The Chartered Institute of Public Finance & Accountancy

IPSASB Consultation Paper
Accounting for Revenue and Non-Exchange Expenses

response to consultation paper

15 January 2018

the people in public finance

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As the world's only professional accountancy body to specialise in public services, CIPFA's portfolio of qualifications are the foundation for a career in public finance. They include the benchmark professional qualification for public sector accountants as well as a postgraduate diploma for people already working in leadership positions. They are taught by our in-house CIPFA Education and Training Centre as well as other places of learning around the world.

We also champion high performance in public services, translating our experience and insight into clear advice and practical services. They include information and guidance, courses and conferences, property and asset management solutions, consultancy and interim people for a range of public sector clients.

Globally, CIPFA shows the way in public finance by standing up for sound public financial management and good governance. We work with donors, partner governments, accountancy bodies and the public sector around the world to advance public finance and support better public services.

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International Public Sector Accounting Standards Board
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Dear IPSASB secretariat

IPSASB Consultation Paper
Accounting for Revenue and Non-Exchange Expenses

CIPFA is pleased to present its comments on this Consultation Paper, which has been reviewed by CIPFA's Accounting and Auditing Standards Panel.

Revenue reporting is a key area for the public sector, whether reflecting commercial imperatives, or the distinctive non-exchange aspect of public services transactions. We also agree that there is a pressing need to fill the gap in the current IPSASB literature on accounting for non-exchange expenses.

CIPFA particularly welcomes IPSASB's engagement with IFRS 15, both as a means of maintaining alignment with private sector best practice when appropriate, and as an opportunity to review existing approaches to public sector reporting. And while we remain of the view that the exchange/non-exchange distinction is fundamentally important to the theory underlying public sector financial reporting, we are very interested in the approaches in this Consultation Paper. Especially those which, rather than trying to more precisely delineate the various combinations of exchange and non-exchange, focus on other aspects of the arrangements.

Response to Specific Matters for Comment

Responses to the SMCs are attached as an Annex.

I hope this is a helpful contribution to IPSASB's work in this area. If you have any questions about this response, please contact Steven Cain
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Yours sincerely

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CIPFA RESPONSES TO ITEMS RAISED IN THE REQUEST FOR COMMENTS

Preliminary View 1 (following paragraph 3.8) The IPSASB considers that it is appropriate to replace IPSAS 9, Revenue from Exchange Transactions, and IPSAS 11, Construction Contracts with an IPSAS primarily based on IFRS 15, Revenue from Contracts with Customers. Such an IPSAS will address Category C transactions that: (a) Involve the delivery of promised goods or services to customers as defined in IFRS 15; and (b) Arise from a contract (or equivalent binding arrangement) with a customer which establishes performance obligations. Do you agree with the IPSASB's Preliminary View 1? If not, please give your reasons
CIPFA agrees with IPSASB's Preliminary View 1. We support straightforward convergence between IFRS and IPSAS for transactions with no specifically non-commercial features, including cases which arise from binding arrangements other than contracts.
Preliminary View 2 (following paragraph 3.9) Because Category A revenue transactions do not contain any performance obligations or stipulations, the IPSASB considers that these transactions will need to be addressed in an updated IPSAS 23. Do you agree with the IPSASB's Preliminary View 2? If not, please give your reasons.
CIPFA agrees with IPSASB's Preliminary View 2. Category A comprises transactions which are straightforwardly non-exchange, to which the original IPSAS 23 applies without controversy. For these transactions, an updated IPSAS 23 seems appropriate.

Specific Matter for Comment 1 (following paragraph 3.10)

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

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

If you believe that there are further areas where the IPSASB should consider providing further 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.

Public sector reporting in the UK does not directly follow IPSAS, but the accounting treatment of taxes, including national insurance contributions, is similar to that set out in IPSAS 23. The UK has experienced no issues in accounting for social contributions.

We acknowledge that accounting for taxes with long collection periods can be complex and the amounts recognised will often be estimates of the amounts receivable. Accountants need to work with others in determining an appropriate methodology to obtain those estimates.

Preliminary View 3 (following paragraph 4.64)

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

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

CIPFA agrees with IPSASB's Preliminary View 3.

That is, Category B transactions should be accounted for using Approach 2 as described from para 4.25-4.58.

Specific Matter for Comment 2 (following paragraph 4.64)

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 (paragraphs 4.29 - 4.35);
Step 2 – Identify the performance obligation (paragraphs 4.36 - 4.46);
Step 3 – Determine the consideration (paragraphs 4.47 – 4.50);
Step 4 – Allocate the consideration (paragraphs 4.51 – 4.54); and
Step 5 – Recognize revenue (paragraphs 4.55 – 4.58).

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

If not, please explain your reasons.

In line with our agreement with Preliminary View 3, CIPFA agrees with these specific aspects of Approach 2.

These broadened requirements seem to be natural counterparts to the IFRS 15 five step approach when considered in the broader context of both contractual obligation and binding arrangements.

Specific Matter for Comment 3 (following paragraph 4.64)

If the IPSASB were to implement Approach 1 and update IPSAS 23 for Category B transactions, which option do you favor 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) - Recognize transfers with time requirements in net assets/equity and recycle through the statement of financial performance.

Please explain your reasons.

Per our response to Preliminary View 3, and Specific Matters for Comment 1 and 2, CIPFA supports Approach 2. However, if IPSASB were to implement Approach 1, then our view on the best approach depends on the extent of review of the current requirements in IPSAS 23 generally, including stipulations which are not time requirements.

If IPSAS 23 is otherwise left basically unchanged, then we suggest that the best approach would be (d) Option (e) - Recognize transfers with time requirements in net assets/equity and recycle through the statement of financial performance.

As noted in the Consultation Paper, this maintains consistency with the conceptual framework. However, in contrast with (a) Option (b) it does offer a way to track the effect of time requirements through the main financial statements. Having said this, whether or not this is superior will depend on the specific implementation – while we are hopeful that this could be done in a way that addresses the concerns of some preparers and users of GPFS, we do not have fully developed thoughts on this. And as noted above, CIPFA supports Approach 2.

If IPSAS 23 is subject to more general review, other approaches might be possible. When developing IPSAS 23, IPSASB were concerned that preparers might recognise liabilities in respect of restrictions with no substance or which are not effective. As a consequence of mitigating this risk, the class of liabilities recognised under IPSAS 23 may be narrower than those which would be recognised from a purely conceptual perspective.

The issue of how to account for time requirements – be they related to the receipt of a grant or transfer in advance of the period for which its use is intended, or to a grant or transfer that covers more than one year – is of significant concern across many jurisdictions, including the UK. The issue needs to be resolved, and we suggest that this might need to be considered in the light of a fuller discussion of substance over form. Insofar as IPSAS 23 discusses substance over form, this is only to reduce the situations where a liability is recognised. There is no consideration of substance over form in circumstances where restrictions taken together with other factors may give rise to a non legally binding obligation (or constructive obligation using the terminology of IPSAS 19 and 23). Some stakeholders also challenge paragraph 19 of IPSAS 23, which suggests that a restriction (ie a stipulation without a return obligation) does not result in a binding obligation, unless and until enforcement action has been taken and/or a legal penalty has been incurred.

If a revised IPSAS 23 approach is developed which mitigates the risk of over-recognition while recognising more performance obligations when these are effective, then we would expect this to improve the treatment of some stipulations which combine time requirements with other factors. Whether they would provide a basis for improving the treatment of stipulations which reflect *only* time requirements is more difficult to assess.

Specific Matter for Comment 4 (following paragraph 4.64)
Do you consider that the option that you have identified in SMC 3 should be used in combination with Approach 1 Option (a) – Provide additional guidance on making the exchange/non-exchange distinction?

(a) Yes

(b) No

Please explain your reasons.

Per our response to Preliminary View 3, and Specific Matters for Comment 1 and 2, CIPFA supports Approach 2. One of the advantages of Approach 2 for Category B is that it does not require a sharp distinction to be made between exchange and non-exchange.

However, if IPSASB were to implement Approach 1 for Category B, this issue may need to be addressed. This will depend on the specific changes made to IPSAS 23.

In particular it is not clear to us that cases where there are time requirements are the only ones where making the distinction is difficult and matters to the accounting treatment. Nor is it clear to us that adopting any of Approach 1 Option (b) to Approach 1 Option (e) will obviate the need for this distinction to be addressed.

Unless the IPSASB is able to show that the need for guidance is very substantially diminished by changes made to IPSAS 23, CIPFA considers that the concerns raised by stakeholders would warrant additional guidance.

CIPFA's answer to SMC4 is therefore (a) Yes

Preliminary View 4 (following paragraph 5.5)

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

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

CIPFA agrees with IPSASB's Preliminary View 4.

Specific Matter for Comment 5 (following paragraph 5.5) (a) Has the IPSASB identified the main issues with capital grants? If you think that there are other issues with capital grants, please identify them. (b) Do you have any proposals for accounting for capital grants that the IPSASB should consider? Please explain your issues and proposals.
CIPFA considers that the CP sets out the main issues with capital grants CIPFA has no specific proposals for accounting for capital grants at this stage.
Specific Matter for Comment 6 (following paragraph 5.9) Do you consider that the IPSASB should: (a) Retain the existing requirements for services in- kind, which permit, but do not require recognition of services in-kind; or (b) Modify requirements to require services in-kind that meet the definition of an asset to be recognised in the financial statements provided that they can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information; or (c) An alternative approach. Please explain your reasons. If you favor an alternative approach please identify that approach and explain it.
CIPFA considers that the IPSASB should pursue approach (b). This is in keeping with the principle that financial reporting should recognise items which satisfy the requirements for recognition, subject to practical consideration of whether these can be measured in a meaningful and reliable way at proportionate cost.
Preliminary View 5 (following paragraph 6.37) The IPSASB is of the view that non-exchange transactions related to universally accessible services and collective services impose no performance obligations on the resource recipient. These non-exchange transactions should therefore be accounted for under The Extended Obligating Event Approach. Do you agree with the IPSASB's Preliminary View 5? If not, please give your reasons.
CIPFA agrees with IPSASB's Preliminary View 5.

Preliminary View 6 (following paragraph 6.39) The IPSASB is of the view that, because there is no obligating event related to non-exchange transactions for universally accessible services and collective services, resources applied for these types of non-exchange transactions should be expensed as services are delivered. Do you agree with the IPSASB’s Preliminary View 6? If not, please give your reasons.
CIPFA agrees with IPSASB’s Preliminary View 6.
Preliminary View 7 (following paragraph 6.42) The IPSASB is of the view that where grants, contributions and other transfers contain either performance obligations or stipulations they should be accounted for using the PSPOA which is the counterpart to the IPSASB’s preferred approach for revenue. Do you agree with the IPSASB’s Preliminary View 7? If not, please give your reasons
CIPFA agrees with IPSASB’s Preliminary View 7.

Preliminary view 8 (following paragraph 7.18)

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

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

(a) Information on the value of what *should* be receivable

CIPFA agrees that, for accountability purposes it is important to know the value of what should be paid to the entity as a non-contractual receivable.

In cases where the full amount is due immediately, this will equate to the face value (legislated amount). We can however envisage situations where settlement of all or part of the full amount can be legitimately deferred. Under these circumstances there is no impairment because no events have occurred or are anticipated which affect the amount due. However, the present value of the receivable at inception is less than face value. Thus, where the amount deferred and the deferral period are significant, it would be appropriate to use discounted cash flow techniques to determine the present value. Otherwise a false impairment will be shown on subsequent remeasurement at fair value.

(b) Information on the present value of *expected* receipts

CIPFA agrees that, having determined the value of what should be receivable, it is necessary to adjust this to reflect known expectations of the present value of what will be received over time. The two main factors affecting this are where amounts are uncollectible, and where collection is significantly delayed. The proposal in Preliminary View 8 does not reflect delays to collection which are expected at inception, and may therefore result in an overstated value for the receivable.

Comment on Preliminary View 8

Against this background, CIPFA supports IPSASB's Preliminary View 8, which is straightforward and notwithstanding the points raised above will work well in many situations.

In respect of (a) above, we suggest that problems in this area can be addressed through explanation in notes.

In respect of both (a) and (b), any misstatement should be corrected immediately on the first remeasurement; the fair value basis will incorporate assumptions about the timing of collection.

Preliminary View 9 (following paragraph 7.34)

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

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

CIPFA agrees with IPSASB's Preliminary View 9.

Specific Matter for Comment 7 (following paragraph 7.46)

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

(a) Cost of Fulfillment Approach:
(b) Amortized Cost Approach;
(c) Hybrid Approach; or
(d) IPSAS 19 requirements?

Please explain your reasons.

CIPFA agrees with the point articulated at the end of para 7.44 of the Consultation Paper, which is that non-contractual payables with cash flows that are certain in timing **or** amount can be considered to be analogous to financial instruments. For payables where there is less certainty, it is more difficult to make this analogy.

However, this is used to support an approach that applies the analogy only to non-contractual payables with cash flows that are certain in timing **and** amount. This is not a conclusion that we would reach without further work.

Now we can see that there is a continuum of uncertainty. At one end there are cases where both timing and amount are certain. At the other, neither timing nor amount is certain. And between these there are cases where timing is certain, or amount is certain, but not both.

Against this background, CIPFA supports Option (c) the Hybrid Approach. However when carrying out further development we suggest that IPSASB should give more consideration to the circumstances under which the amortized cost approach becomes too difficult to apply. This might result in extending the use of the amortised cost approach in line with the final sentence of para 7.44, or provide justification for the hybrid approach as proposed. Stakeholder responses to this SMC may provide relevant input to this process.