



EUROPEAN COMMISSION
EUROSTAT

Directorate C: National accounts, prices and key indicators
Task Force EPSAS

EPSAS WG 18/02
Luxembourg, 10 April 2018

EPSAS Working Group
To be held in Luxembourg
on 7-8 May 2018, starting at 09:30

Item 6 of the Agenda

**EPSAS issue paper on accounting treatment of grants and
other transfers**

*Paper by PwC on behalf of Eurostat
- for discussion*



Accounting treatment of grants and other transfers with a view to financial reporting requirements under the future European Public Sector Accounting Standards (EPSAS)

March 2018

Table of Contents

1	Objectives of the issue paper	6
2	Background of the issue	7
3	Description of accounting guidance available in international accounting frameworks and in statistical rules	9
3.1	International Public Sector Accounting Standards (IPSAS).....	9
3.1.1	Applicable standards.....	9
3.1.2	IPSAS 23 ‘Revenue from non-exchange transactions (taxes and transfers)’	9
3.1.2.1	Scope and definitions.....	9
3.1.2.2	Recognition.....	10
3.1.2.3	Measurement.....	12
3.1.2.4	Application of recognition and measurement principles to grants and other transfers	13
3.1.2.5	Presentation and disclosures	13
3.1.3	Current IPSAS rules regarding expenses from non-exchange transactions	14
3.2	European Union Accounting Rules (EAR)	15
3.2.1	Applicable standards.....	15
3.2.2	EAR 3 ‘Expenses and payables’	15
3.2.2.1	Scope and definitions	15
3.2.2.2	Recognition.....	16
3.2.2.3	Measurement.....	17
3.2.2.4	Cut-off and pre-financing	17
3.2.2.5	Presentation and disclosures	18
3.3	International Financial Reporting Standards (IFRS)	18
3.3.1	Applicable standards.....	18
3.3.2	IAS 20 ‘Accounting for government grants and disclosure of government assistance’ ..	19
3.3.3	IFRS 15 ‘Revenue from contracts with customers’	19
3.4	ESA 2010.....	21
3.4.1	Scope and definitions	21
3.4.2	Recognition.....	22
3.4.3	Measurement.....	22
3.4.4	Transactions with international or supranational organisations.....	22
3.5	Comparison between the different international financial reporting frameworks.....	24
3.5.1	Grants and other transfers received	24
3.5.1.1	Scope and definitions.....	25
3.5.1.2	Recognition.....	26
3.5.1.3	Measurement.....	26
3.5.2	Grants and other transfers given	26
3.5.2.1	Scope and definitions.....	27
3.5.2.2	Recognition and measurement.....	28
3.6	IPSASB current projects on revenue and non-exchange expenses	28

3.6.1	IPSASB project on revenue	28
3.6.2	IPSASB project on non-exchange expenses	31
4	Description of the accounting for grants and other transfers in selected EU Member States (Latvia and Belgium) and one international organisation (the European Commission)	33
4.1	Overall accounting maturity for accounting for grants and other transfers by EU Member States	33
4.2	Selection of benchmark entities used in the analysis and methodology	35
4.3	Latvia	35
4.3.1	Grants and other transfers received	35
4.3.2	Grants and other transfers given	37
4.4	Belgium	38
4.4.1	Grants and other transfers received	38
4.4.2	Grants and other transfers given	39
4.5	European Commission (EC)	40
4.5.1	Applicable accounting rules and scope of analysis	40
4.5.2	Grants and other transfers given	41
4.5.2.1	Entitlements	42
4.5.2.2	Transfers under agreements	42
4.5.2.3	Discretionary grants	43
4.6	Comparison between the different countries and the EC	43
4.6.1	Grants and other transfers received	43
4.6.2	Grants and other transfers given	44
5	Difficulties/issues when accounting for grants and other transfers	46
5.1	Conceptual difficulties	46
5.1.1	Absence of IPSAS standard dealing with non-exchange expenses	46
5.1.2	Problems in determining whether revenue transactions are exchange or non-exchange	47
5.1.3	Problems in determining whether a stipulation is a condition or a restriction under the current IPSAS 23 and how to interpret the concept of public sector performance obligation under the new proposed guidance	47
5.1.4	Lack of guidance on how to account for grants related to assets	48
5.1.5	Lack of guidance on how to account for long-term / multi-year grants	48
5.1.6	Grants and other transfers received as principal or agent	48
5.1.7	Grants that are in substance financing arrangements	48
5.1.8	Accounting for government appropriations	49
5.1.9	Presentation and disclosure of grants and other transfers	49
5.2	Practical difficulties	49
5.2.1	Inventory of all grants and other transfers and data collection	49
5.2.2	Consistent accounting for all types of grants and other transfers	50
5.2.3	Cut-off procedures at year end	50
5.2.4	Reconciliation of inter-government transactions in consolidation	50
6	Discussion of matters relevant for a European harmonisation	52
6.1	Need for more practical application guidance on the future EPSAS standards	52

6.2	Strategic approach for the EPSAS standard setting	52
6.3	Technical accounting discussion on the conceptual approaches in relation to certain specific accounting issues	53
6.3.1	Absence of IPSAS standard dealing with non-exchange expenses.....	54
6.3.2	Problems in determining whether revenue transactions are exchange or non-exchange	54
6.3.3	Problems in determining whether a stipulation is a condition or a restriction under the current IPSAS 23 and how to interpret the concept of public sector performance obligation under the new proposed guidance	55
6.3.4	Lack of guidance on how to account for grants related to assets	55
6.3.5	Lack of guidance on how to measure long-term / multi-year grants.....	55
6.3.6	Other accounting issues relating to grants and other transfers received.....	56
7	PwC's recommendations on the way forward.....	57
7.1	Need for more practical application guidance on the future EPSAS standards.....	57
7.2	Strategic approach for the EPSAS standard setting.....	57
7.3	Technical accounting discussion on the conceptual approaches in relation to certain specific accounting issues.....	58

Table of Figures

Figure 1: IPSAS, EAR, IFRS and ESA 2010 rules for grants and other transfers received compared	24
Figure 2: IPSAS, EAR, IFRS and ESA 2010 rules for grants and other transfers given compared	27
Figure 3: Average accounting maturity per accounting area across the EU	33
Figure 4: Timing of recognition of revenue from transfers	34
Figure 5: Timing of recognition of grants and other transfers provided	34

1 Objectives of the issue paper

The aim of this issue paper is to summarise the approaches taken at the accounting standard level concerning the most important types of grants and other transfers in two European Union Member States ('EU MS') and one international organisation with high accounting maturity. It addresses the approaches that are being used under the existing international financial reporting frameworks (IPSAS, EAR, IFRS and ESA 2010 including the MGDD¹), or are likely to be developed (IPSASB projects).

Based on the request from Eurostat, the issue paper addresses the following questions:

- What are the most important categories and characteristics of grants and other transfers received and given by government entities, the EU and other international institutions, and for which may problematic points/issues with regards to definition, recognition, measurement and presentation arise?
- Which accounting guidance is available for grants and other transfers in IPSAS, EAR, national accounting standards in two EU MSs, IFRS and ESA 2010 and, where relevant and applicable also MGDD?
- How do the analysed approaches in the two MSs and the international organisation differ from the treatment under IPSAS?
- For the main categories of grants and other transfers, what are the advantages and disadvantages of the existing approaches to recognition and measurement under the existing standards (IPSAS, EAR, national accounting standards in EU MSs, IFRS and ESA 2010 and, where relevant and applicable, also MGDD)?
- What are the main difficulties/issues when accounting for the main categories of grants and other transfers?
- If/how a European harmonisation could be achieved in accounting for the main categories of grants and other transfers?
- Taking into account costs and benefits, what way forward in practice would PwC recommend for EPSAS on grants and other transfers?
- What were the consequences of the recommended way forward for a possible convergence between IPSAS /EPSAS and ESA 2010 (and if relevant and applicable, also MGDD)?

Based on the analysis performed, an approach for organising the future discussion on grants and other transfers with the EPSAS stakeholders is proposed.

¹ Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 edition

2 Background of the issue

Grants and other transfers represent a significant share of non-exchange transactions of governments who can act either as their grantors or recipients. Consequently, the accounting treatment of grants and other transfers both provided and received (non-exchange transactions with and without conditions, with and without eligibility criteria attached) is of particular importance.

Grants are frequently provided from one level of government to another or from donors like the World Bank (WB) or the International Monetary Fund (IMF) to governments. In the EU MSs, an important amount of transfers may be paid to or received from the EU. Consequently, accounting for EU grants (transfer payments received) is of particular interest. In addition, national authorities are not only recipient of EU funding, but do also grant EU transfers to others, including lower government level agencies. Finally, governments also frequently give grants and other transfers to third parties to achieve a certain economic or social objective. Thus, not only the volume of transactions is large, but there are also different types of grants and other transfers that are either given or received by governments. The terms and conditions of each individual transaction might vary.

The report commissioned by Eurostat and prepared by PwC in 2014 indicates that the treatment of grants and other transfers varies widely among the central governments in the EU MSs. According to the report, only 10 countries out of 28 EU MSs recognise expenses from grants and other transfers at the time when the conditions attached to the grant have been fulfilled by the recipient/beneficiary, whereas for four countries the timing was linked to the point in time when the invoice or cost claim is received. One country linked it to the time when budgetary commitment was made and cash-based accounting was used in the remaining 13 countries. On the revenue side, there is similar diversity in practice: most of the EU MSs (15 out of 28) recognise revenue from grants and other transfers when cash is received. Others recognise revenue when the right to receive the grant is established or when the conditions attached to the grant are fulfilled.

In addition to this, practical application of the accounting principles related to grants and other transfers appears to be difficult in practice. The Staff Working Document accompanying the report from the Commission to the Council and the European Parliament COM (2013) 114 assessing the suitability of IPSAS for the EU MSs, in Annex 7.1, points out that IPSAS 23 ('Revenue from non-exchange transactions (taxes and transfers)') is among the standards that need adaptation, or for which a selective approach is needed. More specifically, the document mentions in Annex 6.1 (page 114) that 'The distinction criteria for conditions and restrictions for accounting of grants are also perceived as difficult'. The 2014 PwC study² which analysed the suitability of IPSAS for EU Member States included IPSAS 23 in category 2, i.e. the category of standards that (may) need (some) amendments or for which implementation guidance is (may be) needed.

To improve the accounting for revenue and non-exchange expenses, the IPSASB issued a consultation paper (CP) in August 2017 ('Accounting for revenue and non-exchange expenses'). The IPSASB project team has partially identified some of the issues related to non-exchange expenses by conducting interviews with preparers, although the IPSASB acknowledged that the sample chosen was not fully representative.

² See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 134-135.

The main drivers of the related IPSASB project are the following:

- Current IPSAS distinguish between exchange and non-exchange transactions. The determination whether a transaction is exchange or non-exchange in nature is highly judgemental and causes many problems in practice.
- There is currently no IPSAS dealing with non-exchange expenses, which leads to ambiguity and inconsistency in the accounting practice.
- Several application issues regarding IPSAS 23 were identified.
- As under IFRS a new standard for revenue recognition was issued, the CP should promote the convergence between IPSAS and IFRS.
- The approaches applied by resource providers and resource recipients should be consistent.

The deadline for comments on the CP was 15 January 2018.

As the IPSASB CP made a first analysis of the issues relating to the accounting for grants and other transfers in a rather comprehensive way, it can be considered as a good starting point for a deeper analysis of the issue between Member States.

Conversely, the present issue paper may contribute to the IPSASB thinking by providing a more comprehensive analysis at the European level.

3 Description of accounting guidance available in international accounting frameworks and in statistical rules

Accounting guidance available is discussed below, successively for the following accounting and reporting frameworks: IPSAS, EAR, IFRS and ESA 2010 (including references to the MGDD).

IPSAS rules are explained more in-depth because IPSAS has been viewed as a reference framework for the future EPSAS and EAR are based on them. In addition to the current IPSAS 23 which deals with revenue from non-exchange transactions, the IPSASB issued a CP on revenue and non-exchange expenses which, as highlighted in chapter 2 of the present issue paper, provides a very useful starting point for organising the discussion on the accounting for non-exchange transactions, including grants and other transfers, among EPSAS stakeholders.

3.1 International Public Sector Accounting Standards (IPSAS)

3.1.1 Applicable standards

Under IPSAS, one standard specifically deals with the accounting for non-exchange transactions, which include grants and other transfers: IPSAS 23 ‘Revenue from non-exchange transactions (taxes and transfers)’. As there is currently no particular standard dealing with non-exchange expenses, the IPSASB Conceptual framework and IPSAS 1 ‘Presentation of financial statements’ need to be considered in the analysis as well.

IPSAS 23 describes the accounting for revenue from non-exchange transactions, i.e. transactions where an entity receives value from another entity without directly giving approximately equal value in exchange. It contains guidance regarding revenue recognition and measurement (IPSAS 23.1). Besides accounting for revenue from taxes, the standard addresses the accounting of revenue from transfers (e.g. received Member States’ contributions to international public organisations, grants received).

The IPSASB Conceptual framework (CF) and IPSAS 1 include definitions of revenue and expenses which indicate when non-exchange revenue and expenses should be recognised.

In addition to that, the IPSASB issued a CP on revenue and non-exchange expenses which includes in its scope the accounting for grants and other transfers given and received (except for social benefits). We refer to section 3.6 for more details.

3.1.2 IPSAS 23 ‘Revenue from non-exchange transactions (taxes and transfers)’

3.1.2.1 Scope and definitions

IPSAS 23 applies to the accounting for revenue from non-exchange transactions (IPSAS 23.2). Therefore, the terms ‘revenue’ and ‘non-exchange transactions’ are described below.

Generally, revenue arises from both exchange and non-exchange transactions (CF 2.7). The Conceptual framework defines revenue as ‘increases in the net financial position of the entity, other than increases arising from ownership contributions’ (CF 5.29). Ownership contributions are ‘inflows of resources to an entity, contributed by external parties in their capacity as owners, which establish or increase an interest in the net financial position of the entity’ (CF 5.33).

As per IPSAS 23.12, revenue ‘comprises gross inflows of economic benefits or service potential received and receivable by the reporting entity’. In contrast, amounts collected as an agent on behalf of the government, another government organisation or other third parties are not revenue.

Non-exchange transactions are ‘transactions in which an entity receives value from another entity without directly giving approximately equal value in exchange’ (CF 2.7).

Summing up, IPSAS 23 applies when an entity receives resources and provides no or nominal consideration directly in return (IPSAS 23.9). There might also be combinations of exchange and non-exchange transactions. In this case, the entity provides goods or services in return for the resources received, but the fair value of these goods or services does not approximate the fair value of the resources received (e.g. a loan at an interest rate below market terms). In such a transaction, the exchange and the non-exchange components should be accounted for separately (IPSAS 23.10; regarding concessionary loans: IPSAS 23.105Af). For identifying and separating an exchange component and a non-exchange component, significant judgement is required.

IPSAS 23 distinguishes between two major types of non-exchange revenue: taxes and transfers. Considering the purpose of this paper, only transfers will be discussed.

Transfers are ‘inflows of future economic benefits or service potential from non-exchange transactions, other than taxes’ (IPSAS 23.7). Taxes are defined as ‘economic benefits or service potential compulsory paid or payable to public sector entities, in accordance with laws and/or regulations, established to provide revenue to the government. Taxes do not include fines or other penalties imposed for breaches of the law’ (IPSAS 23.7).

Examples of transfers that lead to the recognition of revenue

IPSAS 23 paragraph 77 lists the following examples of transfers in terms of IPSAS 23: grants, debt forgiveness, fines, bequests, gifts, donations, and goods and services in-kind.

The standard IPSAS 23 is of particular interest for governments that receive revenue through grants or other transfers as these transactions qualify as non-exchange. IPSAS 23 provides specific guidance how the receipt of these transfers should be treated and at what point in time revenue should be recognised.

3.1.2.2 Recognition

IPSAS 23 takes a two-step approach to revenue recognition:

- At first, it is determined whether an asset should be recognised in respect of the inflow of resources from the non-exchange transaction.
- If an asset is recognised, revenue is then recognised to the extent that no liability is recognised in respect of the same inflow.

Recognition of an asset

An asset arising from a non-exchange transaction is recognised when the entity gains control of resources that meet the definition of an asset and satisfy the recognition criteria (IPSAS 23.29).

The Conceptual framework defines an asset as a resource presently controlled by the entity as a result of a past event (CF 5.6). A resource is an item with service potential or the ability to generate

economic benefits (CF 5.7). Thus, control of the transferred asset is crucial for its recognition in the entity's financial statements: control generally 'arises when the entity can use or otherwise benefit from the asset in pursuit of its objectives, and can exclude or otherwise regulate the access of others to that benefit' (IPSAS 23.7). The past event on which the entity gains control over the assets may for example be a transfer (IPSAS 23.34).

An inflow of resources from a non-exchange transaction (meeting the definition of an asset) is recognised as an asset 'when, and only when:

- (a) It is probable that the future economic benefits or service potential associated with the asset will flow to the entity; and
- (b) The fair value of the asset can be measured reliably.' (IPSAS 23.31).

The inflow of resources is probable 'when the inflow is more likely than not to occur' (IPSAS 23.31), (i.e. the probability has to be higher than 50 percent). The determination of whether the inflow is probable requires judgement and should be based on the entity's past experience with similar flows of resources and its expectations regarding the transferor (IPSAS 23.35).

Recognition of revenue

As a reminder, an inflow of resources from a non-exchange transaction recognised as an asset shall be recognised as revenue, except to the extent that a liability is also recognised in respect of the same inflow (IPSAS 23.44). This means that revenue is generally recognised when net assets increase (IPSAS 23.46).

If an entity recognises a liability in respect of the inflow from a non-exchange transaction, revenue recognition is (partially or completely) deferred. The carrying amount of the liability is subsequently reduced when the present obligation is satisfied. A reduction in the liability also leads to the recognition of revenue (IPSAS 23.45).

Recognition of a liability

When there is a present obligation arising from a non-exchange transaction that meets the definition of a liability, it is recognised as a liability 'when, and only when the recognition criteria are met:

- (a) It is probable that an outflow of resources embodying future economic benefits or service potential will be required to settle the obligation; and
- (b) A reliable estimate can be made of the amount of the obligation.' (IPSAS 23.50).

Stipulations on transferred assets are terms in laws or regulation, or a binding arrangement, imposed on the use of a transferred asset by an external party (IPSAS 23.7). Stipulations are either conditions or restrictions and a distinction has to be made between the two for accounting purposes.

Conditions require returning the transferred asset or future economic benefits/service potential to the transferor in the event that the conditions are not met, i.e. the future economic benefits or service potential embodied in the asset transferred is not consumed by the recipient as specified.

Restrictions are ‘stipulations that limit or direct the purposes for which a transferred asset may be used, but do not specify that future economic benefits or service potential is required to be returned to the transferor if not deployed as specified’ (IPSAS 23.7).

Therefore, conditions on transferred assets give rise to the recognition of a liability until the conditions are satisfied while restrictions on transferred assets do not.

In practice, grants or other transfers are often subject to an agreement between the grantor and the beneficiary. The question arises whether the grant agreement contains specific clauses that may give rise to a liability. If a transfer or grant is regulated by law, it should be examined whether the law contains any provisions that may lead to the recognition of a liability upon transfer of the asset. Each time, the substance of the arrangement needs to be considered.

In practice, the grant recipient recognises an asset when the right to receive the grant is established, and a corresponding liability to the extent any unfulfilled condition associated with the grant exists. When an entity receives resources (e.g. cash) before a transfer arrangement becomes binding, it recognises an asset together with an advance receipt liability (IPSAS 23.105). The liability reflects the existence of conditions that still needs to be fulfilled in order to recognise revenue.

Illustrative booking entries relating to the recognition of revenue with or without condition under IPSAS 23 (from the perspective of the recipient of the grant):

1.a. Grant is received/receivable and a condition exists

Dr Cash/grant receivable

To Cr Liability (deferred revenue)

1.b. Condition is fulfilled (possibly over-time)

Dr Liability (deferred revenue)

To Cr Revenue

2. Grant is received/receivable and no condition exists

Dr Cash/grant receivable

To Cr Revenue

3.1.2.3 Measurement

If an asset acquired through a non-exchange transaction is recognised, it is initially measured at its fair value as at the date of acquisition (IPSAS 23.42).

Revenue from non-exchange transactions is measured at the amount of the increase in net assets (IPSAS 23.48). Therefore, the amount of revenue that is recognised depends on the initial measurement of the asset acquired and of the amount of the potential liability for any present obligation in respect of the same inflow.

The liability that reflects the present obligation arising from a non-exchange transaction is initially measured at the best estimate of the amount required to settle the present obligation at the reporting date (IPSAS 23.55). Revenue is then recognised to the extent that the conditions attached to the grant or transfer have been fulfilled and the liability is derecognised and recycled through non-exchange revenue.

3.1.2.4 Application of recognition and measurement principles to grants and other transfers

IPSAS 23 includes guidance how to apply the revenue recognition and measurement principles described above to some specific types of non-exchange transactions. The specific provisions regarding transfers are discussed below.

Specific types of transfers

IPSAS 23 contains even more specific rules regarding certain types of transfers. The following applies in addition to the general recognition and measurement principles:

- Debt forgiveness: revenue is recognised when the former debt is derecognised (IPSAS 23.85) and measured at the carrying amount of the debt forgiven (IPSAS 23.87).
- Fines: revenue is recognised when the fine receivable meets the definition of an asset and satisfies the criteria for recognition as an asset (IPSAS 23.89).
- Bequests: revenue can only be recognised when the entity has an enforceable claim (e.g. on the death of the testator or the granting of probate) (IPSAS 23.90). Revenue is measured at the fair value of the resources received or receivable (IPSAS 23.92).
- Gifts and donations: revenue is typically recognised when the entity receives the gift or donation (IPSAS 23.93). Regarding the gift or donation of goods in-kind, this might already be the case when there is a binding agreement to receive the goods (IPSAS 23.96). Goods in-kind might, however, be subject to stipulations, which might defer revenue recognition (IPSAS 23.94 and 96).

If an entity receives services in-kind, it 'may but is not required to recognise services in-kind as revenue and as an asset' (IPSAS 23.98). Due to the many uncertainties surrounding services in-kind, including the ability to exercise control over the services, and measuring the fair value of the services, IPSAS 23 does not require the recognition of services in-kind. An asset resulting from services in-kind is in practice most often directly consumed, which then results in an expense being recognised together with revenue.

Moreover, IPSAS 23.104 clarifies that pledged items are not recognised as assets or revenue by the recipient entity as the control criteria have not been fulfilled.

3.1.2.5 Presentation and disclosures

In the statement of financial performance, revenue from non-exchange transactions is included in the line item 'revenue' (IPSAS 1.102(a)) or is presented as separate line-item if material (IPSAS 1.45).

Furthermore, IPSAS 23 contains comprehensive disclosure requirements. On the face of the statement of financial performance or in the notes, the entity should - in addition to other information - disclose the following:

- The amount of revenue from non-exchange transactions recognised during the period by major classes.
- The amount of receivables recognised in respect of non-exchange revenue.
- The amount of liabilities recognised in respect of transferred assets subject to conditions.
- The amount of assets recognised that are subject to restrictions and the nature of those restrictions.

- The existence and amounts of any advance receipts in respect of non-exchange transactions.
- The amount of any liabilities forgiven (IPSAS 23.106 (a), (b), (c), (d), (e) and (f)).

The accounting policies adopted for the recognition of revenue from non-exchange transactions should also be disclosed (IPSAS 23.107(a)).

3.1.3 Current IPSAS rules regarding expenses from non-exchange transactions

Governments and other public sector entities often incur large amounts of expenses arising from non-exchange transactions, in the pursuit of their policy and service delivery objectives. Social benefits represent a major class of non-exchange expenses but are excluded from the scope of the analysis of the present issue paper. No IPSAS standard on social benefits currently exists.

There is currently no IPSAS standard that deals with expenses from other non-exchange transactions either. This is one of the most significant gaps that remains in the suite of IPSAS standards.

When there is no IPSAS that is specifically applicable, management should use its judgment in developing and applying an accounting policy that results in relevant and reliable financial information. Management should first consider IPSAS dealing with similar and related issues and then the definitions, recognition and measurement criteria for assets, liabilities, revenue and expenses described in other IPSAS. Reference by analogy to IPSAS 23 ‘Revenue from non-exchange transactions’ is therefore appropriate. Management may also consider pronouncements from other standard-setting bodies (IPSAS 3.12 to 15). Finally referring to the definitions of elements and concepts in the Conceptual framework and IPSAS 1 is also useful.

The Conceptual framework defines expenses as ‘decreases in the net financial position of the entity, other than decreases arising from ownership distributions’ (CF 5.30). Ownership distributions are ‘outflows of resources from the entity, distributed to external parties in their capacity as owners, which return or reduce an interest in the net financial position of the entity’ (CF 5.34).

Expenses arise from exchange and non-exchange transactions, other events such as unrealised increases and decreases in the value of assets and liabilities, and the consumption of assets through depreciation and erosion of service potential and ability to generate economic benefits through impairments (CF 5.31).

Examples of transfers that lead to the recognition of expenses
Subsidies granted to beneficiaries, gifts, donations.

A definition of non-exchange transactions can be found in the Conceptual framework (CF 2.7). In addition to that, IPSAS 23 provides guidance in relation to the identification of non-exchange transactions. Please refer to section 3.1.2 of the present issue paper.

Governments may be engaged in multi-year expenditure programs. Grants may be given for a period that spans several reporting periods. Reasoning by analogy to the accounting treatment applicable to revenue arising from transfers under IPSAS 23, expenses from the perspective of the grantor/donor are incurred when a present obligation arises in accordance with the contractual clauses of the grant or subsidy agreement. The grant agreement often indicates the conditions the beneficiary needs to

comply with to secure the grant amount. In practice, the grantor should recognise expenditure to the extent the beneficiary has fulfilled these conditions without any future obligation of repayment. In practice, the stipulations of grants and similar agreements should be checked carefully to identify whether the entity has incurred an obligation and an expense should be recognised. It is also crucial to assess to which extent the beneficiary has fulfilled the conditions attached to the transfer.

Illustrative booking entries relating to the accounting for grants with or without condition using a reasoning by analogy to IPSAS 23 (from the perspective of the grantor):

1.a. Grant is given/recipient's right to receive the grant is established and a condition exists

Dr Asset (deferred expense/pre-financing)

To Cr Cash/grant payable

1.b. Condition is fulfilled (possibly over-time)

Dr Expense

To Cr Asset (deferred expense/pre-financing)

2. Grant is given/recipient's right to receive the grant is established and no condition exists

Dr Expense

To Cr Cash/grant payable

3.2 European Union Accounting Rules (EAR)

3.2.1 Applicable standards

The EAR constitute the accounting framework of the EU institutions, including the European Commission (EC) and its agencies.

EAR 17 'Revenue from non-exchange transactions (taxes and transfers)' deals with the accounting for non-exchange revenue, which includes grants and other transfers received. As EAR 17 is based on IPSAS 23 which is described in detail in section 3.1.2, its rules are not repeated here.

Regarding non-exchange expenses like grants and other transfers provided, the reference is EAR 3 'Expenses and payables'. EAR 3 deals with the accounting for both exchange and non-exchange expenses and the corresponding payables under an accrual basis of accounting.

3.2.2 EAR 3 'Expenses and payables'

3.2.2.1 Scope and definitions

EAR 3 'Expenses and payables' describes the accounting for expenses and the corresponding payables arising from both exchange and non-exchange transactions. Exchange expenses are considered to be similar to expenses in the private sector. However, there is a need to specify rules for the accounting for non-exchange expenses for the European Union (EU).

The definitions of non-exchange transactions, expenses and liabilities are drawn from IPSAS and are therefore not included in this section (please refer to sections 3.1.2 and 3.1.3. for the definitions under IPSAS).

Transfers (like grants and transfers from structural funds) are considered to be non-exchange in nature (EAR 3 section 2) and are defined as follows: ‘Transfers are amounts of money paid or to be paid by the EU to beneficiaries for which the EU do not:

- Receive any goods or services directly in return, as in the case of a purchase/sale transaction.
- Expect to be repaid in the future, as in the case of a loan, or
- Expect a financial return, as in the case of an investment.’ (EAR 3 section 3.8)).

EAR 3 distinguishes between three major types of transfers:

Entitlements	<p>‘(...) transfers that the European Union must make if the beneficiary meets specified eligibility criteria. Under this category, the European Union are automatically obliged to provide benefits to beneficiaries who meet the requirements laid down by the regulations (...)’ (EAR 3 section 4.4).</p> <p>Examples: European Agricultural Guarantee Fund (EAGF), European Agricultural Fund for Rural development (EAFRD) (together replacing the former European Agricultural Guidance and Guarantee Fund (EAGGF)).</p>
Transfers under agreements	<p>‘(...) are similar to entitlements in that the beneficiary has the right to a transfer if he meets the eligibility requirements. They are different, however, in that the beneficiary must spend money to be entitled to any reimbursement. But the main difference is that the terms of agreement are negotiated and agreed upon in a signed contract.’ (EAR 3 section 4.4)</p> <p>Examples: grants under agreements (e.g. DG RTD, DG DEVCO), structural funds (e.g. DG REGIO).</p>
Discretionary grants, contributions and donations	<p>‘The European Union can decide whether or not to make a transfer, what conditions must be fulfilled, if any, what amount will be transferred and who the beneficiaries are to be. (...)’ (EAR 3 section 4.4).</p>

3.2.2.2 Recognition

According to EAR 3 section 4.1, expenses - regardless of whether they are exchange or non-exchange - are recognised ‘when a decrease in future economic benefits or service potential related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably.’ This concept appears to be similar to the current definition of expenses under IPSAS. However, EAR 3 includes more specific rules and stipulates recognition criteria for each major type of transfer.

The general principle for the recognition of non-exchange expenses is that transfers should be recognised as expenses in the period during which the events giving rise to the transfer occurred (EAR 3 section 4.4). In addition to that, three recognition criteria need to be fulfilled.

- 1) The first criterion relates to the governing regulations and proper authorisation.
 - a. Regarding entitlements, the EU is automatically obliged to provide benefits if the beneficiary meets specified eligibility criteria. Therefore, the first criterion is met in this case when ‘the

nature of the transfer is allowed by regulation (Financial Regulation, Staff Regulations, or other specific regulation' (EAR 3 section 4.4(a)).

- b. As a signed contract is required for providing benefits from transfers under agreements, the first criterion is only met in this regard when 'a contract has been signed authorising the transfer (by a government body)' (EAR 3 section 4.4(b)).
- c. Under the last major type of transfers, the provision of benefits is at the discretion of the EU. Thus, no expense should be recognised before 'the transfer has been authorised (by a government body)' (EAR 3 section 4.4(c)).

The second and third criteria are the same for all major types of transfers: an expense is only recognised if:

- 2) Any eligibility criteria have been met by the beneficiary; and
- 3) A reasonable estimate of the amount can be made' (EAR 3 section 4.4(a)-(c)).

3.2.2.3 Measurement

Generally, exchange and non-exchange expenses and the corresponding payables should be measured at the fair value of the consideration given (EAR 3 section 4.1).

Entitlements are pre-recorded at the original payment request amounts. When the recognition criteria are met, the corresponding expense is measured at the eligible amount (EAR 3 section 4.4(a)).

Similarly, transfers under agreements are pre-recorded at the original value shown on the related cost claim or expense summary. When the recognition criteria are met, the corresponding expense is measured at the eligible amount. If there is a correction of the original value and the beneficiary contests the correction, a risk assessment is required and might lead to the recognition of an additional expense (EAR 3 section 4.4(b)).

Discretionary grants, contributions and donations are measured at the amount authorised (EAR 3 section 4.4(c)).

3.2.2.4 Cut-off and pre-financing

Under the accrual basis of accounting, transactions and events should be recorded in the period(s) to which they relate. For this reason, cut-off procedures must be performed at the end of the reporting period (EAR 3 section 4.1).

This means that it might be necessary to estimate part of the non-exchange expense incurred in the reporting period. For instance, the recognition criteria for entitlements might be fulfilled in the reporting period even if no formal request has been received yet. If new information becomes available later, estimates need to be revised and eventually adjusted ('change in estimates') (EAR 3 section 5.2).

EAR 5 'Pre-financing' provides accounting rules for payments of cash advances that are mainly paid within non-exchange transactions by EU institutions and bodies (EAR 5 section 1.). When such a

cash advance is paid, an asset is recorded (EAR 5 section 4.). As soon as the criteria for expense recognition are fulfilled, the asset is reversed against expenses.

Section 4.5 includes more details of the cut-off procedures performed by the EC.

3.2.2.5 Presentation and disclosures

EAR 1 section 9.3 states that expenses should either be presented by nature or by function. There are no special rules for the presentation of non-exchange expenses in this regard.

Nevertheless, EAR 3 includes the following: ‘If there is a correction of eligible expenses (e.g. as a result of the findings of an audit) and the expense is lower than originally assumed, the presentation of the adjustment depends on when the modification occurs:

- When it occurs in the same financial year, a decrease in expense is shown.
- When it occurs later, revenue is recognised (EAR 3 section 5.5).

Decreases or increases of expenses due to changes in estimates should be recorded in the corresponding initial expense account (EAR 3 section 5.2). The nature and amount of a significant change in accounting estimates should be disclosed in the notes (EAR 3 section 5.2).

In addition, EAR 3 requires that the accounting policies adopted and the amount of each significant category of expenses recognised during the period be disclosed.

According to EAR 3 section 4.4(d), any contingent liability (which is not recorded on the balance sheet) should also be disclosed in the notes. This disclosure requirement relates to entitlements and transfers under agreements.

3.3 International Financial Reporting Standards (IFRS)

3.3.1 Applicable standards

Under IFRS no specific distinction is made between exchange and non-exchange revenue and no specific rules exist in relation to non-exchange revenue. This is because IFRS apply to private companies that undertake profit-making activities and nearly all transactions are expected to have the nature of “exchange” revenue/income.

The only standard that deals with non-exchange income is IAS 20 ‘Accounting for government grants and disclosure of government assistance’. IAS 20 sets forth the general accounting principles for government grants received by the entity. In addition, the standard comprises disclosure requirements for all kinds of government assistance provided to the entity.

As the IPSASB currently discusses the performance-obligation approach introduced by IFRS 15 (‘Revenue from contracts with customers’) and thinks about applying a similar approach under IPSAS (the public sector performance obligation approach (PSPOA) - see section 3.6.), IFRS 15 is considered in the following pages too.

3.3.2 IAS 20 'Accounting for government grants and disclosure of government assistance'

As IAS 20 deals with the accounting for government grants (and other government assistance) received, the underlying recognition and measurement principles are considered in this issue paper. It should be noted that IAS 20 applies only to assistance provided by governments (i.e. by the government itself, government agencies and similar bodies whether local, national or international; IAS 20 paragraph 3). Benefits provided by other parties are not in the scope of this standard.

IAS 20 defines government assistance as 'action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria' (IAS 20.3). Government grants are a special type of government assistance and defined as 'assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity' (IAS 20.3).

Government grants are recognised when 'there is reasonable assurance that:

- The entity will comply with the conditions attached to them; and
- The grants will be received' (IAS 20.7).

For instance, 'a forgivable loan from government is treated as government grant when there is reasonable assurance that the entity will meet the terms for forgiveness of the loan' (IAS 20.10).

The recognition of government grants in profit or loss depends on the pattern of expense recognition concerning the costs that the grant is intended to compensate: government grants shall be included in profit or loss on a corresponding systematic basis (IAS 20.12). Grants related to assets are recognised in the income statement at the same rhythm as the depreciation on the assets concerned. Grants related to income are recognised in the income statement to match the expenses they are intended to compensate.

Government grants might be monetary or non-monetary. Regarding the measurement of monetary grants, IAS 20 includes no requirement. Therefore, the general principles should be followed. Non-monetary grants are usually measured at the fair value of the transferred resources (alternatively, at a nominal amount - IAS 20.23).

The presentation of government grants depends on whether the grant is related to assets or to income. On the statement of financial position, grants related to assets might be presented as deferred income or by deducting the grant from the carrying amount of the asset (IAS 20.24). Also with regards to grants related to income, there is an accounting policy choice: the government grant can either be presented separately or under a general heading like 'Other income' or can be deducted from the related expense (IAS 20.29).

Disclosure requirements of IAS 20 include the accounting policy adopted for government grants, the nature and extent of government grants recognised, an indication of other forms of government assistance and information about unfulfilled conditions and other contingencies (IAS 20.29).

3.3.3 IFRS 15 'Revenue from contracts with customers'

IFRS 15 is applicable for annual periods beginning on or after 1 January 2018.

It applies to all contracts with customers, with the exception of e.g. lease contracts and insurance contracts (IFRS 15.5). According to IFRS 15.6, a customer is ‘a party that has contracted with an entity to obtain goods or services that are an output of the entity’s ordinary activities in exchange for consideration’. This definition assumes that the entity receives a consideration for its performance under a contract with a customer which is an exchange transaction. Grants and other transfers are not within its scope.

Under IFRS 15, revenue is generally recognised when the entity satisfies a performance obligation (PO) by transferring a promised good or service (i.e. an asset) to a customer. An asset is transferred to the customer when (or as) the customer obtains control of that asset (IFRS 15.31).

IFRS 15 foresees a five-step approach to revenue recognition:

Step 1: Identify the contract(s) with a customer

According to IFRS 15.10, a contract is ‘an agreement between two or more parties that creates enforceable rights and obligations’. When certain criteria are met, IFRS 15.17 foresees that several contracts need to be combined for accounting purposes.

Step 2: Identify the POs in the contract

A PO is a promise to transfer to the customer either a distinct good or service or - if certain conditions are met - a series of distinct goods or services (IFRS 15.22). A good or service is distinct if ‘the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct) and if ‘the entity’s promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. the promise to transfer the good or service is distinct within the context of the contract)’ (IFRS 15.27).

Step 3: Determine the transaction price

IFRS 15.47 defines the transaction price as ‘the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer’.

Step 4: Allocate the transaction price to the POs in the contract

The allocation of the transaction price is based on relative stand-alone selling prices. Like this, an amount is allocated to each PO which depicts the amount of consideration that the entity expects to receive in exchange for satisfying the PO (IFRS 15.73).

Step 5: Recognise revenue when (or as) the entity satisfies a PO

The underlying principle of IFRS 15 is that revenue should be recognised when control of the asset is transferred to the customer (IFRS 15.31). For each identified PO, it needs to be assessed whether control is transferred over time (IFRS 15.35-37, 39-45) or at a point in time (IFRS 15.38). Certain indicators are used for this purpose.

3.4 ESA 2010

3.4.1 Scope and definitions

Under ESA 2010, grants and other transfers are also ‘transactions’. These are defined as ‘an economic flow that is an interaction between institutional units by mutual agreement or an action within an institutional unit that it is useful to treat as transaction, because the unit is operating in two different capacities’ (ESA 2010 1.66).

ESA 2010 1.66 distinguishes between transactions in products, distributive transactions, financial transactions and other transactions.

Generally, transactions can be both required (‘something for something’) and unrequired (‘something for nothing’). Unrequired means that there are ‘payments in cash or in kind from one institutional unit to another without counterpart’ (ESA 2010 1.71). Such transactions are typically classified as distributive transactions, include taxes, social assistance benefits or gifts, and are called transfers.

Distributive transactions ‘describe how value added generated by production is distributed to labor, capital and government, and the redistribution of income and wealth (taxes on income and wealth and other transfers)’ (ESA 2010 1.66). They include current and capital transfers.

The following ESA categories are mainly relevant for grants and other transfers:

Code	Name	Definition
D.3	Subsidies (type of current transfers)	‘Current unrequited payments which general government or the institutions of the European Union make to resident producers’ (ESA 2010 4.30).
D.7	Other current transfers	Definition n/a; include miscellaneous current transfers like e.g.: <ul style="list-style-type: none">• ‘Current transfers within general government’ (D.73).• ‘Current international cooperation’ (D.74).• ‘Fines and penalties’ (D.759).
D.9	Capital transfers	‘Require the acquisition or disposal of an asset, or assets, by at least one of the parties to the transaction. Whether made in cash or in kind, they result in a commensurate change in the financial, or non-financial, assets shown in the balance sheets of one or both parties to the transaction.’ (ESA 2010 4.145). Include ‘investment grants’ (D.92) which ‘consist of capital transfers in cash or in kind made by governments or by the rest of the world to other resident or non-resident institutional units to finance all or part of the costs of their acquiring fixed assets’ (ESA 2010 4.92).

3.4.2 Recognition

As a general principle, “Flows shall be recorded 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” (ESA 2010 1.101). This means that transactions should not be recorded when the payment is made, but when the economic event takes place.

However, ESA 2010 1.103 acknowledges that recording of taxes and other flows concerning general government might be difficult on an accrual basis and an approximate method might be acceptable. More detailed rules are available for taxes and social contributions (see for example ESA 4.82).

In addition to this general rule, ESA 2010 include recognition rules for each category. Some examples (which are helpful within the context of the present issue paper) are given in the table below:

Code	Name	Time of recording
D.3	Subsidies	‘When the transaction or the event (production, sale, import, etc.) which gives rise to the subsidy occurs’ (ESA 2010 4.39).
D.73	Current transfers within general government	‘Current transfers within general government are recorded at the time the regulations in force stipulate they are to be made’ (ESA 2010 4.119).
D.74	Current international cooperation	‘The time the regulations in force stipulate the transfers are to be made in the case of obligatory transfers, or the time the transfers are made in the case of voluntary transfers’ (ESA 2010 4.123).
D.759	Fines and penalties	‘At the time the liabilities arise’ (ESA 2010 4.134).
D.92	Investment grants	‘Investment grants in cash are recorded when the payment is due to be made. Investment grants in kind are recorded when the ownership of the asset is transferred.’ (ESA 4.162).

3.4.3 Measurement

All items under ESA 2010 ‘shall be measured according to their exchange value, i.e. the value at which flows and stocks are in fact, or could be, exchanged for cash. Market prices are, thus, ESA’s reference for valuation.’ (ESA 2010 1.94).

In case of monetary transactions, the valuation is straightforward. In other cases, the valuation should be based on market prices for analogous goods, services or assets, made by summing up production cost, or refer to the discounted present value of expected future returns (ESA 2010 1.95).

3.4.4 Transactions with international or supranational organisations

An example of transactions with international or supranational organisations is between non-government residents and institutions of the European Union, where these are considered as the principal parties to the transaction even though government units play a role as an intermediary agent in channelling the funds. The recording of the main transactions is directly between the two parties and does not impact on the government sector. The government’s role is recorded as a financial transaction (F.89) (ESA 20.292).

The institutions of the European Union make significant current and capital transfers through structural funds such as the European Social Fund, the European Regional Development Fund and the Cohesion Fund. The final beneficiaries of such transfers can be government or non-government units (ESA 20.294).

Grants paid from structural funds often involve co-financing, whereby the European-Union jointly funds an investment made by government. There can be a mixture of pre-payments, interim and final payments, which may be channelled through at least one government unit. Resident government units may also make advances payments of the receipts expected from the European Union (ESA 20.295).

A distinction is made between grants where the beneficiary is no government unit and where the beneficiary is a government unit.

- When non-government units are the beneficiaries, any payments made by government in advance of European Union cash receipts are recorded as financial transactions in other accounts receivable/ payable. The counterpart of the financial transaction is the European Union if the accrual point of the non-financial transaction has occurred, otherwise it is the beneficiary. The accounts receivable/ payable positions unwind when the cash is paid (ESA 20.296).

The recording time of co-financed government expenditure transfers is the time when European Union authorisation is given (ESA 20.297).

There may be circumstances where government advances exceed the amount allowable once this is determined by the authorisation process. If the beneficiary is in a position to repay the excess this unwinds the other accounts payable it has with government. If the beneficiary cannot repay, then a capital transfer from government is recorded cancelling the other accounts payable (ESA 20.298).

- When government units are the beneficiaries, the government revenue is moved forward to match the time of expenditure in a departure from the general rules on time of recording for such transfers. If there is a considerable time lag between the government expenditure taking place and cash being received, then the revenue can be recorded when the claim to the European Union is submitted; this is applicable only when: reliable information on the time of the expenditure is not available; or amounts are big; or the time lag between the expenditure and submission of claim is small (ESA 20.299).

Part II of the MGDD provides additional guidance on the time of recording. There is one chapter dealing with 'Grants from and contributions to the EU Budget'³. At first, the accounting for grants from the EU budget, i.e. for grants received, is described. Special attention is drawn to cases in which there is a gap between the receipt of the documentation, the authorization and payment of the grant or in which it is difficult to determine when the obligation arises. In addition, advance payments are discussed. The second part of the chapter treats contributions of EU MSs to the EU budget. The chapter also includes examples illustrating the accounting based on booking entries.

³ See Eurostat, Manual on Government Deficit and Debt, Part II.6, pp. 133-148.

3.5 Comparison between the different international financial reporting frameworks

3.5.1 Grants and other transfers received

The table below provides an overview of the main rules relating to grants and other transfers received (i.e. regarding non-exchange revenue) included in the various international financial reporting frameworks analysed.

Figure 1: IPSAS, EAR, IFRS and ESA 2010 rules for grants and other transfers received compared

Grants and other transfers received				
	<i>IPSAS</i>	<i>EAR</i>	<i>IFRS</i>	<i>ESA 2010</i>
Applicable standard	IPSAS 23	EAR 17	IAS 20	General requirements regarding flows and transactions; certain accounts of distributive transactions.
Scope	Revenue from non-exchange transactions.	Based on IPSAS 23	Government grants (and disclosure of other government assistance).	Defined for each account.
Recognition	<p><u>Asset</u> Recognition when the entity gains control of resources (meeting definition of an asset) that satisfy the following criteria:</p> <ul style="list-style-type: none"> • Probable inflow of future economic benefits or service potential; • Reliable measurement. <p><u>Liability</u> Recognition when present obligation (meeting definition of a liability) that satisfies the following criteria:</p> <ul style="list-style-type: none"> • Probable outflow of resources; • Reliable measurement. <p><u>Revenue</u> Recognition when increase in net assets.</p>	Based on IPSAS 23	Reasonable assurance that the entity will comply with the conditions attached to the grant and the grant will be received. Recognition in profit or loss when costs to be compensated are recognised as expenses.	When economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled.

Grants and other transfers received				
	<i>IPSAS</i>	<i>EAR</i>	<i>IFRS</i>	<i>ESA 2010</i>
(Initial) Measurement	<u>Asset</u> Fair value as of the date of acquisition. <u>Liability</u> Best estimate of the amount required to settle the present obligation at the reporting date. <u>Revenue</u> Amount of the increase in net assets.	Based on IPSAS 23	<u>Monetary grants</u> General principles. <u>Non-monetary grants</u> Fair value (alternatively, nominal amount).	Exchange value, i.e. market price.
Presentation	<u>Income statement</u> Revenue (exchange and non-exchange) or separately (only non-exchange) if material.	Based on IPSAS 1 (refer to EAR 1)	<u>Grants related to assets</u> Deferred income or deducted from asset (policy choice) in the balance sheet. Income statement presentation follows the same logic. <u>Grants related to income (income statement)</u> Separately/other income or deducted from related expense (policy choice).	Recorded on a gross basis (i.e. no netting) and impact net lending/net borrowing.
Disclosures	Accounting policies, amounts recognised, further details on amounts recognised.	Based on IPSAS 23	Accounting policies, nature and extent of grants, unfulfilled conditions and other contingencies.	N/A

3.5.1.1 Scope and definitions

As EAR 17 is based on IPSAS 23, the scope and definitions of the two standards are the same. They both refer to the accounting for revenue from non-exchange transactions, regardless of the counterparty.

The scope of IAS 20 is narrower: it only relates to the accounting for government grants (and disclosure of other government assistance). Entities applying IFRS typically incur non-exchange income only in transactions with the government.

ESA 2010 acknowledges that transactions might be required and unrequited, which is similar to the concept of exchange and non-exchange transactions under IPSAS. However, no clear distinction is made between required and unrequited transactions with regard to the recognition and measurement principles.

3.5.1.2 Recognition

IPSAS 23 (and EAR 17 accordingly) follows a two-step approach: an asset is recognised when the entity gains control of resources (meeting definition of an asset) and the recognition criteria are satisfied; revenue is then recognised to the extent that no liability is recognised in respect of the same inflow.

Another approach for the recognition of non-exchange revenue is currently discussed by the IPSASB in the context of its project on revenue and non-exchange expenses: the public sector performance obligation approach (the PSPOA) which might also lead to a different pattern of non-exchange revenue recognition.

Under IAS 20, a government grant is recognised when there is reasonable assurance that the entity will comply with the conditions attached to the grant and the grant will be received. Its recognition in profit or loss depends on the expense recognition of the cost to be compensated.

ESA 2010 contains specific rules for each account and refers to the point in time/period of time when the claim arises.

As the concepts of the various international financial reporting frameworks are different, the timing of recognition of non-exchange revenue from grants and other transfers might differ under each framework.

One major difference arises in respect of investment grants. Investment grants under ESA 2010 affect surplus or deficit when the payment is due to be made or ownership of the asset is transferred. This is different from IFRS which require grant income to be recognised in line with the depreciation expense of the asset subsidised. This may also be different from IPSAS which require revenue to be recognised only when the right to receive the grant is established (if no conditions are attached) or when conditions attached to the grant are fulfilled.

3.5.1.3 Measurement

Under IPSAS 23/EAR 17 the measurement of revenue from grants and other transfers depends on the measurement of the asset (fair value as of the date of acquisition) and the liability (best estimate of the amount required to settle the obligation).

A different approach is taken under IAS 20 and ESA 2010. IAS 20 contains no special rules regarding the measurement of monetary grants because the valuation is straightforward in this case. Non-monetary grants are measured at fair value (or alternatively, at a nominal amount). With the exception of the alternative measurement at a nominal amount, this appears to be similar to ESA 2010 which refers to the exchange value.

3.5.2 Grants and other transfers given

The next table provides an overview of the main rules relating to grants and other transfers given (i.e. these lead to the recognition of non-exchange expense).

Figure 2: IPSAS, EAR, IFRS and ESA 2010 rules for grants and other transfers given compared

Grants and other transfers given				
	<i>IPSAS</i>	<i>EAR</i>	<i>IFRS</i>	<i>ESA 2010</i>
Applicable standard	General requirements in IPSASB Conceptual framework, IPSAS 1.	EAR 3.	General requirements in IASB Conceptual framework.	General requirements regarding flows and transactions. Certain accounts of distributive transactions.
Scope	General definition of expenses in IPSASB Conceptual framework.	Exchange and non-exchange expenses (includes specific rules for non-exchange expenses).	General definition of expenses in IASB Conceptual framework.	Defined for each ESA category.
Recognition	General recognition criteria in the Conceptual framework.	Expense recognition in the period during which the events giving rise to the transfer occurs if: <ul style="list-style-type: none"> • Allowed by regulation/signed contract/authorised; • Performance delivered; • Eligibility criteria (when applicable including meeting the conditions attached to the grant) are met; • Reasonable estimate. 	General requirements in IASB Conceptual framework.	When economic value is created, transformed or extinguished, or when claims and obligations arise, are transformed or are cancelled.
Measurement	General requirements in the Conceptual framework.	Eligible/authorized amount.	General requirements in IASB Conceptual framework.	Exchange value, i.e. market price.
Presentation	General requirements in IPSAS 1.	General requirements in EAR 1.	General requirements in IAS 1.	Recorded on a gross basis (i.e. no netting) and impact net lending/net borrowing.
Disclosures	N/A	Accounting policies, amount of each significant category of expenses.	N/A	N/A

3.5.2.1 Scope and definitions

Under IPSAS, there is no specific standard dealing with non-exchange expenses. Expense recognition should be based on the general requirements in the IPSAS Conceptual framework and IPSAS 1. Given the lack of accounting guidance, diversity arises in practice. The current IPSASB project on non-exchange expenses aims to fill this gap by setting accounting rules.

IFRS also do not contain specific rules for non-exchange expenses as such transactions are not expected to occur in the private sector. In the rare circumstances where non-exchange expenses would be identified, the general requirements of the IASB Conceptual framework would apply.

EAR 3 covers both exchange and non-exchange expenses.

Under ESA 2010, no distinction is made between transfers received and provided. Therefore, please refer to section 3.4 of the present issue paper.

3.5.2.2 Recognition and measurement

As already mentioned, no IPSAS rules specifically relating to non-exchange expenses exist and the general requirements included in the Conceptual framework apply. Under IFRS, the topic is not relevant.

In comparison, EAR 3 has more specific recognition criteria and distinguishes between entitlements, transfers under agreements as well as discretionary grants, contributions and donations. These rules are specifically tailored to the types of grants given by the European Commission. EAR 3 refers to a decrease in an asset or an increase in a liability with regards to expense recognition.

ESA 2010 contains even more specific recognition criteria. It generally refers to the point in time/period of time when the obligation arises.

3.6 IPSASB current projects on revenue and non-exchange expenses

3.6.1 IPSASB project on revenue

The IPSASB initiated a project dealing with revenue recognition in both exchange and non-exchange transactions. Its aim is to develop one or more IPSAS dealing with all revenue transactions, i.e. also with grants and other transfers received.

The project is inspired by a new standard on revenue recognition under IFRS - IFRS 15 'Revenue from contracts with customers'. For details about IFRS 15, please refer to section 3.3.3. IFRS 15 follows a performance-obligation approach, i.e. revenue is recognised when the entity satisfies a performance obligation (PO).

The IPSASB discussed whether such an approach is more straightforward under IPSAS and provides more useful information than the current distinction between exchange and non-exchange transactions. In addition to maintaining convergence with IFRS, the IPSASB wants to respond to difficulties in practice to distinguish between exchange and non-exchange revenue transactions or between stipulations that are either conditions or restrictions under IPSAS 23 as well as to further application issues (e.g. capital grants, services-in-kind received, time requirements not considered in the accounting of multi-year grants).

Besides the revenue project, there is currently a project on non-exchange expenses. As the two projects are closely interrelated, the IPSASB published a CP dealing with both revenue and non-

exchange expenses in August 2017: 'Accounting for revenue and non-exchange expenses'⁴. The comment period ended on 15 January 2018. In combining the discussions about revenue and non-exchange expenses in one single project, the IPSASB aims at ensuring consistent approaches between resource providers and resource recipients.

For discussion purposes, the IPSASB has categorised revenue transactions into three broad categories:

Category A	Revenue transactions with no POs or stipulations
Category B	Revenue transactions that contain POs or stipulations, but do not have all the characteristics of transactions within the scope of IFRS 15
Category C	Revenue transactions that are within the scope of IFRS 15

Performance Obligations (PO's) are promises to deliver distinct services. For a performance obligation to exist, it should be enforceable. Enforceability is based on the ability of the resource provider to take remedies if the POs are not fulfilled, through e.g. legislation, ministerial decision or reduction of future funding for the same program. It goes beyond the obligation to refund if the conditions attached to the grant are breached. The assessment whether a PO exists requires significant judgement.

As grants and other transfers are either in Category A or B, only those categories are discussed below. For transactions in Category C, the IPSASB intends to develop an IPSAS primarily drawn from IFRS 15.

The IPSASB expresses the preliminary view that Category A revenue transactions should be addressed in an updated IPSAS 23. As a number of areas were identified where further clarification or guidance is required, the IPSASB plans to update IPSAS 23.

Illustrative booking entries for category A revenue transactions:

Grant is received/receivable
Dr Cash/grant receivable
To Cr Revenue

Regarding Category B revenue transactions, the IPSASB proposes that those transactions be accounted for under a Public Sector Performance Obligation Approach (PSPOA). This approach is based on IFRS 15 and adapted to the public sector context. While the application of IFRS 15 is restricted to contractual agreements, the PSPOA also deals with other binding arrangements. Furthermore, the PSPOA considers that in the public sector the resource recipient might deliver services to a beneficiary, rather than to the resource provider.

⁴ The consultation paper can be found on the IPSASB website: http://www.ifac.org/publications-resources/accounting-revenue-and-non-exchange-expenses?utm_source=IFAC+Main+List&utm_campaign=267bf8fdec-EMAIL_CAMPAIGN_2017_08_21&utm_medium=email&utm_term=0_cc08d67019-267bf8fdec-80393729.

The PSPOA includes the following five steps:

1. Identify the binding arrangement.
2. Identify the POs.
3. Determine the consideration.
4. Allocate the consideration.
5. Recognise revenue.

The advantage of the PSPOA is that an approach based on POs would be applied to both Category B and Category C transactions. In addition, there would be no need to distinguish between conditions and restrictions anymore, which causes many problems in practice.

Illustrative booking entries relating to category B revenue transactions:

1.a. Grant is received/receivable and a PO exists

Dr Cash/grant receivable

To Cr Liability (deferred revenue)

1.b. PO is fulfilled (possibly over-time)

Dr Liability (deferred revenue)

To Cr Revenue

2. Grant is received/receivable and no PO exists

Dr Cash/grant receivable

To Cr Revenue

In addition to the PSPOA, the CP discusses an approach in which the current distinction between exchange and non-exchange transactions is retained - the Exchange/Non-Exchange Approach. Under this approach, IPSAS 23 would still apply to both Category A and Category B transactions, regardless of whether they contain POs and/or stipulations.

Various options are suggested for updating IPSAS 23:

- To address exchange/non-exchange determination issue:
 - (a) Provide additional guidance on making the exchange/non-exchange determination.
- To address transfers with time requirements:
 - (b) Require enhanced display/disclosure for transactions with time requirements.
 - (c) Classify time requirements as a condition.
 - (d) Classify transfers with time requirements as other obligations.
 - (e) Recognise transfers with time requirements in net assets/equity and recycle through statement of financial performance.

Under option (d), the resource recipient would initially recognise the transfer as an “other obligation” and recognise revenue as the transfer is used, therefore allowing a matching of revenue from grants and the expenses it is intended to compensate. When finalising its Conceptual framework, the IPSASB acknowledged that certain economic phenomena that do not meet the

definition of any element may need to be recognised in the financial statements in order to meet the objectives of financial reporting, and decided that the circumstances under which this may be the case would need to be determined at a standard level. Recognising 'other obligations' would convey to users of the financial statements that the grant recipient has resources that are intended for use in subsequent financial reporting periods. The resource recipient would recognise revenue and reduce the other obligation in the period when the resource provider intends the resource to be used.

As the IPSASB has identified applications issues with regards to capital grants and services-in-kind, the CP also asks for feedback on these issues. Regarding capital grants, preparers complain that the distinction between conditions and restrictions - which is a crucial aspect for the pattern of revenue recognition - is often not clear. The IPSASB proposes that capital grants be addressed explicitly in IPSAS.

Revenue recognition for services-in-kind received is optional under current IPSAS (even though they might be material), which leads to a lack of comparability in IPSAS financial statements. The IPSASB looks for comments on whether the current approach should be retained or whether another approach should be adopted.

3.6.2 IPSASB project on non-exchange expenses

As there is currently no IPSAS dealing with non-exchange expenses, the IPSASB initiated a project aiming at developing a standard dealing with the recognition and measurement requirements for such transactions (including grants and other transfers). One major source of non-exchange expenses are social benefits which are, however, treated in a separate IPSASB project.

As there is diversity in practice, the IPSASB intends to develop accounting rules to ensure consistency in application. The CP issued in August 2017 (see section above) discusses two approaches to account for non-exchange expenses: the Extended Obligating Event Approach and the PSPOA. The board expresses the preliminary view that the PSPOA should be applied.

The PSPOA for non-exchange expenses reflects the PSPOA for revenue transactions (see section 3.6.1). The resource provider recognises an expense and a liability (or derecognises a prepaid expense) when the resource recipient satisfies identifiable and specific POs.

Illustrative booking entries relating to the recognition of expenses when a PO exists using a reasoning by analogy to IPSAS 23:

1.a. Grant is given/recipient's right to receive the grant is established and a PO exists

Dr Asset (deferred expense/pre-financing)

To Cr Cash/grant payable

1.b. PO is fulfilled (possibly over-time)

Dr Expense

To Cr Asset (deferred expense/pre-financing)

2. Grant is given/recipient's right to receive the grant is established and no PO exists

Dr Expense

To Cr Cash/grant payable

Following divergent comments received from constituents on its proposal to also apply the PSPOA to grants and transfers given, the IPSASB indicated that they will give another thinking to it.

The Extended Obligating Event Approach foresees that a liability is recognised when there is an obligating event, i.e. an event which creates a legal obligation or a non-legally binding obligation and the transferring entity has no realistic alternative to settling that obligation. The related expense is either recognised immediately or over time, depending on stipulations relating to the transaction. This approach mirrors IPSAS 23.

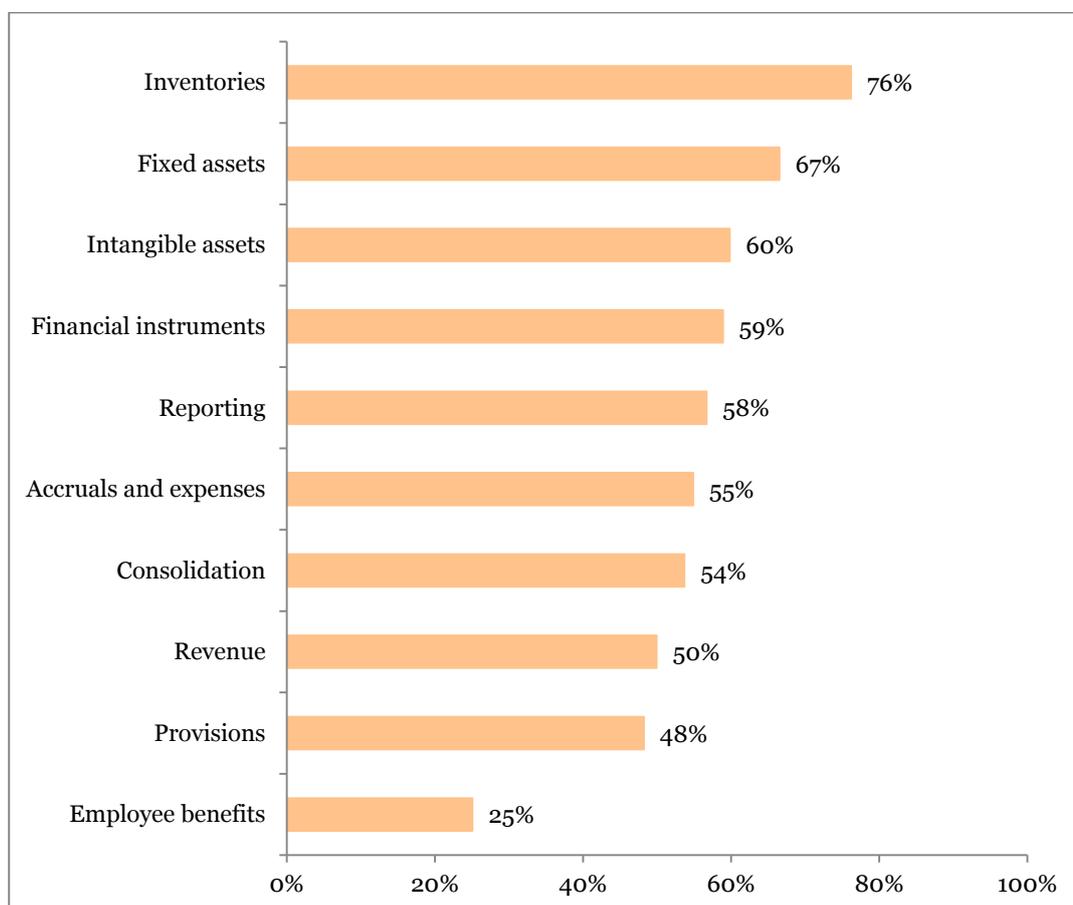
The CP discusses separately the accounting for universally accessible services (e.g. free school), which are available to all individuals or households and where eligibility criteria (if any) are not related to social risks (e.g. education, health services). As they do not contain POs, the IPSASB has the preliminary view that the Extended Obligating Event Approach should be applied. This means that expenses are recognised when services are delivered.

4 Description of the accounting for grants and other transfers in selected EU Member States (Latvia and Belgium) and one international organisation (the European Commission)

4.1 Overall accounting maturity for accounting for grants and other transfers by EU Member States

The graph below is extracted from the 2014 PwC study. It gives an overview of the average accounting maturity score per accounting area across EU governments and highlights the areas which are more closely aligned with generally accepted accrual accounting principles across the EU. It indicates an average maturity of 55 % for accruals and expenses and of 50 % for revenue.

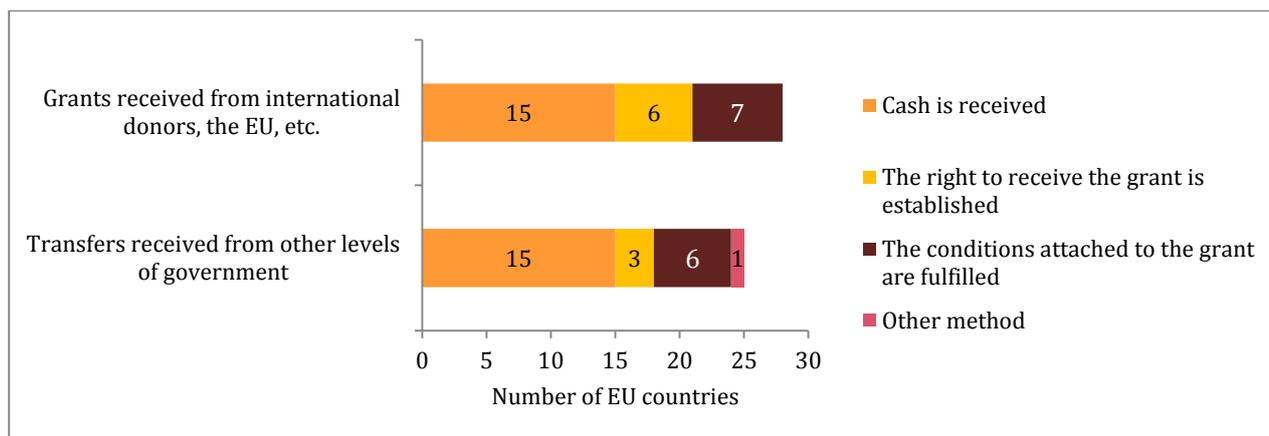
Figure 3: Average accounting maturity per accounting area across the EU⁵



The results above do not make a distinction between exchange and non-exchange transactions. However, it was analysed when revenue from transfers is recognised: the study shows that most of the EU countries recognise revenue when cash is received. The approach is thus often not in line with the accrual basis of accounting and might lead to a different timing of recognition in many cases (e.g. claim arises before cash is received, advance payments).

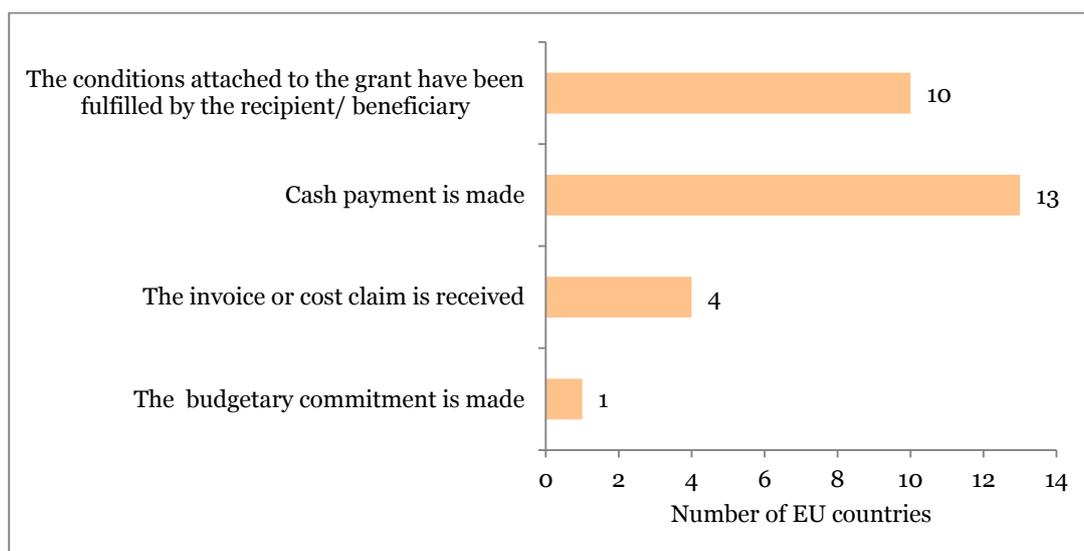
⁵ See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 96.

Figure 4: Timing of recognition of revenue from transfers⁶



Regarding grants and other transfers provided, there is also diversity in practice. 10 EU governments recognise the corresponding expenses when the conditions attached to the grant have been fulfilled by the recipient/beneficiary, which appears to be in line with IPSAS. 13 countries account on a cash basis, four recognise the expense when the invoice or cost claim is received and one when the budgetary commitment is made.

Figure 5: Timing of recognition of grants and other transfers provided⁷



⁶ See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 111.

⁷ See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 106.

4.2 Selection of benchmark entities used in the analysis and methodology

Two EU MSs (Latvia and Belgium) and one international organisation (the European Commission) have been selected for a deeper analysis of the accounting treatment used for grants and other transfers.

For the governments of Latvia (all government levels) and Belgium (central government), both grants received and given are analysed. The analysis of the European Commission case solely addresses the accounting of grants given because it represents the biggest flow of transactions for the Commission and the required cut-off procedures at year-end are a good example to illustrate the issues encountered in practice.

To analyse the approaches taken regarding the accounting treatment of grants and other transfers in the selected MSs, PwC combined an analysis of publicly available information (financial statements, national accounting policies, EAR) with responses obtained to a questionnaire addressed to government representatives of Latvia and Belgium. The first part of the questionnaire addresses the main categories of grants and other transfers received and the accounting for the related income. The second part addresses the main categories of grants and other transfers given and the accounting for the related expense. Both the accounting aspects and the advantages of the implementation approach adopted are discussed in the questionnaire.

4.3 Latvia

4.3.1 Grants and other transfers received

The following table gives an overview of revenue recognised for grants and other transfers received in the consolidated accounts of the Latvian general government⁸. In the years 2014 to 2016, grants and other transfers resulted in revenue reflecting between 8.3 % and 12.6 % of total revenue⁹.

	2016		2015		2014	
	Amount (in million €)	% of total revenue	Amount (in million €)	% of total revenue	Amount (in million €)	% of total revenue
General government	755	8.3 %	1,011	11.5 %	1,079	12.6 %
Central government	753	10.1 %	1,008	13.8 %	1,075	15.3 %
Local government	560	25.4 %	609	28.5 %	616	29.3 %

As transfers between the central government and local governments are eliminated in the consolidated financial statements of the general government, they are shown separately below. Before elimination, the share of revenue from grants and other transfers is even higher for the central government accounts (10.1 % to 15.3 %) and for the local governments (25.4 % to 29.3 %).

⁸ The general government sector includes all central and local government budgetary institutions, the social security fund and excludes the central and local government-financed and controlled enterprises as defined in ESA 2010.

⁹ Source: Annual Reports for 2014, 2015, 2016 on Central Government Budget Execution and Local Government Budgets of the Republic of Latvia (in Latvian) - <https://www.kase.gov.lv/parskati/latvijas-republikas-gada-parskats>

At the central government level, the major part of revenue relates to foreign financial assistance (including EU grants). At the local government level, revenue mainly results from transfers between different levels of government.

Latvia receives the following main types of grants and other transfers:

- EU grants.
- Foreign financial assistance.
- Transfers between central and local governments.
- Donations.

The Latvian national accounting framework is based on IPSAS and Latvia's accounts are thus prepared under the accrual basis of accounting. For the main categories of grants and other transfers the following accounting principles are applied:

Category	Revenue recognition
EU grants	Revenue is recognised in the period when expenses arise. Revenue and expenses are presented for accruals and cash flows in the financial statements. Institutions responsible for supervision provide detailed accounting of EU grants by projects.
Foreign financial assistance	Revenue is recognised in the same period when expenses arise. Revenue and expenses are presented for accruals and cash flows in the financial statement.
Transfers between central and local government	Revenue is recognised in the period when related expenses are approved by the transferor.
Donations	Revenue is recognised upon receipt, except when cash is intended for long-term investments. In that case, revenue is recognised during the useful life of the asset. Moreover, when corresponding expenditures are planned in next financial year, then revenue is recognised when expenditure arises.

The Latvian government sees as main advantage that its accounting meets best international practices and therefore its financial indicators are comparable to those of other states. The accounting treatment adopted is also felt to provide a true and fair view of the financial situation of the Latvian state.

Next to this, Latvia follows an approach whereby the recipient's revenue should be recognised in the same period as the period in which the transferor recognises the related expense, i.e. the accounting of the recipient should mirror the accounting of the transferor. Reconciling inter-governmental transfers in the consolidation process is seen as a major challenge by Latvian representatives. Mirror accounting by the grantor and recipient facilitates the consolidation process.

To ensure proper matching of revenue and expenses, it is necessary to establish and maintain a proper internal control system and appropriate IT as well as human resources are needed for this.

4.3.2 Grants and other transfers given

The following table shows the magnitude of expenses recognised for grants and other transfers given in the consolidated accounts of the Latvian general government and the separate accounts of the central government and local governments¹⁰.

	2016		2015		2014	
	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense
General government	4,897	53.4%	4,667	50.8%	4,715	52.8%
Central government	5,212	68.2%	5,046	66.1%	5,083	69.0%
Local government	243	11.3%	229	10.6%	247	11.3%

Please note that the figures above include social benefits which are not in scope of this paper. Separate figures are only available for regular payments into the EU budget and international cooperation, which represents about 4 % of the total expense amount, and transfers (excluding subsidies and grants), which represent about 8 % of the total expense amount.

Regarding grants and other transfers given, the following main categories are identified:

- Transfers between central and local governments.
- Membership fees to international organisations.
- Donations.

These grants and other transfers are provided to other parties than the Latvian citizens. Those receive social benefits, which are excluded from the scope of this paper.

Also for grants and other transfers given, the Latvian national accounting framework is based on IPSAS and therefore an accrual basis of accounting is applied. Expense recognition rules for each main category of grants and other transfers given are described in the following table:

Category	Expense recognition
Transfers between central and local government	Expense is recognised in the period when the use of the transfer is approved by the transferor.
Membership fees to international organisations	Expense is recognised in the corresponding period.
Donations	Expenses are recognised upon payment.

The main challenges identified and advantages of the accounting treatment adopted by the Latvian government are similar to the ones explained above in relation to revenue recognition in the context of grants and other transfers received.

¹⁰ Source: Annual Reports for 2014, 2015, 2016 on Central Government Budget Execution and Local Government Budgets of the Republic of Latvia (in Latvian) - <https://www.kase.gov.lv/parskati/latvijas-republikas-gada-parskats>

4.4 Belgium

4.4.1 Grants and other transfers received

The table below provides an overview of the revenue from grants and other transfers received in the accounts of the Belgian central government.

	2016 ¹¹		2015 ¹²		2014 ¹³	
	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense
EU grants	47	0.05%	15	0.01%	36	0.04%
Fines	734	0.71%	569*	0.53%	546*	0.55%
Transfers from other levels of government	23	0.02%	10	0.01%	12	0.01%

* Restated to take into account the amounts that accrued during that period.

The main categories of grants and other transfers received by the Belgian central government are:

- EU grants.
- Transfers from other levels of government.
- Fines.

EU grants include funds for Member State initiatives in different policy areas, for example in the policy areas of immigration and regional development. Transfers from other levels of government comprise funds from social security funds to federal public services¹⁴, for instance to the federal public service of Justice (for medical care of prisoners). Fines are received as a consequence of individuals or entities breaching the requirements of laws or regulations; they are collected by federal public services.

The Belgian central government (also called the federal government) does not follow IPSAS 23. Nevertheless, grants and other transfers received are recognised in the period in which they accrue to federal government.

Four conditions have to be met in order to recognise a grant as an asset:

- Grants and transfers received can be measured reliably.
- The parties involved in the transaction can be identified.
- There is an obligation to pay.

¹¹ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2016/2.sejums/2_02_FMInf_290617_kons_kopbudzets.pdf.

¹² Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2015/2.s%C4%93jums/FMInf_230816_kons_kopbudzets.pdf.

¹³ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2014/2.s%C4%93jums/FMInf_300615_kons_kopbudzets.pdf.

¹⁴ Belgium is a Federal State. Federal public services are the equivalent of central government ministries.

- The entity has a document that justifies the transaction.

EU grants may be subject to stipulations. They are recorded in line with Belgian accounting legislation and in line with the ESA reporting framework (refer to section 3.4). The latter sets out the following: revenue for EU grants is recognised when the corresponding expense is recognised. This is done (for practical reasons) to ensure that there is no impact on government lending/borrowing arising from this kind of transactions. Grants with conditions are also recorded as off balance sheet items.

As per Belgian government representative, the advantage of the accounting approach adopted is the fact that the federal government can ensure proper follow-up of grants and transfers receivable by tracking them in the accounting records.

4.4.2 Grants and other transfers given

The following table summarises the types and amounts of expenses recognised for grants and other transfers given in the annual accounts of the Belgian central government.

	2016 ¹⁵		2015 ¹⁶		2014 ¹⁷	
	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense	Amount (in million €)	% of total expense
Private corporations	38	0.03%	34	0.03%	75	0.07%
Public organizations / corporations	3,223	2.75%	3,355	2.90%	2,844	2.52%
Citizens	307	0.26%	233	0.20%	244	0.22%
International organizations	1,475	1.26%	1,359	1.17%	1,623	1.44%
Lower government levels	3,124	2.66%	2,870	2.48%	3,543	3.14%

¹⁵ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2016/2.sejums/2_02_FMInf_290617_kons_kopbudzets.pdf.

¹⁶ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2015/2.s%C4%93jums/FMInf_230816_kons_kopbudzets.pdf.

¹⁷ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2014/2.s%C4%93jums/FMInf_300615_kons_kopbudzets.pdf.

There are five major types of grants and other transfers that are provided by Belgium to third parties:

- Grants given to private corporations to facilitate export or to promote multilingualism.
- Grants given to public corporations/organisations, like transfers to NMBS, Infrabel, Belgocontrol, BPost or Federal Agency Safety Food Chain (Public Health).
- Grants and other transfers to its citizens (in form of compensations/reimbursements, transfers to cults and secularism (Justice), transfers to promote road safety (Mobility) or transfers to disabled and elderly (SocSec).
- Transfers to supranational and international organisations, including transfers in the fields of defence (Def) and aerospace (Belspo), development corporation (BuZa) and transfers for the membership of supranational/international organisations (Bef, BuZa, Economy, Belspo).
- Transfers to lower government levels, for example to regions (IBZ, Fin, Belspo), municipalities (IBZ) or the local police.

Grants and other transfers given are recognised in the period in which the obligation accrues to the federal government. Four recognition criteria need to be met:

- Grants and transfers given can be measured reliably.
- The parties involved in the transaction can be identified.
- There is an obligation to pay.
- The entity has a document that justifies the transaction.

For transfers established by organic law, the expense is recognised when the transfers are due according to organic law; whereas for transfers not established by organic law, the expense is recognised when the deed of the assignment enters into force. Regarding compulsory contributions to international organisations, the expense is recognised when the contributions are due according to the applicable treaty. As far as non-compulsory contributions to international organisations are concerned, the expense is recognised when the deed of the assignment enters into force. Grants with conditions should also be recorded as off balance sheet items.

The advantages cited for this approach are similar to those cited for the accounting for revenue from grants and other transfers.

4.5 European Commission (EC)

4.5.1 Applicable accounting rules and scope of analysis

In accounting for grants and other transfers, the applicable references for the EC are EAR 3 (expenses and payables), EAR 17 (revenue from non-exchange transactions) and EAR 5 (pre-financing), which are all based on IPSAS. For a detailed description of these accounting rules please refer to section 3.2. Section 4.5 focuses more on the practical application of the accounting rules.

EC's expenditure mainly consists of expenses it incurs in the context of grants and other transfers provided to beneficiaries. Due to their importance, they are analysed in more detail. The focus of the analysis is on the cut-off procedures performed at year-end, which are - under an accrual basis of accounting - necessary to ensure that expenses are recorded in the proper accounting period.

4.5.2 Grants and other transfers given

The table below provides an overview of the amounts of grants transferred to the beneficiaries in the most recent financial years. Transfers and grants given represent on average between 83% and 87% of the Commission's operational expenditure.

	2016 ¹⁸		2015 ¹⁹		2014 ²⁰	
	Amount (in million €)	% of total expenses	Amount (in million €)	% of total expenses	Amount (in million €)	% of total expenses
Transfers and grants given	137.719	83%	134.356	86%	126.222	87%

For recognition and measurement purposes, EAR 3 distinguishes between three categories of grants and other transfers given. Please refer to section 3.2.2.1 for a definition of the different categories. The following table provides an overview of the timing of expense recognition.

Type of grant	Examples	Generating event	Recording during the year	Reporting date/cut-off at year-end
Entitlements	EAGF, EAFRD	Expenses incurred in the Member State	Advance payments	Estimate of eligible expenses incurred
Transfers under agreements	Grants under agreements, structural funds	Incurred eligible expenses	Eligible cost claim/expense summary	Estimate of portion of eligible expenditure (+ pro rata temporis)
Discretionary grants (no conditions attached)	Discretionary grants, contributions, donations	Acceptance	Acceptance	Acceptance

As a general principle under the accrual basis of accounting, expenses should be recorded in the period(s) to which they relate. This requires the application of year-end cut-off procedures, i.e. the EC has to estimate a significant part of the non-exchange expenses incurred in the period as they have not been formally approved yet at year end (see also section 3.2.2.4).

When the EC pays an advance for the expenses to be incurred by the beneficiary of a grant, it recognises the prepaid expense as an asset (see also section 3.2.2.4). As conditions attached to the grant are met (i.e. the beneficiary fulfils its performance obligations attached to the grant), the EC releases the prepaid asset and recognises an expense.

¹⁸ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2016/2.sejums/2_02_FMInf_290617_kons_kopbudzets.pdf.

¹⁹ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2015/2.s%C4%93jums/FMInf_230816_kons_kopbudzets.pdf.

²⁰ Refer to

https://www.kase.gov.lv/sites/default/files/public/PD/Saimniecisk%C4%81%20gada%20p%C4%81rskats/2014/2.s%C4%93jums/FMInf_300615_kons_kopbudzets.pdf.

Some specific characteristics of the three categories of grants and other transfers with regard to the cut-off procedures are described below.

4.5.2.1 Entitlements

Entitlements are transfers that are granted automatically if beneficiaries meet specified eligibility criteria, i.e. for instance when a MS incurs a certain expense. One important example are the payments made to farmers financed by the EAGF. The farmers receive the payments not directly from the EC, but from national or regional payment agencies. These agencies are also responsible for checking if the eligibility criteria are met. They report any payments made to the beneficiaries (farmers) which then the EU reimburses on a monthly basis to the agencies. The reimbursements paid might be subject to later corrections following audit.²¹

Cut-off procedures are required for entitlements to ensure expense recognition in the related period. For instance, if beneficiaries meet eligibility criteria before the reporting date, but the cost claim has not yet been formally approved, the EC needs to estimate the corresponding expense incurred. Regarding the EAGF, the EC estimates the portion of reimbursements made to the payment agencies that are corrected later on.

4.5.2.2 Transfers under agreements

Transfers under agreements are similar to entitlements, with however the following main difference: the terms for receiving the grant or other transfer are negotiated and written down in a contract. As such, nearly all transfers include conditions and performance obligations that need to be fulfilled (e.g. the beneficiary needs to make specified expenditures which will then be reimbursed by the EU). In addition, many transfers under agreements have a multi-year life cycle, which requires cut-off procedures at year end.

To ensure proper cut-off, the EC needs to make significant accounting estimates in respect of the state of progress of these grants at each year-end closing date. If reports received from beneficiaries are considered to be reliable, these reports can be used as a basis. Based on historical data, the EC needs to estimate which share of the claims charged will be rejected and exclude this amount from the expense recognised in the reporting period. However, there might also be periods which are not covered by any report. The following example illustrates how proper cut-off procedures are performed by the EC.

Example

The EC has provided a grant to Entity A for 1,000 k€ in March 2017. The eligibility period of the grant goes from 1 April 2017, till 31 March 2021. For the period ending 31 December 2017, eligible expenditure amount to 480 k€. In February 2019, before closing the 2018 year-end accounts, the EC receives a cost statement for 70 k€ covering the period 1 January till 31 October 2018. The EC estimates that on average 5 % of the costs declared on these programmes are rejected.

Based on its experience, the EC considers that the cost statement constitutes reliable financial information. The cost statement covers a 10-month period up to October 2018 and has an expected rejection rate of 5%. The estimated eligible cost to be recognised in the statement of financial performance as per 31 December 2018 is therefore calculated as follows: 70 k€ * 0.95 = 67 k€.

²¹ See https://ec.europa.eu/agriculture/cap-funding_en.

A period of two months in 2018 is not covered by any cost statement. In the absence of any reliable information concerning the spending pattern of the programme, the straight-line method is used to approximate the expense to be recognised for November and December 2018. The remaining portion of the grant, that is 453 k€ (= 1,000 - 480 - 67), is equally spread over the remaining contract period (29 months from 1 November 2018 till 31 March 2021). The expense to be recognised for November and December amounts to 31 k€ (= 453 / 29 * 2).

The total expense recognised in 2018 amounts to 98 k€ (= 67 + 31).

4.5.2.3 Discretionary grants

The EC can freely decide whether to make a transfer or not. As typically no conditions are attached to discretionary grants, they are recognised when they are authorised by the EC.

4.6 Comparison between the different countries and the EC

4.6.1 Grants and other transfers received

The table below provides a high-level comparison of the main categories of grants and other transfers received and the related accounting principles as applied by the Latvian and Belgian governments as well as the EC.

Grants and other transfers received			
	<i>Latvia</i>	<i>Belgium</i>	<i>EC</i>
Main categories of grants and other transfers received	<ul style="list-style-type: none"> • EU grants. • Foreign financial assistance. • Transfers between central and local governments. • Donations. 	<ul style="list-style-type: none"> • EU grants. • Transfers from other levels of government. • Fines. 	<ul style="list-style-type: none"> • Fines. • Recovery from expenses²². • On a project basis, contributions from Member States or third countries. • ²³
Accounting framework	National framework based on IPSAS.	National framework (no application of IPSAS 23).	EAR 17 (based on IPSAS 23).
Revenue recognition	Revenue is recognised on an accrual basis. The recipient's revenue recognition mirrors the transferor's expense recognition.	Grant recognised when the right to the grant is established. With regards to EU grants, revenue recognition matches the expenses the grant is intended to compensate.	Revenue is recognised on an accrual basis. Grants and transfers received recognised as an asset are recognised as revenue, except to the extent a liability is also recognised

²² I.e. amounts to be recovered due to illegal or irregular spending of grants and transfers given by the EU.

²³ Member States' own resources contributions to the EU budget are not included here because the own resource revenue of the European Commission (from VAT, GNI based resources and other levies) can be considered as having similar characteristics as the tax revenue of national governments. The financial statements of the European Commission have a separate heading for 'transfers', which excludes own resources revenue. The own resources revenue of the European Commission is not therefore comparable to transfers within a national government.

Grants and other transfers received			
	<i>Latvia</i>	<i>Belgium</i>	<i>EC</i>
			in respect to the same grant/transfer. A systematic matching of revenue and expenses is not foreseen except in case of conditions attached to the grant/transfer.

It should be noted that the main categories of grants and other transfers received are similar in the two countries: Latvia and Belgium both name EU grants and transfers between different levels of government as the two main categories.

Regarding the timing of revenue recognition, the accrual basis of accounting is adopted. Latvia very much insists on the need to have parallel accounting treatments regarding the recipient's revenue recognition and the transferor's expense recognition. With regards to EU grants, the Belgian approach also puts the stress on matching revenue from grants and the expenses the grant compensates.

The EC applies EAR 17, which is in line with IPSAS 23. There is no matching of revenue from grants and transfers and expenses except for grants and transfers received under conditions.

In contrast to the Latvian and the Belgian approach, current IPSAS rules do not focus on linking revenue and expenses recognition. Revenue is recognised when the right to receive the grant is established or when the conditions attached to the grant are met. It is also worth reminding that current IPSASB proposals included in the CP on revenue and non-exchange expenses recommend to apply the same approach (i.e. the PSPOA) for both revenue and expense recognition.

4.6.2 *Grants and other transfers given*

The table hereafter provides a high-level comparison of the main categories of grants and other transfers given by Latvia, Belgium and the EC as well as of the related accounting principles.

Grants and other transfers given			
	<i>Latvia</i>	<i>Belgium</i>	<i>EC</i>
Main categories of grants and other transfers given	<ul style="list-style-type: none"> • Transfers between central and local governments. • Membership fees to international organisations. • Donations. 	<ul style="list-style-type: none"> • Grants and other transfers to private corporations. • Grants and other transfers given to public corporations/ organisations. • Grants and other 	<ul style="list-style-type: none"> • Transfers under shared implementation (mainly agriculture and cohesion)²⁴. • Grants for actions intended to achieve policy objective. • Operating grants for

²⁴ Under this method of implementation, the budget implementation tasks are delegated to the Member States.

Grants and other transfers given			
	<i>Latvia</i>	<i>Belgium</i>	<i>EC</i>
		transfers to citizens. <ul style="list-style-type: none"> • Transfers to supranational and international organisations. • Transfers to lower government levels. 	operating expenditure of an entity.
Accounting framework	National framework based on IPSAS.	National framework.	EAR 3.
Expense recognition	Revenue is recognised using the accrual basis of accounting. The transferor's expense recognition should mirror the recipient's revenue recognition.	Expense is recognised on an accrual basis when the right of the beneficiary to receive the grant is established.	Expense recognition in the period during which the events giving rise to the transfer occurs if: <ul style="list-style-type: none"> • Allowed by regulation/signed contract/authorised; • Eligibility criteria (when applicable including meeting the conditions attached to the grant) are met; • Reasonable estimate.

Transfers between different levels of government are an important category of grants and other transfers given for the two governments. Both Latvia and Belgium also cited transfers to international organisations as an additional category. Despite of country-specific features, similar grants and transfers appear to be given in the two countries.

EC provides different kinds of grants and other transfers which are linked to the implementation of its policy towards EU Member States. The majority of the non-exchange transfers given by the EU are transfers received by Member States authorities (about 70% of expenses).

Both the Latvian and the Belgian approach tend to lead to a symmetrical accounting for revenue and expenses from the same transactions in order to achieve a neutral impact in consolidation. Under EAR, there is no explicit link between revenue and expense recognition as it is not foreseen by internationally accepted accounting standards for the public sector.

5 Difficulties/issues when accounting for grants and other transfers

Grants and other transfers represent significant amounts of revenue and expenses for governments. This is also the case for the two countries analysed (please refer to section 4.3 for Latvia and to section 4.4 for Belgium) and the European Commission (see section 4.5).

As however highlighted in section 4.1, accounting practices differ significantly from one country to another one. On the one hand, this results from the different stages of accounting maturity (ranging

from cash accounting to accrual accounting under best international practices) of the different Member States and often as well of the different government levels within Member States. On the other hand, even countries that apply IPSAS (or national standards based on IPSAS) may account for these important flows of revenue and expenses differently due to judgemental areas or difficulties to apply the current guidance included in IPSAS 23. In the context of the analysis of the suitability of the IPSAS standards for EU Member States, the 2014 PwC study²⁵ included IPSAS 23 in category 2, i.e. the category of standards that (may) need (some) amendments or for which implementation guidance is (may be) needed.

For instance, the distinction between exchange and non-exchange transactions and between conditions and restrictions is often considered highly judgemental. Concerning non-exchange expenses, the absence of a specific IPSAS standard leads to the application of different approaches in practice. Hence, resource recipients and resource providers may apply inconsistent approaches to the same transaction.

The future IPSAS(s) on revenue and non-exchange expenses might solve some of these issues because the related IPSASB project takes a comprehensive look at the current accounting rules and aims at solving problems encountered in practice. In the following sections, we explain what the main issues are.

A distinction is made between conceptual difficulties and practical difficulties. In commenting on these difficulties, we not only consider the current accounting principles but also the thoughts that are developed in the IPSAS CP on revenue and non-exchange expenses and the discussion that took place on the topic at the IPSAS Working Group in Luxembourg on 21 and 22 November 2017.

5.1 Conceptual difficulties

5.1.1 Absence of IPSAS standard dealing with non-exchange expenses

No IPSAS standard currently deals with the issue of non-exchange expenses (other than social benefits). This is one of the most significant gaps remaining in IPSAS literature as flows from non-exchange transactions (including grants and other transfers given) are significant for governments.

This lack of guidance on the topic leads to diversity of accounting practices, among others in the area of multi-year grants given to other levels of governments or third parties.

5.1.2 Problems in determining whether revenue transactions are exchange or non-exchange

Under the current IPSAS guidance, a distinction needs to be made between exchange and non-exchange revenue: IPSAS 9 deals with revenue from exchange transactions while IPSAS 23 deals with revenue from non-exchange transactions. As a reminder non-exchange transactions are defined under IPSAS as transactions where an entity receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

²⁵ See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 134-135.

The distinction between exchange and non-exchange proves to be problematic in practice. The IPSASB also takes the example of water provision where it may be unclear whether a transaction is non-exchange (a tax) or exchange (a fee for a service).

The concepts of 'approximately equal value' and 'directly giving' may also lead to different interpretations.

5.1.3 Problems in determining whether a stipulation is a condition or a restriction under the current IPSAS 23 and how to interpret the concept of public sector performance obligation under the new proposed guidance

Stipulations are often attached to grant agreements. These can either be conditions or restrictions.

Conditions require returning the transferred asset or future economic benefits/service potential to the transferor in the event that the conditions are breached. Restrictions do not. Conditions on transferred assets give rise to the recognition of a liability until the conditions are satisfied (until then, the recipient has a performance obligation); restrictions on transferred assets do not.

The substance of the arrangement needs to be considered and the distinction between a condition and a restriction is not always easy to make.

The IPSASB CP on revenue and non-exchange expenses foresees to differentiate between three types of transactions: Category A, Category B, and Category C (see section 3.6.1 for more details about these categories). It is crucial for the classification to determine whether the transaction contains performance obligations or not.

The CP contains little guidance and is lacking illustrative examples on how to classify transactions in the proposed three categories. At the current stage of the project, it is not fully clear how the new proposed principles will need to be applied in practice and this may lead to further application issues and a continuing diversity across governments if this is not fixed in the final standard.

Finally, the existence (or lack thereof) of past practices may need to be considered when assessing conditions on transferred assets and restrictions that are set, for example, between a government and a controlled entity. In the separate financial statements of the controlled entity, there may be debates in determining the substance of such stipulations given the power of the government over the entity and the absence of precedents where transfer assets were returned to the government (as original transferor).

5.1.4 Lack of guidance on how to account for grants related to assets

Another main area where guidance is missing concerns grants related to assets (called capital grants in the IPSASB CP on revenue and non-exchange expenses). This can be illustrated by the following two examples.

The first example refers to the construction of a building which is subsidised by a donor. For accounting purposes, the entity receiving the subsidy has to determine if and what stipulations are attached to the grant and if these can be considered as conditions or performance obligations. Stipulations could for example relate to the construction of the building or to the later use of the building. There may be some room for interpretation, which creates diversity in practice.

Secondly, an entity might be allowed to use a building for free. In this case, one could argue that the related income is recognised immediately because no conditions or performance obligations are attached to the grant. However, one might also come to the conclusion that the income should be spread over the term of usage. This appears to reflect the Latvian approach for donations (see section 4.3.1). Questions may also arise regarding measurement (as there is no stated amount). Furthermore, the terms of the agreement may be stated very broadly, which may cause an additional difficulty in assessing whether the recipient has control over the asset.

5.1.5 Lack of guidance on how to account for long-term / multi-year grants

The issue of determining whether a stipulation is a condition or a restriction under the current IPSAS 23 and how to interpret the concept of public sector performance obligation under the new proposed guidance is an important issue in the accounting for long-term grants.

Another issue arises in respect of multi-year grants that have only time requirements. The current IPSAS 23 treatment of transfers with time requirements (and no other stipulations), i.e. revenue recognition by the resource recipient when the transfers are receivable, might not provide useful information about the period over which the resources will be used.

5.1.6 Grants and other transfers received as principal or agent

Amounts collected on behalf of another party should not be included in the reporting entity's revenue - see section 3.1.2.1 regarding IPSAS 23. In some cases, public entities receive funds which they transfer to other parties. In these instances, a detailed analysis is required to determine whether the entity acts as a principal or as an agent. Often these agreements are complex and embedded in (local) law.

5.1.7 Grants that are in substance financing arrangements

The terms of the agreement need to be analysed in depth to determine whether the arrangements in place are in substance grant agreements (possibly with stipulations) or financing arrangements. In the latter case, a financial liability needs to be recognised.

5.1.8 Accounting for government appropriations

There is no clear guidance on how to account for government appropriations²⁶ and such transactions are very frequent with governments.

5.1.9 Presentation and disclosure of grants and other transfers

Under current IPSAS rules, revenue from non-exchange transactions should be presented as part of the total revenue or, if material, separately from revenue from exchange transactions. Such a distinction is not always easy to make. In addition, no separate distinction is required between taxes on the one hand and grants and other transfers on the other hand. In practice however such a distinction is made by governments if it is perceived to be useful information for the users of financial statements.

ESA 2010 foresees specific codes for different types of grants.

The absence of clear guidelines on the topic may lead to diversity in practice and a lack of comparability in EPSAS financial statements.

5.2 Practical difficulties

5.2.1 Inventory of all grants and other transfers and data collection

In order to ensure completeness of the accounting, a comprehensive inventory of all grant and other transfer arrangements received and given should be performed at the level of each reporting entity. Under accrual accounting, information is not only needed when cash is received or paid, but earlier in the process, when a right to receive payment (or an obligation to transfer funds) is established. In addition to this, the terms and conditions of the grant and other transfer arrangements need to be analysed in order to determine the appropriate accounting treatment. Depending on the accounting principles that will be selected under EPSAS, the existence of stipulations, conditions or performance obligations will have an impact on the accounting, including the pattern of revenue or expense recognition.

The collection of all required information might be challenging because governments typically receive and provide many grants and other transfers, different types of grants and transfers exist and the stipulations attached to the grants can differ. Furthermore, grants and other transfers usually impact various government entities within the consolidation scope, and arise at different levels of the government (e.g. lower level agencies which need to be included in the consolidated financial statements), which might further hamper data collection.

Efficient and robust processes need to be put in place to ensure timely collection of data and the availability of all necessary information for accounting purposes. Specific tools may need to be implemented for the purpose of grant data collection and management.

²⁶ "Authority granted under a law by the Legislature to the Executive to spend public funds up to a set limit and for a specified purpose. Annual appropriations are made through annual budget laws or, in some countries, separate appropriation acts consistent with the budget. Supplementary budget appropriations are sometimes granted subsequent to the annual law if the annual appropriation is insufficient to meet the specified purpose" - OECD budget practices and procedures database, Final glossary, 19 December 2016.

5.2.2 Consistent accounting for all types of grants and other transfers

Not only the large number of grants and other transfers, but also their differing nature and their potential complexity creates a challenge in terms of consistent accounting treatment across the different levels of government. As grant agreements may be complex in nature, government staff will need to be trained and possess the necessary skills to account for the transactions in an appropriate manner.

5.2.3 Cut-off procedures at year end

Application of the accrual basis of accounting requires cut-off procedures to be performed at the end of the reporting period to make sure that revenue and expenses are recorded in the period in which they accrue.

Performing the year-end cut-off is especially challenging with regard to multi-year grants and other transfers. At each reporting date, it needs to be assessed to which extent the beneficiary complies with the conditions (under the current IPSAS 23) (or possibly with the stipulations/performance obligations under the future IPSAS and EPSAS standards) attached to the grant.

Financial activity reports in respect of the underlying subsidised activity are often the main source of input. This is for example the case for grants received from the European Commission. These reports enable to estimate the expenses incurred at year end. However, they are subject to a detailed review (in order to check the eligibility of the expenses that are reported), which may turn out to be time consuming.

Some adjustments might be required following grant audits as part of the costs declared may be found not to be eligible. An estimation of eligible expenses at year end could be based on past experiences in terms of rejection rates.

Furthermore, expense reports might not cover the whole reporting period and the expenses for the rest of the year may need to be estimated, e.g. when a report is delivered annually as of 31 October, but the financial statements are prepared as of 31 December. Finally, problems might arise when the reports are delivered late or do not include all the information that is needed for accounting purposes.

An example of how the European Commission performs cut-off procedures for a multi-year grant can be found in section 4.5.2.2.

5.2.4 Reconciliation of inter-government transactions in consolidation

As evidenced by the analysis of accounting practices in Latvia and Belgium, inter-government grants and other transfers (i.e. grants and other transfers between entities that are included in the same consolidation scope) are frequent (see sections 4.3 and 4.4).

The reporting entity and consolidation scope can be defined at different levels. It may for example concern grants by a central government entity to a local government entity in whole-of-government accounts (the reporting entity being in this case the whole public sector in one country). It may also cover grants by a local government to a local agency included in the consolidation scope of the local government (the reporting entity being here the local government as a whole).

Inter-government transactions need to be eliminated for consolidation purposes. This process proves to be challenging if the grantor and the grant recipient do not account for the transaction in a similar way (mirror accounting) and no robust process exists to reconcile and eliminate inter-government balances and transactions in the consolidation. The large number of transactions may lead to an additional complexity.

6 Discussion of matters relevant for a European harmonisation

In our opinion, the topics that are relevant for discussion at a European level in the context of the EPSAS standard setting are the following:

- Need for more practical application guidance on the future EPSAS standards.
- Strategic approach for the EPSAS standard setting.
- Technical accounting discussion on the conceptual approaches in relation to certain specific accounting issues.

6.1 Need for more practical application guidance on the future EPSAS standards

In our view, the first key question to be debated is whether Member States feel the need for more practical guidance on how to apply the future EPSAS standards.

A review of the discussion matters included in IPSASB CP on revenue and non-exchange expenses and of the accounting practices by Member States shows that the subject matter is complex and that diversity exists in accounting practices.

Complexity arises from the variety of grant and other transfer arrangements that exist, from the lack of guidance on certain specific topics (e.g. non-exchange expenses) and the lack of clarity on how to apply the guidance for other topics (e.g. distinction between exchange and non-exchange transactions and interpretation of the concepts of stipulations which are either conditions and restrictions).

The level of detail and tailoring wanted in the EPSAS guidance may be discussed and the response to that question may differ depending on the types of grants. For example, giving more detailed and specific accounting guidance for grants that are commonly received by Member States (e.g. grants received from the European Commission) may be of general interest to all. On the other hand, the characteristics of other types of grants and transfers may be influenced by local regulations and practices, and the accounting for these transactions may refer to more general yet clear accounting guidance.

Finally, the need for a consistent presentation and disclosure of revenue and expenses arising from grants and other transfers may also be discussed in order to enhance comparability of the reporting between EU Member States.

6.2 Strategic approach for the EPSAS standard setting

The second key question relates in our opinion to the choice of the strategic approach to be adopted to develop EPSAS standards for grants and other transfers.

As already highlighted, the topic is complex and there is currently no harmonised approach in accounting for grants and other transfers within the EU. Developing EPSAS standards from scratch

would be very time consuming and the complexity of the topics combined with different approaches taken in national rules may lead to lengthy debates among Member States.

The current IPSASB CP on revenue and non-exchange expenses provides worthwhile insights into the current accounting rules and practices for grants and other transfers and suggestions about how the current accounting could be improved. The CP has been developed after consultation with preparers. Although the IPSASB acknowledged that the sample chosen was not fully representative, the CP makes a first analysis of the issues in respect of accounting for grants and other transfers in a rather comprehensive way.

Member States can consider that the IPSASB CP is a good starting point for a deeper analysis of the issue among EPSAS stakeholders. As already mentioned, the present issue paper may also contribute to the IPSASB thinking by providing a more comprehensive analysis at the European level.

The deadline for comments on the IPSASB CP expired on 15 January 2018. However, Member States still have the possibility to influence the IPSAS standard setting by providing comments on the exposure draft (ED) that will be issued later in 2018, after the IPSASB has analysed and considered the first series of comments received from IPSAS stakeholders on the questions asked/proposals made in the CP.

Specific topics for discussion are commented upon in section 6.3 below.

6.3 Technical accounting discussion on the conceptual approaches in relation to certain specific accounting issues

We propose to organise the discussion around those topics that have been spotted as conceptual difficulties under section 5.1. and one additional issue identified as practical issue, that is reconciliation of inter-government grants and other transfers as it touches a conceptual question too.

On the contrary, the necessity to put in place adequate administrative processes, including to capture the necessary information to account for grants and other transfers, does not, in our view, need to be discussed in the context of the EPSAS standard-setting process. The challenge for governments is of an organisational nature.

To set the scene for the discussion, we herewith recall IPSASB's proposal to classify non-exchange transactions under the three categories below, each of them triggering a different accounting treatment.

Category A	Revenue and non-exchange expense transactions with no POs or stipulations
Category B	Revenue and non-exchange expense transactions that contain POs or stipulations, but do not have all the characteristics of a transactions within the scope of IFRS 15
Category C	Revenue transactions that are within the scope of IFRS 15

For more information we refer to section 3.6 of the present issue paper.

ESA 2010 provides guidance for non-exchange transactions, especially concerning recognition. For this purpose, categories of distributive transactions are defined (e.g. ‘subsidiaries’, ‘current transfers with general government’, ‘capital transfers’). In addition to the general recognition principles, ESA 2010 describes for each category the timing of recording. As EU MSs receive similar types of grants and other transfers, such a categorisation appears to be useful.

An in-depth analysis would be necessary to find out whether the specific rules in ESA 2010 would be in line with IPSAS principles that are currently being developed and whether a convergence can be obtained in respect of the timing of revenue and expense recognition. For investment grants, it would not be possible (see 3.4.2 and 3.5.1.2).

6.3.1 Absence of IPSAS standard dealing with non-exchange expenses

Given the lack of guidance on the accounting of expenses arising from non-exchange transactions in the current suite of IPSAS standards, this issue is specifically addressed in the IPSASB CP on revenue and non-exchange expenses.

The IPSASB proposes that resources linked to non-exchange transactions for universally accessible services and collective services be expensed as services are delivered as no related obligating event exists. This proposal does not seem controversial and EPSAS Working Group members might easily confirm they agree with it.

The IPSASB also proposes an approach whereby grants, contributions and other transfers given, which are non-exchange expenses, should mirror the accounting treatment adopted for equivalent revenue transactions, that is the public sector performance obligation approach. This approach to revenue recognition builds on IFRS 15 applicable to commercial transactions entered into by private companies and adapts it in the public sector context. Following divergent comments received from constituents on its proposal to also apply the public sector performance obligation approach for grants and transfers given, the IPSASB indicated that they will give another thinking to it.

The opportunity of the proposal included in the CP could be discussed between Member States, taking into account its conceptual merits and its practical implications. The Latvian government has insisted on the need to align the accounting of grants and transfers given and received in order to facilitate the treatment in consolidation. Similar comments were received from various members of the EPSAS Working Group during the meeting held in Luxembourg in November 2017.

EAR 3 includes detailed accounting rules for non-exchange expenses. It distinguishes between entitlements, transfers under agreements as well as discretionary grants, contributions and donations. For each type of transfer EAR 3 describes the recognition and measurement principles. In addition, the rule considers the necessity of cut-off procedures and the challenges of accounting for multi-year grants. These principles might be used as a source of inspiration for developing a guidance in relation to the cut-off procedures.

6.3.2 Problems in determining whether revenue transactions are exchange or non-exchange

The CP proposes one single recognition model that does not make the distinction between exchange and non-exchange transactions. The new proposed model would build on whether a transaction includes stipulations and creates performance obligations (in the public sector context) or not.

Member States might comment on whether the new proposed model is an appropriate response to the difficulty to distinguish exchange from non-exchange transactions.

6.3.3 Problems in determining whether a stipulation is a condition or a restriction under the current IPSAS 23 and how to interpret the concept of public sector performance obligation under the new proposed guidance

The PSPOA (public sector performance obligation approach) proposed by the IPSASB would eliminate the need to assess whether a stipulation attached to a grant or transfer arrangement is a condition or a restriction. The determining factor will consist in identifying whether the transaction contains performance obligations or not.

Member States might comment on whether the PSPOA is in their view an adequate response to the issue of interpreting whether stipulations are conditions or restrictions.

Given that the CP does not provide clear guidance on how to apply the PSPOA in practice, Member States could encourage IPSASB staff to develop robust criteria on that aspect.

6.3.4 Lack of guidance on how to account for grants related to assets

IPSASB literature currently does not contain any specific guidance on grants related to assets and the IPSAS CP proposes to develop one.

Some Member States already expressed the need for such guidance during the EPSAS Working Group in Luxembourg. The EPSAS Working Group may confirm that such guidance is needed.

6.3.5 Lack of guidance on how to measure long-term / multi-year grants

Accounting for multi-year grants is a key issue for many governments, not only for grants that have stipulations attached to them but also for grants without stipulations and possibly with time requirements only.

There is inherent tension between the balance sheet (specifically the definition of a liability in the Conceptual framework) and the statement of financial performance (especially to provide performance information which is meaningful for the decision making). IPSAS 23 and IPSASB CP on revenue and non-exchange expenses prescribe revenue from grants to be recognised unless a liability needs to be recorded (i.e. when a condition attached to the grant exists under the current IPSAS 23 and when a performance obligation exists as proposed in the IPSASB CP). Revenue is recognised only the liability is released, i.e. when the condition or the performance obligation is satisfied. Another treatment, not in line with IPSAS 23 and the treatment proposed by the IPSASB in its CP, would consist in matching revenue from grants with the expenses the grant is intended to compensate, without consideration of the existence or not of a liability as defined in the Conceptual framework.

A discussion between EPSAS Working Group members on the objectives of multi-year grant accounting, considering the tension referred to above, could be useful.

6.3.6 *Other accounting issues relating to grants and other transfers received*

In addition to the above key topics, Member States might comment on whether additional accounting guidance is needed on such topics as:

- How the time value of money in dealing with multi-year grants should be considered.
- Whether they act as principal or agent when grants and other transfers are received and what is the consequential accounting impact.
- How grants that are in substance financing arrangements should be accounted for and how to identify such transactions.
- Government appropriations.

7 PwC's recommendations on the way forward

We present below our recommendations in the same order as the topics proposed for discussion for a European harmonisation under Chapter 6.

7.1 Need for more practical application guidance on the future EPSAS standards

Given the current diversity in Member State practices relating to the accounting for grants and other transfers, the complexity of the topic analysed and the difficulties in interpreting the principles included in international financial reporting frameworks, we strongly recommend that detailed and tailored guidance be developed as part of the future EPSAS standard setting.

In thinking about the guidance to be developed under the future EPSAS, comparability of accounting treatment within the EU is of particular importance.

The comparison of the accounting practices in selected countries (Latvia, Belgium) shows that governments receive and provide grants and other transfers that are largely similar. Especially the various types of EU grants offered to beneficiaries are basically the same for all EU MSs. Therefore, it is necessary to ensure that EU grants and comparable grants of the MSs are accounted for consistently across the EU. This could be ensured by developing specific accounting guidelines and illustrative examples per type of grant or other transfer. This may be particularly valuable for the treatment of multi-year grants.

In addition, harmonisation of presentation and disclosure requirements would provide a useful basis of comparison for grants and other transfers received and given by MSs.

7.2 Strategic approach for the EPSAS standard setting

The question on how to approach the discussion for the EPSAS standard setting is crucial in relation to grants and other transfers because the international thinking is currently developing in this respect and the topic is particularly complex.

The current IPSASB CP on revenue and non-exchange expenses provides a very good basis for starting the discussion on the accounting for grants and other transfers between Member States. The issues encountered in practice are explained and some proposals are made to respond to the difficulties in applying current IPSAS rules.

Given this context, we strongly recommend that the discussions between EPSAS stakeholders capitalise on the first analyses and discussions that are taking place at IPSASB level.

Complementary to that, the developments at IPSASB level provide a unique opportunity for Member States to influence the IPSAS standard setting. The IPSASB CP was open for comments until 15 January 2018 but Member States still have the possibility to provide their comments on the exposure draft (ED) that will be issued later in 2018.

The EPSAS Working Group provides a unique platform for progressing on the discussions and sharing the European views with the IPSASB. Member States might consider taking advantage of this opportunity and progress in the discussion to be ready to share their views with the IPSASB when the ED is issued.

7.3 Technical accounting discussion on the conceptual approaches in relation to certain specific accounting issues

The proposals included in IPSASB CP on accounting for revenue and non-exchange expenses are particularly welcome for the following reasons: they aim to fill one of the most important remaining gaps in the suite of IPSAS standards by providing accounting guidance on non-exchange expenses, which represent major transaction flows in the public sector, and they address practical issues in accounting for revenue from exchange and non-exchange transactions.

We share hereafter some thoughts on the input that may be given to the IPSASB to influence the IPSAS standard setting.

IPSASB's proposal to categorise revenue into three categories - (A) transactions with no performance obligations or stipulations (B) transactions with performance obligations or stipulations which do not have all the characteristics of a transaction in the scope of IFRS 15 and (C) transactions that meet the definitions and scope of IFRS 15 - and for category B transactions to recognise revenue following a five-step approach based on the fulfilment of performance obligations and that considers the specific characteristics of the public sector, may be an appropriate response to many of the issues identified in accounting for grants and other transfers.

However given the proposed differences in accounting models, we want to stress the importance of delineating those categories in mutually exclusive while complete scopes.

The proposal to recognise expenses from grants, contributions and other transfers under the public sector performance obligation approach mirrors the accounting treatment for revenue of a similar nature. Transfers between entities that are part of the same consolidation scope are frequent in the public sector. Mirroring the accounting treatment for similar non-exchange revenue could not only make sense from a conceptual point of view but would also facilitate elimination of inter-government balances and transactions in the consolidation process.

On a more general level, we recommend that the IPSASB clearly articulates to what extent the proposals reconcile with the provisions of the Conceptual framework, including the definition of elements and the accountability and decision-making objectives of financial statements.

As the subject-matter is complex, we also strongly recommend to provide sufficient practical guidance and illustrative examples in order to enhance consistency in the application of the proposed approaches.

In addition to that, as highlighted under 7.1, we believe it would be useful to produce tailored and practical guidance as part of the EPSAS standard-setting process to address the accounting treatment of those transactions that are the most frequent for EU governments.