EUROPEAN COMMISSION
EUROSTAT

Directorate C: National Accounts, Prices and Key Indicators
Task Force EPSAS

EPSAS FTIcell 15/03

Luxembourg, 4 June 2015

EPSAS Cell on First Time Implementation

To be held in Luxembourg

on 12 June 2015, starting at 10:00,

BECH Building, B3/464

Item 3 and 4 of the Agenda

First Time Implementation guidance:
Kick-off document

Paper by Eurostat

- *for discussion*

First Time Implementation guidance:

Kick-off document

Introduction

1. This document is to initiate the discussion of the cell on First Time Implementation by summarising the discussions held so far in the EPSAS Task Force Governance, notably at its meeting of March 2015.[1]

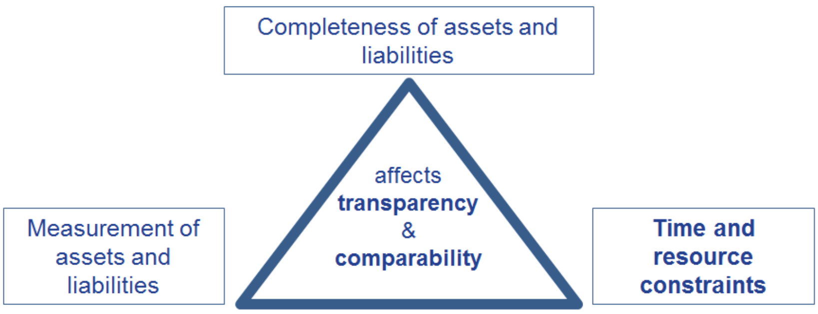
2. It summarises:

> What was referred to as the "First Time-Adoption Dilemma" and the three C's: Compromises that need be done on a basis of a consensus, outlined in a Cookbook.
>
> The IPSASB approach to First Time Adoption.
>
> EPSAS needs: The scope of assets and liabilities to be included in the opening balance sheet and their measurement, providing as far as possible a preferred hierarchy.

3. The paper concludes by inviting cell participants to discuss the above issues and in particular the issue of the scope of assets and liabilities to be included in the opening balance sheet and guidance on measurement. In particular the meeting should discuss the approaches taken by the countries of the cell participants to these two key issues in order to inform the eventual EPSAS proposals. Furthermore the question of subsequent measurement (restatement) may also be discussed by participants.

The First Time-Adoption Dilemma

4. The first-time dilemma describes and contrasts the wish to have complete presentation and the optimal, accurate measurement or valuation of those assets and liabilities in the Opening Balance Sheet (OBS), against the constraints of time and resources.



[1] Discussions based on the presentations by Thomas Müller-Marqués Berger (FEE) at the Task Force EPSAS Governance meetings, 21 November 2014 and 17/18 March 2015.

5. As a consequence of the dilemma, first-time adopters have to make decisions regarding:

- **Completeness (Recognition)**

  How complete should the coverage be of assets and liabilities in the OBS: Is it necessary to accept relief (or exclusions) from complete coverage?

- **Measurement**

  How prescriptive should the measurement (valuation) requirements be for those assets and liabilities covered in the OBS: how far should there be flexibility offered when measuring (valuing those assets and liabilities), as compared to what may be considered the best measurement approaches?

6. It is important to keep in mind that proposals on recognition and measurement should take into account that:

- Financial statements aim at providing a true and fair presentation of the financial position and performance of the entity. Exclusions from coverage or flexibility on valuation which do not materially affect this principle are easier to justify than those which would or might affect this.

- OBSs, even if they are compiled using certain agreed exclusions or flexibilities, should provide a suitable basis for the longer-term – for future BSs, when EPSAS will be in place.

The IPSASB approach to First Time Adoption

7. IPSAS requirements for recognition and measurement already exist for most or all important classes of assets and liabilities. This permits a "top-down" approach to be followed in the IPSAS First Time Adoption standard (IPSAS 33), which is designed to apply to entities adopting accrual-based IPSAS for the first time.

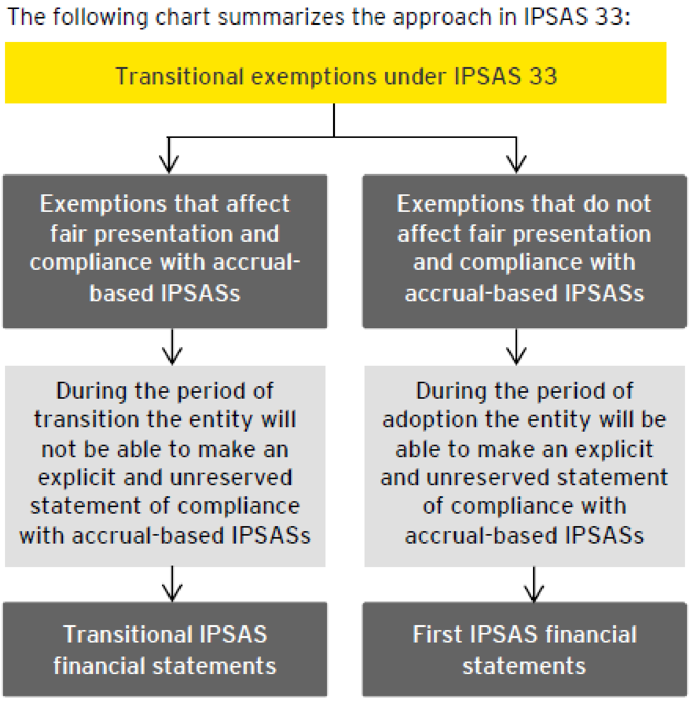
See Annex 1 for a summary of exempted BS items according to IPSAS 33: Those where a first-time adopter is not required to recognize assets and/or liabilities during a 3 year relief period (if they were not recognized under the previous basis of accounting), or is offered relief on the approach to their measurement.

8. Concerning the recognition of assets and liabilities in general (i.e. the completeness of the coverage of assets and liabilities), no concessions are made except for capitalization of borrowing costs. However, the standard allows for a transitional relief period of 3 years for the recognition of certain assets (e.g. property, plant and equipment) and liabilities (e.g. pension liabilities). This is deemed to have an effect on fair presentation of a first time adopter's financial statements.

9. Concerning measurement, a first-time adopter should apply IPSASs in measuring all recognized assets and liabilities in its OBS. However IPSAS 33 describes some exemptions for the transitional period and a <u>hierarchy of measurement</u>: In principle,

measurement at first-time adoption is as required at cost, but for certain assets and liabilities fair value can be used as deemed cost when reliable cost information about the asset/liability is not available. The use of deemed cost approach has no effect on fair presentation, but it has the consequence that any subsequent depreciation is based on the fair value as its deemed cost determined at the date of the OBS and starts from the date that the deemed cost has been determined.

10. The following chart summarises the reliefs or exemptions offered by IPSAS 33 and their relationship to IPSAS fair value measurement, showing the consequences in terms of whether the resulting financial statements are deemed to be "transition" in IPSAS terms or not..



Source: IPSAS Outlook, March 2015.
http://www.ey.com/Publication/vwLUAssets/IPSAS_Outlook_March_2015/$FILE/EY-ipsas-outlook-mar-2015.pdf

EPSAS needs

11. In contrast to IPSAS, EPSAS does not have accounting requirements or standards defined at this stage and therefore the "top-down" approach of reliefs is not applicable. Nevertheless, irrespective of the previous basis of accounting, <u>all</u> entities that will be required to implement EPSAS would have to prepare an EPSAS opening balance sheet. Therefore preparations, primarily for those entities that have not yet prepared an OBS/balance sheets in the past, should be started before EPSAS standards will be in place. Sufficient specific guidance has to be given in order to define what should be recognised in the OBS and on which measurement bases. This would help to reach an acceptable starting level for implementing EPSAS.

12. As discussed in the Task Force Governance meeting of March 2015, EPSAS principles in themselves would not provide sufficient guidance for producing these opening balance sheets, more specific guidance will be necessary. It is also important to set clear priorities for the first time adopters, and the main focus and priority should presumably be on the stock-taking and recognition of assets and liabilities. The issue of measurement requirements should at this stage be of secondary importance.

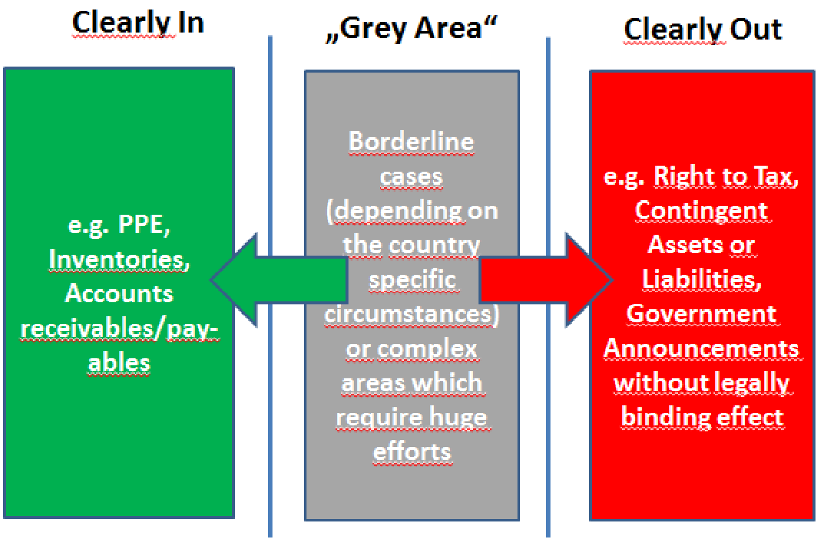
13. For EPSAS there is therefore a need to define clearly the following two aspects:

A. The scope of assets and liabilities to be included in the opening balance sheet.

From a cost-effectiveness point of view, "materiality" should be considered without risking the establishment of a reliable information basis on the stocks of assets and liabilities. Scoping out of assets/liabilities could also take into account the timing or the specificity of a transaction (e.g.: intangible assets older then X years, military assets, emission trading rights, etc.).

Guidance on the scope of assets and liabilities to be included in the OBS could start with the ones that should clearly be not considered in the OBS ("Clearly Out" of the OBS) and all the others would be included ("Clearly in") , except for those borderline cases ("Grey area") which need to be analyzed and reported.

Scoping of assets and liabilities to be included in the OBS



Source: Presentation by Thomas Müller-Marqués Berger (FEE) at the meeting of TF EPSAS Governance, 21 November 2014.

B. The guidance for measurement, providing as far as possible a preferred hierarchy.

The first valuation results for assets and liabilities should allow for ongoing accrual accounting – that is, in subsequent accounting periods - on the basis of the OBS. In this regard, guidance for subsequent measurement during the transition period also needs to be provided

The measurement hierarchy could refer to specific groups of assets and liabilities, analogous to IPSAS 33 on FTA:

- Primarily use historic values like acquisition or construction cost (less accumulated depreciation), where information is available at reasonable cost and with reasonable effort.

- Otherwise, if historic values are not available or could not be established with reasonable effort, the use of alternative valuations as "deemed cost" can be foreseen e.g.:

  - intangible assets: indexed fair values at the date of acquisition
  - land: local average costs based on comparable transactions
  - tangible assets (buildings/infrastructure): indexed fair value at the date of acquisition
  - interest in other entities: equity method

Such a hierarchy might not be suitable for all types of assets and liabilities, for example for financial instruments or investment property, the use of the current value, could be considered necessary. In these cases the use of other alternatives and guidance on the hierarchy of measurement to be applied, should be given for each type of asset and liability scoped in. Different guidance may be developed for different types of assets and liabilities.

Points for discussion by cell participants

14. For the compilation of OBS, discuss the priorities and guidance needed for first time adopters of accruals accounting regarding the recognition and measurement of assets and liabilities, taking into consideration the possibility of a transitional period.

A. Completeness (recognition)

- Taking as a reference the minimum requirements for the presentation of the statement of financial position for IPSAS (see Annex 2), or using as the reference point the national breakdowns or presentations of the balance sheet – (for as example as set out in the national Chart of accounts), participants are invited to outline any exemptions from recognition they have applied nationally.

- Discuss consistencies and differences between the approaches taken by the different countries of cell participants, and compare that with the approach taken by IPSAS 33.

- Discuss items that may not be required in the OBS, taking into account materiality, practicality and other issues.

B. Measurement

- Taking as a reference the minimum requirements for the presentation of the statement of financial position for IPSAS (see Annex 2), or using as the reference point the national breakdowns or presentations of the balance sheet (for as example as set out in the national Chart of accounts), participants are invited to outline national approaches taken to flexibility given on measurement for the OBS, or subsequent BSs, taking as a reference the approaches outlined above in para 13B.

- On the basis of that, discuss the preferred measurement hierarchy. (For the OBS and in subsequent periods)

C. Restatement / correction possibilities of the OBS.

- Applying the above mentioned specific guidelines for OBS would imply that the restatement of BS data could be necessary, when EPSASs standards are defined at a later point in time. Two general approaches can be considered:

- Adjustment of the OBS with consequential adjustments of all following years.
- Adjustment only of the OBS of the year of first full compliance with EPSAS (thereby only net equity would be impacted in the OBS).

- The question of restatement may also be discussed by participants, either at this point or later in the work on the cell.

ANNEX 1

IPSAS 33 approach for exemption related to opening balance sheet

What balance sheet items are (1) exempted according to IPSAS 33 and what are (2) not exempted?	
Current assets	**Current liabilities**
Cash and cash equivalents (2)	Trade payables and other payables (2)
Receivables from exchange transactions (2)	Provisions (current portion) (2)
Receivables from non-exchange transactions (1)	Finance lease obligations (1)
Inventories (1)	Current portion of borrowings (2)
Investments (1 – partly (FI))	Current employee benefit obligation (1 – partly)
Non-current assets	**Non-current liabilities**
Property, plant and equipment (1)	Non-current employee benefit obligation (1 – partly)
Investments (1 – partly (FI))	Non-current provisions (2 – only some , dismantling costs)
Intangible assets (1)	Borrowings (2)
Investment property (1)	Service concession liabilities (1)
Long-term receivables from exchange (2)/non-exchange transactions (1)	Deferred tax liabilities (1)

(1) Balance sheet items exempted according to IPSAS 33 (relief from IPSAS requirements)
(2) Balance sheet items not exempted according to IPSAS 33 (no relief from IPSAS requirements)

ANNEX 2

Extract from IPSAS 1 — Presentation of Financial Statements

Objective

1. The objective of this Standard is to prescribe the manner in which general purpose financial statements should be presented to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities. To achieve this objective, this Standard sets out overall considerations for the presentation of financial statements, guidance for their structure, and minimum requirements for the content of financial statements prepared under the accrual basis of accounting. The recognition, measurement, and disclosure of specific transactions and other events are dealt with in other IPSASs.

IPSAS 1 — Presentation of Financial Statements

(…)

Information to be Presented on the Face of the Statement of Financial Position

88. **As a minimum**, the face of the statement of financial position shall include line items that present the following amounts:

(a) Property, plant, and equipment;
(b) Investment property;
(c) Intangible assets;
(d) Financial assets (excluding amounts shown under (e), (g), (h) and (i));
(e) Investments accounted for using the equity method;
(f) Inventories;
(g) Recoverables from non-exchange transactions (taxes and transfers);
(h) Receivables from exchange transactions;
(i) Cash and cash equivalents;
(j) Taxes and transfers payable;
(k) Payables under exchange transactions;
(l) Provisions;
(m) Financial liabilities (excluding amounts shown under (j), (k) and (l));
(n) Minority interest, presented within net assets/equity; and
(o) Net assets/equity attributable to owners of the controlling entity.