



EUROPEAN  
COURT  
OF AUDITORS

Report on the annual accounts of the Shift-2-Rail Joint Undertaking for the  
financial year 2017

Together with the Joint Undertaking's reply

## CONTENTS

	Paragraph
Introduction	1 - 12
Establishment of the Shift2Rail Joint Undertaking	1 - 2
Governance	3 - 6
Objectives	7 - 8
Resources	9 - 11
The Commission's evaluation	12
Opinion	13 - 25
Opinion on the reliability of the accounts	14
Opinion on the legality and regularity of revenue underlying the accounts	15
Opinion on the legality and regularity of payments underlying the accounts	16
Responsibilities of management and those in charge of governance	17 - 19
Auditor's responsibilities for the audit of the accounts and underlying transactions	20 - 25
Budgetary and financial management	26 - 32
Implementation of the 2017 budget	26 - 27
Multiannual budget implementation under Horizon 2020	28 - 32
Internal controls	33 - 37
Internal control framework	33 - 36
Procurement procedures	37
Other issues	38
Leverage of contributions from industry members	38
Information on the Commission's evaluations	39 - 40
Annex - Follow-up of previous years' comments	

The Joint Undertaking's reply

## **INTRODUCTION**

### ***Establishment of the Shift2Rail Joint Undertaking***

1. The Shift2Rail (S2R) Joint Undertaking, located in Brussels, was set up in June 2014<sup>1</sup> for a period of ten years and started working autonomously on 24 May 2016. The Joint Undertaking began autonomous operations in 2016 and this year's accounts are the second set of S2R financial statements audited by the ECA.
2. The S2R Joint Undertaking is a public-private partnership in the rail sector. The founding members are the European Union (EU), represented by the Commission and rail industry partners (key stakeholders, including rail equipment manufacturers, railway companies, infrastructure managers and research centres). Other entities may participate in the Joint Undertaking as associated members.

### ***Governance***

3. The governance structure of the S2R Joint Undertaking includes the Governing Board, the Executive Director, the Scientific Committee, and the States Representatives Group.
4. The Governing Board is composed of twenty-two members, with two representatives from the Commission and one representative from each industry member. It is responsible for the strategic orientation and operations of the Joint Undertaking and supervises the implementation of its activities. The Executive Director is responsible for the day-to-day management of the Joint Undertaking.
5. The Scientific Committee and the States Representatives Group are advisory bodies. The Scientific Committee provides advice on the scientific and technological priorities to be addressed in the Joint Undertaking's annual work programmes. The States Representatives Group represents EU Member States and countries associated with the Horizon 2020

---

<sup>1</sup> Council Regulation (EU) No 642/2014 of 16 June 2014 establishing the Shift2Rail Joint Undertaking (OJ L 177, 17.6.2014, p. 9).

Research Framework Programme. The Group may offer opinions on the strategic orientations of the Joint Undertaking and on the links between S2R activities and relevant national or regional research and innovation programmes.

6. The Statutes of the S2R Joint Undertaking also stipulate:

- a specific advisory role for the European Union Agency for Railways in contributing to the definition and implementation of S2R work plans, and ensuring that S2R activities lead to technical standards guaranteeing interoperability and safety;
- the establishment of Innovation Programme Steering Committees, comprising representatives of the founding members and associated members, and of the S2R Programme Office, in charge of the technical input and implementation of each Innovation Programme;
- the possibility of creating working groups of experts to assist the Joint Undertaking in carrying out its tasks.

### **Objectives**

7. The S2R Joint Undertaking was created to provide a platform for the rail sector to work together to drive forward innovation to enhance the competitiveness of the railway system and to strengthen the rail transport system in Europe. A key initiative in achieving this goal is the creation of a Single European Railway Area (SERA)<sup>2</sup>.

8. The Joint Undertaking seeks to develop, integrate, demonstrate and validate innovative technologies and solutions that uphold the strictest safety standards, with a view to achieving:

- a 50 % reduction in the life-cycle cost of rail transport;
- a 100 % increase in the capacity of the railway transport system;

---

<sup>2</sup> Further information on the Joint Undertaking's activities is available on its website: <http://shift2rail.org>.

- a 50 % increase in the reliability and punctuality of rail services;
- the removal of the remaining technical obstacles to interoperability and efficiency;
- a reduction in negative externalities linked to railway transport, in particular noise, vibrations, emissions and other environmental effects.

### **Resources**

9. The maximum EU contribution to the activities of the S2R Joint Undertaking is 450 million euro, to be financed from Horizon 2020. This amount includes 52 million euro earmarked for the Horizon 2020 Transport Work Programme 2014-2015 (Lighthouse projects) so far managed by the European Commission, resulting in 398 million euro allocated to the S2R Joint Undertaking<sup>3</sup>. The industry members of the Joint Undertaking are to contribute resources of at least 470 million euro<sup>4</sup>, consisting of at least 350 million euro of in-kind and cash contributions to the Joint Undertaking's operational activities and administrative costs, together with at least 120 million euro of in-kind contributions to additional activities<sup>5</sup>.

10. The administrative costs of the S2R joint Undertaking are limited to 27 million euro, to be covered by the member's cash contributions, divided equally on an annual basis between the EU and the industry members<sup>6</sup>.

11. In 2017, the final budget for the S2R Joint Undertaking was 44,1 million euro (2016: 52,3). At 31 December 2017, the Joint Undertaking employed 19 staff (2016: 17). The lower

---

<sup>3</sup> Article 3(1) of Regulation (EU) No 642/2014.

<sup>4</sup> Article 4(1) of Regulation (EU) No 642/2014.

<sup>5</sup> As provided for in Article 4(2)(b) of Regulation (EU) No 642/2014, additional activities are outside the work plan and budget of the Joint Undertaking but contribute to the objectives of the S2R Master Plan. In line with Article 4(4) of the same regulation, the costs of additional activities must be certified by an independent external auditor and are not subject to audit by the Joint Undertaking, the ECA or by any EU body.

<sup>6</sup> Article 16(2) of the Statutes of the S2R Joint Undertaking (Annex I of Regulation (EU) No 642/2014).

final budget for 2017 was a direct consequence of the confirmation of the European Commission to continue to administer the Lighthouse Projects<sup>7</sup>.

### ***The Commission's evaluation***

12. The Commission completed the interim evaluation of the Joint Undertaking's activities in June 2017, which was followed by an action plan prepared by the Joint Undertaking to address the recommendations raised in the evaluation. On this occasion, we include a section related to the Joint Undertaking's Action Plan in response to the interim evaluation, which is intended only for information purposes and does not form part of our audit opinion or observations.

### **OPINION**

13. We have audited:

- (a) the accounts of the Joint Undertaking which comprise the financial statements<sup>8</sup> and the reports on the implementation of the budget<sup>9</sup> for the financial year ended 31 December 2017, and
- (b) the legality and regularity of the transactions underlying those accounts, as required by Article 287 of the Treaty on the Functioning of the European Union (TFEU).

### ***Opinion on the reliability of the accounts***

14. In our opinion, the accounts of the Joint Undertaking for the year ended 31 December 2017 present fairly, in all material respects, the financial position of the Joint Undertaking at 31 December 2017, the results of its operations, its cash flows, and the changes in net assets for the

<sup>7</sup> Article 3(1) (b) of Regulation (EU) No 642/2014 foresees an additional EU contribution of 52 million euro to the S2R Joint Undertaking in case it takes over the management of the Horizon 2020 Transport Work Programme 2014-2015 (so-called Lighthouse projects).

<sup>8</sup> The financial statements comprise the balance sheet, the statement of financial performance, the cash flow statement, the statement of changes in net assets and a summary of significant accounting policies and other explanatory notes.

<sup>9</sup> The reports on the implementation of the budget comprise the reports which aggregate all budgetary operations and the explanatory notes.

year then ended, in accordance with its Financial Regulation and with accounting rules adopted by the Commission's accounting officer. These are based on internationally-accepted accounting standards for the public sector.

***Opinion on the legality and regularity of revenue underlying the accounts***

15. In our opinion, revenue underlying the accounts for the year ended 31 December 2017 is legal and regular in all material respects.

***Opinion on the legality and regularity of payments underlying the accounts***

16. In our opinion, payments underlying the accounts for the year ended 31 December 2017 are legal and regular in all material respects.

***Responsibilities of management and those in charge of governance***

17. In accordance with Articles 310 to 325 of the TFEU and the Joint Undertaking's Financial Regulation, management is responsible for the preparation and presentation of the accounts on the basis of internationally-accepted accounting standards for the public sector and for the legality and regularity of the transactions underlying them. This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to fraud or error. Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them. The Joint Undertaking's management bears the ultimate responsibility for the legality and regularity of the transactions underlying the accounts.

18. In preparing the accounts, management is responsible for assessing the Joint Undertaking's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting.

19. Those in charge of governance are responsible for overseeing the entity's financial reporting process.

***Auditor's responsibilities for the audit of the accounts and underlying transactions***

20. Our objectives are to obtain reasonable assurance about whether the accounts of the Joint Undertaking are free from material misstatement and the transactions underlying them are legal and

regular and, on the basis of our audit, to provide the European Parliament and the Council or other respective discharge authorities with a statement of assurance as to the reliability of the accounts and the legality and regularity of the transactions underlying them. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit will always detect a material misstatement or non-compliance when it exists. These can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these accounts.

21. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the accounts and the legality and the regularity of the transactions underlying them. The procedures selected depend on the auditor's judgment, including an assessment of the risks of material misstatement of the accounts and of material non-compliance of the underlying transactions with the requirements of the legal framework of the European Union, whether due to fraud or error. In making those risk assessments, internal control relevant to the preparation and fair presentation of the accounts and legality and regularity of underlying transactions is considered in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. An audit also includes evaluating the appropriateness of accounting policies used, the reasonableness of accounting estimates made by the management and the overall presentation of the accounts.

22. For revenue, we verify the subsidy received from the Commission and assess the Joint Undertaking's procedures for collecting fees and other income.

23. For expenditure, we examine payment transactions when expenditure has been incurred, recorded and accepted. This examination covers all categories of payments (including those made for the purchase of assets) at the point they are made.

24. In preparing this report and Opinion, we considered the audit work which the independent external auditor performed on the Joint Undertaking's accounts as stipulated in Article 208(4) of the EU Financial Regulation<sup>10</sup>.

25. The comments which follow do not call the ECA's opinion into question.

---

<sup>10</sup> Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council (OJ L 298, 26.10.2012, p. 1).

## **BUDGETARY AND FINANCIAL MANAGEMENT**

### ***Implementation of the 2017 budget***

26. The final 2017 budget included commitment appropriations of 68,6 million euro and payment appropriations of 44,1 million euro. The implementation rates for commitment and payment appropriations were 94 % and 79 % respectively. Most of the payments made by the Joint Undertaking in 2017 were pre-financing payments for Horizon 2020 projects selected under the 2017 calls for proposals.

27. At the end of 2017, the Joint Undertaking had unused payment appropriations from previous years of around 7,6 million euro. This situation shows weaknesses in the budget planning process, which, however, cannot be fully controlled by the Joint Undertaking.

### ***Multiannual budget implementation under Horizon 2020***

28. Out of the maximum of 398 million euro of EU cash contribution to be allocated to the S2R Joint Undertaking over its lifespan, by the end of 2017, the EU had contributed in cash a total amount of 83,2 million euro.

29. Out of the at least 350 million euro of contributions to be made by the industry members to the operational activities and administrative costs of the Joint Undertaking over its lifespan, by the end of 2017, the members had reported in-kind contributions of 34,9 million euro for operational activities, of which 3 million euro had been certified. In addition, the Governing Board had validated cash contributions by the industry members to the Joint Undertaking's administrative costs of 4,9 million euro.

30. Out of the at least 120 million euro of industry members' contributions to be made to additional activities outside the work programme of the Joint Undertaking, by the end of 2017 the members had already reported 130million euro (108 %), of which 86,3 million euro had been certified. However, as we have no right to audit the members' in-kind contributions to additional activities, we cannot provide an opinion on their nature, quality and quantity.

31. Consequently, by the end of 2017, the total contributions from industry members, amounted to 169,8 million euro (of which 76 % are contributions to additional activities), compared to the EU cash contribution of 83,2 million euro (see also paragraph 38).

32. Out of the maximum operational and administrative budget for the Joint Undertaking of 411,5 million euro<sup>11</sup>, by the end of 2017, the Joint Undertaking made commitments of 158,8 million euro and payments of 78,6 million euro. This shows that the Joint Undertaking has currently signed interdependent multiannual grant agreements and procurement contracts for the implementation of 39 % of the S2R research and innovation programme, in line with the Joint Undertaking's multi-annual work programme.

## **INTERNAL CONTROLS**

### ***Internal control framework***

33. The Joint Undertaking has set up reliable ex-ante control procedures based on financial and operational desk reviews. The situation at end of 2017 showed that the most important internal control standards were largely implemented with some actions remaining to be completed in 2018 such as carrying out the testing of the Business Continuity Plan.

34. The Common Audit Service of the Commission (CAS) is responsible for the ex-post audit of Horizon 2020 project cost claims. In 2017, the Joint Undertaking - together with the Common Audit Service (CAS) of DG RTD - launched the first ex-post audit of a random sample of Horizon 2020 interim cost claims of which the results, however, will only be reported in in the Joint Undertaking's annual activity report 2018.

35. Based on an assessment of the Joint Undertaking's internal control system and substantive testing of revenue, payment, grant and procurement operations, the audit results provided us with reasonable assurance that the overall residual error rate for the Joint Undertaking is below materiality.

---

<sup>11</sup> This amount includes the maximum EU cash contribution to the Joint Undertaking's operational and administrative costs and the industry members' cash contribution to the Joint Undertakings' administrative costs of 13,5 million euro.

36. At the end of 2017, the Commission's common Horizon 2020 grant management and monitoring tools had not finished the specific developments needed for the processing of the Joint Undertaking's in-kind contributions.

### ***Procurement procedures***

37. Some qualitative shortcomings were observed in the Joint Undertaking's open procedure for the procurement of communication and event services of an estimated budget of 1,2 million euro over 4 years.

## **OTHER ISSUES**

### ***Leverage of contributions from industry members***

38. One of the main objectives of the Joint Undertaking is to leverage contributions from industry members in the area of its activities<sup>12</sup>. The minimum leverage factor to be achieved according to the Joint Undertaking's founding regulation is 0,88<sup>13</sup> if only the industry members' contributions to the activities directly covered by the Joint Undertaking's work programme are considered. The minimum leverage factor increases to 1,18<sup>14</sup> if the industry members' contributions to additional activities outside the Joint Undertaking's work programme are equally included. However, as we have no right to audit in-kind

---

<sup>12</sup> Recital 10 of Regulation (EU) No 642/2014 states that substantial participation of industry is an essential element of the Shift2Rail (S2R) initiative. It is therefore fundamental that the public budget for the S2R initiative be at least matched by contributions from industry.

<sup>13</sup> Minimum contributions of the industry members to the operational activities of the Joint Undertaking (350 million euro) divided by the maximum EU cash contribution to the Joint Undertaking (398 million euro).

<sup>14</sup> Total of minimum contributions of the industry members to the Joint Undertaking's operational and additional activities (470 million euro) divided by the maximum EU cash contribution to the Joint Undertaking (398 million euro).

contributions to additional activities we cannot provide an opinion on the nature, and quality of such contributions<sup>15</sup>.

### **INFORMATION ON THE COMMISSION'S EVALUATIONS**

39. The Commission's Interim Evaluation<sup>16</sup> on S2R Joint Undertaking's activities covered the period 2014-2016, and was carried out with the assistance of independent experts as foreseen in the S2R Joint Undertaking Council Regulation<sup>17</sup>. The evaluation covered the performance of the Joint Undertaking in terms of relevance, efficiency, effectiveness, coherence, and EU added value, with additional consideration of openness and transparency. The results of the evaluation were taken into account in the report that the Commission sent to the European Parliament and Council in October 2017<sup>18</sup>.

40. In response to the recommendations raised by the evaluators<sup>19</sup>, the Joint Undertaking prepared an Action Plan adopted by the Governing Board on 28 June 2018. While not all recommendations raised in the Interim Evaluation will be addressed under the current Financial Framework Programme<sup>20</sup>, some actions included in the Action Plan have already

---

<sup>15</sup> In accordance with article 4 (4) of Regulation (EU) No 642/2014 the cost of additional activities are certified by an independent external auditor appointed by the Joint Undertaking. The cost for such activities shall however, not be audited by the Joint Undertaking or any Union body.

<sup>16</sup> Interim evaluation of the S2R Joint Undertaking (2014-2016) operating under Horizon 2020. <https://ec.europa.eu/research/evaluations/pdf/s2r.pdf>

<sup>17</sup> Article 11 of S2R Joint Undertaking Council Regulation (EU) No 642/2014.

<sup>18</sup> Commission Staff Working Document. Interim Evaluation of the Joint Undertakings operating under Horizon 2020 {SWD(2017) 339 final}.

<sup>19</sup> Specific recommendations include the need to increase the collaboration with the other Transport Joint Undertakings (SESAR, Clean Sky and FCH); to increase the balance of participants in S2R activities; to make further use of the Joint Undertaking Scientific Committee, of the European Rail Research Advisory Council (ERRAC), and of the advisory bodies in order to provide technical and strategic advice; and to review the current Key Performance Indicators of the Joint Undertaking, that are considered to be too many, and in some issues, inappropriate.

<sup>20</sup> The Joint Undertaking's Action Plan recognises that certain recommendations such as the need to improve the balance of participants in the Joint Undertaking, or to increase focus on key

been initiated<sup>21</sup>, while others, in accordance with their nature and the current legal framework, are expected to be implemented in the period 2018 to 2020<sup>22</sup>.

This Report was adopted by Chamber IV, headed by Mr Neven MATES, Member of the Court of Auditors, in Luxembourg at its meeting of 2 October 2018.

*For the Court of Auditors*

Klaus-Heiner LEHNE

*President*

---

societal challenges, were not sufficiently covered in S2R and will need to be further addressed in the next programming period.

<sup>21</sup> Regular contacts with the other Joint Undertakings to create synergies between the different programmes are already in place; the Lump Sum Grants scheme has been introduced in the 2018 Annual Work Programme to enhance simplification.

<sup>22</sup> Actions to be implemented include: the invitation to associated members of the Joint Undertaking to increase their commitment in S2R in order to allow further participation of third parties through the associated members activities; the selection of new members of the Scientific Committee; a review of the S2R Multi-Annual Action Plan (Part B) to align it with the S2R executive view adopted by the Governing Board on October 2017 (Part A); and the establishment of a new KPI model in line with the S2R Council Regulation Objectives.

**Annex****Follow-up of previous years' comments**

<b>Year</b>	<b>The ECA's comment</b>	<b>Status of corrective action (Completed / Ongoing / Outstanding)</b>
<b>2016</b>	<b>Anti-fraud strategy</b>	
	The Commission's research anti-fraud strategy is mandatory for the S2R Joint Undertaking. However, at the end of 2016, the Joint Undertaking had not yet performed a specific anti-fraud risk assessment, nor had it established an action plan for the implementation of its own anti-fraud strategy, based on the methodology provided by the Commission.	<b>Completed</b>

### THE JU'S REPLY

27. The usual budget process foresees that for each financial year the Commission pays to the Joint Undertaking the first instalment around March only. The Joint Undertaking therefore considered the full amount of unused payment appropriations from previous years in its budget planning for 2017, to cover the payments of the first quarter in 2018.

37. With regard to the procurement procedure for a communication and event services' framework contract, the Joint Undertaking decided not to introduce minimum financial capacity in order not to discourage the participation of SMEs to the call for tender, a risk that the Joint Undertaking wished to mitigate. In fact, the definition of minimum levels of financial capacity are well known barriers for new entrants.

In the same procedure, Lot 4 was cancelled because the technical solution proposed by the winning tender allowed to merge the services planned initially for two lots into one lot. This solution resulted in saving financial resources. In this context, the Joint Undertaking fully complied with Article 114 of the Financial Regulation ("Cancellation of a procurement procedure").

38. The S2R Joint Undertaking would like to draw attention to the fact that the members other than the Union already provided certified IKAA well beyond the regulatory target. These contributions are certified in accordance with International Audit Standards. The leverage factor according to the Joint Undertaking's founding regulation is 1.24<sup>1</sup> and 1,66<sup>2</sup> respectively when considering the Members other than the Union contributions' only.

---

<sup>1</sup> Minimum contributions of the industry members to the operational activities of the Joint Undertaking (350 million euro) divided by the maximum EU cash contribution to the Joint Undertaking allocated by the S2R Regulation to the Members other than the Union (282.5 million euro).

<sup>2</sup> Considering the total of minimum contributions of the industry members to the Joint Undertaking's operational and additional activities (470 million euro)