

International Public Sector Accounting Standards Board
Mr Ian Carruthers, IPSASB Chair
and Mr John Stanford, IPSASB Deputy Director
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Dear Mr Carruthers, dear Mr Stanford,

Consultation Paper on Accounting for Revenue and Non-Exchange Expenses

We are pleased to respond to the invitation from the International Public Sector Accounting Board (IPSASB) to comment on Consultation Paper on Accounting for Revenue and Non-Exchange Expenses (the Consultation Paper) on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of those firms that commented on the Exposure Draft. “PricewaterhouseCoopers” or ‘PwC’ refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We support the work the IPSASB undertakes to develop high-quality accounting standards for use by governments and other public sector entities around the world with the aim of enhancing the quality, consistency and transparency of public sector financial reporting worldwide.

The Consultation Paper on Accounting for Revenue and Non-Exchange Expenses is particularly welcome for the following reasons: it will fill one of the most important remaining gaps in the suite of IPSAS standards by providing accounting guidance on non-exchange expenses, which represent major transaction flows in the public sector, it will address practical issues in accounting for revenue from exchange and non-exchange transactions and it will enhance convergence with IFRS for those transactions that are similar in substance to those entered into by private companies.

We agree with IPSASB’s proposal to categorise revenue into three categories - (A) transactions with no performance obligations or stipulations (B) transactions with performance obligations or stipulations which do not have all the characteristics of a transaction in the scope of IFRS 15 and (C) transactions that meet the definitions and scope of IFRS 15 - and for category B transactions to recognise revenue following a five-step approach based on the fulfilment of performance obligations and that considers the specific characteristics of the public sector. In line with our

more detailed comments and given the proposed differences in accounting models, we wish to reinforce the importance of delineating those categories in mutually exclusive while complete scopes.

We also agree with the proposal to recognise expenses from grants, contributions and other transfers under the public sector performance obligation approach which mirrors the accounting treatment for revenue of a similar nature.

We recommend that the IPSASB clearly articulates to what extent the proposals reconcile with the provisions of the Conceptual Framework, including the definition of elements and the accountability and decision-making objectives of financial statements.

The subject-matter is complex. We therefore strongly recommend to provide sufficient practical guidance and illustrative examples in order to enhance consistency in application of the proposed approaches.

If you would like to discuss any of these points in more detail, please contact Henry Daubeney ((+44) 20 7804 2160), Patrice Schumesch ((+32) 2 710 40 28) or Sebastian Heintges ((+49) 69 9585 3220).

Yours sincerely,

A handwritten signature in cursive script, likely representing a member of the PricewaterhouseCoopers team.

PricewaterhouseCoopers

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| Responses to the questions in IPSASB's Consultation Paper on Accounting for Revenue and Non-Exchange Expenses |
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1. Preliminary view 1 (following paragraph 3.8)

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 your reasons.

We agree to replace IPSAS 9 'Revenue from Exchange Transactions' and IPSAS 11 'Construction contracts' with a new standard primarily based on the new IFRS standard 'IFRS 15 Revenue from Contracts with Customers'. For transactions entered into by public sector entities that are similar in substance to transactions entered into by private companies and that fall under the scope of IFRS 15 (i.e. Category C transactions in the Consultation Paper), it is appropriate to adopt accounting rules that are aligned on IFRS 15. This is fully in line with IPSASB's strategy to adopt accounting standards that converge with IFRS when no specific public sector characteristic needs to be taken into account.

2. Preliminary view 2 (following paragraph 3.9)

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 your reasons.

We agree with IPSASB's proposal to address the accounting treatment of revenue transactions that do not contain performance obligations or stipulations (i.e. Category A transactions in the Consultation Paper, for example taxes and transfers) in an updated IPSAS 23 'Revenue from Non-Exchange Transactions (Taxes and Transfers)'.

Clear and detailed guidance should be provided on whether a transaction falls under either Category A or Category B (as referred to in the CP).

The substance of the transaction rather than its form needs to drive the accounting treatment. In this context, we note that para. 3.3 (a) refers to general taxation receipts and inter-governmental transfers, such as non-specific and non-earmarked grants. Certain revenue sources may however appear to be earmarked (e.g. because they are labelled as "contributions to" or "charges for" a

particular service), but in substance they may constitute a general tax on income or tax on another phenomena. In some circumstances, they might in-substance create a performance obligation or stipulations on the entity and therefore fall into Category B or even C. In other circumstances, they might in substance even be social benefit contributions and therefore must be considered appropriately in the forthcoming IPSAS standard on social benefits. Robust criteria need to be developed to assist in the classification by preparers.

3. Specific Matter for Comment 1 (following paragraph 3.10)

Please provide details of the issues 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 provide 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.

We concur with the view that additional guidance should be provided in an updated version of IPSAS 23 on social contributions and taxes with long collection periods.

In terms of additional areas where we believe the IPSASB should provide additional guidance, we identified the following:

- Clarify the importance (or lack thereof) of past practices when assessing conditions on transferred assets and restrictions that are set, for example, between a government and a controlled entity. In the separate financial statements of the controlled entity, we have experienced debates in determining the substance of such stipulations given the power of the government over the entity and the absence of precedents where transfer assets were returned to the government (as original transferor).
- Determine whether stipulations under the new guidance would need to represent incremental obligations for the recipient entity as opposed to reinforcing obligations otherwise already present in the recipient entity's constituting mandate.
- Provide guidance on how to account for revenue that has the legal form of a tax but is really a payment for goods or services (e.g. water rates).
- Clarify whether granting of licences is licence revenue, a tax or revenue for the delivery of goods and services and under what circumstances.
- Explain how government appropriations should be accounted for. See also the example developed under SMC 3.
- Clarify how property rates should be accounted for (at one point in time or over time) and under what circumstances.

4. Preliminary view 3 (following paragraph 4.64)

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 your reasons.

We agree with IPSASB's proposal to account for transactions with performance obligations or stipulations which do not have all the characteristics of a transaction in the scope of IFRS 15 (i.e. Category B in the Consultation Paper) using the Public Sector Performance Obligation Approach (PSPOA). This approach would build on the five-step performance obligation approach of IFRS 15 but would be adapted for the public sector environment. Given the early stages of this project, we would encourage the IPSASB to further define the types of transactions within Category B and provide examples of application of the PSPOA to these transactions. This will enable IPSASB stakeholders to better assess the practical application of the PSPOA to typical transactions falling within Category B.

We recommend that the IPSASB clearly articulates to what extent the proposals reconcile with the provisions of the Conceptual Framework, including the definition of elements and the accountability and decision-making objectives of financial statements. This is particularly important given the tension between the balance sheet (specifically the definition of a liability in the Conceptual Framework) and the statement of financial performance (especially to provide performance information which is meaningful for the decision making).

5. Specific Matter for Comment 2 (following paragraph 4.64)

The IPSASB has proposed broadening the requirements to 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 (paragraphs 4.29-4.35);

Step 2 - Identify the performance obligation (paragraphs 4.36-4.46);

Step 3 - Determine the consideration (paragraphs 4.47-4.50);

Step 4 - Allocate the consideration (paragraphs 4.51-4.54); and

Step 5 - Recognise revenue (paragraphs 4.55-4.58).

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

If not, please explain your reasons.

We agree that the way to interpret the five steps included in IFRS 15 should be broadened to appropriately take into account the specific characteristics of the public sector. In particular:

- For step 1, we support the view that determination of whether an obligation exists should not be limited to the analysis of contractual arrangements but should also consider binding arrangements (i.e. enforceable agreements).

- For step 2: we agree that revenue should be recognised in accordance with the PSPOA when (or as) the public sector entity fulfils its performance obligations rather than based on the transfer of promised goods and/or services. This would e.g. cover arrangements where third parties receive the benefits resulting from those performance obligations, rather than the resource provider directly.
- For step 5: we agree that the principles set out in step 5 of IFRS 15 be adapted to public sector transactions. In our view, the application of this particular step to Category B transactions remains unclear, especially when there are no performance obligations and only stipulations. It is hard to understand what is meant by “when (or as) the public sector entity fulfils its performance obligations” (see paras 4.56-58). Therefore, the IPSASB must develop robust criteria to determine the principle of “fulfilling a performance obligation”.

Given the complexity of the topic and the wide range of transactions that fall into Category B in the CP, we strongly recommend that the IPSASB develops detailed guidance and illustrative examples about the principles to be applied for each step in order to enhance consistency in the accounting treatment of similar transactions under similar circumstances.

6. Specific Matter for Comment 3 (following paragraph 4.64)

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.

We do not support Approach 1 but Approach 2, i.e. recognising revenue following the PSPOA for transactions falling under Category B of the CP. We refer to our response to Preliminary View 3.

We agree that the current IPSAS 23 treatment of transfers with time requirements (and no other stipulations), i.e. revenue recognition by the resource recipient when the transfers are receivable, might not provide useful information about the period over which the resources will be used.

Selecting one of the proposed options, for example option (d) (using the concept of ‘other obligations’) might be a response to the above concern. Instead of directly choosing option (b), (c), (d) or (e) if Approach 1 is selected, we however invite the IPSASB to further investigate a spectrum of cases that are encountered in practice starting with transfers with time requirements and clearly no stipulations, finishing with transfers with time requirements and clear stipulations and including in between transfers with time requirements and where it is unclear whether a stipulation exists.

We would encourage investigating whether a wide interpretation of the concept of stipulation might lead to more transactions being classified in category B and therefore adequately respond to the issue raised concerning the current IPSAS 23 treatment of transfers with time requirements.

Again here we encourage to provide illustrative examples for the different types of situations that may exist.

In particular, we would welcome that the IPSASB provides guidance on the accounting treatment of a transfer to one public sector entity that is voted before the year end (in year X-1) but is intended to fund the budget of the following year (in year X). An intuitive accounting treatment would consider linking revenue for the recipient with the costs the transfer intends to compensate (in year X). An interesting analysis would be to analyse what might constitute a stipulation (also interpreting it in the broad sense) therefore leading to a classification in Category B, which would allow revenue recognition in year X.

In the same way, detailed practical guidance and illustrated examples would be welcome for multiyear grants and transfers, especially to clarify those situations where it can be interpreted that a stipulation exists and that revenue should be recognised over several periods.

7. Specific Matter for Comment 4 (following paragraph 4.64)

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

a) Yes.

b) No.

Please explain your reasons.

We refer to our response to SMC 3 above.

Should Approach 1 be retained, we believe that additional guidance should be given on making the distinction between exchange and non-exchange transactions. In practice the terms ‘directly’ and ‘approximately equal value’, which are included in the definitions of exchange and non-exchange transactions, may be difficult to interpret in certain situations. Additional guidance on this issue is needed.

8. Preliminary view 4 (following paragraph 5.5)

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 your reasons.

We agree that the IPSASB should explicitly address the accounting for capital grants within IPSAS to ensure consistency in application.

9. Specific Matter for Comment 5 (following paragraph 5.5)

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.

There is currently no specific guidance about the pattern of revenue recognition when dealing with the accounting of capital grants. This situation creates diversity in application depending on whether the grant agreement includes restrictions and/or conditions as defined by the current IPSAS 23. We therefore agree that the pattern of revenue recognition is the main issue to be addressed. Some of the matters identified under SMC 1 illustrate those challenges.

Under the IFRS equivalent IAS 20 'Government Grants and Disclosure of Government Assistance' revenue is recognised in the statement of financial performance on a systematic basis over the useful life of the asset financed by the grant or as an offset to the depreciation expense. Mirroring this accounting treatment would conflict with the IPSASB Conceptual Framework when no conditions are linked to the grant as revenue would be recognised over time while no obligation exists. It would however provide useful information about the period over which the resources will be used. We recommend that the IPSASB investigates this issue, following a similar reasoning to the one suggested in our response to SMC 3.

10. Specific Matter for Comment 6 (following paragraph 5.9)

Do you consider that the 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.

Recognition of services in-kind that enhance service delivery capacity is useful for accountability and decision-making purposes. In our view, the IPSASB should follow approach b) and revise the existing requirements, whereby the individual circumstances in conjunction with application of the IPSASB's Conceptual Framework should dictate the accounting treatment.

When services in-kind fulfil the criteria for asset recognition, IPSASB should require they be recognised as an asset (and a corresponding donation recognised in accordance with the terms of the arrangement). Unless the entity has control of the donated service (i.e. it has recourse if the service is not delivered) it would not be able to recognise an asset. Such services in-kind would be most appropriately accounted for by recognising an expense and a corresponding revenue as and when they are delivered. In terms of financial reporting of service delivery (comparability and relevant information as to the value of services) there is in substance no difference between donated time and paid time.

We however acknowledge that measurement of some types of services in-kind may be difficult in practice. So the requirement to recognise services in-kind in IPSAS financial statements would go along with the ability to measure them in a way that achieves the qualitative characteristics and takes account of the constraints on information.

Appropriate disclosure about the treatment services in-kind should be required in any case if these are material to the public sector entity.

11. Preliminary view 5 (following paragraph 6.37)

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 your reasons.

We concur with the view that non-exchange transactions related to both universally accessible services and collective services do not impose performance obligations on the resource recipient. They should therefore be accounted for using the Extended Obligating Event Approach.

For clarity, we presumed that the question covered both transactions without performance obligations and also without stipulations (consistent with paragraph 6.36 of the CP).

12. Preliminary view 6 (following paragraph 6.39)

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 your reasons.

We agree that resources linked to non-exchange transactions for universally accessible services and collective services should be expensed as services are delivered as no related obligating event exists.

13. Preliminary view 7 (following paragraph 6.42)

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 your reasons.

We agree with the IPSASB that the approach taken for grants, contributions and other transfers given, which are non-exchange expenses, should mirror the accounting treatment adopted for equivalent revenue transactions.

Transfers between entities that are part of the same consolidation scope are frequent in the public sector. Mirroring the accounting treatment for similar non-exchange revenue does not only makes sense from a conceptual point of view but it should also facilitate elimination of inter-government balances and transactions in the consolidation process.

We therefore support IPSASB's proposal to apply the PSPOA for grants, contributions, and other transfers given and that contain either performance obligations or stipulations. The five-step revenue recognition approach should be reconfigured from the perspective of the resource provider.

14. Preliminary view 8 (following paragraph 7.18)

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 your reasons.

We agree with IPSASB's preliminary view to measure non-contractual receivables initially at face value (legislated amount) of the transaction and record any amount expected to be uncollectible as an impairment. This accounting treatment enhances transparency and accountability as to the collection of public money.

15. Preliminary view 9 (following paragraph 7.34)

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 your reasons.

We agree that non-contractual receivables should be subsequently measured at fair value.

16. Specific Matter for Comment 7 (following paragraph 7.46)

For subsequent measurement of non-contractual payables do you support:

- a) Cost of Fulfilment Approach;**
- b) Amortised Cost Approach;**
- c) Hybrid Approach; or**
- d) IPSAS 19 requirements?**

Please explain your reasons.

We recommend to adopt the hybrid approach for the subsequent measurement of non-contractual payables. By analogy to the accounting treatment of financial liabilities, we believe that the amortised cost approach should be applied to non-contractual payables that are certain in timing and amount. If however cash flows are uncertain in timing and amount, the cost of fulfilment approach should be adopted.