COMMUNICATION TO THE COMMISSION FROM COMMISSIONER OETTINGER

Revision of the Internal Control Framework
INTERNAL CONTROL FRAMEWORK OF THE EUROPEAN COMMISSION

I — Context and definitions

Internal control applies to all activities, irrespective of whether they are financial or non-financial. It is a process that helps an organisation to achieve its objectives and sustain operational and financial performance, respecting rules and regulations. It supports sound decision making, taking into account risks to the achievement of objectives and reducing them to acceptable levels through cost-effective controls.

The internal control framework of the European Commission is designed to provide reasonable assurance regarding the achievement of five objectives set in Article 32.2 of the Financial Regulation: (1) effectiveness, efficiency and economy of operations; (2) reliability of reporting; (3) safeguarding of assets and information; (4) prevention, detection, correction and follow-up of fraud and irregularities, and (5) adequate management of the risks relating to the legality and regularity of the underlying transactions, taking into account the multiannual character of programmes as well as the nature of the payments concerned.

This framework supplements the Financial Regulation and other applicable rules and regulations1 with a view to aligning Commission standards to the highest international standards set by the Committee of Sponsoring Organisations of the Treadway Commission (COSO) framework.2 The latter was revised in 2013 to move from a compliance-based to a principle-based system with the aim of ensuring robust internal control through consistent assessment by the Commission, while providing the necessary flexibility to allow departments to adapt to their specific characteristics and circumstances. This will also help improve the operational performance of Commission departments. In order to keep up with these recent changes in the international best practices framework, it is appropriate to update the Commission’s internal control framework accordingly.

The new Internal Control Framework consists of five internal control components and 17 principles based on the COSO 2013 Internal Control-Integrated Framework.3

The internal control components are: the control environment, risk assessment, control activities, information and communication and monitoring activities. They are the building blocks that underpin the framework’s structure and support the Commission in its efforts to achieve its objectives. The five components are interrelated and must be present and effective at all levels of the organisation for internal control over operations to be considered effective.

In order to facilitate the implementation of the internal control framework and management’s assessment of whether each component is present and functioning and whether the components function well together, each component consists of several principles. Working with these principles helps provide reasonable assurance that the organisation’s objectives are met. The principles specify the actions required for internal control to be effective.

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1 Notably Staff Regulations, governance arrangements, the Commission Communication on anti-fraud strategy, the Better Regulation Guidelines, the strategic planning and programming cycle, etc.
2 Material from the 2013 Internal Control-Integrated Framework is included, ©2013, Committee of Sponsoring Organisations of the Treadway Commission (COSO), U.S.A. All rights reserved. Licensed for use by the European Commission.
The present communication also identifies the **characteristics** of each principle. These characteristics are defined in such a way as to take into account the specific governance arrangements in the Commission. There is no requirement for Directorates-General to assess whether each individual characteristic is in place. The characteristics are defined to assist management in implementing internal control procedures and in assessing whether the principles are present and functioning. Management is expected to have persuasive evidence to support their assessment.

This framework is a basis for reflection, assessment and action across the Commission. Its implementation should not be perceived as a bureaucratic requirement. It is a pragmatic exercise in which common sense should be the guiding principle. To ensure a consistent and effective assessment of the internal control system in the Commission services, best practices will be shared regularly, under the coordination of DG Budget.
II — The components, principles and characteristics of the Commission Internal Control Framework

| CONTROL ENVIRONMENT | 1. Demonstrates commitment to integrity and ethical values  
2. Exercises oversight responsibility  
3. Establishes structure, authority and responsibility  
4. Demonstrates commitment to competence  
5. Enforces accountability |

The control environment is the set of standards of conduct, processes, and structures that provide the basis for carrying out internal control across an organisation. The College and senior management set the tone at the top for the importance of internal control, including expected standards of conduct.

1. **The Commission demonstrates a commitment to integrity and ethical values.**

   **Characteristics:**

   - **Tone at the top.** The College and all management levels respect integrity and ethical values in their instructions, actions and behaviour.

   - **Standards of conduct.** The Commission’s expectations on integrity and ethical values are set out in standards of conduct and understood at all levels of the organisation, as well as by entrusted bodies, outsourced service providers and beneficiaries.

   - **Alignment with standards.** Processes are in place to assess whether individuals and departments are aligned with the Commission’s expected standards of conduct and to address deviations in a timely manner.

2. **The College of Commissioners\(^4\) demonstrates independence from management and exercises oversight of the development and performance of internal control.**

   **Characteristics:**

   - **The College oversees the Commission’s governance, risk management and internal control practices and takes overall political responsibility for management carried out by Directors-General.** This happens through the use of appropriate working arrangements and communication channels between Members of the Commission, cabinets and services.

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\(^4\) ‘Board of Directors’ within the COSO Framework.
Each Director-General oversees the internal control systems within their Directorate-General. Each Director-General oversees the development and performance of internal control. They are supported in this task by the Director in charge of risk management and internal control.

In their capacity as Authorising Officer by Delegation, each Director-General provides a Declaration of Assurance on the appropriate allocation of resources and their use for their intended purpose and in accordance with the principles of sound financial management, as well as on the adequacy of the control procedures in place (see Appendix 2).

The Director in charge of risk management and internal control plays a key role by coordinating the preparation of their Directorate-General’s Annual Activity Report. In this context, they sign a declaration taking responsibility for the completeness and reliability of management reporting (see Appendix 3). This declaration covers both the state of internal control in the Directorate-General and the robustness of reporting on operational performance. However, responsibility for achieving operational objectives remains with the relevant directorate and unit.

3. Management establishes, with political oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.

Characteristics:

- Management structures are comprehensive. The design and implementation of management and supervision structures cover all policies, programmes and activities. In particular for spending programmes, they cover all management modes, expenditure types, delivery mechanisms and entities in charge of budget implementation (i.e. both Commission departments and entrusted external entities) to support the achievement of policy, operational and control objectives.

- Authorities and responsibilities. The Commission and Directors-General, as appropriate, delegate authority and use appropriate processes and technology to assign responsibility and segregate duties as necessary at the various levels of the Commission.

- Reporting lines. Directors-General design and evaluate reporting lines within departments and with entrusted entities to enable the execution of authority, fulfilment of responsibilities, and flow of information.

* Taking account of the specificities of the Directorate-General, this function may be set at a different management level (Deputy Director-General or Head of Unit). In practice, in most Directorates-General the function is assigned to the director responsible for resources.

In certain cases and in line with the organisational structure of the Directorate-General, this responsibility may be entrusted to two distinct members of management, each covering one of the two sections of the Annual Activity Report. In this case, each of them signs a separate declaration covering their scope of responsibility.
4. **The Commission demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.**

Characteristics:

- **Competence framework.** Directorates-General define the competences necessary to support the achievement of objectives and regularly evaluate them across the Commission, taking action to address shortcomings where necessary.

- **Professional development.** Directorates-General provide the training and coaching needed to attract, develop, and retain a sufficient number of competent staff.

- **Mobility.** Directorates-General promote and plan staff mobility so as to strike the right balance between continuity and renewal.

- **Succession planning and deputising arrangements** for operational activities and financial transactions are in place to ensure continuity of operations.

5. **The Commission holds individuals accountable for their internal control responsibilities in the pursuit of objectives.**

Characteristics:

- **Enforcing accountability.** The Commission defines clear roles and responsibilities and holds individuals and entrusted entities accountable for the performance of internal control responsibilities across the organisation and for the implementation of corrective action as necessary.

- **Staff appraisal.** Staff efficiency, abilities and conduct in the service are assessed annually against expected standards of conduct and set objectives. Cases of underperformance are appropriately addressed.

- **Staff promotion.** Promotion is decided after consideration of the comparative merits of eligible staff taking into account, in particular, their appraisal reports.
RISK ASSESSMENT

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Risk assessment is a dynamic and iterative process for identifying and assessing risks which could affect the achievement of objectives, and for determining how such risks should be managed.

6. **The Commission specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.**

**Characteristics:**

- **Mission.** The Directorate-General, directorates and units have up-to-date mission statements that are aligned across all hierarchical levels, down to the tasks and objectives assigned to individual staff members. Mission statements are aligned with the Commission’s responsibilities under the Treaties and the policy objectives set in the legal base.

- **Objectives are set at every level.** The Directorate-General’s objectives are clearly set and updated when necessary (e.g. significant changes in priorities, activities and/or the organigram). They are consistently filtered down from the Directorate-General level to the various levels of the organisation, and are communicated and understood by management and staff.

- **Objectives are set for the most significant activities.** Objectives and indicators cover the Directorate-General’s most significant activities contributing to the delivery of Commission priorities or other priorities relating to the core business, as well as operational management.

- **Objectives form the basis for committing resources.** Management uses the objectives set as a basis for allocating available resources as needed to achieve policy, operational and financial performance goals.

- **Financial reporting objectives.** Financial reporting objectives are consistent with the accounting principles applicable to the Commission.

- **Non-financial reporting objectives.** Non-financial reporting provides management with accurate and complete information needed to manage the organisation at Directorate-General, directorate and unit level.

- **Risk tolerance and materiality.** When setting objectives, management defines the acceptable levels of variation relative to their achievement (tolerance for risk) as well as the appropriate level of materiality for reporting purposes, taking into account cost-effectiveness.

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6 Objectives must be SMART (specific, measurable, achievable, relevant and time-framed).
7 Indicators must be RACER (relevant, accepted, credible, easy to monitor and robust).
- **Monitoring.** Setting objectives and performance indicators make it possible to monitor progress towards their achievement.

7. **The Commission identifies risks to the achievement of its objectives across the organisation and analyses risks as a basis for determining how the risks should be managed.**

**Characteristics:**

- **Risk identification.** The Directorate-General identifies and assesses risks at the various organisational levels (Directorate-General, directorate, unit, cross-cutting across Directorates-General) and those related to entrusted entities, analysing internal and external factors. Management and staff are involved in the process at the appropriate level.

- **Risk assessment.** The Directorate-General estimates the significance of the risks identified and determines how to respond to significant risks considering how each one should be managed and whether to accept, avoid, reduce or share the risk. The intensity of mitigating controls is proportional to the significance of the risk.

- Risk identification and risk assessment are integrated into the annual activity planning and are regularly monitored.

8. **The Commission considers the potential for fraud in assessing risks to the achievement of objectives.**

**Characteristics:**

- **Risk of fraud.** The risk identification and assessment procedures (see principle 7) consider possible incentives, pressures, opportunities and attitudes which may lead to any type of fraud, notably fraudulent reporting, loss of assets, disclosure of sensitive information and corruption.

- **Anti-fraud strategy.** The Commission as a whole and each Directorate-General set up and implement measures to counter fraud and any illegal activities affecting the financial interests of the EU. They do this by putting in place a sound anti-fraud strategy to improve the prevention, detection and conditions for investigating fraud, and to set out reparation and deterrence measures, with proportionate and dissuasive sanctions.

9. **The Commission identifies and assesses changes that could significantly impact the internal control system.**

**Characteristics:**

- **Assess changes.** The risk identification process considers changes in the internal and external environment, in policies and operational priorities, as well as in management’s attitude towards the internal control system.
Control activities ensure the mitigation of risks related to the achievement of policy, operational and internal control objectives. They are performed at all levels of the organisation, at various stages of business processes, and across the technology environment. They may be preventive or detective and encompass a range of manual and automated activities as well as segregation of duties.

**10. The Commission selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.**

**Characteristics:**

- **Control activities are performed to mitigate the identified risks and are cost-effective.** They are tailored to the specific activities and risks of each Directorate-General and their intensity is proportional to the underlying risks.

- **Control activities are integrated in a control strategy.** The control strategy includes a variety of checks, including supervision arrangements, and where appropriate, should include a balance of approaches to mitigate risks, considering manual and automated controls, and preventive and detective controls.

- **Segregation of duties.** When putting in place control measures, management considers whether duties are correctly divided between staff members to reduce risks of error and inappropriate or fraudulent actions.

- **Business continuity plans** based on a business impact analysis following corporate guidance are in place, up-to-date and used by trained staff to ensure that the Commission is able to continue working to the extent possible in case of a major disruption. Where necessary, business continuity plans must include coordinated and agreed disaster recovery plans for time-sensitive supporting infrastructure (e.g. IT systems).

**11. The Commission selects and develops general control activities over technology to support the achievement of objectives.**

**Characteristics:**

- **Control over technology.** In order to ensure that technology used in business processes, including automated controls, is reliable, and taking into account the overall corporate processes, Directorates-General select and develop control activities over the acquisition, development and maintenance of technology and related infrastructure.
- **Security of IT systems.** Directorates-General apply appropriate controls to ensure the security of the IT systems of which they are the system owners. They do so in accordance with the IT security governance principles, in particular as regards data protection, professional secrecy, availability, confidentiality and integrity.

12. **The Commission deploys control activities through corporate policies that establish what is expected and in procedures that put policies into action.**

**Characteristics:**

- **Appropriate control procedures ensure that objectives are achieved.** The control procedures assign responsibility for control activities to the department or individual responsible for the risk in question. The staff member(s) put in charge perform the control activities in a timely manner and with due diligence, taking corrective action where needed. Management periodically reassesses the control procedures to ensure that they remain relevant.

- **Exception reporting** is one of the management tools used to draw conclusions about the effectiveness of internal control and/or the changes needed in the internal control system. A system is in place to ensure that all instances of overriding controls or deviations from established processes and procedures are documented in exception reports. All instances must be justified and approved before action is taken, and logged centrally.

- **The impact assessment and evaluation of expenditure programmes, legislation and other non-spending activities** are performed in accordance with the guiding principles of the Commission’s better regulation guidelines, to assess the performance of EU interventions and analyse options and related impacts on new initiatives.
Information is necessary for the organisation to carry out internal control and to support the achievement of objectives. There is external and internal communication. External communication provides the public and stakeholders with information on the Commission’s policy objectives and actions. Internal communication provides staff with the information it needs to achieve its objectives and to carry out day-to-day controls.

13. **The Commission obtains or generates and uses relevant quality information to support the functioning of internal control.**

Characteristics:

- **Information and document management.** Directorates-General identify the information required to support the functioning of the internal control system and the achievement of Commission’s objectives. Information systems process relevant data, captured from both internal and external sources, to obtain the required and expected quality information, in compliance with applicable security, document management and data protection rules. This information is produced in a timely manner, and is reliable, current, accurate, complete, accessible, protected, verifiable, filed and preserved. It is shared within the organisation in line with prevailing guidelines.

14. **The Commission internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.**

Characteristics:

- **Internal communication.** The Commission and the Directorates-General communicate internally about their objectives, challenges, actions taken and results achieved, including but not limited to the objectives and responsibilities of internal control.

- **Separate communication lines.** such as whistleblowing hotlines, are in place at Commission level to ensure information flow when normal channels are ineffective.
15. The Commission communicates with external parties about matters affecting the functioning of internal control.

Characteristics:

- **External communication**: All Directorates-General ensure that their external communication is consistent, relevant to the audience being targeted, and cost-effective. The Commission establishes clear responsibilities to align Directorate-General communication activities with the Commission’s political priorities and narrative of the institution.

- **Communication on internal control**: The Commission communicates with external parties\(^8\) on the functioning of the components of internal control. Relevant and timely information is communicated externally, taking into account the timing, audience, and nature of the communication, as well as legal, regulatory, and fiduciary requirements.

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\(^{8}\) Not only to the other EU institutions, but also stakeholders and the general public
Continuous and specific assessments are used to ascertain whether each of the five components of internal control is present and functioning. Continuous assessments, built into business processes at different levels of the organisation, provide timely information on any deficiencies. Findings are assessed and deficiencies are communicated and corrected in a timely manner, with serious matters reported as appropriate.

16. **The Commission selects, develops, and performs ongoing and/or separate assessments to ascertain whether the components of internal control are present and functioning.**

**Characteristics:**

- **Continuous and specific assessments.** The Directorate-General continuously monitors the performance of the internal control system with tools that make it possible to identify internal control deficiencies, register and assess the results of controls, and control deviations and exceptions. In addition, when necessary, the Directorate General carries out specific assessments, taking into account changes in the control environment. Ongoing assessments are built into business processes and adjusted to changing conditions. Both kinds of assessment must be based on the general principles set out in Appendix 1.

- **Sufficient knowledge and information.** Staff performing ongoing or separate assessments has sufficient knowledge and information to do this, specifically on the scope and completeness of the results of controls, control deviations and exceptions.

- **Risk-based and periodical assessments.** The Directorate-General varies the scope and frequency of specific assessments depending on the identified risks. Specific assessments are performed periodically to provide objective feedback.

17. **The Commission assesses and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the College of Commissioners, as appropriate.**

**Characteristics:**

- **Deficiencies.** With the support of the Director in charge of risk management and internal control, the Director-General considers the results of the assessments of how the internal control system is functioning within the Directorate-General. Deficiencies are communicated to management and to the departments responsible for taking corrective action. They are reported in the Annual Activity Reports and to the responsible Member of the Commission, as appropriate. The term ‘internal control deficiency’ means a shortcoming in a component or components and relevant principle(s) that reduces the likelihood of a Directorate-General achieving its objectives. There is a major deficiency in the internal control system if management determines that a component and one or more relevant principles are not
present or functioning or that components are not working together. When a major
deficiency exists, the Director-General cannot conclude that it has met the requirements
of an effective system of internal control. To classify the severity of internal control
deficiencies, management has to use judgment based on relevant criteria contained in
regulations, rules or external standards.

- **Remedial action.** Corrective action is taken in a timely manner by the staff member(s) in
  charge of the processes concerned, under the supervision of their management. With the
  support of the Director in charge of risk management and internal control, the Director-
  General monitors and takes responsibility for the timely implementation of corrective
  action.
III — Conclusions

The Commission is invited to:

- Adopt the internal control principles and characteristics set out in Chapter II of this Communication; these constitute the minimum standards referred to in Article 66.2 of the Financial Regulation.

- Instruct the Authorising Officers by Delegation to implement the internal control principles and characteristics in 2017 and to conduct an overall assessment of the presence and functioning of all internal control components at least once a year and for the first time at the latest in the context of the Annual Activity Report 2018.

- Charge DG Budget in collaboration with the DGs, with the coordination and dissemination of best practices among services to ensure a consistent and effective assessment of the internal control system.

- Charge services with taking appropriate action to define the baselines for each internal control principle, taking into account their specificities and risks, and to improve the awareness and understanding of them by all staff, in particular through training, information and support activities.

This Communication supersedes the relevant provisions of the following:


This Communication amends the Communication to the Commission: Towards an effective and coherent risk management in the Commission services (SEC(2005) 1327) as follows:

- The Director in charge of risk management and internal control takes over the responsibilities of the Internal Control Coordinator.
Appendix 1 — General principles for the assessment of internal control

A system of internal control allows management to stay focused on the Directorate-General’s pursuit of their operational and financial objectives. In addition, the Financial Regulation requires that the budget must be implemented in compliance with effective and efficient internal control.

The Directors-General must be able to demonstrate not only that they have put controls in place but also that these controls take account of the risks involved and that they work as intended.

Internal control principle 16 states that Directorates-General must carry out continuous and specific assessments to ascertain whether the internal control systems and their components are present and functioning. They must carry out an overall assessment of the presence and functioning of all internal control components at least once per year.

Even though the principles and their characteristics are straightforward, their implementation in practice, and therefore the assessment of their implementation, can vary from one Directorate-General to another.

Therefore, before assessing its internal control system, each Directorate-General must set its own baseline for each principle, as best adapted to its specificities and risks. The adaptation of baselines by DGs must nevertheless observe the mandatory provisions defined at Commission or DG level. These baselines are a starting point for effective internal control, from which regular monitoring and specific assessments can be implemented.

The baselines should be expressed in terms of relevant and pertinent indicators. Where possible, these indicators should be quantitative.

Since the principles are interdependent, sometimes it is impossible to fully quantify the effective implementation of each individual principle other than through generic qualitative indicators. Nonetheless, effective implementation can be assessed based on a variety of sources of evidence (e.g. process reviews, register of exceptions, reporting of internal control weaknesses, management supervision and ad-hoc verification, surveys and interviews, management self-assessments, audit reports, stakeholder feedback). The baselines may be adapted in subsequent years in order to make sure monitoring activities remain appropriate and up-to-date.

The assessment of whether the internal control system reduces the risk of not achieving an objective to an acceptable level should follow these logical steps, leading to the identification of internal control deficiencies:

- establishment of a baseline for each principle;
- assessment at principle and at component level;
- overall assessment.

To ensure the consistent and effective assessment of the internal control system in the Commission, services will regularly share best practices with the support of DG Budget. In this context, Directorates-General will exchange views on the setting of baselines for the different principles and on designing proper implementing tools with the input of those Directorates-General and central services most qualified and experienced in particular areas.
Appendix 2 — Declaration of Assurance of the Authorising Officer by Delegation

I, the undersigned,

Director-General of

Executive Director of

In my capacity as authorising officer by delegation [Executive Agencies should replace ‘authorising officer by delegation’ by ‘authorising officer for the operating (administrative) budget and authorising officer by delegation for the operational budget’ here]

Declare that the information contained in this report gives a true and fair view.\textsuperscript{9}

State that I have reasonable assurance that the resources assigned to the activities described in this report have been used for their intended purpose and in accordance with the principles of sound financial management, and that the control procedures put in place give the necessary guarantees concerning the legality and regularity of the underlying transactions.

This reasonable assurance is based on my own judgement and on the information at my disposal, such as the results of the self-assessment, ex-post controls, [the work of the Internal Audit Service — delete this if not applicable] [and the lessons learnt from the reports of the Court of Auditors — delete this if not applicable] for years prior to the year of this declaration.

Confirm that I am not aware of anything not reported here which could harm the interests of the institution [Executive Agencies should replace ‘the institution’ with ‘[the name of the executive agency] or those of the Commission’ here].

[However the following reservations should be noted: ........] (delete this sentence if not applicable)

Place …………………, date …………………
………………….

(signature)

[Name of the AOD]

\textsuperscript{9}True and fair in this context means a reliable, complete and correct view on the state of affairs in the DG/Executive Agency.
Appendix 3 — Statement of the Director in charge of risk management and internal control

a) If the Director in charge of risk management and internal control takes responsibility for the completeness and reliability of all management reporting, the declaration should read:

‘I declare that in accordance with the Commission’s communication on the internal control framework,\(^{10}\) I have reported my advice and recommendations on the overall state of internal control in the DG/Executive Agency to the Director-General/Executive Director.

I hereby certify that the information provided in the present Annual Activity Report and in its annexes is, to the best of my knowledge, accurate and complete.’

b) If responsibility for the completeness and reliability of management reporting is split between two people, the text of the declarations should be amended as follows:

For the Director in charge of risk management and internal control:

‘I declare that in accordance with the Commission’s communication on the internal control framework,\(^{11}\) I have reported my advice and recommendations on the overall state of internal control in the DG/Executive Agency to the Director-General/Executive Director.

I hereby certify that the information provided in Section 2 of the present Annual Activity Report and in its annexes is, to the best of my knowledge, accurate and complete.’

For the Director taking responsibility for the completeness and reliability of management reporting on results and on the achievement of objectives:

‘I hereby certify that the information provided in Section 1 of the present Annual Activity Report and in its annexes is, to the best of my knowledge, accurate and complete.’

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\(^{10}\) C(2017) 2373 of 19/04/2017.

\(^{11}\) C(2017) 2373 of 19/04/2017.