

PROCEDURAL ACT OF THE ENERGY COMMUNITY SECRETARIAT

2017/01/ECS-EnC: On amending the Energy Community Accounting Policy

The Energy Community Secretariat,

Implementing the Procedures for the Establishment and Implementation of Budget, Auditing and Inspection of the Energy Community as amended by the Ministerial Council in Skopje on 23 September 2014,

Having regard to the Procedural Act of the Energy Community Secretariat dated 16 January 2008 on the adoption of the International Public Sector Accounting Standards (IPSAS),

Having regard to the management letters issued by the external audit company to the Director in the years 2010 and 2011,

Taking into account experience gained with the preparation of the year-end accounts of the Energy Community,

Having regard to the decision of the Budget Committee of 26 June 2012,

ADOPTS THE FOLLOWING PROCEDURAL ACT:

Article 1

The Director of the Energy Community Secretariat adopts the Energy Community Accounting Policy as attached.

Article 2

This Procedural Act enters into force on the day of its adoption.

For the Energy Community



Janez Kopac
Director

Done in Vienna, 25 January 2017

ENERGY COMMUNITY ACCOUNTING POLICY

Introduction and Objective

In accordance with IPSAS 3, the principle definition of accounting policies refer to *the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements*.

The objective of these accounting policies is therefore to prescribe the manner of adhering to the accounting rules/principles used by the Energy Community as an accounting entity.

In this context, this *Energy Community Accounting Policy* defines any methods and procedures consistently followed by the management of the Energy Community for presenting disclosures to ensure consistency and comparability of the financial statements with previous periods. It is to be read together with the financial statements of Energy Community.

This policy document has been developed in the absence of an IPSAS applicable to transactions or events of specific nature for the Energy Community, like presentation and accounting treatment of unused appropriations or unused legal commitments etc.

The first version of the document was developed in close cooperation with the external audit company, *Ernst & Young*, advising the Energy Community Secretariat, in 2011.

This second edition is a result of further experience made in the course of the audit of the financial statements in 2012 and subject to further regular updates in the future.

These accounting policies need to be disclosed at the end of the financial year. Changes in accounting policy may be made only when required by an IPSAS or when such changes result in the financial statements providing reliable and more relevant information on the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows¹.

Accounting principles and statement of compliance

The accounts of the Energy Community are kept in accordance with Procedural Act 2006/03 of 17 November 2006 on the *Energy Community Procedures for Establishment and Implementation of Budget, Auditing and Inspection (thereinafter: "Budgetary Procedures")*.

Based on the provisions of the Article 73(4) on 16 January 2008 the International Public Sector Accounting Standards (IPSAS) were adopted as accounting rules and methods to be applied for the preparation and presentation of the Energy Community accounts.

The year-end accounts are prepared by the Accounting Officer in accordance with accounting principles laid down in Article 70 of the Budgetary Procedures²; the year-end accounts are validated by the Director.

The objective of financial statements is to provide information about the financial position, performance, cash flows and changes in equity during the financial year. For an entity such as the Energy Community, the objective is also to demonstrate the accountability of the entity for the resources entrusted to it.

¹"IPSAS Explained: A Summary of International Public Sector Standards", Thomas Mueller-Marques Berger, page 49;

² Going concern; prudence; consistent accounting methods; comparability of information; materiality; no netting; fair presentation; accrual - based accounting

The accounting system of the Energy Community is laid down as to enable production of financial statements and budget accounts. The budget accounts give a detailed picture of the implementation of the budget. The applied budgetary principles as listed in Title III of the *Budgetary Procedures*³.

Content of the Accounting Policy document

The document presents in a comprehensive manner few statements – in a table format below - referring to various areas of accounting as relevant for the presentation of the Energy Community year-end accounts.

The content has been indentified based on the several years of experience in presenting the topics of special relevance for the Energy Community year-end accounts (like legal commitment, not used legal commitments etc.) and serves the requirement of internal documentation of working procedures applied.

Finally, few definitions of terms are presented at the end of the document to enable easy reading of the document to any person and/or third party (not only to involved persons).

³ Principle of Unity and Budget Accuracy, Principle of Annuality, Principle of Equilibrium, Principle of Unit of Account, Principle of Universality, Principle of Specifications, Principle of Sound Financial Management and Principle of Transparency;

Accounting Policy Statements

Policy Statement 1:	Unused appropriations and unused commitments are accounted as deductions from the revenue
Background	<p>According to Article 10 of the Procedural Act of the Ministerial Council of the Energy Community on the adoption of the <i>Procedures for the Establishment and Implementation of Budget, Auditing and Inspection</i> ('Budgetary Procedures') of 16 November 2006“</p> <p>1. <i>Appropriations which have not been used at the end of the financial year for which they were entered shall be carried over into the following budget year as revenue.</i></p> <p>2. <i>Appropriations carried over shall be identified respectively in the accounts;</i></p> <p>During the 2nd meeting of the Budget Committee held on 10 March 2008 the Secretariat presented an approach proposal according to which the carryover amount should have been used for paying commitments undertaken in the previous financial year and the remainder would be used to build up a liquidity reserve for unforeseen claims (e.g. rising inflation etc.) up to a certain threshold.</p> <p>Thus the carryover initially was presented as reserve/net assets in prior years' financial statements. However, the Budget Committee rejected the notion of building up reserves at this stage. It considered further that funds from the preceding year can be used to honour the commitments made, but not paid during this year.</p> <p>During its 3rd meeting, held in September 2008, the Chair of the Budget Committee stated that carryover of appropriations which have not been used at the end of the financial year in question shall not be allowed.</p> <p>This implies that unused budget appropriations at the end of the relevant financial year have to be shown as a liability towards the Parties to the Treaty. This implies further, that unused budget appropriations may not be shown as net assets/equity but have to be shown as liability. In accordance with the Budget Committee's intention it may not be split up into a reserve and a liability portion.</p>
Accounting Treatment - <i>Presentation in the statement of financial position</i>	<p>For accounting purposes it has to be considered that as long as there is a restriction on the use of funds, unused appropriations and unused commitments may not be presented as equity but have to be shown as a liability.</p> <p>This is in compliance with the definition laid down in IPSAS 1: <i>“Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.”</i></p> <p>Since the Budget Committee explicitly prohibited the building up of reserves, unused appropriations and commitments may not be shown as (revenue) reserves.</p>
Accounting	In the statement of financial performance, contributions from the parties

<p>Treatment – <i>Presentation in the statement of financial performance</i></p>	<p>should be shown as revenue. Unused commitments and appropriations should be presented separately as a deduction from revenue. They may not be shown as an expense, since they do not meet the definition of expenses as defined by IPSAS 1:</p> <p><i>“Expenses are decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or incurrences of liabilities that result in decreases in net assets/equity, other than those relating to distributions to owners”.</i></p> <p>Although, at the balance sheet date there are firm commitments (eg. in the form of commissions or orders) these funds are not expensed as long as the underlying commitment is not fulfilled by the contracting party (i.e. the service in return has not been received). This is in compliance with the principle of accrual basis of accounting according to which transactions and other events are recognized when they occur (irrespective of when cash or its equivalent is received or paid). Therefore, the underlying transactions and events are recognized in the financial statements of the periods to which they relate. Since unused commitments relate to future periods they may not be shown as expenses but for reasons of transparency should be shown as a deduction from revenue.</p>
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<p>Policy Statement 2:</p>	<p>Unused budget appropriations shall be paid back to the Parties on annual basis.</p> <p>The repayment is calculated in accordance with Annex IV of the Treaty and based on the budget report. The total calculated amount due shall equal the total amount of <i>unused appropriations</i> shown in the balance sheet as of 31 December.</p> <p>The table of repayments is subject to audit each year and shall be part of the Auditor’s report.</p>
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<p>Background</p>	<p>Following the request received from the European Commission in August 2009 on the repayment of non used budget appropriations, the Secretariat presented a technical explanatory note on the issue, including the description of the methodology to be applied for the calculation of the repayment amounts, to the Budget Committee on 28 September 2009 (see <i>Annex 6</i> of the meeting’s materials).</p> <p>The Budget Committee concluded at this 6th meeting that actual expenditure of any financial year, without consideration of accruals for unused annual leave entitlements, shall provide the basis for the recovery of funds.</p> <p>Further, it was decided that according to Article 48 of the Budgetary Procedures the interest income occurred on the bank account of the Energy Community shall be in benefit of the Energy Community.</p> <p>During audit phase in 2012, the question of repayment amounts for non used budget 2011 appropriations occurred. The very question referred to the fact whether the interest and other income shall be paid back. Followed by consultations on the one side with the European Commission and on the other side the external audit company, Ernst & Young – it was concluded that any and all revenue (i.e. not only non</p>
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	<p>used budget contributions appropriations) shall be subject to repayment to the Parties.</p> <p>This decision followed the Commissions opinion stated in the Budget Committee on 22 March 2011 (see Minutes of the Meeting of the 11th meeting). The table of repayments is subject to audit each year and shall be part of the Auditor's report.</p>
Accounting Treatment - <i>Presentation in the statement of financial position</i>	Non-used budget appropriations are shown as a liability. The amount shall equal to the amount calculated as a difference between actual and budget and presented in the budget report under IPSAS 24.
Accounting Treatment - <i>Presentation in the statement of financial performance</i>	In the statement of financial performance, contributions from the Parties should be shown as revenue. Unused appropriations should be presented separately as a deduction from revenue ⁴ .

Policy Statement 3:	Budget amendments shall be made on annual basis to reflect sources of revenue other than contributions from the Parties (i.e. other interest and income interest).
Background	<p>The Commission proposed on 22 March 2011 to the Budget Committee to consider the amendment of 2011 budget in order to reflect interest and other income obtained by the Energy Community in the years 2007-2010⁵. Following this proposal, the Budget Committee decided at the same meeting that the budget 2011 should be amended accordingly. As a consequence, on 6 October 2011, the amendment Decision was approved by the Ministerial Council upon Commission's proposal (see Procedural Act of the Ministerial Council of the Energy Community PA/2011/01/MC-EnC).</p> <p>As proposed by the European Commission, the Ministerial Council decided that, from the Budget 2012-2013, revenues from other sources should be recorded at the beginning of each budget year as pro memoria. The exact amount shall be then reflected in the financial statement for a given year⁶. It implies – based on the principle of equilibrium - that the expenditure in each year can increase up to sum of the contributions from the Parties and of the other revenue obtained by the Energy Community⁷.</p>
Accounting Treatment – <i>Technical amendment of the budget</i>	The amendment of the budget of the year shall be implemented based on the Decision of the Director regarding the allocation of the revenue to the expense account(s).

⁴ See Policy Statement 1 above

⁵ Since the begin of its existence

⁶ See PA/2011/01/MC-EnC On the amendment of the Procedural Act No. PA/2009/01/MC-EnC on the Energy Community Budget 2010-2011

⁷ See PA/2011/02/MC-EnC on the adoption of the Energy Community budget for the years 2012-2013 (page 19)

Policy Statement 4:	The payments for consultancy services requested by the Energy Community on the basis of agreed installments in relevant contract are booked as prepayments. The prepayments are booked into expense account upon receipt of final results of the consultancy service (mainly in the format of a final report).
Background	<p>Energy Community has in its annual budgets of EUR 400.000 to EUR 500.000 foreseen for consultancy work. Following the procurement procedure, the studies are concluded for the duration of up to 1 year (in regular case), whereas their execution may fall in the time beyond the financial year. The agreed upon deliveries are presented in accordance with agreed milestones reflected accordingly in the contracts. It is normally agreed with the service provider(s) that a first payment will be done after the receipt of the inception report and next installments are paid after receiving interim and final reports.</p> <p>All deliverables are subject to Director's approval followed by notification and respective payments of agreed upon installments.</p> <p>Only the final report of a study is generating the benefit for the Energy Community with an added value for the progress to be made within the Treaty implementation. The preceding reports (inception, interim) of the reflecting purely the ongoing progress made in study execution without generating any added value for the Energy Community.</p>
Accounting Treatment – <i>Presentation in the Statement of the Financial Position</i>	<p>In accordance with the International Public Sector Standard framework, the accounting treatment for each transaction has to follow the following rules: Understandability, Relevance, Materiality, Reliability, Substance over Form, Prudence, Completeness.</p> <p>Due to the fact that the installments based on the inception or interim report do not represent an added value for the EnC and - based on the economic content of the regularly requested services and following the general accounting rules in accordance with the IPSAS framework, all installments shall be considered as prepayment in the statement of financial position at 31 December of the relevant financial year.</p>

Policy Statement 5:	VAT of the invoices with total amount below EUR 73 shall be accounted as expense.
Background	<p>Based on the <i>Agreement between the Energy Community the Republic of Austria regarding the seat of the Secretariat</i>, the Republic of Austria recognizes the Energy Community with its international juridical personality and its legal capacity in Austria. Based on this Agreement, the Energy Community enjoys number of privileges, among others – according to Article 10 of the Agreement – it is exempted from all forms of taxation. This freedom from taxation refers – among others - to indirect taxes included in the prices of goods and services (VAT) supplied to EnC;</p> <p>The <i>procedure</i> for claiming the VAT reimbursement is outlined in the following sources of information:</p> <ul style="list-style-type: none"> • <i>Guide to Protocol Matters and Diplomatic Privileges and Immunities in the Republic of Austria, Chapter III.1. Relief from Value Added Tax (VAT) and Customs Duty</i> • Website of the Austrian Federal Ministry of Finance (see:

	<p>www.bmf.gv.at/Steuern/Fachinformation/Umsatzsteuer/Informationen/ -Information concerning VAT refund to diplomatic and consular missions, international organizations and diplomats;</p> <p>The requirements of the claiming procedure result in the fact that the invoices with the gross amount less than EUR 73 are not eligible for tax refund.</p>
Accounting Treatment – Presentation in the Statement of the Financial Position	<p>Any and all invoices with gross amount below EUR 73 are charged to expenditure account. Thus, for such invoices there will be no separate entry to reflect the VAT receivable amount.</p> <p>The total VAT claimed at the end of accounting period shall match the balance on VAT receivable account. The balance as of the end of the year shall reflect only the outstanding VAT receivable for the last VAT claim.</p> <p>Such balance is presented in the Statement of Financial Performance in the Section A. Current Assets, II. Receivables, 1.VAT (Federal Ministry of Finance).</p>

Policy Statement 7:	The Energy Community applies the International Public Sector Standards [IPSAS] when Reporting Foreign Currency Transactions in the Functional Currency
Background	
Accounting Treatment – Presentation in the Statement of the Financial Position	<p>A foreign currency transaction should be recorded on the initial recognition in functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction. The date of the transaction should be understood as the reporting period (month) of accounting in the Energy Community.</p> <p>For practical reasons, a rate that approximates the actual rate at the date of transaction is an average rate for a month (InforEuro Rate) as published under: http://ec.europa.eu/budget/contracts_grants/info_contracts/inforeuro/index_en.cfm</p>
Accounting Treatment – Presentation in the Statement of Financial Performance	<p>Once the conversion from the national currency has been made, the euro amount can be rounded up or down to the nearest euro cent.</p> <p>When the Energy Community translates foreign currency into its functional currency, any resulting profit or loss on exchange shall be recognised in the profit and loss account.</p>

DEFINITIONS:

Appropriation(s): budget funding⁸;

Commitment appropriations⁹: are the total costs of the legal commitments entered into during the current financial year;

Donation: direct financial contribution¹⁰; in concrete case – awarded by the Republic of Austria to finance the Energy Community office rent (operating) expenditures on monthly basis. The amount of the donation is based on a letter of consent issued on 26 July 2004 on behalf of the Republic of Austria by the responsible Minister for energy affairs;

Functional Currency:

Unused appropriations: are budget contributions from any sources of revenue (parties' contributions, finance income, other income) which have not been used in the current year and which have to be paid back to the parties in the following year; unused appropriations are calculated as a difference between total revenue (incl. interest and other income) and incurred actual expenditures (incl. unused commitments);

Unused commitments: are budget contributions which have not been used (paid or invoiced) at the balance sheet date but for which commitments (e.g. by the commissioning of studies) have been entered into in the current year or in prior years;

Revenue: Income from all sources that finances the budget; the budget of the Energy Community receives the revenue from (in order of contribution weight) the Parties to the Treaty, donations from the Republic of Austria as well as from finance and other revenue;

⁸ See glossary on Financial Programming and Budget under: http://ec.europa.eu/budget/explained/glossary/glossary_en.cfm#a

⁹ In accordance with Art 8 of the Energy Community Budgetary Procedures of 17 November 2006

¹⁰ See EU Glossary, grants under: http://ec.europa.eu/budget/explained/glossary/glossary_en.cfm#i