



Technical support to the implementation and management of ENI CBC programmes

Guidance on the preparation of the audit strategy in ENI CBC programmes

Legal framework, standards, practices, tips and recommendations

Update June 2017

DISCLAIMER

This **non-binding document** has been developed by the TESIM project.

It does not necessarily reflect the views of the European Commission on the topic, and is presented to programme practitioners **for illustrative purposes only**.

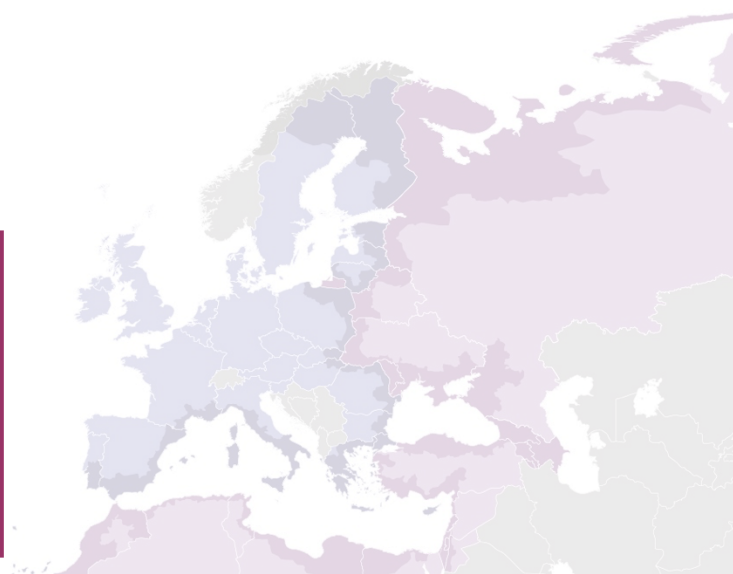


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Clarification on update June 2017

The contents of the document originally delivered have been modified following the discussions which took place at the networking event for ENI CBC Audit Authorities, held in Warsaw on 8-9 March 2017.

In addition to the technical clarifications, the content-related modifications correspond to section 2 (Framework for the audit strategy) and section 3 (Outline of the strategy), in particular:

1. In subsection 2.2, rationale behind planning of the audit strategy is explained;
2. In subsection 3.2,
 - a. audit assurance (risk) model is explained in details;
 - b. the difference between audits of the technical assistance expenses and project expenses in the context of ENI CBC is explained.

1. Purpose of the guidance

The aim of this document is to provide guidance to the Audit Authorities (AA) on the preparation of the audit strategy for ENI CBC programmes under article 28.5 of the ENI CBC Implementing Rules (ENI CBC IR).

The audit strategy is a planning document that sets out the audit methodology on:

- audits on management and control systems¹;
- audits on projects, including the sampling method;
- audit on the annual accounts, and
- the planning of audits for the current accounting year and the two subsequent accounting years.

This guidance sets out the recommendations for the various sections of the strategy. Time-wise, the document shall be submitted to the European Commission within 9 months of the signature of the first Financing Agreement in the respective programme.

In addition, the strategy needs to be updated annually². This update will have to be submitted to the European Commission as part of the annual report of the Managing Authority (MA).

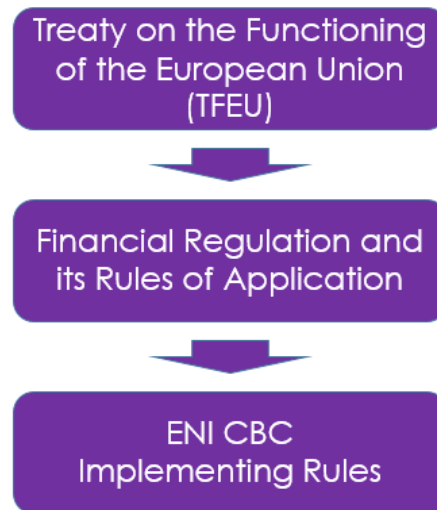
Recommendations included in this guidance are partially inspired by the European Commission document 'Guidance for Member States on Audit Strategy' (European Structural and Investment funds), especially taking into account that a majority of the AAs have an extensive experience in this role in the previous funding period for European Territorial Cooperation programmes. In addition, the guidance highlights the ENI CBC specificities and also draws inspiration from the internationally accepted audit standards and best practice.

¹ Even though article 28.5 does not explicitly mention the audit on management and control systems, article 68.4 stipulates that the audit on accounts shall establish whether "the control systems properly put in place function".

² Article 28.5 of ENI CBC IR requires that the audit strategy needs to be updated annually from 2017 until the end of 2024. However, if the first audit strategy is submitted for the European Commission in 2017/2018, then the updates will be submitted from subsequent year onwards.

2. Framework for the audit strategy

The applicable provisions are defined in the main following legal acts:



The main difference from the previous period in terms of audit is that the scope and responsibility has increased and a **separate authority** is required to be established. This authority is responsible for issuing **an audit opinion**. In order to carry out the entrusted audit work, the **use of international standards** for audit is **compulsory**.

Here is a short comparison of the requirements included in the legal acts for ESIF and ENI CBC:

Topic	ESIF Common Provisions Regulation (CPR)	ENI CBC IR
Functions of the AA	Article 127 Audits on the proper functioning of the management and control system Audits on an appropriate sample of operations on the basis of the declared expenditure + according to the amendment to CPR (Regulation 480/2014) The audits of accounts	Article 28 Audits on the management and control systems Audits on projects Audit on the annual accounts

Sampling	<p>On an appropriate sample of operations on the basis of the declared expenditure</p> <p>The declared expenditure shall be audited based on a representative sample and, as a general rule, on statistical sampling methods (<i>non-statistical sampling is also allowed</i>)</p>	<p>On an appropriate sample of projects</p> <p>No such (or similar provisions) in ENI CBC IR</p>
Annual audit report	<p>A control report setting out the main findings of the audits carried out, including findings with regard to deficiencies found in the management and control systems, and the proposed and implemented corrective actions.</p>	<p>An annual audit report providing a summary of audits carried out, including an analysis of the nature and extent of errors and weaknesses identified, both at system level and for projects, as well as the corrective actions taken or planned.</p>
Annual audit opinion	<p>An audit opinion in accordance with the second subparagraph of article 59(5) of the Financial Regulation</p>	<p>An audit opinion on the annual accounts (establishing whether the accounts give a true and fair view, the related transactions are legal and regular and the control systems properly put in place function)</p>
Additional elements	<p>Implementing acts laying down models for the audit strategy, the audit opinion and the control report</p> <p>Delegated acts to set out the scope and content of audits of operations and audits of the accounts and the methodology for the selection of the sample of operations</p>	<p>No such provisions in ENI CBC IR</p> <p>No such provisions in ENI CBC IR</p>

The basis of the regulatory requirements for the annual reporting of the AAs is article 59(5) of the Financial Regulation. However, the ENI CBC IR have a significantly smaller level of sector-specific regulatory details than the Structural Funds, thus posing additional practical challenges for the AAs.

2.1. International Standards on Audit

Article 28.4 of the ENI CBC IR stipulates that “the Audit Authority shall ensure that the audit work complies with internationally accepted auditing standards”.

There are number of international auditing standards that can be used by the Audit Authorities. This section includes a number of examples, such as the International Standards for Auditing (ISA) which are a set of systematic guidelines used by auditors, ensuring accuracy, consistency and verifiability of auditors' actions and reports. They are issued by IFAC's International Auditing and Assurance Standards Board (IAASB).

A non-exhaustive list of standards, which may be used in ENI CBC, is the following³:

ISA reference	Content of the standard
ISA 200	Overall objective of audit
ISA 220	Quality control for audit work
ISA 230	Audit documentation
ISA 240	The auditor's responsibility to consider fraud in an audit of financial statements
ISA 250	Consideration of laws and regulations in an audit of financial statement
ISA 300	Planning an audit of financial statements
ISA 315	Understanding the entity and its environment and assessing the risk of material misstatement
ISA 320	Materiality in planning and performing an audit
ISA 450	Evaluation of misstatements identified during the audit
ISA 500	Audit evidence
ISA 530	Audit sampling

³ Among this indicative list of standards, it is up to the professional judgment of the AA to decide which ones (ISA, IIA, ISSAI or any other) it will actually follow.

ISA 600	The use of the work of other auditors
ISA 620	Using the work of an Auditor's Expert
ISA 700	Forming an audit opinion
ISA 705	Modifications to the opinion in the independent auditor's report
ISA 706	Emphasis of matter paragraphs and other matter paragraphs in the independent auditor's report

All these standards may be downloaded free of charge from IFAC's website: <http://www.iaasb.org/publications-resources>.

The auditor should consult the ISA and get familiar with the issues covered by them. It is his/her responsibility to fully comply with all relevant ISA and to identify the standards relevant for each particular audit. Therefore, this guide gives only some general indications on a couple of them.

Other standards, such as the International Standards for the Professional Practice of Internal Auditing (IIA standards) or the International Standards of Supreme Audit Institutions (ISSAI) state the fundamental principles in auditing of public entities. IIA standards are issued by the Institute of Internal Auditors and ISSAI are issued by the International Organisation of Supreme Audit Institutions (INTOSAI). They may be downloaded from

http://www.issai.org/en_us/site-issai/issai-framework/4-auditing-guidelines.htm.

Some ISSAI are detailed guidelines and practice notes of the above-mentioned ISA standards. Relevant ISSAI standards not linked to these ones are:

Reference	Content of the standard
ISSAI 3000	Standards for performance auditing
ISSAI 3200	Guidelines for performance auditing process
ISSAI 4000	Compliance audit standard
ISSAI 5300	Guidelines on IT audit
ISSAI 5300	Information System Security Review Methodology

2.2. Rationale of the audit strategy

The audit strategy should be prepared in a way that clearly demonstrates all necessary arrangements for carrying out the audit work and allowing the Audit Authority to draw the audit opinion to:

- establish whether the accounts give a true and fair view;
- the related transactions are legal and regular;
- the control systems put in place function properly.

The **purpose of an audit** is to enhance the degree of confidence of intended users in the financial statements (in the ENI CBC context – annual reports). This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable framework.

According to the ISA200, in order to issue an auditor's opinion, **reasonable assurance** about whether the financial statements as a whole are free from material misstatement should be obtained. Reasonable assurance is understood as a high level of assurance. It is obtained when the auditor has obtained sufficient appropriate audit evidence to reduce the audit risk (that is, the risk that the auditor expresses an inappropriate opinion when the financial statements are materially misstated) to an acceptably low level.

However, reasonable assurance is not an absolute level of assurance, because there are inherent limitations of an audit which result in most of the audit evidence on which the auditor draws conclusions and bases the auditor's opinion being persuasive rather than conclusive.

2.3. Structure of the audit strategy

In each of the sub-sections of the next chapter of this document, the proposed content of the audit strategy is presented. In the beginning of each sub-section the key elements are proposed, followed by the main considerations to be taken into account. In addition, ENI CBC specificities are highlighted.

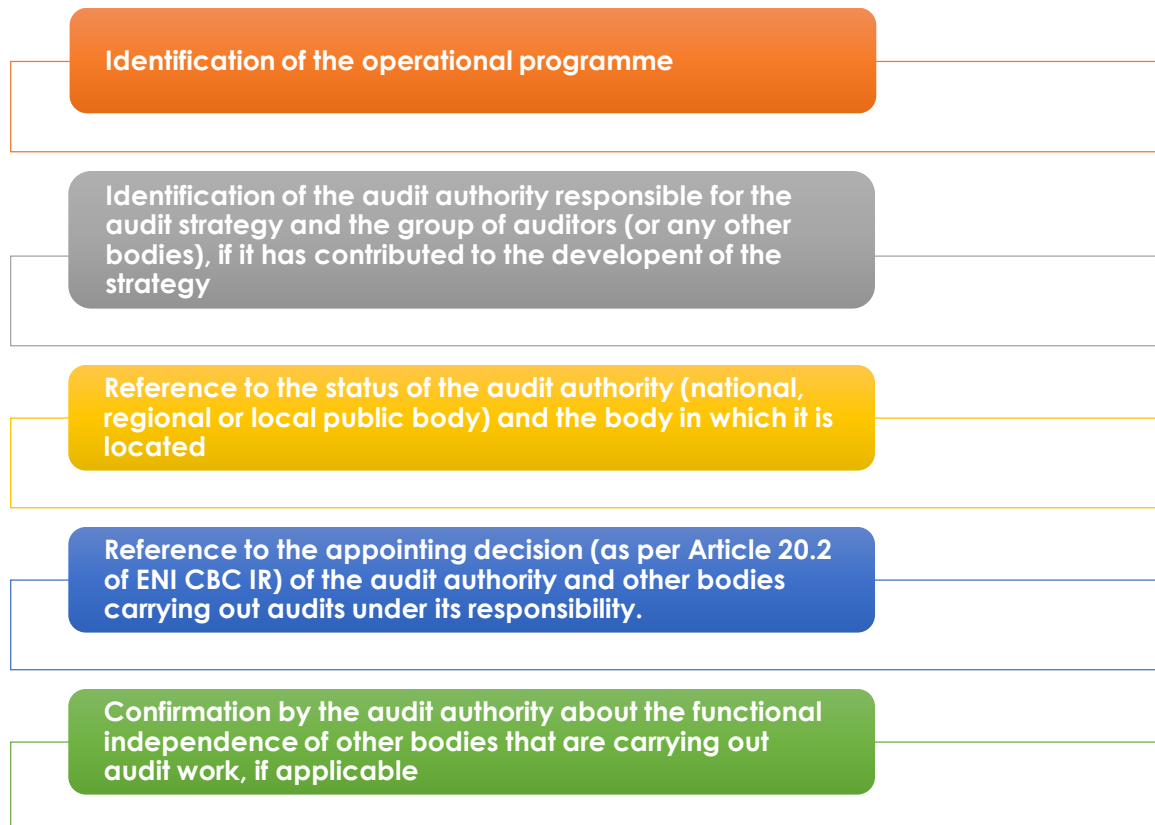
While article 28.5 explicitly refers to few specific elements of the audit strategy, there are a number of responsibilities of the AA described in other articles of the ENI CBC IR. In addition, good practice examples from similar financial instruments are proposed.

Element	Reasoning
Audit risk assessment	<p>Not explicitly required by the article 28.5 of ENI CBC IR, however article 28.1 states ‘...audits are carried out on the management and control systems...’.</p> <p>In case the AAs are not carrying out full MCS audit every year, risk assessment is a method of prioritization of audit work (and serves as justification of selection of audits for annual work plan).</p> <p>In addition, good practice example from similar EU funded instruments.</p>
Audits on management and control systems	<p>Not explicitly required by the article 28.5 of ENI CBC IR, however article 28.1 states ‘...audits are carried out on the management and control systems...’.</p> <p>It is recommended that system audit arrangements are systematically described in the Audit Strategy, as the results of the system audits are crucial part of the basis of annual audit report and audit opinion. Such arrangements would provide a justification that approach planned for system audit work is able to provide sound evidence to conclude on MCS functioning.</p> <p>ENI CBC IR, article 68.2(e) – ‘an annual audit report ...including an analysis of the nature and extent of errors and weaknesses ... at system level ... as well as the corrective actions taken or planned’.</p> <p>ENI CBC IR, article 68.4 – ‘audit opinion shall establish whether...the control systems properly put in place function...’</p>
Audits on sample of projects	<p>ENI CBC IR, article 28.5 - ‘The audit strategy shall set out the audit methodology on projects and the sampling method for audits on projects ...’.</p>
Audits on the annual accounts and verification of the management declaration	<p>ENI CBC IR, article 28.5 - ‘The audit strategy shall set out the audit methodology on the annual accounts ...’.</p> <p>ENI CBC IR, article 68.4 ‘...the audit opinion shall also state whether the audit work puts in doubt the assertions made in the management declaration...’.</p>

<p>Audit opinion</p>	<p>Not explicitly required by the article 28.5 of ENI CBC IR, however article 28.6 states that '...the Audit Authority shall draw up...audit opinion'.</p> <p>Model audit opinion is presented in TESIM 'Guide to programme accounts, audit and reporting to EC in ENI CBC programmes'.</p>
<p>Audit work plan</p>	<p>ENI CBC IR, article 28.5 - 'The audit strategy shall set out the planning of audits for the current accounting year and the two subsequent accounting years ...'.</p>
<p>Audit resources</p>	<p>Not explicitly required by the article 28.5 of ENI CBC IR, however it is recommended to shortly describe necessary audit resources, especially in the light of the mandatory audit work plan.</p> <p>Information on audit resources should provide justification that proposed audit work plan is realistic and reasonable.</p> <p>In addition, good practice example from similar EU funded instruments.</p>

3. Outline of the audit strategy

3.1. Introduction



Where a common management and control system (MCS) applies to more than one programme, a single audit strategy may be prepared for the programmes concerned.

Taking into account that a number of Financing Agreements were signed by the end of 2016, the majority of ENI CBC programmes will have to submit their audit strategies to the Commission in 3rd/4th quarter of 2017.

The AA should keep the documentation related to drawing up, monitoring and updating the strategy as reference.

It is recommended that the AA explains how the audit strategy was drawn-up (especially, if there are contributions from other bodies for the development of strategy) and the arrangements in place to monitor and update the document.

In case the group of auditors has contributed to the strategy⁴, the AA must ensure that their objectives are aligned with those of the strategy, as the AA takes responsibility for the final coordination and the quality of work. It is up to the AA to define how the coordination will be organized, but the process may include written instructions, regular meetings or other means considered useful. Taking into account that audit work in ENI CBC programmes is carried out also outside of the EU Member States, this aspect is especially important.

The **functions and responsibilities** of each of the **audit actors** (AA, group of auditors and other audit bodies, if any) should be described in the **respective rules of procedure** and the **audit strategy should refer to these rules**.

In case the AA is authorised to carry out directly its functions in the whole the territory covered by the programme, rules of procedure of the group of auditors should state whether it is agreed that a member of the group of auditors (of each participating country) can join the AA for on-the-spot audit missions, where relevant. In case each participating country is responsible for carrying out the audit work under article 28.3 of ENI CBC IR, it should be clearly described for each participating country by whom and how the results of the audits on its territory will be transmitted to the AA.

For coordination of audit work the AAs might consider using appropriate international standards, for example, ISA 200 on “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing” and ISA 600 on “Using the Work of Another Auditor”.

⁴ Even though in the ENI CBC IRs the set-up of the group of auditors is related to the designation of the MA (“...shall be set up within three months of the designation ...”), time-wise it is possible that the group of auditors contributes to the development of the audit strategy (“...within 9 months of the signature of the first Financing Agreement ...”).

As required by the article 32.4 of the ENI CBC IR, the **independence** of the programme bodies, including **the AA**, must be **ensured**. This means that the AA does not have any role in the functions pertaining to the MA or other bodies, as well as carrying out tasks under the responsibility of programme bodies. The concept of separation of functions is also reflected in the article 30.1(a) of ENI CBC IR.

The same approach applies to the audit bodies carrying out audits under the AA's responsibility. As an example from the EGESIF document 'Guidance for Member States on Audit Strategy', if audit bodies are internal audit units, special considerations should be taken into account: the AA should be aware of the organisational set up and reporting lines within the organisation in question, in order to assess the position of the internal audit unit and the risk of impaired independence.

In addition, it is important that the audit strategy explains how the **independence of each member of the group of auditors is ensured**, namely in those cases where the members of the group of auditors are involved in the audit work and do not represent the AA.

In case of outsourcing of the audit work, the contractor should be obliged by the contract to immediately inform the AA in case of possible conflict of interests so that the AA, assisted by the group of auditors, can take appropriate measures.

3.2. Audit assurance (risk) model

The assurance model below is based on the model included in the EGESIF 'Guidance for Member States on Audit Strategy' and 'Guidance on sampling methods for audit authorities - Programming periods 2007-2013 and 2014-2020' (which is in turn based on the concepts presented in ISA200). As a core difference, this model includes the audit on accounts as a separate part of the assurance model. The reason for that is the need for a clear distinction between the terms '**projects**' and '**technical assistance**' in the ENI CBC IR. The term 'project' is explicitly described in the Title VII 'Projects', article 38 (especially 38.1 and 38.2). These articles refer to the operations implemented

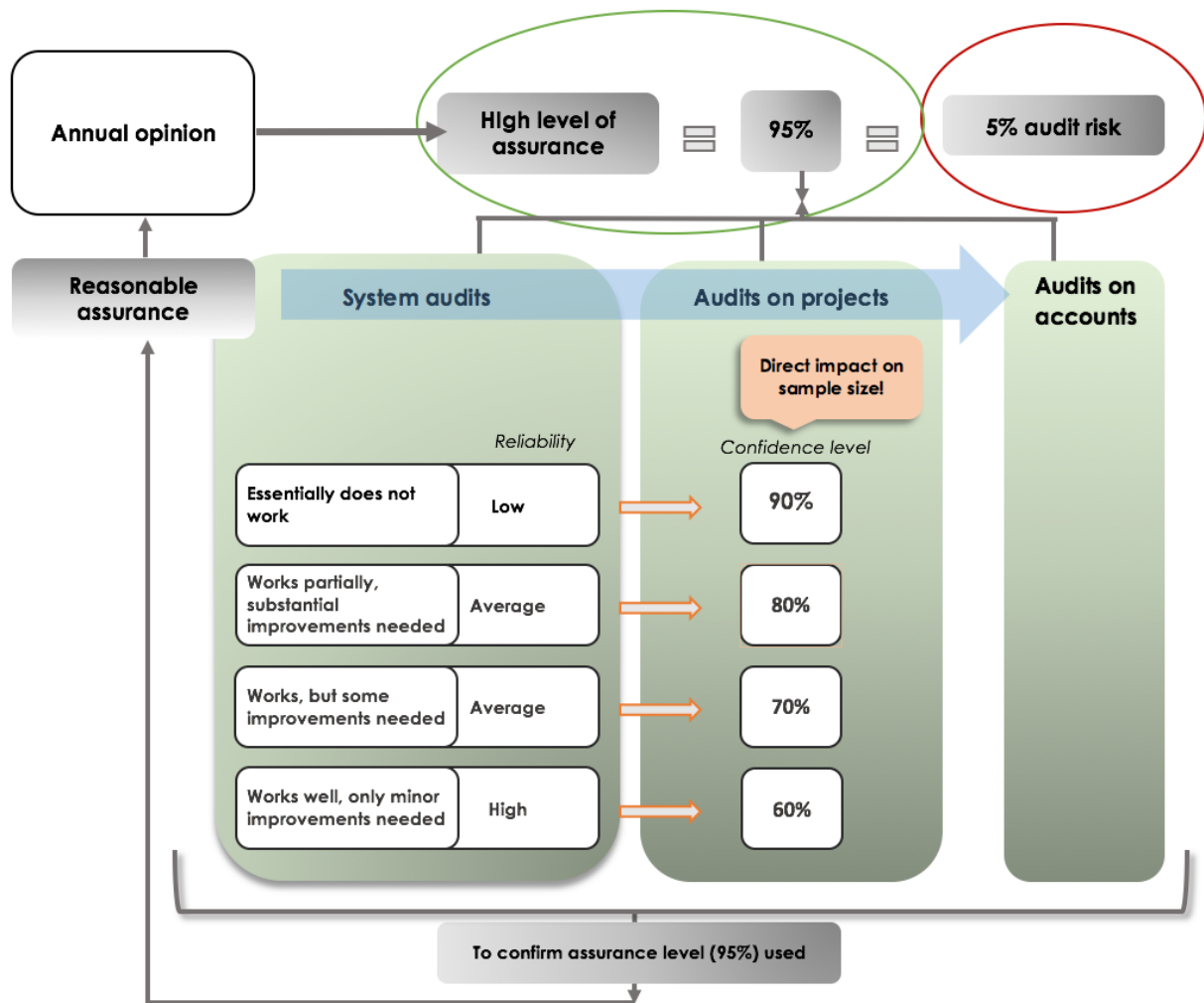
by beneficiaries and to the procedural aspects that are related to projects (for example, 38.2 - 'Financial contributions by a programme to projects shall be provided through grants').

On the other hand, 'Technical assistance' is described in TITLE VI 'Technical assistance', article 34. In this article (and others in the Title VI) there is no reference to the notion of 'project', and the concept of 'technical assistance' is consistently used thorough the articles in this Title.

In addition to that, a number of other articles in the IR also distinguish between the notions of 'projects' and 'technical assistance' (for example, 71.1 'The Managing Authority shall make the financial corrections required in connection with individual or systemic irregularities detected in projects, technical assistance....').

In short, the audit on the technical assistance expenses will have to be carried out separately from the audit of projects and as part of the audit on accounts. The total amount of the technical assistance expenses will serve as the sampling population for this specific audit (i.e., separate from the audit of projects), and it is up to the AA to decide on the sample size, sampling unit and other parameters. In the context of the audit on accounts, the sample size should be sufficient to allow establishing 'whether the accounts give a true and fair view [...]' (article 68.4 of the ENI CBC IR).

The model illustrates the main purpose of the planned audits, which is to provide assurance whether the accounts give a true and fair view, the related transactions are legal and regular and the control systems put in place function properly.



In practical terms, if the aim is to provide a high level of assurance (for example, 95%), then the **audit risk** (possibility for the auditor to issue an unqualified opinion while in fact there are material misstatements in the annual report) has to be kept at the minimum level (5% in this example). Audit risk is a function of the **inherent risk**, **control risk** and **detection risk**.

AUDIT RISK = INHERENT RISK X CONTROL RISK x DETECTION RISK

In order to provide a high level of assurance when issuing an audit opinion (audit risk is fixed at low 5% level) the auditor should develop procedures to take into account the inherent risk (assessment of the entity as such, for example, via audit risk assessment prior to system audits) and control risk (via means of system audits).

If the inherent risk and control risk are assessed as low, the auditor can tolerate a higher detection risk (smaller sample size) for the audit on operations, and vice versa.

Example A

(low assurance from inherent and control risks):

Accepted audit risk is 5% and inherent risk for the system is assessed as 100% (in case of no controls in the systems, material misstatements are expected). During the system audits it was found that the control risks in the ENI CBC programme are rather high (for example, 50%; internal control procedures are not adequate).

Subsequently, the auditor should strive for a very low detection risk at 10%. In order to obtain a low detection risk, the amount of substantive testing and therefore sample size need to be large.

$$\begin{aligned} \text{AR} &= \text{IR} \times \text{CR} \times \text{DR} \rightarrow \text{DR} = \text{AR} / (\text{IR} \times \text{CR}) \\ \text{DR} &= 0,05 / (1 \times 0,5) = 0,1 \end{aligned}$$

Example B

(high assurance from inherent and control risks):

Accepted audit risk is 5% and inherent risk for the system is assessed as 100% (in case of no controls in the systems, material misstatements are expected). During the system audits it was found that the internal control systems are working good and control risk is only at the level of, for example, 12,5%.

Subsequently, to achieve a 5% audit risk, the detection risk level can be at 40%, the latter meaning that the auditor can accept more risks by reducing the sample size.

$$\begin{aligned} \text{AR} &= \text{IR} \times \text{CR} \times \text{DR} \rightarrow \text{DR} = \text{AR} / (\text{IR} \times \text{CR}) \\ \text{DR} &= 0,05 / (1 \times 0,125) = 0,4 \end{aligned}$$

3.3. *Audit risk assessment*

Depending on the size of the MCS, the AA should foresee the **method for the prioritization** of the audit work.

Unless the AA has the necessary resources to carry out a full audit of every MCS element established in the programme, audit priorities should be set. One of such methods (and the most commonly used) is **risk assessment**. The complexity of the MCS will define the level of details for such assessment.

When setting up the overall risk assessment method for prioritising the system audit work on the measures, bodies and internal control components, the AA should consider the relevant risk factors, set a quantification grid from low to high risk and apply them to all priorities and bodies relating to the programme(s) covered by the strategy.

Some examples of **risk factors** which may be considered are the following:

- staff experience,
- quality of internal controls,
- time since the last audit engagement,
- complexity of the organisational structure,
- type of operations and beneficiaries,
- risk of fraud,
- etc.

As a best practice, the results of the AA's risk assessment are reported in a table where the programmes and the main bodies involved in the MCS are classified by risk level. As a good practice example, the risk assessment approach described in EGESIF 'Guidance for Member States on Audit Strategy' can be applied, including the risk assessment table (Annex III of the EGESIF guidance).

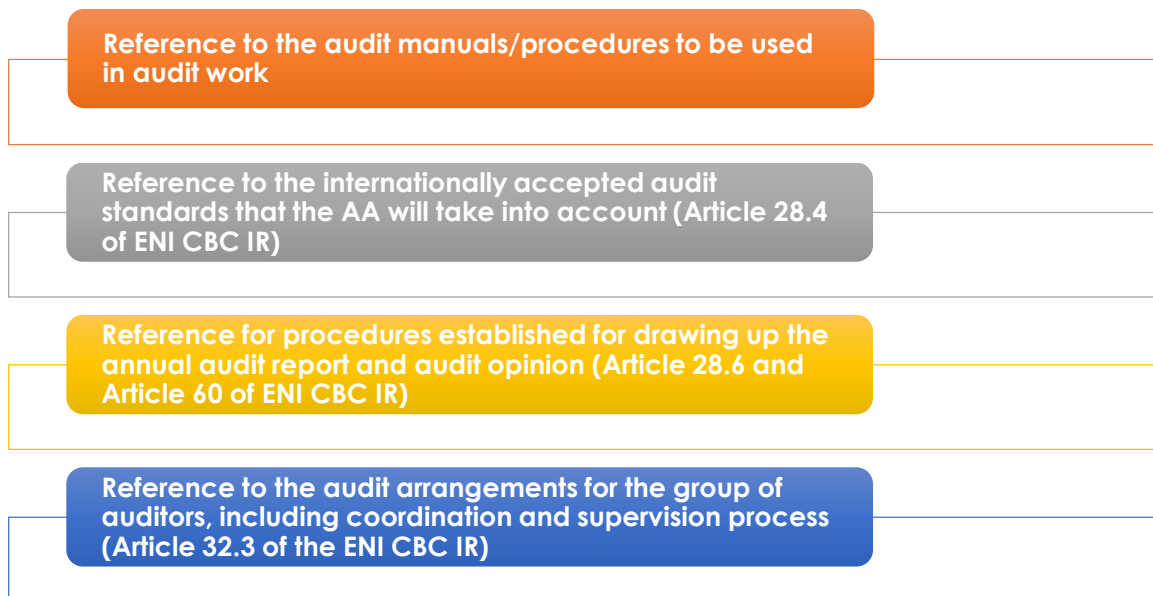
This table would need to be adapted and complemented by the AA with the risk factors that it considers the relevant ones for the programme(s) concerned. For small systems (e.g. where all bodies and main key requirements can be audited in the first exercise), the risk assessment may be less elaborated. Other risk assessment methods are also possible.

On the **basis** of the results of the **risk assessment**, the AA will be able to prioritize the **system audits** of programmes and bodies for which the detection risk is higher over the audit period.

Such prioritization should cover also the specific thematic areas. The timing and scope of the audits might also be influenced by the progress in implementation of the programme.

3.4. Methodology

3.4.1. Overview



As is the case for the introduction, a similar approach to the EGESIF ‘Guidance for Member States on Audit Strategy’ can be taken also for this section of the audit strategy. On this basis, the AA’s audit manual/procedures should provide a **description of the working procedures** for the **different phases of an audit**, this is:

- audit planning,
- risk assessment,
- performance of engagements,
- recording and documentation,
- supervision,
- reporting,

- quality assurance process and external review,
- using the work of other auditors,
- use of any computer assisted audit techniques,
- sampling methods used,
- etc.

The audit manual should contain reference to **materiality thresholds** (international standards such as ISSAI 1320 on "Materiality in Planning and Performing an Audit" and ISSAI 1450 on "Evaluation of Misstatements Identified during the Audit" can be used) and other quantitative and qualitative factors to consider when assessing the **materiality of audit findings** for system audits, audits of operations and audits of the accounts.

The audit manual should also include a **description of the different phases of reporting** (such as draft audit reports, contradictory procedure with the auditee and final audit reports), deadlines for reporting, follow-up processes.

Moreover, the audit manual should include a brief explanation of the reporting process of the AA with the coordinating body that may be designated by the Member State under article 20.5 of ENI CBC IR.

In case the AA has previous experience in the role of the AA in INTERREG/other European Structural and Investment Fund programmes and it plans to use the audit procedures already established for these programmes, it has to be remembered that these documents should be adjusted to the ENI CBC environment, especially taking into account that the system of the financing of the projects differs from the European Structural and Investment Fund programme in question.

3.4.2. Audits on management and control systems

Indication of the bodies to be audited and the related key requirements (in the context of system audits). If applicable, reference to the audit body on which the audit authority relies to perform these audits.

Indication of system audits to target specific areas (including procedures established under Article 26 of ENI CBC IR):

- **system of the administrative and on-the-spot verifications (including respect of public procurement, State aid, environmental and other rules);**
- **project selection procedures;**
- **reliability and security of computerised system for data recording and gathering;**
- **risk management;**
- **anti-fraud measures,**
- **etc.**

A complete list of the **bodies and functions** that will be covered by the system audits can be **provided in the indicative schedule** of audit assignments foreseen under this section of the audit strategy, in line with the risk assessment explained in the section above. In addition to the ENI CBC IR, the TESIM Guidance note on '*Development of the description of the management and control systems in ENI CBC programmes*' can be used as a source document for a detailed description of the bodies involved in ENI CBC programme management.

It is expected that the AA will audit all authorities and functions included in the MCS of a given programme at least once during the programming period. This should also include bodies appointed on the level of participating country (national authority, control contact points) and, where applicable, the intermediate bodies selected on the basis of the AA's risk assessment.

System audits should be carried out as from the first year of implementation of the programme, after the designation process.

The scope of the first system audits should take account of the AA work performed during the designation stage, focusing on the entities, programmes and areas where the risk is higher.

System audits should be carried out on a regular and timely basis throughout the year and in view of the expression of the annual audit opinion, covering primarily the components of internal control, as described in the Annex of the ENI CBC IR and the implementation of the procedures described in the MCS description.

In case some components of the management and control system are similar to the ones established in the previous ENPI programme, the reports of the Internal Audit Service (audit body under ENPI CBC Implementing Rules No 951/2007) can be used either during the audit risk assessment or system audit. Nevertheless, if reports are used for audit work, the AAs should obtain assurance that the part of the system in question has not undergone significant modifications.

Also, it should be remembered that there are differences in terms of internal control components between the European Structural and Investment Fund programmes and ENI CBC programmes. Please see TESIM Guidance note on 'Development of the description of the management and control systems in ENI CBC programmes' for further details. In addition, the checklist on the compliance assessment included in the TESIM 'Guidance on methodology, designation criteria and audit opinion' might be useful source of information when defining the criteria or work plan for system audits.

The AA should ensure that all **key components of internal control** are covered regularly either through **full audits or follow-up audits**. In the ENI CBC programmes, key components of internal control *are the ones indicated in the designation criteria described in the Annex of the ENI CBC IR.*

This would enable the AA to conclude on the functioning of the MCS already from the first annual audit report. Concerning the frequency and scope of system audits, the AA should decide based on its risk assessment. Similarly to

the recommendation in the EGESIF 'Guidance for Member States on Audit Strategy', ISA 330 on the auditor's responses to assessed risks can be used.

This may be complemented with focused system audits where and when considered necessary in order to cover the remaining key requirements and particular requirements where the risk is considered to be systemic.

In case of substantial changes to the MCS (for example, modification of project selection procedures), the AA should perform a new system audit, covering the new aspects, and update the risk assessment accordingly.

During site work of system audit, the auditor shall obtain sufficient and reliable evidence that the MCS in place functions effectively and as described. **Test of controls** is one of the techniques to be applied – it may include walkthrough tests of the relevant documents held by the authorities concerned, interviews with relevant staff and examination of a sample of transactions.

Taken together, sufficient testing should be carried out to enable sound conclusions to be reached on the proper functioning of the systems under examination.

If the tests of controls are used, the AA has to decide on how the sampling for these tests will be carried out. As a good source of inspiration, DG Regio's 'Guidance note on sampling methods for audit authorities' for 2007-2013 period included a dedicated section: 'Sampling techniques applicable to system audits'. The sample selection method for system audits is a matter subject to the AA's professional judgment.

As a good practice example, when determining the number of items for controls testing, one should consider certain factors (such as nature of the system, sampling approach chosen - statistical versus non-statistical -), overall number of items in population, etc.), taking account the internationally accepted audit standards (e.g. ISA 330 on the auditor's responses to assessed risks, the ISSAI 410015 on the factors to be taken when defining materiality, ISSAI 1320 on "Materiality in Planning and Performing an Audit", ISSAI 1450 on "Evaluation of Misstatements Identified during the Audit").

In the context of ENI CBC IR, it is crucial that clear communication lines between the AA and MA are established in relation to the system audits, since the frequency and coverage of the on-the-spot verifications under the responsibility of the MA will directly relate to the risk identified by the AA for the MCS as a whole.



The suggested approach concerning the materiality level in system audits is similar to the one presented in the EGESIF 'Guidance for Member States on Audit Strategy'.

*When planning a system audit, the AA should define in advance the threshold **above which a deficiency will be considered material**. For example, in the context of such audit and having tested the controls related with a given internal control element (e.g., procedures for selection of operations) on a sample of 10 grant contracts (out of a population of say 50 grants), the AA may consider that the controls for that key requirement are materially deficient (i.e., the requirement is rated at least as "works partially, substantial improvements are needed") when 4 out of 10 (i.e., 40%) of the selected grant agreements show that the controls in place were not applied or were inefficient in detecting and correcting irregular expenditure.*

*Different thresholds may be considered depending, for example, on the type of controls at stake. In any case, **the assessment of the materiality** in system audits needs also **to take account of qualitative factors**, in addition to the simple quantitative approach suggested here.*

When the system audit concludes that the deviation rate detected is higher than the materiality threshold defined by the AA for that audit, this means that the MCS does not meet the criterion set for a high assurance level. As a result, the MCS must be classified as having an average or low assurance level, with possible implications in the determination of the sample size of the audits of operations.



Concerning **system audits on the reliability of data** reporting the programme's performance, the AA should assess whether effective controls are implemented over collecting, summarizing and reporting the related data, and whether the reported compiled figures reconcile with the source data.

Regarding **system audits on the functioning of IT systems**, standards related to information technology are not as well developed or universally accepted as in some other audit areas. In addition to the COBIT framework, internationally accepted standards for information security include, but are not limited to the ISO/IEC standard 27001 ("Information technology - Security techniques - Information security management systems – Requirements") and the ISO/IEC 27002 ("Information technology - Security techniques - Code of practice for information security controls"), last re-issued in 2013. The AA may also take into consideration any related international and national standards and guidelines. In addition, TESIM '*Guide to developing Management and Information Systems in ENI CBC programmes*' specifically focuses on the requirements for establishing and assessing the functioning of such systems.

INTOSAI Capacity Building Committee published in 2015 a document called "**Managing Information Communications Technology**". The document is aimed as a support for Supreme Audit Institutions and confirms the same **standards** indicated by EGESIF for security issues as an **option** for ensuring it, but not an obligation. The document adds to them the **Information Security Forum** (<https://www.securityforum.org/>) as a source of good practices. ISSAI 5300 and ISSAI 5310 may also be used.

3.4.3. Audits on a sample of projects

Description (or reference to internal document) of the sampling methodology as required by the Article 28.1 of the ENI CBC IR

In the context of the audit strategy, the key information presented in this section is the **sampling methodology** related to the audit of projects. ENI CBC IR refer only to '*appropriate sample*' (article 28.1).

AA that are experienced with ESIF programmes are well aware of the legislative requirements and the amount of guidance documents describing the sampling methods and these documents can be used as valuable source of inspiration.

Therefore, a key task for the ENI CBC AAs is to decide what will be **appropriate sample** in the context of their **ENI CBC programme**. As the annual result of the AA is the audit opinion, it can be concluded that the **appropriate sample** is a **sample** that will allow the AA to confirm in the opinion that **the transactions are legal and regular**.

Decision on **appropriate sample** also implies a decision on the number of sampling and selection elements, for example:

- assurance/confidence level for the audit of projects,
- sampling method,
- selection method,
- population,
- sampling unit,
- materiality,
- etc.

As a good inspiration document, the EGESIF '*Guidance on sampling methods for audit authorities*' can be used, as it based on the audit assurance (risk) model and presents statistical concepts related to the audits on projects, as well as describes sampling techniques and methods in details.

The amount of the audits on the projects, will depend on the findings of the AA during the system audits. The audit assurance model, as proposed in section 3.2, implies that there are four different levels of assurance for the classification of the audited systems. The confidence level for the sampling will depend from the level of assurance from the system audits. An appropriate confidence level is a critical issue for the auditing of operations, as sample size is strongly dependent on this level (the systems with low error rate mostly will have high assurance, thus auditors can accept lower confidence level (via smaller sample) needed from audits on projects; and vice versa). However, for a number of ENI CBC programmes, especially in the beginning of the programming period, the amount of sampling population

might be too small to apply statistical sample. In this scenario, the AAs have to provide necessary justifications and use non-statistical sampling.

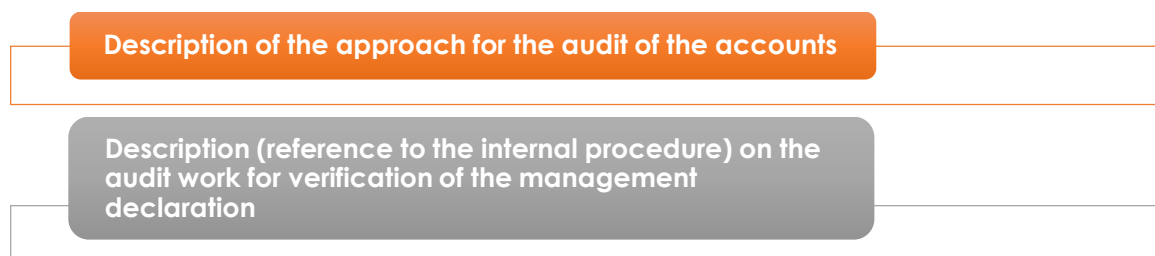
In regards to the individual audits on projects, the AAs should decide and describe in their methodology on what is the scope of each audit (i.e. 100% re-performance of the expenditure verification; reference to the eligibility rules to be followed; etc.).

In addition, the ENI CBC IR article 68.2(e) requires that an “*analysis of the nature and extent of errors and weaknesses identified*” is provided in the annual audit report. This requirement implies that the AA **should have a clear concept on the classification of errors detected** during audit on operations.

The procedure for the classification of errors should include **the following elements** in relation to each audit of operations:

- a **report or conclusion should be prepared** and attached to the audit file containing planning documentation and other documents supporting the findings;
- such report or conclusion should contain a **complete description of the findings**, covering all elements (conditions or actual situation, criteria or standard, effect and – especially - the cause of the errors), as well as the classification of each error.

3.4.4. Audits on the annual accounts of the programme and verification of the management declaration



Audit of accounts is the responsibility of the AA and article 68.2 (d) of the ENI CBC IR stipulates that the annual report of the programme shall include “**an audit opinion on the annual accounts**”, which is a separate document from the annual audit report.

In addition, article 68.4 stipulates that

*“the audit opinion (...) shall establish whether the **accounts give a true and fair view**, the **related transactions are legal and regular** and the **control systems properly put in place function**. The opinion shall also state whether the audit work puts in doubt the assertions made in the **management declaration** referred (...)”.*

Therefore, the opinion cannot only be based on a pure financial check of the accounts, but also need to take into account the results of the **systems audit** and the **audit on projects**. To this end, cross-references could be made to the relevant sections of the annual audit report required by article 68.2 (e) of the ENI CBC IR, and the AA should give a brief description of the audit approach that it uses to audit the accounts in order to reach an audit opinion for each accounting year.

TESIM has developed a detailed ‘Guide to programme accounts, audit and reporting to EC in ENI CBC programmes’ that can be used as a source of information when preparing and planning the audit on accounts.

The AA should explain how it plans to draw assurance that **the accounts give a true and fair view**, on the basis of:

- its **system audits**;
- its **audits** on an appropriate sample **of projects**;
- its **assessment of the management declaration** and the annual summary;
- the nature and extent of the testing done on the accounts submitted.

It should be taken into account (especially in relation to the last two bullet points), that the AA should describe how it intends to carry out its verifications, taking into account the deadline of 15 February for submission of the documents to the European Commission, as set out in the article 68.2. In practical terms, these verifications should take place well in advance.

The AA and MA should strive to agree on the appropriate internal deadlines for submitting the annual accounts to the AA, so the AA can carry out its work, especially in relation to the assessment of management declaration and accounts.

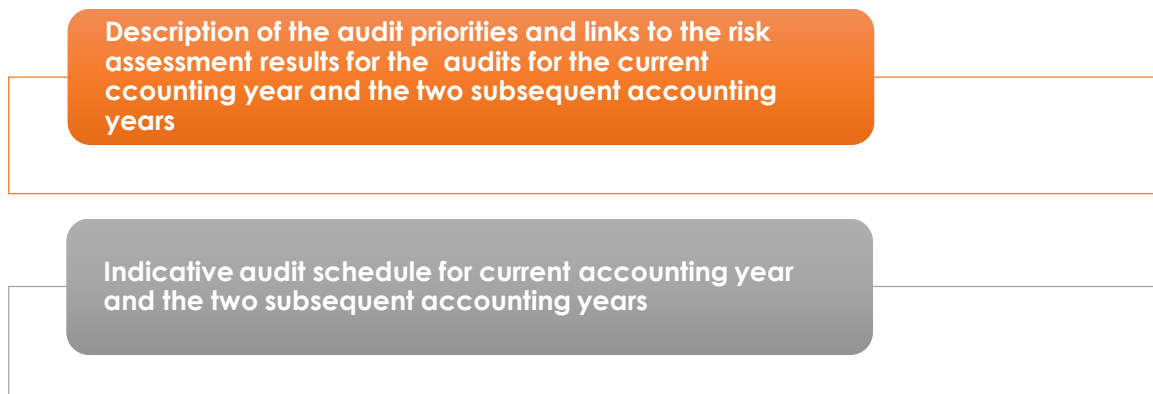
*In practice, the annual accounts have to be presented to the EC by 15 February of year N for the accounting year ending on 30 June of previous year. It leaves 7,5 half months **both for the MA and the AA.***

Special attention could be paid to the analysis of the annual summary of the controls carried out by the MA (article 68.2 (c)) in the context of the system audits carried out by the AA itself.

3.4.5. Audit opinion

TESIM's proposal on the audit opinion for the accounts is included in its 'Guide to programme accounts, audit and reporting to EC in ENI CBC programmes'.

3.5. Audit work plan



Article 28.5 requires that the AA presents the

*“planning of audits for the **current accounting year** and the **two subsequent accounting years**”.*

While the ENI CBC IR do not explicitly require to present the reasons for selecting specific audits for their inclusion in the audit plan, best practice would be to describe the criteria used to determine the audit priorities and the justification as an evidence that **a due planning process** was carried out.

The results of the risk assessment exercise should be the main basis for prioritising the system audit work.

In addition, the AA can consider preparing a general plan for the whole programme implementation period to cover the entire MCS in order to obtain reasonable assurance on their functioning, in addition to the mandatory plan for the current accounting year and the subsequent two accounting years.

Authorities/ bodies or topics to be audited	Body responsible for auditing	Result of risk assessment	20XX Audit objective and scope	20XX+1 Audit objective and scope	20XX+2 Audit objective and scope

3.6. Audit resources

While explicitly not required by the ENI CBC IR, the audit strategy could optionally indicate the **human resources in auditor-days available** (or to be mobilised) to accomplish its objectives for the coming years, including the resources of other audit bodies and outsourced audit activities.

Whenever possible, it is recommended to indicate **separately the auditor-days** available at the level of the **AA**, the **group of auditors** and **outsourced activities**. An indication of available auditor-days per audit type (system audit, audit of accounts and audit of operations) could be included as well.

4. Timeline for ENI CBC audit work

