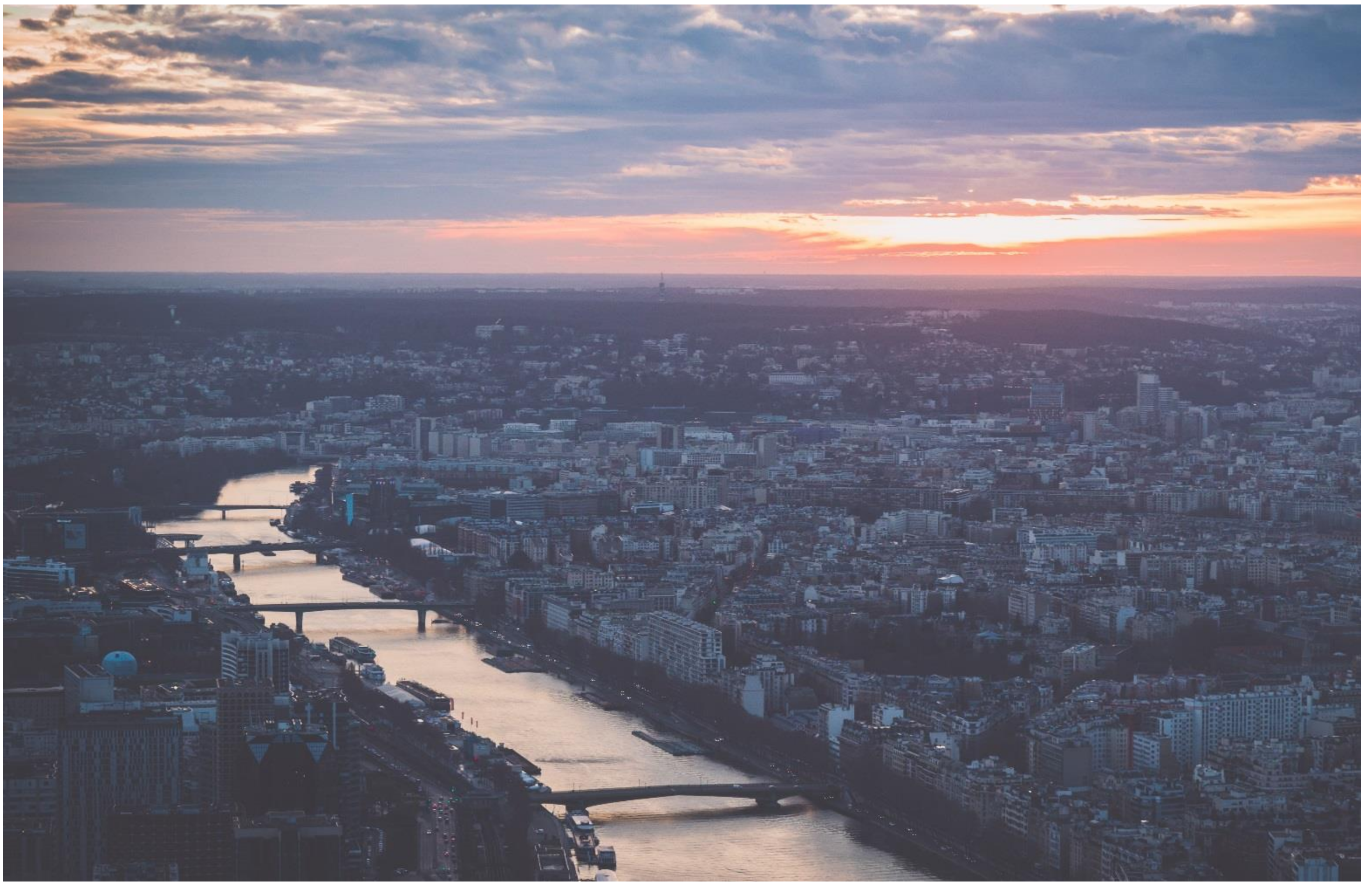
FEEDBACK STATEMENT

DISCUSSION PAPER

NON-EXCHANGE TRANSFERS

A ROLE FOR SOCIETAL BENEFIT?

July 2019



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EFRAG
European Financial Reporting Advisory Group

Introduction

In November 2018, EFRAG issued the Discussion Paper Non-Exchange Transfers: A Role for Societal Benefit? ('DP'). EFRAG requested comments by 30 April 2019.

EFRAG is now issuing a feedback statement, which describes the main comments received.

Why was this Discussion Paper written?

When responding to the IASB's 2016 Agenda Consultation, some constituents identified transfers whereby entities do not directly receive (or give) approximately equal value as an area requiring attention. The DP refers to such transfers as Non-Exchange Transfers (NETs) and suggests that they could require a specific accounting treatment based on their characteristics which differ from the characteristics of ordinary commercial transactions between independent parties. Many NETs are imposed and entities do not have the ability to avoid them. Additionally, for NETs:

a) it is not always possible to identify the goods or services received in exchange for the consideration; or
b) the goods or services received and the consideration transferred are of unequal value.

The DP explores a comprehensive approach to report these transfers. The DP notes that NETs may be motivated by an objective of 'societal benefit' and considers how this notion could be used in accounting for them.

This DP is issued by EFRAG as part of its Research activity. EFRAG aims to influence future standard-setting developments by engaging with European constituents and providing timely and effective input to early phases of the IASB's work.

Responses from constituents

EFRAG has received and considered 13 comment letters from constituents (see list of respondents in Appendix). These comment letters are available on the EFRAG website.

The comment letters received came from national standard-setters, preparers, professional and other organisations.

Purpose and use of this feedback statement

This feedback statement has been prepared as a formal record of the responses received. It summarises the messages received from constituents and notes any key themes identified.

This feedback statement should be read in conjunction with the Discussion Paper on Non-exchange Transfers , which is available on the EFRAG website.

Summary of the responses received

Overview of the feedback received

Some respondents agreed that non-exchange transactions (NETs) have different characteristics but a majority did not support developing an approach aiming to address comprehensively all non-exchange transfers. Some respondents suggested that the existing IFRS Standards provided sufficient guidance as to how to account for NETs and the focus of the DP should be on considering the effects of the revised Conceptual Framework on NETs, in particular whether and how it would address identified issues. Some respondents did not see issues with the current accounting for grants and suggested that identified issues such as the accounting for levies could be addressed as part of the IASB research on provisions. Some respondents raised concerns with the proposed scope exceptions such as income tax, transactions with related parties and with shareholders. Those respondents did not agree with the scope exemptions as they considered that those were the areas which needed of further guidance. Some respondents considered that the broad references to 'societal benefit' and non-exchange transactions proposed approach could have unintended consequences.

Most respondents did not support the 4-step approach to account for NETs. In their view, the criterion of recognition of NETs income and expenses on a 'recurring basis' was not conceptually developed and instead it was based on a rule-based principle.

Outreach events

EFRAG presented the DP at the International Forum of Accounting Standard Setters (IFASS) meeting in March 2019. The key messages received include:

- the treatment of some of the transactions discussed in the DP such as levies and government grants may require standard-setting, however, doubts were expressed that a comprehensive approach would be helpful;
- some concerns were expressed about the clarity of the proposed definition of non-exchange transfers which could potentially apply to a wider number of transactions; and
- although the 'societal benefit' notion in the model provided a pragmatic solution, some reservations were expressed that it lacked a conceptual basis to justify progressive recognition.

Analysis of responses

Question 1 – Do you agree that NETs have differentiating characteristics that warrant the development of a specific accounting treatment?

A majority of respondents did not support the objective of the project and the DP proposal that NETs warrant a specific accounting treatment. Two respondents commented that the existing IFRS guidance has proven to work well in practice and therefore there was not sufficient justification for the replacement of a wide range of existing accounting guidance. Furthermore, those respondents explained that the revised Conceptual Framework could solve some of the application issues with respect to existing IFRS guidance such as IFRIC 21 *Levies*.

Four respondents agreed that NETs had specific characteristics which could warrant a different accounting treatment. However, they commented that the approach explored in the DP applied a model that addressed only those NETs encountered by for-profit entities and did not consider a wider range of transactions encountered by not-for profit and public sector entities which risked developing an accounting treatment that overlooked some NETs characteristics. One respondent suggested developing a stronger conceptual basis that would underpin a set of principles for standard setters to use in considering different types of NETs and to assess whether there was a need to develop specific accounting treatments on a case-by-case basis.

Question 2 – Scope of the project

Question 2.1 - Do you agree with how the scope has been defined? If not, is there a different scope that would provide a better basis for developing a comprehensive approach?

Most respondents disagreed with the scope of the DP. One respondent suggested that the scope of the project should be narrowed to how the revision of the Conceptual Framework would affect the accounting for regulatory bank levies as legally designed in Europe. Conversely, another respondent suggested that the starting point should be to analyse expected effects of the new definition of a liability in different IFRS Standards that deal with different types of NETs. Firstly, whether under the revised Conceptual Framework existing IFRS Standards would provide different recognition models for similar types of NETs and secondly, evaluate what types of NETs do not have any explicit guidance. Another respondent commented that considering that the vast majority of transactions undertaken by public benefit entities meet the definition of a NET, the DP should have given greater consideration to public benefit entities as it which fails to develop a comprehensive approach to accounting for NETs.

Question 2.2 - Is the definition of NETs and the guidance around the assessment of their existence sufficiently clear and operational?

Most respondents disagreed with the proposed definition of NETs. Those respondents expressed concerns that the definition of NETs as proposed in the DP was very broad and would cover a much wider range of contractual transfers which may have unintended consequences such as application by analogy. For example, the definition could be interpreted to classify transactions as NETs where an entity signs loss making contracts in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* on a voluntary basis for a short period of time to enter a new market. Consequently, this would result in different recognition guidance for such transfers compared to existing IFRS guidance. One respondent commented that the conclusion that an exchange of unequal value in a voluntary transaction implied 'societal benefit' was far-fetched and lacked justification.

One respondent suggested that the proposed definition of NETs in the DP should be more specific in order to eliminate the risk of using 'arbitrary' judgement by entities and allow them to use this specific treatment for other transactions. Another respondent suggested that the DP should have given further consideration to how the proposed definition of NETs would apply to voluntary transfers such as charitable donations. Furthermore, some respondents found that the concept of 'non-exchange' was very broad which might have unintended consequences such as including a wide range of transfers within the scope of the DP or including transactions at a contract level which, taking a broader perspective, would not meet the NETs definition. Additionally, one respondent commented that the 'societal benefit' notion was not precisely defined and therefore did not help in conceptualising the derived accounting approaches.

One respondent suggested considering 'societal benefit' in parallel with the IPSASB's current work in order to encourage consistency of accounting for NETs over the private and public sectors which will eliminate complexity and drive greater transparency and accountability in financial reporting.

Question 2.3 - Do you agree with the proposed exclusions from the project? In particular, do you think that the approach could be fit also for income taxes?

Most respondents commented that limiting the scope by excluding certain transactions such as income taxes (IAS 12 *Income Taxes*), rate-regulated activities (IFRS 14 *Regulatory Deferral Accounts*) and transactions with majority shareholders (IFRS 2 *Share-based Payment*) was not clearly explained and resulted in applying a rule-based approach rather than a comprehensive conceptual approach to accounting for NETs. One respondent considered that scope exclusions were not helpful in trying to address the objective of the DP in the first place. In their view, the lack of testing the proposed model on the full range of NETs would run the risk of creating solutions which are of limited application in the longer term.

Two respondents agreed with the scope exclusions. One of them acknowledged that while a comprehensive approach including income taxes was welcomed, it would be difficult to address the conceptual alignment between IAS 12, IAS 37 and the proposed approach to NETs in the DP.

Question 3 – Which of the methods presented in paragraph 2.11 do you support, and why?

Four respondents supported the application of the method presented in paragraph 2.11c) - when a transaction includes a normal commercial exchange and a NET, the entity should allocate the amount to the different components using the guidance in IFRS 15 *Revenue from Contracts with Customers*. In their view this method would provide the most relevant information about the transaction unless such an allocation would be too complex or costly for preparers. One respondent commented that the method proposed in paragraph 2.11c) was technically sound, however, it was likely to be difficult to apply in practice, it was prone to error and created additional costs for preparers. Consequently, the additional information provided to users by allocating the amount to the different components would not justify the additional costs of applying this method.

One respondent supported method 2.11b) - where the entity should allocate the full amount to the predominant component of the transfer. However, this respondent would expect the most appropriate method to be determined by the underlying principles of financial reporting and supported by the basis of accounting for NETs which is consistent with these principles.

Finally, another respondent commented that without an understanding of the wider context and fact pattern of a particular transaction, it was not possible to determine which of the three methods might be the most appropriate way to account for NET included in a commercial transaction. This respondent suggested that the methods outlined in paragraph 2.11 of the DP might better serve as possible ‘factors to consider’ when determining the need for a specific accounting treatment for a particular type of NET.

Question 4 – Which of the approaches presented in paragraph 3.13 do you support, and why?

Most respondents did not comment on this question. One respondent preferred the approach presented in paragraph 3.13a) to recognise the NET income or expense strictly based on the terms of the underlying activity. According to this respondent, the impact of the transaction on profit or loss should depend on the nature of the triggering event and how it is treated under other relevant standards.

Another respondent supported approach 3.13b) - where the underlying activity determines the amount of the transfer at one date but affects profit or loss at a different date, the recognition of the NET income or expense should give prominence to the impact on profit or loss.

Two respondents could not conclude on an appropriate accounting treatment either due to limited context and fact pattern of a particular transaction or misalignment with current accounting practice for similar transaction affecting public benefit entities.

Question 5 – The DP (paragraphs 3.15 to 3.22) proposes that NETs that do not fall in either Step 1 or 2 of the approach explored, and are recurring, are recognised progressively between two payment dates. Do you agree with the outcome? And do you believe that the notion of ‘societal benefit’ provides a conceptually adequate basis to support the outcome?

Most respondents disagreed that NETs that do not fall in either Step 1 or Step 2 of the proposed 4-step approach should be recognised on a recurring basis between two payment dates. One respondent clarified that income from such a NET in practice is considered to be ‘unrestricted income’ and as such should be recognised immediately when there is evidence of entitlement, receipt is probable and the amount can be measured reliably. In their view, this approach resulted in the recipient recognising incoming resources where there is control and a right to spend the assets being transferred. Additionally, this respondent commented that the application of Step 3 and the concept of ‘societal benefit’ focused on transactions with Government and suggested extending the accounting approach in Step 3 by considering a broader range of NETs which are commonly encountered by public benefit entities. This respondent also questioned whether requiring recognition on a straight-line basis would be appropriate and provide users with relevant information considering that the pattern of consumption of the societal benefits was unlikely to be continuous. The respondent saw no conceptual rationale as to why the entity's impact on its beneficiaries should influence its financial performance and financial position. This in their view, represented a significant omission in defining the principles applied in Step 3.

Two respondents agreed with the approach in Step 3 of the proposed 4-step approach to recognise transfers over time between two payment dates. One of these respondents elaborated that unless a specific point in time can be identified, NETs should be accrued over time.

Question 6 – Do you think that the recognition of expense-generating and income-generating transfers should be subject to a symmetrical or asymmetrical approach? Please explain your answer.

A majority of respondents did not address this question.

Three respondents stated that the recognition of expense-generating and income-generating NETs need not be subject to a symmetrical approach as symmetry largely depends on the facts and circumstances of a particular transaction which will affect the resource provider and recipient in different ways. In their view, a symmetrical approach would only be achieved at the expense of prudence and other principles of the revised Conceptual Framework.

Two respondents commented that the recognition of expense-generating and income-generating transfers should follow the approach in the revised Conceptual Framework where uncertainty is a factor affecting measurement rather than recognition.

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APPENDIX – List of Respondents

Respondent	***Country***	***Type***
Accounting Standards Committee of Germany (DRSC)	Germany	National Standard Setter
Swedish Enterprise Accounting Group (SEAG)	Sweden	Business Organisation
The Chartered Institute of Public Finance & Accountancy (CIPFA)	United Kingdom	Professional Organisation
The Charities SORP	United Kingdom	Other Organisation
Autorité des Normes Comptables (ANC)	France	National Standard Setter
ACTEO	Europe	Preparer Organisation
Dutch Accounting Standards Board (DASB)	Netherlands	National Standard Setter
European Savings and Retail Banking Group (ESBG)	Europe	Professional Organisation
Accounting and Auditing Institute (ICAC)	Spain	National Standard Setter
Comissão de Normalização Contabilística (CNC)	Portugal	National Standard Setter
Institute of Chartered Accountants in England and Wales (ICAEW)	United Kingdom	Professional Organisation
BusinessEurope	Europe	Preparer Organisation
Norwegian Accounting Standards Board (NASB)	Norway	National Standard Setter