EPSAS Cell STA 17/10

EPSAS Cell on Principles related to EPSAS standards

Luxembourg, 27-28 September 2017

Note of the meeting – draft

Introduction/ approval of the agenda

1. Eurostat explained that following the EFC sub-committee on statistics meeting, 27 March 2017, TF.EPSAS had intensified its work on impact assessment considerations and the elaboration of the technical proposal on EPSAS. Following a question from the floor, Eurostat clarified that item 6 of the agenda had initially been planned to be taken up in the FTI Cell but in order to achieve quicker progress and since the issue was also in the scope of the EPSAS conceptual framework Eurostat proposed to handle it in this Cell.

2. Eurostat also proposed that the issue of the OCI should be discussed under other business if time permitted.

3. The agenda was agreed.

Note of the meeting 29 March 2017

4. Eurostat had amended paragraph 12 on the note following a modification proposed by one participant concerning sustainability and intergenerational fairness as the origin of a hierarchy of QCs.

5. Eurostat explained that, as had also been suggested by a participant, all references to IPSAS in the proposed outline of definitions would be removed or replaced by EPSAS, as appropriate.

6. With reference to the action point for further reflection on the hierarchy of QCs, cell participants could not report on any hard evidence of problems in financial accounting and reporting resulting from the absence of such hierarchy. Nevertheless a reference was made, for further reflection, to IASB's ongoing work on the IFRS conceptual framework, where a distinction was being proposed between fundamental and enhancing QCs.

7. The revised version of the draft note on the previous meeting was approved without further comments.

Feedback from the EPSAS Working Group - main discussion points/ conclusions

8. Eurostat noted that the discussion at the last EPSAS WG meeting of 26-27 April 2017 concerning the Cell's progress report had focused mainly on the opinion of the EFC sub-committee on statistics, and in particular on the need to explore further the impact considerations and review possible options.

9. The question was raised how the views of the Member States would be taken into consideration during the preparation of the impact assessment and the technical proposal and their transformation into a Commission proposal. Eurostat clarified that the remit of Eurostat's Task Force EPSAS was limited to the drafting of the impact assessment and the development of the technical proposal while the formal adoption procedure was the responsibility of other Commission services, such as the Secretariat General and the Legal Service. The EPSAS Working Group and the EPSAS Cells offered MSs and the Commission the opportunity to exchange views on the issues at stake. A public consultation, a mandatory element of the process, was a further means for taking into consideration views from the wider stakeholder community.

Definitions of QCs, Constraints and Application principles

10. The discussion ensued around the meaning of "non-financial" information in the sense of IPSAS 1.25 that was seen as going beyond the scope of the EPSAS project. The boundaries of GPFRs in IPSAS were not defined and it was still debated whether e.g. sustainability reporting should be within the reporting requirements. Eurostat explained that no connection with IPSAS 1.25 had been established. The intention was to leave it for the future standard-setting body to define reporting requirements beyond GPFSs as necessary.

11. Further explanation was asked about the difference between "true and fair view" and "faithful representation" as in the accounting literature they were often seen as similar, if not identical, concepts. It was clarified that while "true and fair view" was defined as an overarching objective of financial reporting as a whole, "faithful representation" was a QC guiding the treatment of individual economic phenomena, events or transactions.

    Qualitative characteristics

    The definitions of the QCs were discussed and amended as per Annex 1.

12. "Relevance": It was clarified that 'objectives of financial reporting' referred to the objectives of GPFRs rather than to the objectives of the EPSAS project. The text was amended accordingly.

13. "Faithful representation": A participant suggested embedding the principle of "objectivity" in the definition of "faithful representation". In the understanding of

other participants objectivity was already covered by the QC of "verifiability". A discussion ensued on the difference between "reliability" and "faithful representation" and which components the latter comprised. Eurostat suggested taking "reliability" and "faithful representation" as one notion and naming in the definition the notions they were comprised of, including the notion of "prudence" (completeness, neutrality, prudence, free from material error, substance over form). Despite wide consensus, the view that "objectivity" should be mentioned as part of "faithful representation" was retained.

14. "Substance over form": The text was streamlined.

15. "Neutrality": The text was extended with a further sentence explaining that the application of the "prudence" principle did not contradict "neutrality" in that it helped where judgements were made under conditions of uncertainty. This approach was in line with the changes considered in the revision of IASB's Conceptual Framework for private sector financial reporting.

16. "Prudence": One participant requested a further elaboration of the principle following the lines of Art. 6 of the Accounting Directive. Eurostat took the view that even though the formulation used in Art. 6 of the Accounting Directive seemed at first glance to be more restrictive, the Directive gave full relief from the strict application of the principle. Eurostat was of the opinion that "prudence" was an essential element of the EPSAS CF guiding both the standard-setter and the preparer but it should not be used for a-priori narrowing down the choice of a measurement basis, the latter also depending on the measurement objective. Eurostat therefore proposed to keep the current version of the definition.

17. "Completeness": It was suggested to provide a better explanation of completeness and to add a reference to the fulfilment of the recognition criteria. It was also suggested by one participant to use a stronger word than "should" in order to strengthen the requirement in the context of a binding conceptual framework. Eurostat clarified that the text would undergo legal revision to make sure that requirements were properly formulated. Eurostat would provide a revised text after the meeting.

18. "Understandability": A discussion ensued on whether users of financial statements needed to be "educated" in order to understand their meaning or whether they should be formulated in a way that both expert and non-expert users could take advantage of them. It was also felt that the word "enable" was too strong and should be replaced by a less demanding term. The relationship between "understandability" and "comparability" was also discussed. Eurostat agreed to implement those changes and streamline the original text.

19. "Timeliness": The discussion focused on the question whether "timeliness" conflicted with the "reliability" principle. Most of the participants shared the view that "timeliness" did not contradict "reliability" but rather balanced it. No changes to the text were made.

20. "Comparability": The first sentence was extended following a suggestion by a member of the Cell. Parts of the original text were deemed unnecessary and a revised text linking comparability with consistency was also implemented.

21. "Verifiability": Against the background of the earlier point on "objectivity" the discussion focused on the links between verifiability, reproducibility and auditability of the financial information (to be) provided by preparers, and the need for a clear reference to supporting evidence. The text was revised accordingly.

Constraints

The definitions of the Constraints were discussed and amended as per Annex 1.

22. "Materiality": The last sentence of the original text was removed.

23. "Cost-benefit": The particular importance of this constraint was emphasised by one participant who suggested linking it to serving European public good and using a stronger formulation for the purposes of a binding conceptual framework. Eurostat recalled that the text would undergo legal revision before finalisation and took the view that there was no need to make a reference to the European public good as this was anyway an overarching condition, valid for all QCs and Constraints.

24. "Balance between the QCs": One participant suggested the removal of the sentence referring to "professional judgment" as it was not clear who and when should deliver such judgment. The majority of Cell participants agreed.

25. "Presentational sensitivity": It was clarified that it only referred to presentational requirements and had no impact on recognition and measurement requirements.

Application principles

The definitions of the application principles were discussed and amended as per Annex 1.

26. "Compliance": In case of binding EPSAS this would be a legal requirement. It could however be relevant for reporting entities, inside or outside the EU, who wished to follow EPSAS voluntarily, in which case they should be required to state compliance with it. Therefore, Eurostat decided to keep this principle as part of the EPSAS CF, at least for the time being, even if it could be deleted from the final proposal.

27. "Consistency": It was suggested by one participant that the text should refer not only to presentational requirements but also to the consistent choice of the recognition and measurement basis in the accounting policies. Adding a requirement for disclosing information on changes of accounting policies was also proposed. Eurostat agreed and revised the text accordingly.

28. "Aggregation": One participant suggested an addition to the text with reference to the collective measurement of similar items but it was clarified that this principle referred only to presentational requirements. Therefore the text remained unchanged.

29. "Offsetting": It was suggested to merge this principle with "aggregation" as the two were strongly related from the presentational perspective, whereas "offsetting" should appear before "aggregation" in this definition. Eurostat agreed and revised the entry accordingly.

30. "Going concern": With the exception of the second sentence it was suggested removing the other parts of text as they were seen as being too business sector specific. Further changes were left open as "going concern for the public sector" was also discussed as a separate item on the agenda (see below).

31. "Reporting period": One participant mentioned that, in the EU context, similarly to "compliance" in the end this principle might not be necessary as there would be probably concrete legal requirements defining the reporting period. As shorter or longer reporting periods, even if in exceptional cases, could not be ruled out, Eurostat decided to keep the principle subject to minor adjustments.

Going concern approach/ continuity of government

32. Eurostat took the view that it was important to outline public sector specificities and that the French text offered a reasonable approach to do this, even if a range of conclusions might be drawn from this formulation.

33. Eurostat emphasised that, also by reference to the IPSAS CF or the EPSAS CF in preparation, there should be no reason to compromise the exhaustiveness of the accounts or limit the scope of reporting entities. One participant suggested that this issue should be treated outside the going concern approach and probably at the level of the "reporting entity".

34. Another participant warned that it would be best to avoid referring to so complex phenomena such as the "sovereign power" which would be country specific and difficult to interpret.

35. After a tour-de-table wider consensus was achieved that such public sector specificities should be treated at the application principles level but some participants also suggested that a general reference to differences between public and private sector should be mentioned in a preamble or among the introductory considerations. Eurostat agreed and revised the original version of the text for the "going concern" principle accordingly (see Annex 1).

First exchange of views on the definition of elements, recognition and measurement bases

36. Eurostat was of the view that these topics should be treated at a high level in the future EPSAS framework and provide the basis for the future standard setting. In this context it was seen necessary to discuss the completeness and the suitability of the elements, recognition and measurement bases as defined in the IPSAS literature which had served as a first reference base, also taking into consideration the glossary of terms in use of the FTI guidance, which in their turn were based on the Commission's IPSAS-based definitions.

Elements

37. The list of elements under consideration included:

- Assets
- Liabilities
- Expenses
- Revenue
- Ownership contributions
- Ownership distributions

Furthermore, Net worth (net assets/ liabilities) and Net expenses/ revenue (surplus/ deficit) should also be mentioned as the balancing items.

38. Some participants noted that other economic phenomena (such as deferred inflows and outflows) were not defined in the IPSAS CF. Eurostat agreed that the list of elements be widened for the framework to incorporate these additional elements. It seemed better to be exhaustive rather than to omit any concept which might be useful at a later stage.

39. Eurostat emphasised that the elements in the IPSAS CF were well defined and broadly in line with other accounting frameworks such as the French CF and IASB`s CF. Therefore departing from those would require justification. In this context it was mentioned that, for instance, in the French CF, public entities could not recognise liabilities or contingent liabilities arising from constructive obligations specific to public action. This was because in France, public entities are set up to exercise responsibilities which were clearly defined by a legal or regulatory framework, hence their capacity to make commitments in the specific field of public action was strictly regulated; therefore actions from those public entities could not by definition give rise to constructive obligations. It was also noted that the definitions used in the FTI glossary were mainly based on IPSAS 1, which had a slightly different wording from the definitions used in the IPSAS CF. Therefore some minor alignments might be necessary.

Recognition/ derecognition

40. Eurostat briefly presented the general recognition criteria applied in IPSAS.

41. One participant suggested also mentioning that, in exceptional circumstances, a standard may also specify that, in order to deliver true and fair view under EPSAS, a resource or obligation that did not meet the definition of an element or satisfy the recognition criteria, might nevertheless need to be recognized in the financial statements.

42. A discussion ensued as to whether an explicit reference should be inserted in the EPSAS framework requiring the recognition of an element only once so ensuring that an asset was recognised by only one entity. Several participants agreed that this requirement was implicitly already ensured by the QCs (e.g. completeness, verifiability, etc.), the definitions of the elements and the recognition criteria. One participant questioned whether QCs alongside the definitions of elements and recognition criteria might ever ensure the consistency of financial statements among public sector reporting entities without dramatically increasing the costs associated with the preparation of financial statements. Other Cell members took the view that in practice, the auditors were to ultimately ensure that all items that fulfilled the recognition criteria (e.g. an asset controlled by an entity) at the level of an entity were recognised in the financial statement of that entity – subject of course to taking into account materiality constraints. The auditors of the statements of the consolidating entity relied on the system of audits performed at the level of the consolidated entities and were both required and able to focus the scope of their work on the proper elimination of inter-entity transactions. That offered an additional possibility to remove discrepancies, redundancies, duplications and other possible errors in the statements of the consolidated public sector entities at a degree of certainty defined by the materiality threshold set.

43. Eurostat shared this view and would further consider any amendment needed to the IPSAS approach for EPSAS purposes.

Measurement

44. Eurostat briefly presented the measurement bases listed in the IPSAS CF against the background of measurement bases listed in the Eurostat SWD (2013) 57 accompanying the Commission report on the suitability of IPSAS.

45. The chair of the IPSASB updated the participants on the on-going IPSASB project on public sector measurement. IPSASB aimed to issue a standard with application guidance but at this stage was developing a CP that would already include a draft ED. The IPSASB planned to work closely together with the valuation and GFS communities on this project.

46. One participant suggested narrowing down the possible choices of measurement bases to historic cost variants and observable market values as only these measurement methods provided reliable information. Other participants disagreed with this position and emphasised that there were many cases which required the consideration of other measurement bases in order to better reflect the substance of the economic transaction for decision-making but also for accountability purposes.

Another participant proposed using the term "valuation" instead of "measurement" as this term better covered the substance of the definitions.

47. Eurostat emphasised that the objective of the framework in this context was to provide a kind of toolbox for the standard-setter by describing the widest possible range of measurement bases that could be meaningfully applied in various contexts. Therefore a stock-taking approach was necessary.

Next steps / Action Points

1. Eurostat to review the formulations of QCs, Constraints and Application Principles and submit the revised text to the participants for comments.

2. Eurostat to amend the text of the going concern principle taking into consideration elements of the French approach.

3. Eurostat to cross-check with DG BUDG whether there was a need to align the definitions of elements with the IPSAS CF.

4. Two items were left on the agenda for follow-up:
    - OCI
    - Transferability of pension rights

5. The Cell participants would be invited to submit by email their comments on the revised definitions by 20th October 2017.

6. Eurostat would give an update on the work done by the Cell at the next meeting of the Working Group, to be held in Luxembourg on 21-22 November 2017.

Participants List - EPSAS Cell on Principles related to EPSAS standards
Luxembourg, 27-28 September 2017

Belgium:	Marc de Spiegeleire (Ministry of Finance)
France:	Fabienne Colignon (Ministry of Finance)
Finland:	Jaakko Eskola (National Audit Office)
Germany:	Jan Finken (Federal Ministry of Finance)
IPSAS Board:	Ian Carruthers
Accountancy Europe:	Thomas Müller-Marqués Berger
Eurostat:	Alexandre Makaronidis (Chair) Norbert Gáspár Keith Hayes Peeter Leetmaa István Varjas Carmela Zammit (on 28 September 2017)
DG Budget:	Magdalena Zogala

ANNEX 1

EPSAS Outline	Definitions
EUROPEAN PUBLIC GOOD	The whole structure operates under the overarching governance principle of the public interest of the EU - European public good.
OBJECTIVES OF THE EPSAS INITIATIVE **Constraints - Subsidiarity, Proportionality**	The key objectives of the EPSAS project is to increase financial transparency and comparability between and within Member States by developing and implementing a common set of European financial accounting and financial reporting standards in order to provide a true and fair view of the financial position and performance of public sector reporting entities under the accruals basis of accounting, ... subject to taking into account proportionality and subsidiarity principles.
OBJECTIVES OF GPFRs UNDER EPSAS **True and fair view** **Accruals basis of accounting** **Users of GPFRs under EPSAS**	GPFRs under EPSAS should provide a true and fair view of the financial position and performance of public sector reporting entities - governments or other public sector entities – under the accrual basis of accounting for accountability and decision making purposes, including in the context of sustainability and inter-generational fairness. GPFRs support the management of public finances. Under the accrual basis of accounting, transactions and other events are recognized in financial statements when they occur (and not 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 periods to which they relate. GPFRs comprise GPFSs, such as the statement of financial position or balance sheet, the statement of financial performance or income statement, the statement of cash-flows, the statement of comprehensive income and the disclosure notes to those statements, alongside other financial and non-financial information. Non-financial information may be needed in order that the GPFSs provide a true and fair view. The main users of GPFRs are resource providers and their representatives as well as service recipients and their representatives - ultimately the citizens as the key stakeholders of governments and other public sector entities. The

	legislature and members of parliament, and equivalent actors at sovereign or sub-sovereign levels, are among the main users of GPFRs, and may make extensive and ongoing use of GPFRs when acting in their capacity as representatives of the interests of service recipients and resource providers. GPFRs provide a standardised set of reports meeting the information needs of users who are not empowered to require the disclosure of financial information tailored to their specific information needs. GPFRs represent the minimum level of necessary information to be provided to all users.
QUALITATIVE CHARACTERISTICS	
Relevance	Financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of GPFRs. Financial and non-financial information is capable of making a difference when it has confirmatory value, predictive value, or both.
Faithful representation/ Reliability	To be reliable, financial and non-financial information must provide a faithful representation of the substance of economic and other phenomena that it purports to represent. Faithful representation is attained when the depiction of the phenomenon is complete[1], prudent[2], neutral[3], and free from material error. Information that faithfully represents an economic or other phenomenon depicts the substance over the form[4] of the underlying transaction, other event, activity or circumstance.
Completeness [1]	The information which fulfils the recognition criteria should be complete within the bounds of materiality and cost-benefit considerations.
Prudence[2]	Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or revenue are not overstated and liabilities or expenses are not understated.
Neutrality [3]	Information is neutral if it is free from bias. GPFRs are not neutral if the information they contain has been selected or presented in a manner designed to influence the making of a decision or judgment in order to achieve a predetermined result or outcome. The application of prudence under conditions of uncertainty does not constitute bias and does not affect neutrality. Neutrality is supported by the exercise of prudence.

Substance over form [4]	Substance over the form requires that the underlying transactions, other events, activities or circumstances are accounted for and presented in accordance with their substance and economic reality, and not merely their legal form.
Understandability	Understandability is the quality of presenting information in a manner that facilitates expert and non-expert users to comprehend its meaning. Understandability is enhanced when information is classified, characterised and presented clearly and concisely.
Timeliness	Timeliness means having information available for users before it loses its capacity to be useful for accountability and decision-making purposes. Having relevant information available sooner can enhance its usefulness as input to assessments of accountability and its capacity to inform and influence decisions that need to be made. A lack of timeliness can render information less useful.
Comparability	Comparability is the quality of information that enables users to identify similarities in, and differences between, two sets of phenomena in different reporting entities or in one reporting entity at different points in time.
Verifiability	Verifiability is the quality of information that helps assure users that GPFRs is based on supporting evidence in a way that it faithfully represents the substance of economic and other phenomena that it purports to represent.
CONSTRAINTS	
Materiality	Information is material if its omission or misstatement could influence the discharge of accountability by the entity, or the decisions that users make on the basis of the entity's GPFRs prepared for that reporting period. Materiality depends on both the nature and amount of the item judged in the particular circumstances of the entity.
Cost-benefit	Financial reporting imposes costs. The benefits of financial reporting should justify those costs. Assessing whether the benefits of providing information justify the related costs is often a matter of judgment, because it is often not possible to identify and/or quantify all the costs and all the benefits of information included in GPFRs.
Balance between the qualitative characteristics	The qualitative characteristics work together to contribute to the usefulness of information. In some cases, a balancing or trade-off between qualitative characteristics may be necessary to achieve the objectives of financial reporting. The aim is to achieve an appropriate balance among the characteristics in order to meet the objectives of financial reporting.

APPLICATION PRINCIPLES	
Going concern	Financial statements shall be prepared on a going concern basis unless there is an intention to liquidate the entity or to cease operating, or if there is no realistic alternative but to do so. The rights and obligations specific to public action entrusted in public entities may only cease to exist, in full or in part, by law or decision of the government, even where public sector entities are merged, split or dissolved.
Consistency	The accounting policies and the basis of preparation as well as the presentation and classification of items in the financial statements shall be retained from one period to the next unless, following a significant change in the nature of the entity's operations or a review of its financial statements, another accounting policy, basis of preparation, presentation or classification is more appropriate. In this case the resulting changes shall be justified and disclosed. Consistency is a means of delivering comparability by making use of the same accounting principles or policies and basis of preparation, either from period to period within a reporting entity or in a single period across more than one reporting entity.
Offsetting/ Aggregation	Assets and liabilities, and revenue and expenses shall not be offset unless so required or permitted by an EPSAS. It is important that assets and liabilities, and revenue and expenses be reported separately. Each material class of similar items shall be presented separately in the financial statements. Items of a dissimilar nature or function shall be presented separately, unless they are immaterial.
Presentational sensitivity	There are areas where there may be some sensitivity when it comes to the level of detail at which information is presented in financial statements, e.g.: separate presentations or disclosures about individual military items, guarantees or legal cases. Presentational sensitivity however shall not have an impact on the recognition and measurement requirements related to the specific items in question.
Reporting period	Financial statements shall be prepared and presented at least annually. When an entity's reporting date changes or the financial statements are presented for a period longer or shorter than one year, a reporting entity shall disclose, in addition to the period covered by the financial statements, the reason for using a longer or shorter period and the resulting limitation on comparability.

Compliance	A reporting entity whose financial statements comply with EPSASs shall make an explicit and unreserved statement of such compliance in the notes. Financial statements shall not be described as complying with EPSASs unless they comply with all the requirements of EPSASs.