



Interreg South Baltic Programme 2014-2020

GENERAL PRINCIPLES on first level control

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ABBREVIATIONS

AA	Audit Authority
Central ICT system	System referred to in Article 125 (2) d) of CPR
CP	Contact Point
CPR	Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006
ERDF	European Regional Development Fund
EC	European Commission
ETC Regulation	Regulation (EU) No 1299/2013 of the European Parliament and of the Council of 17 December 2013 on specific provisions for the support from the European Regional Development Fund to the European territorial cooperation goal
EU	European Union
FLC	First Level Control / First Level Controller
GoA	Group of Auditors
ICT	Information and Communication Technology
JS	Joint Secretariat in Gdańsk (Poland)
LB	Lead Beneficiary
MA	Managing Authority
NA	National Authority
Programme Manual	Programme Manual of the South Baltic Programme
SL 2014	electronic data exchange system according to Article 122 (3) of CPR – the main application of Central ICT system
South Baltic Programme	Interreg South Baltic Programme 2014-2020

1. INTRODUCTION

The objective of this document is to provide principles of carrying out the verifications by the FLC designated by Member States in the South Baltic Programme under the provisions of Article 23 (4) of ETC Regulation and Article 125 (4) a) in connection with Article 125 (5) of CPR. Member states are recommended to follow the principles in this document, taking into their own organisational structure and control arrangements. The document covers the regulatory requirements, general principles and purpose of verifications, the bodies responsible for national first level control systems and informing on irregularities, the timing, scope and intensity of the verifications, the organisation of on-the-spot checks. Issues regarding public procurement and the functionalities of computerized system have also been covered. The document gives an overview and introduction on the organisation and process of project verification in the South Baltic Programme and tasks related to the above issues. Annexes 1, 2, 7, 8 (criteria for approbation of a FLC in decentralised system, the FLC approbation certificate, the control report from on-the spot check and the notification on irregular expenditure) attached to this document should rest unchangeable. Further annexes, the declaration of impartiality and confidentiality, checklists for administrative and on-the-spot verifications, risk analysis (annexes 3, 4a, 4b, 5, 6) may be adjusted and amended to the concrete needs and scope within the individual Member States.

Due to the different national FLC systems set in the Member States it is not possible to cover every situation in this document. More in-depth information about specific issues relevant in the context of FLC tasks can be found in other programme documents as well as EC and national regulations (see chapter 2).

The information provided in this document will be continuously further developed and updated during the implementation of the South Baltic Programme.

2. FUNCTIONS AND LEGAL BASIS OF FIRST LEVEL CONTROL IN SOUTH BALTIC PROGRAMME

In order to approve declared expenditure related to the implementation of projects within the South Baltic Programme, pursuant to Article 23 (4) of the ETC Regulation and Article 125 (4)(a) of CPR each Member State shall set up a control system making it possible to verify that:

- the co-financed products and services have been delivered,
- the expenditure declared by the partners has been paid,
- the expenditure complies with applicable law, the operational programme and the conditions for support of the operation. For this purpose, each Member State in the South Baltic Programme shall designate the FLCs responsible for verifying the legality and regularity of the expenditure declared by each partner participating in the operation. According to Article 23 (4) of the ETC Regulation, each Member State shall ensure that expenditure can be validated by FLCs within a period of 90 calendar days from the submission of the documents by the partner (the FLC is recommended to complete verification of expenditure in 60 calendar days if possible).

The verification of partner's expenditure by FLCs is the first step in the process of ensuring the approval of expenditure before the ERDF reimbursement takes place. The verifications are carried out by FLCs who have to be impartial towards the project, project activities and partners. They have to be appointed by the participating Member States for verification of expenditure that incurred by partners located on their territory. The verifications carried out by FLCs are followed up by further verifications performed by the entitled audit bodies such as AA (supported by the GoA), EC, Court of Auditors, or authorised national authorities.

The principles of financial control have been defined in this document, along with:

- CPR,
- ETC Regulation,
- Commission Delegated Regulation No 481/2014 of 4 March 2014 – (Delegated Act on Eligibility for cooperation programmes supplements the ETC regulation and provides detailed rules for staff costs, office and administrative expenditure, travel and accommodation costs, external expertise),
- South Baltic Programme approved on 23rd of September 2015,
- national guidance on the FLC system (if applicable),
- national guidance on eligibility of expenditure (if applicable).

The content, scope and the methodology of verifications carried out by the FLCs may also be described in internal control procedures of the entities appointed to carry out the control duties of the projects in the South Baltic Programme.

The FLC tasks include the following:

- verification of partner progress reports (activity and financial part)
- verification of projects on-the-spot ,
- informing the MA on irregularities,
- cooperating with the AA and external auditors during their verifications of the control system of the South Baltic Programme as well as with the NA/ other bodies responsible for establishing the national FLC systems, JS or MA with regard to the implementation of recommendations issued by the AA and external auditors also after the project completion,
- maintaining the documentation connected with project implementation in accordance with Article 140 of the General Regulation and make it available to authorised auditors during the audits.

The above should be included in the agreement or internal procedures of the appointed FLCs.

3. THE FIRST LEVEL CONTROL SYSTEM OF THE SOUTH BALTIC PROGRAMME

The FLC systems vary among the Member States that participate in the South Baltic Programme. There are two kinds of FLC systems in place:

- Poland and Sweden have set up so-called “centralized systems”,
- Denmark, Germany and Lithuania have established “decentralized systems”.

3.1. Centralised Systems (Poland, Sweden)

In the centralised FLC systems in Poland and Sweden, only specific public bodies are entitled to verify expenditure of partners located in these Member States. The FLC bodies designated by the governments are:

- **Sweden:** Swedish Agency for Economic and Regional Growth (Tillväxtverket).
- **Poland:** Voivode of the Pomorskie Voivodeship (Gdańsk), Voivode of the Zachodniopomorskie Voivodeship (Szczecin) and Voivode of the Warmińsko-Mazurskie Voivodeship (Olsztyn) are responsible for verification of expenditure of partners located in the territory of the respective voivodship¹.

Up-to-date contact details of the FLC bodies in Poland and Sweden are available at the Programme website www.southbaltic.eu. FLC is free of charge in Poland and Sweden.

3.2. Decentralised Systems (Denmark, Germany, Lithuania)

In decentralised systems in Denmark, Germany and Lithuania, FLCs are independent private audit companies or auditors chosen by the partners for carrying out the verification (see Programme Manual chapter VI. 8.1 for detailed requirements in these countries). The FLCs have to fulfil requirements with regard to their qualifications and must be approbated by the competent approbation bodies of Member State (see chapters 3.2.1. and 3.2.2. below for further information). Also national public procurement rules have to be respected when selecting the FLCs. The contracts concluded between the partner and the FLC should cover both administrative and on-the-spot checks (see chapter 2, list of FLC tasks).

The costs for FLC in Denmark, Germany and Lithuania have to be covered by the partners. They are considered eligible and, therefore, have to be included into the project budget.

3.2.1. Approbation of First Level Controllers in decentralised systems

After partners have chosen FLCs in line with national public procurement rules (please see chapter VI. point 8.1 in Programme Manual for detailed information on set requirements in each Member State) FLCs have to be approbated by the responsible national body (see chapter 3.2.2. for contact details). Only approved FLCs are entitled to approve partner progress reports in the South Baltic Programme.

The approbation procedure involves the following steps:

1. The partner proposes the selected FLC to the responsible Approbation Body in the Member State by submitting the filled-in *Checklist with criteria for the approbation of a FLC* (annex 1) If it is required by national rules additional documents are attached to the checklist (e.g. a checklist and documents related to public procurement procedure, subsidy contract and application form). It is recommended to start the contracting and approbation process of the FLC as soon as possible. The approbation procedure should be finalised by the end of the first reporting period at the latest. Please note that only the approbated FLC can receive an access to SL 2014.
2. The Approbation Body verifies the qualification and independence of the FLC based on the information provided in the checklist(s) according to the requirements set by the South Baltic Programme and the Member State;

¹ In Poland Technical Assistance of CP is also verified by the Voivodeship Offices.

3. The Approbation Body confirms the positive assessment of the FLC qualification and independence by issuing the *FLC Approbation Certificate* (see annex 2). In the case of approbation, the project partner submits the copy of FLC Approbation certificate to the LB and keeps the original document.
4. The approbation bodies in the Member States deliver the list of approbated FLCs to the MA and the JS and inform on any changes to it (if new FLCs are approbated) before the end of each reporting period. The list is sent to the MA and the JS to confirm that the expenditure is verified only by the approbated FLCs from the aforementioned list and to enable the MA to give the approbated FLC an access to SL2014.
5. Should the proposed FLC be rejected or changed, the respective LB/partner has to select a new FLC and start the approbation procedure again following programme's and national requirements.

3.2.2. Approbation bodies

The following Approbation Bodies were assigned on the national levels in decentralised FLC systems:

Denmark:

Region Zealand

Alleen 15

DK-4180 Sorø

Denmark

(responsible for approbation of FLC of partners located in Region Zealand)

Regional Municipality of Bornholm

Ullasvej 23

DK-3700 Rønne

Denmark

(responsible for approbation of FLC of partners located on Bornholm)

Partners located outside the eligible area are kindly asked to contact one of the bodies in order to identify the responsible body

Germany:

Ministry of Economics, Construction and Tourism Mecklenburg-Vorpommern

Unit 250 European Territorial Cooperation INTERREG

Johannes-Stelling-Straße 14

19053 Schwerin

Germany

Partners located outside the eligible area are kindly asked to contact the authority mentioned above in order to identify the responsible body.

Lithuania:

Ministry of the Interior of the Republic of Lithuania

Regional Policy Department

Šventaragio str. 2

LT-01510 Vilnius

Lithuania

4. CENTRAL ICT SYSTEM AND THE ELECTRONICAL EXCHANGE OF DOCUMENTS AND INFORMATION

4.1. General information

In the 2014-2020 perspective, as a rule, the exchange of documents and information related to the project implementation among the partners and programme institutions is conducted electronically via a system designed for this purpose. Partners, LB and the FLC have an obligation to use the ICT system.

The detailed information on how to use the system, its functionalities and technicalities is to be included in a separate document *User manual on working in the SL2014*.

The Central ICT System comprises of:

- SL2014,
- identity management system,
- reporting application (enables generating reports with data gathered in SL 2014).

4.2. SL2014

The SL2014 ensures among others:

- support for ongoing management, monitoring and evaluation of the Programme,
- collection and storage of data from subsidy contracts, partners' and project progress reports as well as data on the verification and approval process of progress reports..

The SL2014 ensures different processes and communication among partners, FLCs and the JS, in particular in terms of:

- collection and transfer of data on partners' and project progress reports, their approval, amendment, rejection or withdrawal,
- collection and transfer of data on financial schedules, their verification, including approval, amendment or withdrawal,
- collection and transfer of data on public procurement and contracts awarded in line with the programme and national tendering rules,
- for partners and LBs to submit their reports using a dedicated functionality, i.e. application for the progress report processing.

The access to the data stored in the SL2014 is being granted to:

- employees of institutions participating in the implementation of the Programme, i.e. among others the MA, JS, FLC, NA/ other bodies responsible for establishing the national FLC systems, AA, to the extent necessary for the proper performance of their tasks,
- partners and LBs, and persons they authorise to manage projects on their behalf.

4.3. Identity management system

The identity management system ensures coherent and secure identity management of users of the central ICT system who are employees of institutions involved in the Programme implementation system.

4.4. Reporting application

This application allows to create certain reports - based on the data entered into the SL2014, inter alia, the information on the level of EU spending under the Programme, expenditure forecasts, information on implementation of the Programme, information on the administrative verifications and one-the-spot checks etc.

In order to use the central ICT system, FLCs do not have to install any special software. However, they must have access to the Internet. The main application of central ICT system - SL2014 is available via the following web browsers: Mozilla Firefox, Internet Explorer and Google Chrome.

4.5. Responsibilities of First Level Controllers with regard to work in SL2014

4.5.1. Appointment of authorized persons

In decentralised systems the information on persons entitled to work in SL 2014 comes from the list of approbated FLCs (see chapter 3.2.1) and in centralised system in Sweden from the persons who will perform the control tasks in Tillväxtverket. In Poland the Voivodes are responsible for sending the list of employed FLCs in accordance with the concluded agreement. The process of giving the authorisation to the proposed persons to work in the SL 2014 and changes of those persons is described in *User manual on working in the SL2014*. The document is sent electronically to the approbated FLCs by the MA.

4.5.2. Work in the system

In principle the SL2014 is used to support partners, FLCs, the JS and the MA in carrying out their tasks.

The FLCs² use the system to:

- carry out administrative verification of the partner progress report by:
 - a. informing the LBs/partners of a sample of expenditure for verification, unless 100% check of expenditure is performed,
 - b. withdrawing expenditures, asking for corrections / additional information by the correspondence channel,
 - c. approving the partner progress report,
 - d. informing the LBs/partners on results of the administrative verification including the results of the ex-post procurement (list of expenditure that were not approved with the justification).
- registering the results of on-the-spot checks (control reports)

Detailed description of the method of performing the above mentioned tasks is presented in *User manual on working in the SL2014*.

5. KINDS OF VERIFICATIONS

In accordance with Article 125 (5) of CPR the FLCs work includes:

- administrative verifications
- on-the-spot checks.

5.1. Tasks and scope of the verifications

Based on the invoices or other documents with equivalent value of proof, both during the administrative and on-the-spot checks, the FLCs verify the following aspects with respect to the project implementation:

- if the products and services co-financed have been delivered,
- if expenditure declared by the partner is in line with the approved Application Form, the Subsidy Contract and the Partnership Agreement,

² In regard to the decentralised FLC system in Mecklenburg-Vorpommern FLC may perform their tasks on basis of the list of expenditure provided in SL2014 and by verifying the paper versions of supporting documents upon the agreement with the partner and with respect to the applicable international audit standards.

- if the partner progress report provides accurate information regarding the activity and financial progress of the project,
- if supporting documents to the partner progress report are correct (if there are documents proving the expenditure, invoices or other documents with equivalent value of proof, bank account statements, delivery notes, copies of contracts with service contractors),
- if invoices and other financial documents with equivalent value of proof are correctly described and whether they correspond with the expenditure paid out,
- if eligibility rules have been respected (in particular whether the expenditure has been incurred within the eligibility period in relation with activities described in the Application Form, whether the programme and EU rules on eligibility of expenditure have been respected, double financing has not occurred),
- if the expenditure is essential for project implementation, and in compliance with the national and EU rules (in particular with public procurement and fair competition, environment protection, state aid, equal opportunity as well as publicity and information requirements described in the Programme Manual),
- if the amounts of the expenditure seem to follow sound financial management and are in line with principles of economy, efficiency and effectiveness,
- if conditions for payments have been fulfilled for simplified cost options;
- if the partner and other entities engaged in the project implementation maintain a separate accounting system or adequate accounting code for all transactions relating to the project without prejudice to national accounting rules,
- if an adequate audit trail exists,
- if LB fulfils the obligation regarding the transfer of funds to the partners like specified in Art. 13 (3) of the ETC Regulation (applicable for the FLC of LB only)

In the case of flat rate financing, where applicable, the FLCs should also check whether:

- expenditure has been correctly allocated to a given category,
- there is no double declaration of the same expenditure item in different budget categories,
- the flat rate has been correctly applied (it also refers to 0-reports),
- the amount charged based on flat rate has been proportionally adjusted in case the value of the category of costs to which it was applied had been modified.

Moreover during the administrative verification the FLCs check in particular that:

- 1) the partner progress report was submitted within the required deadlines specified in the programme,
- 2) the partner progress report has been properly completed and covers the adequate reporting period,
- 3) the partner progress report is correct with regard to the accounting part and was submitted by a person authorised by the beneficiary,
- 4) the partner progress report illustrates the progress of the project, including the implementation of indicators (if the partner is responsible for the implementation of a specific indicator).

5.2. Documents required for verification

Verification of expenditure of partners is carried out based on the following documents:

- Application Form,
- Partnership Agreement,

- Partner progress reports including the list of expenditure (including 0-report contains only preparation costs).

In addition verification is carried out on the basis of following documents proving the eligibility of expenditure:

- Invoices or other documents with equivalent value of proof for example payslips including the amount eligible for the calculation of an expenditure in the project,
- Contracts signed with contractors (including the annexes),
- Delivery notes (for example a protocol of reception of products and services),
- Documents proving the payment (a bank transfer, a bank abstract or a warrant),
- Job descriptions or timesheets with a description of activities performed by the staff,
- Employment contracts, payslips, calculation of salary and/or hourly rate,
- Documents on the public procurement carried out in compliance with national and community provisions,
- Statements of account reflecting the exchange of the amounts declared in national currency into euro,
- Other documents necessary for verification of expenditure, for example information on eligibility of VAT,
- Other documents required by the FLC.

5.3. Administrative verifications

The partner progress report presents the activities and the list of expenditure of one partner for the given reporting period.

Partner progress reports have to be compiled by all partners, including the LB. In justified cases, in particular in the case of system failure confirmed by the MA, it can be possible to verify the partner progress report submitted to the FLC in paper version. In this case the project progress report may be submitted to the JS in paper version as well.³ The MA provides partners with the template of these reports on the Programme website.

After removing the cause of failure the missing information is immediately included or updated in the SL2014 by all the system users.

5.3.1. Sequence and timing of administrative verifications

In the South Baltic Programme, progress reports have to be compiled and verified twice a year, covering activities and expenditure of 6-months reporting periods. The project specific reporting periods as well as the deadlines for the submission of the progress reports are clearly laid down in the Programme Manual.

Project implementation is divided into 2 cycles of 6-month reporting periods:

Cycle 1:

- from 1 January to 30 June + 120 calendar days for reporting deadline to the JS;
- from 1 July to 31 December + 120 calendar days for reporting deadline to the JS;

Cycle 2:

- from 1 April to 30 September + 120 calendar days for reporting deadline to the JS;
- from 1 October to 31 March + 120 calendar days for reporting deadline to the JS;

Reporting cycles will be applied in rolling order (1st Call - Cycle 1; 2nd Call - Cycle 2; 3rd Call - Cycle 1; etc.).

³ Provided it was not possible to complete the data in SL2014

The process of preparing the reports and confirming expenditure by FLCs has to be organised within these time frames in order to keep up with the programme requirements imposed by the Article 23 (4) of the ETC Regulation.

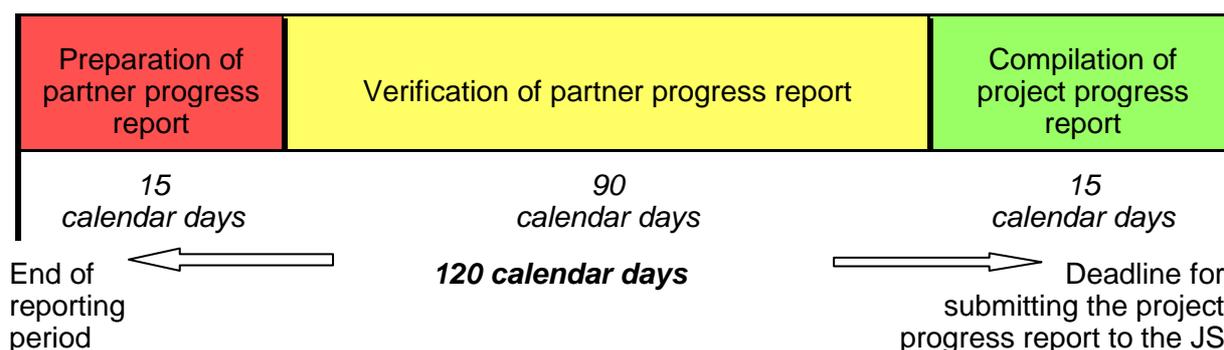
There might be exceptions from the afore-mentioned cycles as well as to the reporting periods:

- a) when - based on the Subsidy Contract provisions - either the MA or the partners explicitly require an additional progress report to be submitted or
- b) when – based on the Programme Manual chapter 7.1 (subpoint “Reporting periods”) a **0-report**⁴ containing only preparation costs is submitted.

The obligatory deadlines for proceeding the progress report are as follows:

- The partner submits the partner progress report for verification to the FLC within 15 calendar days after the end of reporting period (in the case of 0-reports within 3 months from signing the Subsidy Contract))The partner progress report is submitted via SL2014 (with exceptions described in 5.3 and 5.3.2 points);
- In accordance with EU regulations the FLCs have 90 calendar days to complete verification of the **partner progress report**. However, in order to allow timely submission of the project progress report to the JS, the FLC is recommended to complete verification of **partner progress reports** in 60 calendar days (if possible) in order to facilitate a smooth reimbursement process. Bearing in mind the technical character of approving 0-report which base on a lump sum only, the FLC is encouraged to finalize the confirmation of the lump sum amount within 30 days from its submission. To support the verification process, partners should keep the necessary documentation to the partner progress report ready for submission to the FLC. It will allow to provide immediately the FLC with the requested documents.
- The compilation of the **project progress report** and submission to the JS in SL2014 has to be done until 120 calendar days after the end of the reporting period (in the case of 0-report it is recommended to finalize the process within 40 days after its submission to the FLC). It is recommended that the LB schedules 15 calendar days (7 calendar days in the case of 0-reports) for compiling the project progress report after partner progress reports are approved by the FLCs.

Figure 1: Timing and sequence of administrative verifications for Progress Reports



5.3.2. Steps to be taken by FLCs

Before starting the control tasks the FLC in Poland should sign the *Declaration of impartiality and confidentiality*, constituting annex 3. In Sweden the impartiality of the FLC is ensured by

⁴ So called 0-reports are not obligatory, partners however have option to certify the preparation costs already after the subsidy contract has been signed (see Chapter 7.1 of the Programme Manual “Reporting periods”). In the South Baltic programme only a simplified calculation method, i.e. a lump sum, for the preparation costs is allowed.

requirements set in national legislation (Förvaltningslagen (1983:223))⁵. In decentralised systems the FLC confirms its impartiality and independence from project activities by signing annex 1.

As a rule the FLCs carry out the verifications on electronic version of invoices or accounting documents of equivalent probative submitted by the partner in SL2014⁶

The FLC may decide to carry out an administrative verification based on paper versions of documents confirming the incurred expenditure if:

- preparation of the electronic version of the document, because of its size, is particularly burdensome for the partner (e.g. construction documentation, extensive acceptance certificates, comprehensive public procurement documents etc.),
- the quality of the electronic version of the document does not allow for detailed and appropriate verification of the expenditure,
- it is possible or (and) FLC decides that it is necessary to carry out the verification of the document during the on-the-spot check instead of the administrative verification.

In coordination with the project partner the FLC may organise the verification relating to 100% of the expenditure items declared in the list of expenditure or on the basis of a sample on the expenditure items declared in the list of expenditure. The FLC informs the partner on the expenditure selected for verification.

Before informing the partner on the results of the verification the FLC explains the questioned expenditure and/or asks for additional documentation. The time given to the partner for explanations does not suspend the time limit established in the programme for the FLC for the verification of expenditure.

The FLC approves the partner progress report and informs the partner on the result of the verification in the SL2014.

In exceptional cases if the partner is not able to deliver necessary explanations and additional documents proving the eligibility of expenditure as part of the clarifications to the FLC within the set deadline, the FLC deems those expenditure ineligible in a given reporting period and finalises the work (accepts only the expenditure that was not questioned). Related expenditure after final examination and approval by the FLC can be claimed in the next reporting period. In the case of Polish partners it may concern the expenditure that is the subject of the complaint procedure.⁷ However, this rule does not refer to the final report submitted by the partner.

As a rule the FLC approves the partner progress report in SL2014 by giving his/her electronic acceptance and informs the partner on results of the verification (including the information on ineligible expenditure). Information on the excluded expenditure should be provided to the partner through the SL2014 and included in the checklist. If the verification of expenditure has been carried out based on the sample the FLC should describe the applied sample method in the checklist.

In order to facilitate and document the verification process, the MA has prepared a template of the checklist for administrative verification (see annex 5). The questions in the checklist include sections that should be covered by the administrative verifications performed by all FLCs. The FLCs are recommended to make a necessary adjustment of the checklist with regard to the national provisions and in respect to the FLC system.

⁵ It specifically states that the administrators cannot handle any matter where they are not impartial.

⁶In regard to the **decentralised FLC system in Mecklenburg-Vorpommern** FLC may perform their tasks on basis of the list of expenditure provided in SL2014 and by verifying the paper versions of supporting documents upon the agreement with the partner and with respect to the applicable international audit standards.

⁷ The complaint procedure in case of **Polish partners** will be launched after approving the documents in SL2014.

5.3.3. Applying a sampling method⁸⁹

Verification of the supporting documents such as invoices and other documents with equivalent value of proof may be carried out, where justified, on the basis of a sample of transactions.

FLCs may use the sampling method approved in their institution or provided by the NA /other body responsible for establishing the FLC system. In the case of sampling, the controls must be comprehensive in relation to the various expenditure categories and take account of all statistic methods. It is recommended that basic sample includes a minimum of 10% of the amount of expenditure declared in the partner progress report (however not less than 5 single items) and at least one expenditure from each category. The FLC should analyse the chosen sample in order to assess:

- if it includes expenditure which amount considerably exceed the average amount of all declared expenditure,
- if verification of selected expenditure provides reasonable assurance that other items of the population are free from errors/irregularities (e.g. identified during previous administrative or on-the-spot checks of the project).

A reasonable assurance does not mean the absolute assurance, however it can be sufficient to conclude that based on the sample the rest of the expenditure items is also not affected by errors/irregularities. If the FLC detects any errors/irregularities in the chosen basic sample that may have an impact on other expenditure out of the sample, he/she determines the size of the complementary sample based on the professional judgment. The assessment of the detected findings should also include information if they result from the management and control system (systematic nature of findings). In this case the FLC describes it in the comments to the checklist and notifies it immediately to the MA by sending the checklist as scan via e-mail.

It is recommended that FLC review annually the developed sampling method taking into account the size of the sample and different type of partners and projects. The verification of expenditures with regard to public procurement is carried out regardless of the chosen sample.

The applied sample method is always documented by the FLC, in particular as regards:

- population,
- random method,
- list of expenditure randomly selected in the basic sample,
- list of expenditure randomly selected in the complementary sample,
- justification for complementary sample.

The documentation stays at the FLC and has to be made available upon request of the authorised audit bodies as well as the MA/JS. The FLC should describe the sampling method and specify the expenditure that was selected for the sample in the checklist for the purpose of the external audits.

In case the verification is carried out on a sample, partners have to submit to the FLC the supporting documents for the expenditure from the sample.

5.4. On-the-spot checks – steps to be taken by FLC

On-the-spot checks complement the administrative verifications. Their purpose is to further minimise the risk of irregularities. They should focus in particular on reassuring administrative verifications in terms of the reality of deliverables, the accounting systems in place as well as the processes and procedures in the partner's organisations. On-the-spot checks may also include visiting the events organized by partners such as conferences or trainings (however

⁸⁹ In **Lithuania**, it is not possible that FLCs apply a sampling method, because the verification has generally to be based on 100% of the supporting documents according to national regulations. The provisions of the following chapter, therefore, do not apply for Lithuanian FLCs.

⁹⁰ In **Mecklenburg-Vorpommern** sampling is used only in justified cases and in compliance with the international audit standards.

these visits are additional verifications not replacing the FLC task to perform the on-the-spot check in the project).

In contrast to administrative verifications, not all projects and partners should be the subject to on-the-spot checks. The FLC of each partner may decide on the necessity of on-the-spot check on the basis of risk analysis for the type of the partners and the projects concerned.¹⁰. In case of “seed money” projects, on-the-spot checks are carried out before the Request for payment is approved.

In order to provide a reasonable assurance as to the legality and regularity of the expenditure, the risk analysis should refer to project-related criteria (e.g. the amount of ERDF budget, the amount of expenditure calculated by flat rates, the participation of the partner in other projects etc.), partner-related criteria (e.g. type of the partner, previously detected irregularities on the side of the partner, type of expenditure and activities of the partner etc.) as well as the experiences and results from administrative verifications and external audits (e.g. high number of items considered ineligible, quality of the documentation provided by the partner, expenditure identified during the desk-based verifications appearing unusual and requiring further examination, irregularities detected by second level controls etc.). The example of the risk analysis for regular projects is given in annex 4a and for “seed money” projects – in annex 4b. On-the-spot checks may be carried out on a sample of documents. The FLC decides if whether to verify 100% of the documents or use a sample based on e.g. the results of the previous administrative verifications. The sample of expenditure items should be described in the checklist for on-the-spot check, the risk analysis for projects to be carried out during on-the-spot checks should be described in the control report.

The procedure of on-the-spot checks should be based on international audit standards. The partner should be informed by the FLC in advance about the date of a planned on-the-spot check and about the legal basis for the concerned verification.

In order to facilitate and document the verification process, the MA has elaborated a standard checklist for on-the-spot check (see annex 6) and recommends that it is used and filled in by the FLC both in centralised and decentralised FLC systems. However, the FLCs are free to use their own or national checklists alternatively.

As soon as the verification is accomplished, the FLC draws up a *Control Report* (see annex 7) with recommendations for improvements. The signed *Control Report* is registered in the SL2014 by the FLC. If irregularities are detected during the on-the-spot check the FLC makes recommendations and sets a time for their implementation by the partner (for further information see chapter 5.5.1).

In decentralised systems the cost of the on-the-spot check is considered eligible. Partners from decentralised FLC systems have to include on-the-spot checks in the service contracts with the selected audit companies or auditors.

In the case of receiving the information on irregularities in the project or a reasonable suspicion of irregularities the FLC can perform additional on-the-spot verification regardless of the fact that one on-the spot check has already been carried out.

The aim of such a verification (so called “ad hoc” check) is to verify the received information or suspicion on irregularities in reality and confirm if there are facts that may lead to consider the expenditure as ineligible.

¹⁰ In regard to the **decentralized FLC system in Mecklenburg-Vorpommern**, at least one on-the-spot check is obligatory if the FLC carries out administrative verifications by applying a sampling method. In case 100% of the expenditure is checked during the administrative verifications, an on-the-spot check is obligatory only if a Partner has a total eligible budget of 200.000 EUR or more. These thresholds, however, do not exempt FLCs from carrying out on-the-spot checks in case it is necessary for ensuring the verification of costs. In this particular case, the necessity of on-the-spot checks has to be determined on the basis of a risk analysis. If on-the spot-checks are to be carried out, the timing, number and concrete scope of the on-the spot checks is to be decided by the FLC in each concrete case with reference to identified risks. The International Standards of Auditing provide a sound orientation for carrying out the controls (www.ifac.org).

In **Lithuania** and **Denmark** at least one check on the spot shall be carried out within the life time (implementation) of the project by the FLC.

The procedure for carrying out the verification is the same as for on-the-spot check except the deadline for informing the partner about the control visit.

5.5. Procedure and timing of on-the-spot checks¹¹

The purpose of on-the-spot checks is to ensure correctness of the implementation of the project as well as the correctness of verification of delivery of products and services co-financed. They have to be carried out by the appointed FLCs that decide on the timing and intensity of on-the-spot checks, if applicable with reference to the national requirements (see chapter 3.2).

FLCs should set the time and the number of the verifications taking into account the indicative project timetable and the level of the projects spending in order to achieve the maximum effectiveness and efficiency during the verification process. The scope and intensity of on-the-spot checks shall depend on the nature of the project in the programme (or priority/specific objective) and the type of the documentation that is provided by the partner. Alternatively, a random representative sample could be selected. Where problems are identified during the verification carried out on a sample of projects the size of the sample of the population should be increased in order to determine whether similar problems existed in the previously unchecked projects. The FLC should be in position to demonstrate, through adequate documentation of the verifications carried out, that the intensity of on-the-spot checks is sufficient to give reasonable assurance of the legality and regularity of the expenditure and projects co-financed under the South Baltic Programme.

On-the-spot checks may be carried out either during the implementation or upon the completion of the project, or both during and upon the completion of the project. It has to be taken into account that it may be too late to effect any necessary corrective action if an on-the-spot check is carried out when the project has been completed. With regard to that, it is recommended the FLC considers carrying out an on-the-spot check upon the following three conditions:

- timing of the control activities is the most effective taking into account the project implementation and
- the partner presented for a verification at least 25% of the total amount of expenditure from the partners budget and
- the on-the-spot check will take place no later than before approval of the final report by the FLC.

5.5.1. Follow up verification of on-the-spot check¹²

If the on-the-spot check resulted in reservations and recommendations for the further project implementation, the FLC is obliged to verify whether the proposed measures have been implemented by a so-called follow up verification.

That means that the FLC sets a deadline for the partner to implement the recommendations. After this deadline, the FLC verifies if the issued recommendations have been implemented. This can be done either within the scope of another on-the-spot check or an administrative verification, depending on the nature of findings and proposed measures. As a rule, the follow-up verification of the measures to be implemented by the partner should take place within 2 months since the day of issuing the recommendations at the latest, but no later than before the next regular administrative verification.

Afterwards, the FLC registers the information on the results of follow up verification in SL2014.

¹¹ Only limitedly applicable to the **decentralised FLC system in Mecklenburg-Vorpommern**; see specifics for Mecklenburg-Vorpommern in chapter 5.4.

¹² Only limitedly applicable to the **decentralised FLC system in Mecklenburg-Vorpommern**

5.6. Verification of compliance with principles of public procurement and competitiveness

Whenever a project purchases services, goods, equipment, etc. externally, public procurement rules must be adhered to, including European public procurement rules and the relevant national rules.

Verifications should be carried out not later than with the first expenditure that has been incurred under public procurement and is declared by the partner in the partner progress report. It is very important that the public procurement procedures were carried out honestly, fairly, and in a manner that secures best value for public money. This is in line with EU Treaty principles and EU Directives on public procurement. Essential principles to be observed in conducting the procurement procedure include non – discrimination, equal treatment, transparency, mutual recognition, proportionality, freedom to provide service and freedom of establishment.

In order to ensure the quality of public procurement procedure the FLC or an external or internal public procurement specialist may perform upon the partner's request an ex-ante verification of the public procurement before the procedure is initiated by the partner¹³ Such a procedure takes place in Poland only upon the request of the partner. An ex-ante verification is rather a preventive measure which aims at avoiding the potential findings and negative effects of possible infringements of the provisions of public procurement. This should ensure that problems with the initial tendering as well as additional works / supplementary contracts during the project implementation are eliminated. The FLC, however, does not take the responsibility for further proceeding with the public procurement by the partner's institution. Positive results of the ex-ante verification do not exclude the possibility of issuing reservations on the level of the ex-post verification of the public procurement.

Public procurement and/or competitiveness rules should be based on detailed questions on application of national rules. The FLC may prepare a separate checklist or add the questions to the administrative checklist. The checklist should reflect all FLCs' comments to the procurement procedure and indicate the amount of detected irregularity. The previous verification of the public procurement carried out by other external control bodies should be taken into account.

Due to the fact that major irregularities detected in projects concern public procurement, during verifications of expenditure the FLC should take into account the most frequent irregularities in the application of public procurement procedures detected in projects with EU co-financing (see Annex 1 of the Programme Manual). In the case of detecting irregularities, FLCs apply national rules on financial corrections¹⁴ or (if national rules are not set) Commission Decision of 19.12.2013 *on the setting out and approval of the guidelines for determining financial corrections to be made by the Commission to expenditure financed by the Union under shared management, for non-compliance with the rules on public procurement* (C (2013) 9527 final).

The information on the verification of compliance with the public procurement law is communicated to the partner in SL2014 by the FLC.

5.7. Informing on irregularities detected by the First Level Controller

The term irregularity is defined according to Art. 2 (36) of CPR as follows: *any breach of Union law, or of national law relating to its application, resulting from an act or omission by an economic operator involved in the implementation of the ESI Funds, which has, or would have, the effect of prejudicing the budget of the EC by charging an unjustified item of expenditure to the budget of the EC.*

¹³ Ex ante verification of public procurement is not applicable in **Sweden**. In **Lithuania** ex-ante verification of the public procurement is initiated by the partner and is used in case such agreement in service contract is set or mutual agreement between service contract parties is reached.

¹⁴ In **Poland** the following legal act is applied: Ordinance of the Minister of Economic Development conditions for lowering the value of financial corrections and expenditure incurred incorrectly with regard to the award of contracts of 26 of January 2016 (*Rozporządzenie w sprawie warunków obniżania wartości korekt finansowych oraz wydatków poniesionych nieprawidłowo związanych z udzielaniem zamówień*).

In case the FLC of the partner assumes or detects an irregular expenditure, after the partner progress report has been approved, the FLC is obliged to immediately inform the MA and send the *Notification on irregular expenditure* (annex 8) both as a scan version to the following e-mail address: kontrola@mr.gov.pl and the paper version to the following address:

Territorial Cooperation Department
Ministry of Investment and Economic Development
ul. Wspólna 2/4
00-926 Warsaw, Poland

The electronic copy of the notification should be also forwarded to the JS and the NA responsible for reporting the irregularities to the EC according to art. 122 of CPR.

The MA will ascertain if the procedure of recovery of undue payments needs to be applied.

The MA will inform the FLC via e-mail as well as the JS and the NA/other bodies responsible for establishing the national FLC systems on the status of the expenditure (if it has already been refunded or not and if it has been part of a payment claim to the EC or not). In case the payment has not been released, the MA informs the FLC about possible way of proceeding. In case the payment has been released and the expenditure has to be recovered, the expenditure is treated as an irregularity. It should be notified to the EC if it exceeds 10 000 EUR. As a rule the MA asks the LB to repay the irregular amount based on the issued call for payment. Upon the request of the partner and in accordance with the Subsidy Contract provisions, the MA may, however, reduce the amount of the irregularity from the reimbursement of ERDF for the project.

6. THE ROLE OF FLC IN AUDIT PROCESS (SECOND LEVEL CONTROL)

If irregularities are detected by auditors the FLC may be involved in the process of explaining the findings within the contradictory procedure. The contribution of FLCs in formulating remarks/comments on findings during the contradictory procedure is of crucial importance and has a positive impact on the reduction of Programme's error rate. The FLC may be asked for clarifications on detected irregularities directly by the auditors in charge.

However the MA on the level of the draft of the annual control report issued by the AA may also need an up-to-date confirmation or information that:

- the contradictory procedure has been finalised with the auditor
- the FLC will not present new or further objections against the audit result.

If FLC keeps rejecting the opinion of auditors the MA will not confirm the irregularities to the AA. The position of the FLC along with eventual additional argumentation will be forwarded by the MA to the AA and presented to the GoA. It will be verified if the irregularity is still a subject to ongoing bilateral procedures between the FLC and the auditor in charge.

If the AA includes the irregularity in the annual control report the FLC prepares the notification on irregular expenditure (see chapter 5.7) even if the clarification process with the auditor in charge is ongoing. The FLC verifies if any other expenditure of the concerned partner is also affected by the same type of irregularity detected by the auditors and consequently reports on the total amount of the irregularity. The notification will serve the MA for issuing the request for payment.

The same approach shall apply during the audits carried out by the EC or other authorised institutions such as the Court of Auditors.

The MA informs the AA (and if applicable the EC) on implemented follow-up measures and the irregular amounts recovered.

7. FACILITATION AND MONITORING OF THE CONTROL PROCESS

A smooth functioning of the FLC requires that the involved parties not only fulfil their respective tasks as defined in this document, but also cooperate efficiently. This implies especially a proper coordination, communication and information among them. In general, the MA/JS highly recommends the FLCs to attend seminars, workshops or other meetings organised on specific topics such as public procurement, state aid etc. carried out on:

- national level (seminars/trainings available in Member State)
- Programme level (seminars/workshops mainly for the projects partners and /or FLCs)
- EU level (events organised for example by Interact or EC services),

7.1. FLCs and the JS as advisors for partners in eligibility issues

Most problems and discussions concerning the eligibility of expenditure should be solved with the support of the JS and the FLCs. For the programme rules the JS should be addressed with certain questions while in the case of interpretation of the national rules FLCs or NAs should assist the partners. In some institutions responsible for issuing the legislative acts may also be asked by partners/ FLCs for interpretation of national provisions when the eligibility of expenditure is questioned with regard to specific national regulations.

The SL2014 will provide a separate module dedicated to the exchange of correspondence between partners and their FLCs, as well as to exchange correspondence between LBs and the JS. It will be possible to keep contact with the relevant institutions, send comments to progress reports etc. All correspondence will be visible in the system with regard to the implemented project in order to provide the audit trail.

7.2. Support and coordination by Programme bodies

Effective FLC systems and processes with no control delays at the level of all participating Member States will be a key factor for the financial performance of the projects and the South Baltic Programme as a whole. In order to assure this, programme bodies implement the following coordination, monitoring and information measures:

- The FLCs performance is coordinated by the NA/ other body responsible for setting up national financial control systems in a given Member State.
- Regular training seminars or individual consultations may be organised at programme and national level in order to provide the FLCs with the necessary information on the implications of a control system.

LIST OF ANNEXES

Annex 1:	Checklist with criteria for the approbation of a FLC in a decentralised system
Annex 2:	FLC Approbation Certificate
Annex 3:	Declaration of impartiality and confidentiality
Annex 4a:	Sample of risk analyses – regular projects
Annex 4b:	Sample of risk analyses – “seed money” projects
Annex 5:	Checklist for administrative verification
Annex 6:	Checklist for on-the-spot check
Annex 7:	Report on the result of the on-the-spot check
Annex 8:	Notification on irregular expenditure

SUMMARY OF THE DOCUMENTS TO BE CREATED IN THE FIRST LEVEL CONTROL PROCESS AND THEIR CIRCULATION

Document	To be prepared by	To be signed by	Original(s)	Copies	for further information see
<i>Checklist with criteria for the approbation of a First Level Controller</i> annex 1	Partner in cooperation with the FLC (decentralised FLC system)	FLC of the Partner to be controlled <u>and</u> Partner	1 original to be created: - 1 original to be sent by the Partner to the national approbation body and stays there	1 copy of the signed documents to be created: - 1 copy stays at the Partner	chapter 3.2.1. of this document
<i>First Level Controller Approbation Certificate</i> annex 2	National approbation body (decentralised FLC system)	National approbation body	Up to 2 originals to be created: - 1 original to be sent by the national approbation body to the Partner - 1 original stays at the national approbation body (optional)	2 copies of the signed document to be created: - 1 copy of the signed document stays at the national approbation body (if no original is created for this purpose) - 2 copies to be created by the Partner and forwarded to the LB, one of them further on by the LB to the JS	chapter 3.2.1. of this document
<i>Declaration of impartiality and confidentiality</i> annex 3	FLC of the Implementing Partner (Poland)	FLC of the Implementing Partner	- 1 original which stays at FLC (not valid to decentralised systems)	-	chapter 5.3.2. of this document
<i>Sample of risk analyses</i> annex 4a – regular projects annex 4b – “seed money” projects	FLC of the Partner (optional)	FLC of the Partner	to be created 1 original stays at FLC (to be described in the control report for on-the-spot checks)	-	chapter 5.4. of this document
<i>Checklist for administrative verification</i> annex 5	FLC of the Partner	FLC of the Partner	1 original to be created - 1 original stays at FLC	scan version to be uploaded in the SL 2014 (optionally)	chapter 5.3.2. of this document

<i>Checklist for on-the-spot verification</i> annex 6 or own template	FLC of the Partner	FLC of the Partner	1 original to be created - 1 original stays at FLC	scan version to be uploaded in the SL 2014 (optionally)	chapter 5.4. of this document
<i>Control Report for on the on-the-spot check</i> annex 7	FLC of the Partner in dialogue with the Partner controlled	FLC of the Partner <u>and</u> Partner	2 originals to be created: - 1 original stays at the FLC - 1 original stays at the Partner	to be uploaded in the SL 2014	chapter 5.4. of this document
<i>Notification on the irregular expenditure</i> annex 8	FLC of the Partner	FLC of the Partner	1 original to be created 1 original to be sent by the FLC of the Partner to the Managing Authority (both in paper and scan version)	2 copies of the signed documents to be created: 1 copy to be sent as scan by the FLC of the Partner - to NA and JS - 1 copy stays at the FLC	chapter 5.7. and 6. of this document