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Item 6 of the Agenda

**EPSAS issue paper on the accounting treatment of social
contributions**

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- for discussion
(revised version after the WG)*

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

10 October 2017

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1. Objectives of the Issue Paper

The aim of this paper is to develop an analysis of the accounting treatment of social contributions with a view to financial reporting requirements under the future European Public Sector Accounting Standards (EPSAS).

This paper takes into account:

- ▶ The most important categories of social contributions in the European Union (EU);
- ▶ The approaches taken — including analysis of how these categories of social contributions are accounted for — at an accounting standard level: International Public Sector Accounting Standards (IPSAS), European Union Accounting Rules (EAR), International Financial Reporting Standards (IFRS) and the European System of Accounts (ESA); and
- ▶ The approaches taken — including an analysis of how these categories of social contributions are accounted for — in three Member States (Czech Republic, France, and Poland).

The issues paper addresses the following questions that were raised by Eurostat:

- ▶ For which main categories of social contributions do problematic points/issues with regards to recognition and measurement arise?
- ▶ Are the problematic points/issues with regards to recognition and measurement of social contributions satisfactorily treated in IPSAS?
- ▶ Which categories of social contributions should be treated by future EPSAS standards or guidance taking into account materiality and comparability considerations?
- ▶ Would supplementary guidance on some aspects of the treatment of social contributions be necessary and what would this look like?
- ▶ What would the consequences be for a possible convergence between EPSAS and ESA?
- ▶ What way forward is recommended on accounting for social contributions and what would be a good approach for organising future discussions with the EPSAS stakeholders?
- ▶ Are there any key parallels between taxes and social contributions that should be taken into account?

2. Background

As shown in the issues paper on the accounting treatment of taxes, social contributions represent the most important source of non-exchange revenue of governments in Europe.¹ Given the importance of social contributions for the financing of social insurance, the accounting for social contributions is an essential element of public sector accounting.

Statistical information on tax revenue by Eurostat show the importance of social contributions as a percentage of total tax revenue in the EU for the year 2014:

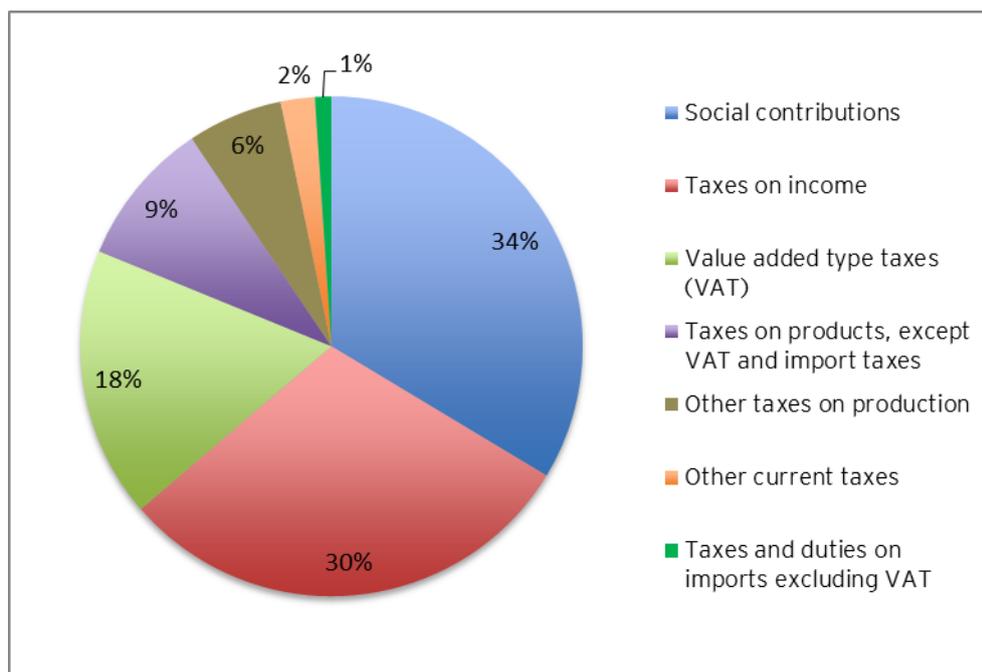


Figure 1: Categories of taxes as a percentage of total EU tax revenue in 2014

The social security systems in the European Union (EU) are not harmonised; they are within the Member States' exclusive responsibility.² Article 168 paragraph 7 of the Lisbon Treaty provides for example that Member States have the competence for the definition of their health policy and for the organisation and delivery of health services and medical care. Each EU Member State (MS) has its own laws determining what benefits citizens are entitled to, how much they will receive and for how long. Currently, EU rules only determine which country's social security covers a beneficiary when two or more countries are involved.

Social contributions are paid on a compulsory or voluntary basis by employers, employees and self- and non-employed persons.³ They typically finance social benefits and may be levied on both employees and employers. Social protection benefits in the EU are transfers to households, in cash or in kind, intended to relieve them of the financial burden of several risks

¹ In 2014, social contributions made up 34% of total tax revenues in the EU. See Eurostat EPSAS Working Group of 22-23 November 2016, Agenda item 7, EPSAS issue paper on the accounting treatment of taxes, p. 7 (<https://circabc.europa.eu/sd/a/5ca5844d-a004-455f-8a54-dbe9eb6f3de4/Item%207%20-%20Issue%20Paper%20on%20taxes.pdf>).

² See European Commission, Social security coordination factsheet - Guiding principles and rules, 2016 (<http://ec.europa.eu/social/BlobServlet?docId=16773&langId=en>).

³ See Eurostat, Statistics Explained, Glossary: Social contributions, http://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Social_contributions.

and needs.⁴ These include benefits to address and/or support disability, sickness/healthcare, old age, survivors, family/children, unemployment, housing and social exclusion not covered elsewhere. Social contributions are usually earmarked to finance social benefits and are often paid to those institutions of general government that provide such benefits.⁵ In terms of accounting, social contributions and social benefits are accounted for separately except where there are insurance-type schemes.

There are large differences in the way Member States have organised social benefits, healthcare and other social security services.⁶ In practice, it can be difficult to distinguish between taxes and social contributions. Sometimes revenues from taxes are used to finance social benefits. However, the EU has regulations in place that coordinate the interaction between national social security systems. This falls within the framework of free movement of persons. Within the EU social security is a very complex and specific legal area. Therefore, national experts from Member States need to be involved in the discussion on the accounting treatment of social benefits.

The public consultation on the assessment of the suitability of the IPSAS for the Member States stated the incompleteness of IPSASs with respect to public sector accounting requirements (e.g. with regard to taxation, social benefits) as one of the main arguments against their implementation.⁷

In that context, it has to be clarified that IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)*, prescribes requirements for the financial reporting of non-exchange transactions under the accrual basis of accounting (see IPSAS 23.1 and 23.2). Additionally, it has to be noted that currently the IPSASB has a project on “Revenue” on its agenda. The aim of this project is to develop one or more IPSASs covering revenue transactions (exchange and non-exchange) in IPSASs.⁸

With respect to recognition of revenues from social contributions, the empirical study by PwC in 2014 showed that on average 13 out of 24 central governments in Europe recognise revenue from social contributions when cash is received, and about 8 out of 24 recognise it when contributions are declared (social declaration).⁹ Only very few central governments use the ‘time adjusted cash’ method in their own public sector accounting/financial reporting, or attribute the revenue to the “taxation period”, with asset recognition based on (year-end) estimates and the use of macro-economic indicators or historical trends/data. The study also showed that the use of methods for the recognition of revenues from social contributions is similar to the use of the methods for the recognition of revenue from taxes. The following graph summarizes these findings:

⁴ See Eurostat, Statistics Explained, Glossary: Social protection benefits, http://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Social_protection_benefits. In the European Union social (protection) benefits are defined in the European system of integrated social protection statistics (ESSPROS).

⁵ See OECD (2017), Social security contributions (indicator). doi: 10.1787/3ebfe901-en.

⁶ See European Commission, Social security systems in the EU, (http://europa.eu/youreurope/citizens/work/unemployment-and-benefits/social-security/index_en.htm)

⁷ See European Commission/Eurostat, Public consultation – Assessment of the suitability of the International Public Sector Accounting Standards for the Member States, Summary of Responses, Luxembourg, 18 December 2012, p. 5.

⁸ See IPSASB, Projects: Revenue, <http://www.ipsasb.org/projects/revenue>.

⁹ 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. 110.

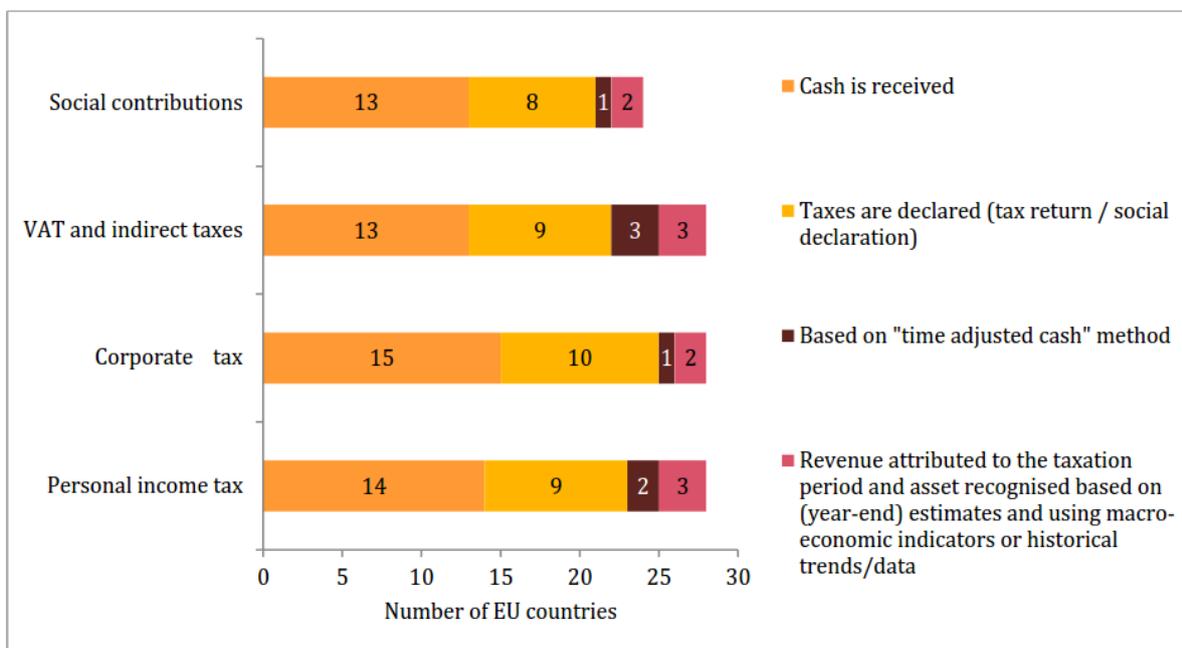


Figure 2: Timing of recognition of revenue from social contributions and taxes¹⁰

Against the background of these practical issues, it was recommended that the development of practical implementation guidance should be considered for the main sources of taxes (including social contributions) for EU Member States to ensure consistent application in similar circumstances.¹¹ The European Commission's report from 2013 concluded that "implementation [of EPSAS; added by authors] would be in steps over the medium term, focusing at first on the accounting issues where harmonisation is most important, such as revenue and expenditure (taxes and social benefits, liabilities and financial assets).

This issues paper is not dealing with taxes themselves, but only with these cases where social contributions should be treated in the same way as taxes. The last chapter of the issues papers discusses key parallels and differences between taxes and social contributions and their implications for public sector accounting.

¹⁰ See PwC, Collection of information [...], p. 110.

¹¹ See *ibid*, p. 130 and 138.

3. Most important categories of social contributions in the EU

The **European system of integrated social protection statistics (ESSPROS)** is a common framework by Eurostat and the European Union (EU) Member States providing a coherent comparison between European countries of social benefits to households and their financing. This system allows for making international comparisons of the administrative national data on social protection.

ESSPROS classifies receipts related to social protection benefits by **type** or by **origin**. The type gives the nature of, or the reason for a payment: social contributions¹², general government contributions, transfers from other schemes and other receipts. The origin specifies the institutional sector from which the payment is received i.e.

- ▶ all resident institutional units:
- ▶ corporations;
- ▶ general government;
- ▶ household sector;
- ▶ non-profit institutions serving households;
- ▶ rest of the world.

According to Eurostat's social protection statistics, besides tax revenues social contributions represent the main source of funding of social protection at EU-28 level.¹³ In 2013, **social contributions** accounted for 55.3 % of all social protection receipts at EU level while **general government contributions from taxes** accounted for 40.5 % of all receipts.¹⁴

At country level, the split of social protection funding for the year 2013 for the three countries included in this paper's country analysis is as follows:¹⁵

Country (2013 data)	Social contributions (%)	General government contributions from taxes (%)	Other receipts (%)
Czech Republic	70.3	28.3	1.4
France	61.9	34.7	3.4
Poland	64.1	16.4	19.5

Table 1: Split of social protection funding for the year 2013 for the three countries analysed¹⁶

Social contributions can be further broken down into contributions paid by the protected person (employees, self-employed person, retired person and others) and those paid by employers (including contributions paid by government where government acts as employer).

¹² The focus of this issues paper is on this category of social protection receipts by governments.

¹³ See Eurostat, Social protection statistics - main indicators, (http://ec.europa.eu/eurostat/statistics-explained/index.php/Social_protection_statistics_-_main_indicators).

¹⁴ See Eurostat, Social protection statistics - main indicators, Table 3 (http://ec.europa.eu/eurostat/statistics-explained/index.php/Social_protection_statistics_-_main_indicators).

¹⁵ See Eurostat, Social protection statistics - main indicators, Table 3 (http://ec.europa.eu/eurostat/statistics-explained/index.php/Social_protection_statistics_-_main_indicators).

¹⁶ The other receipts for Poland in 2014 is an outlier as there was a reform of the pension system in Poland and a part of mandatory pension contributions which originally had been transferred to the private sector pension funds was paid back by those funds to the public insurer. This means that in 2013 the system received a substantial (one-off) payment from the private sector. This was neither a contribution, nor taxes, so it was classified as "other receipts".

4. Approaches for classifying social contributions

4.1 ESA classification and definitions

Social contributions are defined in chapter 4 of ESA 2010 by reference to their role in social protection (or social insurance):¹⁷

“Social insurance schemes are schemes in which participants are obliged, or encouraged, by their employers or by general government, to take out insurance against certain eventualities or circumstances that may adversely affect their welfare or that of their dependants. In such schemes **social contributions** are paid by employees or others, or by employers on behalf of their employees, in order to secure entitlement to social insurance benefits, in the current or subsequent periods, for the employees or other contributors, their dependants or survivors.”

Social insurance schemes range from public schemes organised by government and covering the entire labour force of a country to private schemes run by a single employer for its employees. In the first case, i.e. for **social security schemes**, participation in the scheme is usually imposed by law. In practice, it works similarly to monthly tax prepayments as the social contributions are automatically deducted from employees' salaries and transferred by the employer to the social security institution responsible for the collection of the contributions. In the latter case, i.e. for **employment-related schemes**, participation may either be voluntary for the workers concerned or – more commonly – obligatory. For example, participation in such schemes may be required by the employer as part of the terms and conditions of employment collectively agreed between employers and their employees. These types of schemes are usually used by employers to build up complementary pension reserves and to provide health-related coverage (sickness insurance, accident insurance, hospitalization insurance, etc.) for their employees. Governments usually support the organisation of such schemes through tax reliefs and other financial incentives.

As will be shown in the description below, the classification of social contributions under ESA 2010 can be visualized as follows:

¹⁷ See Eurostat, European System of Accounts – ESA 2010, para. 4.88.

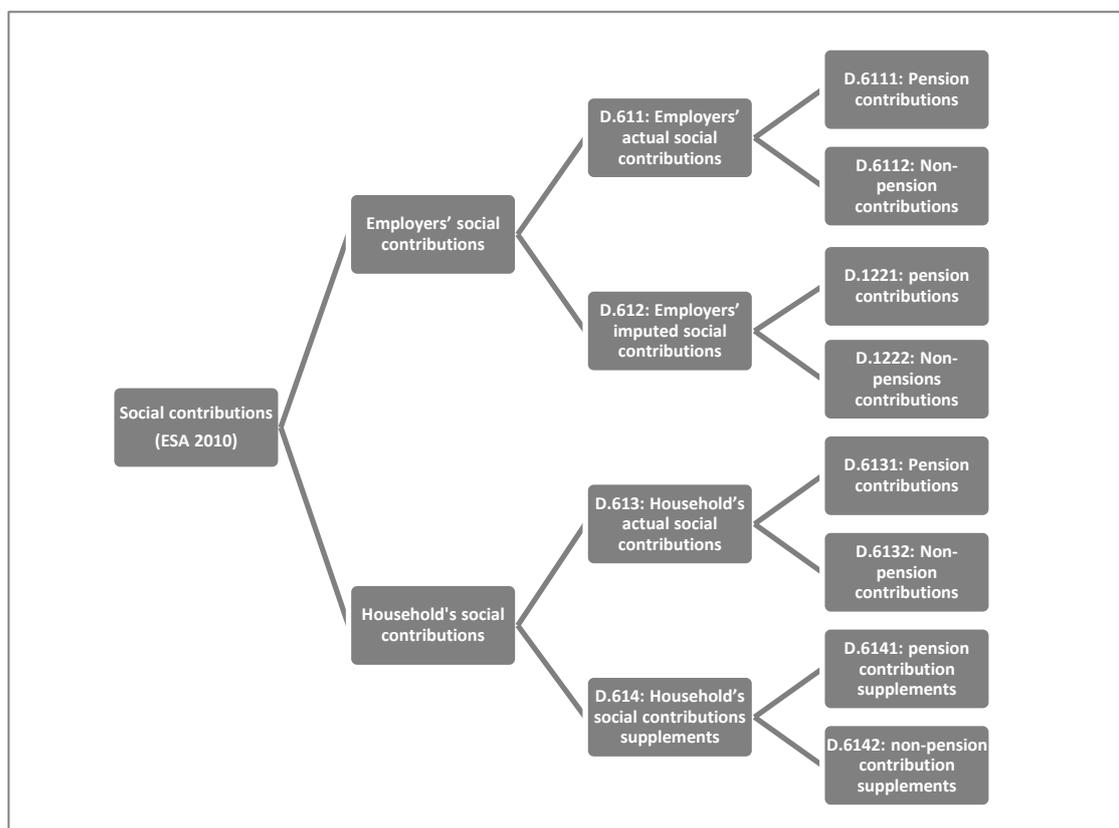


Figure 4: Classification of social contributions under ESA 2010

In the ESA 2010 classification system, social contributions are included within the category “social contributions and benefits (D.6)”, which is part of “Distributive transactions (D.)”. Figure 4 shows that the approach followed by ESA 2010 for classifying social contributions is in the first place based on the **source of the social contributions** (*is it contributed by an employer or is it contributed by a household?*). Accordingly, social contributions are classified according to the nature of the contributor into “Employer’s social contributions” on the one hand and “Household’s social contributions” on the other hand. **Employers’ social contributions** are social contributions payable by employers to social security schemes or other employment-related social insurance schemes to secure social benefits for their employees whereas **households’ social contributions** are paid on their own behalf by employees, self-employed or non-employed persons to social insurance schemes.

As far as employees are concerned, the recovery of employer’s and household’s social contributions is usually closely related in practice. For example, in Belgium, it works as follows:¹⁸ With each monthly salary, the employer withholds the amount of the employee’s own personal social contributions (13,07% of gross salary) from the employee’s salary. Then, at the end of each quarter, the employer transfers the thereby collected contributions to the National Social Security Office (NSSO), together with his own employer contributions (approximately 32% of the employee’s gross salary).

For accounting reasons, the ESA further subdivides employer’s and household’s social contributions into different subcategories. Both types of contributions are reviewed in more detail hereunder.

¹⁸ All information on the Belgium example was taken from the following website: <https://www.onssrszls.fgov.be/en>

Employers' social contributions

Employer's social contributions are part of compensation of employees (i.e. an amount equal to the value of the social contributions incurred by employers is recorded under compensation of employees) together with wages and salaries in cash and in kind.¹⁹

Employers' social contributions can be either actual or imputed:

- ▶ **Employers' actual social contributions** are paid by employers to social security schemes and other employment related social insurance schemes to secure social benefits for their employees. As employers' actual social contributions are made for the benefit of their employees, their value is recorded as one of the components of compensation of employees together with wages and salaries in cash and in kind.²⁰
- ▶ **Employers' imputed social contributions** represent the counterpart to social benefits (less eventual employees' social contributions) paid directly by employers (i.e. not linked to employers' actual contributions) to their employees or former employees and other eligible persons.²¹ Their value must be based on actuarial considerations, or on the basis of reasonable percentage of wages and salaries paid to current employees or as equal to unfunded non-pension benefits payable by the enterprise during the same accounting period.²²

For both categories, ESA distinguishes between pension related social contributions and non-pension related social contributions.

Household's social contributions

In the ESA system, household's social contributions are split into **actual** social contributions and social contributions **supplements**:

- ▶ **Household's actual social contributions** are social contributions payable on their own behalf by employees, self-employed or non-employed persons to social insurance schemes.²³
- ▶ **Household's social contributions supplements** consist of the property income earned during the accounting period on the stock of pension and non-pension entitlements. As this income is, in practice, retained by the (pension) funds, it is treated in the ESA system of accounts as investment income earned by households and immediately reinvested as social contributions supplements into the fund.²⁴

For both categories, ESA again distinguishes between pension related social contributions and non-pension related social contributions.

4.2 GFS classification and definitions

Unlike ESA where social contributions are defined only indirectly (i.e. by reference to their role in social protection), the GFSM provides a direct definition: "**social contributions** are actual or imputed revenue receivable by social insurance schemes to make provision for social insurance benefits payable"²⁵. They exclude contributions receivable under employment-related pension and other retirement schemes that create a liability for future benefits payable

¹⁹ Eurostat, European System of Accounts – ESA 2010, para. 4.08.

²⁰ Eurostat, European System of Accounts – ESA 2010, para. 4.92.

²¹ Refer to section 4.3 of this paper for additional information on imputed social contributions.

²² Eurostat, European System of Accounts – ESA 2010, para. 4.97.

²³ Eurostat, European System of Accounts – ESA 2010, para. 4.100.

²⁴ See Eurostat, European System of Accounts – ESA 2010, para. 4.101 for additional explanations.

²⁵ IMF, Government Finance Statistics Manual (GFSM) 2014, para. 5.94.

(i.e. exchange transactions are excluded). In fact, in GFS, only amounts that constitute revenue (thus excluding transactions that lead to a counterpart liability²⁶) are included in social contributions.²⁷

Under GFS, social contributions are on the one hand classified according to the nature of the scheme under which the contributions are paid and, on the other hand, divided according to the nature of the payee (the “contributor”). This categorisation is shown in the figure below:

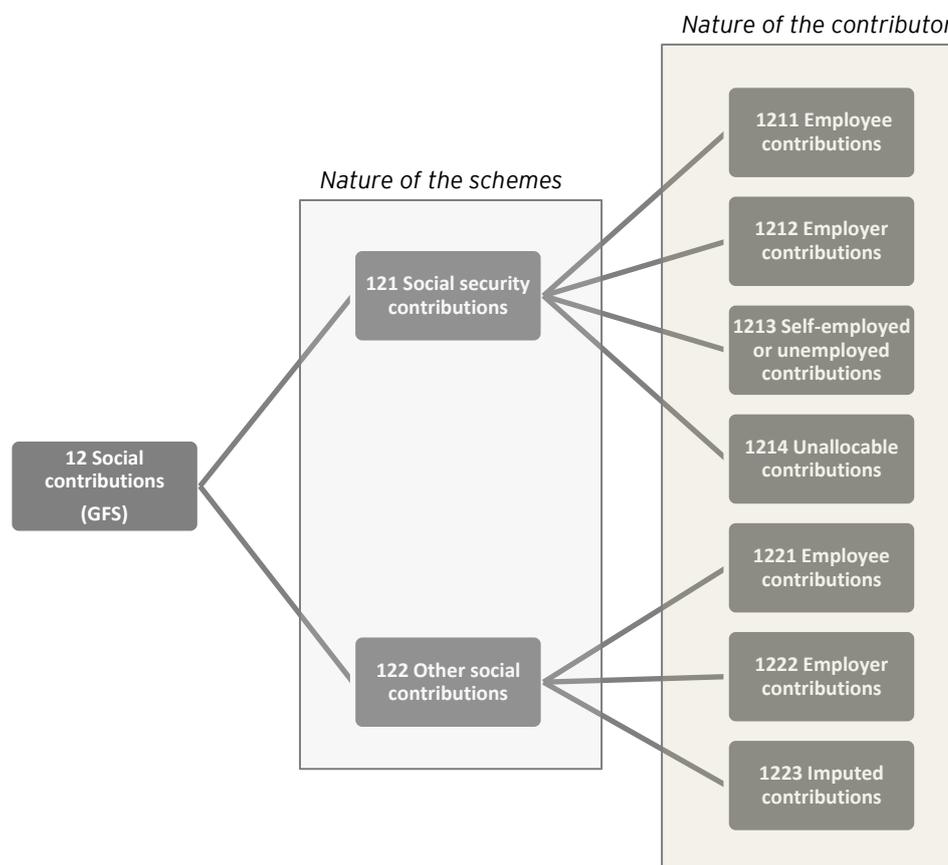


Figure 2: Overview of GFS classification of social contributions

Social security contributions

Social security contributions (121) are defined as being an actual revenue receivable by social security schemes organized and operated by government units, for the benefit of the contributors to the scheme.²⁸ As explained above, these contributions are classified by the source of the contribution:

- ▶ *Employee contributions (1211)*: are either payable directly by employees or deducted from employee’s wages and salaries and transferred on their behalf by the employer;
- ▶ *Employer contributions (1212)*: are payable directly by employers on behalf of their employees;
- ▶ *Self-employed or unemployed contributions (1213)*: are paid by contributors who are not employees;

²⁶ An example of where contributions received by government lead to a counterpart liability and are therefore not recognized as revenue is where government has set up a pension fund to which employees can contribute in order to build up a pension reserve for the future. Contributions paid to the fund are recorded in GFS as incurrence of government liabilities for future pension benefits. They are therefore not considered social contributions under GFS.

²⁷ IMF, GFSM 2014, para. 5.95.

²⁸ IMF, GFSM 2014, para. 5.97.

- ▶ *Unallocable contributions (1214)*: refers to contributions whose source cannot be determined.

Other social contributions

Other social contributions (122) are defined as actual and imputed contributions receivable by social insurance schemes operated by employers (including government where government acts as employer) on behalf of their employees. Unlike social security schemes, social insurance schemes tie the level of benefits directly to the level of contributions.²⁹ Similarly to contributions received under social security, other social contributions are also classified by the source of the contribution, which can be both employees and employers:

- ▶ *Employee contributions (1221)*: definition is the same as for social security contributions above;
- ▶ *Employer contributions (1222)*: definition is the same as for social security contributions above;
- ▶ *Imputed contributions (1223)*: are revenue that arises when government employers provide non-pension benefits directly to their employees, former employees, or dependents out of their own resources without involving an insurance enterprise and without creating a special fund or segregated reserve for the purpose. These benefits can be current period benefits or, instead, payable in the future. Under this situation, existing employees are considered as being protected against various specified needs or circumstances, even though no reserves are built up to provide for future entitlements. In order to reflect this situation in the accounts, the GFS imputes (to be understood as “records”) two “fictitious” transactions: The first, *Compensation of employees*, is recorded as a transaction from government to the household sector³⁰ for an amount representing the level of contributions that the government would have to put aside with an insurance enterprise in order to secure the (future) benefits for its employees. Given that the first transaction is recorded as flowing from government to the household sector, a second simultaneous transaction, *imputed social contributions (1223)*, must be recorded for the same amount in order to reflect the social contributions that would have to be paid by the employees in order to secure the (future) benefits.³¹

4.3 Classification by type of scheme

Finally, in principle, social contributions can be divided into social contributions to funded social security schemes and social contributions to unfunded social security schemes.

In an unfunded social security scheme, no assets are reserved for providing future social benefits. In such a scheme, current contributions are used to finance the current payments for social benefits. Therefore, unfunded social security schemes are also often titled as “pay-as-you-go schemes”. In a funded social security scheme, contributions are reserved to finance future social benefits.

However, it has to be noted that also hybrid forms of these two extremes are possible.

²⁹ See IMF, GFSM 2014, para. 5.98.

³⁰ The household sector being the receiver of the imputed “compensation of employees”

³¹ See IMF, GFSM 2014, para. 5.100.

5. Difficulties when accounting for social contributions under the accrual principle

In this chapter, it is assessed for the main categories of social contributions which problematic points/issues with regards to recognition and measurement arise.

Under the **accrual basis of accounting**, transactions and other events are recognized in financial statements when they occur (and not only when cash or its equivalent is received or paid). Therefore, the transactions and events are recorded in the accounting records and recognized in the financial statements of the period to which they relate. A receivable resulting from social contributions would need to be recognized in the period in which the legal claim against a contributor arises. In the case of social contributions the legal claim for the levying of social contributions is typically the earning of income by the contributor to a scheme/by the taxpayer.

In Europe, the levying of social contributions is generally integrated in the levying of income taxes. Contributions for social security schemes are directly deducted based on a certain percentage from employees' wages. Unlike revenues from taxes³², the amount of social contributions paid or due by employees is in most Member States already known at year-end.³³

In the following difficulties and problems when accounting for social contributions under the accrual principle are discussed. Figure 5 provides an overview of the difficulties identified.

- | |
|---|
| <ul style="list-style-type: none">a) Problems with defining the scope for the accounting for social contributionsb) Difficulties in the recognition of social contributions (especially when there is a time lag between the underlying event for the social contributions and the point in time when the final amount of social contributions due is determined)c) Measurement of social contributions<ul style="list-style-type: none">c.1) Initial measurementc.2) Subsequent measurementd) Difficulties relating to fully funded insurance schemese) Difficulties related to the reporting entities in the case of social contributions. |
|---|

Figure 5: Overview of difficulties when accounting for social contributions under the accrual principle

These difficulties will now be discussed in more detail:

a) Defining the scope of social contributions

A problematic area in terms of accounting for social contributions could be that there is a grey zone where the differentiation between social contributions and taxes is blurred. Member States might levy taxes which follow the logic of taxation but are earmarked and meant to finance social security. The difficulties to make a clear distinction between social contributions and taxes implies that the scope of accounting for social contributions could remain unclear. However, in case that the same accounting

³² In the case of taxes it has to be considered that the taxable income (e.g. in the case of income taxes) it has to be considered that the taxable income is only determined after year-end as tax payers are allowed to deduct certain expenses from their income.

³³ One exception to this are the Netherlands. In the Netherlands a combined premium consisting of taxes and social contribution is levied. Taxes and social contributions are artificially divided at year end and it is only known in February of the following year what revenues from social contributions have been earned.

guidance would apply to social contributions and to taxes, the differentiation between social contributions and taxes might not be relevant for accounting purposes.

b) Recognition of social contributions

Difficulties in the recognition of social contributions may arise when there is a time lag between the period in which the legal claim for the social contributions arises and the point in time when the final amount of social contributions due is determined. This is for example the case for the social contributions by self-employed persons for which the liability to pay the contributions can only be determined in a later accounting period. Generally, it can be assumed that before the point in time when the financial statements are prepared, reporting entities should be able to determine the amount due and payable for social contributions. When self-employed persons file their income tax declarations before the preparation date of the financial statements, then these social contributions can be accounted for appropriately. Difficulties might only arise when the amount due and payable can only be determined after the preparation date of the financial statements (e.g. when the determination of the amount due and payable for social contributions is depending on a tax declaration or a social declaration of the contributor). A similar problem with regards to the aforementioned time lag arises when ad hoc bonuses or other exceptional payments, 13th month, etc. are paid by the employer to the employees and social contributions are levied only at a later point in time (e.g. only when taxes are declared). Therefore, there could be a mismatch between the period when the bonuses or other exceptional payments were earned and when they were levied.

c) Measurement of social contributions

Difficulties in terms of measurement of social contributions might arise in the following instances:

- ▶ 1. Initial measurement: When there is a time lag between the period in which the legal claim for the social contributions arises and the point in time when the final amount of social contributions due is determined, problems to determine the basis of assessment for the social contributions arise. As outlined before this could be the case for the social contributions levied from self-employed persons.
- ▶ 2. Subsequent Measurement: There can be problems with regards to the collectability of social contributions and the respective value of the receivables would have to be adjusted. This could be the case when a company goes bankrupt. In such a case it might remain unclear for a substantial period of time what portion of social contributions the company will be able to pay. This is also the case when self-employed contributors are unable to pay the contributions (e.g. by personal insolvency). The question is how the reporting entity gets hold of those information.

d) Fully funded insurance schemes

Where social security is organised as a fully funded (i.e. capital-based) insurance scheme, contributions to those schemes could also be accounted for using insurance accounting. However, it has to be noted that a fully funded insurance scheme is a very rare case in the European Union.³⁴ The insurance approach considers that some social security schemes are similar in practice to insurance contracts. This approach recognizes a present obligation to pay benefits at the point that coverage begins and symmetrically recognizes a right to future receipts resulting from the provision of that coverage. As outlined in the issues paper on social benefits the insurance approach is only suitable for fully funded contributory schemes. Complex issues may also arise under the insurance approach in respect of:

- ▶ Fully funded schemes and the accounting treatment of the difference between the calculated obligation to provide insurance services based on

³⁴ The IPSASB found one definite case so far worldwide (New Zealand).

- ▶ an individual risk assessment and the calculated claim for all insurance premiums based on actuarial assumptions;
- ▶ partially subsidized schemes and significant changes to the terms of schemes.

e) Reporting entities in the case of social contributions

In many cases the accounting for revenues from social contributions in Europe is done by the respective social security funds. The 2012 EY study has shown that the applicable accounting frameworks for social security funds can vary from Member State to Member State.³⁵ In some Member States, the social security funds are part of the central government and are subject to the same accounting regulations. Then there are Member States where social security funds are not part of central government and separate accounting rules apply to them. It can even be the case, that some social security funds still apply cash accounting. In Germany for example, public health insurance providers follow business accounting rules adapted to the specificities of the health insurance sector, whereas there are private health insurance providers applying IFRS. In addition, contributions to the public pension system in Germany are collected by the public health insurance system. A proposal for an accounting treatment of social contributions therefore need to take these interdependencies into account.

It has to be noted that difficulties cannot be generalized as they arise or not arise depending on country specifics in terms of levying and paying social contributions..

³⁵ See Ernst & Young, Overview and comparison of public accounting and auditing practices in the 27 EU Member States, 19 December 2012.

6. Description of accounting guidance available

6.1 International accounting frameworks

The following sections analyse the guidance on social contributions that is contained in the international accounting frameworks.

6.1.1 International Public Sector Accounting Standards (IPSAS)

6.1.1.1 Relevant accounting guidance under IPSAS

Currently there is no standard on “social contributions” in the IPSASB’s literature. Social contributions can generally be classified as non-exchange transactions and would therefore fall in the scope of IPSAS 23. However, IPSAS 23 only provides specific guidance on taxes but not on social contributions.

According to BC26 of IPSAS 23, compulsory contributions to social security schemes that are non-exchange transactions are not excluded from the scope of the standard. However, IPSAS 23, Revenue from non-exchange transactions (taxes and transfers) also states that determining whether or not compulsory social contributions give rise to exchange or non-exchange transactions depends on the particular arrangements of a given scheme and requires professional judgement. Consequently, either IPSAS 23 applies to social contributions or “principles established in international or national standards addressing such schemes.”³⁶ Therefore, it depends on the characteristics of a social contributions scheme whether IPSAS 23 applies or not.

Based on BC26 of IPSAS 23 it can also be concluded that IPSAS currently do not provide guidance for non-compulsory contributions to social security.

In the following two sub-chapters, the IPSAS accounting guidance regarding the recognition and measurement of compulsory social contributions will be described and it will then be assessed whether the problematic points/issues with regards to recognition and measurement of social contributions are satisfactorily treated in IPSAS.

6.1.1.2 Recognition

IPSAS 23 does not specify whether the general recognition criteria for non-exchange revenue of IPSAS 23.44 ff. or the specific recognition criteria for taxes of IPSAS 23.59 ff. should be applied. Therefore, both possibilities will be assessed in the following paragraphs.

According to the general recognition criteria of IPSAS 23.44 an inflow of resources from a non-exchange transaction recognized as an asset shall be recognized as revenue, except to the extent that a liability is also recognized in respect of the same inflow. Social contributions are transferred to the government with the expectation and/or understanding that they will be used in a particular way and that the government will use these resources accordingly. In the case of compulsory social contributions it can therefore be concluded that there are “stipulations” governing the transfer of such resources.³⁷ In terms of stipulations, IPSAS 23 then differs between restrictions and conditions. Whereas restrictions may require an entity on initial recognition to use the future economic benefits or service potential embodied in the asset for

³⁶ See BC26 of IPSAS 23.

³⁷ See IPSAS 23.14.

a particular purpose (performance obligation), conditions require that future economic benefits or service potential be returned to the transferor in the event that the stipulation is breached (return obligation).³⁸ In the case of compulsory social contributions it can probably be assumed that no conditions are attached to the transfer of resources. Therefore, revenue from compulsory social contributions need to be recognized when the entity accounts for the asset (see IPSAS 23.44 ff.). This corresponds to the point in time when the compulsory social contributions become due and payable. Only cases where conditions were attached to social contributions, revenue would only be recognized to the extent that a liability is not also recognized (see IPSAS 23.44 ff.).

According to the IPSASB's Conceptual Framework an asset is defined as: "A resource presently controlled by the entity as a result of a past event."³⁹ Unlike for taxes, there is currently no guidance under IPSAS for the requirement of a "past event" as a precondition for the revenue recognition of social contributions. As outlined before, earning of income by the contributor to a scheme/taxpayer could probably be defined as the past event; however, there might be deviations depending on a country's social security regulations. The identification of the past event for certain categories of social contributions is therefore one crucial part for the recognition of revenue.

When applying the principles for tax accounting for compulsory social contributions, IPSAS 23.59 specifies that an asset should be recognized in respect of taxes when (a) the taxable event occurs and (b) when the asset recognition criteria are met. By analogy, for social contributions this would mean that revenues from social contributions should be recognized when (a) the past event occurs and (b) when the asset recognition criteria are met. Given the fact that for compulsory social contributions usually no conditions are attached to the transfer of resources, the outcome for the accounting of compulsory social contributions using the tax recognition criteria is the same than when applying the general recognition criteria for non-exchange transactions.

To sum up, resources arising from social contributions satisfy the definition of an asset when the entity controls the resources as a result of a past event and expects to receive future economic benefits or service potential from those resources. As a consequence, "revenue" from social contributions cannot be recognized according to IPSAS 23 until the past event has taken place (e.g. earning of income by the contributor).

6.1.1.3 Measurement

In line with the recognition of non-exchange revenue, IPSAS 23 links the measurement of the revenue to the respective asset, i.e. the cash received or the receivable relating to the non-exchange transaction. According to IPSAS 23.42 "an asset acquired through a non-exchange transaction shall initially be measured at its fair value as at the date of acquisition".

For the case that the same approach as for taxes would be applied, compulsory social contributions would be measured at the best estimate of the inflow of resources to the entity. Therefore, where there is a separation between the timing of the past event for the compulsory social contributions and their collection, an entity might apply statistical models based on the history of collecting the particular social contribution in prior periods for measurement purposes.⁴⁰

³⁸ See IPSAS 23.15.

³⁹ See IPSASB Conceptual Framework, para. 5.6.

⁴⁰ See the Issues Paper "Accounting treatment of taxes with a view to financial reporting requirements under the future European Public Sector Reporting Standards (EPSAS)" from 28 October 2016 for more details.

6.1.1.4 Are the problematic points/issues with regards to recognition and measurement of social contributions satisfactorily treated in IPSAS?

The following table provides an assessment whether the problematic points/issues with regards to recognition and measurement of social contributions are satisfactorily treated in IPSAS:

<p>a) Problems with defining the scope for the accounting of social contributions</p>	<p>IPSAS 23 does currently not provide guidance on the differentiation between social contributions and taxes. As outlined before, this might not be a problem when the same accounting principles apply to both taxes and social contributions.</p>
<p>b) Difficulties in the recognition of social contributions (especially when there is a time lag between the underlying event for the social contributions and the point in time when the final amount of social contributions due is determined)</p>	<p>When there is such a time lag for social contributions then the specific guidance for taxes in IPSAS 23 provides guidance. However, if applied to social contributions, IPSAS 23 does for example not specify how such statistical models can/shall look like in order to achieve a reliable measurement and therefore be able to recognize the social contributions.</p>
<p>c) Measurement of social contributions</p>	<p>IPSAS 23 does provide some guidance on the measurement of non-exchange transactions. Using the “best estimate of the inflow of resources to the entity” seems also appropriate for compulsory social contributions.</p> <p>As outlined before, IPSAS 23 does not specify how statistical models for the measurement of social contributions should be set up (e.g. which parameter would need to be considered in the model).</p> <p>It has to be noted that IPSAS 23 does not provide guidance on the measurement of non-compulsory social contributions.</p>
<p>d) Accounting for social contributions that are dedicated to fully funded social security schemes and accounting for social contributions that are dedicated to partially subsidized schemes</p>	<p>The current suite of IPSAS does not provide guidance on accounting for social contributions that are dedicated to fully funded social security schemes and accounting for social contributions that are dedicated to partially subsidized schemes. The IPSASB is currently working on an Exposure Draft for the accounting of social benefits and will provide clarity on accounting for such contributions under an insurance approach.</p>

e) Difficulties related to the <u>reporting entities in the case of social contributions</u>	Due to the fact that these issues mainly relate to jurisdictional specifics (e.g. that social security funds still apply the cash basis of accounting or business accounting principles) IPSAS 23 does not specifically address these issues. However, the IPSAS on “The Applicability of IPSASs” from 2016 provides characteristics of public sector entities for which IPSASs are designed.
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6.1.2 European Union Accounting Rules (EAR)

Revenue from non-exchange transactions is treated under *EAR 17 – Revenue from non-exchange transactions (taxes and transfers)* which is based on IPSAS 23. As in IPSAS 23, social contributions are currently not explicitly covered in EAR 17. Therefore, accounting for compulsory social contributions under EAR 17 will lead to the same results than under IPSAS 23.

6.1.3 International Financial Reporting Standards (IFRS)

Accounting for “revenues” from social contributions is unique to the public sector. Therefore, there is no IFRS dealing with the accounting for revenues from social contributions. Also in terms of expenses related to social contributions there is no specific IFRS that applies to that. Therefore, the general IFRS accounting principles apply.

6.1.4 ESA 2010

As shown in section 4.1 on ESA classifications, social contributions collected by government fall under four main categories under ESA:

- ▶ Employers' actual social contributions (recorded under D.611);
- ▶ Employers' imputed social contributions (recorded under D.612);
- ▶ Household's actual social contributions (recorded under D.613); and
- ▶ Household's social contributions supplements (recorded under D.614).

The following subsections review the accounting treatment (recognition and measurement) of each of these categories under ESA.

6.1.4.1 Employer's actual social contributions (D.611)

i. Recognition

According to ESA 4.94, employers' actual social contributions are recorded at the time when the work that gives rise to the liability to pay the contributions is carried out. For example, if contributions are levied based on salary, the time of recording will be when the salary is earned by the employee.

ii. Measurement

Depending on the information sources available to the social security institutions, the ESA foresees two different methods to determine the amounts of social contributions to record as government revenue: The amounts of social contributions to record as government revenue can derived from two sources:

- ▶ **Social declaration method;** or
- ▶ **Time-adjusted cash method..**

The **social declaration method** prescribes to measure revenue based on the amounts evidenced by these assessments and declarations. The amounts to record shall be adjusted by a coefficient in order to take into account amounts that, even though assessed and declared, are unlikely to be ever collected. This coefficient is supposed to be specific to the type of social contribution under consideration and shall be estimated on the basis of past experience and current expectations in respect of assessed and declared amounts never collected⁴¹.

The **time-adjusted cash method** prescribes to measure revenue based on amounts evidenced by cash receipts. These cash receipts shall in principle be time-adjusted⁴² so that the cash is attributed to when the activity took place to generate the obligation to pay social contributions. According to ESA 20.174, the time-adjusted cash method is considered an acceptable proxy for accruals, especially when there are no reliable assessments available or amounts unlikely to be collected cannot be reliably estimated.

6.2 Employer's imputed social contributions (D.612)

i. Recognition

With regard to recognition and measurement, two types of employer's imputed social contributions can be distinguished:

- ▶ *Contributions which represent the counterpart of compulsory direct social benefits;*
- ▶ *Contributions which represent the counterpart of voluntary direct social benefits.*

Contributions of the first type are recorded in the period during which the work is done whereas contributions of the latter type are recorded at the time the benefits are provided.⁴³

ii. Measurement

Contributions of the first type are measured either based on actuarial assumptions or on the basis of a reasonable percentage of wages and salaries of current employees in the period during which the work is done. Contributions of the second type are measured at the value of the unfunded non-pension benefits payable by the enterprise during the same accounting period.⁴⁴

6.2.1.1 Households' actual social contributions (D.613)

i. Recognition

Households' actual social contributions are recorded on an accrual basis. For the employed, this moment of recognition is at the time the work that gives rise to the liability to pay the contributions is carried out. For the non-employed, the moment of recognition is at the time the contributions are to be made.⁴⁵

ii. Measurement

The measurement of household's actual social contributions is consistent with the one of employer's actual social contributions above (i.e. social declaration and/or time-adjusted cash method).

⁴¹ See ESA 2010, para. 4.95.

⁴² According to ESA 2010, para 4.150 (b), this adjustment is based on the average time difference between the activity and the cash receipt.

⁴³ See ESA 2010, para. 4.98.

⁴⁴ See ESA 2010, para. 4.97.

⁴⁵ See ESA 2010, para. 4.100.

6.2.1.2 Households' social contribution supplements (D.614)

As explained in section 4.1, household's social contribution supplements consist of the property income earned during the accounting period on the stock of pension and non-pension entitlements. As this income is, in practice, retained by the (pension) funds, it is treated in the ESA system as investment income earned by households and immediately reinvested as social contributions supplements into the fund. These social contributions are recorded when they accrue and measured at the value of the reinvested investment income.

6.2.1.3 Summary

The following table summarizes the findings of this section with regard to the accounting treatment of social contributions under ESA 2010:

Category	Recognition	Measurement
D.611 Employer's actual social contributions	When the work that gives rise to the liability to pay the contributions is carried out	Two methods: ▶ Social declaration method ▶ Time-adjusted cash method
D.612 Employer's imputed social contributions: ▶ <i>Contributions which represent the counterpart of compulsory direct social benefits</i> ▶ <i>Contributions which represent the counterpart of voluntary direct social benefits</i>	▶ During the period in which the work is done; ▶ When the benefits are provided.	▶ Actuarial measurement or based on a reasonable percentage of wages and salaries ▶ At the value of the benefits provided
D.613 Households' actual social contributions: ▶ <i>Employed</i> ▶ <i>Unemployed</i>	▶ When the work that gives rise to the liability to pay the contributions is carried out ▶ When the contributions are to be made	▶ Social declaration method or time-adjusted cash method ▶ Idem above
D.614 Households' social contribution supplements	When they accrue	At the value of the accrued investment income

7. Country analysis

7.1 Selection of countries

The following sections provide an overview on how selected Member States are accounting for social contributions. The selection was based on the following considerations:

- ▶ **Czech Republic:** The Czech Republic adopted the accrual basis of accounting on 1 January 2010.
- ▶ **France:** France applies accrual accounting since 2006 and there are similarities between the IPSAS accounting framework and the French Central Government Accounting Standards.
- ▶ **Poland:** Poland has not been included in one of the issues paper so far. Poland is a younger member of the European Union and became a full member on 1 May 2004.

The focus of this analysis is to identify how the selected Member States account for social contributions.

7.2 Methodology

To get an overview of Member States' approaches to accounting for social contributions, EY used a questionnaire that was answered by Member States in writing. Respondents to the questionnaire were government representatives from the Ministry of Finance/standard setter. The following questions were asked in the questionnaire:

1. What public services are financed by social contributions in your country?
2. How are social contributions levied (e.g. via the tax collection system)?
3. How are social contributions accounted for in public sector accounts in your country?
4. Can you please explain the mechanism how and the basis on which social contributions are calculated in your country (e.g. using a certain percentage of wages/salaries)?
5. At what point in time is the level of social contributions determined (e.g. annually before the fiscal year begins/quarterly/monthly...)?
6. Are there any social contributions in your country that are determined only after the end of the fiscal year, i.e. similar to income taxes that are assessed only when the tax payer has issued a tax declaration?

In the following table we provide an overview of the responses from the selected Member States:

Questions	Czech Republic	France	Poland
<p>1. What public services are financed by social contributions in your country?</p>	<p>Public services as pensions, mandatory illness insurance and unemployment allowance are financed mostly from social contributions. There are some more resources but with a small share on a total budget for social services. This can be explained by the fact that from time to time, additional resources to finance pensions are necessary. These resources are used from the current state budget or from revenues from state property privatisation (especially in the past years).</p>	<p>The social security sector (old-age, health, family, job-related injury or illness), additional compulsory old-age cover mechanisms and unemployment cover mechanisms are mainly financed by social contributions, though additional transfers from general taxes may be needed to match expected expenses.</p>	<p>The social security system in Poland is composed of:</p> <ul style="list-style-type: none"> ▶ social insurance and welfare system, ▶ health insurance system, ▶ benefits in respect of unemployment, ▶ family benefits. <p>Social security tasks are exercised by many institutions, including:</p> <ul style="list-style-type: none"> ▶ Social Insurance Institution – cash benefits and benefits in kind provided from the social insurance under the pension prevention, ▶ Agricultural Social Insurance Institution– money and material benefits in the form of benefit payments made within the framework of benefit prevention from farmer’s social insurance, ▶ Ministry of Family, Labour and Social Policy – benefits in respect of unemployment, family benefits and social benefits (from social assistance) delivered via local authorities, ▶ National Health Fund – benefits in kind from health insurance. <p>Additionally, there are imputed social contributions which refer to non-contribution schemes (for non-capital social security pension scheme) in relation to the specific groups of government employees: police officers, military officers, officers of Government Protection Bureau, Border Guard officers, Special Forces, Prison Guard officers, firemen, prosecutors and judges.</p>

Questions	Czech Republic	France	Poland
			Public servants (as well as teachers and doctors) in Poland have no special, non-contribution schemes. They are included in general insurance and pension scheme.
2. How are social contributions levied (e.g. via the tax collection system)?	Currently the tax collection system is the only way to levy social contributions (exceptions are very rare). As outlined before, the only exception was when pensions were financed by the current state budget or from revenues from state property privatisation	<p>In France there are mainly 4 sources of revenues for the social security sector.</p> <ol style="list-style-type: none"> 1. <i>Social security contributions ("cotisations") which accounted for around 60% of the revenue in 2012:</i> They apply to employees and are computed based on all amounts given by an entity in exchange for service rendered by employees (wages, paid annual leave, performance related bonuses, non-monetary benefits, tips). Those social security contributions are paid by the employer (expense of the employer) and the employee every month. 2. <i>Specific contributions (CSG : "contribution sociale généralisée")</i> represents around 20% of revenue (2012): It applies to all revenues of a household/an individual (wages, gains on investments, etc.). It finances mainly health care, family care, and an old-age fund (set up for social assistance purposes) 3. <i>General taxation</i> represents around 13% of revenue (non-contributory; in 2012): It is made up of various taxes such as: taxes on company cars, VAT on tobacco, taxes on pharmaceutical products, etc. 4. <i>Transfers account for around 6% of revenue (non-contributory, in 2012):</i> Amounts transferred come principally from the Central government and from other social security schemes. 	<p>Social contribution payers are obliged to calculate and deduct due social contributions from an income of the insured for each single month.</p> <p>Social contribution payers are required to present final settlements and pay the contribution no later than till:</p> <ul style="list-style-type: none"> ▶ the 5th day of the following month - budgetary units, ▶ the 10th day of the following month - individuals who pay contributions only for themselves (e.g. self-employed entrepreneurs) ▶ the 15th day of the following month - all the other payers

Questions	Czech Republic	France	Poland
<p>3. How are social contributions accounted for in public sector accounts in your country?</p>	<p>Similar to tax collection revenues – accrual based.</p>	<p>Social security contributions are collected by regional entities (URSSAF) that are part of a national network for the collection of contributions. They are then transferred to an entity (ACOSS) whose role is to centralise those amounts before they are distributed to the various social security sector entities that provide social benefits to end beneficiaries.</p> <p><u>Recognition:</u> An entity recognises revenue at the point in time when the transaction gives rise to a right for that entity. Such a point in time may happen upon the payment of the contributors' salaries or upon the occurrence of a transaction that provides revenue to the contributors (e.g. the proceeds from the sale of financial assets). In some cases, for instance for self-employed contributors, contributions are levied through a tax assessment filed in N+1 for year N based on revenues for year N-1.</p> <p><u>Measurement:</u> Measurement upon initial recognition is at face value. Subsequent measurement is at face value for the gross carrying amount. The net carrying amount would take into account uncollectible contributions through impairment.</p>	<ul style="list-style-type: none"> ▶ The actual social contributions are received by and presented in the following funds: <ul style="list-style-type: none"> ▶ Social Security Fund (FUS) ▶ Bridge Pension Fund (FEP) ▶ Demographic Reserve Fund (FRD) ▶ Labour Fund (FP) ▶ National Health Fund (NFZ) ▶ Guaranteed Employment Benefit Fund (FGŚP) ▶ As for FUS, FEP, FRD and FGŚP: <ul style="list-style-type: none"> ▶ Social contribution are recorded on an accrual basis and then adjusted by the average non-collection coefficient which is calculated as: $100\% - \text{cash receipts} / (\text{amounts from assessments and declarations} - \text{law cancellations}) * 100\%$ ▶ As for FP and NFZ: <ul style="list-style-type: none"> ▶ Social contribution are recorded on an accrual basis (time adjustment method for cash receipts). ▶ Amounts of contribution law cancellations are recorded as capital transfers. <p>As contributions for self-employed entrepreneurs are levied via the same general systems, they are accounted in the same way as the other social contributions.</p>
<p>4. Can you please explain the mechanism how and the basis on which social contributions</p>	<p>Percentage of wages/salaries (employees) and calculation basis (similar to tax base) for entrepreneurs. The tax base is used to calculate self-employed entrepreneurs'</p>	<p><i>1. Social security contributions:</i> Social security contribution rates are set up in the financing law on an annual basis.</p>	<ul style="list-style-type: none"> ▶ Retirement pension - contributions in general 19,52 % including: <ul style="list-style-type: none"> • Insurance payer: 9,76 %

Questions	Czech Republic	France	Poland
<p>are calculated in your country (e.g. using a certain percentage of wages/salaries)?</p>	<p>contributions. Some of their contributions are voluntary to them. However, if they decide not to pay them, they won't receive the full scope of possible social aid.</p>	<p>Rates apply either in full to the whole remuneration for social benefits such as health care, maternity leave, children benefits and job-related injury, or they are differentiated based on the level of earning for instance for old-age benefits. 2. <i>Specific contribution – CSG</i> Various rates are set up annually by law and apply to the various sources of revenues that fall in the scope. Please see https://www.compta-online.com/les-taux-de-cotisations-sociales-au-1er-janvier-2017-ao2149 The table there shows the various contributions, the entity they are paid to, on what basis they are computed and the applicable rates for employers and for employees.</p>	<ul style="list-style-type: none"> • Insured party: 9,76 % ▶ Other pensions – contributions in general 8 % including: <ul style="list-style-type: none"> • Insurance payer 6,50 % • Insured party 1,50 % ▶ Sickness – contributions in general 2,45 % ▶ Accident – contributions in 0,40-3,60%⁴⁶ ; 1,80%⁴⁷ <ul style="list-style-type: none"> • Insurance payer % 0,40-3,60%; 1,80% ▶ The rate of contribution for social insurance charged by <ul style="list-style-type: none"> • National Health Care (NFZ) - Insured party 9 % and • Labour Fund (FP) - Insurance payer 2,45 %. ▶ Support for employees of insolvent companies charged by Guaranteed Employment Benefit Fund - 0,1 % ▶ The amount of social contributions in central government is corrected for amounts of imputed social contribution for Ministry of Defence, Ministry of the Interior and Ministry of Justice.
<p>5. At what point in time is the level of social contributions determined (e.g. annually</p>	<p>Monthly (employees) and annually (entrepreneurs). The annual determination of social contributions for self-employed entrepreneurs is</p>	<p>The finance law specific to the social security sector (Loi de Financement de la Sécurité Sociale) is voted on an annual basis before the start of the fiscal year. Contributions are due and paid on a</p>	<p>Social contribution payers are obliged to calculate and deduct due social contributions from an income of the insured for each single month.</p>

⁴⁶ The contribution for groups of activity, once differentiated, has been in force since 1 April 2015. In the case of insurance payers for whom the rate of percentage contribution for accident insurance is established by ZUS, the rate determined for their activity group is additionally multiplied by a levelling indicator in the range of 0.5 to 1.5.

⁴⁷ The contribution for insurance payers applying for accident insurance for an average month for not more than 9 insured parties as well as for insurance payers not subject to REGON registration – this contribution is in force from 1 April 2015.

Questions	Czech Republic	France	Poland
<p>before the fiscal year begins/quarterly/monthly...)?</p>	<p>based on their tax declaration and financial statements.</p>	<p>monthly basis or upon occurrence of a taxable/contributory event (gain on investment realised). For self-employed entrepreneurs, contributions are levied through a tax assessment filed in N+1 for year N based on revenues for year N-1.</p>	<p>Social contribution payers are required to present final settlements and pay the contribution no later than till:</p> <ul style="list-style-type: none"> ▶ the 5th day of the following month - budgetary units, ▶ the 10th day of the following month - individuals who pay contributions only for themselves, ▶ the 15th day of the following month - all the other payers. <p>Persons that are self-employed are treated by the system as a “social contribution payer”. This means that they pay contributions in the same way as companies. The difference is that they pay for just 1 employee (for themselves), and that they may choose to pay higher contribution than the minimum amount, if they want to receive higher benefits (for example the sick benefit).</p>
<p>6. Are there any social contributions in your country that are determined only after the end of the fiscal year, i.e. similar to income taxes that are assessed only when the tax payer has issued a tax declaration?</p>	<p>None, with the exception of social contributions for self-employed entrepreneurs.</p>	<p>Not that the respondent knew of, , with the exception of social contributions for self-employed entrepreneurs..</p>	<p>As contributions for self-employed entrepreneurs are levied via the same general systems, there are no social contributions that are determined only after the end of the fiscal year.</p>

7.3 Summary of country analysis

The social benefits that are financed by social contributions in all selected Member States are very similar. Social contributions mainly cover pensions, health insurance, unemployment benefits. In France, there are also taxes levied to finance social benefits.

Social contributions are based on the wages/salaries of employees and collected through the tax collection system or specific entities that collect the social contributions. For employees, social contributions are typically deducted on a monthly basis from the salaries/wages or in France also upon occurrence of a taxable/contributory event (gain on investment realised). In the Czech Republic, for entrepreneurs taxes are levied on an annual basis.

In terms of accounting for social benefits, all countries analysed apply the accrual principle. Czech Republic states that it generally applies the accrual principle for social contributions whereas France specifies that an entity recognises revenue at the point in time when the transaction gives rise to a right for that entity. Such a point in time may happen upon the payment of the contributors' salaries or upon the occurrence of a transaction that provides revenue to the contributors (e.g. the proceeds from the sale of financial assets). In France, initial measurement of revenues and possible related receivables is at face value. For subsequent measurement, uncollectible contributions are considered through impairment. In Poland, social contribution are generally recorded on an accrual basis. For social contributions to the Labour Fund (FP) and the National Health Fund (NFZ) the time-adjusted cash method is used. Revenues from social contributions relating to the Social Security Fund (FUS), Bridge Pension Fund (FEP), Demographic Reserve Fund (FRD) and Guaranteed Employment Benefit Fund (FGŚP) are adjusted by the average non-collection coefficient.

With the exception of self-employed entrepreneurs in Czech Republic and in France, in all of the analysed Member States there were no social contributions that were determined only after the end of the fiscal year. In the Czech Republic and in France, revenue for social contributions for self-employed entrepreneurs are only accounted for in subsequent periods.

8. Discussion of matters relevant for a European harmonization

8.1 Categories of social contributions that should be treated by future EPSAS standards

The most elaborated categorizations of social benefits are the statistical categorizations. From a financial accounting and convergence perspective, we recommend differing at least between the following sources of social contributions:

- ▶ Employee contributions
- ▶ Employer contributions
- ▶ Self-employed or unemployed contributions and
- ▶ Unallocable contributions.

Within those four categories it should be differed between pension and non-pension contributions as pension contributions have different accounting requirements from non-pension contributions (e.g. their actuarial treatment). The main advantage of such an approach would be an alignment of EPSAS requirements with the statistical requirements under ESA and GFS.

Against the background that there could be accounting difficulties associated with regards to fully funded and partially funded social insurance schemes (see Chapter 5) a differentiation between the two types of social contributions would be necessary. However, it would have to be considered that many social security schemes in the EU are operated on a pay-as-you-go basis, so that a differentiation does only make sense for such Member States that have funded or partially-funded social security schemes.

As social contributions are often multi-purpose in nature, it is also not recommended to classify social contributions by function/purpose.

8.2 Consequences for a possible convergence between EPSAS and ESA

As outlined before, social contributions together with taxes represent the main source of government revenue in the EU. Their recording in national accounts is particularly crucial in the context of the Excessive Deficit Procedure (EDP).

a) Convergence in terms of categorization

As outlined in the chapter before, a categorization that differs at least between the following sources of social contributions

- ▶ Employee contributions
- ▶ Employer contributions
- ▶ Self-employed or unemployed contributions and
- ▶ Unallocable contributions.

would allow for a convergence between EPSAS and ESA. Within those four categories, it should also be differed between pension and non-pension contributions due to specific accounting requirements for pension contributions.

b) Recognition of revenues from social contributions

Under ESA 2010 social contributions are recognized at the time when the work that gives rise to the liability to pay the contributions is carried out (see Chapter 6.1.4). IPSAS 23 refers to the accounting for the respective asset and specifies that resources arising from social contributions satisfy the definition of an asset when the entity controls the resources as a result of a past event and expects to receive future economic benefits or service potential from those resources. As a consequence, "revenue" from social contributions cannot be recognized according to IPSAS 23 until the past event has taken place (e.g. earning of income by the contributor). Therefore, both IPSAS and ESA take similar approaches with regards to the recognition of revenues from social contributions.

Where there is a time lag between the underlying event for the social contributions and the point in time when the final amount of social contributions due is determined, then IPSAS 23 favours the use of statistical models for the measurement of social contributions. ESA 2010 currently allows the use of statistical models in principle as the coefficients/capital transfers are estimated on the basis of the past information on the uncollectable parts. However, IPSAS 23 also allows to account for social contributions based on the amounts as evidenced by tax assessments and declarations or cash receipts in the case when those methods allow to reliably measure the respective asset. In such circumstances, alignment between IPSAS and ESA can be realized. Unlike than for taxes it has to be considered that the timing differences between when the social contributions are earned and the point in time when they are levied are often not that extensive or are even not existent. The only exception that occurred in the country analysis were the social contributions from self-employed entrepreneurs.

Therefore, in general the amounts as evidenced by tax assessments and declarations or the time-adjusted cash method could be sufficient to measure the revenues from social contributions. Under such circumstances an alignment between IPSAS and ESA would be possible. For self-employed entrepreneurs social contributions are often determined only at a later stage (e.g. when they file their tax declarations). As there is a time lag between the underlying event for the social contributions and the point in time when the final amount of social contributions due is determined, entities may reliably measure assets arising from social contributions by using statistical models based on the history of collecting such contributions in prior periods according to IPSAS 23.68. However, IPSAS 23.70 identifies cases where the assets arising from taxation transactions and the related revenue cannot be reliably measured until sometime after the underlying event occurs. In such cases, IPSAS 23.70 states that the assets and revenue may be recognized in the period subsequent to the occurrence of the underlying event. This approach corresponds to ESA 2010 as para. 4.82 of ESA 2010 also applies to social contributions.⁴⁸ In line with the IPSAS requirements, they may be recorded in the periods in which they are paid.

c) Measurement of social contribution

ESA 2010 4.82 and ESA 2010 4.95 states that taxes and social contributions recorded in the accounts may be derived from amounts evidenced by either tax assessments and declarations or cash receipts. If tax assessments and declarations are used, then the amounts of revenue shall be adjusted by a coefficient reflecting assessed and declared amounts which will be never collected. As an alternative treatment, the revenue may be recorded gross and a capital transfer to the relevant sectors recorded equal to the same adjustment. The coefficients shall be specific to different types of taxes and employers' and households' actual social contributions.

⁴⁸

It was confirmed by Eurostat that para. 4.82 applies by analogy also to social contributions.

In the case that cash receipts are used, they shall be time-adjusted so that the cash is attributed to the accrual time (so-called “time-adjusted cash method”). The ESA treatment of taxes and social contributions therefore shows that the same accounting approaches apply to both types of revenues. As outlined above IPSAS 23 does also allow to account for social contributions based on the amounts as evidenced by tax assessments and declarations or cash receipts when those methods allow to reliably measure the respective asset.

ESA 2010 states that taxes and social contributions accrued (or assessed as due) but unlikely to be collected, for various reasons (such as bankruptcy of companies, lack of efficiency of the tax collecting system, disappearance of individual taxpayers, etc.), shall not be included as government revenue and hence shall have no impact on general government net lending/borrowing. Similarly, IPSAS 23.68 states that statistical models should be based on prior years experience with collecting the particular revenues. Therefore, the approach in ESA and IPSAS are rather similar in that regard. However, it has to be noted that for subsequent measurement of receivables resulting from social contributions under IPSAS would have to be assessed periodically whether there is an indication for impairment. If this were the case, then the respective receivables would have to be impaired. In contrast to that, ESA does not have such impairment procedures in place. Convergence with regards to subsequent measurement of social contributions of ESA and IPSAS can therefore not be achieved.

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

Given that the accounting difficulties for social contributions might not be sufficiently material and significant it would first have to be assessed whether it makes sense to develop supplementary guidance for the accounting of social contributions. As a next step it would therefore have to be assessed whether this is also the case for other Member States. As outlined before we would recommend to involve social security experts in this exercise.

Against the background of the different social contributions systems in Member States, an EPSAS that covers the accounting treatment of social contributions would likely need to be principles-based. This could be done in a separate EPSAS on “Social Contributions” or in an EPSAS on “Revenue” that covers either non-exchange revenues (including taxes and social contributions) or even all types of revenues (non-exchange and exchange revenues). Given the similar nature of the accounting difficulties of social contributions and taxes it is in our view recommended to use the same accounting principles for both types of revenues. An EPSAS on revenue could therefore cover both principles for social contributions and taxes.

Also due to the complexity and variety of the multiple social contribution systems in Member States it is probably not realistic to try developing detailed guidance in a standard which covers all circumstances and arrangements. Therefore, additional guidance next to a standard is likely needed to operationalize the principles of IPSAS 23 or a future IPSAS on revenue. The EPSAS objective of comparability implies that the development of further detailed application guidance compared to what is currently provided by IPSAS 23 (and probably its successor) is needed.⁴⁹ Such application guidance could be provided as a separate part of the EPSAS (similar to application and implementation guidance provided under IPSAS) or as a separate (sub-standard) interpretations document.

Similarly than for taxes, for the measurement of revenues from social contributions based on statistical models (e.g. for social contributions by self-employed entrepreneurs) it would be required to specify on how the statistical model would need to be set up and for which

⁴⁹ In this context it needs to be considered that IPSAS 23 is meant for global application and therefore needs to be more general and less detailed/prescriptive.

categories of social contributions it should be applied. Especially the relevant variables, types of parameters and necessary assumptions for the model should be identified. Likewise guidance needs to be provided for subsequent application of the statistical model as well as on how to determine and handle corrections in subsequent periods. Detailed social contribution-specific application guidance would be needed for the design and application of those statistical models.

For the application of the assessment/social declaration approach it would need to be specified for each category of the relevant social contributions at what point in time an entity would be allowed to recognize a receivable. In addition, recommendations with regards to time adjustments should be given (e.g. until what point in time assessments/social declarations should be considered). With regards to measurement further guidance should be provided on impairment of receivables resulting from outstanding social contributions.

In summary, EY would recommend that future EPSAS guidance on accounting for social contributions should be developed together with guidance on taxes and in a similar manner than for taxes. The following table summarizes our recommendations:

Type of guidance:	Standard (EPSAS)	Interpretations and application guidance (either as part of the EPSAS or as separate document)
Purpose of guidance:	Principles for accounting of revenues (including social contributions and taxes) by Member States	Next to the principles in a standard, providing interpretations and application guidance on accounting for social contributions and for tax revenues relevant for preparers in Member States
Point of reference:	Principles on accounting for social contributions and taxes under IPSAS 23 (or its successor)	Individual social contribution and tax systems of Member States
Issues to be covered:	<ul style="list-style-type: none"> • Recognition principles for tax revenues/social contributions (including social contributions for self-employed entrepreneurs) • Measurement of assets arising from social contributions and taxation transactions (i.a. reliable measurement through statistical models, the tax/social declaration approach or the time-adjusted cash method, factors determining the measurement, impairment of social/tax contribution receivables) • Presentation and disclosures issues 	<ul style="list-style-type: none"> • Concretion of the recognition principles for social contributions/tax revenues taking into account the individual systems of Member States (including social contributions for self-employed entrepreneurs) • Concretion of the measurement principles for social contributions/tax revenues taking into account the individual systems of Member States • Detailed application guidance on presentation and disclosure issues taking into account the individual systems of Member States

9. Way forward recommended

Based on the analysis above, EY has derived the following recommendations:

1. Against the background that the accounting difficulties for social contributions might not be sufficiently material and significant we would recommend to first assess whether it makes sense to develop supplementary guidance for the accounting of social contributions. This assessment would have to be based on a larger sample of Member States. In case that it is decided to develop guidance for the accounting of social contributions there needs to be a principles-based approach for the accounting of social contributions given the different and complex social contributions systems in Member States. Due to the similar nature of the accounting difficulties of social contributions and taxes it is recommended to use the same accounting principles for both types of revenues. An EPSAS that covers social contributions should be based on the principles of IPSAS 23 (or of the future IPSAS on revenue). Next to the principles in an EPSAS, interpretations and/or application guidance on accounting for social contributions should be provided. Given the fact the EPSAS should be principles-based, the standard shall apply to all categories of social contributions (including social contributions for self-employed entrepreneurs). Social security specialists from Member States would need to get involved to develop the accounting principles and any additional guidance.

Rationale:

- ▶ Together with taxes, social contributions are the main source of revenue for governments.
 - ▶ The complexity and variety of the various social security and tax systems in Member States is such that it is not realistic trying to develop detailed accounting guidance in an EPSAS.
 - ▶ IPSAS 23 or a future IPSAS on revenue shall be taken as a first reference base for EPSAS to ensure comparability across Member States on accounting for social contributions on a conceptual level.
2. Additional application guidance for the accounting of social contributions should be developed. Similarly as recommended in the taxes issues paper, this application guidance could be provided as a separate part of the EPSAS (similar to IPSAS) or as a separate (sub-standard) interpretations document. Depending on the type of social contributions and the respective levying system detailed application guidance should be developed for the design and practical application of statistical models, the social declaration/ assessment approach and the time-adjusted cash method. This guidance would need to be specific depending on the category of social contributions and would have to take into account the individual social security/tax systems of Member States.

Rationale:

- ▶ The level of guidance provided by IPSAS 23 (or a future IPSAS on revenue) and ESA needs to be concretized for the accounting of social contributions (e.g. the accounting for social contributions of self-employed persons).
- ▶ Depending on the category of social contributions there are different characteristics that would need to be considered in the development of guidance (e.g. pension and non-pension contributions).
- ▶ Social security systems can vary significantly in Member States.

3. Given the fact that the IPSASB currently has a project on “Revenue” on its agenda, this project should be closely monitored in the context of the development of the EPSAS guidance on accounting for social contributions and for taxes.

Rationale:

- ▶ The aim of IPSASB’s project is to develop one or more IPSASs covering revenue transactions (exchange and non-exchange).
- ▶ Based on the current IPSASB’s work plan a Consultation Paper is envisaged to be approved for June 2017.

10. Key parallels between taxes and social contributions that should be taken into account

As outlined before, the accounting difficulties of social contributions and taxes are rather similar. Similarly than for taxes also social contributions have an underlying event that builds the basis for levying them. In addition, the recognition difficulties of social contributions are similar to taxes. For social contributions there could also be a time lag between the underlying event for the social contributions and the point in time when the final amount of social contributions due is determined. This is especially the case for social contributions for self-employed entrepreneurs. Equally in terms of measurement, the problems identified have similarities as for some types of social contributions estimations would have to be applied.

Based on these observations it is recommended to have the same accounting principles for both types of revenues and the same detailed interpretations and/or application guidance.

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