

Decision in case 306/2018/JAP concerning how the European Commission dealt with an audit of three EU-funded projects

Decision

Case 306/2018/JAP - Opened on 26/11/2018 - Decision on 26/11/2019 - Institution concerned European Commission (No further inquiries justified) |

The complainant took part in three EU-funded projects in the context of the 7th Framework Programme for Research and Technological Development. Its complaint to the Ombudsman concerned how the European Commission dealt with an audit of the expenditure claimed in the context of the projects.

The auditors found that the complainant's time-recording system was unreliable. They asked the complainant to provide alternative evidence to substantiate the costs for personnel and other actions. The complainant submitted a number of documents to prove the costs incurred in the projects. However, the Commission rejected them as unreliable and, according to the complainant, decided to recover more than EUR 225 000.

The Ombudsman opened an inquiry into how the Commission dealt with the audit, and its decision to recover funds. Her inquiry team met with the Commission's representatives and inspected its file.

The Ombudsman found that the Commission took the complainant's allegation that the audit was badly conducted seriously, investigated the matter and assessed the alternative evidence provided.

While the Ombudsman recognises the Commission's duty to safeguard the financial interests of the EU and acknowledges its efforts to obtain alternative evidence from the complainant, she was not convinced that, by rejecting the personnel costs in full, the Commission had adopted a fair or proportionate approach. Since the Commission, on three separate occasions, rejected a request to consider at least a partial waiver of the recovery, the Ombudsman concluded that further inquiries were unlikely to serve any purpose. She makes a suggestion for improvement to seek to avoid similar cases occurring in future.

Background to the complaint



1. The complainant took part in three EU-funded projects in the context of the 7th Framework Programme for Research and Technological Development (the FP7) [1] between 2009 and 2014. Following the projects' completion, in 2014, the Commission decided to carry out an audit. It contracted the audit work to an international consultancy .
2. The audit fieldwork took place from 15 to 18 July 2014 on the complainant's premises in the Philippines. The country was hit by a typhoon while the audit was ongoing [2] . For security reasons, the complainant's premises were temporarily closed, with only partial and restricted access granted to the complainant's staff [3] .
3. After the fieldwork and verification of documents had ended, the Commission sent the draft audit report to the complainant. It rejected more than EUR 280 000, contesting mainly the personnel costs and other indirect costs claimed by the complainant.
4. The complainant replied with extensive clarifications, including several documents intended to prove the hours and costs declared for the project. This included *reconstructed* timesheets, sales invoices and receipts for equipment, and supporting documents for travel expenses.
5. The Commission sent the complainant its final audit report in December 2015. Having reviewed the complainant's clarifications, it decided not to adjust the reclaimed amount or accept any additional costs. The Commission concluded that the time-recording system kept by the complainant did not comply with the requirements set out in the grant agreement and was therefore unreliable.
6. From 2016 to 2017, the complainant engaged in a dialogue with the Commission, providing alternative evidence to prove that the costs complied with the requirements set out in the grant agreements [4] . The Commission maintained its position that the alternative evidence was insufficient to substantiate the personnel costs.
7. In May 2017 and July 2018, the Commission decided to offset the complainant's debt with outstanding payments for other EU-funded projects in which the complainant was involved. It also made a claim for liquidated damages [5] . The complainant calculated that the Commission was seeking to recover more than EUR 225 000. It argued that this would force it to file for bankruptcy.
8. Dissatisfied with the Commission's conduct in this case, in February 2018, the complainant turned to the Ombudsman.

The inquiry

9. The Ombudsman opened an inquiry into how the Commission dealt with the audit of the three projects and its decision to recover funds.



10. In the course of the inquiry, the Ombudsman's inquiry team met with the Commission's representatives and inspected the Commission's file on the case. The Ombudsman invited the Commission to reconsider its recovery claim - in part or in full - based on the principle of proportionality, as enshrined in the EU Financial Regulation. She received supplementary comments from the complainant and the Commission's replies as well.

Arguments presented to the Ombudsman

(i) Audit fieldwork

11. The complainant argued that an inexperienced and unqualified auditor performed the audit fieldwork. In addition, even though the complainant's premises were inaccessible due to the typhoon, the auditor's visit was not extended to complete the interviews, collect the necessary documentation and obtain clarity thereon. The complainant also contended that the auditing process deviated from best practices and breached the principles of fairness and proportionality.

12. The Commission noted that the typhoon did not prevent the audit fieldwork from being carried out. The auditors were present during the typhoon and revisited the complainant's premises [6] at a later stage. During the typhoon, the auditors accessed the premises for a brief time to obtain the available evidence and studied the documents received from a different location. The auditors were thus on the premises at the beginning and at the end of the fieldwork. The auditors also held an exit meeting with the complainant. Moreover, the complainant was given additional time to gather missing documents and alternative evidence after the fieldwork had been completed.

13. The Commission also explained that well-qualified auditors carried out the fieldwork. Having learnt of the complainant's doubts, it verified how the auditors had carried out their work. The Commission's Common Audit Service (CAS), which is hosted by DG Research and Innovation, reviewed their work. In line with standard practice, the auditors informed the complainant of the preliminary assessment and allowed it to make comments based on the draft report. These had been taken into account before the final audit report was drawn up. The Commission therefore concluded that the auditors had complied with all the applicable standards.

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Sub-contracting

14. The complainant stated that it worked as a sub-contractor for the main beneficiary (coordinator) for one of the three audited projects. As such, it was of the view that it was not required (under the FP7 rules) to provide the Commission with any timesheets for that project.



15. The Commission clarified that the complainant was not a sub-contractor. A number of the complainant's employees were linked to personnel registered with a different company not mentioned in the grant agreement. In the relevant project, the complainant was a third party and submitted costs as such, carrying out work for the main beneficiary. Under the applicable rules [7] , a third party has the same obligations as a beneficiary in the project. Since the complainant's time recording or alternative evidence did not comply with these obligations, the Commission rejected the complainant's personnel costs.

(iii) Time-sheets and alternative evidence

16. The complainant's time recording consisted of arrival and exit time records for all its employees. The complainant could not understand why the Commission considered this insufficient as proof of the efforts devoted to the projects. It has tried to provide alternative evidence to prove that the personnel costs incurred in the context of the projects complied with the applicable rules [8] . In this regard, the complainant has sent a number of documents with a view to proving that the work had been carried out. The documents included progress reports, e-mail exchanges, information about work-related travel and meeting reports.

17. It further argued that the Commission had never contested the quality of the results delivered, nor had it found any fraudulent behaviour on the complainant's part. However, by rejecting its personnel costs, the Commission's stance implies that satisfactory results were “ *produced by invented personnel* ”. This constitutes a denial of payment for work actually done. The complainant also questioned the usefulness of the possibility of submitting “ *alternative evidence* ” since no documents were deemed acceptable. It was also disappointed that the Commission had not seen a measurable link between the time claimed for the project and the quality of the results delivered.

18. The Commission noted that the complainant lacked an appropriate time-recording management system. The initial records (log report) given to the auditor included only arrival and departure times for the complainant's staff. Thus, what the complainant provided as *timesheets* did not comply with the requirements of the FP7 action.

19. In the absence of a reliable time-recording system or appropriate timesheets, the complainant was asked to provide alternative evidence with a view to justifying the time declared on the projects. However, this evidence was not in line with the relevant guidelines [9] . In addition, “ *it was not sufficient to demonstrate that a project was correctly implemented to justify the award of a specific grant* ”. [10]

20. The Commission noted that the assessment of alternative evidence is carried out on the basis of the following criteria: whether there is a sufficient and clear link between the work or action and the costs declared in the performance of the project by the person concerned. Moreover, this link must allow the Commission to measure the time spent on the project.

21. According to the Commission, the alternative evidence provided by the complainant did not



allow the auditor **to measure** the time spent on the project. A clear link to the time spent would have sufficed but there was no such indication in the evidence provided. Any assessment by the Commission of the time spent on these projects would therefore have been arbitrary. The Commission can reimburse only actual costs incurred [11] .

22. In addition, the Commission had serious doubts regarding the reliability of the timesheets. The complainant produced the timesheets after a considerable lapse of time, with the sole purpose of convincing the Commission of their veracity [12] . Their value was therefore questionable.

23. Some of the alternative evidence the complainant submitted included detailed reports, which did not allow the Commission to see a clear link between the actions, the persons involved, the time spent, and the costs declared. This was all the more so as the listed actions were not linked, with some exceptions, to any specific staff member [13] . The Commission could not thus calculate the project costs.

24. In addition, the documents were still inconclusive for auditing purposes because they did not comply with the above mentioned verification criteria. It was therefore impossible for the Commission to reconcile the reports with the reconstructed timesheets produced after the audit fieldwork. Moreover, the Commission noted that it was not for the auditors to assess how much time each staff member had spent on each project or task. In any event, the alternative evidence was insufficient to measure the actual time spent on the project.

25. The Commission noted that it had given the complainant a sufficient number of opportunities to provide alternative evidence. This could consist of emails or reports with a clear link to the time spent, expenses and staff member involved.

26. The Commission explained that it had assessed the alternative evidence provided. However, the auditors do not accept 'estimations'. Instead, they look for evidence that is 'measurable'. Alternative evidence should therefore be '*convincing and reliable*'. Since none of the documents submitted by the complainant provided a clear link between the time spent and the projects, the Commission could not consider the complainant's costs eligible.

27. Finally, the Commission did not find any plausible indications that the complainant's existence was threatened by its recovery order. It also noted that the complainant had relied on EU funding previously and therefore should have been aware of the financial requirements. It thus concluded that its approach was not unfair.

Additional arguments set out during the inspection meeting

28. The Ombudsman's inquiry team noted that it is difficult to understand how the Commission can acknowledge that the work was done and results delivered but reject the related personnel costs at the same time.



29. The Commission pointed out that the scientific results of a project and the audit are not linked and have to be considered separately. The audit concerned the financial aspects of the projects only and not the quality of the work performed.

30. The Ombudsman's inquiry team also noted that in cases where no fraudulent behaviour has been detected, and given that the complainant provided alternative evidence partially proving the work performed, a qualified expert could assess how many hours would be necessary to complete these tasks. Therefore, the Commission could deduct this amount from the total sum to be recovered.

31. The Commission stated that it had assessed the alternative evidence with a view to identifying hours spent on the projects. It insisted that it was not possible to decide which costs should be deducted based on considerations of fairness.

The Ombudsman's assessment

(i) Audit fieldwork

32. The Ombudsman finds the Commission's stance on this aspect of the complaint to be reasonable. Although the inspected documents take note of the disruption the typhoon caused for the auditors [14] , their access to the complainant's premises was restricted for one full day only. Regardless of the restriction, there was insufficient information to conclude that the typhoon had prevented the auditors from performing their tasks properly. The complainant was also given a number of possibilities to submit documents and provide extra clarifications on the audit report after the fieldwork had ended.

33. The inspected documents showed that both the auditors and the Commission verified the documents provided by the complainant.

34. Moreover, the Commission took the complainant's allegations seriously and verified the auditors' work. The inspected documents showed that the Commission's CAS reviewed the documents and verified the auditors' findings. Having obtained a detailed account of the fieldwork actions and other audit-related activities, the Commission found the complainant's allegations to be unsubstantiated. The Ombudsman finds this reasonable based on all the information gathered.

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Sub-contracting

35. Under the applicable rules [15] , costs linked to the project but incurred by third parties



should comply with the eligibility requirements. The Ombudsman has found no convincing elements to call into question the Commission's conclusions regarding the sub-contracting issue.

(iii) Time-sheets and alternative evidence

36. Although the Commission accepted the complainant's results, it rejected the personnel costs in this case. Nothing in the file suggests that the complainant had not carried out its work properly. Nor did the documents question the quality of the complainant's work. It is therefore beyond any doubt that the complainant carried out its work on the projects.

37. The Ombudsman notes that the Commission's financial audit practice consists of a two-stage verification process. The auditors verify whether the beneficiaries complied with the requirements set out in the grant agreement by examining their timesheets and linking them with the actions and 'deliverables' under the project. Should the timesheets prove to be unreliable or insufficient, the Commission asks for alternative evidence that could prove that the costs are eligible.

38. The Commission seeks to ensure that **all declared working hours** spent on the projects are reflected in the timesheets or can be reconciled with the alternative evidence. If the Commission cannot satisfy itself that the declared time corresponds to the delivered work, it rejects the corresponding personnel costs.

39. In this case, the Commission concluded that the time-recording system used by the complainant did not comply with the applicable rules. This conclusion seems reasonable on the grounds that a system that simply records the arrival and departure times of personnel is not sufficient to comply with the applicable rules requiring detailed time sheets. However, the absence of a verifiable time recording system can be mitigated by alternative evidence to justify the time spent on the project.

40. The Ombudsman acknowledges that the Commission provided the complainant with several opportunities to submit additional evidence to prove the time spent on the projects, and assessed it.

41. Since the complainant provided insufficient evidence to justify all the working time under the projects, the Ombudsman accepts that the Commission could not reimburse **all** of the personnel costs. The Ombudsman further acknowledges that the alternative evidence provided by the complainant was presented in a chaotic way, was incomplete, and not clearly linked to individual actions under the three projects [16] .

42. At the same time, the alternative evidence appeared sufficient to justify at least a partial reimbursement. While it is a duty of the Commission to safeguard the financial interests of the EU, the Ombudsman took the view that it was disproportionate to take this duty to the extreme of refusing any payment when the Commission acknowledges that the work has been done. It is



clear from the supporting evidence that time was spent by the complainant's employees on the projects in question. It is also clear that the complainant incurred costs in making its contribution to the project.

43. While the implementation of a project is a necessary but not a sufficient condition for reimbursement of the costs incurred in the context of a project, the Ombudsman was of the view that the Commission should give effect to the principle of proportionality to the greatest extent possible. In this case, fairness required at least a partial acceptance of the personnel costs.

44. In an effort to promote a fair and proportionate solution in this case, the Ombudsman asked the Commission to reconsider its recovery decision. The Commission decided not to reconsider its decision on three separate occasions - during the inspection meeting, in its explanatory note following the inspection and in its final reply to the Ombudsman.

45. While the Ombudsman does not expect the Commission to accept costs that do not meet the eligibility criteria or go against the relevant jurisprudence [17], she understands the complainant's disappointment. However, given the Commission's firm stance in this case and its reluctance to reconsider a partial waiver of the recovery, the Ombudsman finds that any further request to the Commission to assess once more the alternative evidence would not serve any purpose. She also does not consider that her further inquiries or engagement with the Commission would result in a more satisfactory outcome for the complainant.

46. The Ombudsman also takes on board, in this context, the Commission's argument that the complainant had relied on EU funding previously and therefore should have been aware of the financial requirements.

47. It is of the greatest importance that, to the extent possible, similar issues do not reoccur. The Ombudsman is reassured to note that under the current Horizon 2020 Framework Programme, the Commission has made a timesheet template available on its website. It has also listed examples of documents and criteria that alternative evidence should comply with in the indicative audit programme [18].

48. To further see to it that similar problems do not occur in the future, the Ombudsman is also of the view that the Commission should, upfront, guide beneficiaries better in terms of what constitutes alternative evidence that is necessary and acceptable for auditing purposes. This case shows that it is extremely difficult even for a beneficiary with experience in EU-funded projects to prove and link the relevant costs. The Ombudsman will make a corresponding suggestion for improvement.

Conclusion

Based on the inquiry, the Ombudsman closes this case with the following conclusion:

Given the unlikely prospects of obtaining a more satisfactory outcome for the



complainant in this case, no further inquiries are justified.

Suggestion for improvement

With a view to guiding beneficiaries better through the auditing process, the Commission should - in the applicable guides to financial issues - provide for a clear and exhaustive list of documents, and examples of documents, which may constitute reliable alternative evidence, in case the time-recording system used by the beneficiary proves unreliable.

The complainant and the Commission will be informed of this decision.

Emily O'Reilly

European Ombudsman

Strasbourg, 26/11/2019

[1] https://ec.europa.eu/research/fp7/understanding/fp7inbrief/what-is_en.html [Link]

[2] <https://earthobservatory.nasa.gov/images/84027/typhoon-rammasun-drenches-philippines> [Link]

[3] Access to the complainant's premises was not possible on 16 July, while only limited access was possible on 17 July. The audit fieldwork could nevertheless take place on 15, 17 (in part) and 18 July. Work resumed on 21 July 2014, after the auditor had left, with the premises sustaining, what the complainant described as, "*substantial damage*".

[4] Notably, the complainant sent a second "reply" providing several documents, including emails and tables including links to meeting reports.

[5] Liquidated damages are presented in certain legal contracts as an estimate of otherwise intangible or hard-to-define losses to one of the parties.

[6] The Commission confirmed that the auditors did not have access to the complainant's premises on one day, that is 16 July 2014.

[7] General Conditions are available at:
https://ec.europa.eu/research/participants/data/ref/fp7/93289/fp7-ga-annex2_en.pdf [Link]

[8] Ibid.



[9] Guide to financial issues relating to FP7 indirect actions, version 30/06/2010 <http://wbc-inco.net/object/document/7196/attach/fp7-financialguide.pdf> [Link] with subsequent changes, sets out guidelines on how to prepare timesheets and what is considered sufficient alternative evidence, “*giving an equivalent level of assurance, to be assessed by the auditor*”, p. 47.

[10] The Commission’s explanation of 24 October 2016.

[11] Judgment of the Court of First Instance of 22 May 2007 in case T-500/04, *Commission v IIC Informations-Industrie Consulting GmbH*, para. 94. Judgment of the General Court of

27 April 2016 in case T-154/14, *ANKO AE Antiprosopion, Emporion kai Viomichanias v European Commission*, para. 140. Judgment of the Court of Justice of 28 February 2019 in case C-14/18 P,

Alfamicro v European Commission, paras. 65 et seq.

[12] The Commission noted that the complainant had “*presented new and seemingly perfect timesheets (...) after the audit, [and] which ha[d] little or no value at th[at] stage*”.

[13] The Commission noted that the complainant had provided a table including the names of the staff members involved and their tasks for only one project and only partially.

[14] E-mail of 15 April 2016 with clarifications from the auditor.

[15] Articles II.3(d) and II.14.2. of the general conditions to the grant agreement.

[16] Verification of personnel costs could, however, be done by cross-referencing different documents, for instance the table mentioned in footnote no 13 with additional documents, mission and meeting reports, etc. The Commission could have asked the complainant to develop this evidence further in an effort to produce a comprehensive and reliable overview of personnel costs incurred for that particular project. Moreover, meeting minutes as well as progress and mission reports and other documents include sufficient details on some of the personnel working on the projects together with some verifiable dates. Accepting even these costs would have been a fairer approach to take.

[17] See reference to the case law under footnote 11.

[18] H2020 Indicative Audit Programme, July 2019.

The three criteria that alternative evidence needs to comply with are:

1) Clear identification of the person concerned; 2) Clear link to the project under scrutiny, and 3) Possibility to quantify time spent on project-related tasks. These criteria are indispensable.

