INTERNATIONAL MARITIME ORGANIZATION

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IMO

COUNCIL
96th session
Agenda item 4(a)

C 96/4(a)
12 April 2006
Original: ENGLISH

PROGRAMME FOR CHANGE

(a) Organizational reforms

Note by the Secretary-General

SUMMARY

Executive summary:	This document provides an update on the continuing progress made on the implementation of the ERP system and its further development to address the Organization's future needs, including the implications for the Organization related to implementation of payroll and human resource functions in the ERP system and the UN Common System adoption of the International Public Sector Accounting Standards (IPSAS)
Action to be taken:	Paragraph 26
Related documents:	C 89/11/Add.2, C 90/13/Add.1 and C 96/14(b)

INTRODUCTION

1 This document reports on ongoing developments of the Organization's financial systems, processes and reporting. It provides information on the Organization's review and future replacement of its Human Resources (HR) and Payroll systems and on the introduction of International Public Sector Accounting Standards (IPSAS), the recommended replacement for UNSAS as the accounting standards for all UN system organizations.

HR AND PAYROLL SYSTEMS

2 The Organization presently uses a highly customized bespoke payroll system (IBM AS400), which was developed many years ago. The system is becoming increasingly difficult to support and maintain, a situation which is anticipated to get worse over time. Internal audit reports have recommended its replacement, a view shared by management which considers that such a key system, through which some 80% of the regular budget is paid, should be robust enough not to pose any risk to the smooth operation of the Organization.

3 As noted in document C 96/14(b), the UN Joint Inspection Unit (JIU) has recommended a move to a system-wide payroll system as a first step in a move to a system-wide ERP system. A preliminary recommendation is that larger organizations should consider acting as "leader" organizations or common service entities, which can provide payroll services, on a fee or other financial basis, to those agencies that have old and antiquated systems. Management agrees with this proposal in principle, but has some practical concerns that will need to be resolved before a decision to outsource the Organization's payroll function is made. Similarly, the principle of a single ERP system for the UN system seems attractive, but one that requires full analysis before converting to it. A phased approach towards a single UN system by first moving towards a smaller number of platforms, each led by a large organization, is reasonable, allowing the Organization, amongst other things, to maximize its benefits from its investment in SAP, without having to move hastily to a different system.

4 Nevertheless, it is clear that the existing payroll system must be replaced in one form or another without too much delay. The remuneration provisions under UN Common System are relatively complex and the rules governing allowances and salary scales are sufficiently different from those in the commercial sector to make developing a replacement system less than straightforward. The majority of standard payroll packages available would be unable to meet our requirements without extensive, and expensive, re-configuration and customization. From this perspective, developing another in-house system or customization of a commercial package is unlikely to be a viable option for the Organization, especially in light of the recent significant investment in SAP.

5 However, UNICEF has successfully implemented the SAP HR and Payroll modules and adapted them for Common System requirements. SAP have themselves taken this development and used it to create a standard "industry solution" designed to meet the payroll requirements of organizations in the Common System as much as possible "out of the box".

6 This opens up a number of options for addressing the replacement of the payroll system. With the present situation set out above in mind, and specifically with regard to payroll standardization, the following options, with their advantages and disadvantages are being considered:

.1 implement SAP payroll or other stand-alone payroll system independently of other UN system work - this would give IMO full control over the solution delivered, but would be costly and labour intensive;

.2 use the SAP-standard HR package which is pre-configured to the Common System as the basis for an implementation here. This will not meet all of IMO's requirements, as the JIU also notes that the application of the Common System does vary across organizations, but would clearly provide a good start. It would be sensible, however, to examine the SAP UN package to determine its 'fit' to IMO's requirements, and from this determine the additional work required and an estimated cost. The use of SAP will also ensure a single integrated source of data for the whole Organization;

.3 use UNICEF, or other UN system organization already using SAP HR, to provide a payroll 'bureau' service, effectively sub-contracting out our payroll. This option will have to be carefully investigated to determine its costs and benefits. Whilst it would appear to avoid the one-off cost of implementing a new system, there is the potential of incurring higher annual costs and there is unlikely to be a direct fit to the application of the Common System used by UNICEF or any other UN system body. The Organization would also have concerns over confidentiality and control of payroll data, which are extremely sensitive; and

.4 retain IMO's existing system until a common UN package is agreed and use that as a platform for the future - this would delay the introduction of a new system and increase the risks of retaining our old system, with the implementation timescale not under the control of the Organization.

7 From a preliminary consideration of the options open to IMO, it would be logical to investigate options 2 and 3 further to determine in more detail their costs and benefits and the timescales involved. If option 2 is deemed to be most appropriate, that is, the implementation of SAP HR and Payroll based on the UN Common System standard SAP package, it may well be prudent to implement this on a common timetable with the work required for IPSAS implementation, described in more detail below.

8 Council will recall that the implementation of SAP HR and Payroll was originally envisaged as a 'Phase II' of the main project (C 89/11/Add.2, paragraph 15 and C 90/13/Add.1, paragraph 11). It was originally envisaged that this would take place in 2005, and would cost some £250,000 but, with the focus on the refurbishment and relocation, this investment has been postponed pending completion of Phase I of the refurbishment.

INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS (IPSAS)

9 The United Nations System Accounting Standards (UNSAS) were developed during the early 1990s to provide clear and consistent guidelines by which financial statements and accounts could be prepared for all organizations in the UN system. However, it has become increasingly apparent that maintaining a separate system of UN accounting standards would be neither possible nor desirable, due, in particular, to the fact that resources are not available, and will not be available in the future, to maintain UNSAS in the face of changing accounting standard requirements. This means that UNSAS is consequently out of step with generally accepted accounting practice.

10 It should also be noted that a number of peer organizations have recently changed their accounting standards. The OECD and the European Commission, for example, have moved from their own standards to International Public Sector Accounting Standards (IPSAS), whilst the World Bank and IFAD have moved to the more commercially-focused International Financial Reporting Standards (IFRS).

11 With this in mind, the UN High-Level Committee on Management (HLCM) recently approved the establishment of an internal project, the Accounting Standards Project, under the supervision of the Task Force on Accounting Standards (TFAS), reporting through the Finance and Budget Network (FBN), to the HLCM. The aim of the project was to determine how, or if, to develop UNSAS, and whether to replace UNSAS with a more appropriate set of international accounting standards. The Organization has played an increasingly active role in the discussions, as consistency in approach across the UN system is highly desirable, both for reporting purposes and to allow the Organization to benefit from the experience and resources of other, larger, organizations.

12 The following paragraphs summarize the options considered and recommendations made by the UN system, and briefly considers the impacts for the future.

Options considered and recommendations

13 The TFAS, having considered a number of options for independently-developed accounting standards and their relative merits and weaknesses, determined that the UN system lacked the resource required to maintain UNSAS to the required level and to develop training and guidance on its implementation across the UN system. With this in mind, it became clear that a change of accounting standards was required, as continuing to use UNSAS in its present form would increasingly leave UN system accounts out of step in format, content and accounting treatment, with those applied elsewhere in the world in the profit and non-profit sectors. As a matter of policy and practice, therefore, the alternative standards would have to be set by an independent body and the primary options considered as a replacement to UNSAS were:

.1 **International Financial Reporting Standards (IFRS)** – these are the primary global standards applied by commercial entities. They are developed purely with commercial activities in mind, and do not reflect public sector concerns. The standards-setting body is the International Accounting Standards Board (IASB);

.2 **International Public Sector Accounting Standards (IPSAS)** – IPSAS has been developed to be consistent with IFRS where possible, but to address specific non-profit sector concerns where necessary. The standards-setting body is the IPSAS Board (IPSASB); and

.3 **National public-sector accounting standards** – many countries have their own accounting standards, modified from commercial standards where necessary, and require their own governmental bodies to report by them. Each is set by the national government.

14 Eventually the TFAS determined that it would not be appropriate for the UN system to adopt a national set of accounting standards, developed and controlled by a specific national government. It is a key requirement that the new accounting standards be international in nature and application. With this in mind, the criteria used to evaluate IPSAS and IFRS were:

.1 **Strong due process** – both IPSAS and IFRS are developed through a transparent independent process with strong due process;

.2 **Full accruals basis** – this is the worldwide standard for accounting principles, and is a fundamental principle of both IPSAS and IFRS;

.3 **Consistent with future trends** – since IPSAS and IFRS are closely related, and both are the only internationally-accepted accounting standards in their respective markets, both may be considered as being consistent with future trends. IPSAS are relatively new and, in that context, the take-up among national governments is strong, whilst many countries have adopted IPSAS-based or IPSAS-consistent standards of their own;

.4 **Compatible software available** – research has indicated that either IPSAS or IFRS are compatible with all major accounting software packages, so this would not be a deciding factor;

.5 **Topic coverage** – IFRS has a greater coverage of topics than IPSAS. However, IPSAS also states that, where there is no relevant IPSAS, IFRS should be applied, thus addressing this issue. IPSAS is designed to be complementary to IFRS;

.6 **Not-for-profit applicable** – IFRS is primarily designed for the private sector, and a direct application of IFRS would lead to misleading accounts, particularly in accounting for non-revenue generating assets and for 'donated' income, neither of which would be recognized properly under IFRS. IPSAS specifically addresses these issues, and consequently would be more relevant. This was considered to be the primary reason for selecting IPSAS over IFRS, as it could be adopted without amendment; and

.7 **Compatible training and education materials available** – there is a much broader and more comprehensive set of training and education materials available for IFRS. However, much of this is also applicable to IPSAS and the development of additional material would be required for the specific areas of difference.

15 On this basis, the TFAS recommended the adoption of IPSAS, which was then approved by the HLCM. The proposal made is that IPSAS should replace UNSAS for all UN system organizations from 2010.

16 As noted above, the Secretariat has recently become actively involved in the TFAS project, and concurs with the group recommendation that IPSAS is the most appropriate replacement for UNSAS. Formal, detailed, proposals to amend the Organization's Financial Regulations and Rules will be submitted to Council in due course.

Implications for the future

17 A change in the Organization's accounting standards from UNSAS to IPSAS will result in a number of changes in different areas. A full impact analysis will be conducted during 2006, to prepare the ground for the change, but the key areas may be summarized as:

.1 **Change in format and content of accounts** – clearly, this will be the major impact of the IPSAS change. The format of accounts required under IPSAS will be significantly different to that provided for under UNSAS. We will be preparing a 'dummy' set of accounts under IPSAS for information during the course of the year, to highlight the differences. The substance will also change, the following being the main areas:

  .1 Fixed Assets – presently, the purchase of fixed assets (that is, those assets which have a useful life of more than one year), typically but not exclusively in the Headquarters Capital Fund, are shown as expenditure in the year of purchase. IPSAS, in common with generally accepted accounting practice, requires that these assets be shown on the balance sheet, and a charge for depreciation of the assets be made in the expenditure statement, effectively spreading the cost of the assets over their useful life;

  .2 Inventory – presently, purchases of stock for IMO Publications are shown in the year of purchase. IPSAS will require this stock to be shown on the

Balance Sheet as an asset, until it is sold, so that the expenditure in the year reflects the cost of books sold, not of books bought;

.3 Liabilities – there is likely to be a requirement to show as a liability on the Balance Sheet items which are presently simply disclosed in notes to the accounts. This will have the impact of directly reducing the Organization's accumulated surplus, to more accurately show the position of the various Funds. Examples of those which may require inclusion in the Balance Sheet include the After Service Health Insurance (ASHI) liability and accrued annual leave and repatriation costs for existing staff; and

.4 Recognition of expenditure – a preliminary analysis indicates that it may be a requirement to record expenditure on the basis of services (or goods) delivered, rather than simply at the time of contracting. This will change the timing of expenditure recording significantly, but will simplify the existing Unliquidated Obligation (ULO) recording procedure dramatically. The first year of a change to such a policy would show a reduction in expenditure, but there would be little impact after that;

.2 **Budgeting changes** – the change in the accounting for fixed assets noted above may require some re-think of the process for budgeting for fixed assets. The Organization's budget is based on cash requirements, i.e. requirements to purchase assets in the year, whilst the expenditure report in the financial statements will reflect not the cost of purchases, but the depreciation charge on all assets held. This will produce a mismatch if the situation is not carefully addressed. This is a major issue for several UN organizations, but is primarily an issue for the Organization with regard to the Headquarters Capital Fund, as most capital expenditure is ring-fenced there;

.3 **System changes** – related to the above, in order to gather and control the information required for the above, particularly with regard to the fixed assets and Publications inventory, it will be necessary to make some changes in SAP and specifically will require the implementation of one additional module for fixed assets. In addition to the information for the accounts, this will have the added benefit of providing improvements in tracking and controlling our assets and linking the asset register directly to the purchasing module;

.4 **Financial Regulations and Financial Rules** – the Organization's Financial Regulations and Financial Rules make specific reference to accounting treatments, not all of which will be consistent with IPSAS. In order to introduce IPSAS, appropriate amendments to the Financial Regulations and Financial Rules will have to be made, and have these approved through the appropriate procedure; and

.5 **Training requirements** – the changes in technical accounting and reporting will be significant and staff in Financial Services and Management Account Services will require training to familiarize them with the new requirements.

18 It is anticipated that the change in accounting standards will bring benefits both for the Organization and the UN system as a whole. It will standardize the accounting practices to a greater degree than at present; improve the financial reporting and transparency across the system; reduce the burden of maintaining a separate accounting standard system, increase the

amount of documentation and guidance available to organizations implementing the new standards; and, most importantly, will provide added credibility to UN system accounts which are compiled in accordance with independently set and internationally recognized standards, rather than with the system's own standards. Nevertheless, the new system will constitute a significant change and will present a number of challenges to overcome before a successful implementation can be made. Further information on the impact of introducing IPSAS, and any costs required for system changes and training, will be submitted to Council and Assembly in due course.

Indicative timetable and costs

19 The major milestones on the steps to IPSAS implementation may be outlined as follows:

.1 **2006 –** Impact assessment. Identify the major impacts of the change: review IPSAS standards in detail to determine additional information requirements; determine how these might be met; identify training needs. Develop 'dummy' IPSAS format accounts for information;

.2 **2007 –** Requirements development and costing. Determine in detail the systems and other work required, training courses, and include these in the budget proposals for 2008/09. Consideration in detail of the impact of IPSAS on format and content of budgets themselves, particularly for capital expenditure items;

.3 **2008** – Procurement of system's consultants based on a detailed requirements definition. Training of key staff. Preliminary work on information gathering, for example on fixed assets;

.4 **2009** – Implementation and testing of system and process changes, broader training of staff. Implementation of any changes required in the budgeting format to take account in the 2010/11 biennium. Completion of data gathering exercise; and

.5 **2010** – Go-live of updated systems and processes from 1 January. Re-working of 2008/09 accounts in IPSAS format for comparative purposes.

20 One of the objectives of the impact assessment referred to above will be to identify more detailed milestones and consequential timings for the remainder of the process.

21 Detailed costings will be developed in line with the milestones outlined above. These will be driven largely by the extent of system change required, but an indicative discussion with SAP system consultants is expected to indicate that system costs alone are likely to be in the region of £100,000, in addition to the internal staff time required for requirements specification, system development and testing. It is anticipated that the major systems and process changes required will be the implementation of the SAP Fixed Assets module and changes to the SAP budgeting, purchasing and inventory modules. The fact that the work will not be undertaken for some three years also means that there is likely to be variation in the market rates for such services over that time.

22 During the course of the implementation by the Organization of the new system, resource, expertise and experience will be drawn from the ongoing work of the TFAS and, through that, the experience of other organizations as they move through the same path. The TFAS originally

had a budget of $881,000 for the initial phase of the project. For the years 2006-2009, during implementation of IPSAS, the budget will be $4,427,000, funded jointly by the UN system organizations, of which the Organization will be required to contribute some $18,000 over the life of the project.

Conclusion

23 A system such as SAP will typically go through a significant upgrade on an approximately five-year cycle, if not more often. The scope of such an upgrade can vary greatly, depending on the requirements of the Organization, from a simple technological upgrade leaving the remainder of the implementation largely untouched, to a full re-implementation of the system. The latter is unlikely to be necessary for the Organization, but we would take the opportunity of an upgrade to determine whether new technology has become available, which would allow us to further streamline our procedures and improve our reporting.

24 With this and the two unavoidable systems amendments noted above – the change in HR and payroll system, and the changes required by a move to IPSAS – in mind, it would be prudent for the Organization to plan the three pieces of work to coincide; to provide the most cost-effective and manageable solution; to avoid re-doing work and making inconsistent changes; and to provide a clear focus. With an integrated system, any change in one area cannot be seen in isolation, and this also supports an integrated approach to the three strands of work. Synergies and certain economies of scale will make it more cost effective to do the work together rather than as independent projects.

25 Over the coming years, therefore, the Organization will continue to develop its existing system and refine it where possible, whilst developing plans and costings for a system upgrade; implementation of HR and payroll improvements; and introduction of IPSAS during 2009. Indicative costing indicates some £250,000 will be needed for the HR and payroll implementation, if this option is selected; £100,000 for the IPSAS amendments required; and a similar sum for the upgrade itself, plus internal resource costs. More detailed plans and costs will be presented to the Council in due course.

Action requested of the Council

26 The Council is invited to take note of the information contained in this document and comment as appropriate.