

Duty of care

You suggested explicitly stating in the engagement that “*the European Commission can rely on the report and use it even though they are not signing the engagement letter*”. Such statements have been incorporated in the final model Terms of Reference and the Independent Report of Factual Findings of the respective certificates¹ (attached to the present letter).

Assurance versus Agreed-Upon Procedures

You suggested including in the document ‘*a statement noting the limitations of such procedures like ‘as this engagement is not an assurance engagement, the auditor does not provide an audit opinion or a statement of assurance’ (ISRS 4400 paragraph 18 (j))’ or ‘a statement that had the auditor performed additional procedures, an audit or a review, other matters might have come to light that would have been reported’.*

Such references clarifying the auditor’s responsibility and scope of the engagement have been incorporated in the certificates² (see attachments).

You also pointed out that in the draft documents ‘*there are items which ask for an opinion or a positive statement (which is assurance) rather than a statement of factual findings (which results from agreed-upon procedures*’ and add that “*certain of the detailed procedures appear to expect that the auditor uses his/her professional judgment and concludes. In agreed-upon procedures, the auditor should not and does not conclude. It is up to the users of the report to assess for themselves the procedures and findings reported by the auditor and draw their own conclusions from the auditor’s work*”. As you may see from the final versions of the certificates the auditor’s responsibilities have been clearly limited to an agreed-upon-procedure (see paragraph above). The applicable standards to be applied by the auditor are stated in the Terms of Reference of the respective final certificates³. Should the certifying

¹ ‘The [Commission] [Agency] is mentioned as a signatory of the Agreement with the Beneficiary only. The [European Union][Euratom][Agency] is not a party to this engagement’ (see Terms of Reference);

‘The Procedures were carried out solely to assist the [Commission] [Agency] in evaluating whether the [Beneficiary’s] [Linked Third Party’s] costs in the accompanying Financial Statement(s) were declared in accordance with the Agreement. The [Commission] [Agency] draws its own conclusions from the Report and any additional information it may require’ (see Independent Report of Factual Findings regarding the CFS);

‘The information provided through the Statements, the Procedures and the Findings will enable the Commission to draw conclusions regarding the existence of the [Beneficiary’s] [Linked Third Party’s] usual cost accounting practice and its suitability to ensure that direct personnel costs claimed on that basis comply with the provisions of the Agreement. The Commission draws its own conclusions from the Report and any additional information it may require’ (see Independent Report of Factual Findings regarding the CoMUC);

‘This Report may be used only for the purpose described in the above objective’ (CFS) or ‘This Report has been drawn up solely for the purpose given under Point 1.1 Reasons for the engagement’ (CoMUC) ... ‘The Report may not be used by the [Beneficiary] [Linked Third Party] or by the [Commission] [Agency] for any other purpose, nor may it be distributed to any other parties’ (see Independent Report of Factual Findings).

² ‘The Commission sets out the Procedures to be carried out by the Auditor. The Auditor is not responsible for their suitability or pertinence. As this engagement is not an assurance engagement, the Auditor does not provide an audit opinion or a statement of assurance’ (see Terms of Reference of the CFS) or ‘The Commission sets out the Procedures to be carried out and the Findings to be endorsed by the Auditor. The Auditor is not responsible for their suitability or pertinence. As this engagement is not an assurance engagement the Auditor does not provide an audit opinion or a statement of assurance’ (see Terms of Reference of the CoMUC);

‘Had the Auditor carried out additional procedures or an audit of the [Beneficiary’s] [Linked Third Party’s] Financial Statements in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to its attention and would have been included in the Report’(see CFS’s model Independent Report) or ‘Had we carried out additional procedures or had we performed an audit or review in accordance with these standards, other matters might have come to its attention and would have been included in the Report’(see CoMUC’s model Independent Report).

³ ‘The Auditor must comply with these Terms of Reference and with the International Standard on Related Services (‘ISRS’) 4400 Engagements to perform Agreed-upon Procedures regarding Financial Information as issued by the International Federation of Accountants (IFAC) and the Code of Ethics for Professional Accountants issued by the IFAC. Although ISRS 4400 states that independence is

auditor believe that the procedures set out by the Commission cannot be carried out or are not adequate to corroborate a standard finding for a specific case, it is explained in the Independent Report that he should raise an exception or make a remark in the report explaining this fact (see attachments).

You are also of the opinion that *'some of the tests seem to be designed to give comfort on systems rather than on reporting results or facts. Providing a positive statement in the way in which the European Commission suggests would require the auditor to carry out sufficient tests to enable him to make such a judgement (which can only be provided under an assurance engagement)'*. In this respect, it has to be noticed that the auditor's obligations were limited in the final model terms of reference to the boundaries of an agreed-upon procedures as explained above. Thus, no opinion is sought and no further tests are requested to be implemented. Similarly, while the objective of the engagement was restricted to carrying out the procedures and reporting on the findings it was also explicitly mentioned that it is not an assurance engagement. Should it not be possible to carry out a certain test or should the test not be adequate to confirm a specific condition, the Auditor is expected to inform the Commission in the form explained above.

You also recommended *'to be clear in the wording of the detailed procedure to be carried out that the tests are applicable to the sample selected only and are not meant to be an extrapolation of the results to the entire population – which is not a factual finding report'*. As you may see in the final versions, the size of the sample has been clearly defined for each category of cost⁴ and no extrapolation of the results to the entire population is required.

Terminology

In order to illustrate your concerns, you provided some examples of the issues you raised above i.e. you are of the opinion that;

i) *'the use of the term "review" is inappropriate in an agreed-upon procedure engagement since it suggests that a review engagement, which concludes by giving limited assurance, has been performed'*,

ii) *'stating that the 'reasonableness of the personnel costs has to be reviewed' de facto includes judgment. This is inappropriate in an ISRS 4400 assignment as it is not a factual finding' and*

iii) *'stating that 'all necessary documents have been reviewed' suggests that the auditor should decide what documents are appropriate'*.

- i. As for the first example, the information contained in the respective final certificates already made clear that the procedures to be carried out constitute neither an audit nor

not a requirement for engagements to carry out agreed-upon procedures, the [Commission] [Agency] requires that the Auditor also complies with the Code's independence requirements.

⁴ For instance, concerning section A on personnel costs it was established following sample size 'The sample should be selected randomly so that it is representative. Full coverage is required if there are fewer than 10 people (including employees, natural persons working under a direct contract and personnel seconded by a third party), otherwise the sample should have a minimum of 10 people, or 10% of the total, whichever number is the highest'; concerning section B on subcontracting the sample size established is as follows "Full coverage is required if there are fewer than 10 items, otherwise the sample should have a minimum of 10 item, or 10% of the total, whichever number is highest"; etc.

a review⁵. I am of the opinion that using the verb “to review” in the table of procedures does not change the character of the engagement. However, this may be clarified in the future, in order to avoid any confusion.

- ii. As for the second example, it has to be noted that the Commission is not generally asking to review the reasonableness of the personnel costs. The CFS does not mention such a check and the CoMUC only refers to the word reasonable in respect to estimated or budgeted elements⁶. Only when the beneficiary applies unit costs as his usual cost accounting practices in the calculation of personnel costs he is allowed to include some estimated or budgeted element in this calculation if certain conditions are fulfilled. The meaning of the condition “reasonable” has been further explained in the Annotated Grant Agreement i.e. estimated/budgeted elements considered reasonable are those that “do not play a major role in calculating the hourly rate” (example “indexation” of salaries⁷). We acknowledge that, even though the Commission has defined what it considers “reasonable”, there may still be a residual question concerning the interpretation of the word “major”. The Commission is aware of that and, consequently, will provide, where possible, for further interpretation of this and similar conditions.

The beneficiary himself must explain in writing why he considers this estimated element relevant for calculating the personnel costs, reasonable and how they are based on objective and verifiable information. This information should be annexed to the CoMUC.

The auditor is expected at least to explain the nature of the estimated element and the value of this element represents (or as % of the total personnel cost) since this information is relevant to properly understand the beneficiary’s methodology. If no further information has been provided by the auditor, the Commission has already some information from the beneficiary and may contact him to further enquiry on this issue if necessary. In order to avoid any confusion about the auditor’s role in this aspect the Commission will also reconsider this point again.

- iii. Regarding the third example, there is no such a statement in the certificates. FEE may be referring to sentences such as “*Any other document that supports the personnel costs declared*” at the end of a list of procedures applicable to certain cost categories to be examined. Let me first explain that this is a residual and a valid procedure to cover all possibilities, since it is materially impossible to mention the name of the type of document applicable for all types of beneficiaries in all countries in which the framework programme is applied. Indeed, the EC expects the auditor to know the specific type of document necessary to carry out the procedure defined by the Commission in order to assess the standard factual finding. Furthermore, apart from being familiar with the legal and financial rules concerning the framework programme

⁵ Since the Procedures carried out constitute neither an audit nor a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, the Auditor does not give a statement of assurance on the Financial Statements (see Independent Report of Factual Findings).

⁶ Standard factual finding 9 “To the extent that actual personnel costs were adjusted on the basis of budgeted or estimated elements, those elements were relevant for calculating the personnel costs, reasonable and correspond to objective and verifiable information. The budgeted or estimated elements used are: — (indicate the elements and their values)”.

⁷ Example provided in the Annotated Grant Agreement i.e. Calculating average 2014 hourly rates by using 2013 payroll data and increasing them by adding the CPI (consumer price index) on which the basic salaries are indexed.

the auditor is also expected to possess the necessary knowledge of the national, regional, local and sectorial rules and regulations applicable to the beneficiary. Therefore, I believe such a procedure cannot be considered as falling outside the scope of the standard ISRS 4400 on agreed-upon procedures.

International framework

Regarding your suggestion to refer to the independent boards of the IFAC i.e. the IAASB and the IESBA as the ones producing the ISRS 4400 and the Code of Ethics for Professional Accountants this will be properly clarified.