessary also via a written declaration/ representation of the Beneficiary) that no implicit interest was included, e.g., by finance leasing or other credit arrangements.</p> <p><b>Finding:</b></p> <p>The Auditor was able to obtain confirmation that no implicit interest was included, and did not find costs which explicitly relate to any of the items specified. For each allocation method used by the Beneficiary, the Auditor reconciled the amount to be allocated to the accounting records, and reconciled the allocation basis to the relevant management accounting information (usage records, floor space, activity-based-costing, headcount, etc.)</p> <p><b>Only the types of excessive and reckless expenditure listed in the Commission's guidance should be considered, the Auditor is not required to exercise professional judgement or provide assurance in this matter.</b></p>

### What is the objective of this procedure?

This procedure does not apply if a flat-rate<sup>30</sup> on eligible direct costs is used for the calculation of overheads/indirect costs.

The three objectives of this procedure are to ensure that:

- all the specific types of costs defined as ineligible in the Grant Agreement have in fact been excluded from the indirect costs,
- the indirect costs do not include any excessive or reckless expenditure,
- a list of allocation methods was provided where the beneficiary is allocating shared costs.

### Which documents should the beneficiary prepare for the auditor?

The same accounting extracts used in the prior procedure should be sufficient to identify the types of costs that have been charged. In certain cases, the auditor will have to rely on a written representation of the beneficiary that certain costs have been eliminated (e.g. on a pro-rata basis).

For value for money, transparency and equal treatment, the beneficiary should provide information demonstrating the **existence** of a procedure to ensure these aspects. The only reportable exception is thus that the beneficiary cannot provide evidence of the existence of a procedure (i.e. contracts are awarded effectively on an ad hoc basis).

For the allocation methods, the beneficiary should provide the appropriate management information. For example, for allocating library costs, the beneficiary is expected to have at its disposal internal management information with staff and student numbers, if this is the basis used. For a company, an analysis of the headcount in the research vs. the trading part of the business could be supplied to support the distribution of the costs of the personnel department.

### What kind of costs do beneficiaries often fail to exclude?

Many beneficiaries fail to remove the irrecoverable VAT elements of indirect costs where they can be identified (for example, making a percentage reduction to certain lines, such as travel or energy consumption, where a known VAT rate is included in the costs).

Servicing of loans, interest, and also the interest element of finance leases are also common examples of ineligible indirect costs which beneficiaries often fail to exclude.

Provisions for possible future losses or charges are ineligible since they do not represent actual costs (already incurred by the beneficiary) but these provisions refer to losses or potential future liabilities: e.g., provisions for litigations, provisions for works (which are not yet undertaken), etc.

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<sup>30</sup> As stipulated in the Grant Agreement

What kinds of indirect taxes are concerned by this procedure?

In most cases, the key indirect tax is VAT. Other national duties should be raised as exceptions if they are identified as not being excluded<sup>31</sup>.

What information on cost allocation is needed for this procedure?

In reviewing the breakdown of expenditure to identify ineligible costs, the beneficiary should also make the auditor aware of any shared costs (i.e. costs which arise from the organisation as a whole) and how the allocation approach ensures that the ineligible costs noted in procedure 5 were eliminated.

Should the auditor analyse whether the cost allocations are reasonable?

No. As this is an agreed upon procedures assignment, the Commission is interested in the existence of the allocation method, but reserves the right to independently assess whether the method is a fair allocation of costs to FP7 project work.

### 6.5.3 Use of estimates in the simplified indirect cost calculation

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Overheads/ Indirect costs</b>	
<p>6. If the organisation is using a simplified indirect cost calculation (either due to the lack of analytical accounting or use of a form of cash-based accounting) all estimates are clearly described and are based on factual criteria which can be objectively confirmed.</p> <p>The Beneficiary must provide a list of cost allocations which are not based on underlying accounting information.</p> <p>In general costs which cannot be identified and allocated using a traceable source of information should not be included in the indirect cost calculation.</p> <p><i>(This procedure does not apply to beneficiaries using a flat rate to claim indirect costs in accordance with Annex II of the Grant Agreement attached to the grant agreement being reviewed.)</i></p>	<p><b>Procedure:</b> The Auditor was able to trace all cost allocation to underlying accounting and management information.</p> <p><b>Finding:</b> Percentage estimates were traced to the supporting factual criteria used by the Beneficiary and were found to be in agreement.</p>

In the left-hand column, the second sentence "*The Beneficiary must provide a list of costs allocations which are not based on underlying accounting information*" means that the

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<sup>31</sup> For instance IRAP in Italy or IGIC in Canary Islands are considered ineligible indirect taxes, further information on taxes are available under the following link  
[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges_en.pdf)

beneficiary may use other sources of information than the accounting information to allocate costs such as floor space, number of staff, etc.

What is the objective of this procedure?

When performing **simplified calculations of indirect costs**, the beneficiary may not have an analytical accounting system which can separate costs of different types as described in the prior procedures. Effectively, it will not be possible to identify or separate with precision certain research related indirect costs from those that are related to other activities such as education. However beneficiaries should be in a position to justify and reconcile the results with the accounting records and be able to demonstrate in case of an audit that the indirect costs are fairly allocated to the research activity/projects.

Which documents should the beneficiary prepare for the auditor?

As above, the beneficiary should provide the appropriate management information. In the case of the simplified method, this can be expected to be based on information from a variety of sources<sup>32</sup>.

What is meant by 'underlying management information'?

Beneficiaries using the simplified method should use the best information available, but which may not be very detailed. For example, the only data the beneficiary may have in order to allocate power consumption is the floor space of the relevant buildings, even though power consumption may in reality be concentrated in certain locations (e.g. the computer research centre). In the absence of real data on consumption, the beneficiary should choose a conservative but objective measure (floor space can be verified by reference to the relevant management information).

What kind of allocation method should give rise to an exception?

Taking the example of the computer centre above, if the beneficiary allocated (say) 30% of its power consumption without having any factual basis, this should be raised as an exception by the auditor. For the Commission the concept of the simplified method does not extend to estimates which do not have a verifiable basis. Thus if the beneficiary cannot demonstrate to the auditor how the 30% was calculated, it should be raised as an exception.

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<sup>32</sup> The source of information will depend on the cost-driver used to distribute the shared costs among the different activities. The Auditor will be interested in any document supporting the correctness of the estimated allocation.

## 6.5.4 Allocation of indirect costs to the project<sup>33</sup>

Statement to be made by Beneficiary	Procedure to be carried out by the Auditor & factual findings
<b>Overheads/ Indirect costs</b>	
<p>7. Allocation of indirect costs to the project is via</p> <ul style="list-style-type: none"> <li>- a percentage of personnel costs;</li> <li>- a fixed personnel hourly rate;</li> <li>- another cost driver to be specified by the Beneficiary</li> </ul> <p><i>(This procedure does not apply to beneficiaries using a flat rate to claim indirect costs in accordance with Annex II of the Grant Agreement attached to the grant agreement being reviewed.)</i></p>	<p><b>Procedure:</b> The Auditor checked that the allocation of indirect costs to the project corresponds with the methodology specified by the Beneficiary;</p> <p><b>Finding:</b> The allocation of indirect costs to the project corresponds with the methodology specified by the Beneficiary; Where percentages are used the Auditor found that, the <b>'chargeable' personnel costs</b> (defined above) multiplied by the overhead percentage does not exceed the total <b>indirect costs to be allocated</b> defined above; Where a fixed hourly rate is used, the productive hours figures used to distribute indirect costs and personnel were found to be the same. Where another cost driver not based on personnel is used, the Auditor found that the result of its application does not exceed the total amount of indirect costs to be allocated.</p>

### What is the objective of this procedure?

The Commission wants to ensure that the manner in which the beneficiary claims its indirect costs does not permit the beneficiary to 'over-recover' its indirect costs (i.e., charge to various projects more than 100% of the relevant indirect costs).

### Which documents should the beneficiary prepare for the auditor?

The period in question will be the period of the "pro forma" Financial Statement or actual Financial Statement (Form C) or the most recent financial year to calculate indirect costs if this is what has been used.

The beneficiary should provide the maximum chargeable hours (if the indirect costs are claimed on a fixed hourly rate) or the maximum chargeable personnel costs (if the indirect costs are charged on a percentage basis).

### What calculation is the auditor expected to perform?

#### *a) For the percentage of personnel costs:*

Take the sum which can be charged (e.g. total chargeable costs of the research staff of the beneficiary) and multiply this by the overhead percentage. Compare this to the research-related indirect costs in the accounting records. If the number is less than or the same in the accounting records, then no exception should be reported. If the number is

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<sup>33</sup> This procedure is not applicable in the case of a flat-rate stipulated in the Grant Agreement. This procedure is applicable in the cases of analytical accounting system and of the simplified method as described in further detail in Part III (Glossary of these guidance notes).

greater than the number in the accounting records, then it appears possible that over-recovery could take place. An exception should be raised.

*b) For the fixed personnel hourly rate:*

Take the sum of the hours which can be charged (e.g. number of researchers multiplied by average productive hours) and multiply this by the hourly overhead rate. Compare this to the research-related indirect costs in the accounting records. If the number is less than or the same in the accounting records, then no exception should be reported. If the number is greater than the number in the accounting records, then it appears possible that over-recovery could take place. An exception should be raised.

c) Where the cost driver differs from a percentage of personnel costs or a fixed personnel hourly rate, the auditor found that the result of its application does not exceed the total amount of indirect costs to be allocated.

## 6.6 Specific provisions for Marie Curie grants

A new Form E has been developed for use in the Marie Curie grants. However, the procedures are identical to the procedures in the Form E of the Standard Model Grant Agreement and the current Guide can be used for information.

## 6.7 Specific provisions for ERC grants

A new Form B (Certificate on the Methodology) has been developed for the ERC grants. However, the procedures are identical to the procedures in the Form E of the Standard Model Grant Agreement and the current Guide can be used for information. Form A does not foresee procedures for indirect costs under the ERC grants.

**PART II: CERTIFICATES ON THE FINANCIAL  
STATEMENTS**



## 1. THE CHANGE IN APPROACH FOR CERTIFYING COSTS CLAIMED

In order to clarify the Commission's objectives and requirements regarding certification of cost claims, in FP7 the Commission requests independent auditors to perform "agreed-upon-procedures" engagements as opposed to assurance engagements as required in previous Framework Programmes.

From the perspective of beneficiaries, this change in the nature of the report provided by the auditor does not represent a radical departure in the process of cost statement preparation. As before, the beneficiary is responsible for providing all the underlying documentation that the auditor needs in order to complete its report, including payroll and accounting information, invoices, etc.

The main change is that the auditor's role is limited to reporting only factual findings as opposed to forming an independent opinion on the eligibility of costs. Part of this change involves the fact that the Commission specifies in detail the procedures to be undertaken, and the auditor reports the factual findings observed as a result of performing those procedures, including exceptions<sup>34</sup> as a basis for the Commission to conclude on the eligibility of the claims.

This process seeks to provide the Commission with a more consistent input from auditors and gives greater possibility of identifying irregularities via the exception reporting. The Commission has specified the procedures in detail thereby making the requirements for documentation and record-keeping more transparent and clear to the beneficiaries.

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<sup>34</sup> Refer to Part III, Glossary of the present guidance notes for a definition of Exceptions.

## 2. KEY CHANGES REGARDING CERTIFICATES ON THE FINANCIAL STATEMENTS<sup>35</sup>

CHANGE	RATIONALE
Compulsory Terms of Reference between beneficiary and auditor	In order to ensure comparability between factual findings reported by different auditors, and consistency in the quality of work to be carried out, the Commission considers that auditors should be engaged on the basis of the same minimum terms and requirements.
Compulsory reporting format	Due to difficulties in FP6 with guaranteeing the same level of detail and completeness in the reporting by auditors, the Commission requires all findings to be presented in the same way, to ensure the Commission has sufficient information to draw conclusions based on the report.
Detailed requirements of type and depth of verification	In an assurance engagement, auditors have considerable discretion as to the nature of the verification procedures they undertake in order to arrive at an opinion. In the interests of consistency and comparability, the Commission has set specific requirements regarding what is to be checked and on areas such as the sample size. The auditors are not permitted to reduce the checks below those specified by the Commission.
Reporting of factual findings	In accordance with ISRS 4400, the auditor is required to describe the procedures carried out. To the extent that the auditor is not able to carry out the required procedures, e.g. because supporting evidence for a cost item is not available, the auditor will include a description of such scope limitation in the report. For procedures that the auditor is able to perform, the auditor will report whether or not the

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<sup>35</sup> Financial Statement is defined in Part III, Glossary of the present guidance notes. Financial Statements refer to different Financial Statement(s) covering different periods.

	<p>findings observed as a result of doing so are consistent with the standard findings described in Annex VII. Both of them will be reported under the heading "Exceptions" in his report.</p>
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### 3. SCOPE AND CONTENT OF CERTIFICATES ON THE FINANCIAL STATEMENTS

The beneficiary is required to submit to the European Commission, in addition to the Form C<sup>36</sup>, a Certificate on the Financial Statements which includes notably an independent report of factual findings produced by an auditor in support of the payment requested by the beneficiary under Article II.4 of the Grant Agreement. Please refer to section 5 for a detailed description of the three components of the Certificate on the Financial Statements.

Certificates on the Financial Statements shall state that the costs claimed and the receipts declared during the period for which they are provided, as well as the declaration of the interest yielded by the pre-financing generated up to 31 December 2012 meet the conditions required by the Grant Agreement. The Terms of Reference for the Certificate on the Financial Statements state that no conflict of interest<sup>37</sup> exists between the auditor and the beneficiary for establishing the certificate.

The auditor undertakes this engagement in accordance with the terms of references of Form D – Annex VII (hereinafter "ToR") and:

- in accordance with the International Standard on Related Services ('ISRS') 4400 Engagements to perform Agreed-upon Procedures regarding Financial Information as promulgated by the IFAC;
- in compliance with the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants (IESBA) of IFAC. Although ISRS 4400 provides that independence is not a requirement for agreed-upon procedures engagements, the European Commission requires that the Auditor also complies with the independence requirements of the Code of Ethics for Professional Accountants.

The auditor performs the procedures specified in 1.9 of the ToR ('Scope of Work – Compulsory Report Format and Procedures to be performed') and uses the evidence obtained from these procedures as the basis for the Report of factual findings.

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<sup>36</sup> In order to ensure the coherence between the Form C and the CFS, it is recommended that the certifying auditor stamps/paraphs the Form C which was the basis for the establishment of the CFS.

<sup>37</sup> A conflict of interest arises when the auditor's objectivity to establish the certificate is compromised in fact or in appearance when the auditor for instance:

- was involved in the preparation of the Financial Statements (Forms C);
- stands to benefit directly should the certificate be accepted;
- has a close relationship with any person representing the beneficiary;
- is a director, trustee or partner of the beneficiary;
- is in any other situation that compromises his or her independence or ability to establish the certificate impartially.

## 4. SUBMISSION OF CERTIFICATES ON THE FINANCIAL STATEMENTS

Unlike the Certificate on the Methodology (CoM), the Certificate on the Financial Statements is not submitted to the Commission via a mailbox but has to be submitted directly to the responsible person of the Commission together with the related beneficiary's Form C and Management Report (periodic or final).

	Required	Not required
Submission of the certificate	<p>A Certificate on the Financial Statements (CFS) is mandatory for every claim (interim or final) in the form of reimbursement of costs whenever the amount of the EU contribution is equal or superior to EUR 375,000 when cumulated with all previous interim payments (excluding pre-financing) for which a CFS has not been submitted<sup>38</sup>. The CFS must be forwarded in the form of a detailed description verified as factual by its external auditor (Form D – Annex VII).</p> <p><i>Specific case of projects with a duration of 2 years or less:</i></p> <p>When the amount of the EU contribution claimed by the beneficiary is equal or superior to EUR 375,000 (cumulated with all previous payments), <b>only one CFS shall be submitted at the time of the final payment.</b></p>	<p>1. A CFS is not required :</p> <ul style="list-style-type: none"> <li>- for Financial Statements where the amount of EU contribution is lower than EUR 375,000 when cumulated with all previous payments for which a CFS has not been submitted.</li> <li>- for indirect actions entirely reimbursed by means of lump sums or flat rates.</li> <li>- for beneficiaries with costs incurred in relation to the project but without EU contribution (in this case this circumstance will be mentioned in special clause 9 to be included in Article 7 of the Grant Agreement).</li> </ul> <p>2. Intermediate CFS for claims on interim payments are not required when a CoM has been approved by the Commission for the beneficiary</p>

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<sup>38</sup> Once a CFS is submitted, the threshold of EUR 375,000 applies again for subsequent EU contributions but the counting starts from the amount not yet covered by the CFS. The threshold is established on the basis of the EU contribution. Examples for the submission of Certificates on the Financial Statements can be found in the Guide to Financial Issues (Part A, Section 2).  
[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide_en.pdf)

### **Threshold of EUR 375,000 and third party covered by special clause n°10<sup>39</sup>**

In the case of a third party included in the article 7 of the Grant Agreement by means of Special Clause 10, each third party fills in its costs in an individual Form C and, where necessary, shall provide its individual certificate on financial statements and/ or on the methodology independently from those of the beneficiary. The beneficiary will submit both forms and a summary report integrating both the costs of the beneficiary and those of the third party(ies).

The threshold of EUR 375,000 for the submission of a certificate on the financial statements applies to each third party independently of the EU contribution of the beneficiary. The submission procedure and rules are the same as for beneficiaries.

### **Submission of Certificate on the Financial Statements before the threshold of EUR 375,000 is reached**

As explained above, a CFS is not mandatory if the EUR 375,000 threshold is not reached. However, if the beneficiary submits a CFS before this EUR 375,000 threshold is reached<sup>40</sup>, the counter will be re-set for the amount not covered by the CFS.<sup>41</sup>

### **Acceptance/rejection of the Certificate on the Financial Statements by the EC**

The agreed-upon-procedures as defined by the European Commission are performed to assist the European Commission in evaluating that the costs claimed by the beneficiary in the accompanying Financial Statements have been claimed in accordance with the provisions of the Grant Agreement. The Authorising Officer of the Commission will use the information included in the Certificate on the Financial Statements (detailed report on factual findings as well as exceptions such as inability to reconcile key information, unavailability of data which prevented the Auditor from carrying out the procedures, etc.) to decide on the amounts to be reimbursed.

### **Reimbursement of the costs of the Certificates on the Financial Statements**

The cost of the certificate on the Financial Statements is an eligible cost in the Grant Agreement for which the certificate is submitted (Art. II.14). Nevertheless, if the beneficiary decides to submit a certificate voluntarily or if the CFS is not required by the Grant Agreement when the EU/Euratom contribution is less than EUR 375,000, the costs of the CFS will not be eligible as long as the cumulative EU contribution claimed does not reach the EUR 375,000 threshold.

This means that the costs of a CFS sent before the threshold is reached may become eligible if such threshold is reached in one of the subsequent periods<sup>42</sup>. Consequently

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<sup>39</sup> For clause n°10, refer to the list of special clauses for FP7 Model Grant Agreement published on Participant Portal.

<sup>40</sup> The CFS must cover at least one full reporting period.

<sup>41</sup> When a beneficiary submits a CFS covering all the reporting periods, the counter is re-set to zero.

<sup>42</sup> Consequently, if a CFS is not required by the Grant Agreement (i.e. when the total EU contribution is less than EUR 375,000), the costs of the CFS remain not eligible since these costs are not considered necessary for the project (even if the Commission proceeds with the analysis of this CFS).

they shall be claimed by the beneficiary only once the EUR 375,000 threshold is reached.<sup>43</sup>

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<sup>43</sup> It should be noted that the EC may reimburse costs of more than one CFS submitted by the beneficiary with respect to one Grant Agreement. However, for the subsequently filed CFS, this will be possible only if and when the total EU/Euratom contribution not covered by previous CFS reaches EUR 375,000.

## 5. FORM OF CERTIFICATES ON THE FINANCIAL STATEMENTS - ANNEX VII

The use by the external auditor or competent public officer of the reporting format attached as part of Annex VII (Form D) of the model Grant Agreement is compulsory.

The Certificate on the Financial Statements has to be transmitted by the beneficiary to the Commission with the Financial Statements (Forms C). The Certificate on the Financial Statements is composed of three separate documents to be found in Annex VII (Form D) of the Model Grant Agreement:

- A list of the minimum terms of reference (sections 1.1 to 1.8) required by the Commission to be included in the engagement letter between the beneficiary and the auditor. **The engagement letter must be dated and signed by both parties.**
- The model auditor's Report of Factual Findings (section 1.9) to be issued **on the auditor's letterhead and dated, stamped and signed by the auditor** (or the competent public officer).
- A detailed description (table of Annex VII - Form D) including the procedures to be performed by the auditor and the findings expected to result there from. **This table has to be dated, stamped and signed by the auditor (or the competent public officer) on completion of its work.**

Certificates on the financial statements regarding grant agreements signed as from 01.01.2013 will have to be hand-signed by an authorised person of the auditing entity on paper, scanned and subsequently sent electronically since the possibility to submit them in paper forms has been explicitly abolished in the FP7 Grant Agreement (see Art. 8 and II.4).

For Grant Agreements signed before 31.12.2012, the consortia may apply the new electronic-only transmission system, provided they introduce a request for an amendment via the coordinator.

Regarding the language of Certificate on the Financial Statements, Article 4 of the FP7 model Grant Agreement states that “Any report and deliverable, when appropriate, required by this Grant Agreement shall be in [*insert language*]”. Therefore, the report of factual findings on the Financial Statements should be written in the language indicated in Article 4 of the Grant Agreement.



## 6. PROCEDURES FOR CERTIFICATE ON THE FINANCIAL STATEMENTS ACCORDING TO ANNEX VII - FORM D

### 6.1 Procedures to be carried out by the auditor regarding Form D

The procedures listed on the left hand side of Form D are to be carried out **unaltered** by the auditor. The Commission has designed these procedures in order to obtain standardised and comparable reports from all auditors, who are expected to carry out the procedures without adaptation for the particular circumstances of the beneficiary.

In particular the minimal sample sizes should always be respected, and all procedures should be carried out in full<sup>44</sup>.

### 6.2 When can the auditor change the model answer and when should he report an exception?

Where the auditor's factual findings are not consistent with the "Standard factual finding" given on the right hand side of the Form D, then an exception should be noted. For each standard finding, non-exhaustive examples where the Commission expects exceptions to be noted is indicated in bold under the corresponding factual findings. In general, if the auditor is not able to establish whether the information provided by the beneficiary matches the standard finding defined by the Commission, this should be reported as an exception. If the auditor comes across issues that are not explicitly described in Form D but could affect the reliability of the Financial Statement, these issues should nevertheless be reported and duly described under point 1.9 "Exceptions".

### 6.3 Will all exceptions result in a rejection of costs by the Commission?

The Commission will consider each exception in the context of the report as a whole and other evidence at its disposal. It will therefore make eligibility decisions on a case-by-case basis using the evidence provided. The more detail the auditor provides regarding exceptions, the easier it will be to assess the situation and come to a reasoned decision on the claim under consideration. The auditor should report the findings as fully as possible to facilitate this process.

### 6.4 Procedures for Certificates on the Financial Statements according to Annex VII – Form D

When a Certificate on the Methodology (Form E) has been approved by the Commission, the auditor will only have to focus on checking compliance with the certified

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<sup>44</sup> Refer to Part III, Glossary for the definition of exceptions to be reported by the auditor

methodology and systems. In this context, some aspects of the procedures included in the Form D will not have to be performed by the auditor.

**For beneficiaries having a Certificate on the Methodology for average personnel costs (CoMAv) only**, the auditor will have to perform all procedures foreseen in the Form D except for procedure 1 where the auditor will be requested to check only the part related to productive hours.

**For beneficiaries having a Certificate on the Methodology covering average personnel costs and indirect costs (CoM)**, the auditor will have to perform all procedures foreseen in the Form D except for procedure 1 where the auditor will be requested to check only the part related to productive hours and for procedure 10 where the auditor will not be requested to recalculate the indirect costs rate.

The table below indicates the procedures to be performed by auditors in different situations.

### Procedures to be performed by the auditor for establishing the CFS

Category of costs	Calculation method used by the beneficiary			
		With approved CoM <sup>45</sup>	With approved CoMAv <sup>46</sup>	Without Certificate
<b>Personnel</b>	Individual costs (per employee <sup>47</sup> )	1, 2, 3	Not applicable	1, 2, 3
	Average rates	1 <sup>48</sup> , 2, 3, 4	1 <sup>49</sup> , 2, 3, 4	1, 2, 3, 4
<b>Subcontracting</b>	All cases	5, 6		
<b>Other Direct Costs</b>	All cases	7, 8, 9		
<b>Indirect Costs</b>	Actual Indirect Costs	10 <sup>50</sup>	10	10

<sup>45</sup> Certificate on the Methodology (Form E).

<sup>46</sup> Certificate on Average Personnel Costs (Form E only covering average personnel costs).

<sup>47</sup> Employee means researcher or research-related person or person with certain coordinating tasks (when there is a project coordinator).

<sup>48</sup> The auditor is requested to check only the part related to productive hours since the auditor performs the procedure n°4 related to average personnel costs.

<sup>49</sup> The auditor is requested to check only the part related to productive hours since the auditor performs the procedure n°4 related to average personnel costs.

<sup>50</sup> The auditor is not requested to recalculate the indirect costs rate.

	Simplified Method	10 <sup>51</sup> , 11	10, 11	10, 11
	Flat-rate	None	None	None
<b>Exchange rates, receipts and interest yielded</b>	All cases	12, 13, 14		

6.4.1 Personnel costs

Procedures	Standard factual findings and basis for exception reporting
<b>Personnel costs</b>	
<p>1. Recalculate hourly personnel and overhead rates for personnel (full coverage if less than 20 employees, otherwise a sample of minimum 20, or 20% of employees, whichever is the greater), indicate the number of productive hours used and hourly rates.</p> <p>Where sampling is used, selection should be random with a view to producing a representative sample.</p> <p><b>'Productive hours'</b> represent the (average) number of hours made available by the employee in a year after the deduction of holiday, sick leave and other entitlements. The auditor obtained the calculation of the productive hours after inspecting all necessary records, national legislation, labour agreements, contracts, any other relevant documentation. The calculation should be based on the period(s) corresponding to the Financial Statement(s) or on the last closed financial year (whichever is used by the beneficiary).</p>	<p>The auditor sampled _____ employees out of the total of _____ employees.</p> <p>For each employee in the sample of ____, the Auditor obtained the personnel costs (salary and employer's costs) from the payroll system together with the productive hours from the time records of each employee.</p> <p>For each employee selected, the Auditor recomputed the hourly rate by dividing the actual personnel costs by the actual productive hours, which was then compared to the hourly rate charged by the Beneficiary.</p> <p>No exceptions were noted.</p> <p>The average number of productive hours for the employees selected was _____. The productive hours calculation corresponds to the usual accounting practice of the beneficiary.</p> <p><b>If the productive hours or costs of personnel cannot be identified, they should be listed (together with the amounts) as exceptions in the main report.</b></p> <p><b>If the productive hours calculation does not correspond to the usual accounting practice of the beneficiary, this should be listed as an exception in the main report.</b></p>

What is the objective of this procedure?

The objective of this check is to verify that the hourly rates being charged have been correctly calculated from the actual underlying cost information for the period in question, namely the costs to the employer (salary / wages including benefits and other

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<sup>51</sup> The auditor is not requested to recalculate the indirect costs rate.

employment costs), divided by the productive hours<sup>52</sup> with a reconciliation of the payroll information for the selected employees to the accounting records and payments.

A complementary objective is to specifically check whether the calculation of productive hours (either individual hours or standard hours) has been consistent with the usual accounting practice of beneficiary.

Which documents should the beneficiary prepare for the auditor?

The actual payroll information for the period in question (base salary, benefits of all kinds, pension contributions, employers' payroll taxes, etc.) and productive hours figures (see Glossary in Part III of the present guidance notes for a description of productive hours) used to calculate the hourly rates. The beneficiary should also provide a reconciliation/calculation showing how the hourly rates were calculated from the payroll information.

The auditor may ask the beneficiary for additional documentation including relevant legislation on productive time, labour agreements to justify working hours, relevant employment contracts defining the working arrangements, as well as any other proof that the calculation of productive hours is in accordance with the usual accounting practice of the beneficiary.

The documents provided by the beneficiary should give the auditor both full understanding of the methodology used by the beneficiary and evidence of the proper application of this methodology. Thus, the penultimate sentence of the right-hand column should be read as follows "if the productive hours or costs of personnel cannot be identified *or justified by the beneficiary*, they should be listed (together with the amounts) as exceptions in the main report".

What if the beneficiary already has a certificate under Form E?

Where there is a Form E approved by the Commission **on average personnel costs**, the individual calculations and re-computations foreseen under procedure 1 are not applicable since the auditor is just expected to check the general compliance with the methodology. The auditor is therefore requested to check only the part related to productive hours in this procedure.

Where individual actual costs have been used and the methodology certified approved by the Commission, the entire procedure has to be performed by the auditor (including recalculations).

What employment costs are not considered eligible or should be regarded as exceptions?

Generally all employment costs which are part of the normal remuneration policy of the beneficiary are accepted. The costs which have been charged and which relate specifically to involvement in European projects, and are not part of these normal remuneration and/or accounting principles should be noted as exceptions.

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<sup>52</sup> Actual productive hours (or standard productive hours if it corresponds to the usual practice of the beneficiary)

How should sampling be carried out?

The size of the sample proposed in this procedure is based on the population of researchers or research-related persons involved in the project. In this context, the size of the sample has to respect the following:

- if the population of researchers or research-related persons involved in the project is less than 20 employees, full coverage,
- if the population of researchers or research-related persons involved in the project is equal or greater than 20 employees,
  - a minimum of 20 employees,
  - or 20 % of the employees (whichever is the greater).

If the sample drawn in line with the guidelines above would not be representative for the audited organisation, then this sample should be expanded to also include research personnel not working on the EU project.

What procedure does the auditor perform in the case of SME owners/natural persons receiving a flat-rate financing for personnel costs **without an approved CoMAv?**

The detailed procedure has been added in this respect in Form D, point 4c. It is based on the Commission Decision C(2011)174 of 24.01.2011. Accordingly, it refers to the calculation of flat-rate financing for SME owners / natural persons who do not receive a salary by reference to the allowances available under the 'People' work programme and to the pre-defined amount of standard productive hours.

Procedures	Standard factual findings and basis for exception reporting
<b>Personnel costs</b>	
2. For the same selection examine and describe time recording of employees (paper/ computer, daily/weekly/monthly, signed, authorised).	Employees record their time on a daily/ weekly/ monthly basis using a paper/computer-based system. The time-records selected were authorised by the project manager or other superior.  <b>If no time records are available which fit the above description, this should be listed as an exception in the main report.</b>

What is the objective of this procedure?

This procedure will provide to the Commission the information it needs to assess whether the recording of project time is in line with the requirements of the Grant Agreement. Normally, time recording should be carried out regularly and authorised by the project manager to ensure that the time worked on the project can be traced and charged correctly. For the employees selected, the hours charged to the project should have been accurately recorded in the time recording system. Any discrepancies between the amount charged to the project and the amount in the time sheets (or if time sheets are absent) should be recorded as an exception.

Which documents should the beneficiary prepare for the auditor?

The beneficiary should provide a description of the time-recording system and, for the employees selected for testing, make available all the time sheets or provide full access to the computer system which records the time of the employees. The auditor should be able to trace the time charged for the sample selected to the time records of each individual employee.

Procedures	Standard factual findings and basis for exception reporting
<b>Personnel costs</b>	
<p>3. Employment status and employment conditions of personnel. The Auditor should obtain the employment contracts of the employees selected and compare with the standard employment contract used by the Beneficiary. Differences which are not foreseen by the Grant Agreement should be noted as exceptions.</p>	<p>For the employees selected, the Auditor inspected their employment contracts and found that they were:</p> <ul style="list-style-type: none"> <li>– directly hired by the Beneficiary in accordance with its national legislation,</li> <li>– under the sole technical supervision and responsibility of the latter, and</li> <li>– remunerated in accordance with the normal practices of the Beneficiary.</li> </ul> <p><b>Personnel who do not meet all three conditions should be listed (together with the amounts) as exceptions in the main report.</b></p>

What is the objective of this procedure?

The Commission seeks to ensure that personnel costs do in fact relate to employees of the beneficiary carrying out the research, and to identify cases where this component may have been effectively "outsourced" to a different entity, where this has not been foreseen in the Grant Agreement with the Commission. The Commission also seeks to ensure that no special employment conditions are applied to employees working in the project which are not normally applied within normal company practices.

Which documents should the beneficiary prepare for the auditor?

Specific employment contracts for the researchers in question, as well as standard employment contracts in use for personnel who perform a variety of work for the beneficiary (i.e. are not exclusively devoted to EU research work).

What kind of information would give rise to exceptions?

Article 15 of Annex II of the model Grant Agreement foresees that with regard to personnel costs, the persons directly carrying out work under the project must:

- be directly hired by the beneficiary in accordance with its national legislation,
- work under the sole technical supervision and responsibility of the latter, and
- be remunerated in accordance with the normal practices of the beneficiaries.

Any difference to the above principles should be highlighted by the auditor as an exception. Please find below some non-exhaustive examples.

**Directly hired:** Exceptions should be raised if there are indications in the contract that the employee is hired by a different legal entity, including a legal entity within the same group (e.g. if the beneficiary is XYZ Research Limited and the contract is with XYZ

holdings or XYZ registered in a different country). Another example giving rise to an exception is if the employee's services are being charged via a service company or other consulting type arrangement.

**Sole technical supervision:** An exception should be raised if it is stipulated in the contract that its objective and participation focuses on a specific deliverable or piece of work rather than on the employee's services. This includes indications that the work is not been carried out at the beneficiary's premises<sup>53</sup> but has more of the characteristics of an external or subcontract. Again, the use of a service company indicates that the beneficiary is not directly supervising the technical work and should give rise to an exception.

**Remunerated in accordance with the normal practices of the beneficiary:** Typical examples which should give rise to an exception are being remunerated in a 'lump sum' instead of via a salary arrangement, or any other form of payment/ charging (such as travel expenses) which does not take place within the normal accounting practice of the beneficiary.

Procedures	Standard factual findings and basis for exception reporting
<b>Personnel costs</b>	
<p>4. Use of average personnel costs</p> <p><b>Apply 4a, 4b or 4c according to the existence or not of an approved Methodology Certificate (CoMAv or CoM if it concerns average personnel costs)_</b></p> <p><b>4a. With an approved Methodology Certificate including average personnel costs:</b></p>	<p>4a.</p> <p>The Auditor found that the personnel costs charged to the financial statement:</p> <ul style="list-style-type: none"> <li>• are calculated using average costs in accordance with the methodology as specified in the Report of findings on the methodology dated _____.</li> <li>• have been calculated using amounts derived from the relevant period which can be reconciled to the accounting records of the relevant period.</li> <li>• Where categories are used, the auditor verified that the researcher (or research-related person) had been correctly classified.</li> <li>• The Auditor obtained confirmation from the Beneficiary</li> </ul>

<sup>53</sup> Tele-working may be accepted if there is a system that allows the identification of the productive hours worked for the project.

<p><b>4b. Without an approved Methodology Certificate (not applicable to SME owners and natural persons not receiving a salary):</b></p> <ul style="list-style-type: none"> <li>• The auditor reviewed all relevant manuals and/or internal guidance describing the methodology used to calculate average personnel costs;</li> <li>• The auditor obtained a list of all average personnel rates calculated by the beneficiary in accordance with the methodology used;</li> <li>• The auditor verified that the calculation of the average personnel costs excludes ineligible items as defined in Art.II.14.3, Annex II to GRANT AGREEMENT or any costs claimed under other cost categories</li> <li>• The auditor obtained a list of all relevant employees (working on EU projects + not working on EU projects) based on which the average personnel rate(s) are calculated;</li> <li>• The auditor reviewed the allocation of employees to the relevant group and verified the correctness of the Full Time Equivalent (FTE).</li> <li>• The auditor performed a numerical reconciliation between the total amount of personnel costs taken into consideration for the calculation of the average personnel rate and the total amount of personnel</li> </ul>	<p>that the rates used were not budgeted or estimated amounts.</p> <p><b>If amounts cannot be reconciled, or if estimates or budgeted amounts were used, this should be reported as an exception in the main report.</b></p> <p><b>4b.</b></p> <p>The auditor found:</p> <ul style="list-style-type: none"> <li>• no discrepancies between the method described in the relevant documents and the method used by the beneficiary;</li> <li>• The methodology used to calculate the average personnel hourly rate(s) represent(s) the usual cost accounting practice of the organisation;</li> <li>• no differences arose from the numerical reconciliation</li> <li>• The Auditor confirms that the rates used for the calculation of the average personnel costs were not based on budgeted or estimated amounts.</li> </ul> <p><b>If amounts cannot be reconciled, or if estimates or budgeted amounts were used, this should be reported as an exception in the main report.</b></p> <p><b>If the usual accounting practice differs from the one described, this should be reported as an exception in the main report</b></p>
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<p>costs recorded in the statutory accounts.</p> <ul style="list-style-type: none"> <li>• The auditor verified on a sample basis that the appropriate average hourly rate was used for the personnel costs claimed on the audited project.</li> </ul> <p><b>4c. Without an approved Methodology Certificate – applicable only for SME owners and natural persons not receiving a salary:</b></p> <ul style="list-style-type: none"> <li>• The auditor reviewed payroll and accounting records, contracts and other relevant legal documents in order to verify that the SME owners and the natural persons concerned (i.e. those who are beneficiaries in a Grant Agreement) do not receive any salary.</li> <li>• The auditor obtained documents (such as employment records, CVs, diplomas and other relevant documents) proving professional experience of the persons concerned and supporting determination of appropriate research category in line with 'People' Work Programme.</li> <li>• The auditor verified that the annual living allowance corresponds to the reference year of the publication of the call under which the project was selected for funding and that the beneficiary applied the appropriate country coefficient correction as published in the 'People' work programme of the year of publication of the call.</li> <li>• The Auditor recomputed the hourly rate by dividing the applicable</li> </ul>	<p><b>4c.</b></p> <ul style="list-style-type: none"> <li>• SME owners and natural persons charging personnel costs based on a flat rate, do not receive salary.</li> </ul> <p><b>If they receive any salary, it should be listed as an exception in the main report.</b></p> <ul style="list-style-type: none"> <li>• Time spent on projects was duly recorded by the persons whose personal work costs are charged on the basis of a flat rate. These time-records have been verified by a superior or another person involved in the project. In the absence of any superior or other person working closely with such persons, the Auditor confirms that documentation is available to ascertain the reliability of the time records.</li> </ul> <p><b>If no time records are available, this should be listed as an exception in the main report.</b></p> <ul style="list-style-type: none"> <li>• The hourly rates applicable to all SME owners and natural persons who do not receiving a salary are correctly calculated.</li> <li>• The total numbers of hours claimed for the European Union project in a year is in line with their time-sheets but is not higher than the standard number of productive hours per SME owner or natural person (1575).</li> </ul> <p><b>If the calculation is not correct, this should be listed as an exception in the main report.</b></p>
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<p>living allowance corresponding to the appropriate research category by the standard number of productive hours (1575) and by multiplying it by the appropriate country correction coefficient.</p> <ul style="list-style-type: none"> <li>• The auditor reviewed the time-sheets completed by the persons whose personal work costs were claimed on a flat rate basis.</li> </ul>	
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Why are there 3 procedures?

The Commission's decision on simplification and the introduction of the new acceptability criteria for average personnel costs makes it possible to claim average personnel costs without a need to obtain a prior methodology certificate covering average costs methodology.

Furthermore, the decision addresses the issue of SME owners and natural persons not receiving a salary. Previously, they also had to obtain a methodology certificate in order to qualify for receiving EU contribution for their personal involvement in the project. Under the current legal provisions, SME owners and natural persons not receiving a salary who are beneficiaries in a Grant Agreement are entitled to charge their personnel cost to the project on the basis of the flat-rate system adopted by the Commission.

The introduction of these simplification measures required amendments to the existing agreed upon audit procedures. This is because, initially, these procedures addressed only the situation where beneficiaries had an approved methodology covering average personnel costs.

Therefore, in view of the Decision on simplification and the introduction of the new acceptability criteria for average personnel costs, the procedures concerning average personnel costs have been specially tailored to cover three situations:

- a) calculation of average personnel costs based on an approved CoMAv or CoM covering average personnel costs,
- b) calculation of average personnel costs without an approved CoMAv or CoM covering average personnel costs,
- c) calculation of personnel costs for SME owners and natural persons who do not receive a salary.

Procedures a) and b) do not apply if the beneficiary does not use averages for the calculation of personnel costs ("*Average* personnel costs per person divided by *average/standard* productive hours"). If the beneficiary uses averages, procedures a) and b) are exclusive, i.e., the auditor should apply only one of them, depending on

whether the beneficiary has an approved methodology certificate (and applies the certified methodology) or has not obtained a certificate.

Procedure c) will apply only in specific situations and it is possible that it can be applied alongside procedure a) or procedure b).

This may be illustrated by an example of a SME that employs 40 employees and calculates personnel costs on average basis (e.g. per category) without a methodology certificate, where the SME owner does not receive a salary. The auditor should perform procedure b) to check the calculation of average personnel costs for the employees and procedure c) for the SME owner not receiving a salary.

#### Which documents should the beneficiary prepare for the auditor?

Where applicable, the beneficiary should prepare the most up-to-date classification grid, together with the criteria for classification of employees (based on experience, qualifications, salary, department, etc.). The information should be sufficient to unambiguously categorise each of the researchers in the sample, and to verify that the rates used were those applicable for the period to which the claim refers. Thus, it may be necessary to consult the payroll/human resources system in detail, and the beneficiary should be able to extract this information.

#### What is the objective of procedure a)?

The procedure to be performed by the auditor in the left-hand column should be as described below.

The auditor is requested to perform a limited check that the methodology which was already approved is in fact being implemented in accordance with the Form E that was approved by the Commission. Thus, rather than tracing the costs of the individual researchers back to the payroll records of each individual employee, the auditor simply verifies that the researcher was charged using a rate corresponding to the rate for that employee's category. For example, the auditor checks that for a researcher belonging to category III according to the beneficiary's classification system, the rate for the category III was used to charge his/her time.

#### How should the auditor check the reconciliation?

The beneficiary should be able to show via the calculation of average rates, where the data in the calculation was extracted from the accounts, and in doing so demonstrate that the correct relevant period and accounting information has been used.

#### What is the objective of procedure b)?

The auditor is requested to review the beneficiary's average personnel costing methodology in the light of the 4 criteria set forth in the Commission decision C(2011)714 on the simplification introducing the new acceptability criteria for average personnel costs.

As a result of carrying out these procedures, the auditor should fully understand and obtain the details of the personnel cost calculation method(s) used by the beneficiary.

#### *Criteria 1 and 4*

*The average costs methodology shall be the one declared by the beneficiary as its usual cost accounting practice (...)*

*The number of productive hours used to calculate the average hourly rates shall correspond to the usual management practice of the beneficiary provided that it reflects the actual working standards of the beneficiary, in compliance with applicable national legislation, collective labour agreements and contracts and that it is based on auditable data.*

These criteria are addressed in procedure 4b bullet points 1, 2, 4, 5 and 7. Also, the auditor should base his work on the results of procedure 1 concerning calculation of standard productive hours.

The auditor should review the methodology/ies used to calculate the average hourly rates, and obtain reasonable assurance that it/they represent(s) the beneficiary's usual cost accounting practice. The auditor is expected to verify the number of productive hours used for the calculation of the average hourly rate. The auditor should obtain manuals and internal guidance documents describing the methodology used to calculate the average hourly rates to see whether average the hourly rates are based on standard or individual productive hours.

In the case of standard productive hours, the auditor is requested to:

- (1) obtain the description of the underlying calculation method;
- (2) obtain a detailed substantiation of the assumptions leading to the assessment of productive and non-productive time;

In the case of individual (actual) productive hours or average of individual (actual) productive hours the auditor should

- (1) obtain the actual number of productive hours used by the beneficiary for each person in the group (employees working on EU projects + employees not working on EU projects). The actual number of hours must be duly substantiated with appropriate evidence.

### *Criterion 2*

*The methodology shall be based on the actual personnel costs of the beneficiary as registered in its statutory accounts, without estimated or budgeted elements.*

By performing procedure b) bullet point 6, the auditor should verify whether the total amount of personnel costs taken into consideration in the average hourly rate formula(s) corresponds with the total amount of personnel costs recorded in the statutory accounts.

The auditor should verify that the rates used do not include budgeted or estimated amounts. There may be an exception to this finding for periods in which the annual accounts have not been closed and the actual figures are not yet available. Procedures by the beneficiary should be foreseen in these cases to ensure that at the time the actual figures are available the costs are adjusted accordingly. These procedures need to be detailed and confirmed by the auditor.

### *Criterion 3*

*The methodology shall exclude from the average personnel rates any ineligible costs item (...) and any costs claimed under the other costs categories in order to avoid double funding of the same costs.*

The auditor should perform procedure b bullet 3 in order to exclude ineligible items, even if they are a component of a usual cost accounting of the beneficiary. Such costs may include, e.g., special bonuses which are payable exclusively in relation to work on EU projects.

Furthermore, the auditor should review all elements of the calculation of the average personnel rate in order to identify the elements which could be eligible but they can be claimed under other cost categories.

This procedure is particularly important for methodologies based on cost centres or similar. Cost centre personnel rates may often include indirect cost components. The auditor must make sure that such costs are claimed just once. Consequently, if they are built-in into the personnel rates, they cannot be claimed under the 'indirect costs' category.

In the particular case of beneficiaries applying a flat-rate indirect cost method, the personnel cost cannot include any indirect cost elements as these are covered by the flat-rate.

How should the auditor check the reconciliation?

The beneficiary should be able to show via the calculation of average rates, where the data in the calculation was extracted from the accounts, and in doing so demonstrate that the correct relevant period and accounting information has been used.

What is the objective of procedure c)?

Essentially, the auditor is requested to verify two elements: eligibility of SME owners or natural persons to receive the flat-rate financing in accordance with the Commission decision C(2011) 174 and the detailed calculation of this flat-rate financing.

The first element is addressed in procedure c) bullet point 1. The auditor must obtain appropriate evidence that the SME owners / natural persons do not receive a salary (i.e. remuneration for their work). If any payments to the SME owners / natural person are identified (corresponding to personnel or other costs), the auditor should identify the legal basis for the payment and assess whether such a payment can or cannot be treated as a salary.

The remaining procedures concern the detailed calculation of the flat-rate financing and are strictly following the calculation methodology set forth in Article 7 of the Commission decision C(2011) 174.

**6.4.2 Subcontracting**

Procedures	Standard factual findings and basis for exception reporting
<b>Subcontracting</b>	
5. Obtain a written description from	The Auditor compared the description of the 3 <sup>rd</sup> party

the Beneficiary regarding 3 <sup>rd</sup> party resources used and compare with Annex 1 to the Grant Agreement.	resources provided by the Beneficiary to the specification in Annex 1 to the Grant Agreement, and found them to be the same  <b>If the descriptions do not clearly match, this should be reported as an exception in the main report.</b>
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What is the objective of this procedure?

The Commission seeks to ensure that the beneficiaries have honoured the structure of the Grant Agreement as originally agreed. In particular, the Commission normally carefully negotiates to which extent third party resources can be used by the beneficiary to ensure that the grant supports its policy objectives. Any discrepancy from this original agreement is therefore of interest to the Commission, and having the auditor report on this information adds value in identifying possible breaches of the Grant Agreement. The final decision on action to take is up to the Commission, depending on how significant the variations from the original Grant Agreement commitments might be.

Which documents should the beneficiary prepare for the auditor?

The check includes a documented comparison between the 3<sup>rd</sup> party resources foreseen in the Grant Agreement (Annex 1 – Description of Work) and the resources actually contracted between the beneficiary and the 3<sup>rd</sup> party. The beneficiary should therefore provide the contracts signed with 3<sup>rd</sup> parties and is expected to show how these fulfil their commitments under the Grant Agreement. In essence the 3<sup>rd</sup> party contracting should match these commitments in terms of the type and quantity of the products and services, as well as the supplier, where this is specified in the Grant Agreement. In these cases the auditor is not expected to provide an analysis of the services, but to note differences, which can be subsequently analysed by the Commission.

Procedures	Standard factual findings and basis for exception reporting
<b>Subcontracting</b>	
<p>6. Inspect documents and obtain confirmations that subcontracts are awarded according to a procedure including an analysis of best value for money (best price-quality ratio), transparency and equal treatment. Full coverage if less than 20 items, otherwise a sample of minimum 20, or 20% of the items, whichever is the greater.</p>	<p>The Auditor obtained tendering documents for each subcontract entered into and found that the tendering process was followed and that a written analysis of value-for-money had been prepared by the Beneficiary in support of the final choice of subcontractor, or that the contract had been awarded as part of an existing framework contract entered into prior to the beginning of the project.</p> <p><b>If the Auditor is not provided with evidence of either of the above situations, the amount of the subcontract should be listed as an exception in the main report.</b></p>

What is the objective of this procedure?

In order to ensure that research funds are efficiently spent, the Commission expects subcontracts to be awarded according to the principle of best value for money, transparency and equal treatment. The objective of this procedure is to verify that these principles have been respected (in particular it may be the case that the beneficiary is unable to provide evidence of fair tendering). The model Grant Agreement also permits contracts to be awarded under existing framework contracts in the interests of efficiency, if in accordance with the beneficiary's usual management principles. In this case the objective is simply to confirm the existence of such a framework contract prior to the beginning of the project.

Which documents should the beneficiary prepare for the auditor?

The auditor should be provided with a report which describes how the offers from subcontractors were obtained and assessed, including an explanation on the criteria used, and showing that the tender was awarded to the contractor who best fulfilled these criteria. The auditor is not expected to analyse the judgemental decisions taken by the beneficiary, but rather to report on the existence of documentation fitting this description for the subcontracts in question.

Please note that the last sentence of the left-hand column "full coverage if less than 20 items, otherwise (...) is the greater" refers to the size of the sample.

The size of the sample proposed in this procedure has to respect the following:

- if the population is less than 20 items, full coverage
- if the population is equal or greater than 20 items
  - a minimum of 20 items
  - or 20 % of the items (whichever is the greater)

What is the most frequent error in this context?

Insufficient documentation to prove the existence of fair procurement procedures<sup>54</sup> (e.g. no offers from other parties) or the existence of a framework contract with the supplier in addition to the specific contract connected with the project.

*6.4.3 Other direct costs (equipment, travel costs, consumables)*

Procedures	Standard factual findings and basis for exception reporting
<b>Other Direct Costs</b>	
7. Allocation of equipment subject to depreciation is correctly identified and allocated to the project. Full coverage if less than 20 items, otherwise a sample of minimum 20, or 20% of the items, whichever is the greater.	The Auditor traced the equipment charged to the project to the accounting records and the underlying invoices. The Beneficiary has documented the link with the project on the invoice and purchase documentation, and, where relevant, the project accounting. The asset value was agreed to the invoice and no VAT or other identifiable indirect taxes were charged. The depreciation method used to charge the equipment to the project was compared to the Beneficiary's normal accounting

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<sup>54</sup> For details on procurement procedures, refer to FP7 Guide to Financial Issues

	<p>policy and found to be the same.</p> <p><b>If assets have been charged which do not comply with the above, they should be listed (together with the amounts) as exceptions in the main report.</b></p>
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What is the objective of this procedure?

Beneficiaries are permitted to charge assets to research Grant Agreements in line with their normal accounting policy. The objective of this procedure is to ensure that the individual fixed assets have been charged according to the normal accounting policy using amounts which can be traced from the accounting records and using the related depreciation rate.

Which documents should the beneficiary prepare for the auditor?

The documents relate to the invoices of the assets concerned and to the extracts from the accounting records showing the relevant entries, as well as the relevant policies for depreciation of the assets (period, straight line or reducing balance, etc.).

Please note that the last sentence of the left-hand column "full coverage if less than 20 items, otherwise (...) is the greater" refers to the size of the sample.

The size of the sample proposed in this procedure has to respect the following:

- if the number of the pieces of equipment is less than 20 items, full coverage,
- if the number of the pieces of equipment is equal or greater than 20 items
  - a minimum of 20 items,
  - or 20 % of the items (whichever is the greater).

What is the most frequent error in this context?

Beneficiaries, having incurred the cash outflow to acquire the asset, try to charge the entire amount in the first period, despite the fact that the asset may be depreciated in their accounts through a number of years. In this case, only the depreciation relevant to the period in question (the period of the cost statement under consideration) can be charged. Another common error is the charging of VAT.

Procedures	Standard factual findings and basis for exception reporting
<b>Other Direct Costs</b>	
<p>8. Travel costs correctly identified and allocated to the project (and in line with Beneficiary's normal policy for non-EC work regarding first-class travel, etc.) Full coverage if less than 20 items, otherwise a sample of minimum 20, or 20% of the items, whichever is the greater.</p>	<p>The Auditor inspected the sample and found that the Beneficiary had allocated travel costs to the project by marking of invoices and purchase orders with the project reference, resulting in traceable allocation in the project accounts.</p> <p>The costs charged were compared to the invoices and found to be the same. No VAT or other identifiable indirect taxes were charged.</p>



<p>The Beneficiary should provide written evidence of its normal policy for travel costs (e.g. use of first class tickets) to enable the Auditor to compare the travel charged with this policy.</p>	<p>The use of first class travel was in line with the written policy provided by the Beneficiary.</p> <p><b>Costs which are not allocated to project accounts and do not have a clear attribution (normally by writing the project number on the original invoice) should be listed (together with the amounts) as exceptions in the main report.</b></p>
<p>9. Consumables correctly identified and allocated to the project. Full coverage if less than 20 items, otherwise a sample of minimum 20, or 20% of the items, whichever is the greater.</p>	<p>The Auditor inspected the sample and found that the Beneficiary had allocated consumable costs to the project by marking of invoices and purchase orders with the project reference, resulting in traceable allocation in the project accounts.</p> <p>The costs charged were compared to the invoices and found to be the same. No VAT or other identifiable indirect taxes were charged.</p> <p><b>Costs which are not allocated to project accounts and do not have a clear attribution (normally by writing the project number on the original invoice) should be listed (together with the amounts) as exceptions in the main report.</b></p>

The wording "project accounts" in the above procedure is defined in Part III, Glossary of the present guidance notes.

What is the objective of this procedure?

To ensure that travel and consumable<sup>55</sup> costs are accurately charged to the project without any identifiable indirect taxes<sup>56</sup> (including VAT) and that only those costs relevant to the project are charged.

Which documents should the beneficiary prepare for the auditor?

Extracts from the accounting records together with the relevant **original** invoices are the basis for performing this procedure. The company policy on travel costs should be made available where first class or business class travel has been used. Only when a policy is in place in general terms and not being used exclusively for EC projects, the costs can be considered. Otherwise, an exception should be noted. The auditor is not expected to make an assessment of project relevance in the absence of information provided by the beneficiary. Invoices should have a clear designation as relating to the project, and the burden of sufficient documentation is on the beneficiary. The auditors are expected to report their findings based on the documentary evidence, and should not take into

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<sup>55</sup> Refer to Part B, Section 1 of the FP7 Guide to Financial Issues for details on consumables

<sup>56</sup> Refer to Part III, Glossary for definition of indirect taxes the following link [http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges_en.pdf)

account supplementary explanations by the beneficiary when these are not supported by the relevant documentation.

Please note that the last sentence of the left-hand column "full coverage if less than 20 items, otherwise (...) is the greater" refers to the size of the sample.

The size of the sample proposed in this procedure has to respect the following:

- if the population is less than 20 items, full coverage,
- if the population is equal or greater than 20 items
  - a minimum of 20 items,
  - or 20 % of the items (whichever is the greater).

What is the most frequent error in this context?

For travel, the most frequent error is failing to deduct ineligible VAT (for example from hotel & transport costs incurred in other countries). VAT should be deducted in all cases, whether it is recoverable by the beneficiary or not, and whether it relates to the VAT regime applying to the beneficiary or not.

For consumables, failing to make a clear link to the project is a common error, assuming VAT has been deducted. The Commission requires a sufficient audit trail which unambiguously ties an invoice to the project, and is thus not able to accept costs which were not linked to the project at the time of processing.

*6.4.4 Indirect costs*

Procedures	Standard factual findings and basis for exception reporting
<b>Indirect costs</b>	
10. Obtain and review a detailed breakdown of Indirect costs (reconciled to the accounting records) and confirm that the following costs are not present: <ul style="list-style-type: none"> <li>a) identifiable indirect taxes including value added tax,</li> <li>b) duties,</li> <li>c) interest owed,</li> <li>d) provisions for possible future losses or charges,</li> <li>e) exchange losses, cost related to return on capital,</li> <li>f) costs declared or incurred, or reimbursed in respect of another Union/Euratom project,</li> <li>g) debt and debt service charges, excessive or reckless expenditure<sup>57</sup>.</li> </ul>	<p>The Auditor obtained the total overhead amount which was allocated and reconciled this to the accounting records for the period in question.</p> <p>The Auditor recalculated the ratio of indirect costs [as a percentage of personnel costs/ as an hourly personnel rate/ as another cost driver specified by the Beneficiary] and agreed it to the rate used in the Financial Statement(s).</p> <p>The Auditor obtained a detailed breakdown from the accounting system of the indirect costs which have been charged to the contract, and reconciled the individual amounts to the general ledger of the Beneficiary.</p> <p>The Auditor found that costs for the non-research activities of the Beneficiary, such as manufacturing, education, marketing of products or services, etc., had not been included in the calculation.</p> <p>For each element of the breakdown, the Auditor obtained the</p>

<sup>57</sup> See definition in Part B, Section 1 of the FP7 Guide to Financial Issues

<p>The above does not apply to beneficiaries using a flat rate to claim indirect costs in accordance with Annex II of the Grant Agreement attached to the grant agreement being reviewed. In such case the procedure to apply is:</p> <ul style="list-style-type: none"> <li>• The auditor confirmed that the flat rate applied on the Financial Statement(s) is consistent with the one provided in Annex II of the Grant Agreement.</li> <li>• The auditor recalculated the indirect costs claimed on the basis of the flat rate for <u>arithmetical accuracy</u>.</li> </ul>	<p>Beneficiary's confirmation that it contained none of the ineligible costs specified (typical examples are leasing costs, loan charges, provisions for doubtful debt (but not normal accruals), local business and property taxes, customs duties, exchange losses from billing in a foreign currency).</p> <p><b>Only the types of excessive and reckless expenditure listed in the Commission's guidance should be considered, the Auditor is not required to exercise professional judgement or provide assurance in this matter.</b></p> <p><b>Amounts which do not meet the above criteria or where the Auditor is not provided with sufficient information in order to inspect and compare the types of cost should be listed (together with the amounts) as exceptions in the main report.</b></p> <p><b>Only for beneficiaries using a flat rate to claim indirect costs:</b></p> <p>The auditor found:</p> <ul style="list-style-type: none"> <li>• that the flat rate has been charged in accordance with Annex II of the Grant Agreement and computed on direct eligible costs excluding costs for sub-contracting and the costs of resources made available by third parties which are not used on the premises of the beneficiary.</li> <li>• that no differences arose from the numerical reconciliation</li> </ul>
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What is the objective of this procedure?

*The first part of this procedure does not apply if a flat-rate<sup>58</sup> on eligible direct costs is used for the calculation of overheads/indirect costs. Nevertheless, when a flat-rate is used for the calculation of indirect costs, the auditor should also check, in accordance with the Annex II of the Model Grant Agreement, that the flat-rate has been calculated on the basis of the direct eligible costs excluding the direct eligible costs for sub-contracting and the cost of resources made available by third parties which are not used on the premises of the beneficiary.*

In addition to the procedure 10 described in the left-hand column where the auditor checks that all the specific types of costs defined as ineligible in the Grant Agreement have in fact been excluded from indirect costs, the auditor will have to check that :

- a list of allocation methods was provided where the beneficiary is allocating shared costs.
- the costs supported under FP7 have been incurred by the beneficiary in its research activity. The concern is that by including non-research related costs in the indirect cost calculation, the beneficiary might include elements related to its non-research activity. This most frequently occurs with universities, which may have educational activities, or companies which have trading businesses where they supply goods and services other

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<sup>58</sup> As stipulated in the Grant Agreement

than research (e.g. a company that carries out applied research but also sells hardware and software to customers and therefore incurs costs supporting the manufacturing, sales and marketing of these products).

The auditor is requested to recalculate the ratio of indirect costs (as a percentage of personnel costs/ as an hourly personnel rate/ as another cost driver specified by the beneficiary). When the cost driver chosen for the indirect costs allocation is not based on personnel, the auditor is invited to provide a description of the allocation method in the factual findings.

What if the beneficiary already has a Certificate under Form E approved by the Commission?

Where a Certificate on the Methodology has been approved by the Commission, the auditor will not have to recalculate the ratio of indirect costs but will have to perform the other checks of this procedure to ensure that the certified methodology has been correctly applied.

Which documents should the beneficiary prepare for the auditor?

The beneficiary needs to provide a detailed breakdown of the components of the overhead cost, together with a sufficient narrative description of the individually accounting elements (chart of accounts) to enable the auditor to identify the nature of the cost, and to be able to distinguish costs that are wholly relevant to research, mixed, or not relevant to research. In order to ensure completeness of this breakdown, the reconciliation to the accounts should be provided in order to link the information provided to the annual accounts of the beneficiary.

For the allocation methods, the beneficiary should provide the appropriate management information. For example, for allocating library costs, the beneficiary is expected to have at its disposal internal management information with staff and student numbers, if this is the basis used. For a company, an analysis of the headcount in the research vs. the trading part of the business could be supplied to support the distribution of the costs of the personnel department.

What should the beneficiary consider when evaluating the existence of ineligible items in indirect costs?

Final responsibility for the correct calculation of indirect costs – especially the exclusion of ineligible costs – lies with the beneficiary. This means the beneficiary must examine each indirect cost component to identify whether it is wholly or partially ineligible.

How can the beneficiary distinguish indirect costs which are related to research from non-research items?

Some cases are clear cut, for example the rent and energy costs of building devoted wholly to the research activity of a beneficiary (research laboratory) can be designated as a research costs that can be 100% allocated across the productive time of the researchers.

Similarly, the trading part of a business (e.g. the manufacturing plant, marketing and sales departments), should be 100% excluded from the indirect cost calculation.

The beneficiary should also describe "mixed-use" cases such as libraries in universities, accounting & personnel departments in trading companies, where the costs will have to be allocated to the different activities using a basis such as the staff to student ratio, or the ratio of research staff to staff working in the business side of the organisation. Beneficiaries should use allocation methods that are easy to compute and understand, and take a conservative approach when allocating 'borderline' costs to research.

#### How is the auditor expected to identify exceptions in the types of costs charged?

The auditor will rely on the detailed breakdown provided by the beneficiary and the detailed description of each cost element. The auditor should identify as exceptions, any items that should normally be charged as direct costs (e.g. direct time of researchers, consumables used on projects, etc.). Identification of "education" or "business" expenses is limited to an analysis of the accounting descriptions (e.g. an account clearly designated as relating to sales, or support to teaching staff, should be identified as an exception).

#### What is meant by "reconciled to the accounts"?

The auditor is not required to perform a sample check of the indirect costs but is required to perform a reconciliation of the data on the basis of the accounting records. The individual cost items should be traceable to the beneficiary's accounting records. If the source of the data is not linked to accounting records but for example to analytical accounting records or management information documents, the beneficiary should provide a reconciliation demonstrating how the figures can be linked to the accounting records.

#### What kind of costs do beneficiaries often fail to exclude?

Many beneficiaries fail to remove the irrecoverable VAT elements of indirect costs where they can be identified (for example, making a percentage reduction to certain lines, such as travel or energy consumption, where a known VAT rate is included in the costs).

Servicing of loans, interest, and also the interest element of finance leases are also common examples of ineligible indirect costs which beneficiaries fail to exclude.

#### What kinds of indirect taxes are concerned by this procedure?

In most cases, the key indirect tax is VAT. Other national duties should be raised as exceptions if they are identified as not being excluded.<sup>59</sup>

#### What is meant by excessive or reckless expenditure<sup>60</sup>?

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<sup>59</sup> For further reference, please see:

[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges_en.pdf)

<sup>60</sup> The Guide to Financial Issues does not refer to a list of excessive or reckless expenditure but provides definitions.

The auditor will have to rely on a written declaration by the beneficiary<sup>61</sup> as to the absence of excessive or reckless expenditure.

Excessive expenditure should be understood as paying significantly more for products, services or personnel than the prevailing market rates, resulting in an avoidable financial loss to the project. Reckless expenditure means failing to exercise care in the selection of products, services or personnel resulting in an avoidable financial loss to the project.

Should the auditor give an opinion whether the cost allocations are reasonable?

No. As this is an agreed upon procedures assignment, the Commission is interested in the existence of the allocation method, but reserves the right to independently assess whether the method is a fair allocation of costs to FP7 project work.

Procedures	Standard factual findings and basis for exception reporting
<b>Indirect costs</b>	
<p>11. Assess use of a simplified method of calculation of overheads at the level of the legal entity.</p> <p>The Beneficiary may use a simplified method of calculation (either due to the lack of analytical accounting or legal requirement to use a form of cash-based accounting). This does not permit the use of a generalised estimate, or the use of a 'standard' rate that is not derived from the accounting records of the period in question. Thus the rate (but not the methodology) should be updated for each accounting period.</p>	<p>The Beneficiary's accounting system does not permit indirect costs to be separately identified for the individual departments. <b>[and/ or]</b></p> <p>The Beneficiary's accounting system is cash-based and year-end adjustments are made using accounting estimates in order to charge certain accrued costs.</p> <p>The Auditor obtained the breakdown of overhead costs and the adjusting entries together with the source of the relevant accounting entries.</p> <p>The Beneficiary provided the Auditor with underlying calculations showing the basis for additional accounting entries. The Auditor agreed these calculations to the relevant sources of management information.</p> <p><b>Any elements of a simplified calculation which represent percentage estimates and which cannot be compared to underlying data should be listed (together with the amounts) as exceptions in the main report.</b></p>

What is the objective of this procedure?

The procedure "to assess" should mean the following: when performing **simplified calculations of indirect costs**, the beneficiary may not benefit from an analytical accounting system which can separate costs of different types as described in the prior procedures. Effectively, it will not be possible to identify or separate certain research costs from those related to other activities such as education. The Commission thus wishes to verify that the beneficiary has carried out a procedure to ensure that the

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<sup>61</sup> Included in the model letter of representation (see Annex I of Part III, Glossary of the present guidance notes).

indirect costs charged in the simplified method are not significantly larger than they would be if the true analytical data was known.

Which documents should the beneficiary prepare for the auditor?

As above, the beneficiary should provide the appropriate management information. In the case of the simplified method, this can be expected to be based on information from a variety of sources<sup>62</sup>.

What is meant by 'relevant sources of management information'?

Beneficiaries using the simplified method should be using the best information available, but which sometimes is not very detailed. For example, the only data the beneficiary may have in order to allocate power consumption is the floor space of the relevant buildings, even though power consumption may in reality be concentrated in certain locations (e.g. the computer research centre). In the absence of real data on consumption, the beneficiary should choose a conservative but objective measure (floor space can be verified by reference to the relevant management information).

What kind of allocation method should give rise to an exception?

Taking the example of the computer centre above, if the beneficiary allocated (say) 30% of its power consumption without having any factual basis, this should be raised as an exception by the auditor. For the Commission the concept of the simplified method does not extend to estimates which do not have a verifiable basis. Thus if the beneficiary cannot demonstrate to the auditor how the 30% was calculated, it should be raised as an exception.

*6.4.5 Exchange rates used*

Procedures	Standard factual findings and basis for exception reporting
<p><b>Exchange rates</b></p> <p>12. Inspect and compare exchange rates into Euros.</p>	<p>The Auditor compared the exchange rates used for conversion with the applicable official exchange rates established by the European Communities and the Beneficiary used [choose one]:</p> <ul style="list-style-type: none"> <li>• the conversion rate of the date where the actual costs were incurred</li> </ul>

<sup>62</sup> The source of information will depend on the cost-driver used to distribute the shared costs among the different activities. The Auditor will be interested in any document supporting the correctness of the estimated allocation.

	<ul style="list-style-type: none"> <li>• the rate applicable on the first day of the month following the end of reporting period</li> </ul> <p><b>Where rates cannot be agreed, an exception should be noted, (together with the amount) in the main report.</b></p>
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What is the objective of this procedure?

As a reminder, Article II.6.4 of FP7 model Grant Agreement foresees that costs shall be reported in EUR. Beneficiaries with accounts in currencies other than EUR shall report in EUR on the basis of the exchange rate that have applied either on the date that the actual costs were incurred or on the basis of the rate applicable on the first day of the month following the end of the reporting period. Beneficiaries with accounts in EUR shall convert costs incurred in other currencies according to their usual accounting practices. For beneficiaries with accounts in currencies other than EUR, the auditor is expected to compare the rates used for foreign currency conversion to the official rates established by the European Central Bank so that the Commission can confirm that they were accurately calculated.

It is imperative that costs be reported in EUR in the Financial Statements and that beneficiaries with accounts in currencies other than EUR report in EUR on the basis of the exchange rate published by the European Central Bank that would have applied either:

- on the date that the actual costs were incurred or
- on the basis of the rate applicable on the first day of the month following the end of the reporting period.

The auditor should therefore check that the exchange rate used in the Financial Statements conforms to one of the two above-proposed options, the European Central Bank website being the official source for the exchange rate to be applied: [www.ecb.eu/stats/exchange/eurofxref/html/index.en.html](http://www.ecb.eu/stats/exchange/eurofxref/html/index.en.html).

If the exchange rate chosen by the beneficiary does not correspond to one of the two above options, the auditor should report an exception on the exchange rate used as a reference. It is expected from the auditor to quantify and report the differences between the exchange rate used by the beneficiary and one of the two options.

Does this procedure apply to beneficiaries with accounts in Euro performing transactions incurred in other currencies?

As mentioned above, Article II.6.4 of FP7 model Grant Agreement states that for beneficiaries using the euro as its accounting currency, but who have incurred expenses in another currency, the rule is not to apply the ECB rates, but their usual accounting practice. Therefore procedure n°12 does not apply to beneficiaries with accounts in EUR



and costs incurred in other currencies. The certifying auditor should indicate the reason for not performing this procedure (i.e. beneficiary with accounts in EUR and costs incurred in other currencies) and this should not be considered as an exception.

#### 6.4.6 Identification of receipts

Procedures	Standard factual findings and basis for exception reporting
<b>Receipts</b>	
<p>13. Identification of receipts. The Beneficiary is obliged to declare in its claim any receipts related to the project (income from events, rebates from suppliers, etc.)</p>	<p>The Auditor examined the relevant project accounts and obtained representations from the Beneficiary that the amounts listed represent a complete record of the sources of income connected with the project. The amount included in the claim regarding receipts is the same as the amount recorded in the project accounting.</p> <p><b>Any discrepancies in the receipts noted in the accounts and those reported by the Beneficiary should be noted (together with the amount) as exceptions in the main report.</b></p>

#### What is the objective of this procedure?

The objective is to ensure that the receipts related to the project have been correctly declared. The wording "Project accounting" in the procedure means the entire process to establish the project accounts<sup>63</sup>.

#### Which documents should the beneficiary prepare for the auditor?

Extracts from the project accounting should be made available showing all income entries. In addition to this, a declaration from the beneficiary should be obtained that receipts reported to the Commission are complete and the beneficiary has taken sufficient steps to ensure their completeness according to its normal accounting practices.

#### 6.4.7 Identification of interest yielded

Procedures	Standard factual findings and basis for exception reporting
<b>Interests yielded</b>	
<p>14. Identification of interest yielded until 31.12.2012 on pre-financing. The Beneficiary, when it is the coordinator of the project, is obliged to declare interest yielded until 31.12.2012 on pre-financing.</p>	<p>The Auditor compared the relevant project accounts with the interest shown in the bank statements and found them to be the same.</p> <p><b>Any discrepancies in the interest noted in the accounts and those reported by the Beneficiary should be noted (together with the amount) as exceptions in the main report.</b></p>

<sup>63</sup> Refer to Part III, Glossary for details on project accounts

### What is the objective of this procedure?

The objective is to ensure that all interest yielded on pre-financing has been correctly declared in the claim for the Commission. This process is only applicable when the beneficiary acts as the coordinator of a multi-partner FP7 project or when the beneficiary is a single participant in a mono-beneficiary grant.

Due to the adoption of the new Financial Regulation<sup>64</sup>, as from 01.01.2013, the coordinator's obligations to:

- i) open and operate an interest-bearing bank account (see Art. II.6) and
- ii) to declare and reimburse to the Commission the interest generated by the pre-financing (see Art. II.19)

have been abolished.

Hence, any interest generated by the pre-financing transferred by the Commission to the coordinator's bank account no longer has to be deducted from the EU contribution and does not need to be offset against the subsequent payment. These new rules apply automatically as from 01.01.2013 to both future and existing (on-going) grant agreements without the need for formal individual amendments to the grant agreement.

However, any interest generated by the pre-financing until 31.12.2012 has to be declared and reimbursed by the coordinator to the Commission. Hence, the scope of this procedure is limited to verifying that interest generated by the pre-financing up to 31.12.2012 has been declared by the coordinator.

### Which documents should the beneficiary prepare for the auditor?

Extracts from the project accounting and the relevant bank statements should be made available showing all interest income entries. In addition to this, a declaration from the beneficiary should be obtained that interest income reported to the Commission is complete.

## 6.5 Specific provisions for Marie Curie grants

A new Form D has been developed for use in the Marie Curie grants. This form addresses in particular the specificities relating to Personnel, Subcontracting, Equipment, Travel and consumable costs.

Since the Marie Curie Grant Agreement provides for a 10% flat-rate for indirect costs, procedures aim at verifying that the flat-rate has been calculated on the basis of the direct

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<sup>64</sup> <sup>64</sup> The Regulation No 966/2012 on the financial rules applicable to the general budget of the Union repealing Council Regulation (EC, Euratom) No 1605/2002 (former Financial Regulation).

eligible costs excluding the direct eligible costs for sub-contracting and the cost of resources made available by third parties which are not used on the premises of the beneficiary.

## 6.6 Specific provisions for ERC grants

A new Form A (Certificate of Financial Statements) has been developed for the ERC grants the procedures concerning direct costs are identical to the procedures in Form D of the Standard Model Grant Agreement and the current Guide can be used for information. Form A does not foresee procedures for indirect costs under the ERC grants.

## PART III: GLOSSARY

## **ACCOUNTING RECORDS**

Refer to the accounting entries and the documents supporting the statutory financial statements and/or reporting requirements, as well as, the internal procedures, reports or other documents necessary to understand the accounting system of the beneficiary.

The accounting records include, among others:

- Accounting entries:
  - Accounting journal
  - General ledger
  - Cash book
  - Inventory register / Fixed assets register
- Supporting documents
  - Sales and purchase invoices
  - Delivery notes, in particular for fixed assets
  - Credit notes
  - Salary slips
  - Bank statements
- Other documents
  - Rules applied for depreciation
  - Method of allocation of indirect costs
  - Internal rules for reimbursement of travel expenses

## **EXCESSIVE OR RECKLESS EXPENDITURE**

The auditor will have to rely on a written representation by the beneficiary<sup>65</sup> as to the absence of reckless or excessive expenditure.

Excessive expenditure should be understood as paying significantly more for products, services or personnel than the prevailing market rates, resulting in an avoidable financial loss/charge to the project. Reckless expenditure means failing to exercise care in the selection of products, services or personnel resulting in an avoidable financial loss/charge to the project.

## **EXCEPTION**

In the context of the Forms D and E, matters to be reported by the auditor in his report under the caption "Exceptions" include the following:

- Error or exception: Any fact detected by the auditor while performing a procedure which prevents him from using the standard text of the findings

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<sup>65</sup> Included in the model letter of representation

proposed in the model Form. Therefore, whenever the standard text of the findings needs to be modified by the auditor following the application of the procedure, this should be reported as an *exception*.<sup>66</sup>

- Scope limitation: Any fact or event which impedes the auditor to perform any of the procedures. This includes any modification made by the beneficiary in the standard model statements of the model Form to reflect the real situation which would prevent the auditor from carrying out the corresponding procedure.

For instance in procedure 1 of the table of statements and procedures of the Form E, the standard statement by the beneficiary reads:

*"Time recording exists, with authorisations, which enables all personnel [...]"*

If the beneficiary states that there is no time recording, the related procedure described in the right-hand column (verification of the time recorded) cannot be carried out. Therefore this scope limitation should be reported as an exception in the auditor's report.

An *exception* should also be raised if auditors decide to carry out alternative procedures on findings due to the specific circumstances related to the beneficiary (such as the lack of time recording but existence of other related evidence). The auditor should explain under "Exceptions" the reasons why he could not carry out the standard procedure(s) and describe the alternative procedure(s) and related findings.

## **FINANCIAL STATEMENT (IN RTD CONTEXT)**

Refers solely to Form C (Annex VI to the EC FP7 Grant Agreement) whereby the Beneficiary declares costs to the Commission in the frame of the Grant Agreement. In this context, Financial Statements are not the beneficiary's statutory financial statements (or equivalent).

Models of Form C can be found at:

[http://ec.europa.eu/research/participants/portal/page/fp7\\_documentation](http://ec.europa.eu/research/participants/portal/page/fp7_documentation)

## **GENERAL LEDGER**

It corresponds to the double-entry accounting in which the financial movements are recorded at the level of each individual account. It presents the chart of accounts of the beneficiary and provides the information on the debit and credit entries made in the individual accounts. The general ledger is the primary source from which the statutory financial statements (or equivalent) are prepared.

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<sup>66</sup> Please note that the Form D uses several examples of findings which trigger an *exception*. However, this does not mean that only these findings should be reported as *exceptions*.

## INDIRECT TAXES<sup>67</sup>

Identifiable<sup>68</sup> indirect taxes including value added tax (either recoverable or not by the beneficiary) are not eligible according to the Grant Agreement provisions. An identifiable indirect tax is a tax charged on the cost of a good or service and paid by the purchaser in the form of an increase of the price.

However, indirect taxes will be allowed when not identifiable. This may be for example the case with foreign invoices where the price indicated is gross without identifying the value added tax. In any case, the beneficiary should be able to justify this in the event of an audit.

## NORMAL ACCOUNTING POLICY

Standards and criteria used by the beneficiary to prepare its statutory financial statements (or equivalent). The accounting policy applied by the beneficiary for FP7 Grant Agreements should not differ from its normal accounting policy. Whenever adjusting entries are necessary to comply with the eligibility criteria of the Grant Agreement, these should be duly documented<sup>69</sup> and reconciled to the accounting records.

The normal accounting policy can never be adapted ad-hoc in order to overcharge the EC Grant Agreement compared with the normal practices of the beneficiary.

### *Example:*

The term "normal accounting policy" is referred in procedure 7 of the Form D concerning the depreciation of the equipment. In this procedure it is explicitly demanded that the depreciation method applied for the assets charged to the Grant Agreement should be the same as the depreciation method normally applied by the beneficiary.

Situations as the following are, therefore, not permitted:

Beneficiary X applies an annual depreciation of 25 % for IT equipment.

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<sup>67</sup> For additional details on the subject, refer to the "Guide to Financial Issues relating to FP7 Indirect Actions", section "Article II.14.3 of GA – Non-eligible costs" and the following link [http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/eligibility-taxes-charges_en.pdf)

<sup>68</sup> Identifiable means explicitly indicated on the purchase invoice.

<sup>69</sup> Adjusting entries refer to the corrections aimed at eliminating costs included in the indirect costs but which are ineligible under FP7 (e.g. provisions for future losses, exchange losses, interest owed, etc).

Two new computers for a total of EUR 3.000 are purchased to be used exclusively for the EU Grant Agreement "Y". The project covered by this Grant Agreement has duration 2 years.

The beneficiary decides to apply yearly depreciation of 50 % in order to charge the full cost of the equipment to the project.

Annual depreciation according to the "normal accounting policy" =  $3.000 * 25 \% = 750$

Total depreciation charged to the Grant Agreement =  $750 * 2 \text{ years} = \mathbf{1.500}$

Annual depreciation according to the ad-hoc accounting policy =  $3.000 * 50 \% = 1.500$

Total depreciation charged to the Grant Agreement =  $1.500 * 2 \text{ years} = \mathbf{3.000}$

The concept of "**normal policy**" can be extended to other areas of costs, for instance travel costs, meaning that no internal rule for allocation of expenses should be modified in order to overcharge the FP7 Grant Agreement.

*Example for travel costs:*

The internal policy of Beneficiary X concerning the flight tickets is that all its researchers should travel in economy class.

However, Beneficiary X realises that they have overestimated the budget necessary for travels for the FP7 Grant Agreement in which it is participating.

Beneficiary X decides then to accept its researchers travelling in business class because the costs will be charged to the Grant Agreement. In addition, they decide that the daily allowance generally paid to the researchers will be increased by 10 % for these trips since there will be sufficient budget.

This kind of derogation from the internal rules is **not** permitted.

Please note, however, that "**normal accounting policy**" cannot override FP7 rules. Therefore, if there is a contradiction between the normal accounting policy and the FP7 rules, for the purposes of the preparation of the costs statement the beneficiary should abide to the FP7 rules. For example, if under the normal practice the calculation of overheads includes marketing costs, they should be removed as non-eligible under the FP7 eligibility rules irrespective of how they are "normally" accounted for by the beneficiary.

## **NORMAL EMPLOYMENT COSTS**

Refers to all costs components related to personnel. These include the basic salary, sickness, pension and social contributions as well as any kind of allowances or benefits granted to the employees. The notion of "normal" implies that those are the standards commonly applied by the beneficiary.



## **PRODUCTIVE TIME**

The productive time for an employee is the time actually spent on direct work. Productive hours have to be clearly justified and should match the underlying time records.

The productive time should exclude annual leave, public holidays, training and sick leave. Productive hours must be calculated according to the beneficiary's normal practices and will vary depending on the personnel category, industry sector, unions, contracts and national legislation.

A figure of 210 working days per year could be considered representative in most cases.

### ***Example:***

Total days in a year	365
Weekends	-104
Annual holidays	-21
Statutory holidays	-15
<u>Illness/Others</u>	<u>-15</u>
Workable days in a year	210

\* 8 working hours/day = 1.680 Productive hours

If the productive hours actually worked (as supported by the time-records) are greater than the productive hours budgeted, the first shall be used for the calculation of the personnel costs.

## **PROJECT ACCOUNTS**

Normally project accounts for FP7 projects are management account codes allocated solely to individual FP7 projects which are integrated in the double entry accounting system of the beneficiary. This integration with the double entry system reduces the likelihood of double counting and makes it easier to reconcile the costs with the accounting records. Thus the invoices (say for travel) which are allocated to the project are posted via double entry to the individual project accounts, so that the travel costs incurred for a particular project in a particular period can be correctly identified. Other forms of recording project expenditure (e.g. spreadsheets) are not considered as reliable as management accounting directly linked to the double-entry accounting system.

## **"PRO FORMA" FINANCIAL STATEMENT**

The "pro forma" financial statement should be prepared by beneficiary in the same format as the Form C. Usually it will cover an interim period from the beginning of the

project<sup>70</sup> in order to be used as a basis for analysis of the Certification on the Methodology when no actual Form C (covering a full reporting period for the Grant Agreement) is yet available.

The "pro forma" Form C is not an official document and should not be submitted to the Commission. It is only to be used by the auditor as the supporting evidence in the absence of the Financial Statement (Form C).

### **REPRESENTATION LETTER<sup>71</sup>**

The representation letter is a document clearly dated in which the Beneficiary confirms in writing all representations made to the Auditor during the course of the procedures specified. The purpose of this letter is to document the responsibility of the Beneficiary with regard to the information presented during the procedures.

*Example:*

An example of Representation Letter is given in the Annex to this glossary.

### **SIMPLIFIED METHOD<sup>72</sup>**

The simplified method is a way of declaring indirect costs applicable to organisations which cannot provide an analysis of their indirect costs at a **detailed level** (i.e. by activity), but can aggregate their indirect costs **at least at the level of the legal entity**.

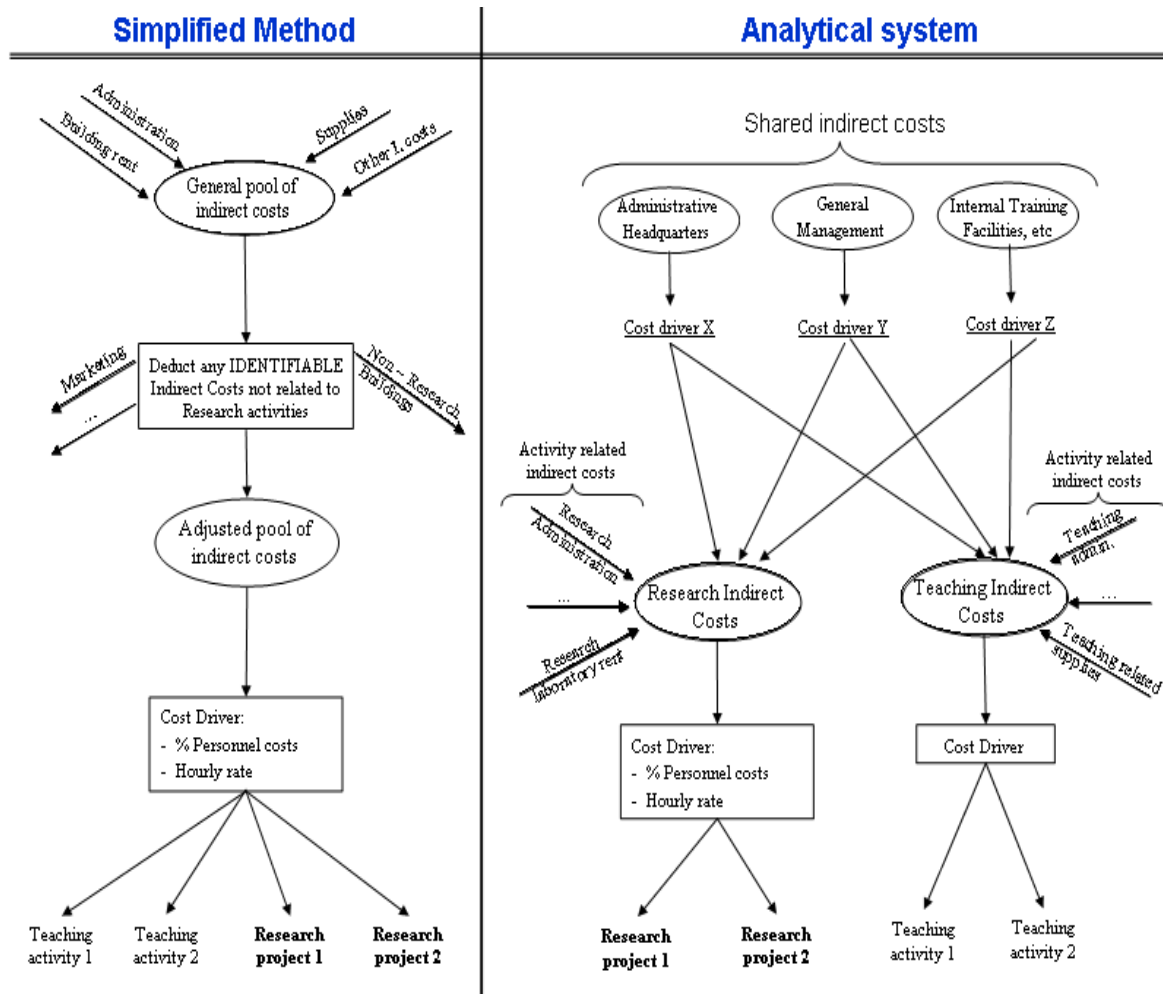
This requires that the beneficiary has an accounting system enabling it to determine the total indirect costs (overheads) of the entity as a whole. However, the same system would not permit the share of the indirect costs generated by the research activities to be fully identified separately from the other indirect costs. Therefore, the indirect costs of the beneficiary should be treated altogether and allocated using a cost driver which accounts for all the productive hours of the entity and not only for the research productive hours.

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<sup>70</sup> When the beneficiary changes its methodology in the course of the duration of the project and seeks for a certificate on methodology, the "Pro forma" financial statement may cover another period for which a Form C has not yet been submitted.

<sup>71</sup> See FP7 Grant Agreement- ANNEX VII – Form E paragraph 1.1

<sup>72</sup> For further explanation on the simplified method, please refer to the "Guide of Financial Issues relating to FP7 Indirect Actions"  
[http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide\\_en.pdf](http://ec.europa.eu/research/participants/portal/ShowDoc/Extensions+Repository/General+Documentation/Guidance+documents+for+FP7/Financial+issues/financialguide_en.pdf)



**UNDERLYING MANAGEMENT INFORMATION<sup>73</sup>**

Accounting policies, internal accounting procedures and supporting documents (working papers, details on calculations, etc.) constitute the basis for the normal calculation of the indirect costs for the beneficiary.

The beneficiary must provide the auditor with the additional information and underlying calculations enabling the reconciliation between the normal calculation and the basis of calculation of the amounts charged to the Grant Agreement. The adjusting entries applied by the beneficiary must be substantiated by the underlying calculations which are to be agreed by the auditor to the relevant sources of management information.

<sup>73</sup> In the context of the simplified indirect costs calculation (Form E, procedure 6)

## ANNEX 1 – EXAMPLES OF LETTERS OF REPRESENTATION

### 1.A Related to the Certificate on the Methodology (Form E)

#### Letter of Representation

(Beneficiary letterhead)  
(Date-same as date of the factual findings report)  
(Addressed to the Audit firm)

Dear Madam, dear Sir,

Taking into consideration our responsibility as mentioned in the Article 1.1 of Annex VII-Form E of the FP7 Grant Agreement N° xxxxx (Project Title Acronym) with the European Commission and in connection with your engagement to perform agreed upon procedures regarding the Methodology (Form E) as at [date] or covering the period from [date] to [date], we hereby confirm the following representations made to you during your engagement:

- We are responsible for the preparation of the statements made in the Form E and for their accuracy and completeness. All the statements cover the methodology used as at (date) or for the period starting (date) and ending (date) to prepare the cost Financial Statements in accordance with the Grant Agreement.
- We have made available to you all records, documents, statements and significant information that we believe are relevant for the purpose of the agreed-upon-procedures you have performed.
- All information given to you regarding personnel and their remuneration, division of their time, and qualifications is accurate, complete and in line with the historic data.
- Costs that we have reported as eligible costs are actual costs excluding any profits<sup>74</sup> and are determined in accordance with our usual accounting principles and allocation methods in place.
- *(if applicable)* We have complied with the conditions of the consortium agreement.
- Personnel costs used in the calculation of average or individual personnel cost to be charged to the EU projects do not include bonuses or special conditions for employees working on European Commission funded projects nor do they include ineligible costs in particular those enumerated in Article II.14.3 of Annex II to Grant Agreement.
- Indirect costs only include those costs which cannot be allocated to specific projects and support the functioning of the organisation as a whole.

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<sup>74</sup> As could be the case, for instance, of internal invoicing, inter-departmental charges, etc

- No implicit interest is included in the expenditures in relation to European Commission funded projects.
- Purchases are made according to the principles of best value for money (best price-quality ratio), transparency and equal treatment. No excessive or reckless expenditure is included.
- No event has occurred after [ending date of period covered by statements], which would have a significant impact upon those statements.

Nothing has come to our attention during the period under review, including management actions and/or other matters of importance that might be considered to represent financial irregularities, fraud or an illegal act which would have an impact on the statements OR the following financial irregularities, fraud or illegal acts which have an impact on the statements have occurred : [...] and sufficient measures have been taken to correct them and to prevent repetition, and they have all been fully disclosed to you.

....

(Name of the Beneficiary)

(Stamp and Signature)

## **1.B Related to the Certificate on the Financial Statements (Form D)**

### **Letter of Representation**

(Beneficiary letterhead)  
(Date-same as date of the factual findings report)  
(Addressed to the Audit firm)

Dear Madam, Dear Sir,

Taking into consideration our responsibility, as mentioned in Article 1.1 of Annex VII - Form D of the FP7 Grant Agreement N° xxxxx (Project Title Acronym) with the European Commission and in connection with your engagement to perform agreed-upon procedures regarding the Financial Statement (Form D) covering the period from [date] to [date] (the “Financial Statement”), we hereby confirm the following representations made to you during your engagement:

- We are responsible for the preparation of the Financial Statement covering the period starting (date) and ending (date) in accordance with the Grant Agreement and for their accuracy and completeness.
- We have made available to you all records, documents, statements and information that we believe are relevant for the purpose of the agreed-upon-procedures you have performed.
- *(if applicable)* We have complied with the conditions of the consortium agreement.
- Personnel costs:
  - (Option 1) Personnel costs reported in the Financial Statement are not based on budgeted or estimated amounts. They are calculated using rates based on actual costs, and reflect the time actually worked on the [ ] project during the period covered by the Financial Statement. OR
  - (Option 2) Personnel costs reported in the Financial Statement are not based on budgeted or estimated amounts. They are calculated using average rates which are compliant with the acceptability criteria adopted by the Commission in its Decision C(2011)174 and reflect the time actually worked on the [ ] project during the period covered by the Financial Statement.
- Subcontracts and contracts to suppliers of goods and services are awarded in accordance with a procedure including an analysis of best value for money (best price-quality ratio), transparency and equal treatment.
- Indirect costs reported in the Financial Statement do not include any of the following costs:

- Identifiable indirect taxes including value added tax (for instance local business and property taxes);
  - Duties (for instance customs duties);
  - Interest owed;
  - Provisions for possible future losses or charges (for instance provisions for doubtful debt (but not normal accruals));
  - Exchange losses, cost related to return on capital (for instance exchange losses from billing in a foreign currency);
  - Costs declared or incurred, or reimbursed in respect of another Union/Euratom project;
  - Debt and debt service charges,
  - Excessive or reckless expenditure (for instance loan charges);
  - Implicit interest (leasing costs or other credit arrangements);
  - Costs attributable to activities other than the research activities covered by the [ ] project, such as manufacturing, education, marketing of products or services, etc.
- Purchases in connection with the [ ] project are made according to the principles of best value for money (best price-quality ratio), transparency and equal treatment. No excessive or reckless expenditure is included in the Financial Statement.
  - The receipts declared in the Financial Statement represent a complete record of the sources of income connected with the European Commission funded project (for example, income from events, rebates from suppliers...), and have been recorded in accordance with our normal accounting practices.
  - (*if applicable*) All interest yielded on pre-financing of the [ ] project during the period covered by the Financial Statement has been reported in the Financial Statement.
  - No event has occurred after [ending last day of the period covered by the Financial Statement], which would have an impact upon the Financial Statement.
  - Nothing has come to our attention during the period under review, including management actions and/or other matters of importance that might be considered to represent financial irregularities, fraud or an illegal act which would have an impact on the Financial Statement OR the following financial irregularities, fraud or illegal acts which have an impact on the Financial Statement have occurred: [...] and sufficient measures have been taken to correct them and to prevent repetition and they have all been fully disclosed to you.
  - [Other matters, as applicable].

(Name of the Beneficiary)

(Stamp and Signature)

**ANNEX 2 – TEMPLATE MODEL FOR CALCULATION OF HOURLY PERSONNEL RATE**

Calculation of hourly personnel rate				
Salary details per person or category		Gross salary (1)	Employer's social charge (2)	Others (3)
Month 1				
Month 2				
Month 3				
Month 4				
Month 5				
Month 6				
Month 7				
Month 8				
Month 9				
Month 10				
Month 11				
Month 12				
Month 13, 14 or other (4)				
Month 13, 14 or other (4)				
Month 13, 14 or other (4)				
<b>Sub-totals</b>		<b>0</b>	<b>0</b>	<b>0</b>
<b>Total salary + Social charges + Others</b>	<b>A</b>			<b>0</b>
Productive hours details				
Number of working hours per week (5)				
Number of weeks during the period (6)				
<b>Sub-total Working hours for the period</b>	<b>B</b>			<b>0</b>
<b>Deduction for : (in days)</b>				
Annual holidays (7)				
Statutory holidays (8)				
Illness/others (9)				
sub-total absence for the period (days)				<b>0</b>
Average numbers of working hours per day (10)				
<b>Total absence in hours</b>	<b>C</b>			<b>0</b>
<b>Total Productive hours for the 12 months period</b>	<b>D = B-C</b>			<b>0</b>
<b>Hourly personnel rate</b>	<b>A/D</b>			<b>0</b>

- (1) The gross salary as shown on the salary slip for the month  
(2) Social charge paid by employer as required by law  
(3) Other components of the salary not included in the gross salary but declared to the Tax Authorities. **Please explain** what it is e.g. company car, company contribution to pension scheme, lunch vouchers.  
(4) Please add here holiday pay, 13th month, bonus, etc.. **Use one line per item and describe the nature of the salary component**  
(5) Following the working contract or the normal practice of the company  
(6) Standard 52 weeks for a year  
(7) As per contract, including seniority, etc. **Please explain** the number of holidays based on the normal practice of your company. The relevant information to report is the number of days of holidays for which the right was generated during the period covered by the salary, not the days actually taken during the period.  
(8) As per law, at country, region or sector level. **Please explain** of the statutory holidays according to your company  
(9) The **average** number of days of illness that can be considered as **normal** for your company  
Days for specific training in the context of the project should **not** be deducted here  
(10) Following the labour contract or the **normal practice** of the company



**ANNEX 3 – EXAMPLE OF TIME-RECORDING**

In the context of the Certification on the Methodology, full time recording per person is required. Please find below a time-sheet example fulfilling the requirements for the Certification of the Methodology.



**Timesheet**

Person : **Name**

Number of hours envisaged i.e. according to the employment contract: **xx hours/week**

**YEAR**      **MONTH**

Indicate the time in hours      Only the yellow cells are writeable

Date	1	2	3	4	5	6	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	Total	Notes		
Day	Sun	Mo	Tue	Wed	Thu	Fri	Sat	Sun	Mo	Tue	Wed	Thu	Fri	Sat	Sun	Mo	Tue	Wed	Thu	Fri	Sat	Sun	Mo	Tue	Wed	Thu	Fri	Sat	Sun	Mo				
<b>EU-Projects</b>																																		
<b>R&amp;D Activities</b>																																		
Project x			3	4	7	8								3,5			3	2	8	9	4										7	58,5	WP3	
Project y			5	5		5,5																										15,5	WP8	
Project z																																0		
Total RTD	0	8	9	7	8	5,5	0	0	0	0	0	0	0	3,5	0	0	3	2	8	9	4	0	0	0	0	0	0	0	0	0	7	74		
<b>Demonstration</b>																																		
Project x																																0		
Project y																																0		
Project z																																0		
Total Demonstration	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	
<b>Management</b>																																		
Project x												8	3,5				5			1												17,5	WP1	
Project y																																0		
Project z																																0		
Total Management	0	0	0	0	0	0	0	0	0	0	0	0	8	3,5	0	0	5	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	17,5	
<b>Other Activities</b>																																		
Project x							3									5																8	WP7	
Project y																																0		
Project z																																0		
Total Other	0	0	0	0	0	0	3	0	0	0	0	0	0	0	5	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	8	
<b>Internal activities and National Projects</b>																																		
Teaching						2,5											6	1		3												12,5		
Training																																0		
National Projects																																0		
(...)																																0		
Total	0	0	0	0	0	2,5	0	0	0	0	0	0	0	0	0	6	1	0	0	3	0	0	0	0	0	0	0	0	0	0	0	0	12,5	
<b>Absences</b>																																		
Annual Leave																									8	8	8	8				32		
Special Leave						0																										0		
Illness									8	8	8																					24		
Total Absences	0	0	0	0	0	0	0	0	8	8	8	0	0	0	0	0	0	0	0	0	0	0	0	0	8	8	8	8	0	0	0	56		
Total productive hours	0	8	9	7	8	8	3	0	0	0	0	8	7	0	5	9	8	8	9	8	0	0	0	0	0	0	0	0	0	0	7	112		
Total hours																																168		

Signed:

Approved:

Productive hours per project:	Project x	84
	Project y	15,5
	Project z	0