COMMUNICATION FROM THE COMMISSION

Modernisation of the Accounting System of the European Communities
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INTRODUCTION

Need for action

The Commission has accomplished major improvements of its financial management and control systems since the adoption of the White Paper on Reform in March 2000. Further efforts are still necessary to achieve Reform's objectives, in particular in the area of accounting where the recast Financial Regulation requires the production of accrual accounts by 2005. This objective, in turn, commits the Commission to undertake a major change to its information systems, as well as necessitating the development of an integrated computerised system to provide the additional functionality required. The Commission acknowledges that there are considerable challenges involved in undertaking a project of such magnitude and complexity and therefore managing these challenges will be an integral part of the process.

Proper forward planning is fundamental to successful project management. This Communication provides the basis for establishing a clear and agreed understanding of the goals and objectives and where possible how the project will deliver them, the outcomes, outputs and timescales, the elements for project management and the reporting lines.

The Court of Auditors, in its Annual Report concerning the financial year 2001, considered that, despite the fact that the accounts reflected faithfully the revenue and the expenditure as well as the financial situation of the Communities, "urgent in-depth action in the Commission’s services to cope with the risks arising from the shortcomings in the accounting system is required (see paragraph 9.6 – 9.8)". It is important to note that criticisms of the Court relate basically to the general accountancy and only to a lesser extent to the budget accounting.

For its part, the Commission has committed itself to improve and modernise the Community accounting system. Thus, in its reply to points 9.7-9.8, the Commission "recognises the accounting problems still present as highlighted by the Court. A reform of accounting will be launched as a matter of urgency. The Commission is strongly committed to the modernisation of the accounting system. By the end of 2002 the Commission will take a decision on the options for development, the proposed calendar for implementation and the projected costs and allocation of resources. Furthermore, given that the new Financial Regulation requires the production of accrual accounts by 2005; urgent and wide-ranging action is necessary to ensure that the Commission has the necessary rules and procedures in place."

The legal framework

The Commission obligations on accounting rise directly from the EC Treaty. Article 275 lays down: "The Commission shall submit annually to the Council and to the European Parliament the accounts of the preceding financial year relating to the implementation of the budget. The Commission shall also forward to them a financial statement of the assets and liabilities of the Community." These provisions are of particular importance because, in the context of the Discharge procedure, Article 276, the Council and the European Parliament shall examine the accounts, the financial statements referred to in Article 275 and the annual report by the Court of Auditors.
The basis for the new accounting system has been established in Article 125 of the new Financial Regulation: “In accordance with the principle of accrual-based accounting, the financial statements shall show the charges and income for the financial year, regardless of the date of payment or collection”. According to Article 181, “These provisions … shall apply gradually … in order to be fully effective for the budgetary year 2005”.

Changes in international public accounting

As most of the other accounting systems in the public sector, the Community system was not designed to comply with accrual accounting principles. However, with the new rules, the Commission will join the group of governments and public institutions which have undertaken important efforts in order to improve their accounting practices.

In recent years, the modernisation of public management has become a major concern. Public accounting practices, most often oriented towards recording payments and receipts, must, on the one hand, become a genuine management tool and on the other hand make the government’s or public organisation’s financial situation more readily understandable and reliable.

The Commission is not alone in moving towards the respect of generally accepted accrual accounting principles. Many developed countries are also engaged in the same process and, encouraged by international bodies and organisations such as the OECD and IFAC1, have begun to modernise their accounting systems over the past few years, switching from a cash-based to an accrual-based system.

Experience in the Member States shows that reforming public accounting systems represents a major upheaval both in terms of the introduction of new practices and in human terms, not to mention the financial resources required.

Changes in the accounting framework within the European Communities

The Commission, too, has felt the need to swing into line with this international accounting reform and some years ago decided to develop its accounting system from a mere record of budgetary expenditure and revenue operations (cash-based accounting) into an accrual accounting system with the objective of providing a fuller picture of the Communities’ financial situation, showing all its assets and liabilities as well as the expenditure and revenue for the financial year.

The Commission launched a multi-annual plan in 2000 for the modernisation of its accounting framework, which comprised:

– a study on the establishment and presentation of the accounts of the EU delivered in mid-2000 by high-level experts on public accounting;

– drawing up in June 2001, an action plan for modernisation, which was discussed with the Court of Auditors. The Court has welcomed the document orientations;

– introducing elements of accrual accounting in the presentation of the financial statements and calculating the economic out-turn since 2000, which “represents

1 IFAC: International Federation of Accountants
a step forward, which is in line with the general trend observed in the public sector at international level\textsuperscript{2}, and adopting an accounting and consolidation manual for all the Institutions;

– analysing several Member States’ experience (United Kingdom, France, Sweden, Spain, Netherlands);

– adopting the new Financial Regulation, including the introduction of new accrual based accounting principles;

– on 24 July 2002 the Member of the Commission responsible for the budget presented a memorandum (SEC(2002)853) to the Commission describing the wide-ranging work to modernise the accounting framework and information system.

**The current information system**

The architecture of the Commission’s central financial management and accounting system is complex and comprises three different systems which are inter-linked and are also linked with the sectorial systems of the spending services which exist primarily to meet sectorial management needs. The system does not meet the requirements of the new Financial Regulation as it was not designed to include accrual accounting data which are essential from the 2005 financial year under the new provisions.

It has to be stressed that first the accounting rules need to be defined and then the information system will be designed accordingly.

**Purpose of this communication**

The steps set out in the memorandum of 24 July 2002 constitute the building blocks for moving from a system based on cash accounts towards an integrated accrual-based accounting system, required by the Financial Regulation for the financial year 2005.

The Commission is aware that further analysis and evaluation will still need to be carried out as part of the normal project management process.

The purpose of this communication is twofold:

– to adopt a detailed proposal to allow the Commission to decide on the accounting framework, in particular on how generally-accepted accrual accounting principles can be implemented;

– to set out the action to be taken as regards project organisation, resources and the timing of the work to develop an integrated computerised system. The system options are appraised in detail, identifying a preferred solution.

\textsuperscript{2} Court of Auditors - Annual report concerning the financial year 2000 (2001/C 359/01)- 9.36
The aim is to embark on detailed development of both the accounting framework and the information system in the beginning of 2003, with the relevant testing and implementation phases getting under way from 2004.
I. PART I: THE ACCOUNTING FRAMEWORK

I.1. Current Situation

The Commission’s accounts are kept in accordance with the Financial Regulation of 21 December 1977.\(^3\)

The accounts comprise the budget accounts and the general accounts. The budget accounts give a detailed picture of implementation of the annual budget. They are based on a modified form of cash accounting (carryovers are included). The budget out-turn for the year is calculated on the basis of amounts actually disbursed and collected (including carryovers).

Several elements of accrual accounting have already been introduced by the Commission for the presentation of the financial statements via annual adjustments. These mainly relate to fixed assets (acquisitions, disposals, withdrawals), stocks, debts, loans, shareholdings, depreciations, provisions and write-downs. They allow the economic out-turn to be calculated.

The economic result aims to make the link between the budgetary cash-based accounts and the general accounts, which are moving towards accrual accounting. It reveals the impact on the balance sheet of expenditure and revenue not originating from budgetary accounting.

However, all the information used to make a balance sheet on accrual basis is not based directly on the accounting entries but comes from extra accounting information, based on provisions of the Accounting and Consolidation Manual, and transmitted to DG Budget by the other DGs of the Commission. In order to assure completeness and reliability, the collection of all this information at source, within the DGs, is a priority.

In its most recent annual reports, the Court of Auditors has stressed the efforts made by the Commission to improve its accounting system, but has also urged it to make further progress and adopt an integrated accounting framework, in line with international accounting standards.

I.2. Evolution Needed

The main objective of the Commission’s new accounting framework and system will be to produce financial information that is useful to interested parties, and to dispose of better management tools.

The principal users of the European Communities’ accounting reports are:

– **Internal users:** Senior managers and authorising services need access to detailed internal financial reports as a tool for decision making and to improve the management of projects and to perform internal controls.

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\( ^3 \) Together with the Rules of Implementation, the Regulation on Non-Financial Fixed Assets and the Accounting and Consolidation Manual.
External users: the European Parliament, the Council, the Court of Auditors, the public and other users, such as governments, rating agencies, economic, political and financial analysts, including the media.

Taken as a collective group, users expect that financial reporting should demonstrate the accountability of the European Communities for the financial affairs and resources entrusted to it, and provide them with information useful for economic decision making.

The quality of the information provided in financial reports determines the usefulness of those reports to users. Basic requirements are: understandability, relevance, materiality, reliability, faithful representation, substance over form, neutrality, prudence, completeness, comparability and timeliness.

Cash accounting provides information, which meets some of the objectives of financial reporting. However, it is not the most informative way of presenting financial information. With cash accounting there is no requirement to match expenditure with revenue for the period to which they relate, and capital spending is booked in total in the year in which the capital purchase or disposal is made. Cash based accounts also lack any framework for accounting for assets and liabilities.

The accrual basis\(^4\) should provide users with financial information about such matters as the resources controlled by the entity, the cost of its operations (cost of providing goods and services), enhanced cash flow information and other financial information useful both in assessing the financial position and changes in it, and in assessing whether the reporting entity is operating economically and efficiently. Users may use financial reports to assess the Commission’s stewardship of resources, compliance with legislation, and the EC’s financial position.

Accrual accounting requires organisations to maintain complete records of assets and liabilities as well as identifying and recording any off-balance sheet transactions. To enable the Commission to fulfil the obligations under accrual accounting principles and standards it will be necessary to identify all appropriate assets and liabilities, which should be recorded as part of the balance sheet.

To achieve these objectives of providing reliable financial information, the accounting framework will change on several fronts. These changes will involve:

- adopting generally accepted accrual based accounting principles;
- developing an integrated accounting system containing all the information necessary for presenting the accrual accounts (see part II of this Communication);
- developing a general accounting system based on accrual accounting and maintenance of cash-based budget accounting;

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\(^4\) **Accrual basis** means a basis of accounting under which transactions and other events are recognised when they occur (and not only when cash or its equivalent is received or paid). Therefore, transactions and events are recorded in the accounting records and recognised in the financial statements of the periods to which they relate. The elements recognised under accrual accounting are assets, liabilities, revenue and expenses” (IPSAS 1)
– adopting accounting methods and valuation rules that flesh out the accounting principles adopted;

– improving the financial statements so that they give an accurate picture of the financial situation in terms of assets and liabilities, budget implementation, the out-turn and the cash flow;

– extending the scope of consolidation.

I.3. Situation in the Member States

Traditionally, public sector accounting has been cash based. No change was contemplated until recently when the demands of good governance and the New Public Management (NPM) postulates have spread throughout the OECD countries.

This new movement has led to a broad range of changes, such as replacement of input control by result control, performance measurement, devolution, outsourcing, empowerment of employees and accrual accounting. This approach is being supported by international bodies such as the International Federation of Accountants (IFAC), the World Bank and OECD.

In this context, several EU member states have started to produce their financial reports on an accrual basis. Nevertheless they are proceeding unevenly and there are still many governments, such as Germany or Denmark, which are presenting their financial statements on a cash basis. Most Member States are not presenting consolidated financial statements for the whole of the government. Even the UK, one of the most advanced countries, only adopted the accrual basis of accounting in the 2000/2001 fiscal year; it will not present consolidated statements until 2005/2006.

There is also a diversity of transition paths towards the accrual basis. Some governments, such as the UK, the Netherlands and Sweden, have moved first to accruals in financial statements and then, in a second stage, have based their budgets on the same principle. Others, such as France and Spain, have decided to adopt this basis just for the financial statements, keeping the budget on a cash basis.

According to an IFAC survey\(^5\), the periods over which reform occur differ from jurisdiction to jurisdiction and depend on the resources available and the extent of political commitment. Reform periods may be short (one to three years), medium (four to six years) or long (over six years). In the UK, for instance, where resources and strong political commitment existed, it took 6 years to adopt full accruals for the majority of the UK government accounts. According to the UK National Audit Office report of March 2002, there are still problems for some accounts.

A 2002 OECD survey\(^6\) conducted by its Public Management Committee revealed that only 3 EU Member States present all their Government financial statements using the full accrual basis of accounting. When Departmental / Agency level financial statements are

\(^5\) IFAC Public Sector Committee Study 14 April 2002

considered, 3 additional member states are added. Therefore, only 6 out of 15 Member States are using full accruals at some level.

I.4. Future System

The choices realised for the future system are the application of a dual system and the use of IPSAS accounting standards.

I.4.1. Dual system

There are two main options when making the transition to accrual accounting:

– either the principle of accrual-based accounts is applied for both the budget and general accounts, in which the budgetary balance will correspond to the difference between the budgetary entitlements established in the course of the financial year and the obligations established in the course of that year, irrespective of what may be disbursed or collected. This is not the structure laid down in the Financial Regulation.

– or the accrual principle is applied to the general accounts only, while budget implementation remains subject to the cash principle, in which case a “

The new Financial Regulation lays down an accounting framework based on such a “dual” system. The dual system requires budget implementation to be based on different principles (budget consumption occurring at the time of disbursement or collection) than the general accounts (based on accrual principles).

This system requires:

– definition of the moment when an accounting event must be recognised in the various financial reports;

– reconciliations between budget implementation and out-turn;

– comparison between the financial reports drawn up according to the accrual principle and those based on cash-flow accounting.

I.4.2. Use of existing standards : IPSAS

The new Financial Regulation specifies in Article 133 that the Commission's Accounting Officer, when adopting the accounting rules and methods, shall be guided by the internationally accepted accounting standards for the public sector but may depart from them where justified by the specific nature of the Communities' activities.

The Commission’s Accounting Officer intends consequently to prepare and publish the financial statements in accordance with International Public Sector Accounting Standards (IPSAS - see annex A), derived from International Accounting Standards (IAS)\(^7\) and

\(^7\) IAS are issued by the International Accounting Standards Board (IASB). IASB is an independent, privately-funded accounting standard setter, committed to developing, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require
issued by the Public Sector Committee (PSC) of the International Federation of Accountants (IFAC - an organisation of national professional accountancy organisations, with member bodies in 114 countries, representing 2 million accountants).

The PSC is the standing committee formed to address, on a co-ordinated worldwide basis, the needs of those involved in public sector financial reporting, accounting and auditing, in order to develop a core set of accounting standards for the public sector. IPSAS are considered central to initiatives directed at strengthening the transparency and accountability of governments. Agencies and public sector entities have been strongly encouraged by the PSC to adopt IPSAS and actively participate in their development process, within a vast world-wide process for convergence and harmonisation.

The importance of the IAS has been recognised by the Regulation (EC) No1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards. This Regulation requires EU listed companies to prepare their consolidated accounts in accordance with IAS from 2005 onwards.

However, the Commission recognises that IPSAS standards will need to be adapted and supplemented in some respects to obtain a framework of accounting principles appropriate to the European Communities. The accounting events not still covered by IPSAS will be disclosed following the IAS.

I.5. Actions to be taken

I.5.1. Devising the new accounting framework

1.5.1.1. Establishing the accounting standards to be applied by the European Communities

The IPSAS set out the requirements for accounting and financial reporting by governments and other public sector organisations. However, not all IPSAS are applicable to the specific situation of the Communities. Presently, there are 20 IPSAS\(^8\) issued, and two others are expected to be published shortly, already covering a wide range of accounting and financial reporting issues. The first IPSAS was adopted in May 2000, the last one in October 2002.

Both IPSAS and IAS refer often to very technical terms and concepts. They will not be an “accounting manual” with rules and explanation applicable to every particular accounting transaction or event of a DG, but a source of general guidance and a conceptual framework.

On the basis of the standards, accounting policies to be followed for each kind of transaction will be developed. It will be necessary:

- to identify those responsible (the Accounting Officer’s services with consultation of the other Institutions and agencies) for developing and reviewing the policies prior to

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\(^8\) IPSAS standards in Annex
The standard setting committee (point I.5.1.2.) has an important role in this matter;

- to establish time frames for development and approval;
- to identify the authoritative accounting standards. Where there is no IPSAS on a particular topic, other sources must be identified;
- to develop a full set of accounting policies for internal use as follows:
  - to identify the transactions and balances for which accounting policies will be required both for the consolidating and the consolidated entities;
  - to determine the level of guidance that will be required on the policies. Minimal guidance is appropriate when employees are familiar with accrual accounting and the standards applied. Detailed guidance includes a summary of the key requirements of an accounting standard and examples of the application of that standard to particular transactions;
  - to review the existing accounting policies to determine if they will be appropriate under the new basis of accounting;
  - to apply the relevant accounting standards or other sources of authoritative guidance for specific accounting transactions and events.
- to develop guidance and education on the application of policies

**Implications for DGs**

The accountant's services will identify and will write the standards to be established.

The DGs will have to familiarise themselves fully with the accounting standards to ensure they are properly applied.

I.5.1.2. Setting up an Accounting Standards Committee

The Financial Regulation of 25 June 2002 sets out the accounting principles that serve as the basis for drawing up the financial statements. However, the principles need to be fleshed out in accounting standards and rules applicable to the activities of the European Communities. In this connection, Article 133 of the Financial Regulation states that the Commission’s Accounting Officer is adopting the accounting rules and methods and the harmonised chart of accounts to be applied by all the institutions.

It would be inappropriate for those responsible for preparing financial statements to have the sole responsibility for deciding on the standards such statements should follow. The Accounting Officer should have a major role in the development of accounting standards. However, other users of the accounts, should also play a part in the setting of these requirements.

To this end, an advisory committee for accounting standards will be set up. Its tasks will be:
to deliver an independent professional judgement on the accounting standards and rules proposed by the Commission’s Accounting Officer;

to advise the Accounting Officer on the application of financial reporting principles and standards.

The committee will play an important role in defining and harmonising accounting standards and rules as well as in defining the conceptual accounting framework. The Commission’s Accounting Officer will adopt the accounting standards and rules after consulting the Accounting Officers of the other institutions and bodies and the Committee.

This advisory committee would comprise at the very least the following representatives:

- the Commission's Accounting Officer;
- the Accounting Officer of one other institution;
- the Accounting Officer of one agency within the scope of consolidation9;
- a representative of the Central Financial Service, expert in financial regulations and trained in accountancy;
- a representative of Unit DG MARKT/F3 “Financial reporting and company law”;
- a representative of the Internal Audit Service;
- two external persons who are recognised experts in public accounting.

The Legal Service can be consulted for advice. The network of responsible accounting people within the DGs is consulted before presenting the standards to the committee for approval.

It will be proposed to the Court of Auditors that it participates in this Committee because, although it is essential that auditors maintain their independence, there are many benefits to be obtained from establishing a co-operative working relationship with the auditor at the beginning of the transition process. An auditor would be unlikely to give an absolute assurance that a particular system or process would meet audit requirements. However, the auditor may be able to provide helpful advice regarding the criteria that would be used in assessing the system or process10.

I.5.1.3. Adapting the chart of accounts

A chart of accounts is a systematic coding system for the classification and coding of transactions and events within the accounting system.

10 IFAC Study 14 chapter 2, point 2.30
The chart of accounts will be analysed to determine what adjustments are necessary to accommodate all the accounting events and so reflect all the new items in terms of assets and liabilities, costs and revenue and contingencies.
The new central chart of accounts will have to:

– meet the needs of both individual and central entities;
– provide a uniform coding structure for coding financial transactions;
– permit flexibility for individual entities to adapt it to their particular requirements;
– contain all the necessary elements to calculate the economic result.

**Implications for DGs**

The different accounting events identified within operational DGs will determine the adaptation of the structure of the chart of accounts.

The Accounting Officer will adopt the new chart of accounts applicable for all DGs, institutions and agencies.

I.5.1.4. Defining the event giving rise

The event giving rise is the key element in the transition to accrual accounting.

Transactions must be recognised when they occur and not merely when a sum of money is received or paid. In the accounting records, accounting events are entered against the financial year to which they relate. Items recognised in this way in the accounts constitute assets and liabilities, costs and income, and contingent assets and liabilities.

In terms of the volume of transactions, it is expenditure where recognition of the event giving rise and hence its definition are especially important. The aim is to harmonise the relevant rules.

An initial analysis has shown different practices within the public sector. However, there are common strands. These common strands are that transfers should be authorised, eligibility criteria met and that it should be possible to estimate amounts reasonably.

The replies to the questionnaire sent to DGs (see point I.5.2.1) will make it easier to define the event giving rise. Initial talks between accounting departments and authorising services have shown that the interpretation of the standards varies considerably depending on the department concerned, area of activity and type of management (direct or shared).

Summarised, the event giving rise for the registration of receivables and revenues and for debts and charges will be defined.

The link between the event giving rise for expenditure and the accounts is discussed further in point I.5.2.5: “Creating a link between the Central Invoice Register and the accounts”.

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Implications for DGs

If the scope of the concept deserves particular emphasis in connection with expenditure, for the DG Budget, in collaboration with the other DGs, it involves adopting the content of the standards for all the accounting items that constitute assets, liabilities, costs and income as well as contingent assets and liabilities.

Besides defining the concept, the DGs will in future have to input all the data required into the central accounting system, either directly or via their local systems, when the various events giving rise are constituted.

1.5.1.5. Extending the scope of consolidation

The scope of consolidation is defined as all the companies or bodies included in the group to be consolidated.

Consolidation is the process of presenting the financial statements of all entities that make up the reporting entity as if they were the financial statements of a single entity. It involves adding together all items on a line-by-line basis and eliminating any transactions or balances between members of the reporting entities. The entities need to conform to the standard policies and classifications when providing financial information for consolidation. The consolidated statements currently comprise the accounts of the European Parliament, the Ombudsman, the Council, the Commission, the Court of Justice, the Court of Auditors, the Economic and Social Committee and the Committee of the Regions. The criterion used to define the scope of consolidation is basically that of the single budget, with the expenditure and revenue of the above-mentioned institutions contained in one budget, that of the European Union. The current definition of the scope of consolidation does not comply with international standards. Agencies have been set up to carry out some of the tasks entrusted to the EU’s activities. They are financed in full or in part by Community general budget. It is therefore logical to say that it is the European Union, which benefits from their activities and that these agencies ought to be consolidated, as stated in Article 121 of the new Financial Regulation which stipulates that the consolidated accounts shall comprise the financial statements of the institutions and of the agencies.

In addition, article 185 indicates that the Commission shall adopt a framework financial regulation for the agencies set up by the Communities, and having legal personality, that actually receive grants charged to the budget. The bodies referred to shall apply the same accounting rules in order to consolidate their accounts with the Commission’s accounts.

Implications for DG Budget, for the institutions and for the agencies

All the institutions and agencies must apply the accounting rules and methods laid down by the Commission’s Accounting Officer. A discussion forum with the Agencies has been created, on the same basis as the existing meetings of the Accounting Officers of the Commission and the other institutions. It should be ensured that the rules for drawing up and presenting these bodies’ financial statements are similar to those applied by the consolidating institution.
For the Commission and particularly for DG Budget, this means a major effort to explain, obtain support for and harmonise the new accounting framework, standards and rules. Agreement is a basic requirement for success.

Most of the additional work in setting up the accounting procedures and consolidating the accounts will fall on DG Budget.

The work to be undertaken by the other Institutions and Agencies although similar to that of the Commission, will be on a smaller scale.

I.5.1.6. Financial statements

The financial statements are an important element in the accounting system. Their purpose is to present a faithful picture of the financial situation in terms of assets and liabilities, budget implementation, the entity’s results and the annual cash flow.

To meet these objectives, and with the aim of bringing the statements into line with the IFAC recommendations, the annual accounts of the European Communities will comprise the following:

1. Budgetary Out-turn Account
2. Balance Sheet
3. Economic Out-turn Account (new)
4. Cash-flow Table
5. Statement of Changes in Capital (new)
6. Explanatory Notes

I.5.2. Integrating accounting data

I.5.2.1. Analysing accounting events and fixing the opening balances

At present, extra-accounting information kept in accordance with the provisions of the Accounting and Consolidation Manual is sent to the central accounting department at the end of the year for the presentation of the accounts.

To obtain a complete list of all accounting events (both on and off the balance sheet) for the entire Commission, DG Budget sent a questionnaire to the other DGs on 17 September 2002 to identify the different transactions liable to have an impact on the accounts. On the basis of the survey, a list of all assets, liabilities and off-balance sheet items will be drawn up. Using the information supplied by services will allow the data to be incorporated in the accounts.

This information-gathering exercise is the first step towards establishing the opening balance. This is a major prerequisite for integrating accounting movements relating to assets. The fixing of the opening balances will require a complete accounting closure.
Implications for DGs

Producing a concrete opening balance will entail a considerable amount of work for DGs since the internal control procedures - put in place in each DG - will have to guarantee the accuracy and completeness of the data.

Before recording the DGs’ various accounting movements in accordance with the principles of the new integrated accounting system, the accounts will have to be ruled off, as happens at the end-of-year closure on 31 December in order to integrate the opening balances in the accounts.

I.5.2.2. Linking the general accounts and the budget accounts via "object codes"

To obtain a new integrated accounting framework, a new coding will be assigned to budgetary transactions so that information can be transferred directly to the general accounts. This will be achieved through “object codes”, which will be linked to budget lines, making it possible to enter revenue and expenditure in the accounts correctly and automatically.

This transfer of information from the budget accounts to the general accounts will substantially reduce the need for extra-accounting information and for reclassification and adjustments of accounting entries.

A classification of budget expenditure and revenue will have to be created

For expenditure, this will be based on various criteria, organic (who does the spending?), economic (what is it spent on?) and functional (what is it spent for?). Revenue will also have to be classified on the basis of economic and organic criteria. The economic classification is a new element, the organic and functional classifications are already available.

The economic classification of expenditure and revenue will distinguish current expenditure and revenue from capital expenditure and revenue. This classification will allow there to be a clearer link between the budget accounts and the general accounts, since current expenditure and revenue will be linked to charges and income for the year, while capital expenditure will be linked to the balance sheet headings.

The organic classification (who does the spending?) allows budget resources to be allocated to authorising officers and enables DGs to draw up their annual activity reports (reform action 82). The level of detail in the organic classification could, however, be refined in the longer term.

The functional classification (what is the spending for?) will make it possible to evaluate the level of economy, efficiency and effectiveness in achieving the institution’s objectives. The budget structure based on ABB (Activity Based Budgeting) could be used for functional classification.

Implications for DGs

DG Budget will have to draw up the chart of "object codes" and then the other DGs will have to implement it into the system. Managing officials and authorising officers will have to assign and check the coding of all transactions.
I.5.2.3. Integrating contingent assets and liabilities (off-balance sheet items)

A “contingent asset or liability” is a possible asset or liability whose existence will be confirmed only by the occurrence of an uncertain future event not wholly within the entity’s control\textsuperscript{11}.

These items must be entered in the accounts and the financial statements, besides those relating to the balance sheet and the out-turn account.

At present, most of the data concerning contingent assets and liabilities are supplied by DGs at the end of the year for the closure of the accounts and are entered under the heading “off-balance sheet commitments”.

Bank guarantees (received or possibly given) deserve special mention because they raise particular problems. Besides the problem of recording them, there is the question of monitoring. A computerised system should make it possible to apply effective management in this respect, providing the link with current contracts, handling the call-in of guarantees and their removal from the accounts on expiry or cancellation.

The action required under this heading involves:

– analysis of the contingent assets and liabilities to be included in accordance with international accounting standards,

– recording of these transactions in the accounting system by authorising services, either directly or via their local systems, using “off-balance sheet accounts”;

– adapting the system and accounting framework to accommodate these entries, for which no budget line exists. The new accounting class “0” will be assigned to these “off-balance sheet accounts”.

\textit{Implications for DGs}

DGs will in future be responsible for identifying, managing, and regularly entering contingent assets and liabilities into the accounting system.

Management of bank guarantees will entail regular extra work but will make it possible to use this procedure more systematically for recovering pre-financing.

I.5.2.4. Management and entry in the accounts of pre-financing, interim payments and final payments

In the course of their activities the European Communities grant pre-financing to third parties. Pre-financing is meant to provide recipients with cash funds. They have to be cleared either through interim payments, final-balance payments, or through a recovery order\textsuperscript{12}.

\begin{footnotesize}
\begin{itemize}
\item[11] The full definition is given in IAS 37.
\end{itemize}
\end{footnotesize}
To ensure the sound management of the funds granted in this way and to obtain a clear and full picture of the situation in terms of the accounts, the data must be incorporated into the computerised accounting system. It should also be pointed out that all pre-financing granted will have to be cleared in the budget accounts. When adopting the accounting standards, the Accounting Officer will determine pre-financing that has to be included on the assets side of the balance sheet.

A link will have to be provided between the expenditure and the revenue environment when pre-financing is cleared by recovery.

To obtain a full picture of the situation regarding pre-financing, new contracts will have to include a provision obliging the contractor to send the Commission periodic reports on the use made of pre-financing. The aim is to be able to determine changes in pre-financing from the accounts.

**Implications for DGs**

To ensure pre-financing is entered correctly and cleared in the accounts, each interim payment and/or final-balance payment will have to indicate what portion of the pre-financing is being cleared.

A detailed procedure for clearing pre-financing will be drawn up by DG Budget and will be brought into operation as soon as possible. However, DGs will have until 1 January 2005 at the latest to draw up the opening inventory of all current pre-financing. This will allow the accounts to show a complete picture of the position as regards pre-financing for 2005.

**I.5.2.5. Creating a link between the Central Invoice Register and the accounts**

A Central Invoice Register has been developed under the present system. Each payment order is generated from the invoice entered. This facility, which makes it easier to monitor payment deadlines, will play an important part in the transition to accrual accounting for charges and debts.

The Central Invoice Register will have to be integrated with the general accounts in order to record debts in the accounts as soon as they are incurred.

It should be noted that the term “invoice” is used in the Commission’s context in a broader sense than simply invoices received from third parties. It refers to any request for payment ultimately giving rise to disbursement of funds.

As a general rule, all expenditure must be recorded in the Central Invoice Register. No payment will be authorised unless the payment request has already been recorded. Exceptions to the rule will be defined for specific cases, such as staff salaries\(^{13}\).

Recording payment requests in the Central Invoice Register will allow there to be full information available concerning the total amount of debts owed to third parties and

\(^{13}\) The feasibility of the use of the Central Invoice Register for payments made by delegations has to be examined.
make it possible for charges recorded in the general accounts (when the event giving rise occurs) to be reconciled with budget expenditure effected (when payments are made).

The balance of supplier accounts will include unsettled payment requests.

Further, it should be noted in this connection that the current “third-party file” based on bank accounts will have to be transformed into a “supplier file” based on legal entities (see point I.5.2.6).

**Implications for DGs**

The general rule is that an official payment request must always be sent to the Commission and use of the Central Invoice Register is compulsory.

Rules will have to be laid down as regards what constitutes the equivalent of a “payment request” in specific areas still to be determined.

DGs will have to ensure that data entered in the invoice register tallies exactly with the supporting documents. They can input the data either directly into the Central Invoice Register or via an interface with their local systems.

DG Budget will develop the link between the Central Invoice Register and the accounts. It will provide DGs with the tools needed to reconcile budget implementation (cash based) and the general accounts (accrual based) and to determine outstanding amounts payable to each supplier.

Use of the Central Invoice Register for expenditure will be made compulsory, except in certain special cases where there is very little time gap between the event giving rise for the expenditure and payment of the debt.

I.5.2.6. Receivables and files of clients and suppliers

Any amount receivable that is identified as being certain, of a fixed amount and due must be established and accounted for. Currently, this accounting entry is made via the recovery orders (RO).

Henceforth, it will be necessary to distinguish the various types of receivables and the third parties concerned.

A critical analysis is necessary since the current accounting system leads to duplicate entries, which have to be eliminated at the time of the closure of the accounts.

The accounting for amounts receivable will be analysed. Various types of RO will be identified, according to whether they involve a claim concerning own resources, a claim concerning a fine within the framework of the free competition, the recovery of an amount from a third party (for example members of staff), or a claim which concerns the refunding of an asset (for example in the case of the granting of loans).

It will also be necessary to distinguish the type of customer. It could be a true "customer" who pays money to the Commission (as in the case of the fines), or a "supplier", to whom the Commission paid an amount for the implementation of a programme, and who has to transfer excess funds back to the Commission.
The treatment of these various types of third parties will be analysed. One or more files will contain the suppliers and the customers. Within this framework, third parties will be identified by legal entity. Currently, the third party file is based upon the bank accounts of the partners.

**Implications for DGs**

The DGs will have to identify the type of receivables and the type of third party involved at the time of the introduction of a recovery order.

The current third party file will have to be adapted in order to include the legal partners of the Commission. The current contractors data base (Icon-DB) will also have to be adapted accordingly to avoid duplication of data.

I.5.3. **Organisation of internal control of accounting data**

I.5.3.1. Expanding internal control in each DG to include accounting aspects

An essential means for assuring the reliability of the financial information is the integration of the accounting transactions into the internal control framework. In the context of reform, internal control is defined broadly, as the globality of policies and procedures conceived and put in place by the organisation’s management to ensure notably the safeguarding of assets and information, the quality of accounting records and the timely production of reliable financial and management information.

This quality of accounting records is not only related to the yearly-consolidated accounts but also to the yearly Declaration and Annual Activity Report. Hereby, Directors General and Heads of Services have to express their reasonable assurance that resources have been used for the intended purposes and in accordance with the principles of sound financial management (effectiveness, efficiency, economy) and that the internal control systems guarantee the legality and regularity of the underlying transactions.

The list of non-exhaustive actions to include the accounting dimension in this context will concern:

- the process handbook developed by the Central Financial Service, related to accounting and financial reporting will have to integrate the issues related to the modernisation of the accounting framework into these risks and related controls mitigating them;
- the charts of the Authorising Officer by delegation and by sub-delegation will have to be adapted in order to cope with the modernised accounting framework;
- the future system must guarantee maximum quality of data introduced in the system and thus reinforce the internal control;
- the exercise of self-assessment in the context of internal control and risk assessment will have to incorporate these modified guidelines, process handbooks and all related procedures;
- the ex ante controls carried out by the DGs will have to incorporate the context renewed by the modernisation of the accountancy framework.
I.5.3.2. Supporting evidence for balance sheet balances through inventories

With regard to internal controls to ensure the reliability of accounting information, it is very important that the accounting balances of all accounts should be supported by inventories.

It is generally accepted in the accounting profession that every entity must, at least once a year, conduct a faithful and prudent exercise of listing, checking, examining and valuation in order to establish, at the selected date, a **complete** inventory of all its assets and entitlements of whatever nature, of the debts, obligations and commitments of any kind relating to its activities and of its own resources allocated to cover them. The inventory should not, therefore, be confined solely to physical stocks and tangible fixed assets.

Together with the journal and the general ledger, the stock ledger is one of the accounting books required under the accounting directives and national accounting legislation.

The stock ledger comprises the inventories and the valuation rules. Inventory operations involve two aspects;

- physical: establishing the existence of assets and liabilities; and

- qualitative: the value to be assigned to the various items, depreciation or value adjustments to be recorded, provisions to be constituted, etc.

The information concerning the institution’s assets and liabilities is generally presented in three distinct dimensions: reality, the management database and the accounts.

- **reality**: physical goods and the titles of ownership, contracts and agreements, titles of ownership, Commission decisions, Court judgements, etc.

- **the database**: must contain all the information required for management and accounting purposes, such as dates, inventory numbers, suppliers, descriptions, supporting document, order slips, etc.

- **the accounts**: record day-by-day transactions and the account balances.

A concrete example is given in Annexe B.

The approach required when performing the inventory involves reconciling these three dimensions. An effective inventory is one which periodically compares transactions in the three dimensions indicated and which will serve as the basis for recording adjustments to correct any discrepancies found\textsuperscript{14}.

\textsuperscript{14} The implementing rules of the new Financial Regulation foresee a three-year verification programme to perform the inventory checks. \textit{Article 222 – Inventory checks} – (\textit{Article 138 of the Financial Regulation}) : Inventory checks carried out by the institutions shall be performed in such a way as to ensure that each item physically exists and matches the relevant entry in the inventory. Such checks shall be carried out under a three-year verification programme.
At present, neither authorising services nor the accounting services have access to all three dimensions at the same time. Authorising services only have access to “reality” and the management database (accounting valuations are rarely recorded in the databases). The accounting services only have access to the balances and transactions in the general ledger and the journal and are sometimes obliged to enter data in the accounts on the basis of non-accounting information from the management inventories. Sharing and checking data are key factors for ensuring reliable account balances.

**Implications for DGs**

The basis for laying down valuation rules for the different assets and liabilities is described in point I.5.1.1.: “Establishing the accounting standards to be applied by the European Communities”. DG Budget shall establish a minimum standard internal control for performing inventories: documents to be drawn up, authorised persons, double counting, halting stock entries and exits during the inventory, etc.

Authorising services will require access to the general ledger in order to check, at any time, the balances and transactions linked to the property under their management. More specifically, DGs will have to:

- determine the physical inventory in order to establish the opening balance for the various assets, liabilities and contingent assets and liabilities;
- establish specific inventory procedures within each DG, after self-assessment of the risks linked to the valuation of their assets and liabilities;
- analyse, in the context of the internal control standards, the segregation of duties between those who authorise transactions, those responsible for the safe-keeping of assets, and those responsible for the inventory.

**I.5.3.3. Certification of local systems**

Article 61 of the new FR mentions that the Accounting Officer shall be responsible for laying down and validating accounting systems and, where appropriate, validating systems laid down by the Authorising officer to supply or justify accounting information.

When systems for financial management laid down by the Authorising Officer provide data for the accounting of the Commission, or when they are required to justify data, the Accountant Officer has to give his agreement to their setting in place as well as to their modification.

The Accounting Officer has also to be consulted on the setting up and the modification by the Authorising Officers of the systems for inventory and for the valuation of assets and liability.

Today, the validation is carried out by the validation of the interfaces between the local systems and the central system. In 2005 the Accounting Officer will have to verify the capacity of local systems to provide to the central system data complying with the new accounting rules. After this verification the central system will no longer accept data provided by non-validated local systems.
The way of dealing with the data is under the Authorising officer’s responsibility. The Accounting Officer needs accounting information that is available, complete, reliable and necessary, in order to produce financial statements according to the new standards, based on the principles of integration of the data and of accrual accounting.

Consequences for the DGs

DG Budget has to identify, within the Commission, the local systems used and requiring validation by the Accounting Officer. To this end, DG Budget should have the audit resources necessary to carry out the certification of these systems. In principle, the certification of local systems will be done by external audit companies.

The DGs have to ensure that their local system will be adapted in time in order to be able to provide the data required by the new accounting framework set out by DG Budget sufficiently in advance.

I.5.3.4. Accounting information by DG

Authorising DGs will be wholly responsible for their accounting operations. Services will need to have access to high-quality management information that is accurate, clear, useful, easily accessible, complete and up to date.

Each DGs annual activity report must contain both its annual accounts and a declaration by the Director-General certifying that adequate internal controls are in place and that resources have been used for their intended purpose.

Besides management information, the justification by inventory of all the balance-sheet accounts will require a breakdown of account balances by authorising department responsible. The system to be put in place will therefore have to allow balances and accounting transactions to be broken down by authorising officer.

Implications for DGs

DGs will have to earmark the necessary resources for analysing and providing supporting evidence for the accounting data.

DG Budget will provide operational DGs with a user-friendly system for exploiting accounting data by DG. The DGs’ requirements in terms of management information will be taken into account.

I.5.4. Training and awareness raising among those concerned

An essential factor for the smooth functioning of the future system will be to implement appropriate training and awareness-raising measures among those concerned.

Awareness

Efforts will have to focus not only on the technical aspects but also on the need for an accounting approach in each DG. If the new accounting framework is to have the desired effect, it is crucial for everyone concerned in the operational services to be made aware of the importance of producing reliable and complete accounting data and of their responsibilities in this area.
Action to raise awareness in Commission services has already been taken through the network of heads of financial units (RUF) and the formation of working parties with the task of preparing the July memorandum and this communication. The other institutions, the agencies and the Commission’s own services will be kept duly informed on the progress of the project.

Training

The training required covers various areas.

During the transition towards the new accounting framework, target groups of staff with similar training requirements will be designated. To identify requirements themselves, a statement of the skills available in operational services will be drawn up and compared with the list of skills required under the reform. These may be expressed in terms of production and actions to be undertaken, or in the form of a graded scale.

At all events, two types of training will be provided: general courses and complementary modules targeted at the specific requirements of DGs managing particular accounting events. By assessing the effectiveness of the training provided, it will be possible to determine any further training that may be appropriate.

It will require continuous training at a steady rate in order to meet the requirements entailed by the changes in methods and systems, staff mobility and the recruitment of new staff.

Recruitment

Recruitment requirements in terms of external staff with accounting qualifications will have to be anticipated sufficiently early because of the time lag inherent in the organisation of competitions; job descriptions will have to be updated in line with the reforms under way.

Network

The effort to raise awareness among staff in authorising services could also be boosted through a number of new arrangements. An accounting correspondent would be designated in each DG and a network of those in charge of accounting would be set up, along the lines of the network of financial units. An easy way of answering the practical questions managing officials would be faced with in their day-to-day work, could be obtained by setting up an “accounting help-desk”.

Lastly, a substantial effort would be required in terms of the documenting of procedures and of the new system.

Implications for DGs

It will be the DGs and other entities concerned that will have to take stock of the skills they have available in order to identify their training requirements and decide on the best way to satisfy them. In this connection, the following points are worth noting:
– it is preferable to anticipate staff turnover during reform implementation, since this has an impact on training and could cause some delay in putting the scheme in place,

– it is useful to try to adopt an integrated approach to training, which entails bringing together participants from different sectors, so enabling them to exchange information about their experience and knowledge.
II. PART II : IT SYSTEM

II.1. Current position

II.1.1. Description of the current system

The Commission’s central financial management and accounting needs are provided for by a central computer system (SINCOM2), introduced for the first time in 1997 and extended to cover all Commission services in 1999. The architecture of this system is complex and comprises three different systems which are inter-linked and are also linked with sectorial systems developed by the spending services to meet sectorial management needs. These systems may be used to initiate financial transactions.

SINCOM2 comprises two interfaced central systems designed to meet the needs of different users:

- **SAP R/3** is used by the services of the Accountant and by the Financial Controller. This system is the official accounting system of the Commission in which budgetary accounting, general accounting, treasury management, the validation of third parties, recoveries and the emission of payments via the SWIFT network are carried out; and

- **Si2** is the budgetary management tool for the authorising services. Transactions are introduced by the Directorates General in Si2, either directly or indirectly via transfer from sectorial computer systems through a standard interface. Irrespective of their origin, all transactions must be validated in Si2 by the authorising officer before transfer into SAP.

The current system architecture is completed by the reporting functionality provided by the data warehouse. A budgetary data warehouse has been created which contains data from Si2 and is used by the authorising services. The legal reporting by the Accountant is carried out on the basis of SAP data copied into the accounting data warehouse.

The standard accounting package SAP is the official accounting system of the Commission. It is from this system that the Commission produces its financial statements. The Commission decided in the SINCOM2 project to create a system (Si2) in which the managing services could introduce their transactions without making detailed accounting entries before approving them and sending them into the central accounting system. Because different spending services operate to different sectorial rules, the current system architecture allows for services to develop their own sectorial information systems and to transfer (through a standard interface and following strict rules) transactions from these systems to Si2 in which the authorising officers must give their approval. Under the provisions of the new Financial Regulation, the Accountant must validate these sectorial systems in the future.
II.1.2. The need to create accrual accounting functionality

SINCOM2 was developed to support the production of cash-based financial statements in line with standard public sector practice at the time. Consequently, the system does not support the production of accrual accounts, as required by the Financial Regulation from the 2005 financial year. There is therefore a need both to develop the accounting framework as outlined in Part 1 of this Communication and to implement functionality in the computerised accounting system to support this framework.

While many of the necessary accounting tools exist in SAP, some of these do not at present form part of the Commission’s implementation of SAP. The tools which need to be implemented to support accrual accounting include an inventory system and client and supplier ledgers. The implementation will depend on the rules fixed by the Accountant in the accounting framework.

II.1.3. The issue of consistency between sub-systems

Under the current system architecture, data are transferred between Si2 and SAP in accordance with fixed workflows. When changes to a transaction are made in one system, these are synchronised with the other system. The interfacing does however allow potential inconsistencies between the systems as the same central budgetary accounting data exist and are treated in both systems – this has an impact for example where the automatic synchronisation does not work correctly or where certain calculations (for example for the revaluation of commitments) are done separately in both systems.

Since the launch of SINCOM2, and particularly in the light of the decentralisation of responsibility as part of the financial reform process, users have been concerned about consistency between the Si2 data to which they have access and the central accounting data held in SAP to which they do not have access. To examine this question, the Commission launched a quality assurance project, the first phase of which has been to reconcile data between Si2 and SAP for the 2001 financial year. This exercise has shown that the two systems are consistent – the systems have been fully reconciled for commitments, payments and receipts. The project has resulted in the improvement of the synchronisation mechanism between the two systems.

Following the successful result of the quality assurance exercise for 2001, the Commission has developed tools to enable a comparison to be made in respect of the 2002 financial year. This work is under way. Once this latter exercise is completed, the Commission will put in place a regular quality control mechanism to ensure that differences can be identified, investigated and corrected as soon as they occur. This work and the improvement to the system will continue until such time as it is replaced by a new system architecture.

II.1.4. Management functionality

In addition to the pure accounting functionality within SINCOM2, the Commission began as part of the financial reform to develop management functionality which is integrated within SINCOM2. To date, a central invoice register (allowing services to register...
invoices received and to manage payment deadlines) has been put into production. A central database of contracts and contractors (ICON) is also being developed and is currently implemented on a pilot basis in two specific areas. Both of these tools are integrated with SINCOM2 and both use “web” technology. The functionality provided by both of these systems will need to be integrated into the new system architecture as aspects of both systems may be used to support accrual accounting. This integration must be at both functional and technical levels.

The Commission has also been developing other separate modules within Si2 – notably a workflow motor which enables the management of security in the new and more complex financial circuits within the spending services which are required under the new Financial Regulation. This workflow motor is adapted to the specific needs of financial management in the Commission and would also need to be integrated in any revised system.

II.1.5. Cost of the current system

The SINCOM2 system cost some €10.4 million to develop between 1994 and 1997, including testing, documentation and the training of users. This cost is relatively low in terms of investments by other organisations to put in place their computerised systems. The budget is also comparable to that of some systems being developed by individual spending services to meet their own sectorial needs. The maintenance costs of the system (new developments, training of new users…) are some €2.6 million per year.

II.2. The situation in the Member States

As identified in Section I.3 above, the Commission is not acting in isolation and most European States are at least at the stage of considering moving towards accrual accounting. To support these moves, Member State administrations are at various stages of implementing new computerised financial management and accounting systems – at both national and local level. These systems are always based on proprietary packages – in-house development is no longer seen as a solution. The main reasons for purchasing packages are that:

– they offer greater flexibility than in the past and it is therefore easier to meet specific requirements by customising the package;

– the total cost of a package solution is considered to be lower than developing in-house; and

– the use of a standard package increases harmonisation between different ministries or departments.

While packages are used, these are always supplemented by additional specific developments – accounting on average for a quarter of the functionality provided. The remaining functionality required is provided by special additional developments or packages or by so-called “legacy systems” – existing systems which are proven and
which the organisation decides to keep and integrate within the new system architecture. Given the accent on providing a significant part of system functionality outside the package solution, there is a concentration on ensuring that systems are easily linked and easy to integrate. Web-based technology is now becoming the standard for these developments.

The timescale for projects to convert to accrual accounting can be long and the resources considerable – project teams number generally from 20 to 50 persons and can be as many as 200 persons. While implementation of the computerised system can be achieved in 18 months, the whole project, including the implementation of accounting rules, generally takes six to ten years.

II.3. Consideration of the options for the future

Whatever the final choice made as regards the systems, some key principles need to be followed in making this choice. Experience with SINCOM2 shows that the future accounting system must be totally integrated (providing all accounting data directly from the system), whether the solution is a standard single package or a package surrounded by other compatible modules which are bought-in or specifically developed. The single package approach is essential for the core accounting functionality. Where the central standard package does not meet users’ needs for management functionality or where it is not cost effective to use the relevant functionality the Commission could envisage purchasing complementary software or developing its own systems to meet identified needs – but always respecting the principles of integration and inter-operability. Where needs are sectorial rather than common, these needs could be met by the development or retention of sectorial systems, again respecting inter-operability and integration principles.

The new system must provide the appropriate accrual accounting functionality as defined by the Accountant. It must also guarantee the security and reliability of data as well as guaranteeing a full audit trail. The requirements for the new system are summarised in the table below.
Table 1: Key requirements for the future accounting system

<table>
<thead>
<tr>
<th>Ensuring full accrual accounting capacity</th>
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<tbody>
<tr>
<td>• full accrual accounting functionality provided by the central standard package</td>
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<tr>
<td>• full respect of generally-accepted accounting principles</td>
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<table>
<thead>
<tr>
<th>Ensuring consistency of data</th>
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<tbody>
<tr>
<td>• no duplicate treatment of data in different parts of the system</td>
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<tr>
<td>• elimination of redundant data and assurance of consistency</td>
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<tr>
<td>• the sectorial functionality must be included in the overall system architecture</td>
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<tr>
<td>• the system must be seamless – where specific management functionality is created, this must respect rules regarding presentation of data and must be designed to ensure full coherence</td>
</tr>
<tr>
<td>• respect of inter-operability principles fixed by the e-Commission initiative</td>
</tr>
<tr>
<td>• services should all have access to the same reliable reporting data – the system must be the sole source of accounting data</td>
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<table>
<thead>
<tr>
<th>Ensuring effective security</th>
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<tbody>
<tr>
<td>• standard security policy to be fully implemented</td>
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<table>
<thead>
<tr>
<th>Other requirements</th>
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</thead>
<tbody>
<tr>
<td>• the transition risks to the new system must be minimised</td>
</tr>
<tr>
<td>• preference for central standard functionality (including management tools) provided by a standard package. Other solutions only to be developed if the standard package solution is not cost effective or does not meet users’ needs</td>
</tr>
<tr>
<td>• ease of maintenance, portability and user-friendliness</td>
</tr>
</tbody>
</table>

The cost of the system is not regarded as a key requirement for the new architecture – the result of the project must be an integrated reliable system and so, while value for money must of course be assured, cost is a secondary consideration in appraising the options. The new system must meet users’ needs, including accrual accounting functionality, integrated operation and tight security. The objective of the project will be to ensure such a system is implemented while also ensuring best value for money for the Commission.
The July memorandum identified three main options for the future:

– using the current SINCOM2 system while continuing to improve its performance;

– to use a single standard package to provide all functionalities; and

– to use elements of the existing system in an evolution towards a new architecture based on the single standard package already in use in the Commission eliminating the causes of incoherence and in which data are stocked only once.

This section of the Communication evaluates each option and reaches a conclusion on its desirability and feasibility.

II.3.1. **Option 1: Continued use of the current system**

This option would in fact mean no change to the present system architecture – Si2 and SAP would remain in operation while action is taken to improve the synchronisation of data and further to reinforce security. Clearly, additional functionality would need to be created to cater for the requirements of accrual accounting. While in SAP this additional functionality could probably largely be created by using existing modules within the system, Si2 would need to be extensively modified to ensure that all accrual accounting data can be captured on entry into the system.

While of course this is likely to be the “least-cost” option, it is not the recommended solution for two main reasons. Firstly, the architecture of the system is not optimal, relying on two separate interfaced systems; and secondly to the option does not integrate sectorial systems in the overall system architecture.

It is for these reasons that this option is rejected. It is clear however that action to improve the functioning of the current architecture must continue until such time as a new architecture is put in place, notably in terms of the consistency of data and the security of the system (see section II.4.1 below).

II.3.2. **Option 2: A single standard package**

The use of a single standard package would mean that existing sectorial systems would no longer be allowed to transmit financial data into the central system. All spending services would need to use the standard functionality in the package in the same way – for management as well as accounting purposes. This option would eliminate the risk of incoherence as all users would be using the same system in the same way and their own existing sectorial financial management systems would effectively be discontinued as the functionality would be provided in the central system.

However, the extent to which this solution could be adopted in practice is uncertain and needs to be studied further as different sectors of Commission activity are conducted under specific sectorial rules imposed by the legislator. In fact the Financial Regulation contains specific and varied provisions for the different sectors. It is not at all clear
without further study whether these different sectorial needs could be met by a single standard package.

The feasibility of developing a common procedure which respects all of the relevant sectorial rules would need to be examined. The extent of the adaptation necessary would of course influence the feasibility and cost effectiveness of this option. While this option is attractive on paper, there are a number of practical aspects which need to be taken into account before a decision can be taken to move in this direction.

Under the terms of the open procurement of the SAP package used in SINCOM2, this package could be retained without further recourse to the market if it were to be used for accounting purposes only. However, if the solution were to be widened to cover other (management and sectorial) functionality, it is likely that a full public procurement procedure would need to be carried out. A full public procurement procedure would be necessary for any system to replace the current package. This would result in a new procurement procedure which would almost certainly delay the introduction of an accrual-based new system until after the 2005 threshold.

The use of a single standard package as the sole system would require the different sectorial rules and practices to be incorporated within the standard procedures required by the package. This option is still open for further consideration as further work is necessary to analyse the feasibility of incorporating all required sectorial functionality in a single standard package. It is not at all certain that these analyses will show that the option is feasible or cost-effective. Therefore a further option must be considered.

**II.3.3. Option 3: A new integrated system**

This option is different from option 2 in that, while ensuring that all accounting functionality is provided by the central accounting package, it recognises that the required management functionality may not be available from the core package and thus calls for sectorial systems to be maintained or developed within the overall system architecture. The feasibility of this architecture and the action necessary to put it in place will be studied in the first quarter of 2003. This option envisages using the current package for the purposes of the original tender (to provide accounting functionality). Additional accounting functionality could be obtained by extending the existing contract. Any new management functionality to be integrated into the system could lead to a need to go to the open market – in co-ordination with the Informatics Directorate. Depending on the amount of additional functionality purchased, option 3 could eventually resemble option 2 in the technical aspects, in terms of recourse to the market and in the time taken for full implementation.

Sectorial systems integrated into the overall system architecture would be approved by the Accountant in conformity with Article 61 (2) of the Financial Regulation and would need to respect strict inter-operability and integration rules to ensure proper security and consistency of data. The option would respect Article 206 of the Implementing Rules for the Financial Regulation, in that accounting would be carried out in an integrated system.
in that **all** accounting functionality would be provided by the central system. For financial management functionality, the following approach would be applied:

– firstly, the feasibility of providing this within the current package would be evaluated. Where this can be done in accordance with users’ needs and at reasonable cost, the functionality would be provided in the common system;

– second, where it is not possible to use the current package to meet user requirements without complementary developments, the option of using a standard package which would fully integrate with the current one would be evaluated. Where this solution is cost effective, it would be adopted;

– third, where the package solution is not possible, a decision would be made on whether the requirement is a common one shared by some or all sectors, or whether it is sectorial in nature. Where there is a common need, an in-house solution would be developed and integrated in the overall architecture to avoid that individual services need to invest in developing their own separate solutions; and

– finally, where the need is sectorial in nature, the responsible services would be invited to develop their own solution, but would be required fully to respect inter-operability principles. These systems would be subject to validation by the Accountant and would need to conform to rigorous specifications to ensure coherence with the central system.

In this option, all functionality (whether provided by the common system or by sectorial systems integrated within the overall architecture) must be totally integrated so as to ensure consistency of data at all times. Accounting functionality would be provided within the package, but through the use of a web front-end, data from other systems validated by the Accounting Officer could be displayed on screen.

The above approach would mean that there will be a common core central financial and accounting system which would be integrated and fully coherent. It would be the **sole source** of accounting data and the data would be shared by all users. Around this central core, systems would operate to provide management functionality which is necessary at sectorial level to meet specific needs not relevant to all Commission services. The central core system would provide appropriate management functionality for those services which do not have specific sectorial needs. A business process analysis would be carried out with the spending services to evaluate their user requirements as part of the design phase of the system.

Full coherence would be ensured by this option because data would be shared between the different system modules following the principles of inter-operability. For example, all data on commitments and payments, whether viewed from sectorial systems or the common system, would be the same. All users would in fact view the same data from sectorial systems or the central system. To ensure the reliability of data, rules would be fixed as to the source of definitive data at any stage in the life cycle of a transaction. For
example, before a transaction launched in a sectorial systems is approved by the authorising officer, the single source of reliable data on that transaction would be the sectorial system (as it would not yet exist in the common system). However, once the transaction is approved by the authorising officer and is registered in the accounts, the common system would become the sole source of financial information on that transaction. The history of the transaction in the sectorial system would be kept for audit trail purposes, but in all cases once a transaction is completed, the user would only see the financial elements of the transaction from within the core accounting system.

The advantages of this solution are that it would allow the maximum possible use of a single standard accounting package while also recognising that some management needs may be more effectively met by other solutions. It would guarantee coherence of data by defining at each stage of the lifecycle of a transaction which is the master system. Users of all other linked systems would only be able to view the master data. Decisions on how to provide this additional functionality would be taken on a case-by-case basis and would be guided by cost effectiveness and operational issues. In no case would the development of a solution external to the central package be allowed to compromise coherence. All decisions would be fully documented.

II.3.4. Inter-operability of systems

The E-Commission project was launched in 2001 to examine how information and communication technologies can be applied to improve administration. An interim report on the project in 2002 concluded that the “lack of inter-operability of corporate and sectorial management information systems is a restraining factor on achieving efficiency”. The report recognised that “achieving a quality administration requires better co-operation between services” although it also noted that “there is currently little incentive for individual services to contribute to corporate approaches”. The report, which covered all common corporate systems, noted that the following risks of lack of inter-operability:

– data inconsistencies between the various information systems;

– data is often “locked” within an information system and cannot be shared between users; and

– information systems are designed to perform a certain function, without regard to the continuity of tasks of the user to support his or her work.

In July 2002, the Commission established an action plan relating to the annual activity reports and declarations of the directors general and heads of service in July 2002 (COM(2002) 426). It had become clear from certain of the declarations that the lack of inter-operability of systems caused management difficulties for some services. In this context, and with the objective of ensuring data quality, it is vital that the new system architecture developed to support the accounting reform should respect inter-operability principles.

The future accounting system must therefore ensure that:
– the user has a single point of access to data, adapted to his own needs;
– there will be a single entry of information and this information will be shared across all systems (respecting security rules); and
– there will be unique and uniform data definitions for each piece of data and these definitions will be shared across systems.

Achieving inter-operability is both a technical question (ensuring that the technology used for the system enables it to share data with other systems) and one of functional design (ensuring that it really meets users’ needs). Inter-operability also means that firm central technical and functional rules would need to be established to govern how the systems operate and are developed. To comply with the latter requirement, the system must be designed to support the work processes of all users. Procedures must also be put in place to ensure that all accounting and financial data presented in other systems comes where relevant directly from the core accounting system.

Other actions relating to inter-operability must also be respected – notably the establishment of common data management principles (to ensure that the same term in one system means the same thing in another system, whether this system is common or sectorial). In line with developments in the context of the overall progress on inter-operability, the system must be able to accommodate the use of a single portal through which users can enter the core system.

II.3.5. Evaluation of the system options

An initial appreciation of the three system options identified is summarised in the table below, using the criteria set out in Table 1.
Table 2: Evaluation of options against key requirements for the future accounting system

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Option 1</th>
<th>Option 2</th>
<th>Option 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ensuring full accrual accounting capacity</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>full accrual accounting functionality provided by the central standard package</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>full respect of generally-accepted accounting principles</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Ensuring consistency of data</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>no duplicate treatment of data in different parts of the system</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>elimination of redundant data and assurance of consistency</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>the sectorial functionality must be included in the overall system architecture</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>the system must be seamless – where specific management functionality is created, this must respect rules regarding presentation of data and must be designed to ensure full coherence</td>
<td>No</td>
<td>Depends</td>
<td>Yes</td>
</tr>
<tr>
<td>respect of inter-operability principles fixed by the e-Commission initiative</td>
<td>No</td>
<td>Depends</td>
<td>Yes</td>
</tr>
<tr>
<td>services should all have access to the same reliable reporting data – the system must be the sole source of accounting data</td>
<td>Yes by end 2003</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Ensuring effective security</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>standard security policy to be fully implemented</td>
<td>Common systems only</td>
<td>Depends</td>
<td>Yes</td>
</tr>
<tr>
<td>Other requirements</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The transition risk must be minimised</td>
<td>N/A</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>preference for central standard functionality (including management tools) provided by a standard package. Other solutions to be developed if the standard package solution is not cost effective or does not meet users' needs</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>ease of maintenance, portability and user-friendliness</td>
<td>No</td>
<td>Depends</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Table 2 shows that, while the improvement of the current system in terms of consistency of data and security is a high priority for the coming year, this action does not support the
principles of the accounting reform form 2005. This option can therefore be eliminated as the longer-term solution.

The Table also shows that the choice between options 2 and 3 is less simple. The options offer many of the same advantages – the main difference being that option 2 envisages all functionality being provided within the common system and there is therefore uncertainty as to whether certain of the criteria can be met by this option. This is mainly because option 2 would mean that different sectorial rules would need to be accommodated within the common system, while sectorial procedures and working practices would need to be adapted to conform with the requirements of this system. Option 2 would also mean major changes which would be implemented in one single step - data would need to be converted from existing sectorial systems and input into the new system and the sectorial systems eliminated at the same time. This would increase the transition risk to the new system and also increase the cost.

The advantage of option 3 is that it enables the maximum possible functionality (and all of the accounting functionality) to be provided by the common system while recognising that the common package may not provide all of the required management functionality or that it may be more cost effective to use other integrated solutions to provide some elements of this functionality. Option 3 also recognises the sectorial systems which already exist and which are adapted to the particular management needs of the services which use them. This option would provide perfect coherence because the core accounting data would only come from the common accounting system. Strict rules would ensure that all systems interfaced with the common system conform completely with inter-operability principles (including the use of standard data definitions describing all data items (name, detailed description/meaning, format, rules applying to them) together with an integrated Data Model).

The development of the new system architecture is a major undertaking for the Commission, as it would be for any organisation. It is vital that this development is a success. Risk will therefore need to be reduced to the absolute minimum. The solution should therefore be based on tried and tested solutions – whether these are bought-in or built in-house. The key principles which must be respected are the integration of systems (and hence the coherence of data) and the maintenance of effective security. These will be the watchwords of the project.

Both common corporate systems and sectorial systems need to be interoperable. Thus, an examination needs to be carried out of how systems developed to meet sectorial needs can be integrated with the common core financial management and accounting functionality. In particular, an external study by recognised experts in the field will be commissioned as early as possible to examine options 2 and 3 and notably the latter option – how sectorial systems can be included in the overall system architecture. The study, the results of which will also be shared with the Informatics Directorate to obtain their comments, will evaluate the options from both technical and practical viewpoints. A detailed road map for the development and implementation of the new architecture will be prepared in the second quarter of 2003 on the basis of this study and will be validated by experts.
II.4. Action to be taken

II.4.1. Improvement of the current system

To ensure its staff have access to high quality financial and accounting data, the Commission needs to improve the current functioning of the SINCOM2 system at the same time as it develops the new architecture. This improvement has been a priority in 2002 and will continue to be so in 2003. The specific concrete actions which will be taken in 2003 in co-operation with external experts include:

– the development and implementation of a web-based version of the Si2 system to facilitate inter-operability (this also goes along the same lines as the new management functionality developed within SINCOM2 – the ICON contractors’ database and the central invoice register);

– the elimination of redundant data by incorporating the possibility to view accounting data from SAP within the web version of Si2;

– the reconciliation of Si2 and SAP data for 2002 and the establishment of a regular quality control of data in the system;

– the development of a written security policy to govern the management of security in the system which will draw on best international practice and which will be strictly adhered to;

– the fixing of rules governing the incorporation of security elements at the development stage of new functionality. This will ensure that all future developments fully conform to the security policy; and

– the development of computerised tools to facilitate the management and audit of access rights within the system.

II.4.2. Development of the new system

Detailed planning will be necessary according to the system option chosen. However, certain common steps can be identified and these are presented in Table 3 below. The timetable for the development of the system is clearly dependent on the progress of the overall accounting reform and the delivery of user specifications to the project team. While the work to improve the functioning of the current system will continue until such a time as the new architecture is put in place, the new functionality can only be developed once users’ needs have been fixed (whether these are accounting rules provided by the Accountant or management needs provided by other users).

15 Including British Standard 7799 – Information security management systems, specification with guidance for use.
In parallel with the development the web-based Si2, the Commission will begin the migration from the current version of SAP to the new module – SAP Enterprise. Migration to this module from the version of SAP currently used 4.0 is necessary, independent of the change of the system, as SAP will cease to support the 4.0 release by end-2004. While SAP Enterprise release 4.7 would provide the same functionality, it also offers the possibility of accessing the system using a web-based approach, thus providing greater flexibility of use. While obligatory in any case, this migration will ultimately permit the implementation of a seamless approach fully integrated with web-based management systems while also moving away from specific technical constraints linked to the use of the current module. The aim is to start to prepare this migration in 2003 with the aim of completion in August 2004 in preparation for the implementation of the new system architecture. It should be noted that, while problems of coherence and security will be solved earlier in the project, it is only at the stage of the full implementation of the new architecture that a fully integrated system will be put in place.

The priority for 2004, apart from the completion of the migration, will be the completion of the future architecture (ensuring that the functionality required by the Accountant is put in place) and the subsequent testing, training and documentation. Subject to successful testing and acceptance of the new system, the new architecture will be implemented from January 2005 for all transactions relating to the 2005 budget.

Existing data from SINCOM2 will of course needed to be incorporated in the new architecture. This will mean that all existing data items will need to be adapted to the new data structures and contents. Under option 3 this would be an evolutionary process, but the conversion would need to be done nonetheless. Time and resources will be necessary to ensure that this process can be carried out in an orderly and efficient way. In particular, a heavy investment of time will be necessary just before the full system is put into production and this needs to be foreseen in the overall timetable. Each Commission service is likely also to be called on to prepare its transactions for the change.

**Table 3: Actions to be taken for the implementation of the new system architecture**

<table>
<thead>
<tr>
<th>Action/ Result</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision by the Accountant of an initial analysis of accounting requirements based on the Commission’s decision</td>
<td></td>
</tr>
<tr>
<td>Feasibility study of the new architecture – and in particular an examination of how sectorial systems can be integrated (option 3)</td>
<td></td>
</tr>
<tr>
<td>Detailed road-map for implementation of next computerised system</td>
<td></td>
</tr>
<tr>
<td>Inventory and analysis of existing sectorial systems and analysis of users’ management needs</td>
<td></td>
</tr>
<tr>
<td>Design of proposed solutions – the progressive functional and technical definition of the</td>
<td></td>
</tr>
</tbody>
</table>
system

<table>
<thead>
<tr>
<th>Start of migration towards SAP Enterprise</th>
</tr>
</thead>
<tbody>
<tr>
<td>Elimination of redundancy of data</td>
</tr>
<tr>
<td>User workshops and feedback</td>
</tr>
<tr>
<td>Progressive implementation of new functionality – once additional functionality is available to meet users’ needs, it would be implemented rather than wait for the deadline of January 2005</td>
</tr>
<tr>
<td>Migration to SAP Enterprise complete</td>
</tr>
<tr>
<td>New functionalities adapted to take account of tests</td>
</tr>
<tr>
<td>Training for key users</td>
</tr>
<tr>
<td>Release of new system</td>
</tr>
</tbody>
</table>

II.4.3. **Timetable**

The time available to make the required changes is short if the system is to be available to support the production of accrual accounts from 2005. Much will depend on the option chosen – in principle, option 2 would take longer to implement than option 3. In addition, infrastructures would need to be put in place in the case of option 2 to oversee the migration of functionality and data from sectorial systems to the central system and, in the case of option 3, the integration of approved sectorial systems both technically and functionally within the new system architecture.

Whichever option is chosen, it is likely that by 2005 not all accrual accounting data will come from the central accounting system. This mirrors the position in the Member States where accrual accounting has been introduced, but where the computerised systems are still being developed. In these cases, the accrual accounting data comes from sources outside the system. It will be important to identify as early as possible the functionality which cannot be put in place for 2005 so that the Accountant can introduce other procedures to collect and ensure the quality of accounting data.

III. **PART III: PROJECT MANAGEMENT**

Clearly, this reform of accounting will be a major undertaking. By approving this communication the Commission gives a clear mandate for the reforms, the expected timing and the authority of the DGs to initiate the changes required. The risks of undertaking the major changes proposed in an organisation as complex as the Commission and in such a short timescale should not however be underestimated. To
reduce these risks, all services will need to play a full role in this major project in order that it can meet the requirements of all users and so that the Commission has a high quality system which meets its own management needs and provides appropriate, timely and reliable information to the Budgetary Authority and other interested parties. The availability of sufficient and competent internal resources and suitably qualified and experienced external support will be vital to the success of the project. The ultimate deadline is to comply with the new Financial Regulation – the new accounting rules must be in place for the beginning of 2005 and the computerised accounting system must be available to support as many of these rules as possible.

This section describes the structure to put in place for the management of the project, the resources needed – both human and financial – and the timetable for implementation.

III.1. Project organisation

The key to the success of the project lies with the project management and organisation. The project organisation requires proper ownership of the project, clear definition of responsibilities and assignment of tasks, high involvement of all interested parties and fluid co-operation between sub-projects.

Given the critical nature of the project, a full commitment and leadership from the top management of DG Budget will be ensured. A Project Oversight Board, presided by the Director General for Budget and including representatives from the horizontal services (General Secretariat and Personnel and Administration) as well as from each sector of Commission activity 16, will be established. This Board, of advisory nature, will provide feed-back and guidance useful for the stewardship of the project. The Internal Audit Service will be invited as observer, the Court of Auditors will also be.

The Accounting Officer will have the central responsibility in conducting the project, establishing accounting standards and validating information systems. All resources and competencies, including information services, within DG Budget and the Commission, as well as external expertise, will be pulled at the service of the Accounting Officer in order to achieve the objectives of the project. Furthermore, the Accounting Officer will chair the Accounting Standards Committee (see section 5.1.2.).

The development and implementation of the new accounting system architecture will be carried out following a tripartite approach, whereby the domain experts (from the accounting department and the spending services), the user service manager (who represents all users interests) and the system supplier belong to the project team. The Informatics Directorate as well will be closely associated to the project team. All aspects of the project will involve appropriately experienced external support.

Finally, users representatives from DGs will be regularly consulted through the networks of accounting correspondents and financial units.

16 Common agricultural policy, structural funds, internal policies (with research on an equivalent basis) and external relations.
III.2. Project resources

The development which is proposed represents a major undertaking for the Commission, and for this to be a success, significant resources need to be mobilised – both in human and financial terms.

This chapter contains estimates of the resources needs that will be updated as the project is implemented.

The following specific needs should be met:

– statutory posts for the management of the project by DG Budget and the carry out of future accrual accounting operations within DG Budget and in all DGs;

– technical assistance for the development of the IT systems, project management and training;

– procurement of software, licenses and technical studies.

DG Budget’s estimated need for 2003 is 15 statutory posts (4A, 8B, 3C) for the tasks related to the modernisation of accounting and 22.5 for the upgrading of the current IT system (8A, 14.5B). Internal redeployments will be examined and the net demand will be made in the framework of the 2003 human resources allocation procedure. The carrying out of future accrual accounting operations within DGs will require resources, either additional or developed by training, only from 2004 onwards (1 to 3 posts by DG depending on the complexity of financial transactions and their impact on accrual accounting). Resources will be required in the 2004 Budget for this purpose, they will be allocated to DGs in the framework of the 2004 human resources allocation procedure.
The estimated external resources needed for the development of the IT system are:

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Running and maintenance of current system</td>
<td>1.040.600</td>
<td>1.051.600</td>
<td>1.051.600</td>
<td>3.143.800</td>
</tr>
<tr>
<td>New Financial Regulation functionalities and ABB implementation</td>
<td>528.000</td>
<td>0</td>
<td>0</td>
<td>528.000</td>
</tr>
<tr>
<td>Accrual accounting (with ICON-DB)</td>
<td>1.149.200</td>
<td>1.897.200</td>
<td>1.897.200</td>
<td>4.943.600</td>
</tr>
<tr>
<td>New architecture: technical and web based upgrade</td>
<td>1.336.200</td>
<td>822.600</td>
<td>484.000</td>
<td>2.642.800</td>
</tr>
<tr>
<td>Quality Assurance – data coherence – tests</td>
<td>660.000</td>
<td>759.000</td>
<td>479.600</td>
<td>1.898.600</td>
</tr>
<tr>
<td>Operation – Production</td>
<td>588.500</td>
<td>748.000</td>
<td>748.000</td>
<td>2.084.500</td>
</tr>
<tr>
<td>Training</td>
<td>600.000</td>
<td>700.000</td>
<td>800.000</td>
<td>2.100.000</td>
</tr>
<tr>
<td>Project Management support</td>
<td>107.800</td>
<td>107.800</td>
<td>53.900</td>
<td>269.500</td>
</tr>
<tr>
<td>Package licences</td>
<td>260.000</td>
<td>260.000</td>
<td>510.000</td>
<td>1.030.000</td>
</tr>
<tr>
<td><strong>Totals</strong></td>
<td><strong>6.270.300</strong></td>
<td><strong>6.346.200</strong></td>
<td><strong>6.024.300</strong></td>
<td><strong>18.640.800</strong></td>
</tr>
</tbody>
</table>

The external resources for the accounting framework sub project for 2003-2005 are estimated at 1.900.000 €. An additional envelope of 400.000 € for 2003-2005 will be needed for the procurement of specific studies on public accounting.

This budget includes the running and improvement of the current SINCOM2 systems, the cost of the migration to SAP Enterprise and the training of users to the new system. In addition, resources need to be foreseen for the development of local financial management functionalities, the cost of new SAP licences and the adaptation of the sectorial systems for their integration in the new system architecture.

This budget concerns Option 3. The cost of Option 2 would include roughly this amount plus the cost of new SAP (or other supplier) licenses for the current users of the local systems that would be replaced by the single standard package.

Several DGs may need external resources in 2004 for the adaptation of sectorial systems which may continue to operate within the new architecture (under option 3). Again, this will be foreseen in the 2004 PDB.
III.3. Timetable

The actions to be taken described in parts 1 and 2 of the present communication will be implemented according to the following timetable:
## Accounting Framework Timetable

<table>
<thead>
<tr>
<th>Action</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
<td>Q3</td>
</tr>
<tr>
<td><strong>Devising the new accounting framework</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Provision by the Accountant of an initial analysis of accounting</td>
<td>q</td>
<td></td>
<td></td>
</tr>
<tr>
<td>requirements based on the Commission’s decision</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>**Establishing the accounting standards to be applied by the</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>European Communities</td>
<td>draft</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Setting up an accounting standards committee</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Adapting the chart of accounts</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Defining the event giving rise</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Extending the scope of consolidation</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Financial statements</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Integrating accounting data</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>fixing the opening balances</td>
<td></td>
<td>▲</td>
<td></td>
</tr>
<tr>
<td>**Defining the “object codes” and linking the budget accounts and</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>general accounts**</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>**Integrating contingent assets and liabilities (off-balance sheet</td>
<td></td>
<td>▲</td>
<td></td>
</tr>
<tr>
<td>items)**</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management and entry in the accounts of pre-financing, interim</td>
<td></td>
<td></td>
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<td>payments and final payments</td>
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48
<table>
<thead>
<tr>
<th>Task</th>
<th>Use of CIR</th>
<th>Link general accounting</th>
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</thead>
<tbody>
<tr>
<td>Creating a link between the Central Invoice Register and the accounts</td>
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<tr>
<td>Receivables and files of clients and suppliers</td>
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<tr>
<td>Organisation of internal control of accounting data</td>
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<tr>
<td>Expanding internal control in each DG to include accounting aspects</td>
<td>△ draft</td>
<td>▲ definitive</td>
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<tr>
<td>Supporting evidence for balance sheet balances through inventories</td>
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<tr>
<td>Certification of local systems</td>
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<td>Training and awareness raising among those concerned</td>
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<td>Training</td>
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<td>Recruitment</td>
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<td>Network accounting correspondent</td>
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## Improvement of current system architecture

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<tbody>
<tr>
<td>Reconciliation of Si2 and R/3 data for 2002</td>
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<td>Development of a written security policy</td>
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<td>Comparison of security management principles</td>
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<td>Fixing of rules governing the incorporation of security elements</td>
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<td>Development of computerised tools to facilitate the management and audit of access rights</td>
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<tr>
<td>Development and implementation of a web-based version of Si2</td>
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<td>Elimination of redundant data</td>
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▲ Indicates urgent need.
## Development of the new system architecture

<table>
<thead>
<tr>
<th>Action</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
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<tbody>
<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
<td>Q3</td>
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<tr>
<td>Feasibility study of the new architecture – and in particular an examination of how sectorial systems can be integrated</td>
<td>▲</td>
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<tr>
<td>Detailed road-map for implementation of the next computerised system</td>
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<td>Analysis of users’ management needs</td>
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<tr>
<td>Design of proposed solutions – the progressive functional and technical definition of the system</td>
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<tr>
<td>Migration towards SAP Enterprise</td>
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<tr>
<td>User workshops and feedback</td>
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<tr>
<td>Progressive implementation of new functionality – once additional functionality is available to meet users’ needs, it would be implemented rather than wait for the deadline of January 2005</td>
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<tr>
<td>New functionalities adapted to take account of tests</td>
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<tr>
<td>Training for key users</td>
<td></td>
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<tr>
<td>Release of new system</td>
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</tbody>
</table>
CONCLUSION

The different steps taken within the framework of the multi-annual plan launched in 2000 for the modernisation of the accounts have been the building blocks for this detailed communication, describing the evolution towards an integrated accounting framework and system, based on internationally accepted accounting standards.

The new regulatory framework which will enter into force on 1 January 2003 provides the legal instruments appropriate for these developments. Indeed, the new financial regulation foresees that an accounting system as described above must be operational by the financial year 2005.

The aim is therefore to develop both the new accounting framework and as far as possible the information system by the end of 2004.

The future system will be a dual system, based on accrual principles for the general accounting and based on cash principles for the budget execution.

The new system architecture will provide integrated functionality, ensuring the consistency and security of data. In the meantime, action will be taken to improve the current SINCOM2 system. Key to the success of the reform are training, awareness raising, project management and organisation.

This communication identifies the various actions to be taken and sets out a timetable to achieve the wide-ranging reforms proposed.

The Commission gives the highest priority to the accounting reform, as well as to the new system to be put in place, and is confident that these are of a nature to improve the financial management of the European Communities. These developments continue and significantly deepen the steps towards financial reform begun by the Commission in 2000.
ANNEX A: THE INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSAS)

IPSAS 1 Presentation of Financial Statements (IAS1) sets out the overall considerations for the presentation of financial statements, guidance for the structure of those statements and minimum requirements for their content under the accrual basis of accounting.

IPSAS 2 Cash Flow Statements (IAS7) requires the provision of information about the changes in cash and cash equivalents during the period from operating, investing and financing activities.

IPSAS 3 Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies (IAS8) specifies the accounting treatment for changes in accounting estimates, changes in accounting policies and the correction of fundamental errors, defines extraordinary items and requires the separate disclosure of certain items in the financial statements.

IPSAS 4 The Effect of Changes in Foreign Exchange Rates (IAS21) deals with accounting for foreign currency transactions and foreign operations. IPSAS 4 sets out the requirements for determining which exchange rate to use for the recognition of certain transactions and balances and how to recognise in the financial statements the financial effect of changes in exchange rates.

IPSAS 5 Borrowing Costs (IAS23) prescribes the accounting treatment for borrowing costs and requires either the immediate expensing of borrowing costs or, as an allowed alternative treatment, the capitalisation of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset.

IPSAS 6 Consolidated Financial Statements and Accounting for Controlled Entities (IAS27) requires all controlling entities to prepare consolidated financial statements, which consolidate all controlled entities on a line by line basis. The Standard also contains a detailed discussion of the concept of control as it applies in the public sector and guidance on determining whether control exists for financial reporting purposes.

IPSAS 7 Accounting for Investments in Associates (IAS28) requires all investments in associates to be accounted for in the consolidated financial statements using the equity method of accounting, except when the investment is acquired and held exclusively with a view to its disposal in the near future in which case the cost method is required.

IPSAS 8 Financial Reporting of Interests in Joint Ventures (IAS31) requires proportionate consolidation to be adopted as the benchmark treatment for accounting for such joint ventures entered into by public sector entities. However, IPSAS 8 also permits – as an allowed alternative – joint ventures to be accounted for using the equity method of accounting.
IPSAS 9 Revenue from Exchange Transactions (IAS18) establishes the conditions for the recognition of revenue arising from exchange transactions, requires such revenue to be measured at the fair value of the consideration received or receivable and includes disclosure requirements.

IPSAS 10 Financial Reporting in Hyperinflationary Economies (IAS29) describes the characteristics of a hyperinflationary economy and requires financial statements of entities, which operate in such economies to be restated.

IPSAS 11 Construction Contracts (IAS11) defines construction contracts, establishes requirements for the recognition of revenues and expenses arising from such contracts and identifies certain disclosure requirements.

IPSAS 12 Inventories (IAS2) defines inventories, establishes measurement requirements for inventories (including those inventories which are held for distribution at no or nominal charge) under the historical cost system and includes disclosure requirements.

IPSAS 13 Leases (IAS17) establishes requirements for the accounting treatment of operating and finance leasing transactions by lessees and lessors.

IPSAS 14 Events After the Reporting Date (IAS10) establishes requirements for the treatment of certain events that occur after the reporting date, and distinguishes between adjustable and non-adjustable events.

IPSAS 15 Financial Instruments: Disclosure and Presentation (IAS32) establishes requirements for the presentation of on-balance-sheet financial instruments and identifies the information that should be disclosed about both on-balance-sheet (recognised) and off-balance-sheet (unrecognised) financial instruments.

IPSAS 16 Investment Property (IAS40) establishes the accounting treatment, and related disclosures, for investment property. It provides for application of either a fair value or historical cost model.

IPSAS 17 Property, Plant and Equipment (IAS16) establishes the accounting treatment for property, plant and equipment, including the basis and timing of their initial recognition, and the determination of their ongoing carrying amounts and related depreciation. It does not require or prohibit the recognition of heritage assets.

IPSAS 18 Segment Reporting (IAS14) establishes requirements for the disclosure of financial statement information about distinguishable activities of reporting entities.


IPSAS 20 Related Party Disclosures proposes requirements for the disclosure of transactions with parties that are related to the reporting entity including: Ministers, senior management, and their close family members.
IPSAS expected to be issued after 2002 are:

– **Financial Reporting under the Cash Basis of Accounting** proposes requirements for the preparation and presentation of the cash flow statement and supporting accounting policy notes under the cash basis of accounting. It includes requirements relating to the identification of the reporting entity and the structure and the minimum content of the cash flow statement.

– **Impairment of Assets** (developed from IAS36)

– **Employee Benefits** (developed from IAS19)

– **Accounting for Development Assistance**

IPSAS that will be probably applicable to the specific situation of the Communities are:

<table>
<thead>
<tr>
<th><strong>IFAC</strong></th>
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</thead>
<tbody>
<tr>
<td><strong>International Public Sector Accounting Standards (IPSAS)</strong></td>
</tr>
<tr>
<td>IPSAS 1 – Presentation of financial statements</td>
</tr>
<tr>
<td>IPSAS 2 – Cash flow statements</td>
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<tr>
<td>IPSAS 3 – Net surplus or deficit for the period, fundamental errors and changes in accounting policies</td>
</tr>
<tr>
<td>IPSAS 4 – The effects of changes in foreign exchange rates</td>
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<tr>
<td>IPSAS 5 – Borrowing costs</td>
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<tr>
<td>IPSAS 6 – Consolidated financial statements and accounting for controlled entities</td>
</tr>
<tr>
<td>IPSAS 7 – Accounting for investments in associates</td>
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<tr>
<td>IPSAS 8 – Financial reporting of interests in Joint Ventures</td>
</tr>
<tr>
<td>IPSAS 9 – Revenue from exchange transactions</td>
</tr>
<tr>
<td><strong>IPSAS 10 – Financial reporting in hyperinflationary economies</strong></td>
</tr>
<tr>
<td><strong>IPSAS 11 – Construction contracts</strong></td>
</tr>
<tr>
<td>IPSAS 12 – Inventories</td>
</tr>
<tr>
<td>IPSAS 13 – Leases</td>
</tr>
</tbody>
</table>
IPSAS 14 – Events after the reporting date
IPSAS 15 – Financial instruments: disclosure and presentation
IPSAS 16 – Investment property
IPSAS 17 – Property, plant and equipment
IPSAS 18 – Segment reporting
IPSAS 19 – Provisions, Contingent Liabilities and Contingent Assets
IPSAS 20 – Related Party Disclosures

**Necessary supplementary IAS:**

For subjects, which IPSAS still do not include any specific standard, the IAS that could be applied are:

1. IAS 19 - Employee Benefits (until IPSAS shall be issued)
2. IAS 36 - Impairment of Assets (until IPSAS shall be issued)
3. IAS 38 - Intangible Assets
ANNEX B: INVENTORY

Information on assets and liabilities normally exists in three different dimensions: reality, management databases and accounts.

For example, the information on disposable assets, borrowings and hardware is presented as follows:

<table>
<thead>
<tr>
<th></th>
<th>Reality</th>
<th>Management database</th>
<th>Accounts</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Disposable assets</strong></td>
<td>Bank account statements received from the bank, contracts to open accounts, etc.</td>
<td>Database where bank statements and data relating to bank contracts are recorded.</td>
<td>Account balances and transactions recorded in the journal and the general ledger.</td>
</tr>
<tr>
<td><strong>Borrowing</strong></td>
<td>Contracts, bank statements, legal opinions, etc.</td>
<td>Database including the details of loans, dates, amounts, due dates, rates, etc.</td>
<td>Account balances and transactions recorded in the journal and the general ledger.</td>
</tr>
<tr>
<td><strong>Hardware</strong></td>
<td>Physical PC, insurance contract, order slip, invoice, etc.</td>
<td>Database recording details, purchase date, depreciation period, inventory No, etc.</td>
<td>Account balances and transactions recorded in the journal and the general ledger.</td>
</tr>
</tbody>
</table>
## Annex C: How the Communication responds to the points made by the Court of Auditors

<table>
<thead>
<tr>
<th>Observations Made by the Court of Auditors Concerning the Communities' Accounting Systems in Connection with the DAS from 1994 to 2000&lt;sup&gt;17&lt;/sup&gt;</th>
<th>Actions Set Out in the Communication to Address the Court of Auditors' Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The accounting framework</strong></td>
<td>The communication sets out the following measures to widen the scope of consolidation and improve the consolidation procedure:</td>
</tr>
<tr>
<td><strong>Harmonisation of accounting methods</strong></td>
<td>- Awareness-raising and training for the Accounting Officers of the institutions and agencies</td>
</tr>
<tr>
<td>Up to 1998 difficulties occurred with the consolidation of the accounts of the individual institutions because of the diversity of the accounting methods and valuation rules applied. Since 1999, the difficulties are only occasional as the methods applied by the institutions have been gradually harmonised.</td>
<td>- Analysis of the accounts of the agencies, explanation of the consolidation manual and the single accounting procedures to be applied</td>
</tr>
<tr>
<td><strong>Accounting standards and policies</strong></td>
<td>- Determination of the procedure for consolidation.</td>
</tr>
<tr>
<td>Between 1996 and 2000, the Court insisted on the need to adopt clear accounting principles and policies complying with the generally accepted international accounting standards (IAS) adapted to the specific features of the public sector. All too often the Community rules were an obstacle to full and correct recording of Community assets and liabilities, mainly because the concept of expenditure was confused with that of payment. With the adoption of the new Financial Regulation on 25 June 2002, the situation should gradually improve after 1 January 2003.</td>
<td>- Establishing and developing an automated system for consolidation</td>
</tr>
<tr>
<td>As regards the adoption of accounting policies and principles, the following actions appear in the communication:</td>
<td><strong>Note from the DAS sector of the European Court of Auditors dated 17 October 2002 given to the rapporteur for the forthcoming discharge, Mr Casaca, on the observations relating to the Communities' accounting systems made by the Court of Auditors in its statements of assurance from 1994 to 2000.</strong></td>
</tr>
<tr>
<td></td>
<td>- Creation of an Accounting Standards Committee</td>
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<td></td>
<td>- Identification of priority accounting standards to be defined and presented to the Standards Committee</td>
</tr>
<tr>
<td></td>
<td>- Preparation of standards and presentation to the Standards Committee for its opinion</td>
</tr>
<tr>
<td></td>
<td>- Definition of the accounting procedure for each type of event</td>
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<tr>
<td></td>
<td>- Proposal for chart of accounts</td>
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<tr>
<td></td>
<td>- Definition of the &quot;event giving rise&quot; for each type of transaction</td>
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</table>

<sup>17</sup> Note from the DAS sector of the European Court of Auditors dated 17 October 2002 given to the rapporteur for the forthcoming discharge, Mr Casaca, on the observations relating to the Communities' accounting systems made by the Court of Auditors in its statements of assurance from 1994 to 2000.
### Accounting procedures

The cash-based accounting system used in the past for recording Community operations is not suitable for the presentation of accrual-based accounts, which requires the recording of entitlements and obligations. What is more, the break between the budget accounts and the general accounts is in itself an obstacle to the correct and full recording of assets and liabilities. In June 2001 the Commission drew up a draft action plan to remedy the shortcomings of its accounting systems but no concrete action has been taken since.

### Economic result

Since 1999, the Commission has to present not only the accounting result proper, but also a broader economic result taking into account the items affecting the assets and liabilities at the end of the year. This calculation is affected both by the unsuitable nature of certain accounting practices and by the accounting system itself, which does not lend itself to production of the necessary records. No specific concrete action appears to have been taken to clarify both the meaning and the practical arrangements required to calculate this broader result.

Besides the adoption of the international principles mentioned in the previous point, the following actions are planned in order to integrate the budget accounts on a cash basis and the general accounts on an accruals basis:

- Survey of accounting events in all DGs and identification of the budget lines concerned
- Establishment of the structure of the "object codes" and extension of the chart of accounts to accommodate them
- Establishment of links between the different object codes and the accounts of the general accounts, and updating of the nomenclature throughout each accounting year
- Reconciliation between cash-based budget implementation and the accruals-based accounts
- The full inventory of contingent assets and liabilities should be available for the closure of the financial year 2003. Their incorporation into the accounts will be an ongoing task.

### Reservations and observations relating to the Community accounts

#### Advances and payments on account

The treatment of payments as expenditure raises the issue of pre-payments or intermediate payments which in actual fact are no more than a cash transfer with no real contra-entry. The Court has been calling since 1994 for a solution to this question so that first of all a distinction can be made between the different types of payment and then a guarantee given that they are recorded unambiguously in the accounts and the end-of-year financial statements. Partial answers have been provided to this question. But some provisional payments continue to be treated as expenditure; this is not consistent with the generally accepted international accounting principles which the Community intends to apply.

The communication provides for the entry in the accounts of pre-financing and its clearance at budget level, and also integration into the general accounts and establishment of the opening balance.

It is also provided that supporting evidence should be given for accounting balances through inventories and the opening balance.
<table>
<thead>
<tr>
<th>Treasury</th>
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<tr>
<td>The questions of recording of cash operations are broadly linked to payments of advances to financial intermediaries or for external action projects. The Commission has not yet put in place a monitoring system which gives it an assurance of the reality and availability of the sums outstanding of which it tries to produce a list at the end of the year..</td>
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<table>
<thead>
<tr>
<th>Fixed assets</th>
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<tr>
<td>The questions relating to buildings between 1994 and 1997 were mainly to do with listing property rights and leasing rights. Since 1998 the focus has been on accounting methods for depreciation of assets. As very few operations are involved, the remaining difficulties concern the value of certain buildings. For equipment and furniture, the question regularly arising is that of the physical existence of the items and the reconciliation between the administrative inventories and reality.</td>
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</table>

| Besides the integration of fixed assets in the accounting system as described in the previous points, the communication provides for supporting evidence for accounting balances through inventories and opening balance. |

<table>
<thead>
<tr>
<th>Third party debtors</th>
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<tbody>
<tr>
<td>The listing of third party debtors is a recurring problem to which no solution has yet been found. The question is closely linked to that of recovery for which the Commission had a specific action in its White Paper (action 96). The final date for this action was put back because unexpected difficulties arose. A second issue is the valuation of amounts due either as traditional own resources (separate account) or under the EAGGF Guarantee Section. In both cases the Commission is given only a very rough idea from Member States about whether these amounts can actually be recovered.</td>
</tr>
</tbody>
</table>

| The communication sets out the following actions to address this issue :
- to distinguish the various types of receivables and the third parties concerned. 
- to identify the type of RO, according to whether they involve a claim concerning own resources, penalties, the recovery of an amount from a third party, or a claim which concerns the refunding of an asset.
- to distinguish the type of customer. It can be a true "customer" who pays money to the Commission (as in the case of the penalties), or a "supplier", to whom the Commission paid an amount for the implementation of a programme, and who has to transfer money back to the Commission.
- to identify third parties as a legal entity. |

<table>
<thead>
<tr>
<th>Off-balance-sheet commitments</th>
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<tr>
<td>Off-balance-sheet commitments are still too much of an overflow tank for items which, according to the accounting principles, should be entered in the accounts (balance sheet, revenue or expenditure) but which, under the Community rules, are not, or not necessarily, entered in the balance sheet. Certain legal obligations appear among the off-balance-sheet commitments while others are recorded in the accounts. Rationalisation of the accounting methods should clarify the scope and presentation of off-balance-sheet commitments.</td>
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</tbody>
</table>

<p>| The communication provides for a full inventory of contingent assets and liabilities, their incorporation in the accounts and the establishment of a computer tool which authorising officers may use for the management of guarantees. |</p>
<table>
<thead>
<tr>
<th>Outstanding commitments</th>
<th>SINCOM 2</th>
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</thead>
<tbody>
<tr>
<td>Since 1994, the Court has been stressing the fact that outstanding commitments are not adequately monitored and that some operations presented in the accounts as ongoing no longer really exist. The sums involved are substantial. The Commission recently began a systematic analysis of outstanding commitments and plans to finish the clearance operation in 2003. It has to stressed, however, that such clearance exercises should not be sporadic; continuous action is required.</td>
<td>Although no specific action is provided for in the communication, the improvement of the quality of financial reporting and the accounting system can clearly help the work in progress on analysing outstanding commitments.</td>
</tr>
</tbody>
</table>

### SINCOM 2

The SINCOM 2 system was put in place in 1999. It gradually took over historical data and this disrupted its operation. Its complex architecture is the result of the way things have developed. Three subsystems operate in virtual independence with only loose links between them. Reconciliation of data between the subsystems, the only guarantee of the coherence of the whole, is a laborious process and the results are not entirely satisfactory, especially as regards the exhaustiveness of the information underlying the production of the statement of assets and liabilities at the end of the year (see point 4).

The procedures for updating the system are not sufficiently tight. Too many people have access to real data. The adjustments to the system are not adequately documented. The plan for resuming operations after neutralisation of the main system was tested in 2000 in conditions which did not perfectly simulate complete destruction of the main system.

The number of users with administrator profiles is still too high.

The Commission has given undertakings concerning corrective measures.

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18 SI2: budget accounts; R3/SAP: general accounts; DWH: accounting records. | The Commission will develop a new architecture for its financial management and accounting system. The key principle which must be respected are the integration of systems (and hence the coherence of data) and the maintenance of effective security. |

The new system needs to show a significant advantage in terms of functionality and performance over the current system – not least to include accrual accounting functionality.

A single standard package (SAP Enterprise) will be used to provide all accounting functionality. Decisions on other functionality (for management purposes) will be taken with the following preferences in mind – firstly to use SAP Enterprise functionality; secondly, to buy-in a standard non-SAP package which meets the integration criteria; and thirdly to develop the functionality in-house, respecting the same rules.
ANNEX D: Detailed actions to be taken for the modernisation of the accounting framework

HORIZONTAL MEASURES

– Adoption of a communication by the Commission (autumn 2002)

– Keeping the Financial Units Network regularly informed (an initial presentation was made at the Network meeting in October). At the January 2003 meeting, the Accounting Officer will present the consequences flowing from this communication. Ongoing task.

– Regular talks with the Internal Audit Service (IAS). DG Budget will report regularly on the project’s state of progress to the IAS for discussion and opinion. A presentation will also be made to the network of internal auditors. Ongoing task.

– Creation of the Accounting Project Team.

*Deadline: December 2002. For the sub-project leaders and teams: February 2003.*

– Setting up a network of heads of accounting in each DG. This network will meet regularly under the chairmanship of the Commission’s Accounting Officer in order to receive information and discuss the project’s state of progress and specific aspects.

*Deadline: January 2003*

– Creation of an Accounting Standards Committee.

*Deadline: February 2003. The first meeting will be held in March 2003. Besides a presentation of the project, its purpose will be to examine a proposed list of standards, to be drafted, defining the priorities in this area and the structure.*

*Deadline: regular meetings will be organised depending on the state of progress of the standards.*

– Regular information of the accounting networks of the institutions and agencies.

*Deadline: an initial meeting was held in 2002. Other meetings will be organised in 2003 to present this communication, propose a timetable of meetings and to fix the contribution expected from the Accounting Officers of the institutions and agencies.*

– Regular contact talks with the Court of Auditors.

The Commission will keep the Court of Auditors regularly informed of the project’s progress and will seek its opinion.

ACCOUNTING FRAMEWORK MEASURES

– Definition of “event giving rise” for each type of transaction.

*Deadline: October 2003*
– Identification of priority accounting standards to be defined and presented to the standards committee.

*Deadline: end February 2003*

– Preparation of standards and presentation to the Standards Committee for its opinion.

*Deadline: staggered timetable, the target being to prepare and present the priority accounting standards to the Accounting Standards Committee by the end of 2003. Standards not identified as priorities should be ready by June 2004.*

– Definition of the accounting procedure for each type of event.

*Deadline: same timing as for the previous measure.*

– Proposal for chart of accounts.

*Deadline: an initial draft should be ready by October 2003; the draft will be liable to improvement in line with the standards and procedures adopted.*

– Organisation of making accounting information available to DGs.

**ACTION TO DEVELOP INTEGRATED ACCOUNTS**

– Survey of accounting events in all DGs and identification of the budget lines concerned.

*Deadline: July 2003*

– Establishment of the structure of the object codes and extension of the chart of accounts to accommodate them.

*Deadline: chart of object codes: October 2003*

– Establishment of links between the different object codes and the accounts of the general accounts, and updating of the nomenclature over the course of each accounting year.

– Entry in the accounts of pre-financing and corresponding clearances at budget level.

*Deadline: January 2004 for clearance at budget level; December 2004 for their integration in the general accounts; 31 December 2004 for the opening balance.*

– Reconciliation between cash-based budget implementation and the accruals-based accounts.

*Deadline: closure for 2005 financial year. Tests for June 2005*

– The full inventory of contingent assets and liabilities should be available for the closure of the financial year 2003. Their incorporation into the accounts will be an ongoing task.
Deadline: beginning of 2004, introduction of a computer tool available to authorising officers for the management of guarantees. Financial year 2005 for the incorporation of contingent assets and liabilities into the accounts.

**INTERNAL CONTROL OF ACCOUNTING DATA**

- Supporting evidence for accounting balances through inventories and opening balance.


- Extension of internal control in every DG to accounting aspects.

  *Deadline: a proposal for the organisation of internal control in the DGs will be drafted by December 2003; it will be implemented gradually during 2004 so as to allow the necessary corrections before definitive implementation in 2005.*

- Certification of local systems. The Accounting Officer will certify local systems in terms of data that can be supplied by those systems.

  *Deadline: June 2005*
TRAINING AND AWARENESS-RAISING

- Analysis of requirements compared with existing expertise in DGs
- Drafting supporting material for general and specific courses.

*Deadline: for general courses: June 2003; for specific training: March 2004.*

- Organisation of general and specific courses. Preparation of effective, interactive training courses, based on new information technology.

*Deadline: from October 2003 for general and May 2004 for the specific courses.*

- Organisation of accounting competitions.

*Deadline: July 2003*

FINANCIAL STATEMENTS (BEFORE CONSOLIDATION)

- Improve the existing financial statements. The Commission will gradually introduce improvements in the financial statements, as has already been undertaken over recent years. The improvements will relate to the quality and comprehensiveness of the data.

*Deadline: ongoing task*

- Develop the new statements: cash-flow table (following the standard pattern), economic out-turn and change in capital. The new statements will be presented for the first time in the 2005 financial statements, as the information contained in the object codes needs to be available.

*Deadline: January 2005. The two new statements will be tested between 01.09.2004 and 31.12.2004 (trial start-up period for object codes).*

ACTION RELATING TO THE SCOPE OF CONSOLIDATION

- Awareness-raising and training for the Accounting Officers of the institutions and agencies

- Analysis of the agencies’ accounts, explanation of the Consolidation Manual and single accounting procedures to be applied.

- Determining the procedure for consolidation.

*Deadline: June 2004. Tools available to the Accounting Officer: January 2005.*

- Establish and develop an automated system for consolidation.