

19 January 2018

Ms Joanna Spencer
Manager, Standards Development and Technical Projects
International Public Sector Accounting Standards Board
277 Wellington Street West
Toronto, ON M5V 3H2

By email: JoannaSpencer@ipsasb.org

Dear Ms Spencer

Invitation to Comment – IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on the IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*. The views expressed in this submission represent those of all Australian members of ACAG.

ACAG supports IPSASB's preference for the use of the public sector performance obligation approach (PSPOA) for revenue recognition. ACAG suggests that a mirror approach for recognising expenses may be difficult to implement.

ACAG recommends that the non-exchange expense project is undertaken concurrently with the social benefits project to ensure consistent liability recognition criteria.

ACAG appreciates the opportunity to comment and trust that you will find the attached comments useful.

Yours sincerely



Andrew Greaves
Chairman
ACAG Financial Reporting and Accounting Committee

ATTACHMENT

ACAG comments on IPSASB Consultation Paper *Accounting for Revenue and Non-Exchange Expenses*

Preliminary View 1

The IPSASB considers that it is appropriate to replace IPSAS 9, *Revenue from Exchange Transactions*, and IPSAS 11, *Construction Contracts* with an IPSAS primarily based on IFRS 15 *Revenue from Contracts with Customers*. Such an IPSAS will address Category C transactions that:

- (a) Involve the delivery of promised goods or services to customers as defined in IFRS 15; and
- (b) Arise from a contract (or equivalent binding arrangement) with a customer which establishes performance obligations.

Do you agree with the IPSASB's Preliminary View 1? If not, please give reasons.

ACAG agrees with Preliminary View 1.

Preliminary View 2

Because Category A revenue transactions do not contain any performance obligations or stipulations, the IPSASB considers that these transactions will need to be addressed in an updated IPSAS 23.

Do you agree with the IPSASB's Preliminary View 2? If not, please give reasons

ACAG agrees with Preliminary View 2.

Specific Matter for Comment 1

Please provide details of the issue that you have encountered in applying IPSAS 23, together with an indication of the additional guidance you believe is needed in an updated IPSAS 23 for:

- (a) Social contributions; and/or
- (b) Taxes with long collection periods.

If you believe that there are further areas where the IPSASB should consider providing additional guidance in an updated IPSAS 23, please identify these and provide details of the issues that you have encountered, together with an indication of the additional guidance you believe is needed.

ACAG is unable to comment, as Australia does not apply IPSAS.

Preliminary View 3

The IPSASB considers that Category B transactions should be accounted for using the Public Sector Performance Obligation Approach.

Do you agree with the IPSASB's Preliminary View 3? If not, please give reasons

ACAG agrees with Preliminary View 3.

ACAG supports IPSASB in the adoption of a Public Sector Performance Obligation Approach (PSPOA). In practice, Category B transactions are not necessarily distinguishable from Category C transactions.

If the PSPOA were to be developed for Category B, it should be aligned with IFRS 15 to allow for Category C transactions to apply and achieve the same outcome as proposed in the Consultation Paper (CP). ACAG also raises issues with the exchange / non-exchange distinction under Specific Matter for Comment 4.

ACAG suggest that future IPSASB considerations for adapting IFRS 15 for the public sector should consider that ‘commercial substance’ will not necessarily mean that there is a ‘commercial return’. A common example of such arrangements is when goods or services are provided on a cost recovery basis or subject to affordability considerations. ACAG notes that the Australian Accounting Standards Board (AASB) has issued an amendment to AASB 15 *Revenue from Contracts with Customers* Appendix F (based on IFRS 15) via AASB 2016-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-profit Entities*. AASB 2016-8 may be useful in the development of PSPOA as it provides additional revenue related implementation guidance for the NFP sector.

Specific Matter for Comment 2

The IPSASB has proposed broadening the requirements in the IFRS 15 five-step approach to facilitate applying a performance obligation approach to Category B transactions for the public sector. These five steps are as follows:

Step 1 – Identify the binding arrangement;

Step 2 – Identify the performance obligation;

Step 3 – Determine the consideration;

Step 4 – Allocate the consideration; and

Step 5 – Recognise revenue.

Do you agree with the proposals on how each of the IFRS 15 five-steps could be broadened?

If not, please explain your reasons.

It is not clear from the Consultation Paper what ‘broadened’ entails. ACAG would consider that the five step approach in IFRS 15 is already broad, and at a level to accommodate industries across the private sector. On that basis, it is expected that the approach in IFRS 15 will be able to accommodate exchange transactions in the public sector. Rather than seeking to broaden IFRS 15, ACAG would suggest that the IFRS 15 principles be interpreted or applied for the public sector through guidance.

ACAG prefers the application of a combined model or approach for Categories B and C transactions. ACAG notes that the Australian Accounting Standards Board issued AASB 1058 *Income for Not-for-Profit Entities* in December 2016 and that this could be a useful reference for the IPSASB’s research deliberations in this area.

Step 1 Comments

ACAG support the view that identifying a binding agreement will require specific consideration and guidance for application in the public sector. In developing guidance of what is a binding arrangement, ACAG suggest that IPSASB review the approach taken by the AASB in adapting IFRS 15 for not-for-profit entities and broaden enforceability to include legal “or equivalent means” (refer

AASB 2016-8, Appendix F). The principle of “equivalent means” broadens the concept of enforceability to include legislative and administrative mechanisms that “oblige the entity to act in a particular way or be subject to consequence”. ACAG acknowledges that broadening the requirements in this manner may require some additional consideration as non-contractual mechanisms such as legislation, cabinet and ministerial decisions commonly exist and operate due to frameworks that exist / are maintained outside of the specific contract provisions. This approach will also present particular challenges for entities and auditors in assessing whether enforcement frameworks outside of contract provisions are applicable as to make a contract enforceable.

As IPSASB observe, identifying a customer (or the recipient of goods or services) is critical, and where there is no customer, it will be unlikely that there is a performance obligation. ACAG agrees with IPSASB’s view in paragraph 4.34, that in the public sector, identification of the customer is not always obvious.

ACAG notes that IPSASB refers to “binding” arrangement, but does not use the term binding in the discussion. ACAG suggests IPSASB consider the term “enforceable”, as used in IFRS 15.

ACAG notes that the IPSASB is proposing to permit the condition of the withdrawal of future funding as establishing enforceability (paragraph 4.32). ACAG does not agree with this proposal, and argues that this factor does not establish a performance obligation. ACAG therefore suggests the IPSASB consider this in more detail.

Step 2 Comments

ACAG support the view that identifying performance obligations will be a matter of judgement¹. ACAG suggests IPSASB review AASB 2016-8, Appendix F where detailed examples were provided to assist in making judgements on how to apply these principles in the not-for-profit sector.

The performance obligation requirement is far more complex for the public sector. There are key performance obligations where reliable measurement will be difficult. There are also incidental or implied performance obligations, which may or may not be measurable. For example, it is common for government agreements to approach performance obligations in the context of validating the delivery of government policy rather than identifying the goods or services to be delivered. While ACAG would encourage IPSASB to undertake further work in relation to implied obligations, ACAG acknowledges that the issues may be more easily understood and resolved if addressed once entities have had some experience with the new standard.

ACAG suggests removing references to stipulations from the discussion on performance obligations.

Step 3 Comments

ACAG is of the view that this step is a hurdle for the public sector. More work is needed to ascertain how consideration will be calculated, especially when the details are not sufficiently specific in the contract. IFRS 15 relies on fair value, which may be problematic for the public sector, especially for specialized assets. Typically, the value is not comparable to an equivalent in an active market.

¹ ACAG considers that the use of a combined approach for Categories B and C transactions would aid preparers in making consistent judgment.

Other research topics that could be further explored by the IPSASB include cash and non-cash considerations, impact of the government statistics requirements, and whole of government and general government sector financial reporting, which relate to the determination of consideration.

Step 4 Comments

ACAG considers that determining the standalone selling price in the public sector will be a particular challenge as IFRS 15 is written to consider each contract or customer individually. In the public sector a more macro perspective is applied, which considers public sector goods and services being delivered in a continuous flow. This collective objective or purpose, is not always related to individual contracts, customers, or individual products or on an individual component basis.

ACAG notes that standalone selling price may result in gains and losses that could impact on an entity's reporting of performance. IPSASB may want to seek additional comments on this issue.

Step 5 Comments

ACAG considers that it may be a challenge for public sector entities to reliably demonstrate when performance obligations are met and revenue recognised. However, ACAG see this as a positive development for users of financial information as it directs entities to report on the progress of outcomes and when obligations are satisfied, rather than on the spend.

In addition, ACAG suggests that consideration is given to exchange transactions that may have performance obligations which are not clearly enforceable or specifically defined. Where such obligations are not sufficiently specific, it is widely regarded that there are no performance obligations. This raises the question whether it is possible for exchange transactions to be without performance obligations.

ACAG notes that the Definitions (para. 2.2) for 'exchange transactions' and 'non-exchange transactions' are more aligned with the risks and rewards model applied in IAS 18 *Revenue*. The performance obligations approach does not hinge on exchanges or transfers of risks and rewards. As part of the IPSASB's research, ACAG recommends that the exchange and non-exchange categorisation may require additional work, or may be abandoned entirely if the PSPOA is adopted. ACAG notes that the diagram on page 27 of the Consultation Paper already highlights expected concerns with Category B transactions. In the public sector, ACAG notes that Category B transactions are likely to be a significant proportion of revenue transactions.

Specific Matter for Comment 3

If the IPSASB were to implement Approach 1 and update IPSAS 23 for Category B transactions, which option do you favour for modifying IPSAS 23 for transactions with time requirements (but no other stipulations):

- (a) Option (b) – Require enhanced display/disclosure;
- (b) Option (c) – Classify time requirements as a condition;
- (c) Option (d) – Classify transfers with time requirements as other obligations; or
- (d) Option (e) – Recognise transfers with time requirements in net assets/equity and recycle through the statement of financial performance.

Please explain your reasons.

ACAG does not support Approach 1. ACAG supports the IPSASB's development of the Public Sector Performance Obligation Approach (PSPOA) or Approach 2.

Specific Matter for Comment 4

Do you consider that the option that you have identified in SMC 3 should be used in combination with Approach 1 Option (a) — Provide additional guidance on making the exchange/non-exchange distinction?

- (a) Yes
- (b) No

Please explain your reasons.

ACAG does not support Approach 1.

ACAG notes that the Public Sector Performance Obligation Approach (PSPOA), which ACAG supports, has some fundamental differences in reasoning to the current IPSAS 23. One fundamental difference is that the PSPOA is based on the reasoning that the grantor / provider of funds can be the customer, as it directs to whom the goods and services are to be provided. In particular, the grantor does not need to directly be the recipient of the goods and services. Therefore, if IPSAS 23 was retained in its current form, the exchange / non-exchange distinction would need to be updated to reflect this reasoning.

Preliminary View 4

The IPSASB considers that accounting for capital grants should be explicitly addressed within IPSAS.

Do you agree with the IPSASB's Preliminary View 4? If not, please give reasons

ACAG agrees with Preliminary View 4.

Specific Matter for Comment 5

- (a) Has the IPSASB identified the main issues with capital grants?
If you think that there are other issues with capital grants, please identify them.
- (b) Do you have any proposals for accounting for capital grants that the IPSASB should consider?
Please explain your issues and proposals

ACAG supports the application of the PSPOA to capital grants provided for the purpose of enabling an entity to acquire or construct a non-financial asset that will be controlled by the entity. ACAG is of the view that the liability has to be recognised until the performance obligations are satisfied. ACAG's view is that additional guidance would be useful given that grants can be varied in terms and conditions.

ACAG does not support the recognition of a deferred liability for the possible obligation to return the non-financial asset, if the non-financial asset ceases to be used for the specified purpose. It is ACAG's view that so long as the agreed purpose is being met then there is no present obligation; the notion of a deferred liability is not consistent with the *Conceptual Framework*.

Specific Matter for Comment 6

Do you consider that IPSASB should:

- (a) Retain the existing requirements for services in-kind, which permit, but do not require recognition of services in-kind; or
- (b) Modify requirements to require services in-kind that meet the definition of an asset to be recognised in the financial statements provided that they can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information;
or
- (c) An alternative approach.

Please explain your reasons. If you favour an alternative approach please identify that approach and explain it.

ACAG suggests the approach outlined in paragraph 5.9(a) is adopted whereby volunteer services are recognised when they meet the definition of an asset (or an expense, when the definition of an asset is not met) if the fair value of those services can be measured reliably and the services would have been purchased if they had not been donated. This is consistent with the approach taken by the AASB. Not-for-profit entities can elect to recognise volunteer services regardless of whether or not those services would have been purchased so long as the fair value of these services can be measured reliably.

ACAG consider that where volunteer goods or services are fundamental to enabling an entity to meet its objectives and the loss of these goods or services would represent a significant change in the operating environment, financial performance or position of the entity, this information is relevant to users and it should be disclosed.

While ACAG support the view that the benefits derived from information should not exceed the costs of obtaining that information (Paragraph 5.8), ACAG is of the view that this assessment is

primarily the responsibility of standard setters, not entities, as it is often the case that the benefits of disclosures are far broader than the immediate users of a single entities financial statements.

ACAG suggest that IPSASB consider that ‘do not require’ considerations be extended to include the encouragement of regulators to consider where additional disclosure would be relevant to users, without representing an unreasonable information burden.

ACAG notes that for some entities the decision to make volunteer disclosures in financial statements is not based entirely on financial considerations, for some entities it provides a basis for making a prominent and public acknowledgement of the important contribution made by volunteers.

ACAG notes that the test “the services would have been purchased if they had not been donated” is often difficult for volunteer time.

Preliminary View 5
The IPSASB is of the view that non-exchange transactions related to universally accessible services and collective services impose no performance obligations on the resource recipient. These non-exchange transactions should therefore be accounted for under The Extended Obligating Event Approach.
Do you agree with the IPSASB’s Preliminary View 5? If not, please give reasons

ACAG suggests that further work needs to be undertaken in relation to this topic.

ACAG suggests that assumptions should not be made that recipients of grants, contributions and other transfers that provide universally accessible services have no performance obligations under their funding agreements. While these funding arrangements would be non-exchange under IPSAS 23, they may be equivalent to contracts under the PSPOA. ACAG suggests that arrangements that meet the criteria for the PSPOA, should be accounted for under the PSPOA, even if they relate to universally accessible services.

Preliminary View 6
The IPSASB is of the view that, because there is no obligating event related to non-exchange transactions for universally accessible services and collective services, resources applied for these types of non-exchange transactions should be expensed as services are delivered.
Do you agree with the IPSASB’s Preliminary View 6? If not, please give reasons

ACAG agrees with Preliminary View 6. The expectation that services will be provided in the future does not represent an obligating event. While there will be a general expectation that government services will be provided in the future, actual service provision is subject to ongoing qualifying criteria which will change as government policy and public expectations change.

ACAG suggest clarity is provided for situations where governments have implied obligations to provide services—such as the education of children of school age.

ACAG recommends that the non-exchange expense project proceed with the social benefits project to ensure consistent liability recognition criteria.

ACAG also seeks clarification whether payments by grantors under social benefit bonds (also called social impact bonds) that relate to the future reduction for the need for universally accessible

services (e.g. initiatives to reduce diabetes and the need for hospitalisation and medical costs) are within the scope of universally accessible services or the social benefit carve-out.

Preliminary View 7

The IPSASB is of the view that where grants, contributions and other transfers contain either performance obligations or stipulations they should be accounted for using the PSPOA which is the counterpart to the IPSASB's preferred approach for revenue.

Do you agree with the IPSASB's Preliminary View 7? If not, please give reasons

ACAG suggests that greater clarity is provided regarding the approach suggested by IPSASB. ACAG supports the Non-Exchange Expenses project considering the PSPOA, subject to the criteria of the conceptual framework being met.

ACAG does not necessarily agree with the mirror approach as an expected means of accounting in all circumstances, as a wholesale approach. Whilst mirror accounting may be the appropriate outcome in certain scenarios, this is not necessarily true in all instances. In particular, ACAG believes that consideration should be given to situations where the funds provided by the entity to external parties (i.e. the service provider) for goods and services to then be provided to other external parties (i.e. the public) represent assets of the reporting entity.

ACAG also considers that accruing by grantors for partially completed up-front grants to service providers is likely to be difficult to apply in practice.

Preliminary View 8

The Board considers that at initial recognition, non-contractual receivables should be measured at face value (legislated amount) of the transaction(s) with any amount expected to be uncollectible identified as an impairment.

Do you agree with the IPSASB's Preliminary View 8? If not, please give reasons

ACAG conceptually agrees with IPSASB Preliminary View 8. ACAG believes that non-contractual receivables should be recognised at the amount entitled to be collected under the relevant legislation, less any uncollectible amounts. ACAG notes that in practice there are often amounts that are uncollectible (e.g. incorrect or old addresses), or not pursued for mainly for social policy reasons.

Preliminary View 9

The IPSASB considers that subsequent measurement of non-contractual receivables should use the fair value approach.

Do you agree with the IPSASB's Preliminary View 9? If not, please give reasons

ACAG believes that the principles underpinning the cost approach—as outlined in paragraphs 7.33 and 7.34, would be appropriate given the nature of non-contractual receivables. As this approach effectively carries non-contractual receivables at the amount expected to be collected and it reflects the nature of these receivables. ACAG suggests where the time value of money would be relevant, the government should be discounting the amount. ACAG would suggest that the 'rate' issue is

readily resolved by reference to the rate used for other present value calculations e.g. employee benefits.

ACAG also recommends that provisions or guidance be included in relation to the assessment of valuation for individual receivables versus a portfolio.

Specific Matter for Comment 7
For subsequent measurement of non-contractual payable do you support: (a) Cost of Fulfilment Approach; (b) Amortized Cost Approach; (c) Hybrid Approach; or (d) IPSAS 19 requirements. Please explain your reasons.

ACAG supports Approach 1 Cost of Fulfilment Approach on the basis that it is consistent with the Conceptual Framework and is therefore relatively straightforward for both preparers and users to understand. This approach is also embedded in other standards and therefore it is an approach that provides for internal consistency and is familiar to both preparers and users.

Additional matters IPSASB may want to consider that are not currently covered in the consultation paper:

1. How to account for goods or services where the value of the goods or services is significantly more or less than the consideration paid or received?
2. How to account for variable inputs under PSPOA e.g. obligation is to provide goods or services to pensioners subject to a means test?
3. How to account for arrangements where service delivery obligations are also subject to payment conditions that are not performance obligations to customers? So for example, there is a service delivery obligation agreement whereby the government will pay entity A to provide specified services to customers, however payment to entity A is subject to entity A meeting certain performance standards which will be assessed by government.