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GUIDELINE NO 2 – CAP STRATEGIC PLAN EXPENDITURE

GUIDELINE ON THE ANNUAL CERTIFICATION AUDIT EAGF/EAFRD EXPENDITURE

Financial Year (FY)2023

(TO ADDRESS THE REQUIREMENTS FOR THE CERTIFICATION BODIES PURSUANT TO ARTICLE 12 OF REGULATION (EU) NO 2021/2116 ON THE FINANCING, MANAGEMENT AND MONITORING OF THE COMMON AGRICULTURAL POLICY)

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TABLE OF CONTENTS

List of annexes

Abbreviations used:

AMS:	Area Monitoring System
APR:	Annual Performance Report
CB:	Certification Body
CR:	Control Risk
CST:	Control statistics
DR:	Detection Risk
EC:	European Commission
ECA:	European Court of Auditors
EU:	European Union
GSA:	Geo-Spatial Application
IACS:	Integrated Administration and Control System
ICS:	Internal Control System
ISAP:	Identification System for Agricultural Parcels
ITGSs:	Information Technology General Controls
IR:	Inherent Risk
MCS:	Management and Control System (within the understanding of Article 1 of Regulation (EU) No 1306/2013 and Commission Implementing Regulation (EU) No 908/2014)
MD:	Management Declaration
MS:	Member State
MUS:	Monetary Unit Sampling
OTSC	On-the-spot check
PA:	Paying Agency
QA:	Quality Assessment
RD:	Rural Development
WCGW:	"What Can Go Wrong" (within the content of the review of the control procedures)

1. PURPOSE

The objective of this document is to provide guidance to Certification Bodies (CBs) in the establishment of their audit strategy in their tasks of gathering sufficient, appropriate audit evidence to issue an audit opinion. Under Article 12(2) of Regulation (EU) 2021/2116, the audit opinion is to be drawn up in accordance with internationally accepted audit standards and should cover:

- the true and fair view of the annual accounts,
- the proper functioning of the Member States' governance systems, in particular:

  (i) the governance bodies referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and Article 123 of Regulation (EU) 2021/2115;

  (ii) the basic Union requirements;

  (iii) the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115;

- the performance reporting on output indicators for the purposes of the annual performance clearance and on result indicators for the multiannual performance monitoring,
- the legality and regularity of the expenditure for the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013 and (EU) No 1308/2013 and in Regulation (EU) No 1144/2014 for which reimbursement has been requested from the Commission.

The CB's opinion shall also state whether the examination puts in doubt the assertions made in the management declaration.

The above opinion shall accompany the set of documents to be submitted to the Commission by 15 February of the year following the financial year (FY) concerned, by the person in charge of the Paying Agency (PA). These documents consist of:

- the annual accounts,
- the annual performance report showing that the expenditure was effected in accordance with Article 37 of Regulation (EU) 2021/2116,
- an annual summary of final audit reports and of controls carried out, including an analysis of the nature and extent of errors and weaknesses identified in relation to the governance systems, and the corrective action taken or planned, as provided for in Article 63(5), point (b), of the Financial Regulation,
- the management declaration as to:

  (i) the fact that the information in the annual accounts is properly presented, complete and accurate, as provided for in Article 63(6), point (a), of the Financial Regulation

  (ii) the proper functioning of the governance systems put in place, with the exception of the competent authority referred to in Article 8, the

coordinating body referred to in Article 10 and the certification body referred to in Article 12 of Regulation (EU) 2021/2116.

As per Article 6(4) of Regulation (EU) 2022/128 the "Commission shall establish guidelines, which contain, in particular: (a) further clarification and guidance in respect of the certification audit to be performed; (b) the determination of the reasonable level of audit assurance to be achieved from auditing." The present Guideline outlines the proposed audit methodology to be followed to allow the CB to express an opinion as referred to above.

The proposed methodology defines the four audit objectives and proposes the audit approach to be followed:

- **Audit Objective 1**: Audit on the annual accounts;
- **Audit Objective 2**: Member States' governance systems (including the performance reporting system);
- **Audit Objective 3**: Audit on the correctness of annual performance report on output and results indicators;
- **Audit Objective 4:** Audit on the legality and regularity of the underlying transactions as regards the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013, (EU) No 1308/2013 and (EU) No 1144/2014, as well as for the crop-specific payment for cotton and support for early retirement under Title III, Chapter II, Section 3, Subsection 2, and Article 155(2), respectively, of Regulation (EU) 2021/2115 (i.e. expenditure not covered by the CAP Strategic Plans) and / or the expenditure of measures / schemes approved before 1 January 2023.

The Guideline also covers how the results should be interpreted and where, based on the audit results, additional work may be required, so as to allow the CB to reach a conclusion on the financial and residual risks at Fund or other relevant level in respect of:

- the annual accounts
- the governance systems,
- the annual performance report,
- the legality and regularity of transactions, where applicable and
- the related management declarations of the PA and if applicable Coordinating Body in the given financial exercise.

PART A gives guidance on the audit of the annual accounts.

PART B explains the work to be done on the audit of the functioning of the governance systems.

PART C explains the work to be done on the audit of the correctness of performance reporting on output and results indicators.

PART D explains the work to be done on the audit of the legality and regularity of expenditure for the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013 and (EU) No 1308/2013 and in Regulation (EU) No 1144/2014 of the European

Parliament and of the Council as per Article 12 (d) of Regulation (EU) 2021/2116 (i.e. expenditure not covered by the CAP Strategic Plans) as well as for the crop-specific payment for cotton and support for early retirement under Title III, Chapter II, Section 3, Subsection 2, and Article 155(2), respectively, of Regulation (EU) 2021/2115 and / or the expenditure of measures / schemes approved before 1 January 2023, and for which reimbursement has been requested from the Commission.

PARTs A, B and C cover the review and assessment of the Member States' governance systems respectively. Furthermore, the relevant parts of the audit work under PARTs A, B, C and D contribute to the assessment of the PA's compliance with the accreditation criteria. PART B also covers the Coordinating Body's compliance with the related accreditation criteria.

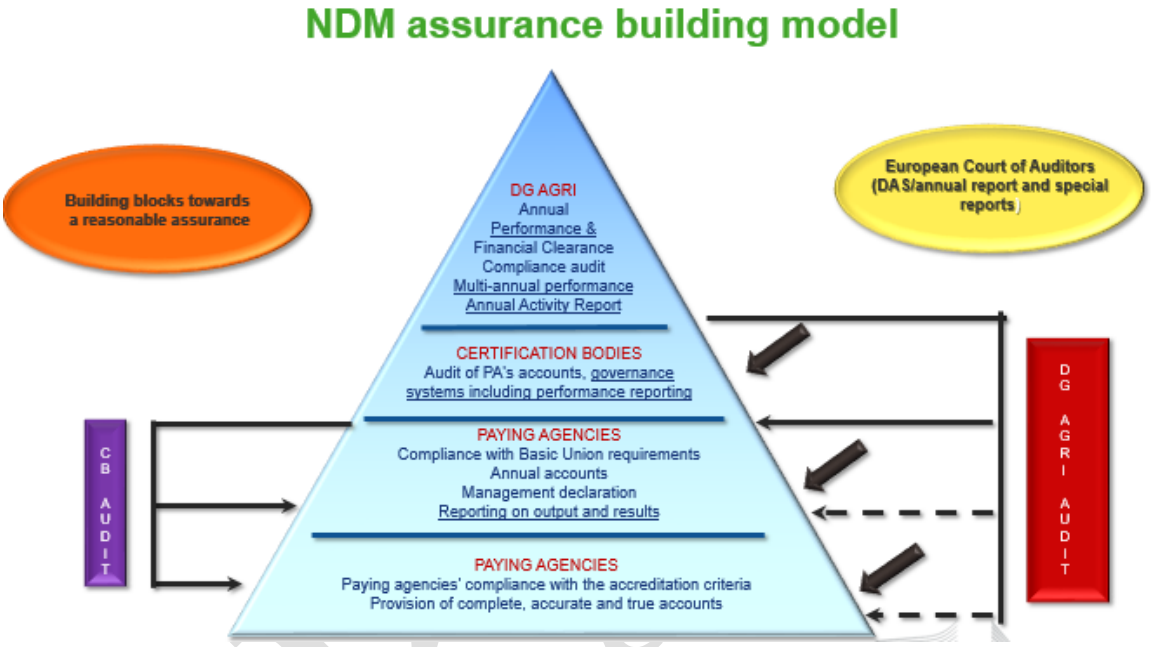
PART E defines the method for aggregating audit results for the audit opinion and it also outlines how to interpret and use the audit results. It also explains how to use the audit results gained for PARTs A, B, C and D for giving an opinion on the assertions made in the management declarations.

This guideline will be fully completed for PART D as from FY2024 onwards (see PART D) and will be reviewed and updated on a periodic basis, taking into account the experience gained.

2. ASSURANCE MODEL AND LEGAL BACKGROUND

2.1. Assurance model

Assurance is an objective examination of evidence for the purpose of providing an assessment of the effectiveness of risk management, control and governance processes. 99 % of CAP expenditure is disbursed under a set-up of shared management with the Member States. DG AGRI's assurance that is expressed in a declaration of assurance in the annual activity report (AAR) is built on the following building blocks in respect of expenditure effected under shared management:



(1) In broader terms the Member States need to set up the management and control system of the CAP under the shared management system of the Funds. More concretely, the MSs need to set up governance bodies, including the PA which is in compliance with the accreditation criteria set for the PAs (Article 1 and Annex I of Commission Delegated Regulation (EU) 2022/127), and, in case of MS with more than one PA, the Coordinating Bodies (Article 2 and Annex II of Commission Delegated Regulation (EU) No 2022/127) as regards the compilation of the Annual Performance Report. Moreover, PAs need to ensure the completeness, accuracy and veracity of the annual accounts, (as per Article 32 of Commission Implementing Regulation (EU) 2022/128).

(2) The management and control system implemented by the MSs in accordance with Article 59(2) of Regulation (EU) 2021/2116 shall ensure compliance with the basic Union requirements governing Union interventions. Member States shall ensure that a level of checks needed for an effective management of the risks to the financial interest of the Union is carried out. The results of these controls are

reflected in the Management Declaration (Article 3, Article 33 and Annex 1 of Regulation (EU) 2021/2116).

(3) The CBs will need to audit the previous two blocks and provide an opinion in accordance with Article 12(2) of Regulation (EU) 2021/2116 on the basis of the audit strategy to be developed in accordance with the present document. Thus, the audit strategy is to be considered a significant part of the annual certification audit.

(4) DG AGRI takes into account the previous three blocks, in addition to its own clearance of accounts procedure and the external auditors' (ECA) reports in order to provide assurance as regards expenditure disbursed.

In conclusion, the aim of the above-described control and audit system that derives from the paragraphs (4) and (5) of Article 63 of Regulation (EU) 2018/1046 (the Financial Regulation) and Regulation (EU) 2021/2116 is to provide an overall assurance on the true and fair view of the accounts, the reliability of the governance systems including the accredited PA and if relevant Coordinating Body; the reliability and correctness of data provided in the annual performance report; and therefore, on the risk of serious deficiencies in the governance systems and errors in the accounts or annual performance report.

On that basis, the CBs' assurance is built on four parts as defined in the audit opinion to be issued by the CBs in accordance with Article 12(2) of Regulation (EU) 2021/2116 on:

- the true and fair view of the PA's annual accounts;
- the proper functioning of the MS's governance systems;
- the performance reporting on output and result indicators;
- the legality and regularity of the expenditure for the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013 and (EU) No 1308/2013 and in Regulation (EU) No 1144/2014 of the European Parliament and of the Council as per Article 12 (d) of Regulation (EU) 2021/2116 (i.e. expenditure not covered by the CAP Strategic Plans) as well as for the crop-specific payment for cotton and support for early retirement under Title III, Chapter II, Section 3, Subsection 2, and Article 155(2), respectively, of Regulation (EU) 2021/2115 and / or the expenditure of measures / schemes approved before 1 January 2023, and for which reimbursement has been requested from the Commission.

The CBs' assurance model is based on the evaluation of the functioning of the governance systems via compliance testing and assessment of the systems/processes/procedures in place for the expenditure effected under the CAP Strategic Plan. For the expenditure effected outside the Strategic Plan the CBs will complement the compliance testing with) the substantive testing of a number of files in order to verify the legality and regularity of the transactions throughout the whole cycle until the authorisation of the payment.

This model should allow the CBs to:

- assess and conclude on the proper functioning of the governance systems including the PA's compliance with the accreditation criteria on the basis of compliance testing and also testing of IT general controls and application controls, for the purpose of verification of the system design and implementation;

- assess and express an opinion on the effectiveness of the performance reporting system on the basis of testing of records and databases to verify if reported performance output and result indicators are correctly reported and match the expenditure financed by the Union. The audit work should also lead to a confirmation as regards the reconciliation of the annual net expenditure declared for an intervention and the gross expenditure used for the calculation of the relevant output and result indicators, a review and confirmation of the justification provided by the Member State as per Article 134(8) of Regulation (EU) 2021/2115 and a verification of the calculation (including algorithms used in the system) for the indicators;

- give an opinion on the legality and regularity of the expenditure not covered by the CAP Strategic Plans, which results from the confirmation of the error rates as reported in the control statistics and /or the management declaration;

- express an opinion on the reliability of the annual accounts which are based on the declarations of expenditure to the Commission.

2.2. Legal background

The legislation governing the financial clearance of accounts, management reporting and related certification procedures is summarized below:

Paying Agencies (PAs)

According to the provisions of Article 53 of Regulation (EU) 2021/2116, the clearance of the accounts of the accredited PAs shall be based on the information transmitted pursuant to Article 90(1)(c) of the same Regulation.

The PA should provide the Commission with the following documents on the annual expenditure under the EAGF and EAFRD, and the related transactions carried out and the internal control system in place:

- Annual accounts as per Article 9(3) of Regulation (EU) 2021/2116,

- Annual performance report showing that the expenditure was effected in accordance with Article 37 of Regulation (EU) 2021/2116,

- Management Declaration as per Article 3 and Annex 1 of Regulation (EU) No 908/2014, including an annual summary of final audit reports and of controls carried out, including an analysis of the nature and extent of errors and weaknesses identified in the governance systems, and the corrective action taken or planned, as provided for in Article 63(5), point (b), of the Financial Regulation.

For the Management Declaration, PAs also need to submit the control data and statistics as per Commission Implementing Regulation (EU) No 809/2014 and the other relevant sectoral regulations as regards the expenditure covered under PART D.

Coordinating Body

When more than one PA is accredited in a Member State, a Coordinating Body shall be designated. The Coordinating Body will collect and send the necessary information to the Commission, supply the Annual Performance Report at Member State level, submitted to the Commission together with a management declaration covering the compilation of the entire report. The latter management declaration should be submitted by the Coordinating Body as per Article 10 (3) of Regulation (EU) 2021/2116.

Applicable guidelines/communication to the Agricultural Funds Committee:

- Guideline no 1 on Accreditation,
- Guideline no 4 on the Management Declarations,
- Guideline no 5 on Irregularities
- Annual Note on the information to be submitted on the annual accounts.

Certification Bodies

Rules concerning the tasks of the CBs, including the checks, the opinion and the reports to be drawn up by those bodies, together with the documents accompanying them, are laid down in Article 12 of Regulation (EU) 2021/2116 and in Articles 5-7 of Regulation (EU) 2022/128. The Certification Bodies are required to carry out the certification audit and prepare a certification report and opinion accordingly.

Applicable guidelines:

- Guideline no 2 on the audit strategy
- Guideline no 3 on the CBs' reporting requirements

Overall, this guideline addresses the requirements of Article 12 of Regulation (EU) 2021/2116, aligned with those of paragraphs (4) and (5) of Article 63 of Regulation (EU) No 2018/1046 (the Financial Regulation).

3. AUDIT OBJECTIVES

3.1. Audit objective 1

The audit objectives are defined by the above-described assurance model. The CBs need to certify that:

- the accounts to be transmitted to the Commission give a true and fair view,
- the PA's internal control procedures have operated satisfactorily.

The CBs' opinion should also state whether the examination puts in doubt the assertions made in the management declaration.

Audit objective 1 is to provide assurance for the financial clearance of accounts decision through the audit of the annual accounts and the control procedures respectively.

PART A of this Guideline sets out the basis for the audit targeting audit objective 1.

As a result of the application of this audit approach the CBs will be able to provide an opinion on:

(1) The effectiveness of the PA's internal control system (ICS), including the management and control system (MCS) (as regards the respective control procedures: execution of payment, accounting for payment, management of irregularities and debts);

(2) The true and fair view given by the annual accounts (considering the results of the substantive testing and the reconciliation work).

3.2. Audit scope for audit objective 1

The audit under audit objective 1 is directed towards the annual accounts of the PA. Thus, this audit objective covers the following control procedures for operational transactions:

(1) execution of payments,

(2) accounting for payments,

(3) for non-operational transactions: managing irregularities and debts, including off-setting and accounting for recoveries,

(4) reconciliations and compilation of declarations performed on payments and non-operational transactions effected within the financial year.

3.3. Audit objective 2

The audit objectives are defined by the above-described assurance model. The CBs need to certify that: the Member States' governance systems put in place function properly, in particular:

(i) the governance bodies referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and Article 123 of Regulation (EU) 2021/2115,

(ii) the basic Union requirements referred to in Article 2(c) of Regulation (EU) 2021/2116,

(iii) the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115 (the results of audit objective 3 will need to be taken into account under audit objective 2 as regards the overall evaluation of the performance reporting system).

PART B of the Guideline sets out the basis for the audit targeting audit objective 2.

By applying this audit approach, the CBs will be able to provide an opinion on the proper functioning of the Member States' governance systems.

3.4. Audit scope for audit objective 2

The audit work done within the scope of Audit objective 2 covers the governance systems of the Member State including:

(i) the governance bodies referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and Article 123 of Regulation (EU) 2021/2115 (Thus it means the accredited Paying Agency and Coordinating Body. Other bodies would be covered just up to the extent of their role in functioning and implementation of the basic Union requirements);

(ii) the basic Union requirements referred to in Article 2(c) of Regulation (EU) 2021/2116 (and as specified in the non-exhaustive reference list of basic Union requirements);

(iii) the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115 (deriving from the work under audit objective 3).

3.5. Audit objective 3

The audit objectives are defined by the above-described assurance model. The CBs need to certify that: the performance reporting on output indicators for the purposes of the annual performance clearance referred to in Article 54 of Regulation (EU) 2021/2116 and result

indicators for the purposes of the multiannual performance monitoring referred to in Article 128 of Regulation (EU) 2021/2115, demonstrating that Article 37 of Regulation (EU) 2021/2116 is complied with, is correct.

PART C of the Guideline sets out the basis for the audit targeting audit objective 3.

By applying this audit approach, the CBs will be able to provide an opinion on:

(1) The effectiveness of the reporting system, as part of the management and control system (MCS) (as regards the respective procedures: data capturing and reporting system and procedures within the PA and from external sources);

(2) The correctness of the annual performance report (Including the confirmation of the reconciliations and justifications provided with the annual performance report).

3.6. Audit scope for audit objective 3

The audit work done within the scope of Audit objective 3 covers the performance reporting system and the correctness of the actual annual performance report.

3.7. Audit objective 4

The audit objectives are defined by the above-described assurance model. The CBs need to certify that:

- expenditure for the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013, (EU) No 1308/2013 and in Regulation (EU) No 1144/2014 of the European Parliament and of the Council as per Article 12 (d) of Regulation (EU) 2021/2116 (i.e. expenditure not covered by the CAP Strategic Plans) as well as for the crop-specific payment for cotton and support for early retirement under Title III, Chapter II, Section 3, Subsection 2, and Article 155(2), respectively, of Regulation (EU) 2021/2115 and / or the expenditure of measures / schemes approved before 1 January 2023, for which reimbursement has been claimed is legal and regular, and

- the PA's internal control procedures have operated satisfactorily.

Audit objective 4 is to provide assurance on the legality and regularity of expenditure for which reimbursement has been requested from the Commission. It is to be achieved through the audit of the legality and regularity of expenditure and the control procedures respectively.

PART D of the Guideline sets out the basis for the audit targeting audit objective 4.

By applying this audit approach the CBs will be able to provide an opinion on:

(1) The effectiveness of the ICS and/or MCS of the PA (as regards the respective control procedures: administrative and on-the spot controls);

(2) The legality and regularity of expenditure for which reimbursement has been requested from the Commission.

3.8. Audit scope for audit objective 4

Scope of Audit objective 4 is the legality and regularity of expenditure referred to in point 3.7. The audit work done within the scope of Audit objective 4 covers the control data and control reports of the PA for certain measures that are reported in the control statistics. All the control procedures (administrative and on-the-spot controls, reconciliations and compilation of management declarations) performed for authorization for payments effected for the transactions reported in the control statistics/control reports should be included in the audit scope.

3.9. Audit work as regards assertions made in the Management Declaration

The CBs' opinion should also state whether the examination puts in doubt the assertions made in the management declaration. The audit work in this respect is already covered under the 4 audit objectives. PART E explains how the audit results already gained can be used for concluding as regards the assertions made in the Management Declaration by the Director of the Paying Agency and the one by the Coordinating Body on the compilation of the Annual Performance Report.

The CBs should draw up a report of their findings and reflect the result in their opinion. The report and opinion should follow the format set out in Guideline No 3 on the Reporting requirements. The audit objectives, audit approach and audit results as used in DG AGRI's assurance procedures as regards PARTs A, B, C and D of the Guideline are summarized in the table below.

Audit objectives, approach and results as used in DG AGRI's assurance procedures

Audit Objectives	Audit approach	Audit results	Use by DG AGRI

Audit objective 1
 	
To express an opinion on:
• The proper functioning of the control systems put in place (compliance with the accreditation criteria – execution of payment, accounting for payment, recording of debts),
 	
• The true and fair view of the annual accounts.
	Main audit procedures:
	• Review of the ICS (test of IT systems, procedures, compliance testing).
	
	• Substantive testing:
	
	  • verification of payment execution and accounting,
	
	  • irregularities, debts
	• Review of reconciliation:
	
	  • financial reconciliations
		a) Measurement of the effectiveness of the ICS of the PA: **grading for the respective control procedures**, based on
		
		  • The review of the internal control system
		
		  • The results of substantive testing: **error rate**
		
		b) **Audit opinion** on the true and fair view of the annual accounts based on the financial reconciliation and point a).
			After validating the CBs' opinion by assessing the CBs' report, the audit results are to be considered in the **financial clearance exercise for the conclusion as regards financial clearance decision**.
			
			Conformity audits on governance systems: payment/accounting and debt management functions of the PA could be launched based on these results, if considered necessary.

Audit Objectives	Audit approach	Audit results	Use by DG AGRI

Audit objective 2
 	
To express an opinion on:
• The proper functioning of the governance systems as regards:
  • the relevant governance bodies;
  • basic Union requirements; including
  • the reporting system (resulting from the work under audit objective 3).
	Main audit procedures:
	• Review of control environment, risk analysis;
	• Compliance testing to confirm control set-up and design.
	Review of management reports:
	• Action Plans
	• Management declaration
		a) Measurement of the effectiveness of the governance systems of the Member State: **grading for the respective elements/blocks**, based on
		• The review of the control environment;
		• The results of compliance testing: **deficiencies found**
		b) **Audit opinion** on the functioning of the governance systems: governance bodies; functioning/implementation of basic Union requirements; reporting systems. (as a result of AO3)
		c) **Negative opinion** on the assertions included in the MD, based on points a) and b) and review of management reports.
			After validating the CBs' opinion by assessing the CBs' report, the audit results are to be considered in the **AAR procedure as regards assurance gained from the CBs' assessment of the governance systems**.
			
			Conformity audits on governance systems: serious deficiencies reported are to be followed up through conformity clearance enquiries and implementation of action plans. These could relate to the accreditation of the PAs, CoBs or system weaknesses in the governance systems as regards functioning/implementation of basic Union requirements.

Audit Objectives	Audit approach	Audit results	Use by DG AGRI

Audit objective 3
To express an opinion on:
• the functioning of the reporting system;
• correctness of Annual performance report as regards:
  • output indicators for the annual performance clearance;
  • result indicators for the multi-annual performance monitoring.
	Main audit procedures:
	• Review of control environment (data capturing and reporting systems and procedures);
	• Compliance testing to confirm control set-up and design;
	• Substantive analytical procedures.
	Review of management reports:
	• Annual performance report (including reconciliation and justifications)
	• Management declaration
		a) Measurement of the effectiveness of the reporting system: **grading** for the respective procedures, based on
		• The review of the control system (and if deemed necessary compliance testing) - to be considered under the audit opinion of AO2
		• The results of substantive analytical procedures: **reporting errors found.**
		b) Audit opinion on the correctness of the Annual performance report based on point a)
		c) Negative **opinion** on the assertions included in the MD, based on points a) and b).
			After validating the CBs' opinion by assessing the CBs' report, the audit results are to be considered in the **clearance exercise for the conclusion as regards the performance clearance decision**.

Audit Objectives	Audit approach	Audit results	Use by DG AGRI

Audit objective 4
 	
To express an opinion on:
 	
• The proper functioning of the control systems put in place (compliance with the accreditation criteria),
 	
• The legality and regularity of expenditure declared to the Fund,
 	
• The assertions included in the MD,
 	
• The system of specific measures/schemes as regards control rate reduction (if applicable).
	Main audit procedures:
	• Review of the ICS (test of procedures, compliance testing).
	
	• Substantive testing:
	
	  • verification of authorization for payments (administrative and on-the-spot checks)
	• Review of management reports:
	
	  • Control statistics, other control reports
	  • Action Plans
	  • Management declaration
		a) Measurement of the effectiveness of the ICS of the PA: grading for the respective control procedures, based on
		
		  • The review of the internal control system
		
		  • The results of substantive testing: **incompliance rate**
		
		b) **Audit opinion** on the legality and regularity of expenditure declared to the Fund based on point a).
		
		c) **Negative opinion** on the assertions included in the MD, based on points a) and b) and review of management reports
			After validating the CBs' opinion by assessing the CBs' report, the audit results are to be considered in the establishment of the **level of risk** in **DG AGRI's annual activity report as regards the expenditure outside CAP Strategic Plan**.
			
			Conformity audits on payment authorisation controls of the PA could be launched based on these results.
			
			If the CB's work on legality and regularity is considered reliable, the CB's results are to be considered as **DG AGRI's own results**.

4. AUDIT RISK MODEL AND AUDIT PROCEDURES

The objective of the CB is to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement, through designing and implementing appropriate responses to the risks identified through the course of the audit.

4.1. Audit risk model

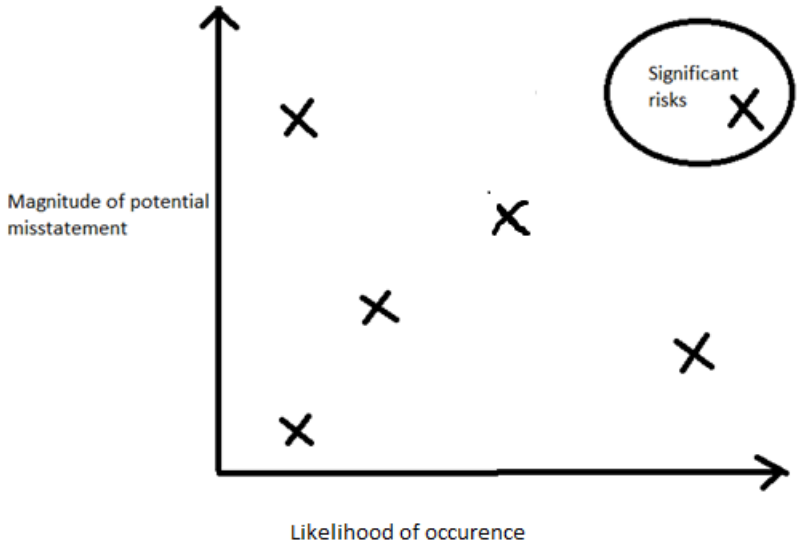
An audit risk model is necessary for planning the audit engagement and for determining the audit procedures.
The **audit risk (AR)** is the risk that the auditor issues an unqualified opinion, when the declaration of expenditure contains material errors or the annual performance report contains incorrect data. The CB needs to obtain a 95% level of assurance from its audit procedures in order to be able to state in its audit opinion that it has "reasonable assurance". Accordingly, the audit risk is 5%. This assertion is fully applicable to Audit Objectives 1, 3 and 4. For Audit Objective 2, the AR is the risk that the auditor issues an unqualified opinion, when the Member State's governance systems do not function properly.
The three components of audit risk are referred to respectively as inherent risk (IR), control risk (CR) and detection risk (DR), reflected in the Audit risk model as follows:

$$AR = IR \times CR \times DR$$

The **inherent risk (IR)** is the perceived level of risk that a material error may occur in the certified statements of expenditure to the Commission, or underlying levels of transactions, in the absence of internal control procedures. The inherent risk is linked to the activities of the paying agency and will depend on external factors (cultural, political, economic, business activities, clients and suppliers, etc.) and internal factors (type of organisation, procedures, competence of staff, recent changes to processes or management positions, complexity of the operations, amount at stake, etc.). For Audit Objective 2, the IR is the perceived level of risk serious deficiencies in the subject matter information (Member State's governance systems) may occur.

The IR needs to be assessed before starting detailed audit procedures (interviews with management and key personnel, reviewing contextual information such as organisation charts, manuals and internal/external documents). The CB should assess the inherent risk at the relevant level (stratum, population, basic Union Requirements (BUR), etc.), and it may assess the inherent risk as high or low. Based on its professional judgement, the CB should identify risks among the inherent risks that require special consideration (i.e. they constitute a significant risk[1]). Significant risks may involve schemes / interventions/ transactions/ BUR/ control environments that are complex, managed by third parties, are prone to fraud, are subject to a high degree of subjectivity, etc. For instance, if all previous conditions are present, the starting point for this element should be high inherent risk. Should the CB consider that a 'population' has a low inherent risk, this judgement should be explained in the audit strategy and in the certification report.

[1] Significant risk- an inherent risk with both a higher likelihood of occurrence and a higher magnitude of potential misstatement which requires special audit considerations.



The **control risk (CR)** is the perceived level of risk that a material error or a significant deficiency will not be prevented, detected and corrected by the management's internal control procedures.

As such, the control risks relate to how well inherent risks are managed (controlled) and will depend on the given governance system including application controls, IT controls and organisational controls. Control risks can be evaluated by means of system audits (mostly to be used for all audit objectives) - detailed tests of controls and reporting (for some of the audit objectives when considered necessary), which are intended to provide evidence about the effectiveness of the design and operation of a control system in preventing or detecting material errors and serious deficiencies. The CR should be assessed as: low (rely on controls) or high (cannot rely on controls). More details are provided in PART B of this guideline with regard to Audit Objective 2.

The combined risk assessment, i.e. (IR x CR) should be evaluated based on the knowledge and experience of the auditors as minimal, low, moderate or high rather than using precise probabilities. If major weaknesses are identified during the systems audit, the control risk is high and the assurance level to be obtained from the system would be low (moderate or high combined risk assessment). If no major weaknesses exist, the control risk is low and if the inherent risk is also low, the assurance level obtained from the system would be high (minimal combined risk assessment).

		Control Risk Assessment	
		Rely on controls (Low)	No reliance on controls (High)
Inherent risk assessment	Low	**Minimal**	**Moderate**
	High	**Low**	**High**
	Significant risk	Special audit considerations	

Further explanations are outlined in the relevant sections, e.g. section 6: Assessment of the internal control system as regards Audit Objective 1.

The product of inherent and control risk is referred to as the risk of material error or serious deficiency.

$$AR = risk\ of\ material\ misstatement\ x\ DR$$

The risk of material error or serious deficiency relates to the result of the system audits.

The **detection risk** is the perceived level of risk that a material error or a serious deficiency will not be detected by the auditor. Detection risks are related to how adequately the audits are performed, including sampling methodology, competence of staff, audit techniques, audit tools, etc. Detection risks are related to performing audits of systems, including compliance (i.e. directed to the confirmation of the implementation of controls) or substantive testing (i.e. tests of details on transactions, usually based on sampling of operations where applicable e.g. Audit Objective 4). The detection risk can be determined based on the defined audit risk, inherent risk and control risk.

$$DR = AR/(IR \times CR)$$

4.2. Assurance levels for audit procedures

The CB's risk assessment procedure is meant to identify and assess the **risk of material misstatement and serious deficiencies**. Later in the guideline, it is explained how to design and implement overall responses through audit procedures and tests to address the assessed risks of material misstatement or serious deficiency.

This risk assessment includes the evaluation of the IR and CR through several steps which should be summarized in the audit strategy/plan. Internationally accepted audit standards generally list the following steps:

(1) **Understanding the entity and its environment**, which should include:

- The control environment (mainly implemented and functioning Basic Union Requirements), including the applicable legal and regulatory framework, based on existing knowledge of the management and control systems in place, and in particular risks identified in prior periods. The risk assessment should be continuously updated by relating the CB's audit findings to potential improvements and by taking into account findings of other auditors, such as the ECA, Directorate Assurance and Audit of DG AGRI, etc.
- The control activities related also to the implementation and functioning Basic Union requirements (primary and monitoring) and those embedded in the information system supporting the main processes; the auditor should evaluate the design of those controls and determine whether they have been implemented and are applied in practice (the components of the Governance System are detailed in the Regulation (EU) 2022/127, in the matrix and reference list of Basic Union requirements and Guideline 1 on the accreditation criteria).

(2) **Assess the changes (if any) to the Governance Systems** since the last audit. The CB has to assess the impact of changes in the organisational and procedural arrangements since the previous audit, thereby assessing the extent to which the PA (and Coordinating Body) continue to meet the accreditation criteria.

(3) **Assess the risk management effectiveness,** by focusing on the following objectives for the management: understand and prioritize risks**,** identify controls addressing the key risks, including fraud risks, identify information

that will persuasively indicate whether the governance systems are operating effectively, develop and implement procedures to evaluate that persuasive information.

(4) **Confirm risks and target functions**. The risks of material misstatements or serious deficiencies may be broken down into two components (inherent risks and control risks), that have to be assessed at each assertion level for transactions (operational and non-operational), accounts, records and elements of controls environments depending on the audit objective. Nevertheless, the extent of verifications should depend on the confirmed risks and their potential impact and may include specific control functions[2] to be assessed regularly (every reporting year).

4.3. Using audit evidence obtained in previous audits and from other auditors

The CB's audit work can be rationalised by relying on the audit evidence from a previous audit for the operating effectiveness of specific controls. To this end, the CB should establish whether the results of previous audits continue to be relevant, by assessing whether significant changes in those controls have occurred subsequent to the previous audit. The CB carries out this assessment through the performance of inquiries combined with observations or inspections, to confirm the understanding of those specific controls (see ISA 330 par. 14):

(1) If there have been changes that affect the relevance of the audit evidence from the previous audit, the auditor should test the controls in the current audit.

(2) If there have not been any such changes, the auditor could test the controls on a reasonable timeframe, and should test some key controls on which the auditor intends to rely during each audit. In that sense a rotation control plan can be instituted by the CB, and correlated to the results of the risk assessment, to be used to identify the key controls for the audit. During the first year of application of this Guideline, the CB could still apply the rotation of test of controls designed under the previous Guideline, as long as this does not contradict the audit methodology under the new Guideline.

4.4. Audit approach – CB's responses to assessed risks and building up assurance

The audit approach consists of implementing procedures in order to respond to the identified risks of material misstatement or serious deficiency detected in the previous step, thereby focusing on the most risky areas and activities for audit purposes.

The audit approach relies to a great extent on the opinion the auditor is expected to express vis-à-vis the governance systems of the Member State. The CB is expected to obtain reasonable assurance concerning:

(a) the true and fair view of the accounts, including the reliability of the financial reporting (financial audit);

[2] See also the Guideline 1 on accreditation

(b) the proper functioning of the Member States' governance systems (systems audit);

(c) the correctness of the annual performance report (systems audit and audit of reporting)

(d) the compliance with the relevant laws and regulations for expenditure not covered by the CAP strategic plan (audit of legality and regularity of expenditure).

The conclusions on these separate audit questions are interdependent, in that the assessment of any one may affect the others.

For Audit Objectives 1, 3 and 4, the total level of assurance required from audit testing is set at 95%. This audit assurance is obtained based on 1) the assessment of the control environment (through assessing the inherent and control risk) and 2) the substantive testing of files (detailed tests based on the established audit risk model, the assessed detection risk). For Audit Objective 2, the CB will have to determine the nature and extent of the overall audit procedures (including compliance testing) instead of designing substantive testing of sampled files.

The **System assurance** represents the reliability of the PA's internal control system or the performance reporting system including compliance with the accreditation criteria. It is determined based on the review of the internal control system (see section 5 as regards Audit Objective 1). Based on this audit work the following four levels of reliance on the internal control system are to be used for the evaluation of the control procedures:

- Works well, only minor improvements are needed – High (Medium high) system assurance
- Works, but some improvements are needed – Average system assurance
- Works partially, substantial improvements are needed – Medium low system assurance
- Essentially not working – Low system assurance.

For Audit Objectives 1, 3 and 4, the assurance level from substantive testing or substantive analytical procedures, and respectively the confidence level, which actually determines the sample size, will depend on the assurance level obtained from the system audit. Generally, the correlation between the assessment of the ICS and the assurance required from substantive testing is the reverse of the correlation between the assessment of the ICS and the system assurance.

Correlation of the ICS assessment, system assurance and confidence level

Combined risk assessment	Assessment of governance systems	System assurance	Assurance from substantive testing
Minimum	Works well	High (Medium High)	Low/Medium Low
Low	Works	Average	Average
Moderate	Works partially	Medium Low	Medium High
High	Not working	Low	High

The table below provides examples of the system assurance levels (coming from the combined risk assessment: IR x CR) in relation to detection risk (DR) and respectively, to the assurance to be drawn from substantive testing.

These examples establish a framework for setting up the risk model and audit assurance model to be followed by the CBs in their audit procedures. The actual audit risk assessed by the CBs in the course of the certification audit can differ from these specific examples.

Examples for assessment of audit risk model and related assurance levels

Combined risk assessment	Assurance level from the system audits	Assurance from the system	Confidence level	Detection Risk
Minimal	Works well, only minor improvements are needed	High (Medium high)	Not less than 60%	Less or equal to 40%
Low	Works, but some improvements are needed	Average	70%	30%
Moderate	Works partially, substantial improvements are needed	Medium Low	80%	20%
High	Essentially not working	Low	Not below 90%	Not greater than 10%

It follows from the above that the higher the auditor assesses the level of the combined risk, the lower the detection risk is. This results in more substantive audit work (larger sample sizes). Equally, a lower combined inherent and control risk assessment allows for a higher detection risk, resulting in less substantive work and more reliance on the internal control system.

Setting an appropriate confidence level is a critical issue for the auditing of transactions (from authorisation to accounting/declarations), as the sample size is strongly dependent on the confidence level (the higher the confidence level, the larger the sample size). As outlined in the above framework and explained further on in this guideline, it is possible

to reduce the confidence level to be obtained from substantive testing and consequently the audit workload for systems with a low error rate or not prone to serious deficiencies (therefore high assurance), while maintaining the requirement of a high confidence level (consequently larger sample size) in the case of a systems that have a potentially high error rate or prone to serious deficiencies (therefore low assurance). In exceptional cases where the CB concluded that no reliance can be placed on the internal control system, the assurance/confidence level to be obtained from substantive testing is 95%.

The related actual sample sizes are to be determined through the audit procedures taking account of the relevant sections; i.e. for Audit Objective 1 sections 5-6-7.

To reduce audit risk to an acceptably low level, the CB should determine overall responses to address the assessed risks of material misstatement or serious deficiency at population level and design and perform further audit procedures whose nature, timing, and extent are responsive to the assessed risks of material misstatement or serious deficiencies at the relevant assertion level.

What is described above regarding the assurance level derived from testing also applies, mutatis mutandis, to **Audit Objective 2** for the determination and the extent of the audit procedures to be performed.

As already described, the CB is not requested to carry out substantive testing to assess the Member States' governance systems. However, within Audit Objective 2 the CB will use the results of the risk assessment to determine the range of the audit procedures, including **compliance testing**.

When the CB will need to select any items of the control procedures to carry out compliance testing, the size of the sample is not to be determined statistically as described for the substantive testing. Using the professional judgment, the CB will however consider the results of the analysis as previously mentioned.

In this regard, further guidance is provided in PART B of this guideline.

4.5. Types of audit procedures

Audit procedures are the processes, techniques, and methods that auditors perform to obtain audit evidence, enabling them to conclude on the set audit objective and express their opinion.

Typically, five types of audit procedures are normally used by auditors to obtain audit evidence such as follows:

i. Analytical review: Auditors use the analytical procedures in any stage of the audit such as planning, execution stages, and conclusion stage. This procedure helps the auditor to pay more attention to the areas that are unusual changes. In other words, in the areas that have a significant change.

ii. Inquiry: Sometimes auditors inquire about the business process of the organisation. The inquiry is also one of the most important audit procedures and it could be used in different stages. Audit inquiry is sometimes used by the auditor to obtain the audit evidence and sometimes is used to understand some nature of business to gain enough knowledge to design and perform testing. However, information from the inquiry is sometimes hard to be used as audit evidence. The audit evidence found as the result of your testing after an inquiry is strong to be used as audit evidence rather than information from the inquiry itself.

iii. Observation: Observation is one of the audit procedures that auditors use to understand and gather audit evidence mainly to the real process and how was actually carried out. This kind of audit procedure mainly confirms the process as described on the PA's manuals and / or described during interviews.

iv. Inspection: Inspection refers to the verification / validation of results. It is one of the most important audit procedures since it provides strong audit evidence. Inspection may include review of documentation, re-performance of controls.

v. Recalculation: Recalculation is the type of audit procedure normally done by re-performing the works performed by the client to assess if there is any difference between the audit's work and the client's work. Recalculation is the procedure that use to confirm the accuracy of a transaction that involves calculation.

Most of the audit work shall include a mix of different audit procedures in order to meet the audit objective. For example, the compliance testing, depending on the audit objective, may include inspection and recalculation of audit procedures. The CB during the planning of its work should design an appropriate mix of audit procedures to be carried out. Such decision should be based on several factors, including whether the PA's or other entity's control procedures envisage a quality assessment (QA) process. For example, the review and validation of the results of the QA required for the ISAP, GSA and AMS union requirements is strongly recommended. However, in order to meet the relevant audit objective (i.e. validation of QA results), the CB is required to design an appropriate mix of audit procedures (e.g. analytical review, inspection, recalculation).

PART A

5. AUDIT PROCEDURES

The audit as regards audit objective 1 will cover one financial year (16/10/202x-15/10/202x+1) and can be carried out over a 12-month period (calendar months) from January of the audited financial year to January of the year following the audited financial year. The timing is proposed in light of this 12-month period hereafter. However, this audit can be carried out in a shorter time period as well depends on the number of sampling phases.

The certification audit as regards audit objective 1 should be carried out through the following main audit procedures:

5.1.1. Definition of audit risk model and assurance levels

Proposed timing

Depending on the number of phases of testing, it can already be carried out in January-March (hereinafter referred to as M1-M3) of the audited financial year, but it should be planned for June-August of the audited financial year at the latest.

Main tasks

- To assess the inherent risk and the control risk (the risk of material misstatement) based on previous years audit results and through the assessment of the internal control system (see section 5).
- To determine the system assurance and the confidence level for the substantive testing, and the requirements for the review of the internal control system and for the substantive testing.
- To plan all the audit procedures (timing and resources) including the assessment of the internal control system, the substantive testing, the review of reconciliations, the interpretation of errors and results and preparation of the certification report and formulation of opinion.

To consider

- At the time of planning estimated expenditure can be used. Adjustment might be necessary to the sample size based on the actual expenditure.
- At the time of planning the results of testing of control procedures are not available. The sample size of substantive testing may need to be increased (if high errors found through the testing of control procedures).

5.1.2. Assessment of the internal control system

Proposed timing

Part of the tasks: assessing the control environment needs to be planned in parallel with the definition of audit risk model and assurance levels. (M1-M3)

Other tasks: test of processes/procedures including test of controls, compliance and tests of the IT system (on the processes and procedures relevant for audit objective 1) will be the first audit procedures to be implemented after the audit plan is established. (M4-M6)

Main tasks

- To assess the effectiveness of the control environment taking account of the previous years' evaluation of the internal control system, any legal, organisational, procedural and system changes in order to determine the system assurance for the audit risk model. This will require conducting walk-through testing.

- To carry out the tests of control procedures for the assessment of the internal control system for the audited financial year result. This can include different types of testing, a particular attention should be focused on the testing of IT systems and controls.

- To evaluate risks identified or deviations found and corroborate results in a final assessment (works well, works, etc.) for the control procedures, and to see if the substantive testing parameters need to be adjusted due to high errors found in the test of control procedures.

To consider

- The final assessment granted to the control procedures will have to be considered in the opinion on the efficiency of the internal control system.

- In respect of compliance testing dual purpose testing can be applied.

- Tests on the IT systems have a significant role in the assessment of these control procedures.

5.1.3. Substantive testing

Proposed timing

As regards audit objective 1 the substantive testing needs to be carried out based on the actual payments made. The substantive testing can be carried out through several phases not to concentrate the workload after the end of the financial year.

- In case of two-phased sampling: M5-M6 and M11-M12, in case of one sampling phase: M11-M12.

Main tasks

- To draw the sample based on the parameters already established at the planning phase and to carry out the actual testing.

- To collect audit evidence (as for all other steps), especially for the documentation of exceptions (deviation, errors) found.

To consider

- Tests on the IT systems play a significant role in the testing of payment transactions and accounting records. In particular, if the PA has an integrated system for processing all payments, the CB should focus on IT testing and use a single sample for the two funds as explained below.

5.1.4. Reconciliations

Proposed timing

For audit objective 1, the reconciliation and review of the reconciliation of the annual accounts need to be carried out after the end of the financial year (M12-M13).

Main tasks

- To review the reconciliation procedure of the PA and to check the accuracy of each part of the annual accounts.

To consider

- A procedure should be established to check the correctness of each FX code used by the PA to explain differences between annual accounts and monthly/quarterly declarations.

- Special attention needs to be paid to transactions resulting in additional amounts charged to the EU budget through the annual accounts (as compared to the monthly/quarterly declarations).

- The proper timing of the work and in that respect collaboration with the PA is essential to ensure that both the PA and the CB can fulfil their tasks.

5.1.5. Interpretation of errors, results

Proposed timing

The individual errors, deviations found throughout the test of control procedures the substantive testing can be interpreted in parallel to these audit procedures (M4-M6 and/or M11-M12).

The error evaluation for the substantive testing should be finalised by M12 to allow for the PA's reaction.

Main tasks

- To establish and to document clearly the calculation of the errors and to perform the error evaluation.

To consider

- If dual-purpose testing is used, all financial errors found will need to be taken into account for the error evaluation of the substantive testing.
- Individual financial errors need to be followed up (by the PA) and the CB needs to report on these.

5.1.6. Formulation of the opinion

Proposed timing

The audit opinion needs to be prepared when all relevant audit procedures are finalised (M13).

Main tasks

- To aggregate the results from the assessment of the internal control system of the PA, the substantive testing and the reconciliation
- To consider previous years' results and to formulate the opinion as regards the internal control system of the PA and the annual accounts (in case of ongoing action plans and weaknesses which are still not fully remedied; as well as in case rotation of control testing is applied (see section 5 on rotation of controls)).

To consider

- The opinion on the Member States' governance systems needs to be formulated taking account of the assessment of the control procedures provided for all four audit objectives.
- For the opinion on the annual accounts only errors related to the payment and accounting have to be considered. Nonetheless, if the CB identifies legality and regularity errors in this sample, they should be reported as known errors under audit objective 4 (PART D).

6. ASSESSMENT OF THE INTERNAL CONTROL SYSTEM

The assessment of the internal control system of the PA for audit objective 1 is part of the overall assessment of the Member States' governance systems. The techniques used for testing controls consist of assessing the control environment, the importance of controls, the risk that tests may not be conclusive and the outcome of other enquiries. Testing will cover the effectiveness of both the design and implementation of the controls. It consists of tests of procedures and tests of controls (compliance testing).

In order for the CB to identify and assess the risk of material misstatement, an understanding of the entity and its environment should be performed. This will include,

among other things, understanding the internal control system of the entity and its components (cf. ISA 315). In the case of the PA, this translates into the accreditation criteria laid down in Annex I Commission Delegated Regulation (EU) 2022/127) (i.e. the components of the internal control system):

- Internal environment (including the organisational structure; human resource standard; risk assessment and delegation);
- Control activities;
- Information and communication (including information systems security);
- Monitoring;

On the basis of the understanding of the accreditation criteria as put in place by the PA, the CB should also assess the design and the implementation of the controls embedded in the processes at PA level (i.e. at entity level). An improper design of entity controls which is not in line with the accreditation criteria may present a significant deficiency in the internal control system.

After assessing the overall internal control system at entity level on the basis of compliance with the accreditation criteria, the CB's work should include a review of the concrete processes in place (through review of the procedures).

The assessment of the internal control system covers the following: it should be the basis for establishing the system assurance at the audit planning stage, and it should be the basis for the assessment of the internal control system for the audited financial year to be expressed in the audit opinion. As regards audit objective 1, the following main control procedures[3] are to be subject to this assessment:

For operational transactions:

- Execution of payment;
- Accounting for payment;
- Reporting of the payments in the monthly, quarterly and annual declarations;
- Reconciliation process.

For non-operational transactions:

- Recording, managing analytics and reporting of irregularities and debts.

These procedures also cover the management of advances and securities (the latter as non-operational transactions). The CB may also decide to test the securities in terms of the PA's examination of securities procedure- to examine why some securities were rejected and some accepted. No separate evaluation is needed for these sub-procedures but they should be assessed within the review of the main procedures.

[3] These control procedures/processes are considered the main ones, however, the CB should revise the above list and add more relevant processes as this list is not considered exhaustive.

The assessment needs to be drawn at the level of the population considered for this exercise (see section 6) for the respective Fund (either EAGF or EAFRD).

6.1. Assessment of the control environment for establishing the system assurance

The CB's work should begin with a review of the general control environment for the above -mentioned control procedures considering the following:

- Previous years' audit results for these control procedures (e.g. grading in the accreditation matrices);
- Changes in the legal, organisational, procedural, IT system/s and human resources set-up.

In addition, the CB should perform the following:

- To get an understanding of the PA's control procedures and systems;
- To review the "translation" process, through which the requirements set out in the EU Regulations are incorporated in the PA's manual, computer procedures and written instructions;
- To conduct "walk-through" tests on the processes/procedures, including IT processes to determine the functionalities of the control system;
- Identify "what can go wrong" (WCGWs) or risks in the process/procedure and related controls;

On the basis of the above, if the CB decides to rely on the ICS, it should carry out compliance testing (test of controls) on selected controls (see section 5.3. below).

Outcome: definition of system assurance based on the following categories:

Combined risk assessment (IR x CR)	Assessment of control procedures	System assurance
Minimal	1. Works well	High/Medium High
Low	2. Works	Average
Moderate	3. Works partially	Medium Low
High	4. Not working [4]	Low

This will allow the auditors to determine the assurance level to be gained from the substantive testing.

6.2. Review of control procedures

Based on the reliability of the control processes/procedures as assessed in the previous step, the CB needs to plan the test of controls. Even if the CB decides that the internal control system is not reliable and thus no assurance is planned to be gained from this

[4] Explanation is provided in the table in section 5.2.3

assessment, it needs to carry out part of the following review work in order to identify the concrete deficiencies and remedial actions

- To get an understanding of the PA's control procedures and systems;
- To review the "translation" process, through which the requirements set out in the EU Regulations are incorporated in the PA's manual, computer procedures and written instructions;
- To conduct "walk-through" tests on the processes/procedures, including IT processes to determine functionalities of the control system;
- Identify "what can go wrong" (WCGWs) or risks in the process/procedure and related controls;

These procedures should allow the auditors to establish whether:

- written guidance on each of the following: payment execution, accounting for payments and registration of debts and computation is comprehensive and up-to-date and available to all staff;
- the IT system/s and related procedures are well designed and operated to comply with the procedural requirements (included in EU, national legislation);
- payment and accounting, as well as debt management duties are appropriately segregated, defined and subject to supervisory control,
- there is appropriate staff training and rotation;
- there are adequate procedures for senior management checks and monitoring, and
- appropriate action is taken in response to recommendations on improvement accepted by the PAs as a necessary part of the accreditation process.

The CB should obtain sufficient and appropriate audit evidence that the controls selected for testing operate effectively as designed throughout the period of reliance to prevent or detect and correct material misstatements at the assertion level. Overall, the CB should be able to conclude whether the ICS is designed in accordance with the accreditation criteria, whether it is operating as designed and whether it is effective in order to safeguard the Union financing. This should be done as part of the audit procedures in case the CB relies on the ICS and in case it does not.

Among the above-mentioned techniques, audit tests on the IT systems have a key role considering that nowadays most of the procedures of the PA for audit objective 1 are IT-driven. IT allows to process data and transactions consistently and enhances the ability to monitor the performance of control activities and to achieve effective segregation of duties by implementing access controls in applications, databases, and operating systems. Therefore, in order to rely on the automated controls embedded in the IT systems, the CB can perform audit procedures to determine whether an automated control has been implemented which may serve as a test of that control's operating effectiveness. To that end, the assessment and testing of IT-general controls (ITGCs), including IT security and change management procedures should be also taken into account. The planning of the tests on the IT system should be adequately reflected in the CBs' audit procedures.

6.2.1. Review of IT general controls (ITGC)

In case the PA is ISO 27001:2013 certified, the CBs can factor that into their ICS testing. If the PA is ISO 27001 / BSI ISO 27001 certified and the CB reviews its scope and is satisfied that the certificate covers all key tasks of the PA, there may be no need for further assurance work to be carried out by the CB regarding information systems security. The CB should have access to the necessary information for this review.The CB may decide to do some audit work on the certification process or its quality or in case the certificate is not covering all key ITGC requirements / delegated bodies. The scope of this audit work is to be defined on a case-by-case basis.

In case the PA is not ISO certified the CB should satisfy itself that the information security controls in the selected information security standard are complied with, chapter by chapter. This audit work can be carried out by the CB itself or by using an external company.

ITGCs apply to all IT systems components, processes and data present in an organisation or systems environment. The ISA 315 ([5]) (revised 2019) include elements relevant for the assessment of the CB in relation to the PA's use of IT and the impact on the audit. Appendices 5 and 6 of that standard provide in particular considerations for understanding information technology and elements that the CB may consider in understanding ITGCs.

6.2.2. Review of IT application controls

Every PA has numerous IT systems and IT applications with embedded controls in them. Some controls are automated (no manual interference) and the CB may consider testing the automated application controls since, if they operate as intended, they provide high reliance, as well as provide for an efficient use of audit resources. In order to rely on the automated controls at the application level, the CB may perform audit procedures to determine whether an automated control has been implemented. However, due to time constraints, the CB cannot review all applications every year and therefore the selection of application(s) to be tested should be based on a risk assessment.

Once the CB selects an IT application, it should determine which automated application controls to test. The rule of thumb is to test the application controls that cover most audit assertions and most WCGWs. Once an automated application control has been selected for testing and determined that it is functioning as intended, the CB may consider performing a **test of one**[6] on that control and some other tests to determine that the control continues to function effectively. Such tests might include a verification that;

- All input data is accurate, complete, authorized and correct;
- All data is processed as intended;
- All data stored is accurate and complete;
- All output is accurate and complete;

[5] https://www.iaasb.org/publications/isa-315-revised-2019-identifying-and-assessing-risks-material-misstatement

[6] The functioning of the control is tested only one time as it is an automated one

- A record is maintained to track the process of data from input to storage, and to the eventual output;
- Access to data is limited based on business needs;
- Incompatible duties within an application are systematically prevented.

Application controls relate to the transactions and data pertaining to each computer- based application system. They are specific to each individual IT application. It is important to note that the degree that application controls can be relied on depends directly on the design and operating effectiveness of ITGS. In other words, if ITGS are not implemented or operating effectively, the Paying Agency may not be able to rely on its application controls to manage risks.

6.2.3 Assessment of control procedures

Outcome: An assessment of system deviations found based on the following categories:

Assessment of control procedures	Assessment of deviations
1. Works well, only minor improvements are needed	All risks are adequately addressed by controls, which are likely to operate effectively. No exception was found. OR only minor (formal) deviations were found which did not affect substantially the effectiveness of controls and did not lead to financial errors.
2. Works, but some improvements are needed	All risks are adequately addressed by controls which are likely to operate effectively with some deficiencies having a limited impact on the functioning of the key requirements. Only minor deviations were found, which did not affect substantially the effectiveness of controls. OR if those minor deviations affected substantially the effectiveness of controls, the PA's ongoing controls detected them and the self-correcting mechanism of the PA operated.
3. Works partially, substantial improvements are needed	All risks are addressed to some extent by controls which may not always operate as intended. Moderate deviations were found, which affected substantially the effectiveness of controls. AND only part of these moderate deviations was detected by the PA's ongoing controls and corrected by the PA itself.
4. Not working	Not all risks are addressed by controls and/or there are likely to be frequent control failures. ICS functions poorly or does not function at all. The deficiencies are systemic and wide-ranging. High deviations were found that were not detected by the PA's internal control system.

Minor deviations signal formal exceptions in the applied procedures compared to the designed procedures or in the designed procedures compared to the legal requirements, which will not lead to financial consequences: errors in the payments.

Moderate/high deviations are meant to be the exceptions in the applied or designed procedures that can lead to financial consequences: errors in the payments. Moderate deviations can lead to minor financial errors with a total estimated financial impact below the materiality. High deviations would trigger financial errors with a material total estimated financial impact.

6.3. Compliance testing (test of controls)

To express an opinion on the effectiveness of the ICS, the CB should examine the specific, pervasive and monitoring controls embedded within the reviewed process(es): systems, procedures, manuals. These tests of controls are performed to support the CBs assessed level of control risk. The test of controls should test the effectiveness of a control used by the PA to prevent or detect material misstatements. When performing compliance testing, the CB should examine for the selected specific transactions, whether:

(1) the necessary controls are in place and designed in accordance with the legal framework;

(2) the necessary controls operate as designed and prevent/detect and correct material misstatements at assertion level.

The following aspects need to be confirmed through the compliance testing:

True and fair [7] accounts

- **Occurrence**: recorded transactions actually took place.
- **Completeness**: all transactions that should have been recorded have been recorded.
- **Accuracy**: the transactions (operational and non-operational) are disclosed in the PA's accounts at the correct/appropriate amounts.
- **Cut-off**: transactions have been recorded in the correct accounting period, i.e. in the period in which the transaction actually took place.

True and fair debtor's ledger and effective and timely recovery of debts

- **Completeness and accuracy:** debtors' ledger include all transactions to be recovered and for the correct amounts
- **Effective procedures:** procedures exist ensuring the timely registration and recovery of debts and are applied correctly
- **Prompt recovery:** amounts recovered are correctly and timely credited to the Funds.

[7] Audit assertions

For that matter, WCGWs that affect the above assertions should be identified and the related controls that mitigate the WCGWs should be identified as well.

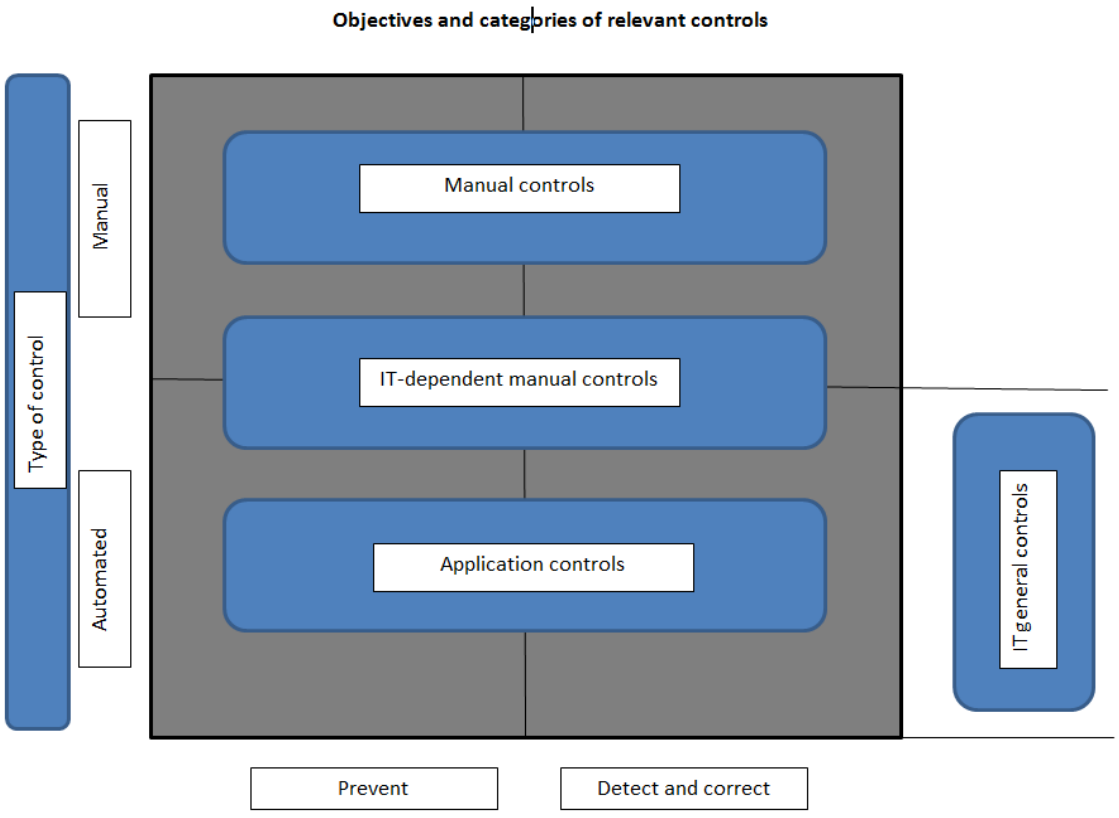
The following WCGWs that could have a material effect on the relevant assertions could be considered:

- There is a likelihood of misstatement;
- The potential misstatement is of a magnitude that could result in a material misstatement.

In order to identify controls that are relevant for the audit (especially if the CB plans to rely on controls), the following should be considered:

- Controls that mitigate significant risks;
- Highly automated processes and application controls;

The CB should consider the different types of controls in their testing.



For some procedures (execution of payments, accounting for payment), these tests can be carried out through an IT application control for all the transactions. Or, provided that the IT general controls (ITGCs) are effective, the operation of an automated application control can be confirmed through a test limited to one transaction.

The test of control will depend on the type of control and the frequency of the control.

Nature of control and frequency of performance	**Minimum number of items to test in case no exception or very few exceptions are expected**
Manual control performed daily or many times per day	25[8]
Manual control performed weekly	5
Manual control performed monthly	2
Manual control performed quarterly	2
Manual control performed annually	1
Automated Application control	Test of 1 for each application control if supported by effective ITGCs, otherwise if ITGCs are ineffective- test 25 transactions

A rule of thumb that could be followed is to test a sample size of approximately 10 percent of the population. The above table provides suggested minimum sample sizes in testing of controls and compliance requirements when no exceptions or very few exceptions are expected. Although the minimum sample sizes suggested in the table often provide the appropriate extent of testing, CBs may use professional judgment to determine if larger sample sizes are warranted in order to obtain sufficient appropriate audit evidence in particular circumstances like high control risk for a particular scheme/measure.

If for example, the CB decides to test the weekly manual reconciliation between the executed payments and the accounting entries in the accounting process, it should test 5 items. The suggested sample for manual daily controls or controls performed many times per day when no or very few exceptions are expected, is 25 items. If in the course of the compliance testing a high rate of errors is found the CB may decide on increasing the sample size or alter its originally planned audit procedures.

Although the purpose of the compliance testing is different from that of the substantive testing, the two may be performed concurrently. This is defined as a "**dual-purpose test"** by ISA 330. Where used, the CB should base a dual-purpose test on the preliminary assessment that there is an acceptably low risk that the rate of deviations from the prescribed control in the population exceeds the maximum rate of deviations that the auditor is willing to accept without altering the planned assessed level of control risk[9].

For example, the CB may design and evaluate the results of a test to examine a claim to determine whether it has been approved and to provide substantive audit evidence of a transaction. A dual-purpose test is designed and evaluated by considering each purpose of the test separately. While recognising that this might be an efficient use of audit resources, care must be taken to properly analyse and document the results, so as to clearly distinguish between the different objectives for the two types of tests. All financial errors found in

[8] Normally 10% of the occurrences (a range between 50 and 250 occurrences)

[9] The results from the substantive testing are to be considered for the effectiveness of the controls. Moreover, the CB is to re-assess the control risk after the audit procedures.

dual-purpose testing should be taken into account as random errors in the extrapolation of the errors for substantive testing except if a known error is quantified via additional work of the CB.

Outcome: An assessment of the errors found based on the following categories:

Assessment of control procedures	Assessment of errors
1. Works well, only minor improvements are needed	No exceptions/errors were found. OR only minor (formal or one-off) exceptions/errors were found which did not affect substantially the effectiveness of controls and did not lead to financial errors.
2. Works, but some improvements are needed	Only minor exceptions/errors were found, which did not affect substantially the effectiveness of controls. OR if those minor exceptions/errors affected substantially the effectiveness of controls the PA's ongoing controls detected them and the self-correcting mechanism of the PA operated.
3. Works partially, substantial improvements are needed	Moderate exceptions/errors were found, which affected substantially the effectiveness of controls. AND only part of these moderate errors was detected by the PA's ongoing controls and corrected by the PA itself.
4. Not working	High rate of exceptions/errors were found that were not detected by the PA's internal control system.

The definition of minor, moderate and high errors correlate to the definition of minor, moderate and high rate of deviations.

6.4. Results of the assessment of the internal control system

Following the three steps mentioned above, the CB will need to conclude on the assessment of the internal control procedures for audit objective 1. The table below represents one possible example for this exercise:

Control procedure[10]	Original assessment (3.1)	Outcome of review of procedures (3.2)	Outcome of compliance testing (3.3)	Final assessment
Execution of payment	Works well	No exceptions/deviations were found	No error was found	Works well
Accounting for payment	Works well	Minor exceptions/deviations were found, the PA's	No error was found	Works

[10] The CB should revise the list of the control procedures to add the most significant ones in the scope of its audit.

		control procedure detected them		
Managing irregularities and debts	Works partially	Moderate exceptions/deviations were found, the PA's control procedure detected them	Moderate errors were found, only some of them were detected by the PA's controls	Works partially

The final assessment should always be aligned with the worst assessment for the outcome of the review of the control procedures (section 5.2) and the outcome of compliance testing (section 5.3).

At this stage, the CB is to see if the substantive testing parameters need to be adjusted due to high deviations and errors found in the test of internal control procedures.

7. SUBSTANTIVE TESTING

7.1. Objective of the substantive testing

The audit procedures for the validation that the accounts are true and fair should include **substantive audit procedures:** a test of detail and analytical procedures. The analytical procedures are explained in section 7-Reconciliation.

The tests of detail as regards the annual accounts should focus on items (operational and non-operational transactions) that are included in the financial statements (annual accounts): declaration of expenditure, Annex II and III (also debtor's ledger) etc.

The substantive testing of **the operational transactions** should cover the procedure for execution of payments and accounting for payments up to the declarations. It should include verifying that (non-exhaustive list):

- Ex-ante payment checks have been conducted[11],
- Data have been correctly recorded and processed for payments,
- The amount payable calculated, correctly takes into account any reductions related to irregularity/debt management;
- The correct amount has been executed for payment, recorded in the accounts, and declared to the Funds[12].

The above-mentioned tests should be applied to advance payments as well. Where appropriate, these tests could consist of evaluating and testing controls embedded in the information systems associated with the process.

[11] The CB can only check that the receipt and handling of the claims was done in line with the procedures, without re-performing the actual checks

[12] Cf. Articles 65, 68, and 90 of the Regulation (EU) No 966/2012 of 25 October 2012 (Official Journal of the EU, L298/1 of 26.10.2012)

Substantive audit procedures for **the non-operational transactions**:

With respect to **securities** the CB should confirm that (non-exhaustive list):

- These are true and fair as to account, amount and period, mainly by testing against supporting documentation;
- The securities exist, and are held in a secure place;
- Only approved standard bank securities are accepted and that these are still valid.

As regards the management of **irregularities and debts**, the CB should verify amongst others:

- Completeness: debts related to undue paid amounts resulting from the occurrence of an irregularity, all penalties that should have been recorded has been in fact recorded;
- Accuracy: the debts are disclosed in the PA's accounts at the appropriate amounts, having had regard to all repayments, interest, offsets and write-offs. Regarding this last event, the CB could verify the validity of the reasons to correct and write-off a debt (including the decision not to pursue the recovery of a debt).
- Timeliness: debts are timely identified, recorded and recovered.

7.2. General concepts

Population/stratification

The population for sampling purposes should include all payments made within the financial year (e.g. 16 October 202x – 15 October 202x+1) that were declared to the Commission. For audit objective 1, the CB needs to express an Opinion per Fund.

According to the preamble of Regulation (EU) 2022/128, the PA should keep separate accounts relating exclusively to expenditure to be financed by the EAGF and by the EAFRD respectively and revenues to be linked to the two Funds. It follows, therefore, that the two Funds should be treated separately.

It follows from this that the CB has to express the opinions stated in Article 9 of the Regulation (EU) No 1306/2013 for the two funds separately.

Thus, for the **operational transactions** the sampling population can be established at the level of Fund:

- All payments made within the financial year declared under EAGF,
- All payments made within the financial year declared under EAFRD.

However, if it can be demonstrated that the operational transactions' movements for both EAGF and EAFRD Funds are managed using a common internal control system, following the same principles, and in particular when the procedures are automated, both the compliance and substantive verifications may be carried out based on one single

population covering both EAGF and EAFRD. In this case, some particular conditions should be met (see Annex 2 of Guideline 2 as applicable for FY2022).

For the purposes of the **substantive testing on the annual accounts**, the CB should establish a statistical sample using the methods described in Annex 2 of Guideline 2 as applicable for FY2022.

In general, stratification is not considered necessary for testing the payments. However, if the auditor expects a different level of misstatements (e.g. higher) in part of the population (it means different level of variability), (e.g. payments made for one specific measure and due to different procedure used for processing these payments), stratification can be used. In this case the population is divided into subpopulations/strata, and each stratum is tested separately. For each stratum a different sampling technique may be used, e.g. the riskier stratum can be tested 100 %, for the other stratum the selected statistical sampling method can be used. Alternatively, the CB may choose to test 100% of the key items (for example transactions whose value is larger than the materiality threshold for the population or whose value is larger than the expected sampling interval). The CB can then establish the sample based on the remaining population.

For **non-operational transactions** the following populations can be defined:

- Management of irregularities and debts
- Population 1: Transactions under EAGF
- Population 2: Transactions under EAFRD

However, if it can be demonstrated that the irregularities and debts' movements for both EAGF and EAFRD Funds are managed using a common internal control system, following the same principles, both the compliance and substantive verifications may be carried out based on one single population covering both EAGF and EAFRD. In this case, some particular conditions should be met (see Annex 2 of Guideline 2 as applicable for FY2022).

The advances and securities process should also be tested.

Sampling unit

For the **operational transactions** the sampling unit is the individual payment made by the PA in the course of the financial year. For the **non-operational transactions,** the sampling unit may vary depending on the CB's decision. However, for both irregularity/debt management and securities it is recommended to use an individual case in the population as the sampling unit.

Sampling method

A statistical sampling method should be used for the **operational transactions**. It is recommended to use MUS. Integrated sampling could be used where possible for efficient use of audit resources and for efficiency gains but without compromising the separate reporting under two funds. Thus, one transaction could be used for compliance testing and substantive testing (dual-purpose testing), as explained in section 5 above.

Detailed explanation of the different statistical methods is included in Annex 2 of Guideline 2 as applicable for FY2022. Some general concepts explained hereafter relate only to statistical sampling.

For non-operational transactions non-statistical, random sampling is recommended to be used (see Annex 2 of Guideline 2 as applicable for FY2022).

Materiality – Tolerable error/misstatement (TM)

The overall materiality is set at 2% of the expenditure at Fund, population, and stratum level.

If duly justified, the CB may fix different performance materiality thresholds at stratum level, under the condition that at Fund level the overall materiality of 2% is respected. The justification for the approach followed has to be duly substantiated and documented in the audit strategy.

The tolerable error is the maximum acceptable error rate that can be found in the population for a certain year. With a 2% materiality level this maximum tolerable error is therefore 2% of the expenditure certified to the Commission for that reference year.

Confidence level

As explained in section 4.2, the system assurance will determine the assurance to be gained from substantive testing or in other words the confidence level for the substantive testing. It gives an interpretation for the sampling results, it expresses the probability that a confidence interval produced by sample data contains the true population error. e.g. a confidence level 95 % means that the CB can assume with 95 % reliability that the population error will fall within the confidence interval produced by the sample data. (If the projected error is 100, and the precision is 10, the true population error will fall within the interval [90, 110] with 95 % reliability).

Anticipated error

It represents the expected misstatement in the tested population or stratum. It is estimated either based on the standard deviation of error(s) or on previous audit results.

Precision

The precision measures the uncertainty that arises as the CB does not audit the entire population and it measures the uncertainty due to sampling, i.e. the sampling risk. The sampling risk means the risk that the conclusions the CB reaches after testing a sample are different to those that would have been reached had the whole population been tested.

The **planned/desired precision** is the maximum sampling error accepted for the projection of errors in a certain year. The planned precision should be always lower than the tolerable misstatement/error.
The difference between the anticipated error and the tolerable error can be used as a measure of precision.

Achieved sampling precision allows the CB to determine the **confidence interval -** the range within which the estimate of the population characteristic will fall at the stipulated confidence level.

Variability

The variability of the population is a very influential parameter on sample size. Variability is usually measured by a parameter known as standard deviation and represented by σ. The larger the standard deviation is, the more heterogeneous the population (or the sample) is.

The sample size needed to audit a population with a low variability is generally smaller than for a population of a high variability.

Sample size

The sample size for the audit of the annual accounts at Fund level for **operational transactions** should be determined by the above mentioned parameters: population, confidence level, precision, tolerable error and anticipated error.

In general, using different sampling methods, including estimation of the standard deviation (on a pilot sample) can result in very different level of sample sizes.

For MUS conservative, the following minimum sample sizes **per Fund** should be respected for the audit of the accounts:

System Assurance	High/Moderate	Average	Medium Low	Low
Audit Risk	5%	5%	5%	5%
Confidence level for substantive testing	**Not less than 60%**	**70% (Average)**	**80% (Medium high)**	**Not below 90%**
Minimum sample sizes	**46**	**60-78**	**80-110**	**115**

In respect of audit objective 1, it is perceived that the PA's personnel is experienced and the PA has functioning systems and procedures in place, thus low inherent risk is used in the above examples. However, this needs to be assessed by the CB carefully at the planning stage of the audit.

Once the sample size has been determined, the sampling interval can be calculated by dividing the population size by the sample size.

Considering that the substantive testing may have to be carried out in several phases the definition of the sample size for substantive testing is recommended to be carried out in the following way:

- In case no stratification is applied, determine the overall sample size to be tested based on the current year's assessment[13] of the internal control system and taking into account the estimated annual expenditure (based on forecasts), following section 4.2.
- In case of stratification:
  - Determine the strata,
  - Determine the sample size per stratum in accordance with the section 4.2 based on selected sampling method;
- In both cases final adjustment may be necessary based on the final expenditure: The final sample size has to be adjusted for the actual annual expenditure declared to the Funds. In case the actual expenditure appears

[13] The review of the ISC should be at least in progress before the start of the substantive testing. If the results of the current year's assessment are not available, the previous year's assessment can be used.

to be significantly higher than expected, the CB may find it necessary to increase the originally determined sample size.

The sample size for **non-operational transactions** may vary between 4-50 depending on the assessed system assurance (see Annex 2 of Guideline 2 as applicable for FY2022/section 4.2).

Evaluating the sampling results

Total projected error - Upper error limit/Total error – Additional work

In compliance with ISA530, the CB should evaluate:

(a) The results of the sample: For the evaluation of the substantive testing results for the **operational transactions** realised through statistical sampling method, the CB will need to establish the total projected error and the upper error limit, and

(b) Whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

The total projected error (TPE) is determined by extrapolating, extending the identified random errors in the sample to the total population/strata. It corresponds to the Most Likely error (MLE) in MUS terminology. In case of audit objective 1 this is referred to as the error rate (ERR).

The upper error limit (UEL) is the sum of projected error and the precision (sampling risk).

The CB needs to assess the correlation of TPE and UEL to the materiality (TM). The following scenarios may occur:

- TPE or MLE exceeds materiality. It can be concluded that there is a material misstatement in the accounts. After confirmation of the calculation the PA may decide on self-correction in the accounts before the submission.

- Both the TPE/MLE and the UEL are below materiality. It can be stated that at the specified sampling risk there is no material error in the accounts.

- TPE or MLE is below materiality and UEL exceeds materiality. The CB's original audit assumption is not confirmed by the sampling results.

If the CB concludes that audit sampling has not provided a reasonable basis for conclusions about the population that has been tested:

(a) it may request management to investigate misstatements that have been identified and the potential for further misstatements and to make any necessary adjustments or
(b) Tailor the nature, timing and extent of further audit procedures to best achieve the required assurance.

There could be four options for the course of actions to follow:

– To check if with a different confidence level the sampling results would prove the original audit assumption, and thus the CB could get still conclusive results based on the performed work.

– To verify if some of the random errors cannot be considered as system errors, and thus based on some additional work a known error could be established.

– To see if with additional testing (either increasing the confidence level or the anticipated error) with reducing the sampling risk conclusive result can be achieved.

– To apply alternative audit procedures to gain additional assurance.

As regards additional sampling and recalculation of confidence level see Annex 2 of Guideline 2 as applicable for FY2022.

Total error is the sum of UEL and known errors. In drawing the final conclusion for the audit opinion, the level of the total error is decisive. However, if the known error is well established and the PA takes actions already before the reporting deadline (e.g. launches the recovery procedure, recovers it, deducts from the accounts, remedies its procedure and system etc.) these corrective actions can be taken into account in the CB's opinion.

For the **non-operational transactions** as non-statistical sampling method is used only projected error can be calculated. The projected error in this case is determined by adding up the differences identified between the recorded and the audited values and by dividing the total error by the total value of the items checked. This projected error needs to be compared to the materiality for the CB's conclusion as regards the extent of error in the population.

8. RECONCILIATIONS – ANALYTICAL PROCEDURES

8.1. General analytical procedures

The CB in order to conclude on the completeness, accuracy and veracity of the annual accounts (audit objective 1), will have to reconcile:

- the annual accounts (both EAGF/EAFRD) with the interim declarations (monthly and quarterly tables of expenditure);
- the annual accounts with the X table data;
- the annual declarations of undue payments and other amounts to be reimbursed to the Funds (both EAGF/EAFRD) with the debtors ledger and annual accounts;
- any other reconciliation deemed necessary and defined in Guideline no. 3 on Reporting requirements.

As for the tests of control procedures and the substantive testing, for the reconciliation as well the appropriate tests on the IT systems play a crucial role and should be considered by the CB.

Some specific issues may need to be addressed during the analytical procedures:

8.2. Late payments

Where required by the Regulations, the CB should verify the timely treatment of payment claims by the PA, in particular whether the interval between receipt of the supporting documents needed to make the payment and the issuing of the payment order does not exceed legal deadlines.

8.3. Compliance with financial ceilings

Where measures are subject to quantitative limits, either in terms of total amounts paid, production or eligible areas, the CB is expected to check that procedures are in place to ensure that the total payments (across all the PAs) are within these quantitative limits. This includes an examination of the basis of the application of the ceilings as set out in measure and scheme specific regulations.

8.4. Compliance with aid intensity ratios

The CB is expected to check that aid intensities have been complied with and that EU and national ratios for allocation of EAGF and EAFRD Funds have been applied correctly.

8.5. Additional expenditure declared only in the annual declaration

The CB should check the accuracy and veracity of the additional expenditure declared only in the annual declaration. To this end, supporting documents should be examined to confirm the reasonableness of such expenditure.

8.6. Expenditure declared for Technical assistance at the initiative of the Member States referred to in Article 94 of Regulation (EU) 2021/2115

When the overall amount to be reimbursed is based on a flat rate of the amounts of expenditure of operations under the rural development measures referred to in Article 125(1), point (e), of the Financial Regulation, in the framework of interim payments pursuant to Article 32 of Regulation (EU) 2021/2116 and as set in the CAP Strategic Plan, the CB should verify that the flat-rate reimbursement is correctly calculated and applied.

9. CATEGORISATION AND CONSOLIDATION OF ERRORS

9.1. Categorisation of errors

As regards the audit of the completeness, accuracy and veracity of the annual accounts (audit objective 1) the following categorisation of the errors shall be used:

- Based on the financial impact triggered by the error/misstatement

– Errors identified after the payment stage and which trigger a financial impact;

– Errors identified after the payment stage and which by their nature remain formal errors (the payment is actually correct as to amount, but represents a transaction where one or more controls failed – e.g. payment was not made at the correct level);

- Based on the nature of the error:

– Systemic errors are errors found in the sample audited that have an impact in the non-audited population and occur in well-defined and similar circumstances. These errors have a common feature (e.g. type of measure

or scheme, transactions, the entity responsible for the authorisation etc.). These are associated with ineffective control procedures within part of the management and control systems. Where such a potential systemic error is discovered, it may be possible to extend the testing of the particular problem identified, if necessary until 100% of all potentially affected transactions have been tested. This testing should allow to "know" the effect of the systemic error over the entire population. This error is then treated as a "***known error***", and no extrapolation is needed. However, if it is not possible to test all transactions which have been affected, the error should be treated as a random error.

– Known errors are those identified either outside the sample, or resulting from a 100% test of a delimited stratum/population. Known errors relating to current year payments are added to the projected error, and therefore included in the total error evaluation unless a correction is made to the accounts.

– In line with ISA450, for systemic and known errors, the CB could apply a clearly trivial threshold of EUR 150 and 2 % of the audited amount. Thus, if the total financial impact of a known/systemic error is EUR 150 and 2% of the audited amount, the CB does not need to consider it in its error evaluation and follow-up.

– Random errors are those that could have occurred in any of the transactions which were not sampled for testing. For example, if an input error is found, it is assumed that the same type of error could, in principle, have affected any of the non-sampled transactions. The CB must, therefore, extrapolate all random errors over the entire population, in order to estimate their total effect. In some instances random errors can be ring-fenced to a known stratum/population. If the PA can demonstrate that errors only relate to a subset of the strata then the CB must extrapolate random errors over the subset identified. For the random errors, a clearly trivial threshold should not be applied as all random errors are subject to extrapolation, thus the financial impact of each financial error should be included in extrapolation and the error evaluation. Nonetheless, for reporting purposes only, random errors below EUR 150 and 2 % of the audited amount may not be described in the CB report. More guidance on that will be provided in the guideline on the reporting requirements.

– For the follow-up of clearly trivial errors (known, systemic or random errors) and their recovery, the provisions of Article 54(3) of Regulation (EU) no 1306/2013 are applicable.

- Based on the audit procedure/audit objective in which the deviation/financial error/misstatement is identified:

– **"Deviations from tests of control procedures and compliance testing"**: For the interpretation of number of deviations and errors found during the assessment of the internal control system refer to section 5. Random financial errors found in dual purpose testing should be taken into account in the ERR.

– **"Error rate – ERR", total projected error (TPE)[14] from the statistical sampling:** covers exclusively the overpayments (payment, accounting and reporting errors) for all transactions selected for substantive testing. The purpose is to estimate the financial impact of the errors identified by the CB. The type of errors to be included in the ERR are: correct calculation of the aid, cut-off issues, exchange rates, co-financing rates, etc.

– **"Reconciliation financial misstatements":** the errors found during reconciliation/analytical procedures.

9.2. Consolidation of errors

For its conclusion as regards audit objective 1, the CB's best estimate of misstatement in the Fund is the sum of the total error (only limited to payment and accounting errors) from substantive testing (UEL + known errors) and any errors related to a given financial year payment but found outside the substantive sample: e.g. errors found during the compliance testing (if not dual-purpose testing was used and therefore not included yet), reconciliation errors. The CB is expected to articulate how the consolidated error evaluation at Fund level factors into the audit opinion. (Hereafter referred to as TE consolidated at Fund level.)

Errors found in the non-operational transactions are not specifically highlighted in the above consolidation and interpretation of errors due to their different nature compared to the errors found in payments. First, the significance of these populations in the overall Fund needs to be assessed. Secondly, the significance of the individual errors needs to be assessed in terms of the respective population (i.e. recoveries or advances). And if it is established that the errors trigger material misstatement in the annual accounts the CB needs to ensure their appropriate inclusion in the overall conclusion as regards audit objective 1.

10. CONCLUSION WITH REGARD TO AUDIT OBJECTIVE 1

10.1. Evaluating the Sufficiency and Appropriateness of Audit Evidence

Based on the audit procedures performed and the audit evidence obtained, the CB should evaluate before the conclusion of the audit whether the assessments of the risks of material misstatement at the assertion level remain appropriate. The CB should conclude whether sufficient appropriate audit evidence has been obtained. In forming an opinion, the CB should consider all relevant audit evidence. If the CB has not obtained sufficient appropriate audit evidence as to a material assertion, the CB should attempt to obtain further audit evidence. If the CB is unable to obtain sufficient appropriate audit evidence, it should express a qualified opinion or disclaimer of opinion.

The conclusion on the completeness, accuracy and veracity of annual accounts should be built on:

- the assessment of the internal control procedures for the given PA functions (execution of payment, accounting for payment and debt management) taking into consideration also the assessment of the ICS on authorisation of payments as taken under audit objective 2,

- the results of the substantive testing (total projected error, upper error limit only limited to payment and accounting errors) and,

[14] TPE corresponds to the Most Likely Error (MLE) under the MUS conservative approach

- the consolidated TE which includes the known errors and the financial misstatements from the financial reconciliation work.

The table below provides an overview of the main scenarios.

Assessment of ICS for the given control procedures	**A) Substantive testing result B) Consolidated error: including reconciliation results**	**Completeness, veracity and accuracy of the annual accounts in the Opinion**
Assessment of the ICS at Fund level for payment, accounting and debt management: Works partially – Works – Works well	a) TPE < UEL < TM b) TE consolidated < TM	**Can be confirmed**
	a) TPE < UEL < TM b) TE consolidated > TM	**Cannot be confirmed – errors need to be corrected by PA**
	a) TPE < TM < UEL b) TE consolidated > TM	**Cannot be confirmed – additional work is necessary (section 6.2)**
	a) TM < TPE < UEL b) TE consolidated > TM	**Cannot be confirmed-errors need to be corrected by the PA Otherwise qualified opinion –differences detected**
Assessment of the ICS at Fund level <u>for payment and accounting:</u> Not working	***One of the 4 above scenarios***	**Cannot be confirmed Qualified opinion for deficient control procedure** – (Procedures need to be remedied – conformity audit procedure on accreditation issue)

All scenarios should take account of the corrective measures taken by the PA after the error evaluation as well as the significance of errors leading to the material consolidated total error.

The conclusion on the overall assessment of the effectiveness of the internal control system of the PA should be drawn based on the relevant sections of PARTS A, B, C and D.

PART B

11. ASSESSMENT OF THE MEMBER STATES' GOVERNANCE SYSTEMS

11.1. Objective

The objective of the CB is to obtain sufficient appropriate audit evidence regarding the functioning of the governance systems as provided in Article 12 (2b) of Regulation (EU) 2021/2116:

(i) the governance bodies referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and Article 123 of Regulation (EU) 2021/2115,

(ii) the basic Union requirements,

(iii) the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115 (deriving from the audit work under audit objective 3) and as interpreted in the matrices.

In this respect the CB should report on deficiencies, including serious deficiencies affecting the functioning of the governance systems either in the design procedure or in their implementation, through designing and implementing appropriate responses (audit procedures) to the risks identified through the course of the audit.

In accordance with Article 2(d) of Regulation (EU) 2021/2116, "serious deficiencies in the proper functioning of the governance systems' means the existence of a systemic weakness, taking into account its recurrence, gravity and compromising effect on the correct declaration of expenditure, the reporting on performance, or the respect of Union law". In other words, such deficiencies affect substantially (i.e. resulting in financial risk) the proper functioning of the governance systems.

As a result, the CB is to provide an assessment of the governance system as per the matrix in Annex 3 for Audit Objective 2. The CB will disclose the relevant findings (including the ones on serious deficiencies) related to the evaluation in the matrix in its annual certification report. In this respect, throughout its audit work (risk assessment, review of the control procedures, applying audit procedures, testing and reporting on results) the CBs should follow the structure as provided for in the matrix under Audit Objective 2:

- Accredited Paying Agency (results from AO1, 3 and 4 should be considered);
- Accredited Coordinating Body;
- Implementation of CAP Strategic Plan;
- Functioning/Implementation of Basic Union requirements per IACS and Non-IACS
- Reporting system (results from AO3 should be considered).

11.2. Financial risk

According to the International Standard on Assurance Engagement (ISAE) 3000, assurance engagements are planned and performed to obtain sufficient appropriate evidence in the context of the engagement about the reported outcome of the measurement or evaluation of the underlying subject matter against the criteria. Professional judgment needs to be exercised in considering materiality, engagement risk, and the quantity and quality of available evidence when planning and performing the engagement, in particular

when determining the nature, timing and extent of procedures and when evaluating whether the subject matter information is free of misstatement or deficiency. The CBs are requested to consider whether their findings affect the governance systems, resulting in a financial risk arising from any of the audit procedures applied for assessing the functioning of the governance systems.

Financial risk is considered in the context of qualitative factors and, when applicable, quantitative factors. The relative importance of qualitative and quantitative factors when considering financial risk in a particular engagement is a matter for professional judgment.

Qualitative factors may include such things as:

- The nature of a deficiency;
- Whether a deficiency affects compliance with law or regulation;
- The expenditure affected by the deficiency.

The interaction between, and relative importance of, various components of the subject when it is made up of multiple components, such as a report that includes numerous performance indicators.

11.3. Risk Assessment for the evaluation of the Governance Systems

A detailed risk assessment, including a risk analysis process for the quantification of the identified risks based on probability of occurrence and the impact factors, is considered to be a key element in order to set an effective and efficient in terms of resources audit strategy.

The techniques used for testing controls consist of assessing the control environment, the importance of controls, the risk that tests may not be conclusive and the outcome of other enquiries. Testing will cover the effectiveness of both the design and implementation of the controls. It consists of tests of procedures and tests of controls (compliance testing).

In order for the CB to identify and assess the risks of not functioning governance systems i.e. prone to serious deficiencies, an understanding of the entity and its environment should be performed (cf. ISA 315). This will include, among other things, an understanding of the:

- Regulatory framework and other external factors;
- Related governance bodies (the Paying Agency and the Coordinating Body) and procedures at other entities relevant to the governance systems;
- Nature of the entity including operations, structure, etc.;
- The internal control environment of the entity and its components;
- Entity’s information systems.

A detailed risk assessment and the relevant risk analysis would allow the CB to design its own proper audit strategy and to decide, among others on:

- The nature of audit procedures to be used;

- The possible synergies that may be applied on the testing of the different horizontal basic Union requirements and interventions;
- The use (or not) and the extent of a rotation plan during the testing;
- The type (random, risk based or mixed) and the size of the samples to be selected for the testing of controls applied by the PA or the other governance bodies in relation to the functioning and implementation of the basic Union requirements.

11.3.1. Accredited Paying Agency

The understanding of the main entity and its environment, in the case of the PA, is translated into the accreditation criteria laid down in Article 1 and Annex I of Regulation (EU) 2022/127 (i.e. the components of the internal control system):

- Internal environment (including the organisational structure; human resource standard; Risk Assessment and Delegation);
- Control activities;
- Information and communication (including information system security);
- Monitoring.

On the basis of the understanding of the accreditation criteria as put in place by the PA, the CB should also determine the design and the implementation of the controls embedded in the processes at PA level (i.e. at entity level). An improper design of entity controls which is not in line with the accreditation criteria may present a significant deficiency in the internal control system.

After assessing the overall internal control system at entity level on the basis of the accreditation criteria, the CB's work should include a review of the concrete processes in place (through review of the procedures). As regards audit objective 2, the accreditation criteria are to be reviewed for the authorization of payments for CAP Strategic Plan Interventions. However, the CBs need to use the results from the opinion for Audit Objective 1 (i.e. true and fair view of the PA's annual accounts), Audit Objective 3 (i.e. performance reporting system and procedure at the PA) or audit objective 4 (the legality and regularity of the expenditure not covered by the CAP Strategic Plans), if applicable for the overall assessment of the accredited PA as a governance body.

The assessment of the governance systems covers the following: it should be the basis for establishing the system assurance at the audit planning stage and it should be the basis for the assessment of the internal control system for the audited financial year to be expressed in the audit opinion.

11.3.2. Accredited Coordinating Body

In the framework of the assessment of the Member State’s governance systems the scope of the audit should cover some procedures implemented by the accredited Coordinating Body (CoB) (when applicable).

Similarly to what described for the PA, the CB should then get an understanding of the CoB and its environment. This is translated into the accreditation criteria laid down in

Article 2 and Annex II of Regulation (EU) 2022/127 (i.e. the components of the internal control system relevant to the compilation of the performance report):

- Communication
- Information Systems Security

In addition, the annual performance report needs to be covered by the scope of the opinion of the CB and that its transmission needs to be accompanied by a management declaration covering the compilation of the entire report. The CB is then requested to assess if the CoB has an administrative organisation and a system of internal control as regards the compilation of the annual performance report, which complies with requirements set by the Competent Authority as regards the procedures involved, and especially the criteria on information and communication as set out in Annex II of Regulation (EU) 2022/127.

11.3.3. Implementation of the CAP Strategic Plan

In order to express an opinion in the proper functionality of the Member State's governance systems, the CB is also requested to perform an overall assessment of the implementation of CAP strategic plan as per Article 9 of Regulation (EU) 2021/2115. The work will be limited to the elements included in the CAP Strategic Plan and not covered by the assessment drawn per blocks of basic Union requirements.

11.3.4. Functioning/Implementation of Basic Union requirements

As regards the functioning/implementation ([15]) of Basic Union requirements, the following main elements or control procedures[16] should be subject to this assessment:

- Aid application process in IACS (including preliminary checks where applicable) and the GSA;
- ISAP update and upkeep;
- Area Monitoring System procedure (where applicable);
- Compliance with Conditionality rules as per article 12 of Regulation (EU) 2021/2115;
- Authorisation of payment including administrative and on-the-spot controls;
- Calculation of payment including reductions/exclusions and penalties;
- Contracting process for public procurement;
- Methodology for establishing Simplified Cost Options (where applicable);

([15]) "Functioning/Implementation" is used as some of the basic Union requirements will need to be implemented (i.e. implementation of CAP Strategic Plan, implementation of interventions), while others will need to be functioning as implemented controls in the related governance systems (i.e. functioning Public procurement rules).

[16] These control procedures are considered to be the main ones. This list is not considered to be exhaustive and the CB should only use it as a basis and add other processes it considers to be relevant.

- Systems to ensure the eligibility of the beneficiaries, of the interventions and of the payments;

The assessment needs to be drawn at the level of EAGF and EAFRD. It means separately for EAGF IACS, EAGF Non-IACS, EAFRD IACS and EAFRD Non-IACS. However, the underlying compliance work can be set up across these populations. If for specific interventions there are significant system weaknesses identified, it is recommended to "isolate" the intervention / basic Union requirement or its element and to address the related financial risk with separate audit procedure.

The CB's work should begin with a review of the general control environment for the above-mentioned control procedures considering the following:

- Previous years' audit results for these control procedures (e.g. grading in the matrices);
- Changes in the legal, organisational, procedural, IT system and human resources set-up;
- Ongoing action plans which are not finalized.

In addition, the CB should perform the following:

- To get an understanding of the MS governance systems including the PA's control procedures and systems;
- To review the "translation" process, through which the requirements set out in the EU Regulations are incorporated in the PA's manual, computer procedures and written instructions;
- To conduct "walk-through" tests on the processes/procedures, including the IT processes to determine the functionalities of the control system;
- To identify "what can go wrong" (WCGWs) or risks in the process/procedure and related controls. For the above procedure the Non-exhaustive reference list of basic Union requirements should be taken into account as the benchmark against the MS governance systems including the PA's control procedures and systems.

On the basis of the above, the CB can design its audit strategy.

As a result of this exercise the CB will have the inventory of intervention / basic Union requirements assessing the inherent risk and the control risk and the combined risk assessment. Based on the results obtained and the knowledge gained, the CB will select appropriate testing procedures and sampling for compliance testing (test of controls) on selected controls to confirm the control system set-up and design.

11.4. Review of control procedures

11.4.1. Accredited Paying Agency and Functioning/Implementation of basic Union requirements

Based on the inherent risk assessed per basic Union requirement / intervention (Inherent Risk quantification) and the reliability of the control procedures as assessed in the previous step (quantification of control risk), the CB needs to consider for which part of the work it

needs to plan the test of controls and then plan it accordingly. Without elaborating an exhaustive list these procedures should for instance allow the auditors to establish whether:

- written guidance on the authorization of payments and computation is comprehensive and up-to-date and available to all staff;
- the IT system and related procedures are well designed and operated to comply with the procedural requirements (included in EU, national legislation);
- the tasks related to authorization of payments are appropriately segregated (as required by sector specific regulations), defined and subject to supervisory control;
- the PA's controls are in line with the basic Union requirements;
- there is appropriate staff training and rotation;
- there are adequate procedures for senior management checks and monitoring;
- and appropriate action is taken in response to recommendations on improvement accepted by the PAs as a necessary part of the accreditation process.

The CB should obtain sufficient and appropriate audit evidence that the controls selected for testing operate effectively as designed throughout the period to prevent or detect and correct serious deficiencies at the assertion level. Overall, the CB should be able to conclude whether the governance systems are designed in accordance with the basic Union requirements, including the internal control procedures of the PA against the accreditation criteria, whether these are operating as designed and whether these are effective in order to safeguard the Union's financial interests.

Among the above-mentioned techniques, audit tests on the IT systems have a key role considering that nowadays most of the governance systems and mainly the procedures of the PA are IT-driven. IT allows to process data and transactions consistently and enhances the ability to monitor the performance of control activities and to achieve effective segregation of duties by implementing access controls in applications, databases, and operating systems. Therefore, in order to rely on the automated controls embedded in the IT systems, the CB can perform audit procedures to determine whether an automated control has been implemented which may serve as a test of that control's operating effectiveness. To that end, the assessment and testing of IT-general controls (ITGCs), including IT security and change management procedures should be also taken into account. Planning the tests on the IT system adequately should be reflected in the CBs' audit procedures.

In Member States with more than one PA, some of the controls of a governance system or a basic union requirement might be implemented at national level. In such a case, the CB(s) may consider to carry out the risk assessment, the review of the control procedures and the relevant sample selection at national level. In such cases as regards the actual testing, it is up to the MS to decide on the allocation of resources (i.e. full work by one CB vs allocation of the task to various CBs). However, this approach should be applied with great consideration and only in cases where systems established at national level and procedures are the same at all levels and without any interference other than at central level.

For interventions/measures where the system is managed partly at central and at local level, the review of the proper functioning of the systems at national level should be complemented with testing at local level . In this work it should be ensured that the total sample selected at national level and the additional sample(s) selected at each local entity level are representative, as to provide assurance that the system as a whole operates properly.

11.4.1.1. Review of IT general controls (ITGC)

In case the PA is ISO 27001:2013 certified, the CBs can factor that into their ICS testing and rely on the implementation of the Information Security Management System (ISMS). If the PA is ISO 27001 / BSI ISO 27001 certified, and the scope of the certificate covers all key tasks of the PA, there is no need for further assurance work to be carried out by the CB regarding information systems security. However, the CB may decide to do some audit work in case: the CB has some justified doubts about the certification process or its quality or in case the certificate is not covering all key tasks / delegated bodies.

In case the PA is not ISO certified, the CB should satisfy itself that the information security controls in the selected information security standard are complied with, chapter by chapter. This audit work can be carried out by the CB itself or by using an external company.

ITGCs apply to all IT systems components, processes and data present in an organisation or systems environment. The ISA 315 ([17]) (revised 2019) include elements relevant for the assessment of the CB in relation to the PA's use of IT and the impact on the audit. Appendices 5 and 6 of that standard provide in particular considerations for understanding information technology and elements that the CB may consider in understanding ITGCs.

As provided for in Annex 1, point (3)(B), Information systems security, the PA's information systems security shall be certified in accordance with International Standards Organisation 27001 for PA responsible for the management and control of a yearly expenditure not higher than EUR 400 million. The ISO27001 certification demonstrates that the organisation has implemented the Information Security Management System (ISMS). The required level of assurance expected in instances where reliance on the application controls is intended is not entirely covered by this certification. ISO27001 allows the PA to apply their discretion on the adherence and implementation of the controls. In addition, to issue the certification the ISO27001 auditor is not required to test samples to the same scale as that expected in standard audits. Therefore, additional work should be considered by the CB to achieve the operational effectiveness requirements which would allow them to adopt a control-based approach i.e., relying on a test of 1 for IT Application controls.

The CB should leverage the controls identified and tested as part of the ISO27001 certification process and ensure they address the following IT risks:

- Reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both
- Unauthorized access to data that may result in destruction of data, improper changes to data, including the recording of unauthorized or non-existent transactions, or inaccurate recording of transactions

[17] https://www.iaasb.org/publications/isa-315-revised-2019-identifying-and-assessing-risks-material-misstatement

- The possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties, thereby breaking down segregation of duties
- Unauthorized changes to data in master files
- Unauthorized changes to systems, programs, and configurations
- Failure to make necessary changes to systems or programs
- Inappropriate manual intervention
- Potential loss of data or inability to access data as required

The CB will be required to test the operational effectiveness of the ITGCs throughout the period. Since reliance on the IT application controls is expected, the appropriate sample sizes should be used to test the controls which mitigate IT risks above. The sample sizes should be commensurate with the frequency of the controls. See suggested guidance in this respect below:

Frequency	**Minimum sample sizes**
Performed daily or many times per day	25
Performed weekly	5
Performed monthly	2
Performed quarterly	2
Performed annually	1

11.4.1.2. Review of IT application controls

Every PA has numerous IT systems and IT applications with embedded controls in them. Some controls are automated (no manual interference) and the CB may consider testing the automated application controls since if they operate as intended, they provide high reliance, enabling an efficient use of audit resources. In order to rely on the automated controls, the CB may develop audit procedures to determine whether an automated control has been implemented. However, for efficiency the CB can select the IT application(s) under an intervention / measure based on a risk assessment.

Once the CB selects an IT application, it should determine which automated controls to test. The rule of thumb is to test the application controls that cover most audit assertions and most WCGWs. Once an automated application controls has been selected for testing and determined that it is functioning as intended, the CB may consider performing a **test**

of one[18] on that control and some other tests to determine that the control continues to function effectively. Such tests might include a verification that;

- All automatically input data are accurate, complete, authorized and correct;
- All data are processed as intended;
- All data stored are accurate and complete;
- All output data are accurate and complete;
- A record is maintained to track the process of data from input to storage, and to the eventual output;
- Access to data is limited based on business need;
- Incompatible duties within an application are systematically prevented.

Application controls relate to the transactions and data pertaining to each computer- based application system. They are specific to each individual IT application. It is important to note that the degree that application controls can be relied on depends directly on the design and operating effectiveness of ITGCs. In other words, if ITGCs are not implemented or operating effectively, the Paying Agency may not be able to rely on its application controls to manage risks.

For the testing of the IACS cross-checks and automated/application controls, please refer to the audit methodology on IACS cross-checks and data integrity as mentioned in 1.1.6.1.

11.4.2. Accredited Coordinating Body

Based on the inherent risk and the reliability of the control procedures as assessed in the previous step (quantification of control risk), the CB needs to tailor its audit procedures in order to establish whether the CoB adopts the necessary procedures to ensure that every change in the Union's regulations is recorded and the instructions and databases updated in good time (point 1 (A) of Annex II or Regulation (EU) 2022/127). With regard to "Information Systems Security", the information systems security shall be certified in accordance with International Standards Organisation 27001: Information Security management systems – Requirements (ISO). We refer to the previous chapter for the assessment of the IT controls under Accredited Paying Agency.

Moreover, the CB has to establish audit procedures to assess whether the CoB has set up control procedures to ensure that the annual performance report is timely and correctly transmitted to the EC and that its transmission is accompanied by a management declaration covering the compilation of the entire report.

To perform a review of the IT controls implemented by the CoB, the CB should define its audit procedures similarly to what is described in the previous chapters concerning the PA. Moreover, to assess the controls implemented by the CoB, the CB will apply analytical procedures (such as reconciliation and data analysis), as well as walkthrough analysis and interview with the management.

[18] The functioning of the control is tested only one time as it is an automated one

11.4.3. Implementation of the CAP Strategic Plan

As mentioned in previous paragraphs, following the quantification of control risk, the CB also needs to assess the steps/actions related to the implementation of the CAP Strategic Plan (as per Article 9 of Regulation (EU) 2021/2115) which are not directly implemented by the accredited Paying Agency (and when applicable by the accredited Coordinating Body).

Similarly to what described for the Accredited Coordinating Body, these residual controls will mainly be checked by the CB via analytical procedures and interviews with the key staff involved.

11.5. Assessment of control procedures

Outcome: An assessment of system deviations found based on the following categories:

Assessment of control procedures	Assessment of deviations
1. Works well, only minor improvements are needed	All risks are adequately addressed by controls which are likely to operate effectively. No exception was found. OR only minor (formal) deviations were found which did not affect substantially the effectiveness of controls and did not lead to financial consequences.
2. Works, but some improvements are needed	All risks are adequately addressed by controls which are likely to operate effectively with some deficiencies having a moderate impact on the functioning of the basic Union requirements. Only minor deviations were found, which did not affect substantially the effectiveness of controls. OR if those minor deviations affected substantially the effectiveness of controls the PA's ongoing controls detected them and the self-correcting mechanism of the PA operated.
3. Works partially, substantial improvements are needed	All risks are addressed to some extent by controls which may not always operate as intended. Moderate deviations were found, which affected substantially the effectiveness of controls. AND only part of these moderate deviations was detected by the PA's ongoing controls and corrected by the PA itself.
4. Not working	Not all risks are addressed by controls and/or there are likely to be frequent control failures. The governance systems function poorly or does not function at all. The deficiencies are systemic and wide-ranging. Financial consequence was established and that was not detected by the PA's internal control system.

Minor deviations signal formal exceptions in the applied procedures compared to the designed procedures or in the designed procedures compared to the legal requirements, which means that the controls work in most cases and prevent or detect/correct financial consequences.

Moderate/high rate of deviations are exceptions in the applied or designed procedures which means that the controls failed to prevent or detect/correct the financial consequences. This may be translated in financial risk.

11.6. Compliance testing (test of controls)

11.6.1. Accredited Paying Agency and Functioning/Implementation of basic Union requirements

In order to express an opinion on the effectiveness of the governance systems, the CB should examine the specific, pervasive and monitoring controls embedded within the reviewed process(es): systems, procedures, manuals. The compliance testing is performed to support the CBs assessed level of the control risk. The test of controls should test the effectiveness, i.e. set-up, design and functioning of a control used to prevent or detect serious deficiencies. When performing compliance testing the CB should examine for the selected specific items[19] if:

(1) the necessary controls are in place and designed in accordance with the legal framework;

(2) the necessary controls operate as designed and prevent/detect and correct deficiencies at assertion level.

The following aspects need to be confirmed through the compliance testing:

- The elements of the basic Union requirements were set properly in the procedures and systems of the PA and they function properly, e.g. as regards public procurement, or conditionality;
- The systems to ensure eligibility of beneficiaries, interventions and payments were set properly in the procedures and systems of the PA and of the competent control bodies and they function properly, etc.

For that matter, WCGWs that affect the above assertions should be identified and the related controls that mitigate the WCGWs should be identified as well.

The following WCGWs that could have a substantial effect on the relevant assertions could be considered:

- there is a likelihood of deficiency;
- the potential deficiency is of a magnitude that could result in a serious deficiency.

To identify controls that are relevant for the audit, the following should be considered:

- controls that mitigate significant risks;
- highly automated processes and application controls;

[19] Refer to section on Sampling unit

The CB should consider the different types of controls in their testing. Part of these tests can be carried out through an IT application control for all the populations (the system detects double claims for example). Alternatively, provided that the IT general controls (ITGCs) over maintenance, information security and computer operations activities are effective, the operation of an automated application control can be confirmed through a test on the automated application control limited to one transaction. In these cases, there will be one test of control (test of one) for one selected automated application control in the IT application. The CB should explain the method used in its certification report. For the testing of the IACS cross-checks and automated/application controls, please refer to the methodology on IACS cross-checks and data integrity (Ares(2017)6225522 - 19/12/2017).

Type and size of samples:

For the controls which are not considered fully automated, the compliance testing is carried out through the review of a sample of files processed and authorized for payment. Although the type of samples selected per test is based on the CBs professional judgement, it is considered that the basis of the selection of the sample should be the result of the overall risk assessment and the review of the procedures as described above. Thus, a mixed type of samples selected mainly on a risk basis linked with the risk assessment results with additional items selected randomly in order to confirm the sampling process is strongly recommended.

For the horizontal requirements (i.e. requirements that affect more than one intervention), the following aspects, among others, should be taken into consideration during the sampling formation:

- Coverage of interventions affected;
- Isolated risks per intervention;
- Different competent control bodies responsible for the checks.

The test of control will depend on the type of control and the frequency of the control and whether the CB decides to draw a sample per intervention, or other horizontal element of basic Union requirements. It should be noted that the frequency of the control is calculated on the basis of the times that the control has been applied and not on the basis of the transaction / claim, neither at the level of the beneficiary. For example, the control of the public procurement procedure in a LEADER project under EAFRD Non-IACS has been carried out equal times as the procedure itself has been applied even if the transaction at the level of the beneficiary is one. However, the establishment of the sampling population depends on the nature of the data that can be provided to the CB (e.g. it is not always the case that the PA can provide the number of invoices where the administrative control on reasonableness of cost has been carried out). The CB will need to use its professional judgement as regards the sample size determination. The selection process (i.e. risk factors used, total sample size per audit procedure, split between risk based and random, etc.) should be described in detail in the CB's audit strategy. Nevertheless, details on the establishment of the overall sample of compliance tests performed for AO2 for each of the IACS and Non-IACS populations are included in Annex 1.

Test of controls mapping:

Although each basic Union requirement should be tested and evaluated separately, the CBs may consider applying synergies between the various tests of controls. A mapping of

different samples selected for the testing of different controls is, therefore, recommended when the CBs want to explore the possibility of serving different audit purposes (test of a basic Union requirement) with the same samples or part of samples. It is highlighted that items selected for one audit purpose on a risk basis can be used for other audit purposes only as items selected randomly unless the CB can, based on its professional judgement, provide adequate arguments that the exact items can serve the needs of a risk-based selection also for different audit purposes. The CB is requested to provide further details in its audit strategy as regards the synergies applied on the various tests.

Rotation of controls:

The CB may choose to rotate the controls or the whole control testing of certain interventions in the respective population. Any decision taken as regards the rotation of controls per horizontal basic Union requirement and / or intervention should be based on the results of the risk assessment already performed. In such case, the CB may decide to avoid annual testing for less risky basic Union requirements and / or interventions. It is however noted that the horizontal requirements as presented in the matrix are expected to be tested annually.

A rotation of controls could be done under the following conditions:

- The governance systems (current and previous period) have been operating effectively;
- The CB has confirmed its understanding of the processes/procedures and the relevant controls in the current period through walkthroughs;
- The processes and routine have been found to operate well in the past and there are no major changes in the current period;
- The rotation period could be set to 3 years but in case of a high number of different schemes/measures in a given population, to 5 years.

Bottom up approach:

Grouping of different samples can be applied.

This approach starts from the various basic Union requirements of the various interventions, which the CB decides to test based on the risk assessment already performed (rotation of controls may be applied to less risky requirements and / or interventions as described above). Different samples (mixing items selected on a risk basis and randomly) are selected for testing. The testing of those items can also be used for the testing of the horizontal requirements, which are to be tested annually. The testing of the horizontal requirements may be expanded in the case the samples already tested per individual intervention do not cover the objectives of the risk assessment performed for the horizontal requirements (e.g. different risks identified or bodies involved in the process, etc.) or the samples formulated for the horizontal requirements are not considered adequate.

Sampling unit

Items (transactions, files, invoices) as referred to so far represent the sampling unit, which should be established in a way that meets the audit needs as revealed after the overall risk assessment, the design of the audit strategy and the potential synergies that the CB would like to achieve by grouping the testing of the basic Union requirements of the different interventions with other requirements that are considered horizontal. For Audit Objective 2, the CB is to provide an assessment of the governance systems as per the matrix in

Annex 3. Therefore, the CB is recommended to use a sampling unit which is linked to the control embedded in the governance systems.

For example, if the CB decides to test the LPIS QA, a sample selected at the level of parcels might serve the audit needs, while for the confirmation of the set-up and design of on the spot controls a sample of controls and thus OTSC reports might be more appropriate. On the contrary, for Non-IACS populations, if the CB decides to test the administrative control on reasonableness of cost, a sample on the basis of invoices subject to such a control can be considered appropriate.

It should be noted that even if the sampling units per sample are different, synergies may still apply, if the CB decides to further expand the testing as described above. It is recommended that the sampling unit used for the population determination is also used for the sample size determination. Reduction or multiple use of samples for synergies should not go to the detriment of the quality of the audit work.

Whichever sampling unit is applied the overall objective of the testing remains, i.e. the confirmation of the functioning of the controls and thus the set-up and design of the controls.

Outcome: An assessment of the financial consequences found based on the following categories:

Assessment of control procedures	Assessment of errors
1. Works well, only minor improvements are needed	No exceptions/errors were found. OR only minor (formal or one-off) exceptions/errors were found which did not affect substantially the effectiveness of controls and did not lead to financial consequences
2. Works, but some improvements are needed	Only minor exceptions/errors were found, which did not affect substantially the effectiveness of controls. OR if those minor exceptions/errors affected substantially the effectiveness of controls the PA's ongoing controls detected them and the self-correcting mechanism of the PA operated.
3. Works partially, substantial improvements are needed	Moderate exceptions/errors were found, which affected substantially the effectiveness of controls. AND only part of these moderate errors was detected by the PA's ongoing controls and corrected by the PA itself.
4. Not working	High rate of exceptions/errors were found which were not detected by the PA's internal control system.

The definition of minor, moderate and high errors correlate to the definition of minor, moderate and high deviations as mentioned above.

11.6.1. Accredited Coordinating Body

As regards the systems or procedures at the Coordinating Body compliance testing would be relevant in terms of assessment of the performance reporting system, depending on the

set-up of that system at Member State level. And as described in point 11.4.2 mostly this would be addressed by audits of IT controls.

Other criteria related to the accredited Coordinating Body can be addressed via other type of audit procedure.

11.6.2. Implementation of the CAP Strategic Plan

As mentioned in point 11.4.3 compliance testing will not be relevant for this part of the audit work. However, the CB will need to address the related procedures by other types of audit procedure.

11.7. Results for assessment of the internal control system

Following the three steps as mentioned above the CB will need to conclude on the assessment of the governance systems as per the matrix for AO2. The table below represents one possible example for this exercise:

Population / Intervention	**Basic Union requirement**	**Combined risk assessment / Systems assurance**	**Outcome of compliance testing**	**Final assessment**
IACS / Eco Schemes	**Systems to ensure eligibility of interventions**	Works well Minor exceptions/deviations are expected or detected by the PA's systems	No error was found	Works
Non IACS / LEADER	**Public procurement**	Works partially Moderate exceptions/deviations are expected or detected by the PA's systems	Moderate errors were found, only some of them were detected by the PA's controls	Works partially

The final assessment should always be aligned with the worst assessment for the outcome of the inherent risk assessment (section 11.3) combined with the review of the control procedures (section 11.4) and the outcome of compliance testing (section 11.6), as illustrated on the first example of the above table (i.e. the assessment of the control procedures indicates a "works" control environment while no errors – works well- were found during the compliance testing, thus the final assessment).

The work performed by the CBs would allow the evaluation of the accreditation criteria regarding the Accredited PA as presented in the first matrix of audit objective 2 but also the assessment of the functioning/implementation of the basic Union requirements (horizontal and non-horizontal). The results of all audit procedures performed for the assessment of the functioning/implementation of the basic Union requirements is expected to be used for the assessment, mainly, of the "control activities" accreditation criteria but also for other criteria if the CB has assessed that the cause of the deficiencies identified affect other criteria too (e.g. lack of supervision on delegation, lack of experience staff to perform the controls, etc.).

12. ANALYTICAL PROCEDURES

The CB also has to verify the state of play of the implementation of any action plans addressing conformity findings triggering reservations in the management declaration of DG AGRI in the AAR.

Action plans triggered by conformity findings based on which reservations were made in DG AGRI's management declaration in the AAR or related to other DG AGRI findings and conclusions should have an impact on the planning of the CB's audit procedures. As regards the analytical procedures the CB could verify:

- If the action plan was set up when it was required,
- If the action plan is implemented in accordance with its planned schedule,
- If the remedial actions in the action plan will remedy the deficiencies included in the conformity findings.

13. CATEGORISATION OF FINDINGS AND ESTABLISHMENT OF THE FINANCIAL RISK

13.1. Categorisation of findings

As regards Audit Objective 2, the CB is required to express an opinion whether the functioning of the governance system is free of serious deficiencies or not. In general terms, a deficiency is described as a situation whereby the management and control systems do not ensure the appropriate functioning of governance bodies and the respect of basic Union requirements including the proper functioning of the reporting system. A deficiency, therefore, should be assessed at system level and not at the level of the individual beneficiary. Regarding the deficiency as such, a distinction needs to be made between those that are considered "serious" and others.

A serious deficiency occurs where the proper functioning of the governance systems is impeded by a serious system weakness. Such a deficiency may have an impact on the correct reporting of individual interventions. A serious deficiency must have a systemic impact in terms of its occurrence and its gravity as to be considered as such.[20] Without elaborating a comprehensive list, the following situations are considered where serious deficiency would manifest:

- Where a certification body has not been appointed or a paying agency has not been accredited.
- Where the accreditation criteria were not respected. For example, where the appropriate technical skills as required at different operational level are absent or clearly dysfunctional.
- Absent or insufficient remedial actions taken where the quality assessments for the ISAP, geo-spatial application and area monitoring system, revealed deficiencies. This may have an impact on the correct reporting.

[20] This would also be the case where a management and control element is absent.

- Non-respect of public procurement rules. Since clear legal Union requirements were not respected; the expenditure cannot be considered eligible.

- The non-application of penalties. For example, where since there is no deterrent effect, the management and control system is not functioning properly.

- For example, where it is found that the body certifying that land has been managed according to organic practices is not operating to an appropriate standard. This means that the output was not correctly reported, in this case "area managed organically".

- Any serious system weaknesses with regard to the control and penalty system for conditionality.

- Lack of a system to ensure the sound financial management of the interventions.

- Lack of a system for verifying the reality of the costs and the implementation of the actions.

- Use of unit costs, flat rates or lump sums without being established based on an appropriate calculation method (fair, equitable and verifiable)

- Any other serious system weaknesses (it can be established via a combination of factors) identified through the annual certification audit by the certification bodies and that would impact upon the eligibility of expenditure at MS level.

- Other deficiencies not categorized as serious. A "non-serious" deficiency could constitute e.g. a situation:

  - Where there is insufficient staff in the paying agency without adverse impact on the proper functioning of the management and control systems.

  - Where the certification body has been appointed late but delivers the opinion on time and the appointment does not affect significantly the quality of the work performed.

  - Where the ISAP (now ISAP instead of LPIS) /GSA/Monitoring QA is submitted late but with no adverse impact on the positive test results.

- Where reconciliation anomalies are found by the CB, but they relate exclusively to reporting mistakes (possibly event corrected before the submission of the APR) and do not relate to weaknesses in the management and control system.

Regarding the classification of the deficiencies found, the CBs are requested to provide a description of all issues found during the assessment of the governance systems.

At least, the following aspects should be taken into consideration:

- the recurrence, gravity and compromising effect of each deficiency identified;

As per Article 2 of Regulation (EU) 2021/2116, serious deficiencies in the proper functioning of the governance systems' means the existence of a systemic weakness, taking into account its recurrence, gravity and compromising effect on the correct declaration of expenditure, the reporting on performance, or the respect of Union law. The Guidelines on the calculation of financial corrections are to give further details as regards these aspects of assessment.

- The action taken by the MS to remedy the deficiencies identified;

The CBs should always consider that "other" persistent or recurrent deficiencies can become serious over time. In contrast, the impact of serious deficiencies may be reduced, if immediate actions are taken. In many cases, the positive, in case of immediate action, or negative impact, if no action is taken, of the MS decisions can be assessed, even during the same certification audit. In such case, a re-assessment, several months later, is strongly recommended. However, the basis of the re-assessment should always remain the impact of the deficiencies to the expenditure of the financial year under certification.

13.2. Consolidation of findings – Scoring in the matrices

For its conclusion as regards Audit Objective 2 (i.e. Member States' governance systems put in place function properly), the CB's should assess:

a) The Governance Bodies', referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and their compliance with the accreditation criteria; and the Managing Authority as per Article 123 of Regulation (EU) 2021/2115 for the implementation of the CAP Strategic Plan;

b) The functioning / implementation of the basic Union requirements;

   See the non-exhaustive reference list of the basic union Requirements; which are incorporated through basic Union requirements blocks (as per Annex 2) in the matrix presented in Annex 3 for assessment purposes.

c) The functioning of the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115, as per Article 59(3) of Regulation (EU) 2021/2116.

As regards, the PA's compliance with the accreditation criteria (i.e. Article 1 and Annex I of Regulation (EU) 2022/127), the assessment should be carried out per accreditation component following also Guideline 1 on accreditation. For several components (e.g. Control activities, Communication, Delegation), the assessment should also take account of the results of the testing for the functioning / implementation of the basic Union requirements if the root of the deficiency identified can be linked to a specific accreditation criterion / component.

In case of Member States with more than one PA, the compliance of the Coordinating Bodies with the relevant accreditation criteria (Article 2 and Annex II of Commission Delegated Regulation (EU) No 2022/127) as regards the compilation of the Annual Performance Report, is required. Similarly to the accredited PAs, the assessment should be carried out per accreditation component.

For both cases described above, the overall conclusion is based on the assessment of each component multiplied with a weighted factor per component.

- As regards, the assessment per block of basic Union requirements as presented in the matrix in Annex 3, the following aspects should be taken into consideration: The recurrence, gravity and compromising effect of each deficiency identified;

- The number of deficiencies identified per block of basic Union requirements as per the matrix;

For example, when assessing the proper functioning of the ISAP (proper update and upkeep as per chapter 11.1), the following elements should be taken into account:

– The correct level of accuracy;

– The proper identification of parcels and the localization of agricultural parcels and non-agricultural areas claimed for payment;

– The use of up to date values considered eligible by the MS for receiving the aid for the interventions referred to in Article 65(2) of the Regulation (EU) No 2021/2116 and identify

– Appropriate action following the ISAP QA results.

It is often the case that deficiency(ies) per element of basic Union requirement can be assessed as non-serious. However, the overall assessment at the level of basic Union requirement may lead to serious deficiency or, vice versa. The overall assessment of the system can be "Functions partially" while one system element is assessed as seriously deficient.

- The interventions and the relevant expenditure affected by the deficiencies identified;

Horizontal basic Union requirements (e.g. public procurement, GSA, AMS, etc.) refer to more than one intervention. In addition, although the non-horizontal basic Union requirements (e.g. eligibility of the applicants) are linked to individual intervention, the matrix requires an overall assessment at population level (IACS / Non-IACS). Moreover, the CBs may decide to apply the compliance testing and, thus the relevant sampling, by grouping the interventions per block of basic Union requirements as presented in the matrix (Annex 3). The deficiencies identified should be reported with identifying the relevant interventions. However, the overall assessment in the matrix is the result of all individual assessments per block of basic Union requirements taking into account the relevant expenditure for which the deficiencies are identified.

Further guidance regarding the assessment of the compliance testing results and the grading of the matrices can be found on annex 3 of the Guideline,

Based on the grading in the matrix, the CBs should conclude whether:
- the governance systems function; or
- serious system weaknesses (serious deficiencies) impede the proper functioning of the governance systems

Assessment of systems	System assurance	Grading
Functions well	High/Medium high	3.51-4
Functions	Average	2.51-3.5
Functions partially	Medium low	1.51-2.5
Not functioning	Low	1-1.5

14. CONCLUSION WITH REGARD TO AUDIT OBJECTIVE 2

The CBs need to present the assessment of the governance systems using the above mentioned grading in compiling the matrix as per Annex 3 and accordingly feed the overall results from the matrix into their opinion.

Even if based on the overall grading of the matrix to be presented in the CB's annual audit report the governance systems function properly serious deficiencies found at the level of an assessment component of the accreditation criteria or basic Union requirements would need to be highlighted and explained in the report and if financial impact justifies also referred to in the CB's opinion. To be noted that all deficiencies identified would need to be reported in the CB's report as mentioned above and consequently to be considered in the assessment of the governance systems.

The financial impact of a serious deficiency identified would need to be estimated by the CB in order to express an opinion on the overall functioning of the governance systems. The establishment of the financial impact may follow the guidance provided in the Guidelines on the calculation of financial corrections and other methods used by the CBs and Member States to provide the actual financial impact of a system weakness.

In case no such estimation or punctual calculation can be provided within the CB's report the Member State authorities will be requested to provide information on the actual financial impact in a conformity clearance procedure that is to be launched in all cases when serious deficiency is found in the governance systems and no mitigating factors can be taken into account.

As explained above the Member States immediate follow-up and remedial action can be taken into account not only in the overall assessment of governance systems but also in terms of evaluation of the financial risk and thus the follow-up of any serious deficiencies when found and reported for the audit of the given financial year. Remedial actions could include actions taken to improve the system, to mitigate the financial impact (i.e. self-corrections in the payments and declared amounts, etc.) that could be verified and reported by the CB.

15. PARTICULAR CONSIDERATIONS

15.1. Use of work performed by other auditors / expert bodies

The CB can choose to outsource audit procedures to experts/expert bodies if they have the relevant competence and expertise. In case the CB outsources a part of its work and depending on the arrangements, the provisions of ISA 600 *"Using the work of another auditor"*, ISA 610 *"Using the work of internal auditors"* and 620 "*Using the work of an auditor's expert*" should be considered.

In principle to ensure a fully impartial assessment, the CB should not outsource its work to the PA. Whenever the audit work is outsourced the CB should follow the requirements of ISA 500 “Audit Evidence” par, 8. Pertaining to that, according to ISA 500, par. 8 and A34-48, if information to be used as audit evidence has been prepared using the work of a management's expert, the auditor should, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes:

- evaluate the professional qualifications, independence/objectivity, professional competence and resources (ex. 3rd party certificates in case of experts);
- obtain an understanding of the work of that expert; and
- evaluate the appropriateness and adequacy of that expert's work as audit evidence for the relevant assertion.

In all cases, the CB's audit work, including the supervision and monitoring over the expert / expert body / other audit body should be carried out in accordance with internationally accepted audit standards and adequately documented.

If the CB relies on a 3rd party certificate in order to gain assurance, then it should also ensure the appropriateness, scope and quality of the work performed. The audit report related to the 3rd party certificate should be provided.

In case the CB relies on the work of the PA's Internal audit, the extent to which the CB uses the work of the Internal audit should be described in the audit strategy and the annual report.

PART C

16. AUDIT RISK MODEL AND AUDIT PROCEDURES

The objective of the CB is to provide an opinion:

- on the effectiveness of the reporting system, as part of the management and control system (MCS) (as regards the respective procedures: data capturing and reporting system and procedures within the PA and from external sources); (this work will be used also in the context of AO2)

- on the correctness of the performance reporting, demonstrating that Article 37 of this Regulation is complied with, as regards:

    (1) output indicators for the purposes of the annual performance clearance referred to in Article 54, and

    (2) result indicators for the multiannual performance monitoring referred to in Article 128 of Regulation (EU) 2021/2115

The audit as regards audit objective 3 will cover one financial year (16/10/202x-15/10/202x+1)

16.1. Definition of audit risk model and assurance levels

Refer to chapter 4 above.

16.2. Risk analysis and definition of audit procedures

Proposed timing

Depending on the number of phases of audit procedures including the testing if considered necessary, the risk analysis can already be carried out in January-March of the audited financial year, but it should be planned for June-August at the latest.

Main tasks

- To assess the inherent risk and the control risk (the risk of material misstatement) based on previous years audit results and through the assessment of the internal control system (AO2);

- To plan all the audit procedures (timing and resources) including the assessment of the reporting system, the compliance testing, the review of reconciliations, the interpretation of errors and results and preparation of the certification report and formulation of opinion.

16.3. Risk Assessment for the assessment of the performance reporting system

For the CB to identify and assess the risks that the Performance Reporting System does not function properly, an understanding of the PA and its environment should be performed in the context of AO2 (cf. point 11.3). In addition, the risk assessment for the assessment of the Performance Reporting system will include an understanding of the:

- Regulatory framework and other external factors related to the Performance Reporting System;

- Related information systems and procedures at other entities relevant to the Performance Reporting System.

16.4. Review of procedures and IT controls for the performance reporting system

The review should cover the data capturing and reporting procedures and systems established at the Paying Agency and also provided by other bodies. The procedures are expected to be fully automated IT system based.

The CB shall consider testing the automated controls at the application level of the IT systems for performance reporting. A review of the IT controls for the performance reporting system is recommended on an annual basis. However, when the system has not altered from the previous year the CB can rely on its work of the previous years.

The CB may perform audit procedures to determine whether an automated control has been implemented. Such tests might include a verification that;

(1) All input data are accurate, complete, authorized and correct;

(2) All data are processed as intended;

(3) All data stored are accurate and complete;

(4) All output data are accurate and complete;

(5) A record is maintained to track the process of data from input to storage, and to the eventual output;

(6) Access to data is limited based on business need;

(7) Incompatible duties within an application are systematically prevented.

This review will provide the basis for the assessment of the reporting system, the result of which is to be used also under Audit Objective 2, as well as for the subsequent substantive analytical procedures to establish the correctness of the annual performance report.

16.5. Substantive analytical procedures

In order to express an opinion on the correctness of the Annual performance report, the CB should verify that the data on output and result indicators established in the system of the PA or other entity correspond to the data included in the report.

In a fully automated environment this could already be confirmed through the review of the procedures and controls. However, if the following aspects have not been covered yet the CB needs to confirm them through substantive analytical procedures:

- **Completeness**: all data that should have been recorded have been recorded.

- **Accuracy**: the data are disclosed in the Annual performance report at the correct/appropriate amounts.

- **Cut-off**: data have been recorded in the correct reporting period, i.e. in the period in which the payment actually took place.

Type and size of samples:

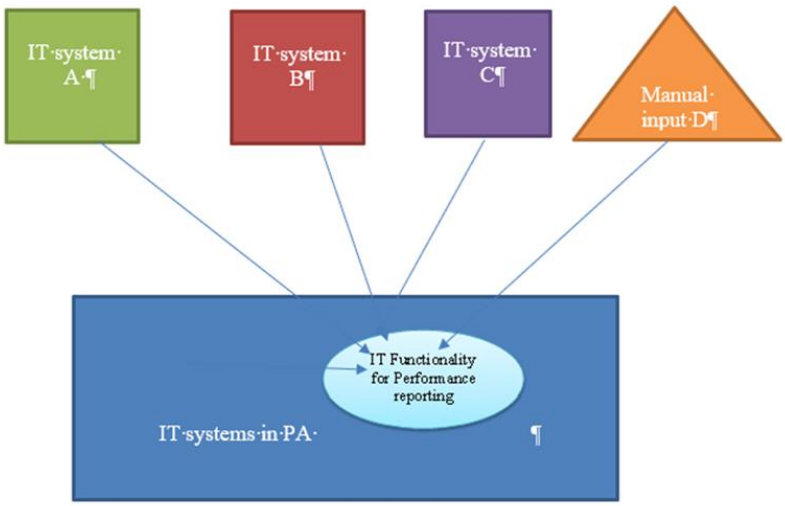
Although the type of samples selected per test is based on the CBs professional judgement, it is considered that the basis of the selection of the sample should be the result of the overall risk assessment. Thus, a mixed sample selected mainly on a risk basis linked with the risk assessment results with additional items selected randomly in order to confirm the sampling process is strongly recommended, following different scenarios of structure (cf. relevant examples below):

Scenario A

All output indicators can be produced from the PA's IT systems which feeds the IT functionality for the Performance reporting.

Scenario B

The output indicators are produced in different IT systems of the PA and transmitted to the IT functionality for the Performance reporting and/or includes manual input.



16.6. Review of reconciliations

Proposed timing

For audit objective 3, the reconciliation and review of the reconciliation of the annual performance report need to be carried out after the end of the financial year.

Main tasks

To review the reconciliation procedure of the PA and to check the accuracy of each part of the of the annual performance report.

To consider

A procedure should be established to assess and confirm the reconciliation (provided by the PA in the APR) between expenditure (gross expenditure) as per the annual performance report and expenditure declared in the annual accounts (net expenditure) taking into consideration any adjustments relating to any penalties, other reductions, recoveries etc.

The proper timing of the work and in that respect collaboration with the PA is essential to ensure that both the PA and the CB can fulfil their tasks.

16.7. Interpretation of errors, results

Proposed timing

The individual errors, deviations found throughout the testing must be interpreted and evaluated before M12 to allow for the PA's reaction.

Main tasks

To establish and to document clearly the errors and to perform the error evaluation.

17. PARTICULAR CONSIDERATIONS

17.1. Use of work performed by other auditors / expert bodies

In case the CB chooses to outsource the audit procedures to experts/expert bodies chapter 15.1 of this Guideline should be applied.

PART D

18. ASSURANCE ON THE LEGALITY AND REGULARITY OF EXPENDITURE

The objective of the CB is to provide an opinion on:

- expenditure for the measures laid down in Regulations (EU) No 228/2013, (EU) No 229/2013, (EU) No 1308/2013 and in Regulation (EU) No 1144/2014 of the European Parliament and of the Council as per Article 12 (d) of Regulation (EU) 2021/2116 (i.e. expenditure not covered by the CAP Strategic Plans) as well as for the crop-specific payment for cotton and support for early retirement under Title III, Chapter II, Section 3, Subsection 2, and Article 155(2), respectively, of Regulation (EU) 2021/2115 and / or the expenditure of measures / schemes approved before 1 January 2023, for which reimbursement has been claimed is legal and regular, and

- the PA's internal control procedures have operated satisfactorily.

Guideline 2 as applicable in FY2022 is to be used for the expenditure under legality and regularity mechanism in FY2023.

The audit under audit objective 4 will be based on declared or estimated expenditure[21] in the financial year. However, if deemed appropriate by the CB, the actual sampling could also be done on claimed amounts. Since for NON-IACS there are no time constraints, the actual sampling could be based on the actual payments. However, for cases of IACS schemes that are subject to audit objective 4 (e.g. crop-specific payment for cotton), the time constrains of the controls, including on-the-spot controls, should be taken into considerations on the establishment of the sampling unit and the relevant selection.

[21] Amount of expenditure determined following **all checks** done by the PA, compiled in the database/records and paid

PART E

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19. FACTORING CONCLUSIONS INTO THE AUDIT OPINION

Based on the conclusion as per section 10 for audit objective 1, section 15 for audit objective 2, section 16 for audit objective 3 and section 18 for audit objective 4, the CB concludes on the following elements of the Opinion:

I. Based on section 9 – audit objective 1: – on the completeness, accuracy and veracity of annual accounts.

II. Based on section 15 – audit objective 2: – on the proper functioning of the Member States' governance systems, in particular:

(i) the governance bodies referred to in Articles 9 and 10 of Regulation (EU) 2021/2116 and Article 123 of Regulation (EU) 2021/2115,

(ii) the basic Union requirements referred to in Article 2(c) of Regulation (EU) 2021/2116,

(iii) the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115

III. Based on section 16 – audit objective 3: on the correctness of the performance reporting, as regards:

(i) output indicators for the purposes of the annual performance clearance referred to in Article 54, and

(ii) result indicators for the multiannual performance monitoring referred to in Article 128 of Regulation (EU) 2021/2115

IV. Based on section 18 – audit objective 4: on legality and regularity of expenditure for which reimbursement has been requested from the Commission.

The CBs' opinion should also state whether the examination puts in doubt the assertions made in the management declaration. The audit work in this respect should take into consideration the audit results under all 4 audit objectives.

As regards the proper functioning of the Member State's governance system, the main sources for the audit opinion are the results under the testing of audit objectives 2 and 3, taking into account that the opinion on the reporting system put in place for the purposes of the annual performance report referred to in Article 134 of Regulation (EU) 2021/2115 derives partially from the work under audit objective 3. For the audit of FY2023 the CB's audit work should focus on audit objective 4 as most of the expenditure effected in that year falls under the scope of that audit objective. However, in case there is expenditure under the CAP Strategic Plan is executed, the CB should also perform the relevant work for audit objectives 2 and 3.

It should be noted that the Member State's governance system includes the PA's internal control system. Thus, when assessing the Member State's governance system, the results of the Certification Body's work for audit objective 1 should be taken into consideration too. Furthermore, under certain circumstances, the Certification Body's results under audit objective 4 can be also used for the opinion under audit objective 2 and vice versa. For

example, the results of transactions approved before 1st of January 2023 and processed within the financial year (i.e. "old" expenditure under audit objective 4) may be used also for audit objective 2 under the condition that the control system remains stable and the regulatory framework does not significantly change. Similarly, the results of the Certification Body's testing of the horizontal Basic Union requirements under audit objective 2 can be used, under certain occasions, also for the opinion on the PA's internal control system for the purposes of audit objective 4 (i.e. expenditure outside the CAP Strategic Plan). For example, the results of the ISAP and AMS requirements under audit objective 2 can also be used for the assessment of the internal control system of the crop-specific payment for cotton.

For further details as regards the compilation and use of the audit opinion refer to Annex 4 of this Guideline and Guideline 3 for FY2023.

3.5