



<b>Project:</b>	<b>IPSASB Exposure Drafts on Revenue and Transfer Expenses (ED 70, 71 &amp; 72)</b>	<b>Meeting:</b>	AASB September 2020 (M177)
<b>Topic:</b>	<b>Draft AASB submission to IPSASB</b>	<b>Agenda Item:</b>	8.1
		<b>Date of this paper:</b>	2 September 2020
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		<b>Decision-Making:</b>	Medium
		<b>Project Status:</b>	Consider draft submission to IPSASB

## Objective of this agenda item

- 1 The objective of this agenda item is for the Board to:
  - (a) **provide feedback** to staff on the draft responses to the International Public Sector Accounting Standards Board (IPSASB) in respect of the three Exposure Drafts listed in paragraph 2; and
  - (b) for each Exposure Draft, **decide** on which Specific Matters for Comment (SMC) to comment.

## Reasons for the Board to consider this paper at this meeting

- 2 The IPSASB issued the following three Exposure Drafts (EDs) in February 2020 for comment until 1 November 2020.
  - ED 70 *Revenue with Performance Obligations*;
  - ED 71 *Revenue without Performance Obligations*; and
  - ED 72 *Transfer Expenses*.
- 3 Paragraph 20 of *The AASB's Approach to International Public Sector Accounting Standards* (October 2019) states that the Board will make formal submissions to the IPSASB in response to significant consultation documents issued by the IPSASB where there is no equivalent IFRS Standard or a known gap or practice issue in public sector accounting, or

the document addresses a transaction or issue prevalent and significant to the public sector.

- 4 These EDs were not explicitly exposed in Australia as the Board has gone through its own due process when developing Appendix F – Australian implementation guidance for not-for-profit entities that accompanies AASB 15 *Revenue from Contracts with Customers* and AASB 1058 *Income of Not-for-Profit Entities*. Significant issues in accounting for transfer expenses have not been raised in Australia.
- 5 At the November 2019 meeting, the Board decided to comment on the then soon-to-be published Exposure Drafts. This is because even though the IPSASB had been developing these proposals based on IFRS 15 *Revenue from Contracts with Customers*, the Board was aware that the IPSASB might take a different approach to AASB 1058 and Appendix F of AASB 15. It would be useful for the AASB to comment to the IPSASB on any differences in accounting principles.
- 6 Since there is no Australian Accounting Standard specifically stipulating the recognition and measurement requirements for expenses from the transfer providers' perspective, it would be useful for the AASB to consider and comment on ED 72 as Australian entities providing funds/grants to another entity might benefit from further guidance on the recognition and measurement of transfer expenses.
- 7 Staff have contacted the Financial Reporting and Accounting Committee (FRAC), a sub-group of the Australasian Council of Auditors General (ACAG), and Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) to obtain their input on the IPSASB's proposals. However, they have not been in a position to comment as yet.
- 8 At this meeting, staff ask Board members to provide feedback to staff on the draft responses to the IPSASB and decide on which Specific Matters for Comment in each ED to comment. Staff plan to finalise the submission letter out of session in order to provide comments to the IPSASB by the 1 November 2020 due date.

### **Summary of staff views**

- 9 The overall staff views are summarised below:
  - ED 70 – Staff support the proposals in ED 70 as it is aligned with IFRS 15 and AASB 15;
  - ED 71 – Staff disagree with the proposal in ED 71 that an agreement to carry out a specified activity or to incur an eligible expenditure that is not a performance obligation would give rise to a present obligation for the transfer recipient;
  - ED 72 – Transfer expenses with performance obligations – Staff agree with the proposal in ED 72 for the transfer provider to recognise initially an asset if the binding arrangement has performance obligations and the transfer provider monitors the satisfaction of the performance obligations by the transfer recipient. However, staff are concerned that arrangements with the same nature might have a different accounting outcome depending only on whether the transfer provider does that monitoring; and

- ED 72 – Transfer expenses without performance obligations – Staff agree with the overall proposal for the transfer provider to recognise a transfer expense at the earlier of when (a) the transfer provider has a present obligation and (b) the resource is transferred to the transfer recipient.

### **Attachments (in supplementary folder)**

Agenda Paper 8.2 IPSASB ED 70 *Revenue with Performance Obligations* and At-a-Glance document

Agenda Paper 8.3 IPSASB ED 71 *Revenue without Performance Obligations* and At-a-Glance document

Agenda Paper 8.4 IPSASB ED 72 *Transfer Expenses* and At-a-Glance document

### **Structure**

10 This staff paper is set out as follows:

- (a) Background (paragraphs 11–22)
- (b) Proposed next steps (paragraph 23)
- (c) [Section A](#): IPSASB ED 70 *Revenue with Performance Obligations*
- (d) [Section B](#): IPSASB ED 71 *Revenue without Performance Obligations*
- (e) [Section C](#): IPSASB ED 72 *Transfer Expenses*
- (f) [Appendix](#): Glossary and Extracts from AASB 1058 (for reference only)

### **Background**

11 ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations* propose accounting requirements and guidance on revenue (arising from both exchange and non-exchange transactions). ED 72 *Transfer Expenses* proposes accounting requirements applicable to providers of non-exchange transactions (such as grants and contributions, but excluding social benefits, which are subject to an existing IPSAS).

### **ED 70 vs AASB 15**

12 ED 70 is primarily aligned with the requirements in IFRS 15 *Revenue from Contracts with Customers* and provides recognition, measurement, presentation and disclosure requirements for revenue transactions with performance obligations. It adopts the same five-step model in IFRS 15 in recognising revenue from transactions with performance obligations, but has modified some requirements and key terms for use in the public sector.

13 Therefore, ED 70 is expected to align with AASB 15 *Revenue from Contracts with Customers*, which is also based on IFRS 15. AASB 15 has been modified similarly by the addition of Aus paragraphs, Appendix F – Australian implementation guidance for not-for-

profit entities, Appendix G – Australian implementation guidance for not-for-profit public sector licensors, and accompanied by Australian illustrative examples for not-for-profit entities.

- 14 [Section A](#) of this paper provides a high-level summary of the approach the IPSASB has proposed in ED 70, staff views, and draft text for the AASB’s submission to the IPSASB.

### **ED 71 vs AASB 1058**

- 15 AASB 1058 *Income of Not-for-Profit Entities*, which is effective for reporting periods beginning on or after 1 January 2019, prescribes the accounting treatment for not-for-profit entities to recognise transactions where consideration to acquire an asset is significantly less than fair value principally to enable the entity to further its objectives, as well as accounting for the receipt of volunteer services.
- 16 IPSASB ED 71 proposes the accounting treatment for revenue and cash flows arising from transactions without performance obligations. Revenue transactions without performance obligations are transactions where there is no requirement for a transfer recipient to transfer any goods or services to a transfer provider or a third-party beneficiary (ED 71 paragraph 5).
- 17 Staff expect that AASB 1058 and ED 71 would scope in similar transactions because many transactions of not-for-profit public sector entities where consideration to acquire an asset is significantly less than fair value principally to enable the entity to further its objectives are likely to be transactions without performance obligations (eg grants, donations and taxes etc). However, staff note the accounting outcome proposed in ED 71 might be different from AASB 1058. Therefore, staff believe it is important for Board members to consider:
- the principles in ED 71, particularly where the proposals differ from AASB 1058 requirements; and
  - the rationale behind the IPSASB’s proposals that is different to the Board’s rationale for the Australian amendments to AASB 15 and AASB 1058.
- 18 [Section B](#) of this paper provides a high-level overview of the proposals in ED 71, a comparison with requirements in Australian Accounting Standards, staff views on the proposals, and draft text for the AASB’s submission to the IPSASB.

### **ED 72**

- 19 Currently, the AASB and the IPSASB do not have a Standard specifically on the recognition and measurement of expenses from the transfer providers’ perspective in respect of non-exchange transactions. ED 72 proposes accounting principles to recognise ‘transfer expenses’ from a transfer providers’ perspective. A transfer expense is “an expense arising from a transaction, other than taxes, in which an entity provides a good, service, or other asset to another entity (which may be an individual) without directly receiving any good, service, or other asset in return” (ED 72 paragraph 8).

20 [Section C](#) of this paper provides a summary of the key proposals in ED 72, staff views on the proposals, and draft text for the AASB’s submission to the IPSASB.

**Glossary**

21 ED 71 and ED 72 have introduced some defined terms (note [Section A](#) explains new defined terms introduced in ED 70). The definitions of the most relevant key terms are reproduced in the [Appendix](#) for reference to assist Board members in reviewing this paper.

**Questions to the Board**

22 Specific questions for the Board regarding staff’s views are contained in each section of the paper.

**Proposed next steps**

23 Staff propose the following steps to finalise the submission to the IPSASB for the Board’s consideration and comment. Staff will also discuss the proposals with stakeholders as opportunity permits.

Date	Tasks
<b>16-17 September 2020:</b> Board meeting	<ul style="list-style-type: none"> <li>• Board to provide feedback to staff on the draft responses to the IPSASB.</li> <li>• Board to form a subcommittee to review and approve the final submission letter.</li> </ul>
<b>Present to 9 October 2020</b>	<ul style="list-style-type: none"> <li>• Staff to prepare a draft submission letter.</li> </ul>
<b>9-23 October 2020</b>	<ul style="list-style-type: none"> <li>• Board subcommittee to review the draft submission letter and provide feedback to staff.</li> </ul>
<b>30 October 2020</b>	<ul style="list-style-type: none"> <li>• Board subcommittee to approve the final submission.</li> </ul>

**Question to the Board:**

Q1 Do Board members agree with the proposed next steps in paragraph 23, including to form a subcommittee and finalise the submission out of session?

## Section A: IPSASB ED 70 *Revenue with Performance Obligations*

A1 This section contains a high-level overview of the approach the IPSASB has taken in developing ED 70 *Revenue with Performance Obligations* and staff views on the proposals. It is set out as follows:

- [Part 1: Overview of IPSASB’s approach in developing ED 70](#)
- [Part 2: Staff’s analysis and proposed responses to the Specific Matters for Comment.](#)

### Part 1: Overview of IPSASB’s approach in developing ED 70

A2 ED 70 is aligned with the requirements in IFRS 15 *Revenue from Contracts with Customers* and provides recognition, measurement and disclosure requirements for revenue transactions with performance obligations. It adopts the same five-step model in IFRS 15 in recognising revenue from transactions with performance obligations, but has modified some requirements and key terms for use in the public sector.

A3 Key modifications proposed in comparison with the requirements in IFRS 15 are as follows:

- (a) replaced the concept of a ‘contract’ in IFRS 15 with a broader concept of a ‘binding arrangement’<sup>1</sup>. This is because some public sector entities are not allowed to enter into ‘legal contracts’ but do enter into binding arrangements, which are similar in substance to contracts in the private sector or the public sector. The IPSASB also uses this term in other Standards;
- (b) expanded the explanation of the term ‘enforceability’ of a binding arrangement to include mechanisms that are outside the legal system, such as transactions through legislative or executive authority and/or cabinet or ministerial directives;
- (c) scoped in transactions with performance obligations where the ultimate beneficiary is a third party;
- (d) included public-sector-specific application guidance relating to:
  - the definition of a binding arrangement (paragraphs AG7–AG12);
  - the enforceability of a binding arrangement (paragraphs AG13-AG24); and
  - identifying the binding arrangement (paragraphs AG26–AG31); and
- (e) added public-sector-specific illustrative examples, as well as modifying the illustrative examples that accompany IFRS 15 to reflect scenarios in the public sector.

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1 “A binding arrangement is an arrangement that confers both enforceable rights and obligations on both parties to the arrangement. A contract is a type of binding arrangement.” (IPSASB ED 70 paragraph 7)

### **Staff's view on IPSASB's approach**

A4 Staff consider that ED 70 is consistent with all the accounting principles in IFRS 15. Additionally, staff noted that AASB 15 includes examples in paragraph F12 about the terms in an agreement that may result in 'enforceable rights and obligations', which might be useful for users of IPSAS in determining whether a binding arrangement exists. These examples are reproduced below for the Board's reference:

- (a) a refund in cash or kind is required when the agreed specific performance has not occurred;
- (b) the customer, or another party acting on its behalf, has a right to enforce specific performance or claim damages;
- (c) the customer has the right to take a financial interest in assets purchased or constructed by the entity with resources provided under the agreement;
- (d) the parties to the agreement are required to agree on alternative uses of the resources provided under the agreement; and
- (e) an administrative process exists to enforce agreements between sovereign States or between a State and another party.

### **Part 2: Staff's analysis and proposed responses to the Specific Matters for Comment**

A5 ED 70 contains five specific matters for comment (SMCs). Each SMC is reproduced below, in boxes, with draft wording for the proposed AASB response included below each SMC for the Board's review. Staff's analysis of each SMC is included below each box for the Board's consideration.

#### **Specific Matter for Comment 1:**

This Exposure Draft is based on IFRS 15, *Revenue from Contracts with Customers*. Because in some jurisdictions public sector entities may not have the power to enter into legal contracts, the IPSASB decided that the scope of this Exposure Draft would be based around binding arrangements. Binding arrangements have been defined as conferring both enforceable rights and obligations on both parties to the arrangement.

Do you agree that the scope of this Exposure Draft is clear? If not, what changes to the scope of the Exposure Draft or the definition of binding arrangements would you make?

#### **Proposed AASB response:**

The AASB agrees that the scope of ED 70 is clear.

Paragraph F12 of AASB 15 *Revenue from Contracts with Customers* provides additional examples of terms in an agreement that may result in enforceable rights and obligations, which could be added to the Application Guidance on enforceability in paragraphs AG13–AG24 of ED 70.

The AASB disagrees with paragraph AG24 of ED 70 (and paragraph 24 of ED 71) that if past experience indicates that the transfer provider never enforces an arrangement if a breach occurs, then the transfer recipient may conclude that the arrangement is not enforceable in substance. The AASB noted in paragraph F16 of AASB 15 that “The identification of an agreement as being enforceable by another party ... does not require a history of enforcement of similar agreements by the customer or even an intention of the customer to enforce its rights. A customer might choose not to enforce its rights against an entity. However, that decision is at the customer’s discretion, and does not affect the enforceability of the customer’s rights. Enforceability depends solely on the customer’s capacity to enforce its rights.”

- A6 As mentioned in paragraph A3, the scope of ED 70 is based on IFRS 15 but amended to replace the concept of a ‘contract’ with a broader concept of a ‘binding arrangement’ and extended to cover transactions with performance obligations where the ultimate beneficiary is a third party.
- A7 Therefore, staff are of the view that the scope of ED 70 is clear and is consistent with the scope of AASB 15 – Appendix F addresses various forms of arrangement that would be covered by the term ‘contract’ and discusses third-party arrangements in relation to the term ‘customer’.
- A8 Binding arrangements are defined as giving rise to enforceable rights and obligations for both parties. ED 70 includes application guidance addressing the enforceability of arrangements. AASB 15 paragraph F12 provides additional examples of terms that result in enforceable agreements, which staff suggest the IPSASB to consider adding to the Application Guidance in ED 70.
- A9 However, staff note that paragraph AG24 of ED 70 (as well as paragraph 24 of ED 71) states that if past experience indicates that the transfer provider never enforces an arrangement if a breach occurs, then the transfer recipient may conclude that the arrangement is not enforceable in substance. This is different to paragraph F16 of AASB 15, which states “Identification of an agreement as being **enforceable** by another party through legal or equivalent means **does not require a history of enforcement of similar agreements** by the customer or even an intention of the customer to enforce its rights. A customer might choose not to enforce its rights against an entity. However, that decision is at the customer’s discretion, and does not affect the enforceability of the customer’s rights. Enforceability depends solely on the customer’s capacity to enforce its rights.” [emphasis added]
- A10 Staff recommend the Board include specific comments in response to the IPSASB’s proposals regarding the enforceability of binding arrangements. The Board’s response to SMC1 is the best place to locate these comments.

**Specific Matter for Comment 2:**

This Exposure Draft has been developed along with [draft] IPSAS [X] (ED 71), *Revenue without Performance Obligations*, and [draft] IPSAS [X] (ED 72), *Transfer Expenses*, because there is an interaction between them. Although there is an interaction between the three Exposure Drafts, the IPSASB decided that even though ED 72 defines transfer expense, ED 70 did not need to define “transfer revenue” or “transfer revenue with performance obligations” to clarify the mirroring relationship between the exposure drafts. The rationale for this decision is set out in paragraphs BC20–BC22.

Do you agree with the IPSASB’s decision not to define “transfer revenue” or “transfer revenue with performance obligations”? If not, why not?

**Proposed AASB response:**

The AASB agrees with the reasons explained in paragraph BC21 that it is not necessary to define “transfer revenue” or “transfer revenue with performance obligations” to clarify the mirroring relationship between the exposure drafts. The terms alone would not explain the interaction between the exposure drafts. For example, the exposure drafts propose asymmetrical treatment in some circumstances, which would not be affected by including transfer revenue definitions that mirrored the transfer expense definitions.

The AASB notes that it is not essential to have symmetrical accounting between the transfer provider and the transfer recipient for revenue and expenses arising from a binding arrangement. Their accounting treatment should be based on the perspective of each entity.

A11 As set out in paragraph BC20 in ED 70, the IPSASB considered defining the terms as follows:

- Transfer Revenue – a transaction, other than taxes, in which an entity receives a good, service, or other asset from another entity without directly providing any good, service, or other asset in return; and
- Transfer Revenue with Performance Obligations – revenue earned from the provision of goods or services to third-party beneficiaries.

A12 The IPSASB decided not to define the terms ‘transfer revenue’ or ‘transfer revenue with performance obligations’ for the reasons stated in ED 70 paragraph BC21:

- (a) The key distinguishing feature for revenue to be within the scope of ED 70 is whether the revenue arises from a transaction with or without performance obligations. A number of IPSASB members were concerned that introducing new definitions relating to revenue may confuse constituents.
- (b) Transfer revenue with performance obligations would have been a subset of revenue within the scope of ED 70, while transfer revenue would have been a subset of revenue within the scope of ED 71. Separately defining these terms when their recognition and measurement would have been the same as other types of

revenue within their respective standards seems to be adding an unneeded level of complexity.

- A13 Staff agree with the reasons explained in ED 70 paragraph BC21 and therefore support the IPSASB decision not to introduce defined terms for ‘transfer revenue’ and ‘transfer revenue with performance obligations’.
- A14 Staff note that mirroring the relationship between exposure drafts does not necessarily mean that the accounting treatment by the parties to a binding arrangement for their revenue and expenses should be symmetrical. Their accounting treatment should be based on the circumstances of each entity and should be determined independently of how the counterparty treats the transaction.

**Specific Matter for Comment 3:**

Because the IPSASB decided to develop two revenue standards—this Exposure Draft on revenue with performance obligations and ED 71 on revenue without performance obligations—the IPSASB decided to provide guidance about accounting for transactions with components relating to both exposure drafts. The application guidance is set out in paragraphs AG69 and AG70.

Do you agree with the application guidance? If not, why not?

**Proposed AASB Response:**

The AASB agrees with the application guidance set out in paragraphs AG69 and AG70.

The AASB provided a pragmatic approach in the last sentence of AASB 15 paragraph F30 to assessing the materiality of such “donation” components in balancing the costs and benefits of separately recognising those components. Under the AASB’s approach, materiality is assessed in relation to each contract, and is not reassessed subsequently (e.g. at the end of the financial year) at an aggregate or portfolio level. Adopting such an approach would avoid undue costs that entities might incur if reassessment was required.

- A15 Paragraphs AG69 and AG70 state:

AG69 This [draft] Standard typically requires an entity to allocate the transaction price to each performance obligation in the binding arrangement so that the allocation depicts the amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to a purchaser or third-party beneficiary. This is based on the rebuttable presumption that the transaction price is **wholly related to the transfer of goods or services**. [emphasis added]

AG70 In the public sector, a purchaser may enter into a binding arrangement with an entity with a dual purpose of obtaining goods or services and to help the entity achieve its objectives. Such transactions may rebut the presumption that the transaction price is wholly related to the transfer of goods or services, as a portion of the consideration relates to helping the entity achieve its objectives. To demonstrate that this presumption is rebutted, the terms of the binding

arrangement must clearly specify that **only a portion of the consideration is to be returned** to the purchaser in the event the entity does not deliver the promised goods or services, as this indicates that the remaining consideration is intended to help the entity achieve its objectives. When the presumption is rebutted, the entity shall disaggregate the transaction price and account for the component that relates to the transfer of promised goods or services in accordance with this [draft] Standard. The remainder of the transaction price shall be accounted for in accordance with [draft] IPSAS [X] (ED 71), *Revenue without Performance Obligations*. [emphasis added]

A16 Staff agree with the application guidance set out in paragraphs AG69 and AG70. This is consistent with paragraphs F28-F30 of AASB 15, which state:

F28 A customer may enter into a contract with a not-for-profit entity with a dual purpose of obtaining goods or services and to help the not-for-profit entity achieve its objectives. An entity shall allocate the transaction price to each performance obligation so that the performance obligation allocation depicts the amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to the customer. This is based on the rebuttable presumption that the transaction price is treated as **wholly related to the transfer of promised goods or services** [emphasis added].

F29 The presumption is rebutted where the transaction price is **partially refundable** in the event the entity does not deliver the promised goods or services [emphasis added].

F30 Where the presumption is rebutted, the entity shall disaggregate the transaction price and account for the component that relates to the transfer of promised goods or services in accordance with this Standard. The remainder of the transaction price shall be accounted for in accordance with AASB 1058. Whether the element not related to the performance obligation is material, and therefore needs to be accounted for separately, **shall be assessed in relation to the individual contract, without reassessment at an aggregate or portfolio level**. [emphasis added]

A17 Staff consider that it would be beneficial for the IPSASB to incorporate the approach the Board adopted (to achieve a better balance of costs and benefits) to assessing the materiality of these “donation” components, as reflected in the last sentence of AASB 15 paragraph F30.

**Specific Matter for Comment 4:**

The IPSASB decided that this Exposure Draft should include the disclosure requirements that were in IFRS 15. However, the IPSASB acknowledged that those requirements are greater than existing revenue standards.

Do you agree that the disclosure requirements should be aligned with those in IFRS 15, and that no disclosure requirements should be removed? If not, why not?

**Proposed AASB Response:**

The AASB agrees that the disclosure requirements should be aligned with those in IFRS 15. The AASB concurs with the IPSASB's reasons explained in paragraph BC48 that since all of the concepts from IFRS 15 on recognition and measurement of revenue have been retained in the proposals in ED 70, there is no public sector-specific reason to remove any of the disclosure requirements.

A18 Staff agree with the IPSASB's reasons explained in paragraph BC48 that since all of the concepts from IFRS 15 on recognition and measurement of revenue were retained in ED 70, there is no public sector-specific reason to remove any of the disclosure requirements.

A19 The AASB decided initially to adopt all the disclosures in IFRS 15 when developing AASB 15. As noted in paragraph BC59 to AASB 2016-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities*, the Board confirmed not making any amendments to the disclosure requirements in AASB 15 specifically for not-for-profit entities when finalising its NFP entity implementation guidance.

**Specific Matter for Comment 5:**

In developing this Exposure Draft, the IPSASB noted that some public sector entities may be compelled to enter into binding arrangements to provide goods or services to parties who do not have the ability or intention to pay. As a result, the IPSASB decided to add a disclosure requirement about such transactions in paragraph 120. The rationale for this decision is set out in paragraphs BC38–BC47 and BC50.

Do you agree with the decision to add the disclosure requirement in paragraph 120 for disclosure of information on transactions which an entity is compelled to enter into by legislation or other governmental policy decisions? If not, why not?

**Proposed AASB Response:**

The AASB notes that the proposed disclosure requirements in paragraph 120 are more extensive than IFRS 15 requires of for-profit entities that have price concessions. However, the additional disclosures might be justified if users of financial statements are interested in this information for public sector entities where such transactions are prevalent and material, as stipulated in paragraph BC40 of ED 70.

A20 ED 70 (paragraph 120) proposes the following additional disclosure requirements about transactions with parties that do not have the ability or intention to pay:

120 In the public sector, an entity may be compelled by legislation or other governmental policy decisions to satisfy a performance obligation regardless of a purchaser's ability or intention to pay for the goods or services (see paragraph AG29). In addition to the information in paragraph 119, an entity shall disclose the following:

- (a) A description of the legislation or policy decision which compels the entity to satisfy the performance obligation;
- (b) The amount of revenue from these transactions that was recognized after application of paragraphs 13-15 of this [draft] Standard;
- (c) The amount from these transactions that was not recognized as revenue, as the collection of consideration was not probable; and
- (d) If the transaction price has been reduced after consideration of an implicit price concession from the application of AG31, an entity shall disclose the following:
  - (i) The amount from these transactions that was recognized as revenue after identification of the implicit price concession; and
  - (ii) The amount from these transactions that was not recognized as revenue, as it was considered an implicit price concession as described in AG31.

A21 Illustrative examples 6, 7 and 46 in ED 70 illustrate implicit price concessions and a simple disclosure under the requirements proposed in paragraphs 120(a) and (d).

A22 Staff note the proposed disclosure requirements in paragraph 120 of ED 70 are more extensive than IFRS 15 requires of for-profit entities that have price concessions. However, as noted in paragraph BC40 of ED 70, additional disclosures might be justified for public sector entities. Paragraph BC40 of ED 70 states that “The IPSASB acknowledged that arrangements an entity is compelled to enter where the collectability of the consideration is in question could be prevalent and material in certain jurisdictions. The IPSASB noted that there is information value in disclosing in the notes to the financial statements the amounts invoiced for such binding arrangements where collection of consideration is not probable or only considered probable after accepting a price concession as described in AG31.”

**Questions to the Board:**

Q2 Do Board members agree to provide responses on each SMC in ED 70?

Q3 Do Board members agree with staff’s views and the draft wording for responses to each of the above SMCs?

## Section B: IPSASB ED 71 Revenue without Performance Obligations

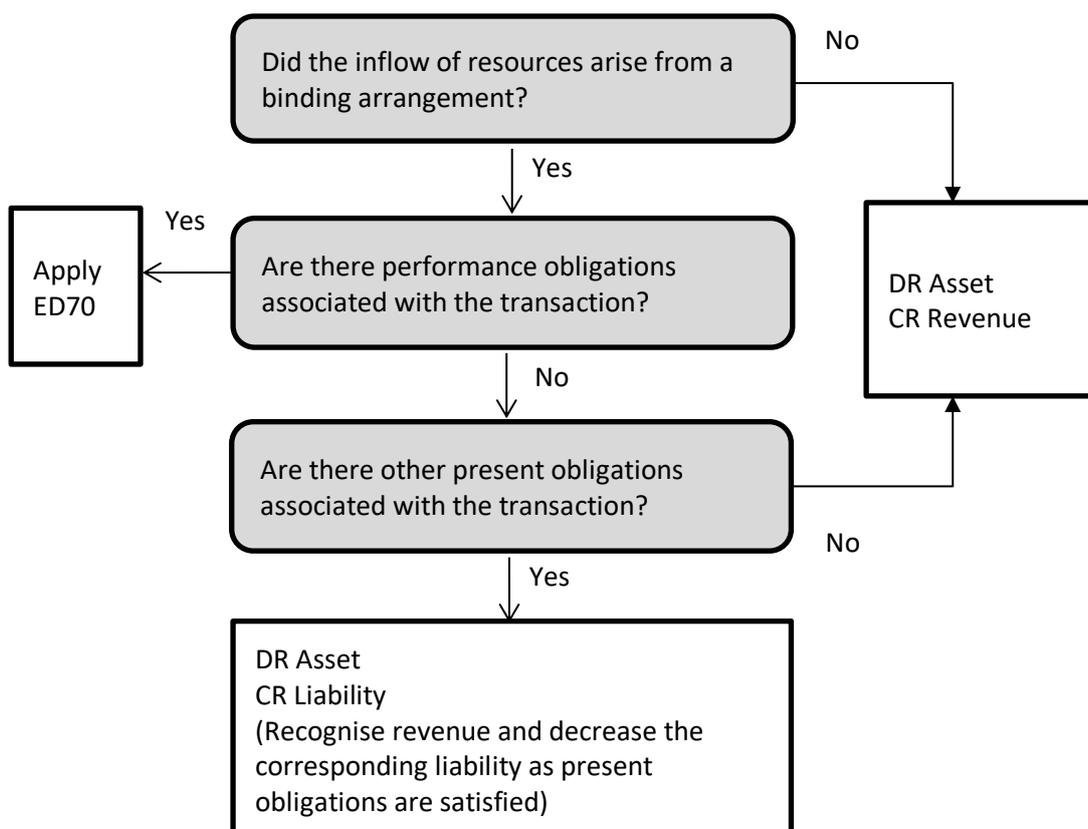
B1 This section provides a high-level overview of the proposals in ED 71 *Revenue without Performance Obligations* and a comparison with requirements in Australian Accounting Standards. It is set out as follows:

- [Part 1: Compare key principles in ED 71 and AASB 1058](#)
- [Part 2: Does a specified activity or an eligible expenditure give rise to a liability for the transfer recipient?](#)
- [Part 3: Capital transfers](#)
- [Part 4: Proposed responses to the Specific Matters for Comment.](#)

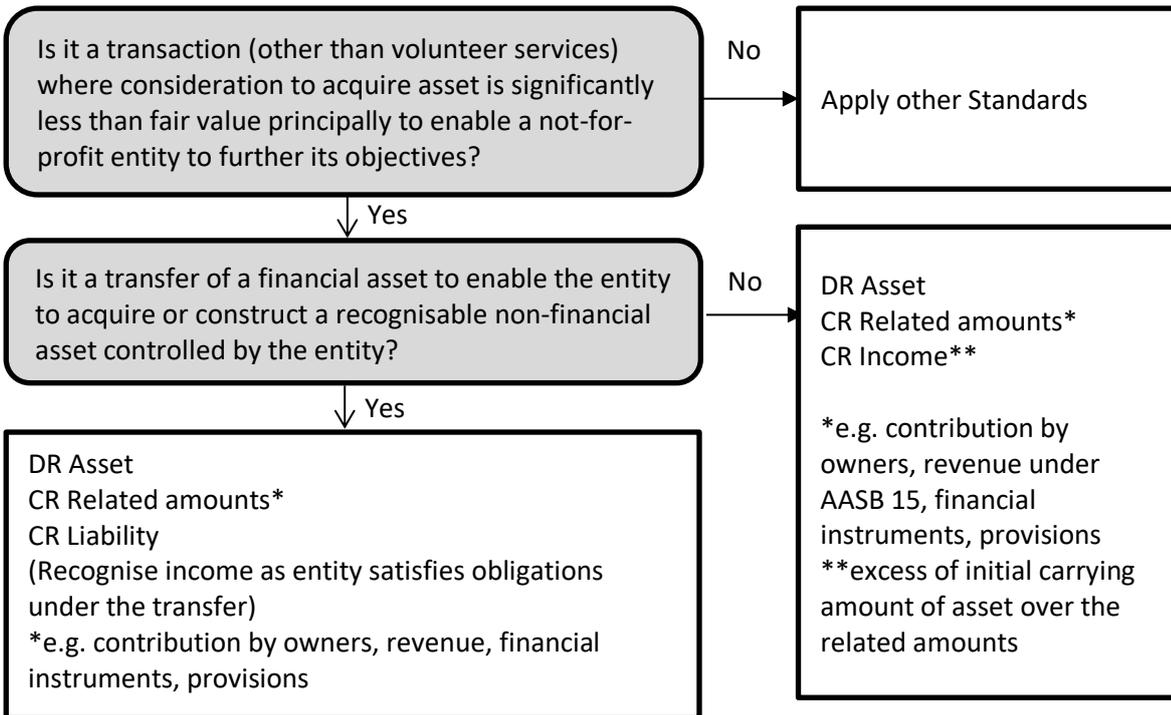
### Part 1: Compare key principles in ED 71 and AASB 1058

B2 Both ED 71 and AASB 1058 require that an asset is recognised when controlled by an entity. This paper does not discuss this aspect, as staff do not consider this to be a contentious issue.

B3 The following diagram provides a high-level overview of the relevant core principles in ED 71 regarding revenue recognition.



B4 The following diagram provides a high-level overview of the relevant core principles in AASB 1058 regarding revenue recognition, other than volunteer services.



B5 The following table provides a high-level comparison of the general recognition principles in the IPSASB’s proposals (as illustrated in the diagram in paragraph B3) and AASB Standards (as illustrated in the diagram in paragraph B4) that would apply to common types of resource inflows received by public-sector entities.

Table 1: Accounting principles in IPSASB ED 70, ED 71 and AASB Standards

Type of resource transfer	Accounting under IPSASB proposals	Accounting under AASB Standards	Staff comment
Inflows with performance obligations	ED 70 Recognise revenue over time or at a point in time depending on facts and circumstances	AASB 15 Recognise revenue over time or at a point in time depending on facts and circumstances	IPSASB proposals appear to be consistent with AASB principles
Inflows arising from a non-binding arrangement (i.e. no binding performance obligations or	ED 71 DR Asset CR Revenue	AASB 1058 <sup>2</sup> DR Asset CR Related amounts CR Income	Even though AASB 1058 requires an entity to consider whether there are related amounts (e.g.

2 Whether an inflow of resources arises from a binding arrangement is not a consideration to assess whether AASB 1058 would apply, paragraph BC34 of AASB 1058 states that the Board had intended from AASB 1058 to address the accounting for inflows of resources arising from donations, grants, taxes, and similar transactions and events. Staff think that these inflows are often arising from non-binding arrangements and AASB 1058 would apply in most cases.

Type of resource transfer	Accounting under IPSASB proposals	Accounting under AASB Standards	Staff comment
<p>present obligations for the transfer recipient)</p>			<p>provision) to be recognised before determining the amount of income to be recognised, staff consider that it is unlikely that there will be other related amounts to be recognised in an arrangement that is not binding.</p> <p>Therefore, staff consider the IPSASB proposals to be consistent with AASB principles for this type of transfer.</p>
<p>Inflows arising from a binding arrangement with no performance obligations but with other present obligations</p> <p>ED 71 states that a present obligation exists if the transfer recipient, in a binding arrangement, is obligated to perform a 'specified activity' or incur an 'eligible expenditure' (please refer to the <a href="#">Appendix</a> for the definition of these terms).</p>	<p>ED 71</p> <p>Initially: DR Asset CR Liability</p> <p>Subsequently: Recognise revenue and decrease corresponding liability as present obligations are satisfied</p>	<p>AASB 1058</p> <p>DR Asset CR Related amounts (including provisions, financial liabilities) CR Income (residual amount)</p>	<p>AASB 1058 requires an entity to consider whether there are 'related amounts' associated with a transaction.</p> <p>AASB 1058 indicates that an obligation to perform a specified activity or incur an eligible expenditure does not give rise to a liability that would be recognised as a related amount, based on the exception for capital grants.</p> <p>Part 2 below explores this issue.</p>
<p>Binding arrangement – Capital transfers (i.e. transfers to enable an entity to acquire or construct</p>	<p>ED 71</p> <p>Initially, as present obligation exists: DR Asset</p>	<p>AASB 1058</p> <p>Initially: DR Asset CR Related amounts</p>	<p>Other than the recognition of intangible assets, it appears that ED 71 proposes a similar</p>

Type of resource transfer	Accounting under IPSASB proposals	Accounting under AASB Standards	Staff comment
a non-financial asset to be controlled by the entity)	<p>CR Liability</p> <p>Subsequently: Recognise revenue as present obligations are satisfied.</p> <p>Includes grants provided to develop intangible assets, because ED 71 does not refer to <i>recognisable</i> non-financial assets.</p>	<p>CR Liability (residual amount)</p> <p>Subsequently: Recognise revenue as the obligation to acquire or construct the asset is satisfied.</p> <p>Explicitly excludes grants received to conduct research activities from the capital transfer accounting because AASB 138 <i>Intangible Assets</i> does not permit the recognition of an entity's research activities as an asset.</p>	<p>accounting treatment to AASB 1058 (which limits this to <i>recognisable</i> non-financial assets).</p> <p>However, staff note that the Board's rationale in deciding the accounting treatment of such transfers is different to IPSASB's rationale. This is explored in Part 3 below.</p>

**Part 2: Does a specified activity or an eligible expenditure give rise to a liability for the transfer recipient?**

B6 As noted in Table 1 in paragraph B5, the key apparent difference between the ED 71 proposals and AASB 1058 is whether a binding arrangement would create a liability for the transfer recipient when it is required to perform a specified activity or incur eligible expenditure, that are not performance obligations.

***Specified activity and eligible expenditure are not considered performance obligations***

B7 ED 70 defines a performance obligation as:

“... a promise in a binding arrangement with a purchaser to **transfer to the purchaser or third-party beneficiary** either:

(c) A good or service (or a bundle of goods or services) that is distinct; or

(d) 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.” [emphasis added]

B8 ED 71 paragraphs 17-21 propose that the transfer recipient has a present obligation when it is obligated under a binding arrangement to perform a specified activity or incur an

eligible expenditure. ED 71 paragraph BC14 states that a specified activity or the requirement to incur eligible expenditure differs from a performance obligation because there is no requirement for the transfer recipient to transfer a good or service to either the transfer provider or a third-party beneficiary.

- B9 A specified activity is “a particular action, stated in a binding arrangement, that the transfer provider can compel the transfer recipient to perform, such as construct a hospital or conduct a form of research” (ED 71 paragraph 18).
- B10 An eligible expenditure is “an outflow of resources incurred in accordance with the requirements set out in a binding arrangement” (ED 71 paragraph 10). ED 71 paragraph 20 states that “A binding arrangement may require a transfer to be used by a transfer recipient for a particular purpose and incur eligible expenditure for that purpose, but does not have an identifiable specified activity.”
- B11 ED 71 proposes that where a transfer recipient is obligated to perform a specified activity or incur an eligible expenditure (i.e. a present obligation exists), the transfer recipient would initially recognise a liability and subsequently recognise revenue and decrease the corresponding liability as the present obligations are satisfied. Paragraph BC12 of ED 71 states the IPSASB’s rationale for this conclusion, that the present obligation gives rise to a liability because:
- the past event occurs when the transfer provider and transfer recipient enter into a binding arrangement, creating enforceable rights and obligations; and
  - such an arrangement leads to an outflow of resources because the transfer recipient cannot avoid using those resources either to fulfil the requirements in the binding arrangement or, in the event of a breach of a binding arrangement, repaying the resources to the transfer provider or incurring some other form of penalty.

***When does an obligation give rise to a present obligation (i.e. liability)?***

- B12 To analyse the IPSASB’s rationale mentioned in paragraph B11, staff have referred to the explanations of when an obligation would give rise to a present obligation or a liability in:
- The IPSASB’s *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities*;
  - The AASB’s *Framework for the Preparation and Presentation of Financial Statements* (CF 2004), which is applicable to non-for-profit entities;
  - The AASB’s *Conceptual Framework for Financial Reporting* (CF 2019), which is applicable to for-profit entities. The Board is currently undertaking a project to modify this Conceptual Framework where necessary for not-for-profit entity considerations; and
  - IPSAS 19 Provisions, Contingent Liabilities and Contingent Assets and AASB 137 Provisions, Contingent Liabilities and Contingent Assets, which are both based on IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

B13 The following table includes extracts of texts from the five documents mentioned in paragraph B12. Common aspects across those documents of when an obligation would give rise to a present obligation or a liability are marked in highlighted text.

Table 2: Comparing the explanations of the term ‘present obligation’ in the IPSASB and AASB pronouncements

IPSASB Conceptual Framework	AASB Conceptual Framework (2004)	AASB Conceptual Framework (2019)	IPSAS 19 and AASB 137	Staff comment – aspects in common
<p>“A liability is a present obligation of the entity for an <b>outflow of resources</b> that results from a <b>past event</b>.” [Paragraph 5.14]</p> <p>“Public sector entities can have a number of obligations. A present obligation is a legally binding obligation (legal obligation) or non-legally binding obligation, which an entity has little or no realistic alternative to avoid. ...” [Paragraph 5.15]</p> <p>“A liability must involve an <b>outflow of resources from the entity</b> for it to be settled. An obligation that can be settled without an outflow of resources from the entity is</p>	<p>“A distinction needs to be drawn between a present obligation and a future commitment ... the irrevocable nature of the agreement means that the economic consequences of failing to honour the obligation, for example, because of the existence of a substantial penalty, leave the entity with little, if any, discretion to avoid the <b>outflow of resources to another party</b>.” [Paragraph 61]</p> <p>“The settlement of a present obligation usually involves the entity <b>giving up resources</b> embodying economic benefits in order to <b>satisfy the claim</b></p>	<p>“A liability is a present obligation of the entity to <b>transfer an economic resource</b> as a result of <b>past events</b>.” [Paragraph 4.26]</p> <p>“For a liability to exist, three criteria must all be satisfied:</p> <p>(a) the entity has an obligation;</p> <p>(b) the obligation is to <b>transfer an economic resource</b>; and</p> <p>(c) the obligation is a present obligation that exists as a result of <b>past events</b>.” [Paragraph 4.27]</p> <p>“An obligation is a duty or responsibility that an</p>	<p>“An obligating event is an event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.” [IPSAS 19 paragraph 18 and AASB 137 paragraph 10]</p> <p>“It is only those obligations arising from <b>past events</b> existing independently of an entity’s future actions (ie the future conduct of its business) that are recognised as provisions ...” [IPSAS 19 paragraph 27 and AASB 137 paragraph 19]</p> <p>“An <b>obligation always involves another party to whom the obligation is</b></p>	<p>An obligation is a present obligation (i.e. a liability) if:</p> <ul style="list-style-type: none"> <li>• <b>it is a result of a past event;</b></li> <li>• <b>it requires an outflow/transfer of resources from the entity;</b></li> <li>• <b>the obligation is to an external party/claim of the other party and the other party has a right to receive that resource; and</b></li> <li>• <b>the obligation presently exists and is independent of the entity’s future actions – i.e. the entity has little or no realistic alternative to avoid the outflow/transfer</b></li> </ul>

IPSASB Conceptual Framework	AASB Conceptual Framework (2004)	AASB Conceptual Framework (2019)	IPSAS 19 and AASB 137	Staff comment – aspects in common
<p>not a liability.” [Paragraph 5.16]</p> <p>“... An obligation must be to an external party in order to give rise to a liability. An entity cannot be obligated to itself ... Identification of an external party is an indication of the existence of an obligation giving rise to a liability. However, it is not essential to know the identity of the external party before the time of settlement in order for a present obligation and a liability to exist.” [Paragraph 5.18]</p>	<p>of the other party” [Paragraph 62]</p> <p>“Liabilities result from past transactions or other past events ...” [Paragraph 63]</p>	<p>entity has no practical ability to avoid. An obligation is always owed to another party (or parties). The other party (or parties) could be a person or another entity ... or society at large. It is not necessary to know the identity of the party (or parties) to whom the obligation is owed.” [Paragraph 4.29]</p> <p>“If one party has an obligation to transfer an economic resource, it follows that another party (or parties) has a right to receive that economic resource ...” [Paragraph 4.30]</p>	<p>owed ...” [IPSAS 19 paragraph 28 and AASB 137 paragraph 20]</p>	<p>of resources independently of its future actions.</p>

B14 In summary, based on Table 2 in paragraph B13, staff are of the view that for a liability to exist for the transfer recipient, there must be:

- (a) an obligation owing to another party as a result of a past event;
- (b) an obligation that presently exists and is independent of the transfer recipient’s future actions – i.e. the transfer recipient has little or no realistic alternative to avoid the outflow/transfer of resources independently of its future actions; and
- (c) the obligation creates a present entitlement for another party to receive the outflow/resource.

B15 Therefore, staff disagree with the IPSASB proposal that a present obligation exists (i.e. a liability exists) for the transfer recipient where the transfer recipient, under a binding arrangement, is required to use the transferred resources to carry out specified activities or to incur eligible expenditure. This is because staff do not consider that, upon the recognition of the transferred asset, the transfer recipient has a **present obligation to transfer the resources to other entities independently of its future actions**.

B16 ED 71 included illustrative examples of where the IPSASB is proposing that there is a present obligation for the transfer recipient, which would therefore recognise a liability and defer revenue recognition when the transfer resource is controlled. Table 3 summarises one of the examples and the staff analysis whether the example would give rise to a present obligation and a liability for the transfer recipient, based on staff’s view noted in paragraph B14.

Table 3: Analysis of Illustrative Example 20

ED 71 illustrative example	Staff analysis
<p>Example 20 Revenue of Aid Agency (eligible expenditure)</p> <ul style="list-style-type: none"> <li>• Green-Aid Agency (transfer recipient) relies on funding from a group of governments (transfer providers).</li> <li>• Green-Aid Agency can only use the funds to meet the agreed expenses of the budget year for which the funds are provided.</li> <li>• Any funding not used in the budget year is refundable to the governments in the same proportion as the transfers were received.</li> <li>• For the budget year 20X8, the profile of amounts and timing of payments was as follows:               <ul style="list-style-type: none"> <li>○ CU15 million received as at 31 December 20X7</li> </ul> </li> </ul>	<p><b>At the point of controlling the transfer resource, does the transfer recipient have little or no realistic alternative to avoid the outflow/transfer of resources to a <u>transfer provider</u> independent of its future actions?</b></p> <p>No, Green-Aid Agency can avoid outflows to the transfer providers by taking a future action – use the funds based on the agreed terms and conditions.</p> <p><b>Do the <u>transfer providers</u> have a present entitlement to receive or reclaim transferred funds?</b></p> <p>No, the transfer providers would only have an entitlement to receive or reclaim any funds either:</p>

ED 71 illustrative example		Staff analysis
	<ul style="list-style-type: none"> <li>○ CU38 million received during 20X8.</li> </ul> <p>In 20X7, recognise amount of transfers received (controlled): DR Cash CU15 million CR Liability CU15 million</p> <p>In 20X8, recognise amount of transfer received (controlled): DR Cash CU38 million CR Liability CU38 million</p> <p>In 20X8, when the present obligation is satisfied: DR Liability CU53 million CR Revenue CU53 million</p>	<ul style="list-style-type: none"> <li>● when Green-Aid Agency spends the government funding (or part of) in a way not specified in the agreement; or</li> <li>● when funds remain unspent at the end of the budget year.</li> </ul> <p><b>At the point of controlling the transfer resource, does the transfer recipient have little or no realistic alternative to avoid the outflow/transfer of resources to another party (other than the transfer providers) independent of its future actions?</b></p> <p>No, Green-Aid Agency only has an obligation to transfer a resource to another party if it enters into an agreement with a third party for goods or services.</p>

B17 AASB staff are of the view that, in the above example, the transfer recipient recognises assets for its own use and does not have a present obligation to transfer cash or other resources to other entities independently of its future actions.

B18 AASB staff acknowledge that the cash or other resources would eventually need to be paid to another party or parties to pay for the goods or services that the other parties would provide, to comply with the conditions of the arrangement (or else returned to the transfer providers). However, this “obligation to pay cash or resources” arises only when a separate arrangement is entered with another party to provide goods or services, and not at the point when the transfer recipient recognises an asset on obtaining control of the transfer resource. Recognition of the transfer resource as revenue should not depend on entering a subsequent separate arrangement with other parties.

B19 Therefore, staff disagree with the proposal in ED 71 that the transfer recipient would have a liability to transfer resources to another party where it is required to perform a specified activity or incur an eligible expenditure (as defined in ED 71) that is not a performance obligation.

**Question to the Board:**

Q4 Do Board members agree with the staff’s view in paragraph B19?

### Part 3: Capital transfers

B20 As noted in Table 1 in paragraph B5, staff observe that ED 71 proposes a similar accounting treatment to AASB 1058 in respect of “transfers to enable an entity to acquire or construct a non-financial asset to be controlled by the entity” (called ‘capital transfers’ in ED 71), with the exception that ED 71 does not limit the approach to transfers in respect of *recognisable* non-financial assets.

B21 However, staff note that the IPSASB’s rationale in deciding the accounting treatment of capital transfers is different from the Board’s rationale. This is addressed in the following paragraphs.

#### ***Does a capital transfer give rise to a present obligation (i.e. liability) that is not a performance obligation?***

B22 IPSAS 71 defines a capital transfer as “... an inflow, that arises from a binding arrangement, of cash or another asset with a specification that the transfer recipient acquires or constructs a non-financial asset that will be controlled by the transfer recipient” (ED 71 paragraph 10).

B23 ED 71 requires a transfer recipient to initially recognise an asset and a liability, and subsequently recognise revenue as it satisfies present obligations. This accounting treatment – to defer revenue recognition – is aligned with AASB 1058 requirements (except for research grants as explain in paragraphs B29–B32 below).

B24 ED 71 (paragraph AG24) notes that a capital transfer does not give rise to a performance obligation as there is no requirement to transfer the non-financial asset to the transfer provider or another party, and therefore would be outside of the scope of ED 70. This aligns with the AASB’s decision that capital transfers are outside the scope of AASB 15 as there is no performance obligation to transfer a good or a service (including the non-financial asset) to the transferor or another party (AASB 15 paragraph 22).

B25 Both ED 71 and AASB 1058 mention that, despite not having a performance obligation, there is an “obligation” to acquire or to construct the non-financial asset. ED 71 considers this “obligation” to be a present obligation, which gives rise to a liability for the transfer recipient. In contrast, AASB 1058 does not treat the requirement to acquire or construct the non-financial asset, which would be recognised by the entity, as an obligation owing to another party. Therefore, the obligation is not a “present obligation”. The Board decided that income recognition should be deferred so that the timing of income recognition is aligned with how the transfer recipient “receives” the *recognisable* non-financial asset. The Board’s rationale is summarised in paragraphs B26 and B27 below.

B26 AASB 1058 paragraph 15 states that a capital transfer is one that:

- (a) requires the entity to use the financial asset transferred to acquire or construct a **recognisable** non-financial asset to identified specifications;
- (b) **does not require the entity to transfer the non-financial asset to the transferor or other parties;** and

(c) occurs under an enforceable agreement. [emphasis added]

B27 Despite concluding that ‘capital transfers’ are outside the scope of AASB 15 as there is no performance obligation to transfer a good or a service to another party, the Board decided to apply the principles in AASB 15 by analogy. The Board made this decision because it considered:

- the transfer provider had intended to transfer a recognisable non-financial asset to the transfer recipient for use by the entity itself, and therefore income should not be recognised until the transfer recipient has satisfied its obligation to construct or acquire the asset. The Board decided that the timing of income recognition should reflect the transfer recipient receiving the asset directly, rather than the cash to construct or acquire the asset (AASB 1058 paragraph BC98);
- the key criterion is that the recognisable non-financial asset will be under the control of the entity (i.e. for its own use) – it will not be transferred to the transferor or other parties (AASB 1058 paragraph B15); and
- the recognisable non-financial asset could increase the entity’s ability or capacity to provide goods or services to other parties pursuant to other transactions, which are separate to the transfer that enabled the entity to acquire or construct the non-financial asset for its own use (AASB 1058 paragraph B15).

The full text of AASB 1058 paragraphs B15 and BC98 is included in the [Appendix](#) for the Board’s reference.

#### *Staff’s view*

B28 As mentioned in Part 2 of this Section, staff are of the view that for an obligation to meet the definition of a liability (i.e. for it to be a present obligation), the obligation must be a transfer of resources **owing to another party** and the other party must have the right to receive the resources. In the context of capital grants, the “obligation” refers to a commitment to acquire or construct a recognisable non-financial asset for the entity’s own use, and not an obligation to transfer a resource to another party or to the transfer provider.

#### ***Capital transfers to conduct research activities***

B29 Capital transfers in the context of ED 71 include grants provided to conduct research activities because it does not limit such transfers to those for the acquisition or construction of recognisable non-financial assets. In contrast, AASB 1058 explicitly excludes transfers received to conduct research activities from the capital transfer accounting stated in paragraphs 15–17 of AASB 1058 (i.e. to defer revenue recognition so that the timing of income recognition is aligned with how the transfer recipient receives the recognisable non-financial asset). This is because AASB 138 does not permit the recognition of an entity’s research activities as an asset.

B30 Paragraph AG27 of ED 71 provides the IPSASB’s proposed guidance on accounting for capital transfers to conduct research activities. It states:

AG27 This [draft] Standard defines a specified activity as an action specified in a binding arrangement that must be completed by a transfer recipient. A specified activity differs from a performance obligation because there is no requirement to transfer any good or service to the transfer provider or a third-party beneficiary. For example, a transfer provider provides funding to a government science agency (transfer recipient) to **conduct research** and development into a plant-based meat substitute. Any intellectual property developed by the government science agency remains the property of that agency. The funding is provided on the basis of a detailed project plan (with the individual stages of research and development identified) provided by the government science agency and the transfer provider requires the government science agency to report back at each stage. **Each of these stages constitutes an specified activity and revenue would be recognized when (or as) they are completed and for the amount incurred in completing that specified action.** [emphasis added].

B31 When developing AASB 1058, the Board had considered extending the capital grant accounting treatment to grants received where the non-financial asset to be acquired or constructed would meet the definition of an asset but would not be permitted to be recognised by an Accounting Standard, such as specified research activities. Paragraph BC104 of AASB 1058 documents that the Board was concerned that extending the accounting treatment in this manner would:

- (a) create ambiguity in the distinction between a service and a good, and lack of clarity as to whether an implicit good component in a contract needs to be separately identified from the service. The Board observed that many service contracts in both the not-for-profit and for-profit sector arguably give rise to (unrecognised) knowledge or expertise to the service renderer;
- (b) result in a lack of comparability, as some constituents may contend that all the value in such a contract is attributable to the unrecognised good acquired; while others contend that the value remains with the service rendered (ie the good is an incidental product that the customer does not value in entering the contract). Yet others may contend that some apportionment is appropriate;
- (c) be seen as being inconsistent with the Board's decision not to extend the accounting specified by AASB 15 to all transactions of not-for-profit entities, regardless of whether a contract with a customer exists. The Board could not see a clear distinction why the accounting should differ between transactions that through the conduct of an activity result in incidentally gaining control of intellectual property assets, and an arrangement to deliver services for which income may be recognised immediately in accordance with this Standard; and
- (d) create confusion as to whether this Standard would allow certain intangible assets to be recognised, where their recognition is otherwise prohibited.

B32 Consequently, the Board decided that the accounting set out in paragraphs 15–17 of AASB 1058 should be limited to transactions that would result in a recognisable non-financial asset controlled by the entity, and therefore should not be extended to include capital transfers to conduct research activities. Therefore, such capital transfers would

have a different accounting outcome under ED 71, which proposes that revenue should be deferred.

B33 Staff recommend the Board provide specific comments to the IPSASB outlining the Board's rationale in concluding its accounting treatment of capital transfers. The draft response is included in the draft response to SMC1 in paragraph B40 below.

**Question to the Board:**

Q5 Do Board members agree with the staff recommendation in paragraph B33 to provide specific comments to IPSASB about the Board's rationale in concluding its accounting treatment of capital transfers?

**Part 4: Proposed responses to the Specific Matters for Comment**

B34 ED 71 contains seven Specific Matters for Comment (SMC), which cover the following topics:

- SMC1: Determining when a transfer recipient has a present obligation
- SMC2: Flowchart for revenue transactions without performance obligations
- SMC3: Determining when a present obligation is satisfied
- SMC4: Allocating the transaction price to present obligations
- SMC5: Subsequent measurement of receivables
- SMC6: Disclosure requirements
- SMC7: Structure of the proposals.

B35 Staff recommend the Board provide a detailed response to SMC1 based on the discussions in Parts 2 and 3 of this Section of the paper. The proposed AASB response to SMC1 is included in paragraph B40 for the Board's consideration.

B36 SMCs 2–4 are about the application of core principles in ED 71. Since the proposed AASB response to SMC1 does not support the core principle in ED 71 regarding the identification of present obligations, staff consider that it is not necessary to provide specific responses to SMCs 2–4.

B37 Staff recommend that the Board not comment on SMC5 regarding the subsequent measurement of receivables. When finalising its Income of Not-for-Profit Entities project, the AASB decided that the *initial* recognition and measurement requirements of AASB 9 *Financial Instruments* should be applied to statutory non-contractual receivables (AASB 9 paragraph Aus2.1.1). However, the Board decided not to require entities to apply the *subsequent* measurement requirements of AASB 9 to statutory receivables. At the time, the Board noted that the IPSASB planned to address this topic. The Board decided to monitor the IPSASB's work and consider the subsequent measurement of statutory receivables in a future project (paragraph BC12 of the Basis for Conclusions to AASB 2016-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance*

for *Not-for-Profit Entities*, which has been attached to AASB 15). The IPSASB is now addressing statutory receivables under ED 70 and 71. The Board would need to follow its due process to consider the impact of the subsequent measurement proposals for statutory receivables outlined in the EDs, in proceeding with such a project.

- B38 SMC6 is about disclosure requirements. Staff recommend that the Board not comment on this SMC, given the proposed Board response to SMC1 does not support a core principle in ED 71 and the lack of specific justification in the ED for public sector-specific disclosures.
- B39 Since the proposed Board response to SMC1 does not support a core principle in ED 71, staff consider that it is not necessary to respond to SMC7 regarding the structure and broad principles of the ED.

**Question to the Board:**

Q6 Do Board members agree with the staff's view to respond only to SMC 1?

***SMC1: Determining when a transfer recipient has a present obligation***

- B40 The proposed Board response to SMC1 set out below is based on the discussion in the previous paragraphs of Section B of this paper.

**Specific Matter for Comment 1:**

The ED proposes that a present obligation is a binding obligation (legally or by equivalent means), which an entity has little or no realistic alternative to avoid and which results in an outflow of resources. The IPSASB decided that to help ascertain whether a transfer recipient has a present obligation, consideration is given to whether the transfer recipient has an obligation to perform a specified activity or incur eligible expenditure.

Do you agree with the IPSASB's proposals that for the purposes of this [draft] Standard, *Revenue without Performance Obligations*, a specified activity and eligible expenditure give rise to present obligations? Are there other examples of present obligations that would be useful to include in the [draft] Standard?

**Proposed AASB Response:**

***Transfers to perform a specified activity or to incur eligible expenditure***

The AASB does not agree with the proposal that a transfer recipient would have a liability to transfer resources to another party where it is required to perform a specified activity or incur an eligible expenditure that is not a performance obligation. The AASB did not take the IPSASB's proposed approach in its Standard AASB 1058 *Income of Not-for-Profit Entities* (December 2016).

The AASB notes the guidance in paragraphs 5.14–5.18 of the IPSASB’s Conceptual Framework and paragraphs 18 and 27 of IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* and suggests that for a liability to exist for the transfer recipient, there must be:

- (a) an obligation owing to another party as a result of a past event;
- (b) an obligation that presently exists and is independent of the transfer recipient’s future actions – i.e. the transfer recipient has little or no realistic alternative to avoid the outflow/transfer of resources independently of its future actions; and
- (c) the obligation creates a present entitlement for another party to receive the outflow/resources.

The AASB acknowledges that the cash or other resources would eventually need to be paid to another party or parties to pay for the goods or services that the other parties would provide, to comply with the conditions of the arrangement (or else returned to the transfer providers). However, this “obligation to pay cash or resources” arises only when a separate arrangement is entered with another party to provide goods or services, and not at the point when the transfer recipient recognises an asset on obtaining control of the transfer resource. Recognition of the transfer resource as revenue should not depend on entering a subsequent separate arrangement with other parties.

### ***Capital transfers***

Although ED 71 proposes the same accounting outcome as AASB 1058 regarding capital transfers (except for capital transfers to conduct research activities), the IPSASB’s rationale is different to the AASB’s rationale in AASB 1058.

The AASB agrees with the IPSASB that a capital transfer does not give rise to a performance obligation as there is no requirement for the transfer recipient to transfer a good or a service to another party (as stated in paragraph 27 of AASB 15). Therefore, capital transfers would not be in the scope of ED 70.

ED 71 considers the “obligation” to acquire or construct the non-financial asset to be a present obligation, which gives rise to a liability for the transfer recipient. In contrast, AASB 1058 does not treat the requirement to acquire or construct the non-financial asset, which would be recognised by the entity, as an obligation owing to another party. Therefore, the obligation is not a “present obligation”. The AASB took the view that the transfer provider had intended to transfer a recognisable non-financial asset to the transfer recipient for use by the entity itself. Accordingly, the AASB decided that revenue recognition should be deferred so that the timing of income recognition would be aligned with how the transfer recipient “receives” the recognisable non-financial asset, rather than the cash to construct or acquire the asset.

Additionally, AASB 1058 explicitly excludes transfers received to conduct research activities from the capital transfer accounting stated in paragraphs 15–17 of AASB 1058 (i.e. to defer revenue recognition so that the timing of income recognition is aligned with how the transfer recipient receives the recognisable non-financial asset). This is because AASB 138 *Intangible Assets* does not permit the recognition of an entity’s research activities as an asset.

When developing AASB 1058, the AASB had considered extending the capital transfer accounting treatment to transfers received where the non-financial asset to be acquired or constructed would meet the definition of an asset but would not be permitted to be recognised by an Australian Accounting Standard, such as specified research activities. Paragraph BC104 of AASB 1058 documents that the AASB was concerned that extending the paragraphs in this manner would:

- (a) create ambiguity in the distinction between a service and a good, and lack of clarity as to whether an implicit good component in a contract needs to be separately identified from the service. The Board observed that many service contracts in both the not-for-profit and for-profit sector arguably give rise to (unrecognised) knowledge or expertise to the service renderer;
- (b) result in a lack of comparability, as some constituents may contend that all the value in such a contract is attributable to the unrecognised good acquired; while others contend that the value remains with the service rendered (ie the good is an incidental product that the customer does not value in entering the contract). Yet others may contend that some apportionment is appropriate;
- (c) be seen as being inconsistent with the Board's decision not to extend the accounting specified by AASB 15 to all transactions of not-for-profit entities, regardless of whether a contract with a customer exists. The Board could not see a clear distinction why the accounting should differ between transactions that through the conduct of an activity result in incidentally gaining control of intellectual property assets, and an arrangement to deliver services for which income may be recognised immediately in accordance with this Standard; and
- (d) create confusion as to whether this Standard would allow certain intangible assets to be recognised, where their recognition is otherwise prohibited.

Consequently, the accounting set out in paragraphs 15–17 of AASB 1058 is limited to transactions that will result in a recognisable non-financial asset controlled by the entity. The AASB recommends that the IPSASB also consider introducing this limitation to the capital transfer accounting proposed in ED 71.

***Indication of past experience or knowledge in the context of the enforceability of binding arrangements***

As noted in the AASB's response to SMC1 of ED 70, the AASB disagrees with ED 71 paragraph 24 that if past experience or knowledge indicates that the transfer provider never enforces an arrangement if a breach occurs, then the transfer recipient may conclude that the arrangement is not enforceable in substance. The enforceability of a binding arrangement depends solely on the transfer provider's capacity to enforce its rights under the arrangement.

**Question to the Board:**

- Q7 Do Board members have any comments on the draft wording of the proposed responses to SMC 1?

## Section C: IPSASB ED 72 *Transfer Expenses*

C1 This section provides a high-level overview of the proposals in ED 72 *Transfer Expenses* and a comparison with requirements in Australian Accounting Standards. It is set out as follows:

- [Part 1: Summary of key proposals in ED 72](#)
- [Part 2: Compare key principles in ED 72 and AASB 137](#)
- [Part 3: Contrast the definitions of an asset in the IPSASB and AASB Conceptual Frameworks](#)
- [Part 4: Staff's analysis and proposed responses to the Specific Matters for Comment](#)

### Part 1: Summary of key proposals in ED 72

C2 ED 72 sets out proposals for a new Standard on transfer expenses. 'Transfer expense' is defined in ED 72 (paragraph 8) as "an expense arising from a transaction, other than taxes<sup>3</sup>, in which an entity provides a good, service, or other asset<sup>4</sup> to another entity (which may be an individual) without directly receiving any good, service, or other asset in return".

C3 ED 72 deals with transfers from a transfer provider to a transfer recipient for (i) use in delivering goods and services to a third-party beneficiary; or (ii) use by the transfer recipient for other purposes. Expenses arising from fulfilling performance obligations to deliver goods and services to a purchaser are not transfer expenses. The definition of a transfer expense also excludes expenses where an entity directly receives any good, service or other asset in return.

C4 The requirements in ED 72 vary, depending upon whether there is a binding arrangement and, if so, whether the transfer recipient has performance obligations (as defined in ED 70). If there is no binding arrangement, the transfer provider recognises the transfer expense when the resources are transferred to the transfer recipient.

C5 If a transfer gives rise to performance obligations for the transfer recipient and meets certain criteria (see paragraph C6), the transfer provider recognises a transfer expense when (or as) the transfer recipient satisfies the performance obligations in accordance with the Public Sector Performance Obligation Approach (PSPOA). The PSPOA adopts a five-step approach<sup>5</sup> (see paragraphs 10-89 in ED 72 for detailed requirements), based on the five-

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3 Taxes include other compulsory contributions and levies, as defined in ED 71.

4 The definition of a transfer expense includes references to "other asset" (for example, a non-current asset) for completeness. Elsewhere in the ED, references to goods and services or to goods or services are to be read as incorporating references to assets.

5 As noted in paragraph 12 of ED 72, the five steps are (1) identifying the binding arrangement; (2) identifying the performance obligations; (3) determining the transaction consideration; (4) allocating the transaction consideration to the performance obligations; and (5) recognise transfer expenses when (or as) the performance obligations are satisfied.

step, IFRS 15-aligned approach proposed in ED 70 for recognising revenue in relation to satisfying performance obligations.

C6 In order to apply the PSPOA, all of the following criteria must be met (ED 72, paragraph 13):

- There is an approved binding arrangement and all parties are committed to perform their respective obligations.
- The transfer provider can identify each party's rights regarding the goods and services to be transferred.
- The transfer provider can identify the payment terms for the goods and services to be transferred.
- The transfer provider can identify the other party's performance obligations and monitors satisfaction of them throughout the arrangement.

If any of these conditions are not met, the transfer provider accounts for the transaction as one without performance obligations for the transfer recipient.

C7 The application of the PSPOA in ED 72 would lead to the transfer provider recognising assets and liabilities before recognising transfer expenses. The assets and liabilities recognised under ED 72 would be:

- (a) transfer provider binding arrangement liabilities;
- (b) payables; and
- (c) transfer provider binding arrangement assets.

C8 If a transaction gives rise to performance obligations and meets the criteria listed in paragraph C6, the transfer provider would be required to recognise an asset (a transfer provider binding arrangement asset) for the right to have a transfer recipient transfer goods and services to third-party beneficiaries.

C9 The transfer provider subsequently recognises and measures the expense as the transfer recipient provides goods and services to third-party beneficiaries, under the PSPOA. The proposals for transactions with performance obligations in ED 72 mirror the proposals for such transactions in ED 70. Under ED 72, the transfer provider's binding arrangement asset will be derecognised (and transfer expense recognised) when (or as) the transfer recipient fulfills its performance obligations.<sup>6</sup>

C10 If a transfer does not give rise to performance obligations, the transfer provider recognises an expense at the earlier of the following two dates (ED 72, paragraph 91):

- (a) when it has a present obligation to transfer resources to the transfer recipient; and

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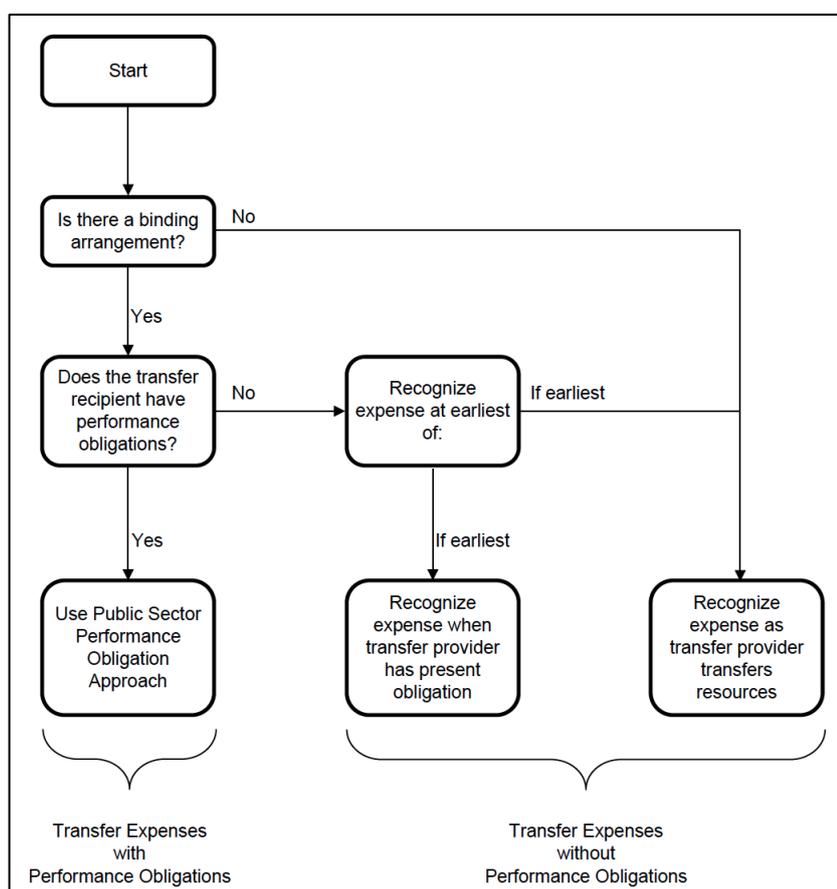
<sup>6</sup> Under ED 70, a transfer recipient recognises revenue when (or as) the transfer recipient fulfills its performance obligations.

(b) when it transfers the resources.

The transfer provider would recognise a transfer expense for such transfers before the transfer recipient recognises revenue if the transfer recipient recognises a liability for present obligations under the proposals in ED 71.

C11 However, if a transfer provider transfers resources to the transfer recipient prior to the point at which the transfer provider has a present obligation to transfer the resources, and is entitled to a refund on demand, the transfer provider still retains control of the resources. Consequently, the transfer provider does not derecognise the resources, nor recognise an expense, until the transfer provider has a present obligation to transfer (paragraph AG95 of ED 72). However, transfers with return obligations do not give rise to an asset for the transfer provider until the transfer recipient breaches the agreement (i.e. a breach is treated as a separate event).

C12 The diagram (from ED 72, paragraph IG1) below provides an overview of the accounting for transfer expenses with and without performance obligations proposed in ED 72.



## Part 2: Compare key principles in ED 72 and AASB 137

C13 Currently, there is no specific guidance for transfer expenses in Australian Accounting Standards. Of some relevance are Australian-specific modifications to AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*. Paragraphs Aus26.1 and Aus26.2 were added to AASB 137 to address the recognition of liabilities arising from government policies, election promises and statements of intent, such as a formal policy to provide financial aid

to victims of natural disasters. These liabilities require the transfer of resources to other parties without the transfer provider directly receiving any good, service or other asset in return. The incurrence of such liabilities is typically accounted for by public sector entities as an expense – which would be a ‘transfer expense’ as defined in ED 72.

- C14 The guidance in AASB 137 does not distinguish between government policies, election promises and statements of intent with performance obligations and those without performance obligations for the transfer recipients. Staff consider that the guidance in AASB 137 does not establish a clear and complete framework for accounting for transfer expenses.
- C15 As IPSASB Standards also do not set out a framework for accounting for transfer expenses, ED 72 proposes an approach based on whether the transfers arise under binding arrangements, and if so, whether the transfer recipients have performance obligations. The proposals also address the timing of the transfer provider recognising transfer expenses, for example initially requiring the transfer provider to recognise an asset (rather than a transfer expense) in certain circumstances.
- C16 ED 72 also includes proposals for the measurement, presentation and disclosure of transfer expenses. These are not specifically addressed in AASB 137, although it does specify the scope of present obligations for the transfer provider in respect of social benefits as excluding social welfare payments that might arise in future reporting periods. Similarly, under AASB 137, a government does not have a present obligation to sacrifice future economic benefits under multi-year public policy agreements until the grantee meets conditions such as grant eligibility criteria, or has provided the services or facilities required under the grant agreement. The scope of a present obligation affects its measurement.

### **Part 3: Contrast the definitions of an asset in the IPSASB and AASB Conceptual Frameworks**

#### ***A transfer provider binding arrangement asset under IPSASB CF***

- C17 As noted in paragraph C8, if a transfer expense transaction gives rise to performance obligations and meets certain criteria, ED 72 proposes that the transfer provider should initially recognise a transfer provider binding arrangement asset for the right to have a transfer recipient transfer goods and services to third-party beneficiaries. The conceptual question to consider is whether the transfer provider has an asset even when it has already transferred resources to the transfer recipient and controls what the recipient does with the resources by virtue of the arrangement under which the transfer occurred.
- C18 ED 72 is based on the view (paragraphs BC21-BC32) that binding arrangement assets satisfy the definition of an asset in the IPSASB’s *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (IPSASB CF): an asset is “a **resource presently controlled** by the entity as a result of a **past event**” (paragraph 5.6, emphasis added).
- *Resources* – the rights to have goods or services transferred to the specified third parties satisfies the definition of a “resource” as that right will be an item with service potential, which enables the transfer provider to meet its objectives (paragraphs 5.7-5.8 of IPSASB CF).

- *Control* – under the binding arrangement, the transfer provider will have an enforceable right to have goods or services transferred to a third-party beneficiary. The transfer provider therefore will have the means to ensure that the resources are used to achieve the transfer provider’s objectives, which means that the transfer provider presently controls the resources (paragraphs BC29-BC31 of ED 72).
- *Past event* – the past event is entering into the binding arrangement, which gives rise to the enforceable right and control by the transfer provider (paragraph BC32 of ED 72).

ED 72 concludes that binding arrangement assets meet the definition of an asset in the IPSASB Conceptual Framework. The transfer provider would control this asset until the transfer recipient satisfies its performance obligation.

### ***Definition of an asset under the AASB Conceptual Frameworks***

C19 The AASB *Framework for the Preparation and Presentation of Financial Statements* (AASB CF 2004) defines an asset as “a **resource controlled** by the entity as a result of **past events** and **from which future economic benefits are expected to flow to the entity**” (paragraph 49 of the CF 2004, emphasis added). An Australian-specific paragraph for not-for-profit entities in the public or private sector states:

Aus49.1 In respect of not-for-profit entities in the public or private sector, in pursuing their objectives, goods and services are provided that have the capacity to satisfy human wants and needs. Assets provide a means for entities to achieve their objectives. Future economic benefits or service potential is the essence of assets. Future economic benefits is synonymous with the notion of service potential, and is used in this Framework as a reference also to service potential. Future economic benefits can be described as the scarce capacity to provide benefits to the entities that use them, and is common to all assets irrespective of their physical or other form.

C20 Staff consider that the definition of an asset in the AASB CF 2004 is closely aligned with the definition of an asset in the IPSASB CF. A transfer provider binding arrangement asset that meets the definition of an asset under the IPSASB CF would also meet the definition of an asset under the AASB CF.

C21 The AASB *Conceptual Framework for Financial Reporting* (CF 2019) defines an asset as “a present economic resource controlled by the entity as a result of past events” (paragraph 4.3) and an economic resource as “a right that has the potential to produce economic benefits” (paragraph 4.4). Staff consider the definition of an asset in AASB CF 2019 closely aligns with the definitions in the IPSASB CF and AASB CF 2004. The AASB CF 2019 currently is not applicable to not-for-profit entities and does not yet include modifications to address the link between service potential and future economic benefits for assets of not-for-profit entities. The Board is currently undertaking a project to modify this Conceptual Framework where necessary for not-for-profit entity considerations.

#### **Part 4: Staff's analysis and proposed responses to the Specific Matters for Comment**

C22 ED 72 contains nine Specific Matters for Comment (SMC), which cover the following topics:

- SMC1: Scope of ED 72 (paragraphs C24-C26)
- SMC2: Distinguishing transfer expenses with and without performance obligations (paragraphs C27-C29)
- SMC3: Transfer provider monitoring of transfers with performance obligations (paragraphs C30-C34)
- SMC4: Recognition and measurement of transfer expenses with performance obligations (paragraphs C35-C40)
- SMC5: Practical difficulties re recognition and measurement of transfer expenses with performance obligations (paragraphs C41-C42)
- SMC6: Recognition and measurement of transfer expenses without performance obligations (paragraphs C43-C45)
- SMC7: Asymmetry in recognising transfers with present obligations (paragraphs C46-C48)
- SMC8: Binding arrangement subject to appropriations (paragraphs C49-C50)
- SMC9: Disclosure requirements (paragraph C51).

C23 Staff recommend the Board provide detailed responses to SMC1-SMC8. Staff consider that it is not necessary to provide a response to SMC9.

#### ***SMC1: Scope of ED 72***

C24 Staff consider the scope of ED 72 as detailed in paragraphs 3-5 of ED 72 might be difficult to apply consistently in practice, since for some transactions it will not be clear whether a Transfer Expenses Standard or another IPSAS should be applied. Staff sought to test the transfer expense definition and the scope exclusions by applying them to a range of Australian transactions. They appeared difficult to apply in practice, which may lead to diverse outcomes with public sector entities applying different IPSAS to arrangements that may be economically similar in substance.

C25 For example, the JobKeeper scheme, administered by the Australian Taxation Office, supports businesses during the COVID-19 pandemic to retain their employees by subsidising their salary and wages. Eligible businesses are required to register with the ATO to receive these payments for their eligible employees. There might be different views on whether the predominant objective of the scheme is to support the employers (via subsidy of their expenses) or to support employees and their household income during the pandemic (i.e. mitigating social risks). The transfer provider would have to apply its judgement to determine whether to account for the transfer as a social benefit or a transfer expense.

C26 The draft Board response to SMC1 is included in the box below for the Board's consideration.

**Specific Matter for Comment 1:**

The scope of this [draft] Standard is limited to transfer expenses, as defined in paragraph 8. The rationale for this decision is set out in paragraphs BC4–BC15.

Do you agree that the scope of this [draft] Standard is clear? If not, what changes to the scope or definition of transfer expense would you make?

**Proposed AASB response:**

The AASB does not agree that the scope of ED 72 is clear. The AASB considers the scope as detailed in paragraphs 3-5 of ED 72 might be difficult to apply consistently in practice, since for some transactions it will not be clear whether a Transfer Expenses Standard or another IPSAS should be applied. This may lead to diverse outcomes, with public sector entities applying different IPSAS to arrangements that may be economically similar in substance. A transfer provider would have to apply its judgement to determine whether to account for the transfer as a transfer expense or other transactions, such as social benefits.

***SMC2: Distinguishing transfer expenses with and without performance obligations***

C27 As discussed in Part 2 of this section (paragraphs C2-C16), the requirements in ED 72 vary, depending upon whether there is a binding arrangement and, if so, whether the binding arrangement establishes performance obligations for the transfer recipient. The approach proposed in ED 72 mirrors the distinction for revenue transactions proposed in ED 70 *Revenue with Performance Obligations* and ED 71 *Revenue without Performance Obligations*.

C28 This approach in ED 72 is consistent with the AASB's approach in addressing Australian stakeholders' concerns that determining whether a transaction is reciprocal or non-reciprocal (or exchange or non-exchange) in practice is not always straightforward (see paragraph BC3 to AASB 2016-8, attached to AASB 15). One of the amendments the Board made to AASB 15 to address these concerns, along with other amendments to support not-for-profit entities applying AASB 15 for revenue recognition, was to clarify that any contract with a customer that is not enforceable or does not contain sufficiently specific performance obligations is not within the scope of AASB 15 for not-for-profit entities (paragraph Aus9.1 of AASB 15). These entities would consider the requirements of AASB 1058 in accounting for such contracts. The Board noted that this amendment would help to avoid confusion and divergence in practice (paragraph BC18 to AASB 2016-8).

C29 Therefore, AASB 15 and AASB 1058 address revenue recognition for not-for-profit entities depending on whether the contract (or other arrangement) is enforceable and contains sufficiently specific performance obligations. Distinguishing between transfer expenses with performance obligations and transfer expenses without performance obligation

would apply a similar basis for the counterparty in recognising expenses. The draft Board response to SMC2 is included in the box below for the Board's consideration.

**Specific Matter for Comment 2:**

Do you agree with the proposals in this [draft] Standard to distinguish between transfer expenses with performance obligations and transfer expenses without performance obligations, mirroring the distinction for revenue transactions proposed in ED 70, Revenue with Performance Obligations, and ED 71, Revenue without Performance Obligations?

If not, what distinction, if any, would you make?

**Proposed AASB response:**

The AASB generally agrees with the approach in ED 72 to distinguish between transfer expenses with performance obligations and transfer expenses without performance obligations. This would be similar to the distinction, based on performance obligations, applied under Australian Accounting Standards for the recognition of revenue by not-for-profit entities, through AASB 15 *Revenue from Contracts with Customers* and AASB 1058 *Income of Not-for-Profit Entities*.

***SMC3: Transfer provider monitoring of transfers with performance obligations***

- C30 One of the modifications proposed by the IPSASB to enable transfer providers to use the Public Sector Performance Obligation Approach (PSPOA) in accounting for transfer expenses would require the transfer provider to monitor the satisfaction of the transfer recipient's performance obligations throughout the duration of the binding arrangement. Without such monitoring, the transfer provider would not have reliable information about when to recognise a transfer expense, and in that case would account for the arrangement as if it gave rise to a transaction without performance obligations for the transfer recipient. The IPSASB had concerns that a lack of monitoring by the transfer provider could lead to inappropriate delays in the recognition of an expense (paragraphs AG27 and BC38 of ED 72). The guidance proposed in ED 72 has been developed taking into account the information that is expected to be available to a transfer provider (paragraph AG25 of ED 72).
- C31 Staff agree with the IPSASB's reasoning that monitoring would enable a transfer provider to acquire reliable information about when to recognise a transfer expense. However, the approach could mean that arrangements with the same nature might have a different accounting outcome depending only on whether the transfer provider chooses to monitor the satisfaction of performance obligations by the transfer recipient. Nevertheless, it would not be appropriate for a transfer provider to attempt to recognise transfer expenses based on assumptions as to the transfer recipient's satisfaction of performance obligations. That approach would most likely not result in a faithful representation of the transfer provider's binding arrangement assets and transfer expenses. In such circumstances, the transfer should be accounted for as a transfer expense without performance obligations, as proposed in ED 72.

- C32 The diagram in paragraph IG1 in ED 72 (also included in paragraph C12 of this paper) that summarises the accounting for transfer expenses does not portray the effect of the transfer provider monitoring (or not monitoring) the transfer recipient satisfying the performance obligations under an arrangement. The diagram should be revised for this. A revised diagram is presented in the draft Board response to SMC3.
- C33 The diagram is also confusing in the way it presents the recognition of transfer expenses without performance obligations, based on the earlier of when the transfer provider (a) has a present obligation to transfer resources and (b) transfers the resources to the transfer recipient. The suggested amendments to the diagram for this point are also shown in the draft SMC3 response.
- C34 The draft Board response to SMC3 is included in the following box:

**Specific Matter for Comment 3:**

Do you agree with the proposal in this [draft] Standard that, unless a transfer provider monitors the satisfaction of the transfer recipient's performance obligations throughout the duration of the binding arrangement, the transaction should be accounted for as a transfer expense without performance obligations?

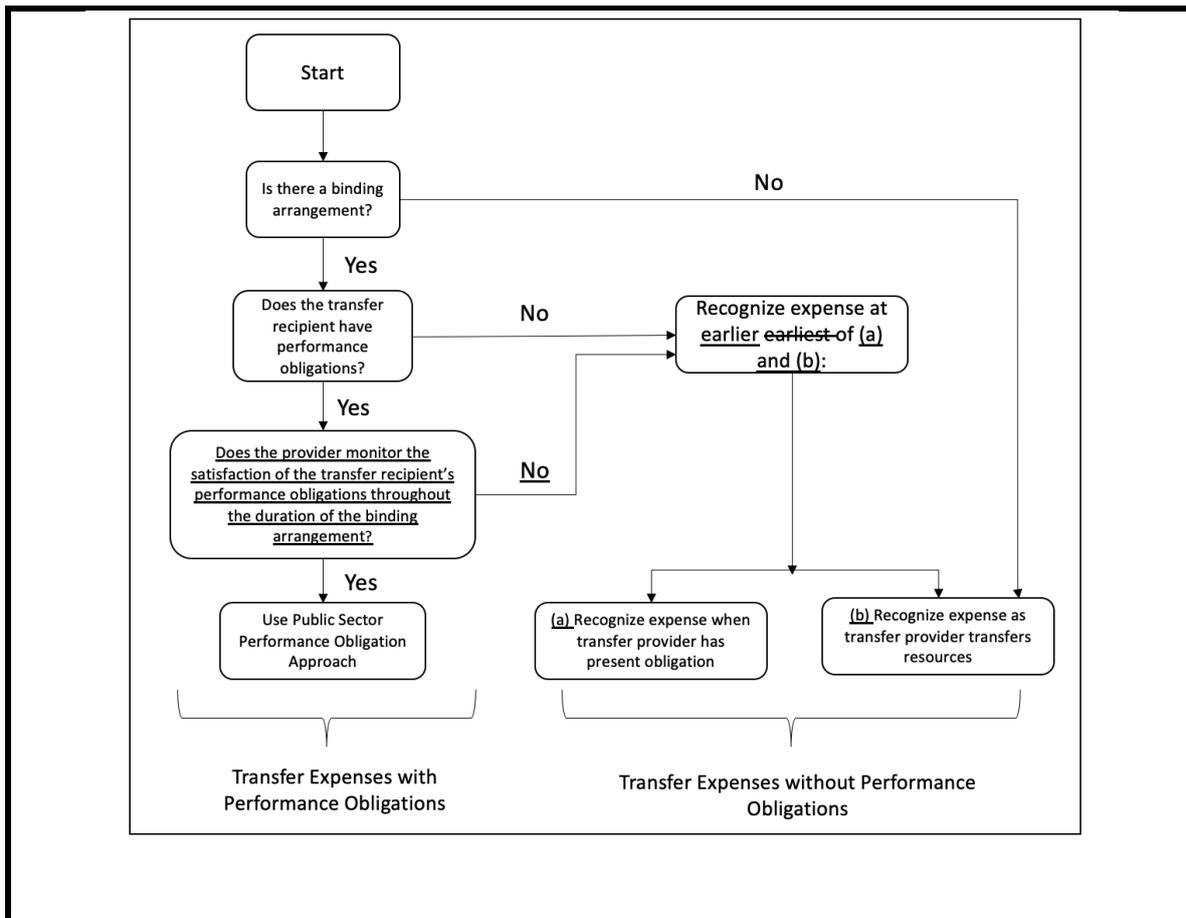
**Proposed AASB response:**

The AASB agrees with the IPSASB's reasoning that monitoring would enable a transfer provider to acquire reliable information about when to recognise a transfer expense. However, the approach could mean that arrangements with the same nature might be accounted for differently depending only on whether the transfer provider chooses to monitor the satisfaction of performance obligations by the transfer recipient.

Nevertheless, it would not be appropriate for a transfer provider to attempt to recognise transfer expenses based on assumptions as to the transfer recipient's satisfaction of performance obligations. That approach would most likely not result in a faithful representation of the transfer provider's binding arrangement assets and transfer expenses. The AASB therefore agrees with the proposal in ED 72 that the transfer should be accounted for as a transfer expense without performance obligations in such circumstances.

The diagram in paragraph IG1 in ED 72 that summarises the accounting for transfer expenses does not portray the effect of the transfer provider monitoring (or not monitoring) the transfer recipient satisfying the performance obligations under an arrangement. The diagram should be revised for this.

The diagram is also confusing in the way it presents the recognition of transfer expenses without performance obligations, based on the earlier of when the transfer provider (a) has a present obligation to transfer resources and (b) transfers the resources to the transfer recipient. The suggested amendments to the diagram are shown in the following diagram:



**SMC4: Recognition and measurement of transfer expenses with performance obligations**

C35 As discussed in Part 3 of this section (paragraphs C17-C21), a transfer provider binding arrangement asset that meets the definition of an asset under the IPSASB CF would also meet the definition of an asset under the AASB CF. Conceptually, staff agree with the ED 72 proposal that a transfer provider should initially recognise an asset for the right to have a transfer recipient transfer goods and services to third-party beneficiaries as required by performance obligations under the binding arrangement.

C36 The recognition criteria in the IPSASB CF are as follows (paragraph 6.2 of the IPSASB CF):

- (a) an item satisfies the definition of an element; and
- (b) can be measured in a way that achieves the qualitative characteristics and takes account of constraints on information in general purpose financial reports.<sup>7</sup>

<sup>7</sup> The constraints on information in GPFs are materiality, cost versus benefit, and balance between the qualitative characteristics (i.e. the qualitative characteristics working together to contribute to the usefulness of information) (paragraphs 3.32-3.42 of the IPSASB CF).

C37 Similarly, the AASB CF 2004 addresses the recognition of assets and expenses as follows:

89 An asset is recognised in the balance sheet when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably.

94 Expenses are recognised in the income statement when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably. ...

C38 As noted in Part 3 (paragraph C18), the transfer provider expects to benefit under the binding arrangement because the transfer of the goods or services to the third-party beneficiaries by the transfer recipient will further the objectives of the transfer provider. Accordingly, the “future economic benefit” part of the asset recognition criteria under the AASB CF 2004 will be satisfied.

C39 Staff expect that if the transfer provider is monitoring the satisfaction of the transfer recipient’s performance obligations throughout the duration of the binding arrangement, then the decrease in the asset and the transfer expense can be reliably measured by the transfer provider based on supporting evidence, in accordance with the PSPOA. The recognition criteria under both the IPSASB CF and the AASB CF 2004 are therefore able to be satisfied.

C40 The draft Board response to SMC4 is included below in the box:

**Specific Matter for Comment 4:**

This [draft] Standard proposes the following recognition and measurement requirements for transfer expenses with performance obligations:

- (a) A transfer provider should initially recognize an asset for the right to have a transfer recipient transfer goods and services to third-party beneficiaries; and
- (b) A transfer provider should subsequently recognize and measure the expense as the transfer recipient transfers goods and services to third-party beneficiaries, using the public sector performance obligation approach.

The rationale for this decision is set out in paragraphs BC16–BC34.

Do you agree with the recognition and measurement requirements for transfer expenses with performance obligations? If not, how would you recognize and measure transfer expenses with performance obligations?

**Proposed AASB response:**

The AASB agrees conceptually with the recognition and measurement requirements for transfer expenses with performance obligations.

The transfer provider's rights under a binding arrangement to have the transfer recipient transfer agreed goods or services to third-party beneficiaries furthers the objectives of the transfer provider and justifies the initial recognition of an asset.

Since the transfer provider is monitoring the transfer recipient's satisfaction of its performance obligations, the transfer provider will have sufficient information with which to measure and recognise the decrease in the asset and the incurrence of transfer expenses, in accordance with the PSPOA.

***SMC5: Practical difficulties re recognition and measurement of transfer expenses with performance obligations***

C41 Staff have concerns that transfer providers will face both practical difficulties and some level of compliance cost to monitor a transfer recipient satisfying performance obligations throughout an arrangement. Monitoring could require continuous assessment of the progress and quality of performance. This could be costly for transfer providers, particularly if there is no readily available system for performing such assessments. It is not clear in ED 72 whether monitoring requires continuous assessment or whether periodic assessment would be sufficient. It would be useful for the IPSASB to develop application guidance on monitoring processes to assist transfer providers.

C42 The draft Board response to SMC 5 is included below in the box:

**Specific Matter for Comment 5:**

If you consider that there will be practical difficulties with applying the recognition and measurement requirements for transfer expenses with performance obligations, please provide details of any anticipated difficulties, and any suggestions you have for addressing these difficulties.

**Proposed AASB response:**

The AASB notes that there are potential practical difficulties and compliance cost for the transfer provider in monitoring the transfer recipient's performance obligation throughout the duration of a binding arrangement. The AASB is of the view that transfer provider monitoring needs continuous or periodic assessment of the progress and quality of performance, which could be costly for transfer providers, particularly if there is no readily available system for performing such assessments. It is not clear in ED 72 whether periodic assessment would be sufficient, and if so, how frequent that might need to be.

The AASB recommends the IPSASB develop application guidance on monitoring processes to assist transfer providers.

***SMC6: Recognition and measurement of transfer expenses without performance obligations***

C43 Staff generally agree with the proposed recognition and measurement requirements for transfer expenses without performance obligations but have a few comments. First, the

guidance in ED 72 for transfer expenses without performance obligations made as a series of transfers of resources appears to be insufficient. Paragraph 97 of ED 72 requires a transfer provider to apply paragraphs 91-94 to each transfer of resources to determine whether an expense should be recognised. However, paragraphs 91-94 do not address the timing of recognising the present obligation for each transfer of resources. That is, should the transfer provider recognise an expense and a liability at the beginning of the arrangement only for the next transfer or for some or all of the transfers? This lack of guidance in ED 72 may lead to inconsistent treatment for transfer expenses without performance obligations made as a series of transfers of resources. Staff therefore recommend the IPSASB provide further guidance on this issue.

C44 Second, the subsection for the subsequent measurement of other non-contractual payables appears to be outside the scope of the ED altogether, as paragraph 120 is stated to apply to payables that do not meet the definition of a transfer expense. Therefore, staff recommend the IPSASB to delete the paragraph. If such other payables should apply the subsequent measurement requirements of paragraphs 116-119, then that should be incorporated into another IPSAS – IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* is a better candidate. Consequential amendments could be proposed to IPSAS 19.

C45 The draft Board response to SMC 6 is included below in the box:

<p><b>Specific Matter for Comment 6:</b></p> <p>This [draft] Standard proposes the following recognition and measurement requirements for transfer expenses without performance obligations:</p> <ul style="list-style-type: none"><li>(a) A transfer provider should recognize transfer expenses without performance obligations at the earlier of the point at which the transfer provider has a present obligation to provide resources, or has lost control of those resources (this proposal is based on the IPSASB’s view that any future benefits expected by the transfer provider as a result of the transaction do not meet the definition of an asset); and</li><li>(b) A transfer provider should measure transfer expenses without performance obligations at the carrying amount of the resources given up?</li></ul> <p>Do you agree with the recognition and measurement requirements for transfer expenses without performance obligations?</p> <p>If not, how would you recognize and measure transfer expenses without performance obligations?</p>
<p><b>Proposed AASB response:</b></p> <p>The AASB generally agrees with the recognition and measurement requirements for transfer expenses without performance obligations. However, the AASB has some specific comments.</p>

First, the guidance in ED 72 for transfer expenses without performance obligations made as a series of transfers of resources appears to be insufficient. Paragraph 97 of ED 72 requires a transfer provider to apply paragraphs 91-94 to each transfer of resources to determine whether an expense should be recognised. However, paragraphs 91-94 do not address the timing of recognising the present obligation for each transfer of resources. It is unclear whether the transfer provider should recognise an expense and a liability at the beginning of the arrangement only for the next transfer or for some or all of the transfers. This lack of guidance may lead to inconsistent treatment for transfer expenses without performance obligations made as a series of transfers of resources. The AASB recommends the IPSASB provide further guidance on this issue.

Second, the subsection for the subsequent measurement of other non-contractual payables (paragraph 120) appears to be outside the scope of the ED, as it addresses payables that do not meet the definition of a transfer expense. Consequential amendments could instead be made to another IPSAS, such as IPSAS 19.

***SMC7: Asymmetry in recognising transfers with present obligations***

C46 The requirements proposed in this section of ED 72 (paragraphs 90-119) do not mirror those in ED 71. ED 71 proposes that transfer recipients that do not have performance obligations might still have present obligations (to carry out specified activities or incur eligible expenditure), and in such cases should recognise revenue when (or as) they satisfy those obligations. In contrast, transfer expenses without performance obligations will be recognised immediately by transfer providers when the resources are transferred (or, if earlier, when the transfer provider has a present obligation to transfer the resources), regardless of whether the transaction gives rise to present obligations for the resource recipient. This will lead to asymmetric recognition of transfer expenses and revenue by the transfer provider and the transfer recipient respectively. The IPSASB's rationale for this approach is set out in ED 72 paragraphs BC52-BC58.

C47 Staff generally consider that asymmetry in the accounting by transfer providers versus transfer recipients is appropriate, if it reflects the differing circumstances of the entities. Symmetrical accounting should not simply be assumed. However, the approach in ED 71 that would require transfer recipients to recognise liabilities for present obligations under transfers without performance obligations is not supported.

C48 The draft Board response to SMC 7 is included in the box below:

**Specific Matter for Comment 7:**

As explained in SMC 6, this [draft] Standard proposes that a transfer provider should recognize transfer expenses without performance obligations at the earlier of the point at which the transfer provider has a present obligation to provide resources, or has lost control of those resources. ED 71, *Revenue without Performance Obligations*, proposes that where a transfer recipient has present obligations that are not performance obligations, it should recognize revenue as it satisfies those present

obligations. Consequently, a transfer provider may recognize an expense earlier than a transfer recipient recognizes revenue.

Do you agree that this lack of symmetry is appropriate? If not, why not?

**Proposed AASB response:**

The AASB generally considers that asymmetry in the accounting by transfer providers versus transfer recipients is appropriate, if it reflects the differing circumstances of the entities. Symmetrical accounting should not simply be assumed. However, the approach in ED 71 that would require transfer recipients to recognise liabilities for present obligations under transfers without performance obligations is not supported.

***SMC8: Binding arrangement subject to appropriations***

C49 Staff agree with the proposal in ED 72 that when a binding arrangement is subject to appropriations, the transfer provider needs to consider whether in substance it has a present obligation to transfer resources and, if so, should recognise a liability, prior to the appropriation being authorised. In some jurisdictions, the transfer provider might lose its discretion to avoid proceeding with a transfer through entering into a binding arrangement, with the subsequent appropriation a matter of form. However, in other jurisdictions, an arrangement might be implicitly subject to a formal appropriation process in order to become binding. Paragraphs AG98-AG102 in ED 72 address both circumstances.

C50 The draft Board response to SMC 8 is included in the box below:

**Specific Matter for Comment 8:**

This [draft] Standard proposes that, when a binding arrangement is subject to appropriations, the transfer provider needs to consider whether it has a present obligation to transfer resources, and should therefore recognize a liability, prior to the appropriation being authorized. Do you agree with this proposal?

If not, why not? What alternative treatment would you propose?

**Proposed AASB response:**

The AASB agrees with the proposal in ED 72 that when a binding arrangement is subject to appropriations, the transfer provider needs to consider whether in substance it has a present obligation to transfer resources and, if so, should therefore recognise a liability, prior to the appropriation being authorised.

***SMC9: Disclosure requirements***

C51 Staff recommend that the Board not comment on this SMC. The proposed disclosure requirements in ED 72 mirror the requirements in ED 70 and ED 71. As staff recommend

the Board not comment on the disclosure requirements for ED 71 (see paragraph B38), staff consider it is not necessary to respond to SMC9 regarding the disclosure requirements proposed in ED 72.

**Specific Matter for Comment 9:**

This [draft] Standard proposes disclosure requirements that mirror the requirements in ED 70, *Revenue with Performance Obligations*, and ED 71, *Revenue without Performance Obligations*, to the extent that these are appropriate.

Do you agree the disclosure requirements in this [draft] Standard are appropriate to provide users with sufficient, reliable and relevant information about transfer expenses? In particular,

- (a) Do you think there are any additional disclosure requirements that should be included?
- (b) Are any of the proposed disclosure requirements unnecessary?

**Proposed AASB response:**

(Staff recommend the Board to not comment on this SMC.)

**Questions to the Board:**

Q8 Do Board members agree to provide responses on all SMCs for ED 72, except for SMC9 regarding disclosure requirements?

Q9 Do Board members agree with staff's views and the draft wording for responses to each of the above SMCs?

## Appendix – Glossary and Extracts from AASB 1058

### Glossary

This Appendix contains definitions of defined terms use in ED 71 and ED 72 for the Board’s reference.

A **transfer** is a transaction, other than taxes, in which an entity receives a good, service, or other asset from another entity (which may be an individual) without directly providing any good, service, or other asset in return.

A **transfer expense** is an expense arising from a transaction, other than taxes<sup>8</sup>, in which an entity provides a good, service, or other asset to another entity (which may be an individual) without directly receiving any good, service, or other asset<sup>9</sup> in return.

A **transfer provider** is an entity that provides a good, service or other asset to another entity without directly receiving any good, service or other asset in return.

A **transfer recipient** is an entity that receives a good, service, or other asset from another entity without directly providing any good, service, or other asset to that entity.

A **transfer recipient's binding arrangement asset** is an entity’s right to a transfer to satisfy a present obligation when that right is conditioned on something other than the passage of time (for example, the entity’s future performance).

A **transfer recipient's binding arrangement liability** is an entity’s obligation to satisfy a present obligation for which the entity has received an amount (or the amount is due) from the transfer provider.

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

**Eligible expenditure** is an outflow of resources incurred in accordance with the requirements set out in a binding arrangement.

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

### Extracts from AASB 1058 (relevant for the discussion in ED 71 – see paragraph B27)

B15 An entity that receives a financial asset, such as cash, in a transfer to enable the entity to acquire or construct a recognisable non-financial asset to be controlled by the entity shall apply the requirements of AASB 9 to that financial asset. The acquisition or construction of the non-financial asset is accounted for separately to the transfer of the financial asset, in accordance with other Standards. If the non-financial asset is not

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8 Taxes include other compulsory contributions and levies, as defined in ED 71.

9 The definition of a transfer expense includes references to “other asset” (for example, a non-current asset) for completeness. Elsewhere in ED 72, references to goods and services or to goods or services are to be read as incorporating references to assets.

permitted to be recognised by another Standard (eg knowledge or intellectual property developed through research, which cannot be recognised as an asset in accordance with AASB 138), paragraphs 15–17 do not apply. The key criterion is that the recognisable non-financial asset will be under the control of the entity (ie for its own use) – it will not be transferred to the transferor or other parties. Therefore, the transfer of the financial asset (or the relevant part) to the entity does not occur under a contract with a customer and is not subject to AASB 15. However, the recognisable non-financial asset could increase the entity's ability or capacity to provide goods or services to other parties pursuant to other transactions, which are separate to the transfer that enabled the entity to acquire or construct the nonfinancial asset for its own use.

- BC98 For avoidance of doubt, the Board decided to identify the accounting that applies to such transfers ... the Board observed that in such arrangements, in substance, the transferor had intended to transfer a recognisable non-financial asset to the not-for-profit entity. The Board considered that an in-substance transfer of a good for use by the entity itself should not result in income until the recipient has satisfied its obligation to construct or acquire the asset. That is, the timing of income recognition should reflect the entity receiving the asset directly, rather than the cash to construct or acquire the asset. Accordingly, the Board decided that the accounting for such transactions should reflect that of the approach in AASB 15. However, given the diverse views as to whether AASB 15 applies, the Board decided to specify instead requirements in AASB 1058 to mirror, to the extent appropriate, the accounting that would be achieved had the transaction been accounted for had it been incontestably a contract with a customer within the scope of AASB 15.