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Mr John Stanford
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International Public Sector Accounting Standards Board
International Federation of Accountants
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Submission via www.ifac.org

Dear John

Submission on Consultation Paper: Accounting for Revenue and Non-Exchange Expenses

We welcome the opportunity to comment on the Consultation Paper ("the CP"). Our responses to the specific questions raised in the CP are set out in Appendix A. We commend the IPSASB for its efforts in identifying the divergent accounting treatment of revenue and expenses, and proposing an alternative model. Against this back drop of support below we outline a summary of our responses:

- The proposed model for recognition of both revenue and expenses is over-complicated.
- Revenue transactions should not be classified as exchange or non-exchange.
- Revenue transactions should not be categorised as A, B or C.
- The model for revenue recognition should be based on whether there are sufficiently specific performance obligations.
- Where there are sufficiently specific performance obligations, a public sector performance obligation approach based on the principles of IFRS 15 should be applied.
- Where sufficiently specific performance obligations do not exist, a residual standard or a residual section of a standard based on the applicable parts of IPSAS 23 should be applied.
- Where an agreement contains consumption-based terms, such as time requirements, these should be accounted for as an 'other obligation' so revenue can be deferred.
- The model for expense recognition does not necessarily have to mirror the revenue recognition approach.

In New Zealand the accounting standards for public benefit entities (PBEs), which includes both public sector entities and not-for-profit entities (NFPs), are mainly based on IPSAS. The New Zealand Accounting Standards Board (NZASB) modifies IPSAS for application by NFPs. Where applicable, the language is generalised and NFP-specific illustrative examples are added. NFPs have their own set of unique challenges, and as such the implications for this sector must be considered too.

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We note that the Australian Accounting Standards Board (AASB) completed a similar project at the end of 2016 and issued AASB 1058 *Income of Not-for-Profits*. We encourage the IPSASB to draw upon this project as the AASB has already worked through some of the challenges outlined in the CP.

Appendix B includes more information about Chartered Accountants Australia and New Zealand (CA ANZ). Should you have any queries concerning the matters in this submission, or wish to discuss them in further detail, please contact Ceri-Ann Ross (Reporting Leader) via email; ceri-ann.ross@charteredaccountantsanz.com.

Yours sincerely

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Appendix A: Responses to specific questions

Preliminary View 1

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

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

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

We agree with replacing IPSAS 9 and IPSAS 11 with an IPSAS primarily based on IFRS 15. We support close alignment between IFRS and IPSAS so that financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances. This reduces consolidation adjustments for mixed groups.

We support removal of the extant exchange or non-exchange distinction, but we do not agree with the three categories of revenue transactions as proposed in the CP. We believe it is appropriate to apply the principles of IFRS 15 to all transactions which contain sufficiently specific performance obligations. In our view, such transactions should be accounted for using the proposed public sector performance obligation approach (PSPOA) that is based on the five-step revenue recognition model in IFRS 15.

Preliminary View 2

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

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

We agree that revenue transactions that do not contain sufficiently specific performance obligations should be accounted for under a residual standard or a residual section of a standard, based on the applicable parts of IPSAS 23. As mentioned above, we do not agree with the categorisation of revenue transactions into A, B and C.

Specific Matter for Comment 1

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

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

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

We have no specific comments on (a) or (b). Areas in IPSAS 23 that we understand to be challenging, broadly speaking, are:

- The initial distinction between whether a transaction is exchange or non-exchange.
- Tripartite arrangements. These do not meet the definition of an exchange transaction because they are not a ‘direct’ transaction. However in all other ways they have the substance of an exchange transaction.
- Transactions that include both an exchange component and a non-exchange component. This is particularly evident in transactions like university fees for example, where a degree is received but the amount paid by the student is only a small portion of the total cost to taxpayers.
- Determining whether a provision in law, regulation or other arrangement is enforceable through legal or administrative processes, and thus is in fact a stipulation (restriction or condition).
- Agreements where funding is to be used in a specific time period (“time requirements”) but no other stipulations. The absence of a ‘use or return’ condition gives rise to revenue at the point at which the funds are receivable. It can be problematic where the associated costs related to the funding are recognised in a different reporting period. Despite the disclosure of such unexpended funds, many users do not understand the substance of the transaction and this can have unintended consequences for the entity concerned such as reductions in future funding.

Preliminary View 3

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

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

As per our response to PV1, we believe the PSPOA should be applied to all transactions which contain sufficiently specific performance obligations. As previously noted, we do not agree with the categorisation of revenue transactions into A, B and C.

Specific Matter for Comment 2

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

Step 1 – Identify the binding arrangement
Step 2 – Identify the performance obligation
Step 3 – Determine the consideration
Step 4 – Allocate the consideration
Step 5 – Recognise revenue

Do you agree with the proposals on how each of the IFRS 15 five-steps could be broadened? If not, explain your reasons.

We agree with broadening the requirements in the IFRS 15 five-step approach, and the proposals for how they could be broadened. We encourage the IPSASB to consider further broadening step 2 so that the construction or acquirement of an asset meets the definition of a performance obligation. This would enable capital grants to also be accounted for using the PSPOA. Also see our response to SMC5.

Specific Matter for Comment 3

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

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

Please explain your reasons.

As previously noted, we do not agree with the categorisation of revenue transactions into A, B and C. In our view, the model for revenue recognition should be based on whether there are sufficiently specific performance obligations. We agree that a time requirement does not create a performance obligation and does not meet the definition of a liability in the IPSASB Conceptual Framework. Therefore such transactions should be accounted for under a residual standard or a residual section of a standard based on the applicable parts of IPSAS 23.

Our preference is for option (d) – such revenue transactions should be accounted for as 'other obligations' so the revenue can be deferred. We note that 'other obligations' are provided for in paragraph 5.27 of the IPSASB Conceptual Framework where an obligation does not satisfy the definition of an element. This would convey to users of the financial statements that the entity has resources that are intended for use in subsequent reporting periods. This avoids the unintended consequences that are discussed in our response to SMC1.

Option (e) also makes sense conceptually, but our preference is to keep the accounting treatment as simple as possible so that users understand the substance of the transaction.

Specific Matter for Comment 4

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

(a) Yes
(b) No

Please explain your reasons.

No. We support removal of the distinction between exchange revenue and non-exchange revenue because it causes challenges that are discussed in our response to SMC1.

Preliminary View 4

The IPSASB considers that accounting for capital grants should be explicitly addressed within IPSAS. Do you agree with the IPSASB's Preliminary View 4? If not, please give your reasons.

We agree with the IPSASB's preliminary view.

Specific Matter for Comment 5

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

This is one area that the AASB had to work through in its project. Capital grants are explicitly separately addressed in AASB 1058 and revenue is recognised as and when obligations are satisfied, instead of upon receipt. The challenge arises because the obligation is to construct or acquire an asset, not to deliver goods or services. Therefore this does not meet the definition of a performance obligation so the transaction is technically out of scope of IFRS 15. We note that the accounting treatment of capital grants under AASB 1058 is the same as it would be under IFRS 15. In our view, the definition of performance obligation should be further broadened so that the capital grants could be accounted for using the PSPOA. Also see our response to SMC2.

Specific Matter for Comment 6

Do you consider that the IPSASB should:

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

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

We support the option to recognise revenue from services in kind (and the associated expense) where they can be reliably measured and those services would have been purchased if they had not been donated. Given the amount of volunteer services provided to the sector and the inherent issues in determining fair value, we believe additional research and cost-benefit analyses should occur before any mandatory requirements are introduced.

User needs would be better met by disclosure of non-financial information in this regard. Increased transparency as to how reliant on volunteer services the public sector is would better facilitate policy decisions. This is particularly so for those entities where without volunteers, governments may need to step in (eg essential services such as ambulance and fire).

Preliminary View 5

The IPSASB is of the view that non-exchange transactions related to universally accessible services and collective services impose no performance obligations on the resource recipient. These non-exchange transactions should therefore be accounted for under the Extended Obligating Event Approach.

Do you agree with the IPSASB's Preliminary View 5? If not, please give your reasons.

We agree that universally accessible services and collective services impose no performance obligations on the resource recipient. However, we do not agree that such transactions should be accounted for using the Extended Obligating Event Approach (EOEA). In our view, universally accessible services and collective services have similar characteristics to social benefits and therefore should be considered in conjunction with the Social Benefits project. We note that ED 63 is proposing to use an Obligating Event Approach (OEA) for the recognition of social liabilities.

Preliminary View 6

The IPSASB is of the view that, because there is no obliging event related to non-exchange transactions for universally accessible services and collective services, resources applied for these types of non-exchange transactions should be expensed as services are delivered.

Do you agree with the IPSASB's Preliminary View 6? If not, please give your reasons.

There are varying views as to whether the existence of legislation (or similar) that provides for such services to be delivered establishes an obligating event. These are discussed in ED 63. We encourage the IPSASB to consider the decisions made in the social benefits project in the development of an approach for universally accessible services and collective services.

Preliminary View 7

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

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

The model for expense recognition does not necessarily have to mirror the revenue recognition approach. Whilst using the PSPOA is conceptually sound for expense transactions with performance obligations, it poses a number of challenges in practice. The primary issue is information availability. The PSPOA is reliant on the resource recipient providing reliable reporting of the achievement of performance obligations to the resource provider. Our preference is to keep the accounting treatment as simple as possible. Grants in particular are made with no expectation that any funds will be returned. Therefore, in our view these types of transactions should be expensed as the commitment to provide the resource is entered into.

Preliminary View 8

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

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

We agree with the IPSASB's preliminary view for statutory receivables. Statutory receivables do not generally have performance obligations so the PSPOA would not apply to such transactions. It is challenging to determine fair value for such transactions, and face value is more understandable to users than fair value. However, this approach may not be appropriate for other types of non-contractual receivables. Initial recognition of other types of non-contractual receivables would depend on the applicable revenue recognition model.

Preliminary View 9

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

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

We agree with the IPSASB's preliminary view for statutory receivables. It appears to be the most workable in practice of the three approaches proposed in the CP. However, this approach may not be appropriate for other types of non-contractual receivables. Subsequent measurement of other types of non-contractual receivables would depend on the applicable revenue recognition model.

Specific Matter for Comment 7

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

(a) Cost of Fulfilment Approach
(b) Amortised Cost Approach

(c) Hybrid Approach; or
(d) IPSAS 19 requirements?
Please explain your reasons.

Subsequent measurement of non-contractual payables would depend on the applicable expense recognition model. But the Cost of Fulfilment Approach (CFA) is our preference because social benefits are non-contractual payables and the CFA is consistent with the proposals in ED 63.

Appendix B: About Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand is a professional body comprised of over 117,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations.
We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation accounting professionals across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.