EFRAG TEG meeting
July 2017
Paper 09-03
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Proactive – Transactions other than Exchanges of Equal Value
Summary of relevant pronouncements

Objective

1 A number of accounting bodies have issued guidance on the recognition of income from transactions where there is no exchange of fair value. These transactions are referred to as non-exchange or non-reciprocal transactions.

2 The scope of the pronouncements include in this paper may be different from the scope of the EFRAG Research project. Firstly, the pronouncements generally apply to public sector entities or non-for-profit entities; secondly, they generally refer only to the recognition of income-generating transactions. The EFRAG project applies to private entities and addresses the recognition of both cost-generating transactions (taxes, levies) and income-generating transactions (grants, contributions).

Available pronouncements

3 EFRAG Secretariat has reviewed the following documents:

(a) IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*[1]*;*

(b) European Union Accounting Rule 17 *Revenue From Non-exchange Transactions (Taxes and Transfers*);

(c) AASB 1004 *Contributions*;

(d) AASB 1058 *Income of Not-for-Profit Entities (effective from 2019*);

(e) Statement 33 of the Governmental Accounting Standards Board Accounting and Financial Reporting for Non-Exchange Transactions; and

(f) UK FRC Staff Education Note 12 *Incoming Resources from Non-Exchange Transactions*.

4 These pronouncements usually address the following aspects:

(a) When the entity receiving the transfer should recognise an asset;

(b) How the asset should be measured at initial recognition;

(c) Whether the entity should recognise a liability;

(d) How any liability recognised should be initially measured;

(e) When should the liability be released to profit or loss.

5 The initial recognition of an asset results in the recognition of income, unless the entity is required to recognise a liability for the same amount.

[1] The IPSASB has a current project to develop one Standard to cover revenue from exchange and non-exchange transactions. The IPSASB is finalising a Consultation Paper to be launched in the summer with a comment period until the end of 2017.

What transactions are in scope?

6 IPSAS 23 applies to non-exchange transaction, that are described as transactions where an entity gives or receives value without directly receiving or giving approximately equal value in exchange. Non-exchange transactions include taxes and transfers, which may take the form of debt forgiveness, bequests, donations and services in-kind.

7 The Standard acknowledges that in some cases professional judgment is required to conclude if a transaction qualifies as a non-exchange transaction. For instance, a purchase at a subsidised price is a non-exchange transaction, but a commercial discount does not necessarily make a transaction qualify as such. The Standard also indicates that in some cases, a transaction may include exchange and non-exchange components.

8 European Union Accounting Rule 17 applies to non-exchange transactions such as taxes and transfers entered into by the European Union (transactions in scope are s similar to IPSAS 23).

9 AASB 1004 applies only to not-for-profit entities (both private and public) and disciplines the recognition of income from non-reciprocal transfers. These are identified when an entity receives an asset without directly giving approximately equal value to the other party. Although the term used is different, the definition is in substance the same as in IPSAS 23. The Standard applies to both voluntary and compulsory contributions.

10 Similarly, AASB 1058 refers to transactions where the consideration to acquire an asset is significantly less than fair value principally to enable a not-for-profit entity to further its objectives.

11 GASB 33 also defines non-exchange transactions as transactions where a government gives or receives value without directly receiving or giving equal value in return. GASB 33 identifies four classes of non-exchange transactions:

(a) Derived tax revenues, which are imposed on exchange transactions – such as income or sales tax;

(b) Imposed non-exchange revenues, which are imposed on non-governmental entities and are different from derived tax revenues, such as property taxes;

(c) Government-mandated non-exchange transactions, when one level of Government provides resources to another level to be used for a specific purpose; and

(d) Voluntary non-exchange transactions, such as grants and private donations.

12 GASB 33 notes that judgment is required to distinguish between exchange and non-exchange transactions – an example would be a private entity providing a grant to a university to fund a research would be an exchange transaction if the entity is entitled to the result of the research. In some cases, a transaction may have an exchange and a non-exchange component.

13 Since these Standards are written from the beneficiary's perspective, they do not refer to cases where the entity cannot determine the nature of what has been received. Unless there is an explicit requirement to provide goods or services in return of the transfer, the entity recognises immediately the transfer as income.

When does the entity recognise an asset and how should it be measured?

14 IPSAS 23 requires recognising an asset in compliance with the definition in the Conceptual Framework. The elements referred to are:

(a) Control over the asset, which is linked to:

(i) Enforceability of the rights;

(ii) Occurrence of a past event

(b) Probability of future economic benefits or service potential flowing to the entity;

(c) Reliability of measurement

15 IPSAS 23 provides that control of an asset arises when the entity can use or otherwise benefit from the asset in pursuit of its objectives and can exclude or otherwise regulate the access of others to that benefit. The ability to exclude or regulate the access of others to the benefits of an asset is an essential element of control that distinguishes an entity's assets from those public goods that all entities have access to and benefit from.

16 In relation to taxes, IPSAS 23 refers to the taxable event. Paragraph 65 of the Standard identifies what is the likely taxable event, unless specified otherwise in the laws or regulations. In particular, paragraph 65(e) it states that for property tax the taxable event is likely to be the passing of the date on which the tax is levied or the period for which the tax is levied, if the tax is levied on a periodic basis.

17 EFRAG Secretariat notes that the requirement in paragraph 65(e) may not provide a very clear answer on whether the recognition of the asset is immediate or progressive. It is possible that this issue is not considered critical to entities reporting under IPSAS because there is no interim reporting required.

18 European Accounting Rule 17 requires to recognise an asset arising from a non-exchange transaction when control is gained of resources that meet the definition of an asset and satisfy the recognition criteria, similar to IPSAS 23.Control of transferred resources is obtained either when the resources have been transferred to the EU, or the EU has an enforceable claim against the transferor. Like IPSAS 23, the ability to exclude or regulate the access of others to the benefits of an asset is an essential element of control that distinguishes an entity's assets from those public goods that all entities have access to and benefit from.

19 AASB 1004 also requires the recognition of an asset under similar conditions. When dealing to contributions of assets, an entity does not obtain control until it has met conditions or provided performance that makes it eligible to receive the contribution. AASB 1004 states that its requirement may result in an outcome different from the application of IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*.

20 The Standard specifies that in most cases income from taxes will be recognised in the reporting period in which the tax assessments are issued or the tax collections are received. When the transfers arise from a periodical charge, such as a land tax, the entity obtains control on the day it becomes entitled to levy the tax. This may suggest a point-in-time recognition pattern for certain taxes.

21 AASB 1004 prevents entities to recognise a right to future funding, until it has complied with the conditions that make it eligible to receive the funding. However, an entity would recognise cash from taxes, rates or other fines, irrespective of whether restrictions or conditions are imposed on the use of the contributions

22 AASB 1058 does not set specific recognition criteria for assets arising from transactions in scope. Rather, it refers to other Standards such as Leases, Intangible Assets and Property, Plant and Equipment.

23 GASB 33 dictates different recognition assets and revenue criteria for the classes of transactions identified under paragraph 10 above. However, no transaction should be recognised when it is not measurable or not probable of collection.

24 Under GASB 33, an asset should be recognised:

(a) For derived tax revenues, at the earlier moment of when resources are received or when the exchange transaction occurs;

(b) For imposed non-exchange transactions, at the earlier moment of when resources are received or when an enforceable legal claim arises. The Standard suggests that if the law specifies a date, this is the moment when the enforceable legal claim arises;

(c) For Government-mandated and voluntary non-exchange transactions, when all eligibility requirements have been fulfilled. Eligibility requirements include time requirements – the period over which the resources are required to be used; and contingencies, specified actions on which the provider's offer of resources is contingent on.

When does the entity recognise a liability and how should it be measured?

25 IPSAS 23 distinguishes between stipulations on the use of the asset that are conditions and those that are only restrictions. Stipulations that are conditions create an obligation to the entity which requires the recognition of a liability when:

(a) It is probable that an outflow of resources including future economic benefits or service potential will be required to settle the obligation; and

(b) The amount of the obligation can be measured reliably.

26 Restrictions do not create an obligation to return the asset if it is not deployed as specified and therefore do not require the recognition of a liability.

27 The measurement of the liability is independent from the measurement of the asset; therefore, an entity could still recognise revenue even if the contribution is subject to conditions.

28 European Accounting Rule 17 establishes the same distinction between conditions and restrictions and contains and provides for similar accounting. The amount recognised as a liability shall be the best estimate of the amount required to settle the present obligation at the reporting date

29 AASB 1004 specifies that when a local Government or other similar entity obtains control of a contribution, the existence of restrictions or conditions on the use of the funds does not give rise to a liability. This is because the fiduciary responsibility of the entity to pursue its objectives pertains to all assets and not specifically to the funds obtained,

30 AASB 1058 requires an entity to assess if the transaction has given rise to a liability under other relevant Standards, such as a contract liability, a lease liability, a provision or a financial liability. The measurement of the liabilities is independent of the measurement of the asset. With exception of the transactions described in the paragraph 29 below, an entity charges or credits profit or loss for the difference between:

(a) The difference between the fair value of the asset recognised and the consideration paid; and

(b) The carrying amount of any liability recognised under the relevant Standards.

31 One area of judgment is to identify whether the entity has a contract liability for an obligation to provide future goods or services, and if so, how to measure it. Failing to identify a contract liability would lead to overstating the income immediately recognised.

32 The relevant guidance is found in Appendix F *Australian Implementation Guidance for Not-for-Profit Enti*ties of AASB 15. The entity has a contract obligation to the extent that it has a sufficiently specific performance obligation, which requires, among other conditions, that the entity must be able to determine when the obligation is fully satisfied.

33 When a contribution is made for both the purpose of providing a donation and also in consideration for future goods or services, the entity need to use judgment to avoid allocating all the consideration to the performance obligation. The Standard refers to the discussion in the Basis for Conclusion in IFRS 15 about the fact that any stand-alone selling price estimated using the residual approach should be considered for appropriateness.

34 AASB 1058 has a specific requirement for transfers made to enable an entity to acquire or construct a non-financial asset for its own use. In this case, the entity is required to return the transfer if it does not acquire or construct the non-financial asset. The Standard requires the entity to recognise a liability for any excess of the amount in 25(a) over 25(b) above, with the liability representing the entity's obligation to acquire or construct the asset.

35 Under GASB 33, a liability is recognised if:

(a) For derived tax revenues, the entity has received the resources but the exchange transaction has not yet occurred;

(b) For imposed non-exchange transactions

(i) In the case of property taxes, if the entity has recognised an asset before the period for which the taxes are levied;

(ii) In the case of other taxes (that are not derived from transactions), when the entity recognises an asset but the law indicates time requirements - the period over which the resources are required to be used.

(c) For Government-mandated and voluntary non-exchange transactions, when an entity has recognised an asset but eligibility requirements have not been fulfilled.

36 The UK FRC Staff Education Note 12 requires the recognition of a liability when a transaction imposes future performance-related conditions and the resources are received before the conditions are met. However, the existence of restrictions does not require to recognise a liability, until as a result of a failure to meet the restriction repayment has become probable.

When and how does the entity recognise income?

37 Under IPSAS 23, income is recognised at the moment the asset is recognised, to the extent that the fair value of the asset exceeds the value of any recognised liability. Any liability recognised is released to profit or loss as the related condition is satisfied.

38 European Accounting Rule 17 similarly requires that income is recognised when an inflow of resources from a non-exchange transaction recognised as an asset except to the extent that a liability is also recognised in respect of the same inflow.

39 Under AASB 1004, assets and income are normally recognised at the same time.

40 Under AASB 1058, an entity recognises income:

(a) Either immediately on recognition of the asset, for any excess of its fair value over the carrying amounts of any liability recognised; or

(b) As it satisfies its obligation under a transfer made to enable the entity to acquire or construct a non-financial asset for its own use.

41 It should be pointed out that the Standard considers that part of a transfer may be in exchange for performance obligation arising from contracts with customers. In that case, the entity recognises that portion of the transfer as revenue in accordance with the Australian corresponding to IFRS 15 Revenue from Contracts with Customers.

42 Under GASB 33, income is recognised when:

(a) For derived tax revenues, the exchange transaction occurs;

(b) For imposed non-exchange transactions

(i) In the case of property taxes, in the period for which the taxes are levied, irrespective of the date when the legal claim arises or the payment is due;

(ii) In the case of other taxes (that are not derived from transactions), when the asset is recognised, unless the law indicates time requirements;

Critical matters

43 In the EFRAG Secretariat's view, the pronouncements highlight the following critical issues:

(a) There is an unavoidable degree of judgment to distinguish those cases where the entity gives and receives approximately the same value. If special requirements are introduced for these transactions, a risk of diverging application may arise;

(b) What is role played by conditions and restrictions on the use of transfers in:

(c) The timing of recognition of the assets; and

(d) The recognition of a liability.

Questions for EFRAG TEG

44 Do EFRAG TEG have questions or comments on the content of the analysis?