Decision in case 2218/2019/MDC on the Research Executive Agency's decision to consider ineligible certain costs claimed by a partner in an EU-funded project on the interoperability of unmanned vehicles (DARIUS)

Decision
Case 2218/2019/MHZ - **Opened on** 21/02/2020 - **Decision on** 16/09/2020 - **Institution concerned** European Research Executive Agency (No maladministration found) |

The case concerned the decision of the Research Executive Agency (REA) to consider ineligible certain costs claimed in the context of a project that was co-funded by the EU: the DARIUS project on the interoperability of unmanned vehicles in search and rescue operations.

The complainant considered that the REA had acted in a contradictory and inconsistent manner, and should not have deemed the costs ineligible. It raised various concerns about the findings of the audit on which that decision was based .

The Ombudsman found that the REA acted reasonably and in line with the grant agreement. She therefore closed the inquiry with a finding of no maladministration.

Background to the complaint

1. The complainant is a small business that provides consultancy services on innovative information management systems. It received funding in the context of the DARIUS project [1] [Link], which was co-funded by the EU under the Seventh Framework Programme for Research (FP7) [2] [Link], and concerned the interoperability of unmanned air, ground and maritime vehicles in search and rescue operations. The project began in March 2012 and ran for three years.

2. The owner of the business carried out work on the project together with other consultants. During the work on the project, the business operated from what the complainant referred to as 'unofficial premises' in Greece. The business was officially registered in the United Kingdom.

3. The preliminary results of an audit, carried out in May 2015, found some of the costs claimed by the complainant to be ineligible. The complainant contested this finding.

4. On 21 November 2016, the REA sent a 'letter of conclusion' together with the final audit report to the complainant. The final report had been adjusted, to take into account the comments made by the complainant, but continued to deem some of the costs ineligible, including the 'indirect costs' related to the consultants.

5. The complainant contested the findings of final audit report. In particular, the complainant argued that it was inconsistent that the audit had deemed ineligible the indirect costs of the consultants because the work had been carried out in Greece (not in the UK), but had accepted the indirect costs of the business owner. The complainant asked the REA to reconsider its acceptance of the final audit report.

6. In the context of subsequent correspondence between the REA and the complainant, the REA stated that the location of applicants is an important criterion in determining the award of grants for projects, and that the complainant had been selected as a UK-based company, and had not notified the REA that it was relocating to Greece, which it was obliged to do under the grant agreement. It also stated that different rules apply to small business owners and consultants they recruit. [3] [Link]

7. The complainant contested the REA's position. In particular, it argued that the business had not relocated, but had simply carried out the work at premises in another country. It pointed to advice given by the Research Enquiry Service Validation Helpdesk (RES), which stated that entities that receive grants ('beneficiaries') need to inform the REA only if the legal address of the organisation changes, and not if they simply open a branch or an office at a different address . **[4]**

8. The REA subsequently asked the complainant to provide evidence of the legal establishment of a formal branch in Greece, with a view to deeming eligible the indirect costs of the consultants.

9. In September 2019, the REA stated that as the complainant had failed to provide evidence of the official registration of a branch in Greece, it was maintaining the conclusions of the audit report.

10. On 5 December 2019, the complainant turned to the Ombudsman.

The inquiry

11. The Ombudsman opened an inquiry into the complaint's claim that the REA should not have considered ineligible certain indirect costs relating to the consultants.

12. In the course of the inquiry, the Ombudsman examined all the evidence provided by the complainant, as well as the REA's reply to the complaint and the comments of the complainant in response to the REA's reply.

Arguments presented to the Ombudsman

13. The **complainant** contended that the REA's position on the eligibility of the indirect costs of the consultants was contradictory, given it accepted the indirect costs of the business owner. In addition, despite having acknowledged that the 'Financial Guidelines' [5] [Link] are not part of the contractual provisions, the REA approved the revised final audit report, which deemed the costs ineligible on the basis of the provision in the guidelines that work must be carried out at the official premises of the 'beneficiary'. It argued that the applicable rules [6] do not exclude the possibility of the beneficiary having unofficial premises in another Member State.

The complainant argued that the REA did not explain why it requested evidence that it had legally registered a branch in Greece, in order to consider eligible the indirect costs of in-house consultants. In the complainant's view, this additional requirement is contrary to EU case-law. [7] Prior to the audit, the REA never explicitly informed the complainant that in-house consultants must offer their services at the official premises of the beneficiary. Moreover, according to the complainant, the RES's statement calls this into question.

Finally, the REA had failed to address issues concerning the credibility of the audit, for example the lack of a 'closing meeting' with the auditors, despite inconsistencies in the final audit report.

14. In its reply to the Ombudsman, the **REA** pointed out that, under the grant agreement, "[i] *ndirect costs are all those eligible costs which cannot be identified by the beneficiary as being directly attributed to the project* **but which can be identified and justified by its accounting system as being incurred in direct relationship with the eligible direct costs attributed to the project** " [8] [Link] (emphasis added).

15. The apartment in Greece, where the work on the project was carried out, was rented by the owner of the business, and not by the business itself. As the business was registered in the UK only, the auditors could consider the apartment to be premises of the business only if it was registered as such in Greece. Furthermore, since the business's accounts did not list costs of the rental, the audit deemed that they were not costs incurred by the business, and could not be reimbursed.

16. In addition, the REA stated that the complainant had failed to inform it that consultants would be involved in carrying out the project, or that the work on the project would be carried out not in the UK but in a private apartment in Greece. According to the REA, both circumstances could have affected the eligibility of the costs under the grant, and, according to the grant agreement, the complainant was obliged to inform it about them. The REA added that, had it been notified, it would probably not have accepted such arrangements.

17. Despite this, the REA stated that, given the work had been carried out, it had tried to be as flexible as possible and accepted the direct personnel costs related to the consultants, based on supporting documents and other evidence produced by the complainant.

18. The REA explained that the indirect costs for companies are calculated using a flat rate of 60% of the direct personnel costs of the business owner [9] , and *automatically* added to the eligible costs [10] .

19. However, individuals hired directly by the beneficiary to work on the project on the basis of a contract that does not fulfil the conditions set out in the grant agreement [11] [Link], are considered to be subcontractors hired to provide a service [12] [Link]. The costs of such individuals can be considered as equivalent to direct personnel costs (in-house consultants) only if certain criteria are fulfilled. [13] Although the consultants in this case did not meet one of these criteria [14] , the REA accepted their costs as personnel costs. However, in accordance with the grant agreement [15] , these costs were not included for the calculation of the indirect costs flat rate, as the indirect costs were not incurred by the beneficiary, which is established in the UK.

20. The REA requested evidence of the registration of a branch of the complainant's business in Greece because this could have enabled it to deem the costs eligible, even though the complainant's business has no VAT number or formal presence in Greece, according to the relevant authorities. As the complainant did not provide any evidence of the official registration of a branch in Greece, and since the costs of the rental were not listed in the business's accounts, the REA deemed these costs to be ineligible and maintained its decision to reject the indirect costs of the consultants.

21. The REA considered that the answer provided by the RES provides general guidance on the update of the legal situation of a legal entity (such as legal form, legal name and legal address) in the Beneficiary Register of the European Commission, and does not apply to the participation of a legal entity in a specific grant agreement. As such, it does not have a bearing on whether the indirect costs of the consultants were eligible. Moreover, the REA pointed out that the RES gives general guidance only. It cannot give advice on specific cases and its replies do not take precedence over contractual provisions or audit findings.

22. The REA stated that when the on-side audit was completed, there was a significant amount of missing information. The complainant was given the opportunity to submit further documents and information, which it did by 28 July 2015. In addition, the auditors informally discussed the identified issues with the complainant after the on-site audit.

23. The REA pointed out that, some of the complainant's observations on the preliminary audit report were taken into account in the final audit report. The final audit report was also subsequently amended to take into account further comments that the complainant sent to the REA after the audit was closed. On the basis of those comments, and after discussions with REA, the auditors amended the final audit report where appropriate.

24. Thus, while a formal 'closing meeting' had not taken place, the complainant was not deprived of the possibility to submit comments. On the contrary, the comments and additional information provided by the complainant were taken into account at various stages, including

after formal closure of the audit procedure. The REA had also reminded the auditors of the importance of closing meetings at the end of on-site audits.

25. Finally, the REA stated that it was not possible to compare the indirect costs of the consultants to the travel costs of the complainant's owner, since the indirect costs were not recorded in the business's accounts.

26. The complainant argued that the REA failed to provide any justification or explanation as to how carrying out the tasks at its unofficial premises in Greece could affect the implementation of the project. According to the complainant, the objective was to develop software, an activity that is not dependent on location, provided the appropriate infrastructure is available, which the complainant claimed was the case at its unofficial premises in Greece. Moreover, the complainant contended that the grant agreement did not require it to inform the REA about and obtain its approval for carrying out the project at premises other than its official premises.

27. The complainant took issue with the REA's reference to the beneficiary's unofficial premises as a " *private apartment* ". The complainant argued that the work in Greece was carried out " *in an office that had been rented for that specific purpose* ". In support of this, the complainant referred to the lease, which states that the premises were to be used for " *professional/commercial* " purposes.

28. The complainant further argued that the reply by the RES was not general information on grant agreements, but was the answer to a specific question on whether there was an obligation to communicate the opening of unofficial premises in a country other than the legal seat.

29. The complainant also stated that the REA had recognised that, although the closing meeting was " *obligatory* ", this had not taken place. Instead, the REA merely reminded the auditors about the importance of such meetings. The fact that it was given different opportunities to submit comments cannot replace the lack of a closing meeting, especially in light of the serious issues that the complainant had raised, and which were still pending.

The Ombudsman's assessment

30. The Ombudsman considers that, despite the fact that the Financial Guidelines are not part of the contractual provisions, they play an important role in ensuring the consistent interpretation of the contractual provisions. The REA must follow them to ensure all beneficiaries are treated equally and consistently.

31. The REA adopted a flexible approach and decided to accept the direct costs of the consultants, despite reservations as to whether the contractual provisions were properly fulfilled. However, this does not mean that it was obliged to adopt a flexible approach also with regard to the indirect costs of the consultants.

32. The complainant insists that the consultants met the criteria (listed in the Financial

Guidelines) to be considered 'in-house consultants'. However, one of those criteria states that, to be considered as in-house consultants, the individual " *must work in the premises of the beneficiary (except in specific cases where teleworking has been agreed between both parties and provided such a practice is in full compliance with the provisions regarding teleworking and instructions given by the beneficiary as described here above)* ". As the REA has demonstrated, this criterion was not fulfilled, since the beneficiary's official premises were in the UK, and the work was carried out in Greece at a premises that was rented by the owner of the beneficiary in her own name, not in the name of the company. In addition, there was no agreement to permit the work on the project to be carried out remotely (teleworking). While the REA accepted the direct costs of the consultants, as the work had been carried out, there was no clear evidence that the indirect costs were incurred by the beneficiary.

33. Against this background, it was also reasonable that the REA requested evidence that the complainant had registered a branch in Greece.

34. The Ombudsman also finds convincing the REA's position with regard to the answer provided by the RES. In any event, the RES provided its reply long after the project had been concluded. Therefore, the information had no effect on the decisions taken by the complainant concerning the location from where the complainant's consultants offered their services whilst the project was ongoing.

35. Finally, the Ombudsman is satisfied that, despite the regrettable lack of a closing meeting between the complainant and the auditors, the complainant was given ample opportunity to put forward its comments even after the audit was closed. Therefore, the lack of a closing meeting cannot be considered to have had a negative material impact on the complainant. The Ombudsman also notes that the REA has reminded the auditors of the importance of closing meetings.

36. The Ombudsman finds that the REA adopted a flexible approach and took into account the particular circumstances of the case. This resulted in the REA accepting certain costs, even where there were doubts about their eligibility. Thus, the Ombudsman considers that the REA did not adopt "contradictory" positions, but rather tried to strike the right balance between the principle of proportionality (for the benefit of the complainant) and the principle of equal treatment (for the benefit of all other beneficiaries).

Conclusion

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

There was no maladministration by the Research Executive Agency.

The complainant and REA will be informed of this decision **.**

Emily O'Reilly European Ombudsman

Strasbourg, 16/09/2020

[1] [Link] More information: https://cordis.europa.eu/project/id/284851/reporting [Link].

[2] [Link] More information: https://ec.europa.eu/research/fp7/index_en.cfm [Link].

[3] [Link] The REA referred to Article II.14.1 of the grant agreement concerning SME owners and Article II.15.2.c concerning in-house consultants (third parties). The latter states that " *flat rates for indirect costs cannot be charged on the costs of resources made available by third parties* which are not used on the premises of the beneficiary " (emphasis added by the REA).

[4] [Link] On 27 October 2017, the following reply was provided by the RES: "[t] *he establishment of a branch/operational office in a different address than the legal address, which does not entail any modification in the legal address, does not need to be communicated to the REA Validation Service for updating the Information registered in the Beneficiary Register".* https://ec.europa.eu/info/research-and-innovation/contact/research-enquiry-service-and-participant-validation_en [Link]

[5] [Link] Guide to Financial Issues relating to FP7 Indirect Actions: https://ec.europa.eu/research/participants/data/ref/fp7/89556/financial_guidelines_en.pdf [Link].

[6] [Link] Regulation (EC) 1906/2006 laying down the rules for the participation of undertakings, research centres and universities in actions under the Seventh Framework Programme and for the dissemination of research results, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1581016858847&uri=CELEX:32006R1906 [Link]

This Regulation has now been repealed but was applicable at the time when the grant agreement was entered into.

[7] [Link] The complainant referred to the judgement of the Court of Justice of the European Union in case C-167/01 [Link] and to the Ombudsman's decision in case 2411/2003/MHZ [Link] in support of this argument .

[8] [Link] The criteria can be found in Article II.15.2 of the Annex II to the General conditions to the Grant Agreement.

[9] [Link] The direct personnel costs of SME owners are calculated on the basis of the formula set out in paragraph 6 of Article II.14.1 of the grant agreement.

[10] [Link] This is explained in p. 43 and 44 of the FP7 Guide to Financial Issues.

[11] [Link] Article II.15.1, which sets out the conditions applying to personnel of the beneficiary.

[12] [Link] In accordance with Article II.7 of the grant agreement.

[13] [Link] This is explained in p. 61-68 of the FP7 Guide to Financial Issues.

[14] [Link] The consultants were not working in the premises of the beneficiary, and there was no teleworking agreement in place.

[15] [Link][15] Article II.15.2