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EPSAS issue paper on the accounting treatment of military assets

Paper by Ernst & Young on behalf of Eurostat
- for discussion

Accounting treatment of military assets with a view to financial reporting requirements under the future European Public Sector Accounting Standards (EPSAS)

12 April 2017

EY

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1. Objectives of the Issue Paper

The aim of this paper is to develop an analysis for Member States' discussion on how to account for military assets under the future EPSAS.

This paper takes into account:

- All publicly available information on the IPSASB meetings in which military assets were discussed;
- The existing approaches under the following international financial reporting frameworks, i.e. IPSAS, North Atlantic Treaty Organization (NATO) accounting framework, IFRS and ESA 2010; and
- The approaches taken at the accounting standard level in three Member States (Austria, Belgium and France).

The issues paper will address the following issues:

- What are the most important categories of military assets?
- For which of these categories do problematic points/issues arise with regards to definition, recognition, measurement and presentation?
- Which are the main practical difficulties and sensitivities that may arise with the recognition and measurement of military assets, and how could they be addressed?
- What are the advantages and disadvantages of the existing approaches to recognition and measurement?
- Which categories of military assets should be treated by future EPSAS standards or guidance taking into account materiality and comparability considerations?
- What are the consequences for a possible convergence between IPSAS and ESA?

The issue paper concludes with a suggestion for an approach that could be followed to organize future discussions on accounting for military assets with the EPSAS stakeholders.

2. Background

Military assets[1] can encompass a large variety of assets. Some of these assets are civilian assets (for example office buildings), while others are very specific (for example nuclear weapons). The accounting for these specific military assets is a "material, technically complex and sensitive issue for some Member States"[2].

The following graph provides an indication of the materiality of military spending in the Member States.[3] It shows the total government expenditure on defence in 2015 (as a percentage of GDP) for each Member State. The horizontal yellow line provides the average government expenditure on defence in 2015 in the EU as a whole. The total government defence spending is further broken down by function[4], namely into *military defence spending, civil defence spending, foreign military aid spending, R&D defence spending,* and *defence spending not elsewhere classified* (defence n.e.c.).

[1] Please note that the term "military assets" is not a stable, finally defined term. "Cyber War" became more frequent, and armies establish new units called "Cyber Defense" which use different (IT-related) assets to a larger extent compared to before.

[2] See EPSAS, Cell on First Time Implementation: Draft Final Report, EPSAS WG 16/02, Luxembourg, 16 June 2016, page 9.

[3] Considering the objectives of this paper, the following limitation should be noted: Even though providing an indication of the materiality of military spending in the Member States, Figure 1 does not allow to isolate the amount spent on military assets in particular. In fact, figure 1 provides the total defence spending of the Member States, which includes spending on military assets but also significant spending on items which are not related to assets (such as administrative costs, soldiers' salaries, operational expenses, etc.).

[4] This functional sub-classification is based on the "Classification of the Functions of Government" (COFOG) method. For more information on COFOG and on the meaning of these sub-classifications, please refer to http://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Classification_of_the_functions_of_government_(COFOG).

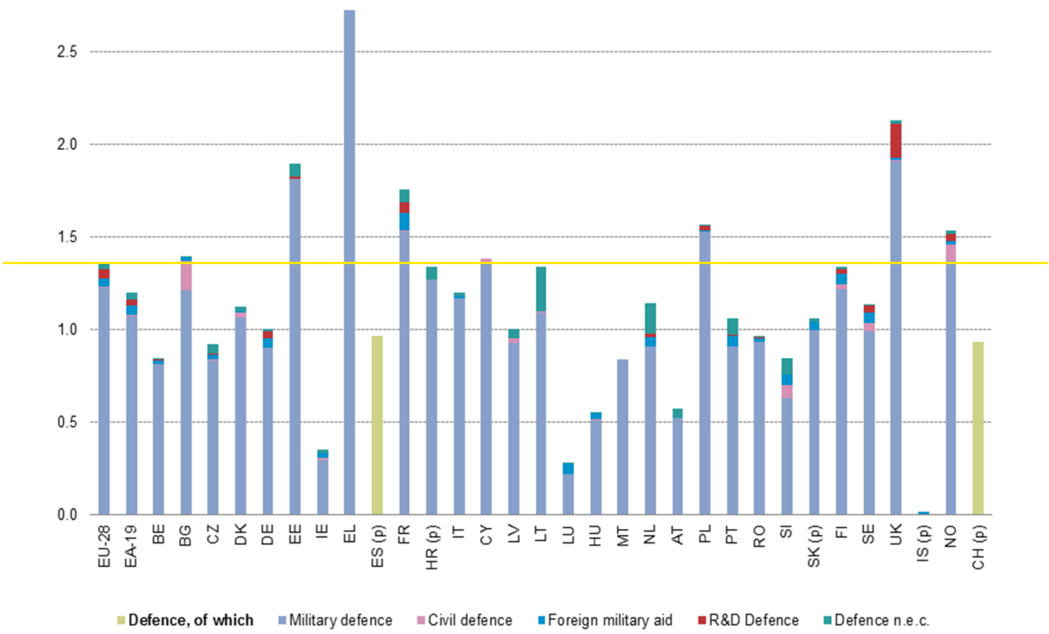

Figure 1: Total general government expenditure on defence, 2015 (% of GDP) and breakdown by function[5]

On an international level, no specific standard on the accounting treatment of these military assets exists. Instead under IPSAS, IPSAS 17, the standard applicable to property, plant and equipment, is applied to the accounting of all military assets. The Commission Staff Working Document[6] has indicated that the application of this standard to the specific military assets can be problematic:

"The recognition and measurement of assets (notably for military or heritage assets) may require a substantial amount of work, depending on the extent to which an entity already has information available on them. IPSAS 17 allows two methods: the cost method or the revaluation method: irrespective of the method, the asset should be depreciated. The recognition and valuation of immovable property would be a long and difficult process. It requires consumption of economic benefit to be estimated against impairment loss. Specific issues arise for accounting of impairment and for use of the component method for measurement."

The PwC report from 2014 [7] provides a first high level view of the current practice in the EU Member States at central government level and gives an indication on whether central governments in Member States account for these types of assets and if so, how: [8]

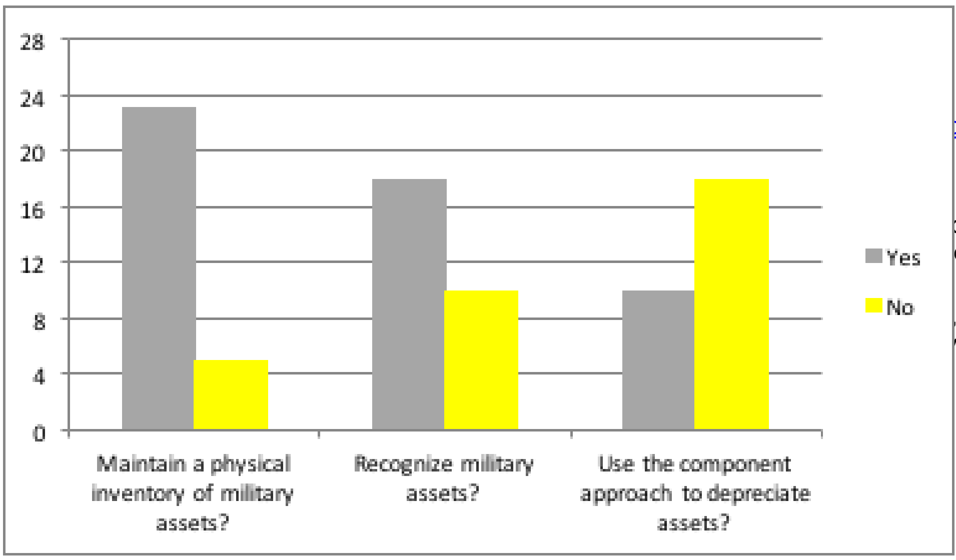

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Figure 2: Summary results of the PwC report from 2014 (central government level)

The EPSAS Cell on First Time implementation recognizes in its revised draft final report[9] that military assets are a material, technically complex and presentational sensitive issue for some Member States. Nevertheless, the Cell concludes that comprehensive stocktaking and recognition of assets having as their main purpose to serve military activities, i.e. military assets, in the first opening balance sheet is needed. It is deemed to be acceptable to recognize the short term, high turnover military assets under the inventories. Next to that, the Cell also concludes that with reference to “presentational sensitivity”, military assets may be presented as an aggregate amount without presenting individual disclosures or individual measurement. It is recommended to present this aggregate amount as a separate line item under property, plant and equipment in the statement of financial position. The following template is provided in Annex 1 to the draft final report regarding minimum recommendations for the statement of financial position for property, plant and equipment:

“*Property plant and equipment*

- ► *Infrastructure assets*
- ► *Buildings*
- ► *Dwellings*
- ► *Land*
- ► *Assets under construction*
- ► *Military equipment*
- ► *Other*”

[9] See EPSAS, Cell on First Time Implementation: Revised Draft Final Report, EPSAS WG 22-23/11, Rome, page 11 and Annex 1 page 18.

3. Description of accounting guidance available

The following paragraphs provide an overview of the existing accounting guidance with respect to accounting for military assets.

3.1 IPSAS

The IPSASB's conceptual framework[10] sets out that the primary reason for holding property, plant and equipment and other assets in the public sector is their service potential rather than their ability to generate cash flows. Because of the types of services provided, a significant proportion of assets used by public sector entities are specialized in nature. One type of these specialized assets is military assets. The accounting guidance with respect to accounting for these assets is embedded in IPSAS 17 "Property, plant and equipment". In a military environment, research and development expenditure are incurred on a regular basis. The accounting treatment for this type of expenditure is embedded in IPSAS 31 "Intangible assets".

Definition of military assets

The current IPSAS guidance[11] does not define military assets but specifies that specialist military equipment will normally meet the definition of property, plant and equipment, and should be accounted for in accordance with IPSAS 17. Neither explicit categorization to further distinguish military specialist equipment nor examples are mentioned in the current standard.

Recognition

IPSAS 17 requires the application of the general recognition criteria[12] for property, plant and equipment also to specialist military equipment. These criteria require the capitalization of initial costs if and only if:

- It is probable that future economic benefits or service potential associated with the item will flow to the entity; and
- The cost or fair value[13] of the item can be measured reliably.

Upon initial recognition, application of the component approach requires to identify the different items (with a cost that is significant in relation to the total cost of the asset) the asset is composed of, so that each component of the property, plant and equipment asset can be depreciated separately based on its respective useful life.

Costs incurred after initial recognition are divided into three groups for recognition purposes:

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[10] Conceptual Framework, Preface, paragraph 14.

[11] IPSAS 17 "Property, plant and equipment", paragraph 20.

[12] IPSAS 17 "Property, plant and equipment", paragraph 14.

[13] The IPSASB's Conceptual Framework does not include fair value as a measurement basis. Instead of fair value, the Conceptual Framework refers to market value as a measurement basis. For more details see IPSASB, The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities, October 2014, BC7.20 ff. In 2017, the IPSASB will start a project on "Public Sector Measurement".

- Repairs and maintenance expenditure[14]: not recognized in the carrying amount of the asset;
- Parts that require replacement[15]: recognized if it meets the recognition criteria; and
- Costs of major inspections[16]: recognized if these are a condition of continuing to operate the asset.

As outlined above, spare parts[17] and servicing equipment have to be recognized in accordance with IPSAS 17 when they meet the definition of property, plant and equipment. Otherwise, such items are classified as inventory. The standard clarifies[18] that major spare parts and stand-by equipment qualify as property, plant, and equipment when an entity expects to use them during more than one period. Similarly, if the spare parts and servicing equipment can only be used in connection with an item of property, plant, and equipment, they are accounted for as property, plant, and equipment.

Research and development expenditure for military assets is recognized in accordance with IPSAS 31 when the definition and recognition criteria in IPSAS 31 are met. In order to make this assessment, the generation of the asset has to be broken down into a research and a development phase[19]. The accounting treatment for each phase is described in the table below:

Research phase[20]	No intangible assets arising from research shall be recognized. Expenditure on research shall be recognized as an expense when it is incurred.
Development phase[21]	An intangible asset arising from development shall be recognized if, and only if, an entity can demonstrate all of the following: ► The technical feasibility of completing the intangible asset so that it will be available for use or sale; ► Its intention to complete the intangible asset and use or sell it; ► Its ability to use or sell the intangible asset; ► How the intangible asset will generate probable future economic benefits or service potential. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset; ► The availability of adequate technical, financial and other resources to complete the development and to use or sell

14 IPSAS 17 “Property, plant and equipment”, paragraph 23.
15 IPSAS 17 “Property, plant and equipment”, paragraph 24.
16 IPSAS 17 “Property, plant and equipment”, paragraph 25.
17 IPSAS 17 “Property, plant and equipment”, paragraph 17.
18 IPSAS 17 “Property, plant and equipment”, paragraph 17.
19 IPSAS 31 “Intangible assets”, paragraph 50.
20 IPSAS 31 “Intangible assets”, paragraph 52.
21 IPSAS 31 “Intangible assets”, paragraph 55.

	the intangible asset; and ► Its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Table 1: IPSAS 31 accounting treatment of expenditure incurred in the research phase and of expenditure incurred in the development phase

Measurement

IPSAS 17 requires the application of the general measurement rules[22] for property, plant and equipment also to tangible military assets. These rules require for initial measurement:

- An asset acquired through an exchange transaction to be measured at cost; and
- An asset acquired through a non-exchange transaction to be measured at fair value.

Subsequently, an entity can choose[23] to apply either the cost model or the revaluation model.

No exception is provided for military assets in terms of application of the component approach.[24] This approach requires each part of an item of property, plant, and equipment with a cost that is significant in relation to the total cost of the item to be depreciated separately.

Military assets must be tested for impairment similarly as other property, plant and equipment through the application of the rules stated in IPSAS 21 “Impairment of non-cash generating assets” and IPSAS 26 “Impairment of cash-generating asset”.

Disclosures

IPSAS 17 requires the application of the general disclosure requirements[25] for property, plant and equipment also to military assets. These require disclosure of matters such as:

- The measurement basis used;
- The depreciation method used;
- The gross carrying amount;
- The accumulated depreciation at the end of the period; and
- A reconciliation of the carrying amount at the beginning and end of the period showing certain components thereof.

[22] IPSAS 17 “Property, plant and equipment”, paragraph 26 and 27.
[23] IPSAS 17 “Property, plant and equipment”, paragraph 42.
[24] IPSAS 17 “Property, plant and equipment”, paragraph 59.
[25] IPSAS 17 “Property, plant and equipment”, paragraph 88.

3.2 NATO Accounting Framework (NAF)

The NAF is an adapted version of International Public Sector Accounting Standards and has been developed to provide minimum requirements for financial reporting for all NATO Reporting Entities following approval by the North Atlantic Council (NAC). The NAF has made adjustments to both IPSAS 17 and IPSAS 31 as agreed by the NAC.

Definition of military assets

The NAF does not define military assets but specifies that these meet the definition of property, plant and equipment. The military assets are broken-down into the following categories:

- Land;
- Buildings;
- Other infrastructure;
- Installed equipment;
- Machinery;
- Vehicles;
- Aircrafts;
- Vessels;
- Mission equipment;
- Furniture;
- Communications; and
- Automated information systems.

Recognition

In terms of recognition of military assets, the NAF provides additional guidance compared to IPSAS 17. This additional guidance has been summarised in the table below:

Capitalization thresholds[26]	The NAF puts in place capitalization thresholds to reduce the administrative burden and simplify the accounting of the many military assets held by NATO reporting entities. Any assets with a value lower than the capitalization threshold are expensed. An extract of the capitalization thresholds has been included for illustration in annex 1.
Specialist military equipment[27]	Specialist military equipment is defined as weapons system platforms, weapons, repairable items, major spare parts and stand-by equipment. The NAF requires recognition of these assets if the NATO reporting entity intends to use them during more than one financial reporting period.
Indicators for control of property, plant and equipment[28]	The NAF includes control indicators to be applied by NATO reporting entities when defining whether they have ownership of the asset and thus should account for it. Control is evidenced as from the moment that six out of ten control indicators defined are met. In case a conflict between more than one NATO reporting entity exists, only the end-use reporting entity shall report the asset in its financial statements based on reliable information shared by the services provider reporting entity. An extract of the control indicators has been included for illustration in annex 1 as well.

Table 2: Additional guidance in the NAF in terms of recognition of military assets

The NAF includes capitalization thresholds to be applied to intangible assets and specifies that the same control indicators as described in the table above are to be applied to the intangible assets. However, additional guidance on capitalization of intangible assets is included when compared to the guidance included for the tangible assets:

- The intangible assets category “integrated systems” has to be capitalized, including related research, development and implementation;
- The following types of intangible assets acquired after 1 January 2013 shall always be capitalized: copyrights, intellectual property rights and software development; and
- The following types of intangible assets shall, on the contrary, never be capitalised: rights of use (air, land and water), landing rights, airport gates and slots, historical documents and publications.

The spare parts are recognised as property, plant and equipment if these are major spare parts and are expected to be used by the NATO reporting entity during more than one financial period.

Spare parts are considered to be major spare parts when their value is greater than the capitalisation threshold defined for the relevant category of military assets. If not accounted

[26] NATO Accounting Framework, IPSAS 17 Adapted - Property Plant and Equipment, page 16.
[27] NATO Accounting Framework, IPSAS 17 Adapted - Property Plant and Equipment, page 17.
[28] NATO Accounting Framework, IPSAS 17 Adapted - Property Plant and Equipment, page 15.

for as property, plant and equipment, the spare parts are classified as inventory if a threshold of EUR 50.000 per location and per warehouse is exceeded. The other spare parts are expensed.

Measurement

In terms of measurement, the NAF provides additional guidance[29] when compared to IPSAS 17. This additional guidance has been summarised in the table below:

Useful life	The NAF has defined maximum useful lives for each category of military assets. An extract of the useful lives defined has been included for illustrative purposes in annex 1 as well.
Military assets used in allied operations and missions	The NAF requires to capture the cost and to depreciate the asset in full during the first year of its useful life.
Disposal of military assets	The NAF standard procedures are to be applied to decide on the disposal of any military assets at the end of the specific operation for which they were originally acquired.
Component approach	The use of the component approach is optional in the NAF.

Table 3: Additional guidance in the NAF in terms of measurement of military assets

Disclosures

The NAF requires full disclosure in the accounting policies by the NATO reporting entity of the use they made of the adapted IPSAS.

The set of financial statements of one of the NATO reporting entities[30] was further analysed. It was noted that military assets are not presented as a separate line item in the statement of financial position.[31] There is also no separate disclosure on military assets nor differentiation between regular assets and military assets in the property, plant and equipment note.

3.3 IFRS

No specific standard on military assets exists in the suite of IFRS standards. If owned by a private sector entity, military assets would be accounted for using the same principles as those applied to other assets held by entities, which are provided in IAS 16 “Property, plant and equipment”.

[29] NATO Accounting Framework, IPSAS 17 Adapted - Property Plant and Equipment, page 17-18.

[30] North Atlantic Programme Management Agency (NAPMA) financial statements for the financial year 2015.

[31] It is important to note that all assets of NAPMA are military assets given the nature of the entity. The question that arises is whether the regular military assets (for example office buildings) should be segregated from the specific military assets (for example bunkers). Currently, both the office buildings and the bunkers are probably shown in the category property.

3.4 National accounts/statistical reporting (ESA 2010)

3.4.1 Definitions and classification of assets under ESA 2010

A balance sheet is defined as a "statement, drawn up for a particular point in time, of the values of assets economically owned and of liabilities owed by an institutional unit or group of units"[32].

With regard to the recording of assets on the balance sheet, ESA distinguishes two main categories of assets:

- Non-financial assets (denoted as AN); and
- Financial assets (denoted as AF)

Any military assets recorded under ESA need to be included within the first category of "non-financial assets". This category is further subdivided into AN.1 "produced non-financial assets" and AN.2 "non-produced non-financial assets". While the former category will include all military assets that result from some kind of production process (e.g. barracks, weapons, inventories, etc.) the later will include those military assets that came into existence other than through the process of production (e.g. land and training fields, contracts, permits, etc.). Despite the fact that the military often owns substantial amounts of land in many Member States, there is no specific category for military land under ESA.

For **produced military assets**, it can be derived from ESA table 7.1[33] on *Classification of Assets* that they will be recorded either within category AN.114 "Weapons systems" (itself a subcategory of AN.11 "Fixed assets") or within category AN.124 "Military inventories" (itself a subcategory of AN.12 "Inventories"). As regards **non-produced military assets**, given that ESA does not foresee specific subcategories for this latter type of military assets, they will be included in the general subcategories of AN.2 "Non-produced non-financial assets" (e.g. AN.21 "Natural resources", including land, or AN.22 "Contracts, leases and licences") together with the non-military assets. Hence, the rules governing their accounting treatment under ESA will be the general rules already applicable to non-military assets included in the same subcategories.

According to paragraph 20.190 of ESA 2010, the aforementioned category AN.114 (weapon systems) comprises vehicles and other equipment such as warships, submarines, military aircrafts, tanks, missile carriers and launchers etc., which are used continuously in the production of defence services. The acquisition of these items is recorded as gross fixed capital formation, i.e. as capital expenditure, similarly to other types of fixed assets. The aforementioned category AN.124 (military inventories) on the other hand consists of single-use items, such as ammunition, missiles, rockets and bombs, which are not part of fixed assets. These items are treated as military inventories.[34]

In order to assess the accounting treatment of military assets under ESA 2010, the sections below will review the recognition and measurement of "weapons systems" (AN.114) and "military inventories" (AN.124).

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[32] See ESA 2010, paragraph 7.01.

[33] See ESA 2010, Table 7.1, p. 172.

[34] However, some types of ballistic missiles are regarded as providing an on-going service of deterrence and therefore meet the general criteria for classification as fixed assets (see ESA 2010, paragraph 20.190).

3.4.2 Recognition

The general principle under ESA 2010 is to record all items that are within the system's boundary, i.e. all items which meet the definition of a particular asset category under ESA.

With regard to the time of recording, the general rule is then to record flows and transactions on an accrual basis; that is, when economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled[35]. According to this general rule, weapons systems and military inventories are recognized in the accounts (i.e. balance sheet, capital account, and financial account, see below) in the moment they are acquired or built.

Paragraph 20.191 of ESA 2010 provides additional specifications with regard to the time of recording of asset acquisitions: in this case the time of recording is when the transfer of ownership of the asset takes place. Moreover, for long-term contracts involving complex weapon systems, the time of recording of the transfer of assets should be upon actual delivery of the assets, not the time of cash payments. Finally, if some long-term contracts also cover the provision of services (in addition to the provision of military assets), then the corresponding government expenditure should be recorded at the time the said services are provided. The provision of the services is recorded separately from the provision of the assets.

Paragraph 20.192 of ESA 2010 mentions that where military equipment is leased, the transaction is invariably recorded as a finance lease and not as an operating lease. This implies that the recording of an acquisition of a leased military asset is matched (or balanced) by the incurrence of an imputed loan by the government lessee. As a result, payments by government are recorded as debt servicing (one part as repayment of the loan, and another part as payment of interest).

Finally, under ESA, investments in fixed assets (including military assets) are recorded as increases of government deficit (or reductions of government surplus) for amounts equivalent to the cost of the assets[36].

In fact, in the ESA 2010 sequence of accounts, revenues and expenditures are also recorded in the capital account (amongst others). The balancing item of the capital account corresponds to the surplus/deficit[37] (equivalent to the difference between revenues and expenditures). Under ESA, the notion of "expenditure" however also comprises capital expenditures, which includes expenditures on acquisitions and constructions of fixed assets[38]. Therefore, investments in fixed assets (including military assets, both weapon systems and military inventories) by government are not only recorded on government balance sheet but also in the capital account, and thus reflected in government surplus/deficit.

At the same time as an investment is recorded in the capital account, the financing of that investment is also recorded in the financial account[39] for the same amount. In the case of

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35 See ESA 2010, paragraph 1.101.

36 Manual on Government Deficit and Debt (MGDD) – Implementation of ESA 2010, 2016 ed., page 289.

37 Equivalent to the net lending(+)/borrowing(-), which is the balancing item of the capital account in the ESA sequence of accounts, see ESA 2010, paragraphs 1.113 and 20.68 – 20.72.

38 ESA 2010, paragraph 20.70.

39 The financial account records net acquisitions of financial assets and net incurrence in liabilities. Expenditure and revenue entries in the capital account always have a counterpart entry in the financial account, see ESA 2010, paragraph 20.71.

military investments, the capital account will include an entry for the military asset expenditure while the financial account will include entries for the incurrence of liabilities and/or the use of cash related to the financing of the military asset.

3.4.3 Measurement

The general rule with regard to the measurement of items on the balance sheet is to value each item as if it were being acquired on the date to which the balance sheet relates. ESA 2010 specifies that estimates should be used in those cases where no observable market prices are available (for example when there is a market but no assets have recently been sold on it)[40]. This applies to both weapon systems and military inventories under ESA.

According to paragraph 7.42 of ESA 2010, fixed assets (including weapons systems) should be measured at market prices if possible (or basic prices in the case of own-account production of new assets) or, if not possible, at current purchasers' prices reduced for the accumulated consumption of fixed capital[41] (which is known as the written-down replacement cost). ESA 2010 specifies that most fixed assets can normally be recorded at written-down replacement cost. However, in those cases where no direct information on the stock of fixed assets is available, ESA indicates that the "**perpetual inventory method**" should be used in order to estimate its current market value.[42]

The perpetual inventory method is a practical approach applied in finance statistics that is used to approximate the conceptually ideal variation in total fixed asset values. Under the perpetual inventory method, the variation in "total fixed asset values" from one year to the other is calculated as the sum of investments (referred to as "Gross fixed capital formation") minus depreciation for the year (referred to as "Consumption of fixed capital"[43]) plus other changes in the volume of the assets, and adjusted according to an asset price index in order to reflect current value (referred to as "Revaluations"):

Net value of a certain category of assets in closing balance sheet

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Net value in opening balance sheet + Gross fixed capital formation – Consumption of fixed capital + Other volume changes + Revaluations

Figure 3: Calculation of the net value under the perpetual inventory method

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40 See ESA 2010, paragraph 7.34.

41 "Consumption of fixed capital" " is a macroeconomic concept which reflects the decline in value of fixed assets owned, as a result of normal wear and tear and obsolescence (see ESA 2010, paragraph 3.139). In defining consumption of fixed capital, reference is made to linear depreciation (see ESA 2010, paragraph 1.24 (b)).

42 See ESA 2010, paragraph 1.24 (b) and paragraph 3.141.

43 The term "consumption of fixed capital" has a different name than depreciation because it is an economic concept.

Each component of the formula is explained in more detail below:

- Gross fixed capital formation[44]: resident producers' acquisitions, less disposals, of fixed assets during a given period plus certain additions to the value of non-produced assets realised by the productive activity of producers or institutional units;
- Consumption of fixed capital[45]: decline in value of fixed assets owned, as a result of normal wear and tear and obsolescence;
- Other volume changes[46]: changes in volume of assets which do not result from an economic transaction but which will affect the values of assets at the closing period. Other volume changes refer to real changes to fixed capital brought about by events which are not part of the economy, e.g. a large earthquake destroying a significant amount of assets; and
- Revaluations[47]: changes in value for the owner of the asset as a result of a change in its price. Similarly, to other volume changes, they do not result from an economic transaction.

This modelling approach allows to approximate variations between periods and based on that, absolute values at period end of each period. It has also to be noted that ESA does not use the concept of impairment of assets.

Finally, the statistical systems also provide rules with regard to the capitalization of expenditures under the perpetual inventory model: expenditures that increase the useful life of the assets (e.g. major structural works) can be capitalized as investments (i.e. recorded within gross fixed capital formation[48]). Ordinary maintenance and repairs, in contrast, are not capitalized as it is seen as "intermediate consumption" rather than as an investment.[49]

3.5 National public sector accounting frameworks

This chapter describes the approaches used to account for military assets in Member States with a high accounting maturity. The Member States France, Austria and Belgium were selected for further analysis. For each of these, EY either consulted their country subject matters experts or got directly in touch with representatives of these jurisdictions. The results of this analysis are detailed below. Next to that, a summary of the differences between the approaches used by the three Member States compared to the IPSAS 17 approach is provided in annex 2.

3.5.1 France

The accounting guidance with respect to accounting for military assets on a Central Government level is embedded in CGAS 6 "Tangible assets".

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[44] See ESA 2010, para. 3.124.
[45] See ESA 2010, para. 3.139.
[46] See ESA 2010, para. 1.129.
[47] See ESA 2010, para. 1.129.
[48] See ESA 2010, para. 3.129 (f).
[49] See ESA 2010, para. 3.86 (f) (2).

Definition of military assets

CGAS 6 does not define military assets, but classifies them as one of the classes and sub-classes of property, plant and equipment. The following categories[50] of military assets are outlined in the standard:

- Certain Ministry of Defence properties that form a class of their own: Hereafter is the exclusive comprehensive list of these assets vital to the accomplishment of the Central Government's sovereign mission of defence, which are not intended to be replaced and which moreover have no equivalent in the private sector and would require extensive conversion work to be suitable for everyday use, if ever it made sense or were feasible to do so:
  - Nuclear air bases ("BAVN"): the features of these bases include storage facilities for nuclear warheads and delivery vehicles, and protected areas for nuclear strike and refuelling aircraft as well as underground shelters for staff;
  - Arsenals with nuclear reception and storage facilities;
  - Centres of military expertise of the Directorate General for Armaments ("DGA");
  - Fuel depots of the army fuel unit ("SEA") operational on 1 January 2006, with common characteristics, namely that, in spite of their age, they have not undergone deterioration over time or wear due to use, because the storage facilities have indestructible concrete walls and other characteristics specific to army requirements: half buried depots, with reinforced walls, spread out and inconspicuous to meet these requirements; and
- Military equipment: it consists of military equipment held and controlled by Central Government made up of different components (e.g. air, land, sea and police), except equipment withdrawn from active service and classified as other tangible assets.

Recognition

The CGAS 6 requires application of the general recognition criteria[51] for property, plant and equipment also to military assets. These require recognition of a tangible asset if and only if:

- The tangible asset is controlled by Central Government; and
- Its cost or value can be measured with sufficient reliability.

The French standard emphasizes the importance of considering the control criterion[52] when assessing recognition for the Central Government since a large number of assets belonging to Central Government are transferred to other entities. The control criterion is to be applied in these situations and is further defined in CGAS 5 "Intangible assets". The definition[53] specifies that control generally takes a specific legal form (ownership or right of use) and is characterised by:

- The ability to govern the conditions of use of the asset;

[50] CGAS 6 para I.6.
[51] CGAS 6 para I.2.
[52] CGAS 6 para 1.2.
[53] CGAS 5 para 1.2.1.

► The ability to govern the service potential and/or future economic benefits derived from using the asset.

Next to the above, the fact that the Central Government bears the risks and expenses associated with holding the asset also constitutes a presumption of control. CGAS 6 concludes that the entities to whom the assets are transferred control the conditions of use of the assets and can derive economic benefit or service potential from them. Thus, these entities control the assets transferred to them and therefore the assets are recognized in the balance sheet of those entities and not in the balance sheet of Central Government.

Once the asset is recognized, the following difficulty is how to define which subsequent costs incurred after initial recognition are to be capitalized. The following elements[54] have to be considered in this analysis:

Future economic benefits or service potential will flow to the Central Government resulting from the subsequent expenditure	>	Most recent assessment of the level of performance originally defined for the existing asset or defined when the expenditure is incurred

If the benefits or service potential that will flow to the Central Government exceeds the original level of performance of the asset, the subsequent costs will be capitalized. The difference compared to the original level of performance represents an increase in the useful life of the asset, an expansion of its capacity, a decrease in the cost of use or a substantial improvement in production quality.

Any subsequent expenditure of a capital nature related to assets measured at cost or a token or non-revisable fixed amount[55] at the reporting date, is recognized as an asset separately from the main asset to which it relates. The applicable depreciation schedule is based on the nature of the asset. If the capitalisable subsequent expenditure is a replacement of all or part of the main asset, and the latter is not fully depreciated, then the depreciation schedule will be reviewed accordingly.

The Central Government holds spare parts essential for the maintenance of military equipment in operational condition. Despite their value, these items are inventories, provided they meet the current definition of an asset[56]. Ammunition is by definition part of inventories. However, ammunition classified as a nuclear deterrent, and therefore by definition not intended for use, is recognized as a fixed asset[57].

The following costs incurred after initial recognition are expensed: minor repairs, routine upkeep and maintenance and one for one replacement or restoration costs without improvement.

In terms of accounting for internally generated intangible military assets deriving from research and development expenditure, CGAS 5 is in line with IPSAS 31. CGAS 5 provides

54 CGAS 6 para 1.5.1.
55 A “non-revisable fixed amount” is neither depreciated nor revalued.
56 CGAS 6 para I.3.5.
57 CGAS 6 para I.3.6.

roughly for the same conditions as IPSAS 31 to be met altogether to recognise intangible assets in a development phase[58]. Projects that generate capitalisable applied research and development costs are within the scope of the standard on intangible assets. In exceptional circumstances, where this expenditure contributes to the creation of a tangible asset (for example, the creation of laboratory), it is recognised in the relevant fixed asset account.[59]

Measurement

The following initial measurement rules are applied:

- Token or non-revisable amount[60]: nuclear air bases, arsenals equipped with nuclear reception and storage facilities, centres of military expertise of the Directorate General for Armaments, fuel depots of the army operational on 1 January 2006 and military equipment withdrawn from active service[61];
- Acquisition cost when acquired in an exchange transaction: military equipment not withdrawn from active service[62].

At the time of first-time adoption, military equipment (for example tanks, fighter aircrafts and submarines) was measured at acquisition cost as of the acquisition date. The acquisition costs were generally available for this type of asset. If not, statistical models were employed to reconstitute costs, which were unavailable, in particular due to the age of the assets[63].

The so-called "standard cost method" was for example used at first-time adoption[64] to measure the assets related to weapon programmes and operations of the Ministry of Defence. For this method the following approach was used:

- Ten significant weapons programmes were analysed. The result of this assessment carried out on these programmes was extended to all DGA (Directorate General for Armaments) weapon programmes;
- Data on investments coming from budgetary accounting applications were systematically taken into account. These data are not exhaustive and, to restore the cumulative expenditures per weapons programme and thus obtain a realistic overview of the assets, they were completed by using data such as tracking records and expert statements;
- Work was conducted to exclude from the first-time amounts the non-capitalisable expenditure related to weapons programmes. Adjustment coefficients per major weapons programme were determined based on the initial analysis of ten programmes. For naval and satellite programmes, with few exceptions, all expenses were capitalized.

The following subsequent measurement rules are applied:

- No depreciation nor impairment: the nuclear air bases, arsenals equipped with nuclear reception and storage facilities, centres of military expertise of the Directorate General

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58 CGAS 5 para 2.3.

59 CGAS 6 para 2.1.1.

60 The token amount is a symbolic amount such as a token euro. The non-revisable amount on the contrary is a fixed amount that is not revised, depreciated nor impaired in subsequent measurement.

61 CGAS 6 para 6.

62 CGAS 6 para 2.1.1.

63 CGAS 6 para 5.1.

64 See PwC, Collection of …, Brussels, 1 August 2014, page 103.

for Armaments, fuel depots of the army [65] and military equipment withdrawn from active service, not for sale, intended for training purposes on the ground, or for museums, static displays cannibalisation or destruction[66];
- Cost model: military equipment not withdrawn from active service[67].

The component approach is not applied to depreciate property, plant and equipment.[68]

Disclosures

The CGAS 6 requires application of the general disclosure requirements[69] for property, plant and equipment also to military assets. These require disclosure of matters such as:

- The measurement basis used;
- The depreciation method used;
- The gross carrying amount;
- The accumulated depreciation at the end of the period; and
- A reconciliation of the carrying amount at the beginning and end of the period showing certain components thereof.

The financial statements of the French Republic[70] have been analysed. It was noted that military assets are not presented as a separate line item in the statement of financial position. There is also no separate disclosure on military assets. However, qualitative information is provided on military assets both in the intangible assets note as well as in the property, plant and equipment note. In the property, plant and equipment note, military assets are defined as a separate category of assets in the movement schedule provided.

3.5.2 Austria

As IPSAS has to be applied through national law in Austria, the Austrian accounting rule for property, plant and equipment used at Central Government Level is IPSAS 17.

Definition of military assets

IPSAS 17 is applied and in this standard no definition of military assets is given. Military assets are deemed to meet the definition of property, plant and equipment and should as such be accounted for following the same rules as set out for all property, plant and equipment. The Austrian accounting rule does not divide the military assets into categories.

Recognition

The IPSAS 17 initial recognition criteria are applied. Subsequent costs are capitalized if they prolong the military asset’s useful life or add functionality. If this is not the case, subsequent costs are expensed.

65 CGAS 6 para 2.2.5.
66 CGAS 6 para 2.2.7 and 3.2.
67 CGAS 6 para 2.2.7 and 3.2.
68 CGAS 6 para I.4.
69 CGAS 6 para 4.1 and 4.3.
70 Financial statements of the French Republic for the year ended 31 December 2015.

Spare parts with a value above 5.000 EUR are accounted for as inventories (for example the spare chains for a tank). If the spare part is physically integrated in the asset, it will be reclassified from inventory to property, plant and equipment. The useful life of the spare part will be the same as the useful life of the item of property, plant and equipment.

The main difficulty encountered by Austria at first-time implementation was to define the scope of the opening balance sheet. To overcome this hurdle, capitalization thresholds were set. These capitalization thresholds have been included for illustration in annex 3. The longer the acquisition of the item dated back in time, the higher the threshold was set. The capitalization threshold applied as of 2013 amounts to EUR 400 and was used at first-time adoption as well as in the ongoing accounting. Next to the capitalization thresholds, Austria decided not to capitalize “smaller items” at first-time implementation due to high administrative burdens. Examples of these smaller items were clothing, and ammunition.

In terms of accounting for research and development expenditure, Austria has a practice of expensing these.

Measurement

Military assets are measured at cost at initial recognition. The cost model is afterwards applied for subsequent measurement purposes. Military assets are depreciated; however, the component approach is not applied.

In terms of impairment, Austria did not incur this issue in practice yet and has therefore not defined a standard procedure for determining recoverable service amounts. In case an impairment would be incurred, the provisions of IPSAS 21 would be applied.

Disclosures

Given the sensitive nature of the military assets, Austria encountered difficulties at first-time implementation to define the detail of disclosure that would be provided in the financial statements. A consensus was reached not to present the military assets separately in the statement of financial position. Instead, the military assets are embedded in the property, plant and equipment sub-line items (for example, the sub-line item “Buildings” contains the “Military buildings”).

Next to that, no separate note on military assets is disclosed. Austria carefully considers, which information it discloses that can be useful for financial analysis purposes (for example, variations in spending, overspendings, comparisons, etc.) without giving away operational insights.

3.5.3 Belgium

The Member State Belgium does not apply IPSAS. The Belgian Ministry of Defence applies the national accounting rule applicable to property, plant and equipment in general also to military assets.

Definition of military assets

The Belgian Ministry of Defence has based its definition of military assets on the ESA guidance[71]. At first-time implementation, it was challenging to develop categories of military assets and to define the scope of military assets. This hurdle was resolved by relying on the guidance and descriptions of military assets provided by ESA 2010. The four following categories of military assets have been defined:

- ► Ground force military assets ("Rollend materieel vernietigingswapens");
- ► Navy force military assets ("Varend materieel vernietigingswapens");
- ► Air force military assets ("Vliegend materieel vernietigingswapens"); and
- ► Other military assets ("Ander materieel vernietigingswapens").

Recognition

The Belgian Ministry of Defence did not define specific recognition criteria for its military assets but rather applies the general property, plant and equipment recognition criteria. Subsequent expenditure is capitalized if it increases the value or useful life of the asset substantially. Spare parts are recognized as a separate sub-category of the inventories.

Measurement

The military assets are initially measured at cost. At first-time implementation (in 2012), the value of the military assets was calculated as follows:

Value at first-time implementation
=
Initial cost price + price of the upgrades – depreciation on initial cost price and on upgrades.

Figure 4: Calculation of the value of the Belgian Ministry of Defence military assets at first-time implementation

The cost model is used for subsequent measurement purposes. All military assets are depreciated, however the component approach is not applied. The useful life has been determined at Federal level and is reassessed when subsequent expenditure is incurred. A specific general ledger ("GL") category is allocated to each category of military assets listed above. Each GL category follows its own depreciation rules.

Disclosures

The financial statements at Federal level were analysed. The military assets are not presented as a separate line item in the statement of financial position. Moreover, no specific disclosures for military assets are provided in the notes to the financial statements.

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71 In the ESA 2010, military assets comprise military weapons systems, comprising vehicles and other equipment such as warships, submarines, military aircrafts, tanks, missile carriers and launchers etc. which are used continuously in the production of defence services. They are fixed assets, like those used continuously for more than one year in civilian production (see section on statistical reporting above).

4. Discussion of matters relevant for a European harmonization

The following matters relevant for a European harmonization are addressed:

- ► Taking stock of military assets (4.1.);
- ► Problematic points/issues that can arise with regards to definition, recognition, measurement and presentation (4.2.);
- ► Internally developed military assets (4.3.);
- ► Impairment of military assets (4.4.);
- ► Advantages and disadvantages of the existing approaches to recognition and measurement (4.5.);
- ► The need for supplementary guidance to what is currently foreseen under IPSAS and the format of that guidance (4.6.);
- ► The consequences for a possible convergence between IPSAS and GFS/ESA (4.7.).

4.1 Taking stock of military assets

The PwC 2014 report concludes that five out of twenty-eight Member States do not have an inventory of military assets in place. In EY's opinion, stock-taking is a crucial hurdle to take by each Member State when transitioning to accrual based accounting/IPSAS and to get a complete overview of all their military assets. This view is confirmed by the EPSAS Cell on First Time implementation, which has recommended in its draft final report[72] to perform comprehensive stock-taking of assets including military assets.

4.1.1 The stock taking process

The Member States that do not have an inventory yet, face the challenge of stock-taking at the date of first-time implementation. It is crucial that Member States at this point also collect information needed to measure the asset (for example the relevant data that is needed for the calculation of cost less depreciation or the data that is needed for the componentization of the asset in compliance with the component approach). This implies, that Member States should have already determined which measurement approach they will apply at the time of the stock-taking (e.g. whether they follow a deemed cost approach using fair value as a measurement basis, whether they will follow a component approach and also how detailed the assets should be broken down into components, and whether thresholds will be used and how they will be determined etc.). In practice, taking stock of military assets will bring with it an additional challenge due to the sensitive nature of these assets. As a result, the stock taking process will be even more time-consuming and might require the development of specific procedures. The challenges linked to the stock taking process are confirmed through the analysis of the national public sector accounting frameworks (see Annex 4).

Even though the process can be challenging, there is no questioning of the need for or added value of taking stock of the military assets of the Member States. Experience from the United Kingdom transition to accrual based accounting shows that such an exercise may often prompt a major cleaning of the military assets. To reduce the administrative burden of

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[72] See EPSAS, Cell on First Time Implementation: Draft Final Report, EPSAS WG 16/02, Luxembourg, 16 June 2016, page 9 and Annex 1.

the stock taking process, putting in place capitalization thresholds can be a potential solution to reduce the administrative burden. It has been noted through the analysis of the national public sector accounting frameworks that this is common practice among the Member States analysed. Therefore, the question can be raised whether a common materiality or capitalization threshold[73] is needed for first-time adoption and subsequent accounting.[74]

4.1.2 Componentization of military assets

IPSAS 17 requires[65] separate depreciation of each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item. For example, an airframe and engines of a military aircraft would be depreciated separately. This componentization has to be done at the date of first-time implementation and subsequently each time an asset is acquired except for the case that the exemption in IPSAS 33 is used. According to this standard, where a first-time adopter has not recognized assets and/or liabilities under its previous basis of accounting, it is not required to recognize and/or measure the following assets and/or liabilities for reporting periods beginning on a date within three years following the date of adoption of IPSASs[66]. This exemption is applicable to IPSAS 17. Therefore, the component approach would not have to be applied during the transitional period. However, it has to be noted that the use of the exemption affects fair presentation and compliance with IPSASs during the period of transition. When the transitional period of 3 years ceases then a first-time adopter would have to apply the component approach. It is possible that the first-time adopter applies IPSAS 17 in full before the end of the transitional period. In that case, also the component approach would have to be applied.

Typically military assets are very complex assets with many different components each having different useful lives. Therefore, the application of the component approach would be time-consuming, cumbersome and an administrative burden. For this reason, France, Austria and Belgium decided not to apply the approach. The NAF specifies that the application of the component approach by the NATO reporting entities is optional.

Whether or not the component approach should be a requirement for military assets needs to be discussed considering its advantages and disadvantages. In EY's view these advantages and disadvantages are as follows:

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[73] Capitalization thresholds may reduce the administrative burden, but in practice these have an impact on the audit process and can be an element of discussion with the auditor.

[74] In practice, practical experiences show that countries often put in place a threshold during their first-time adoption phase and afterwards put in place a lower threshold to be used in subsequent accounting.

[65] IPSAS 17 "Property, plant and equipment" para 59.

[66] IPSAS 33 "Intangible assets" para 36.

	Application component approach	**Component approach not applied**
Faithful representation of the statement of financial position	Each component will be depreciated over its specific useful life resulting in a faithful representation of the military assets' net book value in the statement of financial position.	The full asset will be depreciated over the useful life of the main component and as such may not result in a faithful representation of the military assets' net book value in the statement of financial position in cases of multi-component assets with heterogeneous components.
Comparability	Comparability achieved if all Member States apply the component approach. However, there can be discretion in defining components. Furthermore, useful lives of components might vary between entities due to entity-specific circumstances (e.g. differing construction approaches).	Comparability achieved if none of the Member States apply the component approach.
Cost versus benefit*	Higher implementation cost	Lower implementation cost
Ease of application*	More complex to apply in practice due to volume, complexity etc. of assets.	Easy to apply

	Advantage
	Disadvantage
	Neutral

Table 4: Advantages and disadvantages of the use of the component approach

* In EY's view, the implementation cost and application complexity can be reduced by applying thresholds in accordance with the materiality principles in IPSAS. Components would only be treated separately if they, for example make up 10% or 20% of the total asset value. IPSAS 17 does not specify a threshold for the definition of a component.

4.2 What are the problematic points/issues with regards to definition, recognition, measurement and presentation of military assets?

A comparison has been made between IPSAS 17, the NAF and the national public sector accounting frameworks analysed. This comparison was used as a basis to define the problematic points/issues to be considered in this issue paper and has been summarized in the table below:

	NAF	French accounting framework	Austrian accounting framework	Belgian accoun-ting framewor k	Proble-matic point/issue
Definition of military assets	Supplemen-tal guidance	Supplemen-tal guidance	No definition is provided (in line with IPSAS 17)	Based on ESA	4.2.1.
Recognition	Deviation from IPSAS 17	Deviation from IPSAS 17	Deviation from IPSAS 17	IPSAS 17 is not applied	4.2.2.
Measurement	Deviation from IPSAS 17	Deviation from IPSAS 17	Deviation from IPSAS 17	IPSAS 17 is not applied	4.2.3.
Disclosures	Deviation from IPSAS 17	In line with IPSAS 17	Deviation from IPSAS 17	Deviation from IPSAS 17	4.2.4.

(orange)	National public sector accounting framework and/or NAF deviates from IPSAS 17
(light green)	National public sector accounting framework and/or NAF provides additional guidance compared to IPSAS 17
(green)	National public sector accounting framework and/or NAF is in line with IPSAS 17

Table 5: Differences between the national public sector accounting frameworks analysed, the NAF and IPSAS 17

4.2.1 Problematic point/issue 1 - Categorization of military assets

IPSAS 17 does not include a categorization of military assets. However, it was noted in the analysis of the NAF and national public sector accounting frameworks that military assets are often categorized to define specific accounting rules for each category of military assets. Next to that, in EY's view a categorization can be useful for presentation purposes in the statement of financial position and/or in the notes of the financial statements depending on the level of detail that will be provided considering the presentational sensitivity.

The question can be raised whether the categorization in the NAF and national public sector accounting frameworks is used to define specific accounting rules. A summary of the analysis of this question has been included in the table below:

Accounting framework	Categorization?	Is this categorization used to define specific accounting rules?
NAF	Yes	Yes, the categorization is used to define capitalization thresholds. Next to that, the maximum useful life for each category of military assets is defined.
French accounting framework	Yes	Yes, the categories are used to define the measurement approach to be applied. In terms of initial measurement, the token or non-revisable amount is used for the Ministry of Defence properties that form a class of their own. In terms of subsequent measurement, these same military assets are not depreciated nor impaired.
Austrian accounting framework	No	Not applicable
Belgian accounting framework	Yes	Yes, a specific general ledger category is allocated to each category of military assets. Each general ledger category follows its own depreciation rules.

(orange)	No categorization and/or no specific accounting rules
(green)	Categorization and/or specific accounting rules

Table 6: Analysis of the question raised whether categorization is used to define specific accounting rules

Based on the table above, it can be concluded that if Member States categorize their military assets this categorization is used to define specific accounting rules mainly for recognition and/or subsequent measurement purposes. In EY's view, it is important to discuss with the EPSAS stakeholders whether categorization should be embedded in an accounting standard and if so what level of categorization is to be included. Other points relevant for discussion are the potential need to define common capitalization thresholds, specific measurement rules and useful lives.

4.2.2 Problematic point/issue 2 - Recognition of military assets

In terms of initial recognition criteria and recognition rules for subsequent expenditure, it was noted that often additional guidance is provided by the NAF and national public sector accounting frameworks analysed when compared to IPSAS 17. In the area of spare parts a deviation from the IPSAS 17 rules was even noted. More details are provided below.

4.2.2.1 Initial recognition

In terms of initial recognition rules, the NAF and national public sector accounting frameworks analysed (excluding the Belgian framework) were found to be in line with IPSAS 17. However, in some areas the frameworks include more guidance to facilitate the application of the standard in practice. The additional guidance has been summarized in the table below:

Additional guidance	**NAF**	**French accounting framework**	**Austrian accounting framework**
Control	► Indicators to define control of the asset to determine economic ownership	► Indicators to define control of the asset to determine economic ownership	► No additional guidance provided
Additional guidance	► NAF	► French accounting framework	► Austrian accounting framework
Capitalization thresholds	► Inclusion of capitalization thresholds	► No additional guidance provided	► Inclusion of capitalization thresholds
Other	► Specific guidance is included for the specialist military equipment	► No other additional guidance provided	► No other additional guidance provided

Table 8: Additional guidance provided in terms of initial recognition in the NAF and the French and Austrian national public sector accounting frameworks

4.2.2.2 Subsequent expenditure

In terms of recognition rules for subsequent expenditure, the national public sector accounting frameworks[75] analysed (excluding the Belgian framework) were found to be in line with IPSAS 17. However, in some areas the frameworks include more guidance to facilitate the application of the standard in practice. The additional guidance has been summarized in the table below:

French accounting framework	The capitalization of subsequent costs is determined considering the following two elements of which the first will have to be greater than the second: 1) The probability that these subsequent costs will result in future economic benefits or service potential for the Central Government; 2) An assessment of the level of performance of the existing asset when the expenditure is incurred or if it is available a recent assessment performed in the past If one element is greater than the other the subsequent costs will be capitalized. In other words, the subsequent costs need to contribute to the asset and increase the current level of performance and as such result in a future economic benefit for the Central Government. This difference compared to the

75 The NAF is not included in this analysis as this level of detail could not obtained for this framework.

	original level represents an increase in the useful life of the asset, an expansion of its capacity, a decrease in the cost of use or a substantial improvement in production quality.
Austrian accounting framework	Subsequent expenditure is capitalised if it prolongs the useful life or adds functionality.
Belgian accounting framework	Subsequent expenditure is capitalised if it prolongs the useful life substantially.

Table 9: Additional guidance provided in terms of recognition of subsequent expenditure in the national public sector accounting frameworks analysed

Next to the additional guidance noted above, the NAF and the national public sector accounting frameworks analysed deviate from the IPSAS 17 rules in the area of spare parts as explained in the table below:

IPSAS 17	Spare parts are recognized as property, plant and equipment if they meet the definition of property, plant and equipment. If the definition is not met, spare parts are accounted for as inventories.
NATO accounting rule	The spare parts are recognised as property, plant and equipment if these are major spare parts and are expected to be used by the NATO reporting entity during more than one financial period. Spare parts are considered to be major spare parts when their value is greater than the capitalisation threshold defined for the relevant category of military assets. If not accounted for as property, plant and equipment, the spare parts are classified as inventory if a threshold of EUR 50 thousand per location and per warehouse is exceeded. The other spare parts are expensed.
French accounting framework	All spare parts, despite their value, are inventories provided they meet the definition of an asset. Ammunition is by definition part of inventories and ammunition classified as a nuclear deterrent is recognized as a fixed asset, i.e. property, plant and equipment, given that it is not intended for use.
Austrian accounting framework	Spare parts are accounted for as inventories unless they are physically integrated in the asset. In the latter case the spare parts are accounted for as property, plant and equipment.
Belgian accounting framework	Spare parts are accounted for as inventories.

Table 10: Deviation from IPSAS of the NAF and national public sector accounting frameworks analysed in terms of accounting for spare parts and ammunition

The main deviations to IPSAS 17 noted are:

- Spare parts are in practice often by default considered to be inventories to simplify the accounting process;
- Ammunition have been defined to be inventories by the French Member State; and
- Thresholds for capitalization as property, plant and equipment are set.

4.2.3 Problematic point/issue 3 – Measurement

Some problematic points/issues were noted when comparing the national public sector accounting frameworks and the NAF with the IPSAS framework, dealing with both initial and subsequent measurement. Each problematic point/issue is further described below.

4.2.3.1 Initial measurement

The initial measurement provisions under IPSAS 17 (acquisition cost) can be applied to military assets acquired in an exchange transaction without difficulties. However, for some military assets such as nuclear air bases, the French Member State initially measures them at a token or non-revisable amount.

Next to the above, measurement at first-time implementation can be a challenge. The cost value is not always determinable and the deemed cost approach using fair value as a proxy for cost is often not suitable for military assets due to their unique character. In order to overcome this hurdle, the French Member State used a standard cost method at first-time implementation. This implied the use of the following methodology for the weapon programmes and operations of the Ministry of Defence:

- A selection was made of the largest programmes and the outcome of the assessment carried out for these was extended to all programmes;
- Data on investments coming from budgetary accounting applications was used complemented by non-accounting data such as tracking records and expert statements;
- In order to be able to exclude non-capitalisable expenditure adjustment coefficients per major programme were determined.

4.2.3.2 Subsequent measurement

The analysed national public sector accounting frameworks and the NAF subsequently measure their military assets using the cost model. The only exception noted is the French accounting framework, which only measures military equipment in active service using the cost model. Some other military assets, such as nuclear air bases, are not depreciated nor impaired.

The non-application of the component approach for measurement purposes is an additional deviation by the national public sector accounting frameworks from IPSAS 17. The NAF leaves an option for the NATO reporting entities to apply the component approach. No further details are provided in respect of this deviation since this has already been discussed under section 4.1.2.

4.2.4 Problematic point/issue 4 – Disclosures

IPSAS 1 does not provide a breakdown of military assets into categories in the statement of financial position[76] nor provides examples of military assets. In general, the standard[77] requires additional line items, headings, and sub-totals to be presented in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position. Entities with significant military assets would therefore, based on IPSAS 1, be required to present additional line items on military assets in the statement of financial position.

The guidance above cannot be applied to military assets without considering and discussing the presentational sensitivity attached to them. The question can be raised how Member States and the NATO handle this presentational sensitivity in their financial statements.

In order to answer this question, an analysis of the respective financial statements has been performed and has been summarized in the table below:

	How is the presentational sensitivity considered?
2015 financial statements of the NATO Reporting Entity NAPMA (North Atlantic Programme Management Agency)	The military assets are not presented as a separate line item in the statement of financial position. No separate note nor breakdown in the other notes is provided either. A high-level movement schedule is rather included together with limited qualitative information[78].
2015 financial statements of the French Republic	The military assets are not presented as a separate line item in the statement of financial position. In the notes to the financial statements, the following disclosures are made: ► Internally generated military assets: the internally generated intangible assets are presented separately in the movement schedule. Underneath, qualitative disclosure is given explaining that the internally generated intangible assets are mainly related to military developments. Full qualitative disclosure is provided explaining the movement of the year; and ► Acquired military assets: a separate note is provided on the military assets. This note consists of a movement schedule detailed per type of military assets. These types of military assets are not the same as the categories defined in the accounting framework. Underneath the table, full qualitative disclosure is provided explaining the movement of the year.

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76 IPSAS 1 "Presentation of financial statements", paragraph 88.

77 IPSAS 1 "Presentation of financial statements", paragraph 89.

78 An important side note to this information is that all assets of NAPMA are military assets given the nature of the entity. The question that arises is whether the regular military assets (for example office buildings) should be segregated from the specific military assets (for example bunkers). Currently, both the office buildings and the bunkers are probably embedded in the category property.

	How is the presentational sensitivity considered?
2015 financial statements of the Austrian Ministry of Defence	The military assets are not presented as a separate line item in the statement of financial position. Next to that, no separate note on military assets is disclosed. Austria carefully considers, which information it discloses that can be useful for financial analysis purposes (for example, variations in spending, overspendings, comparisons, etc.) without giving away operational insights.
2015 financial statements of the Belgian Federal State	The military assets are not presented as a separate line item in the statement of financial position. No breakdown is provided in the notes to the financial statements either. Very limited qualitative information (for example the amount of military assets sold is disclosed together with the manner in which new assets acquisitions is financed) is provided on the military assets.

Table 7: Analysis of the question raised on how the presentational sensitivity is monitored in the financial statements

Based on the table above, it can be concluded that neither NAPMA nor the national public sector accounting frameworks analysed disclose their military assets as a separate line item in the statement of financial position. Regarding disclosure of information in the notes, the Member State France is the only example found providing detailed disclosures on their military assets in the notes to the financial statements. The other two Member States provide aggregated, high-level information given the sensitive nature of the subject.

In EY's view separate presentation of the military assets in the statement of financial position can be useful given the fact that military assets are often a significant portion of the total assets held by a central government. This would also be in line with the IPSAS 1 requirements described above table 8 and would prevent distortion of the face of the statement of financial position due to the inclusion of the military assets under the property, plant and equipment line item. This view is aligned with the EPSAS Cell on First Time Implementation, which recommends presenting the aggregate amount of military assets as a separate line item under the property, plant and equipment in the statement of financial position.

In the area of disclosure in the notes of the financial statements, from a materiality point of view a need arises to have a separate note on military assets or at least a further disaggregation in the property, plant and equipment note of the high value military assets in line with IPSAS 1 requirements. Next to that, this disaggregation might be needed anyway in order to comply with specific disclosure requirements of accounting standards other than the property, plant and equipment standard. For example, a disclosure on contingent liabilities might be required for certain nuclear weapons held by the Member State. However, in EY's view this matter cannot be discussed without considering the presentational sensitivity linked to military assets. Therefore, the level of required disclosure is a matter for discussion with the EPSAS stakeholders. In this discussion, the view of the EPSAS Cell on First Time Implementation has to be considered together with the information above. The view of the Cell is that given their sensitive nature, military assets may be presented as an aggregate amount without individual disclosures or individual measurement

4.3 Internally developed military assets

IPSAS 31 "Intangible assets" explains how to define which development expenditure is to be capitalized as internally developed intangible military assets. The question can be raised whether in practice this is applied. In order to answer this question, the national public sector accounting frameworks and the NAF have been analysed. The outcome of this analysis is summarized in the table below:

NAF	The following rules deviating from IPSAS 31 are set-out: ► Integrated systems need to be capitalized including research, development and implementation expenditure; ► No intangible military assets have to be recognized if acquired before 1 January 2013. After this date, only specific assets (for example: copyright and intellectual property rights), included in a list, have to be recognised; ► Assets are listed that shall never be capitalized (for example right of use, landing rights, airport gates and slots). Next to the above, thresholds for capitalization are applied.
French accounting framework	IPSAS 31 is applied. However, the accounting framework includes additional guidance when compared to IPSAS 31 in which thresholds are set for capitalization.
Austrian accounting framework	Intangible military assets which are acquired are capitalized. In contrast, the military intangible assets that are internally generated are expensed.
Belgian accounting framework	Given the sensitive nature, no information could be obtained.

Table 11: Analysis of the question raised on whether the capitalization of internally generated military assets is in line with the IPSAS 31 guidelines

In EY's view, the IPSAS 31 criteria can be applied to internally generated intangible assets. However, it is noted that in practice this can be cumbersome and time-consuming. This is also confirmed by the table above illustrating that in practice Member States deviate from the IPSAS 31 guidelines.

4.4 Impairment of military assets

Given the fact that military assets are held for service delivery purposes rather than with the primary objective of generating a commercial return, military assets are non-cash generating and, therefore, IPSAS 21 "Impairment of non-cash generating assets" applies to them.[70]

According to this standard, an impairment[79] will occur if:

[70] IPSAS 21 "Impairment of non-cash generating assets", paragraph 20.
[79] IPSAS 21 "Impairment of non-cash generating assets", paragraph 25 and 35.

Carrying amount of the asset > recoverable service amount Recoverable service amount = (higher of) *Fair value less cost to sell and value in use*

Figure 5: Impairment of military assets as per IPSAS 21

Application of the impairment guidelines under IPSAS to military assets may require judgment.[80] In EY's view, judgment will be required to identify impairment and to measure the recoverable service amount.

4.4.1 Identification of impairment

IPSAS 21 defines primary impairment indicators[81], which if any of those is met requires the entity to perform an impairment test, and secondary impairment indicators[82], which are less strong.

These indicators have been summarized in the table below:

80 IPSASB Agenda Item 4, September 2014, Brussels meeting, question 8 respondent comment 14 and PwC, Collection of…, Brussels, 1 August 2014, page 139.

81 IPSAS "Impairment of non-cash generating assets", paragraph 27.

82 IPSAS "Impairment of non-cash generating assets", paragraph 29.

Primary indicators	Secondary indicators
External indicators: ► Cessation, or near cessation, of the demand or need for services provided by the asset; ► Significant long-term changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, legal, or government policy environment in which the entity operates; Internal indicators ► Evidence of physical damage of an asset is available; ► Significant long-term changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which an asset is used or is expected to be used; ► A decision to halt the construction of the asset before it is complete or in a usable condition; and ► Evidence is available from internal reporting that indicates that the service performance of an asset is, or will be, significantly worse than expected.	► During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use; ► A significant long-term decline (but not necessarily cessation or near cessation) in the demand for or need for services provided by the asset.

Table 12: Primary and secondary IPSAS 21 impairment indicators

In practice, there are a range of indicators that need to be considered given the large amounts and variety of military assets jurisdictions have under their control. In EY's view the discussion should focus on whether it is feasible and solutions such as the shortening of the list of impairment indicators should be explored. Next to that, it is important to consider the specificities of military assets. Military assets are serving the purpose of being used in warfare and therefore the assets often end up being destroyed or heavily damaged. As a result, the assets will have to undergo an impairment procedure that finally impacts the statement of financial performance.[83]

The Member State France can serve as an example on how to shorten the list of impairment indicators. This Member State provides only two indicators for impairment in its property, plant and equipment accounting rule:

► Significant deterioration in the physical condition of the asset caused by exceptional circumstances (for example, terrorist attacks, flooding, etc.) which prevents normal use of the asset; and

[83] Member States which use accrual based budgeting will have an impact on their budget due to these impairments. However, if budgets are on a cash basis there will not be an impact.

- Evidence of technical obsolescence caused by an event preventing the normal use of the asset in the short term.

4.4.2 Measuring the recoverable service amount

An entity does not necessarily have to measure both the fair value less costs to sell and the value in use.[84] If either of these amounts exceed the carrying amount, the asset is not impaired, and it is not necessary to estimate the other amount. The fair value less costs to sell[85] and/or value in use are to be measured as follows:

Fair value less cost to sell	Value in use
► Best evidence to determine fair value less cost to sell is the price in a binding sales agreement; ► If this information is not available and the asset is traded in an active market, the market price less costs of disposal will be the fair value less costs to sell; ► If this information is also not available, the fair value less costs to sell will be based on the best information available to reflect the amount that an entity could obtain, at reporting date, from the disposal of the asset.	The value in use is the present value of the asset's remaining service potential and can be measured using any of the following three approaches: ► Depreciated replacement cost: cost to replace the asset's gross service potential depreciated to reflect the asset in its used condition; ► Restoration cost: cost of restoring the service potential of an asset to its pre-impaired level; ► Service units approach: reducing the current cost of the remaining service potential of the asset before impairment to conform to the reduced number of service units expected from the asset in its impaired state.

Table 13: Methods to measure the recoverable service amount

In EY's view, for some military assets (for example nuclear air bases) there is a lack of an active market. Determining the fair value less costs to sell for these assets will be complex and the value in use will be more appropriate to determine the recoverable service amount. On the other hand, there are military assets (for example guns) for which there is an active market and for which fair value less costs to sell can be easily determined.

4.5 What are the advantages and disadvantages of the existing approaches to recognition and measurement?

In EY's view, the property, plant and equipment and intangible assets initial recognition criteria can be applied to military assets. Therefore, no discussion of the advantages and disadvantages of the existing approaches regarding the recognition of military assets is performed here.

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84 IPSAS 21 "Impairment of non-cash generating assets", paragraph 36.

85 IPSAS 21 "Impairment of non-cash generating assets", paragraph 40, 41 and 42.

In EY's view, acquisition cost can be applied to military assets. However, it was noted in the analysis that the Member State France foresees two additional measurement methods next to the acquisition cost:

- Use of a token amount in case the cost value cannot be determined; and
- Use of a non-revisable amount for some military assets such as nuclear air bases that the Member State will not depreciate nor revise in subsequent measurement.

The advantages and disadvantages of each of these initial measurement methods are described in the table below:

	Acquisition cost	**Token amount**	**Non-revisable amount**
Faithful representation of the statement of financial position	The use of the acquisition cost will result in a faithful representation of some military assets (for example guns).	A token amount can never lead to a faithful representation.	The use of the non-revisable amount will only result in a faithful representation for some military assets that are deemed not to deteriorate.
Comparability	Comparability is achieved	Comparability is not achieved	Comparability is achieved
Cost versus benefit	Low implementation cost	Low implementation cost	Low implementation cost
Ease of application	Easy to apply	Easy to apply	Easy to apply

(green)	Achieved
(orange)	Not entirely or not achieved

Table 14: Advantages and disadvantages of the use of the acquisition cost, token amount or non-revisable amount

In terms of existing approaches to subsequent measurement, the need for an additional approach next to the cost and revaluation model is a subject for discussion. It was noted that the Member State France foresees an approach not to depreciate nor impair certain military assets, which have been initially measured at a **non-revisable amount**. These military assets are not intended to be used and/or do not deteriorate.

The advantages and disadvantages of each model are described in the table below:

	Cost model	**Revaluation model**	**No depreciation nor impairment**
Faithful representation of the statement of financial position	Faithful representation is endangered due to the lack of yearly indexation. For example, an asset acquired 20 years ago has a different cost value compared to the cost at the reporting date.	Faithful representation is endangered, as there is often no active market for military assets. Therefore, in practice revaluation would often require the use of valuation models.	Faithful representation is endangered due to the lack of yearly indexation and the fact that the reduction in service potential (if there is any) is not considered.
Comparability	Comparability among Member States can be problematic as price developments are not reflected.	Comparability might be limited since Member States may use different valuation models and/or inputs to these valuation models.	Comparability among Member States can be problematic as price developments are not reflected.
Cost versus benefit	Low implementation cost	Higher implementation cost	No implementation cost
Ease of application	Easy to apply	More complex to apply	Easy to apply

(green)	Achieved
(orange)	Not entirely or not achieved

Table 15: Advantages and disadvantages of the use of the cost or revaluation model for subsequent measurement

4.6 Need for supplementary guidance to what is currently foreseen under IPSAS and format of that guidance

The question to be raised is whether a separate standard on military assets is needed under EPSAS or whether additional guidance should be included in the EPSAS standard on property, plant and equipment.

In EY's view, the general accounting requirements under IPSAS 17 for property, plant and equipment can be applied to military assets. However, we do believe that the following is to be considered:

- The potential need to categorize military assets in the accounting standard;
- The need for supplementary guidance either in the form of a standard or a separate interpretation document; and
- The potential simplification through removal of the currently existing options in IPSAS 17.

Each of the items above are further described below.

4.6.1 Need for categorization

In the analysis performed for this issue paper, we have identified the potential need for categorization of military assets at the accounting standard level in the following areas:

- Intangible versus tangible military assets: there is a potential need to differentiate between intangible and tangible military assets at an accounting standard level. By making this categorization it can be explained that for the intangible military assets a different accounting standard, the standard applicable to intangible assets, will apply;
- Initial measurement: in EY's view, the acquisition cost can be applied to all military assets. However, it should be explored whether there exist military assets that do not deteriorate. If such assets exist and conceptual sound arguments which defend the different accounting treatment can be found, the application of a non-revisable amount might be appropriate;
- Subsequent measurement: in EY's view, the cost model can be applied to all military assets. However, it should be explored whether there are military assets that do not deteriorate. If such assets exist and conceptual sound arguments which defend the different accounting treatment can be found, it might be appropriate to allow not to depreciate nor impair these assets;

4.6.2 Need for supplementary guidance

In the analysis performed for this issue paper, we have identified a need for supplementary guidance for military assets at the accounting standard level in the following areas:

- Componentization of military assets at initial recognition: application of the component approach can be time-consuming, cumbersome and an administrative burden. More guidance can be useful to reduce diversity in practice such as the inclusion of thresholds in accordance with the materiality principles in IPSAS. If more guidance on the component approach would be considered under EPSAS, the advantages and disadvantages listed in section 4.1.2 should be taken into account;
- Economic ownership of military assets: determining the economic ownership of military assets can be complex as one government entity might own the asset while it is used by another government entity. Additional guidance as for example provided in the French accounting framework or NAF can be useful;
- Initial recognition: some of the national public sector accounting frameworks analysed and the NAF include thresholds for capitalization. The need to define common thresholds should be explored as to reduce the administrative burden that can be created by requiring capitalization of all military assets that meet the initial recognition criteria. The Cell on First Time Implementation suggests in this perspective to recognize the short term, high turnover military assets under the inventories instead of property, plant and equipment;
- Recognition of subsequent expenditures: additional guidelines can be provided considering the difficulties perceived by Member States currently applying IPSAS to differentiate between repairs, maintenance and expenses of a capital nature. Next to that, it is clear that in practice Member States deviate from IPSAS when it comes to

accounting for spare parts and ammunition. In our view, the reasons and arguments for this deviation needs to be discussed with the EPSAS stakeholders;

- Internally developed military assets: it was noted that amongst the Member States there is currently diversity in practice in terms of accounting rules being applied. Additional guidance tailored to the specificities of military assets might be needed to resolve this;
- Impairment: monitoring impairment for military assets can be cumbersome. To smoothen this process, impairment indicators tailored to specific types of military asset would be helpful. If specific impairment indicators for military assets would be considered under EPSAS, possibly further guidance would be needed;
- Presentational sensitivity: additional guidance is needed to tackle the issue of presentational sensitivity, which will exist if the general property, plant and equipment disclosure requirements are to be applied to the military assets. The information in section 4.2.1 is to be considered when discussing this matter with the EPSAS stakeholders.

4.6.3 Potential simplifications

Next to the above, in EY's view, it should be considered whether the option in IPSAS 17 to apply either the cost or the revaluation model can be removed or narrowed down.[86] The discussion on this matter can be conducted based on the advantages and disadvantages listed in section 4.5.

86 We refer to issue paper on "Approach for narrowing down of options within IPSAS" from 22 June 2016 where the option to apply the cost or the revaluation model for PP&E has already been identified as a critical issue.

4.7 What are the consequences for a possible convergence between IPSAS and GFS/ESA?

As has been shown in section 3.4, under ESA military assets are recorded in the statement of financial position as part of the "fixed assets" (AN.11) category. Hence, since IPSAS also recognizes military assets in the statement of financial position, both ESA and IPSAS will show military assets in their respective statements of financial position.

The main difference between ESA and IPSAS stems from the diverging impacts of assets on their respective surplus/deficit calculations, i.e. on the statement of financial performance under IPSAS and on the net lending(+)/borrowing(-) under ESA. Under ESA rules, acquisitions (or constructions) of fixed assets are recorded as capital expenditures within surplus/deficit in the period of acquisition. Since they are recorded within surplus/deficit for their full amount in the year of acquisition, their impact on government deficit is described as a "one-shot" impact. The same holds true for capital grants under ESA. They are also going directly into surplus or deficit. It is to be noted that this difference applies to the entire category of property, plant and equipment and is not specific for military assets.

In contrast, under IPSAS, the surplus/deficit impact only appears over time, namely through yearly depreciation expenses and/or impairments. Yearly depreciation expenses might be off-set by corresponding revenues based on the derecognition of performance obligations related to capital grants.

A further difference between IPSAS and ESA is that, in practice, ESA applies a group or portfolio valuation approach (through the perpetual inventory method, see section 3.4.3 above) rather than an individual asset measurement approach as would be the case under IPSAS. Another difference with respect to measurement is impairment. As outlined before, the concept of impairment is not used under ESA (ESA records consumption of fixed capital and other volume changes for catastrophic losses instead) and as such no regular impairment assessments are allowed.

The figure below illustrates this difference in impact on surplus/deficit under both systems using the example of an acquisition of military asset for a cost of EUR 10 million and a useful life of 5 years. As can be seen in the figure, the impact on government deficit is a "one-shot" in year 0 under ESA 2010 whereas it is spread over the asset's useful life under IPSAS:

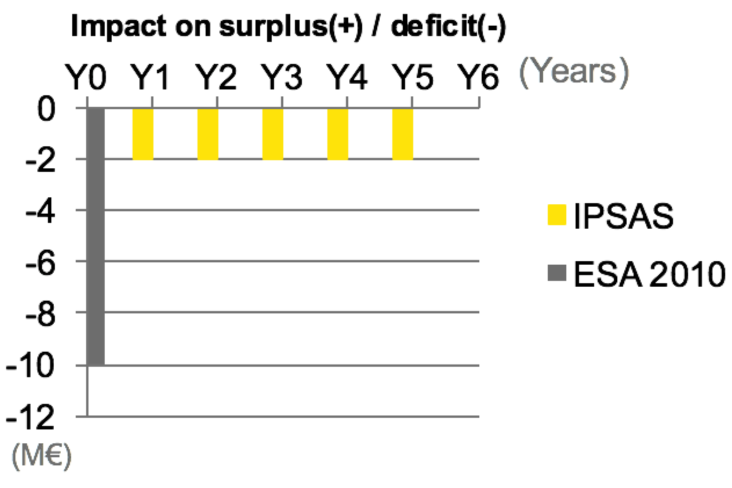

Figure 6: Impact of military acquisition under IPSAS and under ESA

Finally, as regards to a possible convergence between IPSAS and ESA, the analysis shows that convergence can be achieved at the level of the statement of financial position recordings but not at the level of the surplus/deficit calculation. In fact, by choosing the revaluation model for military assets under IPSAS, this would in principle ensure convergence at statement of financial position level since in this case IPSAS and ESA would both use current value approaches for measuring military assets in the statement of financial position. However, because of the difference in the treatment of capital expenditures under IPSAS and ESA (see above), convergence cannot be achieved at the level of the surplus/deficit calculation.

5. Develop an approach for organizing the future discussion on military assets with the EPSAS stakeholders

In EY's view, the general accounting requirements under IPSAS 17 for property, plant and equipment and under IPSAS 31 for intangible assets can be applied to military assets. However, through the analysis performed for this paper it was noted that practical application difficulties do exist. In this issue paper the need for categorization of military assets, additional guidance and reducing the current options in IPSAS 17 are listed as matters for discussion with EPSAS stakeholders, which can help to overcome these difficulties.

It is to be noted that taking stock is a first step before applying accrual based accounting/IPSAS. Member States that do not have an inventory in place should take into account, especially given the sensitive nature of military assets, that this is a time-consuming and complex exercise. In practice, the Member States selected for analysis are putting in place capitalization thresholds to simplify the stock taking process at the date of transition. In EY's view, whether or not a common materiality or capitalization threshold is needed is to be further discussed with the EPSAS stakeholders.

The following table can be used to facilitate the discussions indicated above:

	Practical application difficulties	**Matters for discussion with EPSAS stakeholders**
Definition	No categorization is foreseen in IPSAS 17. Therefore, there are no practical application difficulties at the moment.	In practice, Member States are currently categorizing military assets and defining specific accounting treatments based on this categorization. Given the fact that no guidance is provided in IPSAS 17, there is a diversity in practice. The need for categorization in order to define specific accounting rules and from a presentational point of view is therefore a matter for discussion with the EPSAS stakeholders. This discussion can be conducted considering the argumentation in section 4.6.1.
Recognition	No guidance is included in the property, plant and equipment accounting standard (IPSAS 17) on how to determine the economic ownership of military assets. However, this can be complex in cases where the asset is owned by another entity as the one operating the asset.	The possibility to include additional guidance to support entities in making the economic ownership assessment can be explored. The French accounting framework and the NAF can be taken as an example of how this guidance could look like.
	If IPSAS 17 would be followed, military assets would need to be divided in components (component approach) at the time of initial recognition. However, it has to be considered that military	Whether or not the component approach should be applied to all military assets is a matter for discussion considering the following advantage and disadvantage:

	assets are very complex assets with many different components having different useful lives.	(+) Faithful representation of the statement of financial position (-) Time-consuming leading to a high implementation cost If it is concluded that the component approach is to be applied, in EY's view, additional guidance is recommended to avoid diversity in practice.
	The application of the IPSAS 31 guidelines on internally generated military assets can be cumbersome and time-consuming.	It should be discussed whether the disadvantages and practical difficulties of applying IPSAS 31 outweighs its advantages: (-) Time-consuming and Cumbersome (+) Faithful representation of the statement of financial position In the discussion, the advantage versus the disadvantage needs to be weighed considering the significance of self-developed assets in relation to the overall military assets.
	Subsequent expenditure is to be divided into items of a capital nature and items to be accounted for as expenses that impact surplus or deficit. During the analysis performed for this issue paper it was noted that in practice this can be complex when applied to military assets.	The possibility to include additional guidance to support entities in making this analysis can be explored. The national public sector accounting frameworks analysed can be taken as an example of how this guidance could look like.
Measurement	Initial measurement at the acquisition cost is appropriate for the majority of the military assets. No practical application difficulties have been identified for determining acquisition cost.	In EY's view, there are no matters for discussion with EPSAS stakeholders re. the initial measurement of military assets. We assume that using a non-revisable amount for measurement purposes is also based on acquisition cost.
	Subsequent measurement can be done using the cost model or the revaluation model. The revaluation model can be complex to apply to military assets due to the potential absence of an active market. This will result in Member States being required to set-up estimation/valuation models to perform the yearly revaluation. A further approach is to neither	Considering the advantages and disadvantages of both primary models listed in this issues paper, it has to be explored whether the current option to use the revaluation model can be removed from a practical point of view. Next to that, the existence of military assets that do not deteriorate needs to be further discussed.

	depreciate nor impair certain military assets and to use a non-revisable amount for subsequent measurement. In practice however, it might be questioned whether there are military assets that are not subject to wear and tear.	
Disclosures	If IPSAS 17 would be followed, the general property, plant and equipment disclosure requirements would have to be applied to military assets. These requirements do not take into consideration the sensitive nature of military assets.	The presentational sensitivity has to be considered. Therefore the need for and the extent of separate line items in the statement of financial position and separate disclosures in the notes to the financial statements is a matter for discussion.

Table 16: Summary practical application difficulties and the resulting matters for discussion

Annex 1: NAF capitalisation thresholds and indicators of control

Capitalisation thresholds for property, plant and equipment

The following recognition thresholds have been defined in the NATO accounting rule for each category of tangible military assets:

Category of military assets	Threshold in EUR	Useful life in years	Depreciation method
Land	200.000	N/A	N/A
Buildings	200.000	40	Straight line
Other infrastructure	200.000	40	Straight line
Installed equipment	30.000	10	Straight line
Machinery	30.000	10	Straight line
Vehicles	10.000	5	Straight line
Aircraft	200.000	Dependent on type	Straight line
Vessels	200.000	Dependent on type	Straight line
Mission equipment	50.000	3	Straight line
Furniture	30.000	10	Straight line
Communications	50.000	3	Straight line
Automated information systems	50.000	3	Straight line

Capitalisation thresholds for intangible assets

The following recognition thresholds have been defined in the NATO accounting rule for each category of intangible military assets:

Category of military assets	Threshold in EUR	Useful life in years	Depreciation method
Computer software (commercial off the shelf)	50.000	4	Straight line
Computer software (bespoke)	50.000	10	Straight line
Computer database	50.000	4	Straight line
Integrated system	50.000	4	Straight line

Control indicators

Ten control indicators have been defined in the NATO accounting rule:

1. The act of purchasing the asset carried out (or resulted from instructions given) by the NATO reporting entity;
2. The legal title is in the name of the NATO reporting entity;
3. The asset is physically located on the premises or locations used by the NATO reporting entity;
4. The asset is physically used by staff employed by the NATO reporting entity or staff working under the NATO reporting entity's instructions;
5. The fact that the NATO reporting entity can decide on an alternative use of the asset;
6. The fact that the NATO reporting entity can decide to sell or to dispose the asset;
7. The fact that the NATO reporting entity, if it has to remove or destroy the asset, can take the decision to replace it;
8. The fact that a representative of the NATO reporting entity regularly inspects the asset to determine its current condition;
9. The fact that the asset is used in achieving the objectives of the NATO reporting entity;
10. The fact that the asset will be retained by the NATO reporting entity at the end of the activity.

Control is evidenced as from the moment that six control indicators are met.

Annex 2: Summary accounting treatment national public sector accounting frameworks versus the IPSAS 17 treatment.

	IPSAS 17	French accounting framework	Austrian accounting framework	Belgian accounting framework
Definition of military assets	IPSAS 17 does not define military assets, but specifies that these meet the definition of property, plant and equipment. IPSAS 17 does not categorize military assets nor provides examples.	CGAS 6 does not define military assets, but specifies that these are one of the classes of property, plant and equipment. CGAS 6 categorizes military assets into two main categories and four sub-categories.	The Austrian accounting framework does not define military assets, but specifies that these meet the definition of property, plant and equipment. The Austrian accounting framework does not categorize military assets.	The Belgian accounting framework has put in place a definition based on ESA. The Belgian accounting framework categorizes military assets into four categories.

	IPSAS 17	French accounting framework	Austrian accounting framework	Belgian accounting framework
Recognition	IPSAS 17 requires the application of the general initial recognition criteria. Application of the component approach is required. Subsequent expenditure: ▶ Repairs and maintenance are expensed; ▶ Replacement parts are recognized when the recognition criteria are met. If not, they are classified under the inventories; ▶ Costs of major inspections are recognized if these are a condition to continue to operate the asset.	In addition to IPSAS 17 a control criterion is put in place to help define economic ownership. The component approach is not applied. In addition to IPSAS 17, more guidelines are included in order to facilitate determining whether subsequent expenditure are to be capitalized.	The Austrian framework requires the application of the general initial recognition criteria. A capitalization threshold is used. The component approach is not applied. In addition to IPSAS 17, more guidelines are included in order to facilitate determining whether subsequent expenditure are to be capitalized.	The Belgian framework requires the application of the general initial recognition criteria. The component approach is not applied. In addition to IPSAS 17, more guidelines are included in order to facilitate determining whether subsequent expenditure are to be capitalized.

	IPSAS 17	French accounting framework	Austrian accounting framework	Belgian accounting framework
Measurement	IPSAS 17 requires the application of the general measurement rules to military assets.	Next to the acquisition cost, the CGAS also introduces the token or non-revisable amount.	Military assets are measured at acquisition cost.	Military assets are measured at acquisition cost.
	Subsequently, the cost or revaluation model are to be used.	Next to the cost model, the CGAS also introduces a model in which military assets are not depreciated nor impaired.	Subsequently, the cost model is applied.	Subsequently, the cost model is applied. Depreciation rules are set per category of military assets.
	The component approach is to be applied.	The component approach is not applied.	The component approach is not applied.	The component approach is not applied.
	IPSAS 21 and 26 are to be applied for impairment purposes.	As described above, not all military assets are subject to impairment testing.	IPSAS 21 and 26 are applied for impairment purposes.	No information could be obtained regarding impairment.
Disclosures	IPSAS 17 requires the application of the general disclosure requirements.	CGAS requires the application of the general disclosure requirements.	Limited information is provided in the financial statements due to the presentational sensitivity.	Limited information is provided in the financial statements due to the presentational sensitivity and due to the fact that IPSAS is not applied and therefore disclosure requirements are less extensive.

	National framework deviates from IPSAS 17
	National framework provides supplemental guidance compared to IPSAS 17
	National framework is in line with IPSAS 17

Annex 3: Austrian capitalisation thresholds

The following recognition thresholds have been defined in the Austrian national public sector accounting framework:

Year of acquisition asset	**Recognition threshold in EUR**
2013 – to date	400
2007-2013 (year opening balance sheet)	1.000
2004-2007	100.000

Annex 4: Difficulties encountered by the Member States analysed in the stock-taking process

French Member State[78]	To facilitate the stock-taking process, the French Member State took the following measures: ► Only the most important items were subject in the stock-taking process to exhaustive data compilation (weapons is given as an example); ► A complete or partial stock-taking was only conducted for Ministry departments where the assets (military equipment is given as an example) were considered significant either financially or in terms of activity; ► Non-significant items were not subject to any inventory and were compiled when possible based on accumulated budget flows; ► In certain specific cases (including work in progress on the military weapon programmes), lump sum or statistical methods were used to facilitate the stock-taking process; and ► The items involving a significant degree of difficulty with regard to their inventory and/or valuation (including some military assets) were not included in the stock-taking process at first-time implementation given the lack of availability of robust information.
Austrian Member State	► The main difficulty encountered at first-time adoption was to define the scope of the opening balance sheet; ► Capitalization thresholds were set in order to overcome this hurdle.
Belgian Member State	► The main difficulty encountered at first-time adoption was to define the scope of the opening balance sheet; ► The guidance and descriptions of military assets provided by ESA were consulted to overcome this hurdle.

78 See PwC, Collection of information…, Brussels, 1 August 2014, page 159.

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