

INTRODUCTION TO IPSAS



Revenues

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Introduction to Revenues

Revenue

Information on revenues is important in assisting users to assess the financial condition and performance of public sector entities. Comparing revenues with expenses helps users to assess whether current revenues are sufficient to cover the costs of programs and services provided in the current period. Information on revenues is also important to the assessing the impact of taxation and other revenues on the economy or the need for borrowing in the long- term. The material in this module identifies and discusses the definition and the issues arising in reporting revenues that result from the unique types and nature of public sector revenues.

Public sector entities have some revenues which have exact equivalents in the for-profit sector and which can, under full accrual basis of accounting, be given the same accounting treatment. For example, public sector entities may have revenue from sales of goods and services, interest and dividends. In these transactions, the consideration exchanged is approximately of equal value to the goods and services received. However, the majority of governmental revenues are non-reciprocal transfers such as taxes, fees, duties, and fi es obtained through the exercise of the sovereign powers.

The existence of an exchange relationship in non- reciprocal transfers is tenuous. While it could be argued that a government receives taxation revenues in return for goods and services, (e.g. roads, health care, education, law enforcement, defense, etc.), the citizens who pay for the services are not necessarily the beneficiaries of them. Payment of tax does not necessarily entitle the taxpayer to an equivalent value of services or benefits.

This module focuses on requirements of [IPSAS 9, Revenue from Exchange Transactions](#) and [IPSAS 23, Revenue from Non-Exchange Transactions \(Taxes and Transfers\)](#).

Specific topics include:

- [Scope of standards](#)
- [Definitions](#)
- [Recognition and measurement of revenues](#)
- [Recognition of transfers with stipulations and conditions](#)
- [Expenses paid through the tax system and tax expenditures](#)

Learning Objective

- IPSAS 9, *Revenue from Exchange Transactions*
- IPSAS 23, *Revenue from Non-Exchange Transactions*
- At the end of this session you are able to
 - distinguish between exchange and non-exchange revenues
 - apply the requirements for identification, recognition and measurement of revenues
 - apply the presentation and disclosure requirements for reporting revenues

Common types of revenue for public sector entities include:

Non-exchange revenues: (IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)*)

- (i) Direct and indirect taxes;
- (ii) Duties;
- (iii) Fees and fines; and
- (iv) Other non-reciprocal transfers.

Exchange revenues: (IPSAS 9, *Revenue from Exchange Transactions*)

- (i) Sales of goods or services;
- (ii) Dividends;
- (iii) Interest; and
- (iv) Net gains arising from the sale of assets.

Gains:

- (i) Increases in fair value of financial instruments; (IPSAS 29, *Financial Instruments: Recognition and Measurement*)
- (ii) Foreign exchange gains; (IPSAS 4, *The Effects of Changes in Foreign Exchange Rates*) and
- (iii) Other gains. (for example, gains on sale of assets under IPSAS 17, *Property, Plant and Equipment*) (Study 14, chapter 8, page 167, paragraph 8.2)

Module focus on requirements of IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)*. Most public sector entities will have some form of non-exchange revenue, and for many, it will be their main source of revenue. Emphasis is placed on recognition of revenues from non-exchange transactions because this is one area that is likely to cause a significant change when entities are transitioning to a full accrual basis of accounting.

- IPSAS 9, *Revenue from Exchange Transactions* prescribes the accounting treatment of revenue arising from exchange transactions and events
- IPSAS 23, *Revenue from Non-Exchange Transactions* prescribes requirements for the financial reporting of revenue arising from non-exchange transactions.

At the end of this session participants are able:

- To distinguish between exchange and non-exchange revenues and understand the impact this has on accounting and reporting of revenues;
- To apply the requirements for identification, recognition and measurement of revenues.
- Are able to apply the presentation and disclosure requirements for reporting revenues.

Definition of Revenue

- Gross inflow of economic benefits or service potential resulting in increases in net assets/equity
- Excludes contributions from owners
- All items of revenue included in surplus or deficit for the period
- Excludes amounts collected as an agent and financing inflows
- When collection not probable, expense recognized

Background:

- Revenue is the gross inflow of economic benefits or service potential during the reporting period when those inflows result in increases in net assets/equity
- Revenue excludes increases in net assets/equity relating to contributions from owners.
- All items of revenue recognized in a period shall be included in surplus or deficit, unless an IPSAS requires otherwise.

Normally, all items of revenue recognized in a period are included in surplus or deficit. However, circumstances may exist when particular items may be excluded from surplus or deficit for the current period.

IPSAS 3, Accounting Policies, Changes in Accounting Estimates and Errors deals with two such circumstances: the correction of errors and the effect of changes in accounting policies. Other examples include revaluation increases and decreases and particular foreign exchange differences to be recognized directly as changes in net assets/equity.

- Amounts collected as an agent do not give rise to an increase in net assets or revenue

Revenue includes only the gross inflows of economic benefits or service potential received and receivable by the entity on its own account. Amounts collected as an agent of the government or another government organization or on behalf of other third parties; for example, the collection of telephone and electricity payments by the post office on behalf of entities providing such services are not economic benefits or service potential that flow to the entity, and do not result in increases in assets or decreases in liabilities. This is because the agent entity cannot control the use of, or otherwise benefit from, the collected assets in the pursuit of its objectives. Therefore, they are excluded from revenue.

An entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that an entity is acting as an agent is that the amount the entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer. For example, the entity does not have:

- a) the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer;
- b) inventory risk before or after the customer order, in shipping or on return;
- c) discretion in establishing prices, either directly or indirectly, for example by providing additional goods or services;
- d) customer's credit risk.

Similarly, in a custodial or agency relationship, the gross inflows of economic benefits or service potential include amounts collected on behalf of the principal that do not result in increases in net assets/equity for the entity. The amounts collected on behalf of the principal are not revenue. Instead, revenue is the amount of any commission received, or receivable, for the collection or handling of the gross flows.

- Financing inflows are not revenues because they have no impact upon net assets/equity (affect asset and liability only)

Financing inflows, notably borrowings, do not meet the definition of revenue because they (a) result in an equal change in both assets, and liabilities and therefore (b) have no impact upon net assets/equity. Financing inflows are taken directly to the statement of financial position and added to the balances of assets and liabilities.

- The amount of revenue recognized for which recovery has ceased to be probable, is recognized as an expense, rather than as an adjustment of the amount of revenue originally recognized.

Revenue is recognized only when it is probable that the economic benefits or service potential associated with the transaction will flow to the entity. However, when an uncertainty arises about the collectability of an amount already included in revenue, the uncollectable amount, or the amount in respect of which recovery has ceased to be probable, is recognized as an expense, rather than as an adjustment of the amount of revenue originally recognized.

Illustrative Example

Scenario:

A municipality collects education property taxes on behalf of the state. During the year it billed residential and commercial property taxes of CU 1,116,644 million. Of that amount, CU 527,442 was billed on behalf of the state.

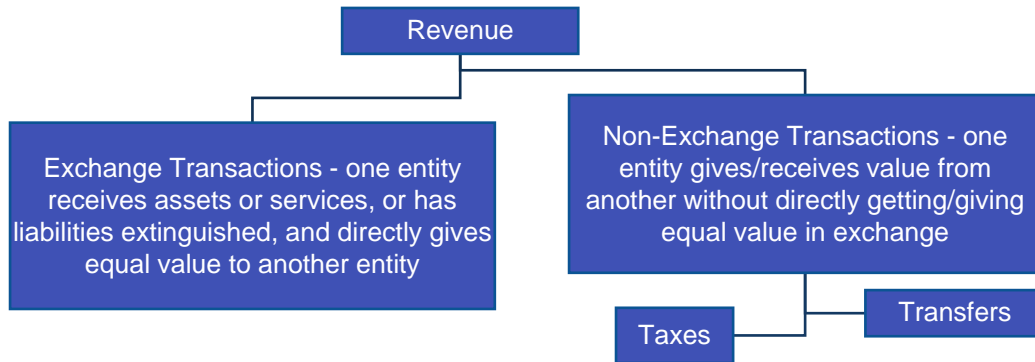
How much would it report as revenue for the fiscal period from property taxes? Explain.

- a) CU 1,116,644
- b) CU 589,202.

Answer:

The answer is (b). The property taxes billed on behalf of the state does not result in gross inflows of economic benefits or service potential by the entity on its own account. Amounts collected as an agent of the state are not economic benefits or service potential that flow to the municipality, and do not result in increases in its assets or decreases in liabilities. This is because the municipality cannot control the use of, or otherwise benefit from, the collected assets in the pursuit of its objectives. Therefore, they are excluded from revenue.

Types of Revenue



Public sector entities may derive revenues from exchange or non-exchange transactions.

Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

Applies to:

- a) rendering of services;
- b) sale of goods including the sale of land and other property held for resale; and
- c) use by others of entity assets yielding interest, royalties, and dividends or similar distributions.

Rendering of services typically involves the performance by an entity of an agreed task over an agreed period of time. The services may be rendered within a single period, or over more than one period. Examples of services rendered by public sector entities may include the provision of housing, management of water facilities, management of toll roads, and management of transfer payments.

Goods include:

- a) Goods produced by the entity for the purpose of sale, such as publications, and
- b) Goods purchased for resale, such as merchandise or land and other property held for resale.

The use by others of entity assets gives rise to revenue in the form of:

- a) Rent – The lease of property, plant, and equipment at market rates (other than those under lease
- b) Interest – charges for the use of cash or cash equivalents, or amounts due to the entity;
- c) Royalties – charges for the use of long-term assets of the entity, for example, patents, trademarks, copyrights, and computer software; and
- d) Dividends or equivalents – distributions of surpluses to holders of equity investments in proportion to their holdings of a particular class of capital.

Non-exchange transactions are transactions that are not exchange transactions.

In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange or gives value to another entity without directly receiving approximately equal value in exchange.

Examples of non-exchange transactions are:

- a) Taxes; and
- b) Transfers (whether cash or noncash), including grants, debt forgiveness, fines, bequests, gifts, donations, goods and services in-kind, and the off-market portion of concessionary loans received.

Taxes are economic benefits or service potential compulsorily paid or payable to public sector entities, in accordance with laws and/or regulations, established to provide revenue to the government. Taxes are the major source of revenue for many governments and other public sector entities. A government levies taxation on individuals and other entities, known as taxpayers, within its jurisdiction by use of its sovereign powers. Taxes satisfy the definition of non-exchange transaction because the taxpayer transfers resources to the government, without receiving approximately equal value directly in exchange. While the taxpayer may benefit from a range of social policies established by the government, these are not provided directly in exchange as consideration for the payment of taxes.

Taxes do not include fines or other penalties imposed for breaches of the law. Noncompulsory transfers to the government or public sector entities such as donations and the payment of fees are not taxes, although they may be the result of non-exchange transactions. Advance receipts, being amounts received in advance of the taxable event, may also arise in respect of taxes.

Transfers are inflows of future economic benefits or service potential from non-exchange transactions, other than taxes. Transfers include grants, debt forgiveness, fines, bequests, gifts, donations, and goods and services in-kind.

Transfers have the common attribute that they transfer resources from one entity to another without providing approximately equal value in exchange and are not taxes as defined. If an agreement stipulates that the recipient entity is to provide approximately equal value in exchange, the agreement is not a transfer agreement, but a contract for an exchange transaction that should be accounted for under IPSAS 9.

There is a further group of non-exchange transactions where the entity may provide some consideration directly in return for the resources received, but that consideration does not approximate the fair value of the resources received. For example, an entity receives a loan from another entity, but only is required to repay a portion.

There are also additional transactions where it is not immediately clear whether they are exchange or non-exchange transactions. In these cases an examination of the substance of the transaction will determine if they are exchange or non-exchange transactions.

Governments may charge for goods and services provided to other entities or directly to members of the public. The sale of goods is normally classified as an exchange transaction. In some cases, a government will charge a price for goods or services which does not relate to the cost of providing the goods or services or does not relate to the price a recipient is willing to pay. For example, a government may provide goods and services at a price which is well below cost. The government may be subsidizing the consumer in order to meet other economic or social objectives. Because a government has the ability to raise taxes, it can continue in operation even when expenses exceed non-tax revenues.

If the transaction is conducted at a subsidized price, that is, a price that is not approximately equal to the fair value of the goods or services sold, that transaction falls within the definition of a non-exchange transaction that is accounted for in accordance with IPSAS 23.

In determining whether the substance of a transaction is that of a non-exchange or an exchange transaction professional judgment is exercised. An entity may receive trade discounts, quantity discounts, or other reductions in the quoted price of assets for a variety of reasons. These reductions in price do not necessarily mean that the transaction is a non-exchange transaction.

Recognizing Non-Exchange Transactions

- Analyze non-exchange transactions
 - Do resource inflows meet definition and criteria for recognition of an asset
 - Is there a performance obligation that requires recognition of a liability
- Measured at the amount of increase in net assets
- Inflow is probable and fair value is measurable
- Outflow is probable and amount estimable

There are two different approaches to revenue recognition under IPSAS 9 and IPSAS 23. IPSAS 9 takes an earnings approach whereby revenue is recognized when it is earned. IPSAS 23 takes a performance obligation approach. Under IPSAS 23 revenue is recognized when the entity has satisfied the performance obligations associated with the non-exchange revenue.

IPSAS 23 requires that:

- a) entities analyze inflows of resources from non-exchange transactions to determine if they meet the definition of an asset and the criteria for recognition as an asset;
- b) if the inflows result in recognition of an asset, entities determine whether a performance obligation is created that requires a liability to be recognized;
- c) assets recognized initially be measured at their fair value as at the date of acquisition;
- d) liabilities recognized as a result of a non-exchange transaction be recognized in accordance with the principles established in IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*;
- e) revenue equal to the increase in net assets associated with an inflow of resources be recognized.

An entity will recognize an asset arising from a non-exchange transaction when it gains control of resources that meet the definition of an asset and satisfy the recognition criteria.

In certain circumstances, such as when a creditor forgives a liability, a non-exchange transaction results in de-recognition of a liability. Both will result in an increase in the net assets/equity of the entity and recognition of revenue.

The ability to exclude or regulate the access of others to the benefits of an asset is an essential element of control. An entity has control of resources when it can exclude access to them by the transferor. The entity will need to establish enforceability of its control of resources before it can recognize an asset.

Many arrangements to transfer resources become binding on all parties before the transfer of resources takes place. However, only when (a) a claim is enforceable, and (b) the entity assesses that it is probable that the inflow of resources will occur, will assets, liabilities, and/or revenue be recognized. Until that time, the entity cannot exclude or regulate the access of third parties to the benefits of the resources proposed for transfer.

An announcement of an intention to transfer resources to a public sector entity is not of itself sufficient to identify resources as controlled by a recipient. An entity will need to establish enforceability of its control of resources before it can recognize an asset.

Enforceability may be contained in legislation or in binding agreements. Generally governing legislation or regulations identify specific eligibility criteria that recipients must meet to be entitled to receive a transfer. Once those criteria have been met, the recipient is entitled to receive the transfer and the transferor must make the transfer to all entities who meet the specified eligibility criteria. Once an entity meets the eligibility criteria under the legislation or binding agreement, it may have enforceable control of resources.

For example, the terms of shared cost agreements are usually negotiated and agreed upon in the signed contract. The transferor may agree to pay for all or only a portion of the eligible expenditures. There may be a ceiling on the total amount that will be shared.

Under shared cost agreements the recipient is entitled to a transfer of resources once it has incurred eligible expenditures. At the point when the recipient makes eligible expenditures under the agreement it controls the resources that the transferor has agreed to share pursuant to the shared cost agreement. Under the agreement, the government must reimburse the recipient for the specified percentage of those eligible expenditures.

An inflow of resources from a non-exchange transaction, other than services in-kind, that meets the definition of an asset is recognized as an asset when, and only when:

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

An inflow of resources is probable when the inflow is more likely than not to occur. The entity bases this determination on its past experience with similar types of flows of resources and its expectations regarding the taxpayer or transferor. The degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition.

For example, where (a) a government agrees to transfer funds to a public sector entity (reporting entity), (b) the agreement is binding, and (c) the government has a history of transferring agreed resources, it is probable that the inflow will occur, notwithstanding that the funds have not been transferred at the reporting date.

An asset acquired through a non-exchange transaction is initially measured at its fair value at the acquisition date. Fair value most faithfully represents the actual value the public sector entity accrues as a result of the transaction.

The IPSASB is of the view that this is appropriate to reflect the substance of the transaction and its consequences for the recipient. In an exchange transaction, the cost of acquisition is a measure of the fair value of the asset acquired. However, by definition, in a non-exchange transaction the consideration provided for the acquisition of an asset is not approximately equal to the fair value of the asset acquired.

The recognition and measurement of assets at fair value is consistent with other IPSASs. Inventories, property, plant, equipment, or investment property acquired through non-exchange transactions are to be initially measured at their fair value as at the date of acquisition, in accordance with the requirements of IPSAS 12, *Inventories* and IPSAS 16, *Investment Property*. Initial measurement of assets acquired through non-exchange transactions at their fair value is consistent with the approach taken in IPSAS 17, *Property, Plant and Equipment*, for assets acquired at no cost or for a nominal cost. Financial instruments, including cash and transfers receivable that satisfy the definition of a financial instrument, and other assets, will also be measured at fair value as at the date of acquisition in accordance with IPSAS 29, *Financial Instruments; Recognition and Measurement* (or IPSAS 41, *Financial Instruments* when that IPSAS is applied).

Transfers include services in-kind. Services in-kind are services provided by individuals or entities to public sector entities in a non-exchange transaction. These services meet the definition of an asset because the entity controls a resource from which future economic benefits or service potential are expected to flow to the entity. These assets are, however, immediately consumed, and a transaction of equal value is also recognized to reflect the consumption of these services in-kind. Due to the many uncertainties surrounding services in-kind, including the ability to exercise control over the services, and measuring the fair value of the services, entities may, but are not required, to recognize services in-kind. Entities are encouraged to disclose the nature and type of services in-kind received during the reporting period.

When, as a result of a non-exchange transaction, an entity recognizes an asset, it also recognizes revenue equivalent to the amount of the asset unless it is also required to recognize a liability. If an entity is required to recognize a liability, the difference between the amount of the asset and the amount of the liability is the increase in net assets resulting from the non-exchange transaction. When an entity recognizes an increase in net assets as a result of a non-exchange transaction, it recognizes revenue.

Revenue from non-exchange transactions is measured at the amount of the increase in net assets recognized by the entity.

A present obligation is a duty to act or perform in a certain way and may give rise to a liability in respect of any non-exchange transaction. Present obligations may be imposed by stipulations on how resources are to be used in laws or regulations or binding arrangements establishing the basis of transfers. They may also arise from the normal operating environment, such as the recognition of advance receipts.

As an entity satisfies a present obligation recognized as a liability in respect of an inflow of resources from a non-exchange transaction recognized as an asset, it will reduce the carrying amount of the liability recognized and recognize an amount of revenue equal to that reduction.

When a liability is subsequently settled, the amount of the reduction in the liability will be recognized as revenue.

The recognition criteria for a liability are the same as the general recognition criteria under IPSAS 19, *Provisions, Contingent Liabilities and Contingent Assets*.

A present obligation arising from a non-exchange transaction that meets the definition of a liability is recognized as a liability when, and only when:

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

The estimate takes account of the risks and uncertainties that surround the events causing the liability to be recognized.

Accounting for Announcement

Scenario:

A senior level of government has made an announcement that it will include additional operating funds in its next budget for local housing authorities to allow them to increase subsidies to low income families.

Do local housing authorities have an inflow of resources that meet the definition of an asset as a result of the announcement? Explain.

Answer:

Local housing authorities do not have an enforceable claim against the senior government that gives them control over the resource.

An announcement of an intention to transfer resources to local housing authorities is not of itself sufficient to identify resources as controlled by the housing authorities. There does not appear to be legislation in place. That is, there is no appropriations act or other authority for the senior government to make the transfer. The government announcement is not specific such that it creates a valid expectation among the local housing authorities that the senior government will fulfill its obligation. The announcement does not, for example identify;

- a) specific local housing authorities that will receive additional funding
- b) the amount of the additional funding
- c) the time period over which the funding will be provided.

Discussion and Questions

That concludes our introduction to revenue. Participants should refer to the review questions to test themselves on their knowledge.

Visit the IPSASB webpage.

<http://www.ipsasb.org>

Review Questions

Question 1

A local government bills and collects property taxes on behalf of a state government for education purposes. The local government remits taxes collected to the state government on a quarterly basis based on the tax rate set by the state and property assessed values. The local government charges back for any uncollectible education taxes.

Is the education tax revenue of the local government?

Answers to Review Questions

Question 1

Education taxes billed and collected on behalf of the state government are not revenues of the local government. Revenue includes only the gross inflows of economic benefits or service potential received and receivable by the entity on its own account. Amounts collected as an agent of the government or another government organization or on behalf of other third parties are not economic benefits or service potential that flow to the local government, and do not result in increases in assets or decreases in liabilities. This is because the local government cannot control the use of, or otherwise benefit from, the collected assets in the pursuit of its objectives. The local government is not exposed to significant credit risk. Therefore, they are excluded from revenue.

Revenue from Exchange Transactions

Accounting for Exchange Transactions – IPSAS 9

As noted, exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

Applies to:

- a) rendering of services;
- b) sale of goods including the sale of land and other property held for resale; and
- c) use by others of entity assets yielding interest, royalties, and dividends or similar distributions.

Recognition and Measurement

- Revenue recognized from
 - Rendering of services on percentage completion method
 - Sale of goods when significant risks and rewards of ownership and effective control transferred
 - Interest on time proportion basis using effective yield
 - Royalties as earned
 - Dividends when right to receive payment established
- Measured at fair value of consideration
- Recognized when recognition criteria met

Revenue is measured at the fair value of the consideration received or receivable taking into account the amount of any trade discounts and volume rebates allowed by the entity. In most cases, the consideration is in the form of cash or cash equivalents, and the amount of revenue is the amount of cash or cash equivalents received or receivable.

The amount of revenue arising on a transaction is usually determined by agreement between the entity and the purchaser or user of the asset or service.

Rendering Services

- Recognize by reference to stage of completion at reporting date
- Conditions:
 - Amount of revenue can be measured reliably
 - Probable that service potential or economic benefits will flow to the entity
 - Stage of completion can be measured reliably
 - Costs incurred and costs to complete can be measured reliably

When a transaction involves the rendering of services, revenue associated with the transaction is recognized by reference to the stage of completion of the transaction at the reporting date. Under this method, revenue is recognized in the reporting periods in which the services are rendered. The recognition of revenue on this basis provides useful information on the extent of service activity and performance during a period.

For example, an entity providing property valuation services would recognize revenue as the individual valuations are completed.

Under the percentage completion method, revenue is recognized when the outcome of a transaction can be estimated reliably. The outcome of a transaction can be estimated reliably when:

- a) The amount of revenue can be measured reliably;
- b) It is probable that the economic benefits or service potential associated with the transaction will flow to the entity;
- c) The stage of completion of the transaction at the reporting date can be measured reliably; and
- d) The costs incurred for the transaction and the costs to complete the transaction can be measured reliably.

Estimates of the revenue are made by reference to agreement with the other parties to the transaction. An entity is generally able to make reliable estimates after it has agreed to the following with the other parties to the transaction:

- a) Each party's enforceable rights regarding the service to be provided and received by the parties;
- b) The consideration to be exchanged; and
- c) The manner and terms of settlement.

When services are performed by an indeterminate number of acts over a specified time frame, the stage of completion of a transaction may be determined by a variety of methods. An entity uses the method that measures reliably the services performed. Depending on the nature of the transaction, the methods may include:

- a) Surveys of work performed;
- b) Services performed to date as a percentage of total services to be performed; or
- c) The proportion that costs incurred to date bear to the estimated total costs of the transaction. Only costs that reflect services performed to date are included in costs incurred to date. Only costs that reflect services performed or to be performed are included in the estimated total costs of the transaction.

When the outcome of the transaction involving the rendering of services cannot be estimated reliably, revenue shall be recognized only to the extent of the expenses recognized that are recoverable.



Examples of Rendering Services

- Housing
- Transportation
- Managing toll roads
- Financial services fees
- Admission fees
- Tuition fees
- Franchise or concession fees

See the implementation guidance in IPSAS 9 for several examples and general guidance on recognition.



Sale of Goods

- Recognize revenue from the sale of goods when all the following conditions have been satisfied:
 - The entity has transferred to the purchaser the significant risks and rewards of ownership of the goods;
 - The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
 - The amount of revenue can be measured reliably;
 - It is probable that the economic benefits or service potential associated with the transaction will flow to the entity; and
 - The costs incurred or to be incurred in respect of the transaction can be measured reliably.

The assessment of when an entity has transferred the significant risks and rewards of ownership to the purchaser requires an examination of the circumstances of the transaction. In most cases, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the purchaser. This is the case for most sales.



Other Exchange Revenues

- Interest
- Royalties
- Dividends

Interest is recognized on a time proportion basis that takes into account the effective yield on the asset.

The effective yield on an asset is the rate of interest required to discount the stream of future cash receipts expected over the life of the asset to equate to the initial carrying amount of the asset. Interest revenue includes the amount of amortization of any discount, premium, or other difference between the initial carrying amount of a debt security and its amount at maturity. When unpaid interest has accrued before the acquisition of an interest bearing investment, the subsequent receipt of interest is allocated between pre-acquisition and post-acquisition periods; only the post-acquisition portion is recognized as revenue.

Royalties are recognized as they are earned in accordance with the substance of the relevant agreement.

Dividends or their equivalents are recognized when the shareholder's or the entity's right to receive payment is established.

The general recognition criteria apply. Revenue would be recognized when it is probable that the economic benefit or service potential associated with the transaction will flow to the entity and the amount can be measured reliably.

Revenue Recognition

Scenario:

A government treats and distributes water for residential and commercial use. Water consumption is metered.

Users are billed in arrears on a quarterly basis. The billing cycle is staggered so that meter readings are taken and invoices issued 15 days after the quarter end for each group of consumers. Revenue is posted to the general ledger when invoices are issued. From past experience, water consumption is spread evenly over the billing period. The estimated unbilled consumption for Group A for Dec 20X1 is CU 200,000. Invoices are due in thirty days. The fiscal period ends December 31, 20X1.

Billing Group	Invoice Date	Consumption Period	Due Date	Amount (CU)
Group A	Dec 15, 20X0	Sept-Oct-Nov	Jan 15, 20X1	900,000
Group B	Jan 15, 20X1	Oct-Nov-Dec	Feb 15, 20X1	1,000,000
Group C	Feb 15, 20X1	Nov-Dec-Jan	Mar 15, 20X1	1,200,000

What adjustment should be made to revenue for the period ended Dec 31, 20X1? Explain.

The entity should accrue revenue for the year ended Dec 31, 20X1 of CU 2,000,000 as follows:

Billing Group	Invoice Date	Consumption Period	Due Date	Amount (CU)	Period end accrual (CU)
Group A	Dec 15, 20X0	Sept-Oct-Nov	Jan 15, 20X1	900,000	200,000 ¹
Group B	Jan 15, 20X1	Oct-Nov-Dec	Feb 15, 20X1	1,000,000	1,000,000 ²
Group C	Feb 15, 20X1	Nov-Dec-Jan	Mar 15, 20X1	1,200,000	800,000 ³
Total					2,000,000

¹ Unbilled consumption for Group A

² Consumption for 3 months ended Dec 31 billed January 15

³ Estimated consumption for Group C for Nov and Dec 20X0 (Feb 15, 20X1 billing/3 months * 2 months)

Interest Revenue

Scenario:

A public sector entity holds a debenture purchased January 1, 20X0. The cost was CU100,000. The public sector entity will receive a payment of CU 115,763 on maturity on its third anniversary. The debenture has a coupon rate of zero (i.e. it is 'interest-free'). Present value financial tables have been used to determine that the effective yield is 5%.

What are the interest revenue, interest accrual and carrying amount of the debenture at the end of each of the 3 years to maturity? Explain. (For ease of calculation interest is accrued on an annual basis and not prorated on days in period.)

	Interest Revenue CU	Carrying Amount CU
Jan. 1, 20X0		100,000
Dec. 31, 20X0	?	?
Dec. 31, 20X1	?	?
Dec. 31, 20X2	?	?

Answer:

The effective rate is the rate of interest required to discount the stream of future cash receipts expected over the life of the asset to equate to the initial carrying amount of the asset

Year	Calculation	Carrying Amount CU	Interest Revenue CU
January 1, 20X0		100,000	
December 31, 20X0	CU 100,000 *5% effective rate	105,000	5,000
December 31, 20X1	CU 105,000 *5% effective rate	110,250	5,250
December 31, 20X2	CU 110,205* 5%% effective rate	115,763	5,513

Illustrative Note Disclosure

The illustrative note highlights the following note disclosure requirements in IPSAS 9:

An entity shall disclose:

- a) The accounting policies adopted for the recognition of revenue, including the methods adopted to determine the stage of completion of transactions involving the rendering of services;
- b) The amount of each significant category of revenue recognized during the period, including revenue arising from:
 - (i) The rendering of services;
 - (ii) The sale of goods;
 - (iii) Interest;
 - (iv) Royalties; and
 - (v) Dividends or their equivalents; and
- c) The amount of revenue arising from exchanges of goods or services included in each significant category of revenue.

The following example shows a sample note that an entity might be used to explain the items reported on the statement of performance as sales of goods and services. The accounting policy for recognition of revenue from exchange transactions is likely to be included in the accounting policy note to the financial statements.

Note X – Sales of Goods and Services

Revenue is recognized when services are rendered or title to goods is transferred.

The revenue reported is comprised of the following items

	20X1 (CU)	20X1 (CU)
Water and sewage charges	209,249	186,559
Transit fares	96,660	90,828
Other	49,202	45,539
Total	355,111	322,926

Discussion and Questions

That concludes our module on revenue from exchange transactions. Participants should refer to the review questions to test themselves on their knowledge.

Visit the IPSASB webpage.

<http://www.ipsasb.org>

Review Questions

Question 1

A secondary institution collects tuition fees at the beginning of each semester. The fees payable are for the fair value of the instruction. There are no refunds once the semester begins. The revenue is recognized:

- a) **In the period in which the fees are collected.**
- b) **Over the period of instruction.**
- c) **At the beginning of the semester.**
- d) **At the end of the semester.**

Answers to Review Questions

Question 1

The answer is (b).

As the fees payable are for the fair value of the instruction, the transaction is an exchange transaction accounted for under IPSAS 9

The percentage of completion method is used to recognize revenue. Under this method, revenue is recognized in the reporting periods in which the services are rendered. The recognition of revenue on this basis provides useful information on the extent of service activity and performance during a period.

Revenue from Non-Exchange Transactions: Taxes

Accounting for Non-Exchange Transactions

Issues associated with accounting for revenues from non-exchange transactions include classification, determining recognition points, and measurement at initial recognition.

These inflows from non-exchange transactions, as with inflows from exchange transactions, have to be distinguished from financing inflows such as borrowings and custodial receipts, for example taxes collected as an agent of another entity. These latter transactions are not revenues of the entity.

Accounting for Taxes

- Entity that imposes taxes recognizes the assets when
 - Taxable event occurs
 - Recognition criteria satisfied
- Taxable event – event subject to taxation
- Assets measured at fair value at acquisition date - best estimate of the inflow taking into account
 - Probability resources will flow
 - Fair value of resultant assets
- Revisions accounted for in current period

An entity that imposes taxes recognizes an asset in respect of taxes when the taxable event occurs, and the asset recognition criteria are met.

Taxation revenue arises only for the government that imposes the tax, and not for other entities. For example, where the national government imposes a tax that is collected by its taxation agency, assets and revenue accrue to the government, not the taxation agency.

When a national government imposes a sales tax, the entire proceeds of which it passes to state governments, based on a continuing appropriation, the national government recognizes assets and revenue for the tax, and a decrease in assets and an expense for the transfer to state governments. The state governments will recognize assets and revenue for the transfer.

Similarly, when a single entity collects taxes on behalf of several other entities, it is acting as an agent for all of them. For example, where a state taxation agency collects income tax for the state government and several city governments, it does not recognize revenue in respect of the taxes collected. Rather, the individual governments that impose the taxes recognize assets and revenue in respect of the taxes.

Resources arising from taxes satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur, and their fair value can be reliably measured. The degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition, which includes, but is not limited to, disclosure of the taxable event by the taxpayer.

The taxable event is the event that the government, legislature, or other authority has determined will be subject to taxation.

This is the earliest possible time to recognize assets and revenue arising from a taxation transaction and is the point at which the past event that gives rise to control of the asset occurs.

Similar types of taxes are levied in many jurisdictions. The reporting entity analyzes the taxation law in its own jurisdiction to determine what the taxable event is for the various taxes levied.

Unless otherwise specified in laws or regulations, it is likely that the taxable event for:

- a) Income tax is the earning of assessable income during the taxation period by the taxpayer;
- b) Value-added tax is the undertaking of taxable activity during the taxation period by the taxpayer;
- c) Goods and services tax is the purchase or sale of taxable goods and services during the taxation period;
- d) Customs duty is the movement of dutiable goods or services across the customs boundary;
- e) Death duty is the death of a person owning taxable property; and
- f) Property tax is the passing of the date on which the tax is levied, or the period for which the tax is levied, if the tax is levied on a periodic basis.

The fair value of assets arising from taxation transactions are measured at the best estimate of the inflow of resources to the entity. The best estimate will take account of both the probability that the resources will flow to the government, and the fair value of the resultant assets.

Reporting entities have to develop accounting policies for the measurement of assets arising from taxation that measures them at their fair value as at the date of acquisition. Reliably measuring the assets arising from taxation transactions and the related revenue is challenging because information may not become available until sometime after the taxable event occurs. For example, the amount of income tax owed by taxpayers is not known until tax returns are filed and assessed.

Where there is a separation between the timing of the taxable event and collection of taxes, public sector entities may reliably measure assets arising from taxation transactions by using, for example, statistical models based on the history of collecting the particular tax in prior periods. These models will include consideration of the timing of cash receipts from taxpayers, declarations made by taxpayers, and the relationship of taxation receivable to other events in the economy. Measurement models will also take account of other factors such as:

- a) The tax law allowing taxpayers a longer period to file returns than the government is permitted for publishing general purpose financial statements;
- b) Taxpayers failing to file returns on a timely basis;
- c) Valuing nonmonetary assets for tax assessment purposes;
- d) Complexities in tax law requiring extended periods for assessing taxes due from certain taxpayers;
- e) The potential that the financial and political costs of rigorously enforcing the tax laws and collecting all the taxes legally due to the government may outweigh the benefits received;
- f) The tax law permitting taxpayers to defer payment of some taxes; and
- g) A variety of circumstances particular to individual taxes and jurisdictions.

In some cases, the assets arising from taxation transactions and the related revenue cannot be reliably measured until sometime after the taxable event occurs. Consequently the recognition criteria may not be satisfied until a subsequent period or when payment is received or receivable. This may occur if a tax base is volatile and reliable estimation is not possible. In many cases, the assets and revenue may be recognized in the period subsequent to the occurrence of the taxable event.

There are exceptional circumstances when several reporting periods will pass before a taxable event results in an inflow of resources embodying future economic benefits or service potential that meets the definition of an asset and satisfies the criteria for recognition as an asset. For example, it may take several years to determine and reliably measure the amount of death duty due in respect of a large deceased estate because it includes a number of valuable antiques and artworks, which require specialist valuations. Consequently the recognition criteria may not be satisfied until payment is received or receivable.

When assets and revenue arising from taxation transactions are measured using statistical models, the actual amount realized in subsequent reporting periods may be different from the estimated amounts determined as being due from taxpayers in respect of the current reporting period. Revisions to estimates are made prospectively in accordance with IPSAS 3, *Accounting Policies, Changes in Accounting Estimates and Errors*.



Illustrative Example

Scenario:

A national government levies a tax on the income of individuals. The fiscal period of the government and the tax year end is December 31. Taxpayers have until April 30 of the following year to file their tax return, and until June 30 to pay any outstanding taxes.

Does the national government recognize an asset and revenue at the fiscal period end? Explain.

Answer:

Income tax revenue should be recognized in the reporting period in which the taxable event occurred, that is, the earning of taxable income.

As the tax returns of individuals will not be filed until April 30 of the following year, the government is unable to directly measure the income tax receivable at December 31. It could wait until all tax returns have been filed and processed to finalize its financial statements. This may not satisfy the qualitative characteristic of financial information, that is, that it be timely. The government develops a statistical model to indirectly measure income taxation revenue receivable.

The government uses the income tax collection statistical history, which it compares to other observable phenomena to develop a reliable model. Other phenomena can include other economic statistics, such as gross domestic product, financial phenomena such as income tax installments deducted by employers and banking statistics collected by the central bank. This government may enlist the assistance of econometricians in developing the model.

The model enables the reporting entity to reliably measure the asset and revenue accruing to it during the reporting period, which are then recognized and disclosed in the general-purpose financial statements. The notes to the general-purpose financial statements disclose the accounting policies, including the basis of measurement of income tax revenue.

In these circumstances, estimates of tax revenue for one reporting period may be revised in a subsequent period. Changes in estimates are recognized prospectively in accordance with IPSAS 3, *Accounting Policies, Accounting Estimates and Errors*.

Other Tax Accounting Issues

- Resources received prior to the taxable event are recognized as advance receipts of taxes
- Taxation revenue is gross amount
 - Not reduced for expenses paid through the tax system
 - Not grossed up for tax expenditures
- Taxes levied for specific purposes

Resources for taxes received prior to the occurrence of the taxable event are recognized as an asset and a liability (advance receipts), because

- (i) the event that gives rise to the entity's entitlement to the taxes has not occurred, and
- (ii) the criteria for recognition of taxation revenue have not been satisfied.

Consistent with the definitions of assets, liabilities, resources for taxes received prior to the occurrence of the taxable event are recognized as an asset and a liability (advance receipts), because (a) the event that gives rise to the entity's entitlement to the taxes has not occurred, and (b) the criteria for recognition of taxation revenue have not been satisfied, notwithstanding that the entity has already received an inflow of resources. Advance receipts in respect of taxes are not fundamentally different from other advance receipts, so a liability is recognized until the taxable event occurs. When the taxable event occurs, the liability is discharged and revenue is recognized.

Taxation revenue shall be determined at a gross amount. It shall not be reduced for expenses paid through the tax system. Expenses paid through the tax system are amounts that are available to beneficiaries regardless of whether or not they pay taxes.

In some jurisdictions, the government uses the tax system as a convenient method of paying benefits to taxpayers that would otherwise be paid using another payment method, such as writing a check, directly depositing the amount in a taxpayer's bank account, or settling another account on behalf of the taxpayer.

The key is that expenses paid through the tax system are available to recipients irrespective of whether they pay taxes or use a particular mechanism to pay their taxes. IPSAS 1 prohibits the offsetting of items of revenue and expense unless permitted by another standard. Therefore offsetting of tax revenue and expenses paid through the tax system is not permitted.

Tax expenditures are preferential provisions of the tax law that provide certain taxpayers with concessions that are not available to others. In most jurisdictions, governments use the tax system to encourage certain financial behavior and discourage other behavior. These types of concessions are available only to taxpayers. If an entity (including a natural person) does not pay tax, it cannot access the concession. These types of concessions are called tax expenditures.

Tax expenditures are foregone revenue, not expenses, and do not give rise to inflows or outflows of resources – that is, they do not give rise to assets, liabilities, revenue, or expenses of the taxing government.

Some taxes are levied for specific purposes. Generally, taxes levied for a specific purpose do not create a performance obligation that requires a liability to be recognized. If the government is required to recognize a liability relating to assets recognized as a consequence of specific purpose tax levies, it does not recognize revenue until the performance obligation is satisfied and the liability is reduced. However, in most cases, taxes levied for specific purposes are not expected to give rise to a liability, because the specific purposes amount to restrictions on how the resources are used. The entity retains discretion in how it uses the resources. If the resources are not used for the intended purpose, there is no obligation to return the resources. The specific purposes amount to restrictions not conditions. See the discussion on stipulations, conditions and restrictions

Tax Expenditure/Expense

Scenario:

A national government permits individual taxpayers who are homeowners to deduct mortgage interest and property taxes from their gross income when calculating tax-assessable income. The policy has been adopted to encourage home ownership.

1. Is the deduction a tax expense or expenditure? Explain.
2. How should the national government account for and report the impact of the deduction of tax revenues? Explain.

Answer:

The impact on tax revenue as a result of the deduction of mortgage interest and property taxes is a tax expenditure. It is a tax concession only available to taxpayers. Taxation revenue shall not be grossed up for the amount of the tax concession. Tax expenditures are not reported in the statement of financial performance. They are forgone tax revenue.

Disclosures

Disclose :

- Revenue from non-exchange transactions
- Receivables recognized
- Amounts of advance receipts
- Amount of liabilities forgiven
- Accounting policies adopted
- Basis on which the fair value was measured
- Information about taxes that cannot be measured reliably

An entity discloses either on the face of, or in the notes to, the general purpose financial statements:

- a) The amount of revenue from non-exchange transactions recognized during the period by major classes showing separately:
 - (i) Taxes, showing separately major classes of taxes; and
 - (ii) Transfers, showing separately major classes of transfer revenue.
- b) The amount of receivables recognized in respect of non-exchange revenue;
- ...
- e) The existence and amounts of any advance receipts in respect of non-exchange transactions; and
- f) The amount of any liabilities forgiven.

Disclosure in (e) requires entities to disclose the existence of advance receipts in respect of non-exchange transactions. These liabilities carry the risk that the entity will have to make a sacrifice of future economic benefits or service potential if the taxable event does not occur. Disclosure of these advance receipts assists users to make judgments about the entity's future revenue and net asset position.

An entity also discloses in the notes to the general purpose financial statements:

- a) The accounting policies adopted for the recognition of revenue from non-exchange transactions;
- b) For major classes of revenue from non-exchange transactions, the basis on which the fair value of inflowing resources was measured;
- c) For major classes of taxation revenue that the entity cannot measure reliably during the period in which the taxable event occurs, information about the nature of the tax; and

In many cases an entity will be able to reliably measure assets and revenue arising from taxation transactions, using, for example, statistical models. However, there may be exceptional circumstances where an entity is unable to reliably measure the assets and revenue arising until one or more reporting periods has elapsed since the taxable event occurred. In these cases, the entity makes disclosures about the nature of major classes of taxation that cannot be reliably measured, and therefore recognized, during the reporting period in which the taxable event occurs. These disclosures assist users to make informed judgments about the entity's future revenue and net asset position

Illustrative Note Disclosure

Note X: Tax Revenues

Tax revenues are reported net of amounts collected on behalf of provinces. Income tax revenue is recognized when the taxpayer has earned the income. Revenues for the fiscal year are based on amounts assessed and estimates of income tax earned but not yet assessed. Goods and services tax revenue is recognized at the time of sale or provision. Employment insurance premiums are recognized as insurable earnings are earned. Differences between estimates and actual amounts are reported in the period in which the actual assessment is completed.

Tax revenues are summarized in the table below.

	20X1 (000s CU)	20X0 (000s CU)
Income Tax	139,601	151,798
Goods and services tax	26,947	25,740
Employment insurance premiums	40,573	39,806
Total tax revenue	207,121	217,344

The example illustrates a sample note on accounting policy, recognition and measurement of tax revenues.

The illustrative note shows how an entity discloses in the notes to the general-purpose financial statements:

- a) The accounting policies adopted for the recognition of revenue from non-exchange transactions;
- b) For major classes of revenue from non-exchange transactions, the basis on which the fair value of inflowing resources was measured.

Discussion and Questions

That concludes our module on revenue from exchange transactions. Participants should refer to the review questions to test themselves on their knowledge.

Visit the IPSASB webpage.

<http://www.ipsasb.org>

Review Questions

Question 1

A national government imposes a sales tax, the entire proceeds of which it passes to state governments, based on a continuing appropriation. Which of the following is the appropriate accounting for the assets and revenue?

- a) **The national government recognizes assets and revenue for the tax, and a decrease in assets and an expense for the transfer to state governments**
- b) **The national government, as agent for the state governments does not recognize assets and revenue. The state governments recognize assets and revenue for the tax.**

Why?

Question 2

An entity recognizes an asset and revenue from taxes when the taxable event subject to taxation occurs. A national government levies a tax on income at 25%. It requires taxpayers to make quarterly installments of estimated taxes payable for the tax year. Tax returns must be filed by April 30 and the balance of taxes paid by June 30 in the year following. The taxable event occurs when

- a) **Individuals file their annual tax returns**
- b) **Individuals make quarterly installments**
- c) **Individuals make their final payment**
- d) **Individuals earn taxable income?**

Question 3

A local government (reporting entity) levies a tax of one percent of the assessed value of all property within its jurisdiction. The government's reporting period is July 1 to June 30. The tax is levied on July 31, with notices of assessment being sent to property owners in July, and payment due by August 31. If taxes are unpaid on that date, property owners incur penalty interest rate payments of three percent per month of the amount outstanding.

When does the local government recognize an asset and revenue? Why?

Question 4

A local government levies property tax on July 31, with notices of assessment being sent to property owners in July, and payment due by August 31. It allows taxpayers to pay taxes in monthly installments commencing in October of the preceding year.

When does the local government recognize the revenue for property taxes collected in advance? Why?

Answers to Review Questions

Question 1

The answer is (b).

The national government is the taxing authority that is imposing the sales tax. The national government recognizes assets and revenue for the sales tax. It recognizes a decrease in assets and an expense for the transfer to state governments. The state governments will recognize assets and revenue for the transfer.

Question 2

The answer is (d).

Resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of the occurrence of the taxable event that the government, legislature, or other authority has determined will be subject to taxation.

Resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of a past event (the taxable event) and expects to receive future economic benefits or service potential from those resources. Resources arising from taxes satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur and their fair value can be reliably measured. The degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition, which includes, but is not limited to, disclosure of the taxable event by the taxpayer.

Question 3

The government controls a resource – property taxes receivable – when the taxable event occurs, which is the passing of the date on which the taxes are levied, July 31. The government recognizes assets and revenue in the general purpose financial statements of the reporting period in which that date occurs.

Question 4

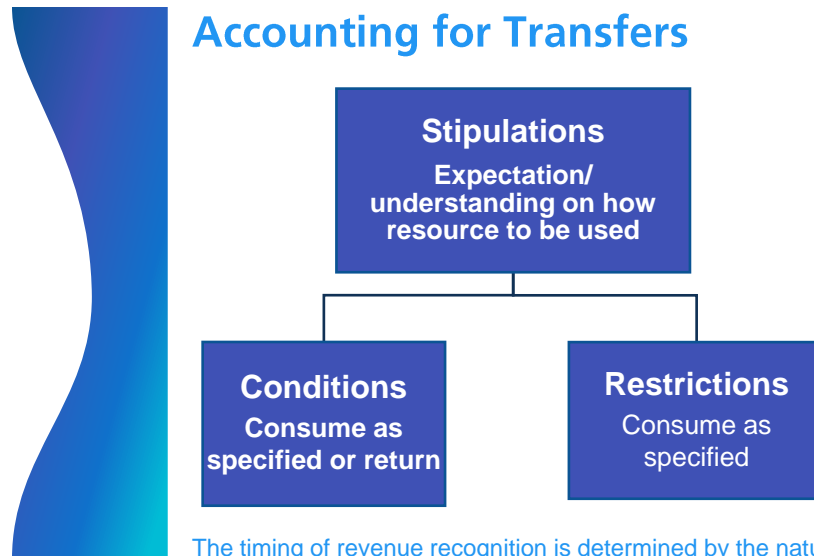
The local government recognizes an asset and a liability for the property taxes paid in advance at the time of receipt. It recognizes a reduction in the liability and a corresponding amount as revenue on July 31.

Consistent with the definitions of assets, liabilities, resources for taxes received prior to the occurrence of the taxable event are recognized as an asset and a liability (advance receipts), because (a) the event that gives rise to the entity's entitlement to the taxes has not occurred, and (b) the criteria for recognition of taxation revenue have not been satisfied, notwithstanding that the entity has already received an inflow of resources. Advance receipts in respect of taxes are not fundamentally different from other advance receipts, so a liability is recognized until the taxable event occurs. When the taxable event occurs, the liability is discharged and revenue is recognized.

Revenue from Non-Exchange Transactions: Transfers

Accounting for Non-Exchange Transactions

Issues associated with accounting for revenues from non-exchange transactions include classification, determining recognition points, measurement at initial recognition and determining the appropriate accounting treatment of conditions attached to grants.



The timing of revenue recognition is determined by the nature of the stipulations and their settlement.

Transactions which give rise to non-exchange revenue often also involve the recognition of liabilities. It is common for assets to be transferred in a non-exchange transaction with the expectation and/or understanding by the transferor that they will be used in a particular way and, therefore, that the recipient entity will act or perform in a particular way. Stipulations that require the recipient to use or consume the future economic benefits or service potential embodied in an asset for a particular purpose impose a performance obligation on the recipient. The performance obligation may, in certain circumstances, create a present obligation that meets the definition of a liability.

Stipulations on transferred assets are terms in laws or regulation, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity. Key features of stipulations include:

- a) Stipulations are enforceable through legal or administrative processes. If a term in laws or regulations or other binding arrangements is unenforceable, it is not a stipulation as defined by IPSAS 23.
- b) Stipulations are not constructive obligations. A decision by an entity's governing body or controlling entity on how it intends to use a transferred asset does not give rise to a constructive obligation under IPSAS 23, regardless of whether that decision has been communicated before the reporting date to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the entity will discharge its responsibilities.
- c) A key feature of stipulations, as defined in this Standard, is that an entity cannot impose a stipulation on itself, whether directly or through an entity that it controls.

Stipulations relating to a transferred asset may be either conditions or restrictions. Both restrictions and conditions may require an entity to use or consume the future economic benefits or service potential embodied in an asset for a particular purpose (performance obligation) on initial recognition.

An entity analyzes any and all stipulations attached to an inflow of resources, to determine whether those stipulations impose conditions or restrictions. The distinction is critical to the accounting for transferred assets.

Conditions on transferred assets require that the entity either consume the future economic benefits or service potential of the asset, or return future economic benefits or service potential to the transferor in the event that the conditions are breached. Only conditions require that future economic benefits or service potential be returned to the transferor in the event that the stipulation is breached (return obligation).

It is the return obligation associated with the transferred asset that creates the present obligation that meets the definition of a liability. That is, the entity has a present obligation to transfer future economic benefits or service potential to third parties when it initially gains control of an asset subject to a condition. This is due to the fact that the recipient is unable to avoid the future outflow of resources. It is required to consume the future economic benefits or service potential embodied in the transferred asset in the delivery of particular goods or services to third parties, or to return them to the transferor. Therefore, when a recipient initially recognizes an asset that is subject to a condition, it also incurs a liability.

The present obligation is recognized as a liability when it is probable that an outflow of resources embodying future economic benefits or service potential will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The present obligation is recognized as a liability on initial recognition of the asset.

Restrictions on transferred assets do not include a requirement that the transferred asset, or other future economic benefits or service potential, is to be returned to the transferor if the asset is not deployed as specified. Therefore, gaining control of an asset subject to a restriction does not impose on the recipient a present obligation to transfer future economic benefits or service potential to third parties when control of the asset is initially gained.

Where a recipient is in breach of a restriction, the transferor, or another party, may have the option of seeking a penalty against the recipient, by, for example, taking the matter to a court or other tribunal, or through an administrative process such as a directive from a government minister or other authority, or otherwise.

Such actions may result in the entity being directed to fulfill the restriction or face a civil or criminal penalty for defying the court, other tribunal, or authority. Such a penalty is not incurred as a result of acquiring the asset, but as a result of breaching the restriction.

Again, gaining control of an asset subject to a restriction that could be enforced does not impose on the recipient a present obligation to transfer future economic benefits or service potential to third parties when control of the asset is initially gained. It is only in the case of a breach of the restriction that an entity may have a present obligation.

If an entity has recognized a liability in respect of the inflow of resources arising from the non-exchange transaction, when the liability is subsequently reduced, because a condition is satisfied, it recognizes revenue. For example, if a condition specifies that the entity is to provide goods or services to third parties, or return unused funds to the transferor, revenue is recognized as goods or services are provided.



Characteristics of Conditions

- An outflow of resources will be probable, and performance against the condition is required and is able to be assessed
- Condition enforceable and in cases of breaches, it would be enforced
- Performance is assessable and monitored - specifies
 - The goods and services to be provided or assets to be acquired
 - The periods within which performance is to occur

To satisfy the criteria for recognition as a liability, it is necessary that an outflow of resources will be probable, and performance against the condition is required and is able to be assessed.

In determining whether a stipulation is a condition or a restriction, it is necessary to consider the substance of the terms of the stipulation and not merely its form.

The mere specification that, for example, a transferred asset is required to be consumed in providing goods and services to third parties or be returned to the transferor is, in itself, not sufficient to give rise to a liability when the entity gains control of the asset.

Similarly, a condition must impose a performance obligation on the recipient entity. The performance obligation is required as a consequence of the condition itself. A term in a transfer agreement that requires the entity to perform an action that it has no alternative but to perform may lead the entity to conclude that the term is in substance neither a condition nor a restriction.

For example, a government may receive a transfer to provide health services. The government has a constitutional requirement to provide health services. The stipulation may not be a condition in these circumstances since the government is required to provide health services whether or not it receives the transfer.

To make the determination that a stipulation is a condition, the entity considers whether a requirement to return the asset is enforceable. If the transferor could not enforce a requirement to return the asset, the stipulation fails to meet the definition of a condition, and will be considered a restriction.

A stipulation is not a condition if, in cases of breaches, it would not be enforced by the transferor. If past experience with the transferor indicates that the transferor never enforces the requirement to return the transferred asset when breaches have occurred, then the recipient entity may conclude that the stipulation has the form but not the substance of a condition, and is, therefore, a restriction. Lacking evidence to the contrary, an entity would assume that the transferor would enforce the stipulation and, therefore, the stipulation meets the definition of a condition.

To meet these requirements, a condition will need to specify such matters as:

- (i) the nature or quantity of the goods and services to be provided or the nature of assets to be acquired as appropriate and
- (ii) if relevant, the periods within which performance is to occur.

Performance will need to be monitored by, or on behalf of, the transferor on an ongoing basis.



Illustrative Example

Scenario:

A national government provides funds to a provincial government entity subject to the stipulation that the entity raise a matching contribution. The funds are returnable to the national government if it fails to raise the matching contribution.

Is the stipulation a condition that would result in recognition of a liability?

Answer:

In this case, an asset may be transferred subject to the stipulation that it be returned to the transferor if a specified future event does not occur. A return obligation does not arise until such time as it is expected that the stipulation will be breached, and a liability is not recognized until the recognition criteria have been satisfied.

However, the state government would need to consider whether the transfer is in the nature of an advance receipt. Advance receipts give rise to an asset and a present obligation because the transfer arrangement has not yet become binding.



Advance Receipts

- Resources received before a transfer arrangement becomes binding recognized as an asset and advance receipt liability

Where an entity receives resources before a transfer arrangement becomes binding, the resources are recognized as an asset when they meet the definition of an asset and satisfy the criteria for recognition as an asset. The entity will also recognize an advance receipt liability if the transfer arrangement is not yet binding.

Advance receipts in respect of transfers are not fundamentally different from other advance receipts, so a liability is recognized until the event that makes the transfer arrangement binding occurs and all other conditions under the agreement are fulfilled. When that event occurs and all other conditions under the agreement are fulfilled, the liability is discharged and revenue is recognized.



Exchange and Non-Exchange Components of a Transaction

- A transaction may include two components, an exchange component and a non-exchange component.
- Where an asset is acquired by means of a transaction that has an exchange component and a non-exchange component, the entity recognizes
 - The exchange component according to the principles and requirements of other IPSASs; and
 - The non-exchange component is recognized according to the principles and requirements of this IPSAS 23.

Where an asset is acquired by means of a transaction that has an exchange component and a non-exchange component, the entity recognizes the exchange component according to the principles and requirements of other IPSASs. The non-exchange component is recognized according to the principles and requirements of this standard. In determining whether a transaction has identifiable exchange and non-exchange components, professional judgment is exercised. Where it is not possible to distinguish separate exchange and non-exchange components, the transaction is treated as a non-exchange transaction.

Exchange and Non-Exchange Components

Scenario:

A local school board (the reporting entity) purchases land with a fair value of CU100,000 for CU50,000 from a municipality.

How should the school board account for the acquisition? Why?

Answer:

The reporting entity concludes that the transaction comprises two components, an exchange component and a non-exchange component. One component involves the purchase of a half share in the land for CU50,000; the other component is a non-exchange transaction that transfers the remaining half share of the land to the school.

The exchange component would be accounted in accordance with IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 17, *Property, Plant and Equipment*. The non-exchange component is accounted for in accordance with IPSAS 23. An asset acquired through a non-exchange transaction is initially measured at its fair value as at the date of acquisition. An inflow of resources from a non-exchange transaction recognized as an asset is recognized as revenue.

In its general-purpose financial statements for the reporting period in which the transaction takes place, the local school board recognizes the land at CU100,000, its fair value. It would also report a transfer of CU50,000 being the revenue from the non-exchange component of the transaction to purchase the land. This is the increase in net assets/equity as a result of the acquisition. That is, an increase in land assets of CU 100,000 less the cash payment.

Other Non-Exchange Transactions

The following non-exchange transactions generally follow the recognition and measurement requirements as for other non-exchange transaction

- Fines
- Forgiven debt - revenue is carrying amount
- Bequests
- Gifts and donations
 - Measured at fair value at date of acquisition
 - Pledges not recognized

Fines are economic benefits or service potential received or receivable by a public sector entity, from an individual or other entity, as determined by a court or other law enforcement body. Fines normally require an entity to transfer a fixed amount of cash to the government, and do not impose on the government any obligations which may be recognized as a liability. Assets arising from fines are measured at the best estimate of the inflow of resources to the entity.

Lenders will sometimes waive their right to collect a debt owed by a public sector entity, effectively canceling the debt. For example, a national government may cancel a loan owed by a local government. In such circumstances, the local government recognizes an increase in net assets because a liability it previously recognized is extinguished. Revenue arising from debt forgiveness is measured at the carrying amount of the debt forgiven.

Entities recognize revenue in respect of debt forgiveness when the former debt no longer meets the definition of a liability or satisfies the criteria for recognition as a liability, provided that the debt forgiveness does not satisfy the definition of a contribution from owners.

A bequest is a transfer made according to the provisions of a deceased person's will. The past event giving rise to the control of resources embodying future economic benefits or service potential for a bequest occurs when the entity has an enforceable claim, for example on the death of the testator, or the granting of probate, depending on the laws of the jurisdiction.

Bequests that satisfy the definition of an asset are recognized as assets and revenue when it is probable that the future economic benefits or service potential will flow to the entity, and the fair value of the assets can be measured reliably. Determining the probability of an inflow of future economic benefits or service potential may be problematic if a period of time elapses between the death of the testator and the entity receiving any assets. The entity will need to determine if the deceased person's estate is sufficient to meet all claims on it, and satisfy all bequests. If the will is disputed, this will also affect the probability of assets flowing to the entity.

Gifts and donations are voluntary transfers of assets, including cash or other monetary assets, goods in-kind, and services in-kind that one entity makes to another, normally free from stipulations. The transferor may be an entity or an individual. For gifts and donations of cash or other monetary assets and goods in-kind, the past event giving rise to the control of resources embodying future economic benefits or service potential is normally the receipt of the gift or donation.

Goods in-kind are tangible assets transferred to an entity in a non-exchange transaction, without charge, but may be subject to stipulations. On initial recognition, gift and donations including goods in-kind are measured at their fair value as at the date of acquisition, which may be determined by reference to an active market, or by appraisal.

Goods in-kind are recognized as assets when the goods are received, or there is a binding arrangement to receive the goods. If goods in-kind are received without conditions attached, revenue is recognized immediately. If conditions are attached, a liability is recognized, which is reduced and revenue recognized as the conditions are satisfied.

Pledges are unenforceable undertakings to transfer assets to the recipient entity. Pledges do not meet the definition of an asset, because the recipient entity is unable to control the access of the transferor to the future economic benefits or service potential embodied in the item pledged. Entities do not recognize pledged items as assets or revenue. Pledges may warrant disclosure as contingent assets under the requirements of IPSAS 19.

Concessionary Loans

- Loans received at below market terms
 - Portion of the loan that is repayable plus interest is an exchange transaction
 - Difference between the transaction price (loan proceeds) and the fair value of the loan on initial recognition is non-exchange revenue except to the extent that conditions result in a liability
 - As liability is reduced an equal amount of revenue recognized
- Accounted for as financial instrument

Concessionary loans are loans received by an entity at below market terms.

The portion of the loan that is repayable, along with any interest payments, is an exchange transaction and is accounted for in accordance with [IPSAS 29, *Financial Instruments: Recognition and Measurement*](#) (or [IPSAS 41, *Financial Instruments*](#)).

An entity considers whether any difference between the transaction price (loan proceeds) and the fair value of the loan on initial recognition (see IPSAS 29 or IPSAS 41) is non-exchange revenue that should be accounted for in accordance with IPSAS 23. Where an entity determines that the difference between the transaction price (loan proceeds) and the fair value of the loan on initial recognition is non-exchange revenue, an entity recognizes the difference as revenue except if a present obligation exists.

Where conditions imposed on the transferred assets result in a present obligation it is recognized as a liability. As the entity satisfies the present obligation, the liability is reduced and an equal amount of revenue is recognized.

Examples of concessionary loans granted by entities include loans to developing countries, small farms, student loans granted to qualifying students for university or college education and housing loans granted to low income families. Entities may receive concessionary loans, for example, from development agencies and other government entities.

Loan to Health Authority

Scenario:

A local health authority receives loan funding of CU5 million from an international development agency. The agreement stipulates that loan should be repaid over the 5 year period. Interest is paid annually in arrears, at a rate of 5% per annum on the outstanding balance of the loan. A market related rate of interest for a similar transaction is 10%. There are no conditions attached to the loan.

Is the loan a concessionary loan? Explain.

Answer:

The loan is a concessionary loan. That is, the interest rate on the loan at 5% is concessionary when the market rate is 10%.

The portion of the loan that is repayable, along with any interest payments, is an exchange transaction. However, the health authority considers whether any difference between the transaction price (loan proceeds) and the fair value of the loan on initial recognition is non-exchange revenue that should be accounted for in accordance with IPSAS 23.

Fair value is determined by discounting future cash payments using market related rate of interest.

Disclosures

Disclose:

- Revenue from non-exchange transactions
- Receivables recognized
- Liabilities recognized in respect of conditions
- Amount and nature of assets subject to restrictions
- Amounts of advance receipts
- Amount of liabilities forgiven
- Accounting policies adopted
- Basis on which the fair value was measured
- Nature and type of bequests, gifts and donations

An entity discloses either on the face of, or in the notes to, the general purpose financial statements:

- a) The amount of revenue from non-exchange transactions recognized during the period by major classes showing separately:
 - (i) Taxes, showing separately major classes of taxes; and
 - (ii) Transfers, showing separately major classes of transfer revenue.
- b) The amount of receivables recognized in respect of non-exchange revenue;
- c) The amount of liabilities recognized in respect of transferred assets subject to conditions;
- d) The amount of assets recognized that are subject to restrictions and the nature of those restrictions;
- e) The existence and amounts of any advance receipts in respect of non-exchange transactions; and
- f) The amount of any liabilities forgiven.

Conditions and restrictions impose limits on the use of assets, which impacts the operations of the entity. Disclosure of (a) the amount of liabilities recognized in respect of conditions, and (b) the amount of assets subject to restrictions assists users in making judgments about the ability of the entity to use its assets at its own discretion. Entities are encouraged to disaggregate by class the information required to be disclosed by (c).

Disclosure in (e) requires entities to disclose the existence of advance receipts in respect of non-exchange transactions. These liabilities carry the risk that the entity will have to make a sacrifice of future economic benefits or service potential if a transfer arrangement does not become binding. Disclosure of these advance receipts assists users to make judgments about the entity's future revenue and net asset position.

An entity also discloses in the notes to the general-purpose financial statements:

- a) The accounting policies adopted for the recognition of revenue from non-exchange transactions;
- b) For major classes of revenue from non-exchange transactions, the basis on which the fair value of inflowing resources was measured;
- c) The nature and type of major classes of bequests, gifts, and donations, showing separately major classes of goods in-kind received.

Item (c) requires entities to make disclosures about the nature and type of major classes of gift donations, and bequests it has received. These inflows of resources are received at the discretion of the transferor, which exposes the entity to the risk that, in future periods, such sources of resources may change significantly. Such disclosures assist users to make informed judgments about the entity's future revenue and net asset position.

Where services in-kind meet the definition of an asset and satisfy the criteria for recognition as an asset, entities may elect to recognize these services in-kind and measure them at their fair value. IPSAS 23 encourages an entity to make disclosures about the nature and type of all services in-kind received, whether they are recognized or not. Such disclosures may assist users to make informed judgments about (a) the contribution made by such services to the achievement of the entity's objectives during the reporting period, and (b) the entity's dependence on such services for the achievement of its objectives in the future.

Discussion and Questions

That concludes our module on revenue from non-exchange transactions. Participants should refer to the review questions to test themselves on their knowledge.

Visit the IPSASB webpage.

<http://www.ipsasb.org>

Review Questions

Question 1

Transfers may have stipulations attached. An entity analyzes stipulations attached to transfers to determine whether those stipulations impose conditions or restrictions on use of assets. Conditions on a transferred asset give rise to a liability on initial recognition. A condition includes stipulations that

- a) **Require an entity to use an asset for a particular purpose**
- b) **A penalty will be incurred if the asset is not used as specified**
- c) **Require the entity to use the asset as specified or return it to the transferor**
- d) **Require the entity to raise matching funds**

Question 2

The national government (transferor) lent a local government (reporting entity) CU20 million to enable the local government to build a water treatment plant. After a change in policy, the national government notifies the local government that it is forgiving the loan. There are no stipulations attached to the forgiveness of the loan.

How does the local government account for the loan forgiveness transaction? Why?

Question 3

The national government grants CU10 million to a provincial government under an agreement that it be used to improve mass transit systems. The agreement includes a five-year capital investment plan that identifies eligible projects. By June 30 of each year, the provincial government must submit an audited report of expenditures. The funds must be spent by the end year five. Unspent funds or the amount of ineligible expenditures are “clawed back” from other transfers that flow to the provincial government.

How is the transfer accounted for by the provincial government?

Question 4

A national government makes a cash transfer of CU50 million to a state government social housing entity, specifying that it:

- a) Increases the stock of social housing by an additional 1,000 units over and above any other planned increases; or
- b) Uses the cash transfer in other ways to support its social housing objectives.

If neither of these stipulations is satisfied, the recipient entity must return the cash to the national government.

How is the transfer accounted for by the state government social housing entity? Why?

Answers to Review Questions

Question 1

The answer is (c).

The key distinction between a condition that imposes a liability on an entity and other stipulations is the requirement to return the transferred assets if the conditions are breached.

The mere specification that a transferred asset is required to be consumed in providing goods and services to third parties is, in itself, not sufficient to give rise to a liability when the entity gains control of the asset.

A stipulation that requires an entity to return the asset to the transferor if a specified future event does not occur does not create a liability at initial recognition. A return obligation does not arise until such time as it is expected that the stipulation will be breached, and a liability is not recognized until the recognition criteria have been satisfied. For example, a national government provides funds to a provincial government entity subject to the stipulation that the entity raise a matching contribution. A liability does not arise until the provincial government expects that it will not be able to raise the matching funds.

Question 2

When it receives the notification from the national government, which communicates its decision to forgive the loan, the local government derecognizes the liability for the loan and recognizes revenue in the statement of financial performance of the reporting period in which the liability is derecognized.

Lenders will sometimes waive their right to collect a debt owed by a public sector entity, effectively canceling the debt. Entities recognize revenue in respect of debt forgiveness when the former debt no longer meets the definition of a liability or satisfies the criteria for recognition as a liability. Revenue arising from debt forgiveness is measured at the carrying amount of the debt forgiven.

Question 3

In determining whether a stipulation is a condition or a restriction, it is necessary to consider the substance of the terms of the stipulation and not merely its form. The mere specification that, for example, a transferred asset is required to be consumed in providing goods and services to third parties or be returned to the transferor is, in itself, not sufficient to give rise to a liability when the entity gains control of the asset.

To satisfy the criteria for recognition as a liability, it is necessary that an outflow of resources will be probable, and performance against the condition is required and is able to be assessed. Therefore, a condition will need to specify such matters as the nature or quantity of the goods and services to be provided or the nature of assets to be acquired as appropriate and, if relevant, the periods within which performance is to occur. In addition, performance will need to be monitored by, or on behalf of, the transferor on an ongoing basis.

In this case, the provincial government has entered into a binding agreement that stipulates that the funds be used to improve mass transit systems. The agreement includes a five-year capital investment plan that identifies specific eligible projects. There is a time frame within which funds must be spent for the purposes stipulated. There is a reporting mechanism to monitor the compliance of the provincial government with the terms of the agreement. There is a mechanism for the claw back of unspent funds or ineligible expenditures.

Lacking evidence to the contrary, the provincial government assumes that the national government would enforce the agreement and, therefore, the stipulations in it would meet the definition of a condition.

The provincial government recognizes the grant money as an asset. The provincial government also recognizes a liability in respect of the condition attached to the grant. As the province satisfies the condition, that is, as it makes authorized expenditures, it reduces the liability and recognizes revenue in the statement of financial performance of the reporting period in which the liability is discharged.

Question 4

The state government social housing entity recognizes an increase in an asset (cash) and revenue in the amount of CU50 million. The stipulations in the transfer agreement are stated so broadly as to not impose on the recipient a performance obligation – the performance obligation is imposed by the operating mandate of the entity, not by the terms of the transfer.



IPSASB Proposals for Revenue



Purpose of Session

The IPSASB is proposing changes to its requirements for accounting for revenue

Participants who are preparing to adopt the accrual basis IPSAS should be aware of the proposals so that they can ensure any revenue systems and procedures being developed for the transition process will be capable of dealing with the proposed accounting.

The accounting discussed in this session relates to proposals only and is therefore subject to change.

Because this final session discusses proposals rather than requirements published by the IPSASB, there are no review questions. The purpose of this session is to provide sufficient information for participants to identify whether their processes and systems are capable of providing the information needed to implement the proposals if the IPSASB agrees to proceed with them.



Proposed New Standards

- [ED 70, Revenue with Performance Obligations](#)
- [ED 71, Revenue without Performance Obligations](#).

These proposals are complemented by a proposed new Standard on transfer expenses. ED 72, *Transfer Expenses* is discussed in the Expenses module.

Under these proposals, the current distinction between revenue transactions that are exchange transactions and those that are non-exchange transactions will be replaced by a distinction based on whether the entity must satisfy performance obligations to be entitled to the revenue or not.



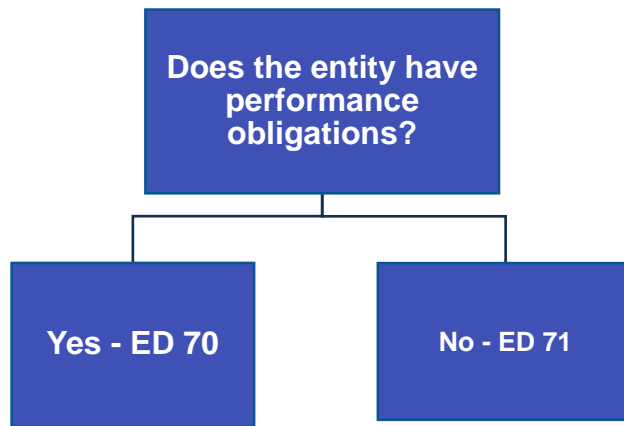
Performance Obligations

A performance obligation is a promise in a binding arrangement with a purchaser to transfer to the purchaser or third-party beneficiary either:

- a) A good or service (or a bundle of goods or services) that is distinct; or
- b) A series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the purchaser or third-party beneficiary.

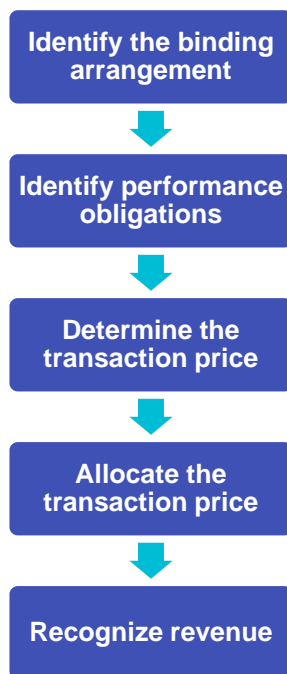
The performance obligation concept is used to determine whether a revenue transaction is within the scope of ED 70 or ED 71. Furthermore, under ED 70, revenue is recognized when (or as) a performance obligation is satisfied by the transfer of the promised goods or services to the purchaser or third-party beneficiary.

Types of Revenue



For there to be performance obligations, there must first be a binding arrangement (a contract or similar). If the binding arrangement imposes performance obligations on the entity in exchange for the revenue it will receive, the transaction is accounted for under ED 70. If there is no binding arrangement, or the binding arrangement does not impose performance obligations on the entity in exchange for the revenue it will receive, the transaction is accounted for under ED 71.

Performance Obligations



Step 1: Identify the Binding Arrangement

The parties to the binding arrangement must have approved the binding arrangement and be committed to performing their respective obligations.

The entity must be able to identify each party's rights regarding the goods or services to be transferred and be able to identify the payment terms for the goods or services to be transferred.

The binding arrangement must also have economic substance, and it must be probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred.

ED 70 proposes detailed guidance on the accounting for binding arrangements which do not meet all of the above criteria.

Step 2: Identify Performance Obligations

At the inception of the binding arrangement, the entity shall identify all performance obligations in the binding arrangement.

A performance obligation in this step of the model is the same as the performance obligation concept used to determine whether a transaction falls within the scope of ED 70 or ED 71.

Step 3: Determine the Transaction Price

The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services.

Determination of the transaction price may be complex due to the following factors:

- Variable consideration;
- Existence of a significant financing component;
- Non-cash consideration; and
- Consideration payable to a purchaser.

Step 4: Allocate the Transaction Price

The total transaction price is typically allocated to individual performance obligations based on their relative stand-alone price.

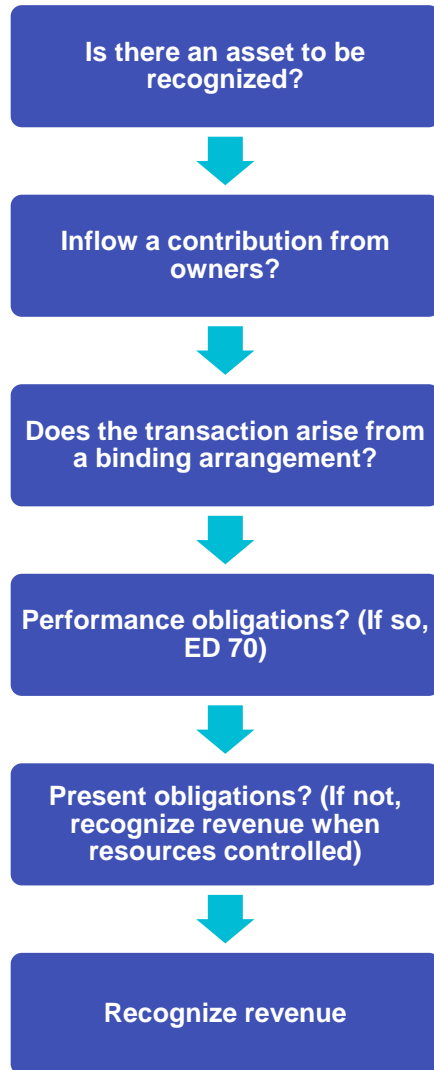
The stand-alone price of a good or service is the amount of consideration to which the entity expects to be entitled in exchange for transferring the individual promised goods or services.

Step 5: Recognize Revenue

An entity recognizes revenue at the amount allocated to a performance obligation when (or as) the entity satisfies that performance obligation by transferring the promised good or service.

A good or service is transferred when (or as) the purchaser or third-party beneficiary obtains control of that good or service—this transfer of control can occur at a point in time or over time

Accounting for Revenue without Performance Obligations



Step 1 – Is there an asset to be recognized?

If there is no asset to be recognized, then there is no revenue to be recognized. If an asset meets the definition and recognition criteria move onto Step 2.

Step 2 – Does the inflow result from a contribution from owners?

Contributions from owners are not revenue and are therefore outside the scope of ED 71. If the inflow is not a contribution from owners move onto Step 3.

Step 3 – Does the transaction arise from a binding arrangement?

If the transaction does not arise from a binding arrangement then revenue is recognized when the transfer recipient has control of the resources (DR Resources (e.g., Cash) CR Revenue). If the transaction arises from a binding arrangement move onto Step 4.

Step 4 – Are there performance obligations in the binding arrangement?

If there are performance obligations in the binding arrangement, then the proposals in ED 70 are the correct requirements to use. If there are no performance obligations, move onto Step 5.

Step 5 – Are there present obligations in the binding arrangement?

If there are no present obligations in the binding arrangement, then revenue is recognized when the transfer recipient has control of the resources (the same as in Step 3). If there are present obligations move onto Step 6.

Step 6 – Recognize revenue when (or as) present obligations are met.

If the transaction has present obligations then when the transfer recipient has control of the resources, they will initially recognize an asset and a liability (e.g., DR Cash, CR Liability). As the present obligations are met, the transfer recipient will recognize revenue and derecognize the liability in an amount of the revenue recognized. (e.g., DR Liability, CR Revenue)

ED 71 covers two types of transaction – those with present obligations (that do not meet the definition of a performance obligation in ED 70), and those without present obligations.

Revenue without present obligations can arise where:

- a) There is no binding arrangement; or
- b) The binding arrangement does not impose any present obligations on the entity.



Present Obligations in ED 71

- Capital Transfers
- Eligible Expenditure
- Specified Activity

A **capital transfer** is an inflow that arises from a binding arrangement, or cash or another asset with a requirement that the transfer recipient acquires or constructs a non-financial asset that will be controlled by the transfer recipient.

Capital transfers are within the scope of ED 71 and not ED 70 because there is no requirement to transfer the asset once acquired or constructed.

An example of a capital transfer is using resources provided to build a hospital.

An **eligible expenditure** is an outflow of resources incurred in accordance with the requirements set out in a binding arrangement. An eligible expenditure does not have an identifiable specified activity.

A **specified activity** is an action specified in a binding arrangement that must be completed by a transfer recipient.

An example of eligible expenditure is using resources provided to pay the salary for a particular position within an entity – e.g., medical specialist

An example of a specified activity is using resources to buy hospital beds for a hospital.



Accounting for Taxes Under ED 71

ED 71 does not propose any changes in the accounting for tax revenue. Accounting for taxes would remain the same as in IPSAS 23.

For Further Information

That concludes our module on IPSASB proposals for revenue. Participants seeking more information on the proposals should refer to the documentation on the IPSASB website.

Visit the IPSASB webpage.

<http://www.ipsasb.org>

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