Think Ahead ACCA

Submission by the Association of Chartered Certified Accountants

30 October 2020

To: Ian Carruthers
Chair, IPSAS Board
227 Wellington Street West
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Submission via website

Dear Ian

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer relevant, first-choice qualifications to people around the world who seek a rewarding career in accountancy, finance and management.

ACCA supports its 227,000 members and over 544,000 future members in 176 countries, helping them to develop successful careers in accounting and business, with the skills required by employers. ACCA works through a network of 110 offices and centres and 7,571 Approved Employers worldwide, who provide high standards of employee learning and development.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. Through its public interest remit, ACCA promotes appropriate regulation of accounting and conducts relevant research to ensure accountancy continues to grow in reputation and influence.

ACCA has introduced major innovations to its flagship qualification to ensure its members and future members continue to be the most valued, up to date and sought-after accountancy professionals globally.

The expertise of our senior members and in-house technical experts allows ACCA to provide informed opinion on a range of financial, regulatory, public sector and business areas. Further information about ACCA's comments on the matters discussed here can be requested from:

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ACCA welcomes the opportunity to comment on the Exposure Drafts issued by IPSAS Board on *Revenue with Performance Obligation, Revenue without Performance Obligation, and Transfer Expenses*. The ACCA Public Sector Global Forum, staff experts and broader ACCA stakeholders have considered the matters raised and their views are represented in the following.

ACCA also contributed to the Accountancy Europe (AE) response on this consultation. The purpose of this response is to highlight clarifications and additional comments from ACCA regarding ED 70 to ED 72.

It is particularly worth noting that the concept of present obligation appears to be inconsistent between ED 71 and ED 72 (please see SMC1 from ED 71 and SMC6 from ED 72 for more information).

AREAS FOR SPECIFIC COMMENT:

ED 70 – Revenue with Performance Obligations

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?

We agree that the definition is clear and is essentially consistent with the definition of a contract in IFRS15 in referring to enforceable rights and obligations. It might be better to omit the first “both” in the definition since AG29 highlights that some binding arrangements may create only rights for the purchaser and no obligation to pay.

The considerable guidance on enforceability in the public sector in the Application Guidance section is very helpful.

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?

Yes, we agree.

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?*

While we do not disagree with the Application Guidance on splitting of revenue into elements with performance obligations and those without, it seems unnecessary in principles-based standards and could be removed. Instead, it might be better if under Step 1 it was recognised that a binding arrangement may include both elements and preparers are directed to ED71 where there is revenue with no performance obligations.

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?

Yes, retain these disclosures, but in many cases they might not be material or relevant.

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. 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?

In general, we support the additional disclosure requirements.

However, we note that the quantification of revenue foregone where there are implicit price concessions may not be practicable in many cases. In these cases, the disclosure of the existence of implicit price concessions, the parties involved and the government policy which requires the price concessions to be made may provide sufficiently useful information.

Transactions where there is an understanding from the outset that goods or services would not be paid for would fail the recognition test. As such, separate disclosure of any income that is still received, without performance obligation, would be right. We note further that in cases where goods and services are supplied at a loss, the onerous contract disclosures would apply.

ED 71 – Revenue without Performance Obligations

Specific Matter for Comment 1: (Paragraphs 14-21) 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?

The notion of present obligation in ED 71 seems unhelpful. In IFRS and the IPSASB Public Sector Conceptual Framework, 'present obligations' is used to define a liability that should be recognised in the accounts. By contrast, in ED 71, the term 'present obligations' is used to determine the recognition of revenue, in particular where there is a 'specified activity' or 'eligible expenditure.'

Another source of confusion lies in the wording of paragraph 14, which defines 'present obligation' as a 'binding obligation.' This would seem to contradict the definition in the IPSASB Conceptual Framework[1]. Further, it is unclear how this definition interacts with paragraph 47, which states: 'A present obligation is a duty to act or perform in a particular way and may give rise to a liability in respect of any transaction without a performance obligation.'

To avoid confusion, we would recommend a different term should be used, such as 'specified requirements.' In the context of ED 71, it would appear that the meaning contained in paragraph 47 is more relevant than that which is set out in paragraph 14.

The term 'present obligation' is also used in a different context in ED 72. Please refer to our SMC6 response in ED 72 for further reflections on present obligations.

S*pecific Matter for Comment 2: (Paragraph 31) The flowchart that follows paragraph 31 of this [draft] Standard illustrates the process a transfer recipient undertakes to determine whether revenue arises and, if so, the relevant paragraphs to apply for such revenue recognition. Do you agree that the flowchart clearly illustrates the process? If not, what clarification is necessary?*

Yes, we agree that the flowchart illustrates the process.

[1] IPSASB Conceptual Framework, paragraph 1.15: '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. Obligations are not present obligations unless they are binding and there is little or no realistic alternative to avoid an outflow of resources.' This definition is, in itself, contradictory.

Specific Matter for Comment 3: (Paragraph 57-58) The IPSASB decided that a transfer recipient recognizes revenue without performance obligations but with present obligations when (or as) the transfer recipient satisfies the present obligation. Do you agree that sufficient guidance exists in this [draft] Standard to determine when a present obligation is satisfied and when revenue should be recognized? For example, point in time or over time. If not, what further guidance is necessary to enhance clarity of the principle?

Yes, the level of detail in the guidance found in paras 57-58 is sufficient for principles-based standards. At the same time, ED 72 contains more guidance on determining whether revenue should be recognised over time or at a point in time. It would be of value to preparers if the same level of guidance was available in ED 71, or at least having the relevant guidance in ED 72 referenced in ED 71.

Specific Matter for Comment 4: (Paragraphs 80-81) The IPSASB decided that the objective when allocating the transaction price is for a transfer recipient to allocate the transaction price to each present obligation in the arrangement so that it depicts the amount to which the transfer recipient expects to be entitled in satisfying the present obligation. The amount of revenue recognized is a proportionate amount of the resource inflow recognized as an asset, based on the estimated percentage of the total enforceable obligations satisfied. Do you agree sufficient guidance exists in this [draft] Standard to identify and determine how to allocate the transaction price between different present obligations? If not, what further guidance is necessary to enhance clarity of the principle?

It is our view that the guidance in paras 80-81 is sufficient for a principles-based standard.

Specific Matter for Comment 5: (Paragraphs 84-85) Do you agree with the IPSASB's proposals that receivables within the scope of this [draft] Standard should be subsequently measured in accordance with the requirements of IPSAS 41, Financial Instruments? If not, how do you propose receivables be accounted for?

Yes, we agree.

Specific Matter for Comment 6: (Paragraphs 126-154) The disclosure requirements proposed by the IPSASB for revenue transactions without performance obligations are intended to provide users with information useful for decision making, and to demonstrate the accountability of the transfer recipient for the resources entrusted to it. Do you agree the disclosure requirements in this [draft] Standard provide users with sufficient, reliable and relevant information about revenue transactions without performance obligations? In particular, (i) what disclosures are relevant; (ii) what disclosures are not relevant; and (iii) what other disclosures, if any, should be required?

The proposed disclosure requirements are relevant for users.

Specific Matter for Comment 7: (Paragraphs N/A) Although much of the material in this [draft] Standard has been taken from IPSAS 23, Revenue from Non-Exchange Transactions (Taxes and Transfers), the IPSASB decided that the ED should establish broad principles for the recognition of revenue from transactions without performance obligations, and provide guidance on the application of those principles to the major sources of revenue for governments and other public sector entities. The way in which these broad principles and guidance have been set out in the ED are consistent with that of [draft] IPSAS [X] (ED 72), Transfer Expenses. Do you agree with the approach taken in the ED and that the structure and broad principles and guidance are logically set out? If not, what improvements can be made?

The decision to issue three separate EDs is appropriate. Equally, the EDs are comparatively lengthy, with interdependencies across the three, which could make it difficult for some preparers to follow the principles. To address this, summary guidance, covering the three standards, will be important to aid preparers in understanding the interrelation between ED 70 to ED 72.

There are potential issues arising from the transition from the current IPSAS of non-exchange transactions to these new standards.

ACCA Think Ahead

ED 72 – Transfer Expenses

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?

We agree that the scope of this standard is clear.

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?

We agree with the proposals in this draft to distinguish between revenue with and without performance obligations. However, we suggest that definitions for all key terms should be presented in this standard, instead of cross-referencing to other standards (ED 70 and ED 71). Any differences in the application of these terms between ED 72 and other standards should be explicitly identified. For example, unlike ED 70, the term 'performance obligations' in ED 72 does not cover the supply of goods and services to the transfer provider itself. This should be specified.

In particular, we note that the term 'present obligations' currently does not feature in the definitions section of any of the proposed standards. This is unhelpful because 'present obligations' is a core underlying concept. Noting our comments regarding the term in our response to ED 71 (SMC 1), we would recommend that the definition of 'present obligations' (and/or its alternative term) is defined separately in ED 70, ED 71 and ED 72.

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?

We agree that if the transfer provider cannot reasonably measure the transfer recipient's progress towards complete satisfaction of their performance obligation(s), then the transaction should be accounted for as a transfer expense without performance obligations.

However, we would recommend that the provisions of ED 72 are clarified. There is some inconsistency at present between:

- Paragraph 13(d), which states that transfer expenses should be accounted for in accordance with the Public Sector Performance Obligation Approach only if 'the transfer provider can identify the transfer recipient's performance obligations and monitors the satisfaction of those performance obligations throughout the duration of the binding arrangement'; and

- Paragraph 46, which states that 'Where the transfer provider expects to be able to measure the outcome of a transfer recipient's performance obligation at a later date, the transfer provider shall not recognize an expense until such time that it can reasonably measure the outcome of the transfer recipient's performance obligation.'

This inconsistency could lead not only to divergence in practice in terms of the classification of transfer expenses (as transfer expenses with or without performance obligations), but crucially, affects the timing of the recognition of the transfer expense. This is not helped by the provisions in paragraph 45, which requires the transfer provider, if they are unable to reasonably measure progress, to choose between two approaches the one that 'more faithfully represents the transfer provider's obligations to transfer resources to the transfer recipient.'

In our view, if the transfer provider cannot reasonably measure the transfer recipient's progress from the start of the binding arrangement, the transfer expense should be accounted for as one without performance obligations. This will ensure consistency in practice, and in particular prevent delays in the recognition of transfer expenses.

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?

We agree with the recognition and measurement requirements for transfer expenses with performance obligations.

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.

In general, we find that the guidance in IFRS 15 has been sufficient to deal with the issues arising from applying the recognition and measurement requirements for revenue with performance obligations. As ED 72 is aligned with IFRS, the guidance in the ED should be adequate, barring our comments to SMC 3 above.

Specific Matter for Comment 6: This [draft] Standard proposes the following recognition and measurement requirements for transfer expenses without performance obligations: (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 (b) A transfer provider should measure transfer expenses without performance obligations at the carrying amount of the resources given up? Do you agree with the recognition and measurement requirements for transfer expenses without performance obligations? If not, how would you recognize and measure transfer expenses without performance obligations?

We agree with the proposals.

However, the term 'present obligation' appears to be used in a different context than in ED 71. Within ED 72, the existence of a present obligation is not linked in any way to an obligation to perform a specified activity or incur an eligible expenditure. Instead, it is an obligation resulting in an outflow of resources, which an entity has little or no realistic alternative to avoid (see paragraph 14 of ED 71). We would suggest that the term 'present obligation' is separately defined in ED 72 consistently with the IPSASB Conceptual Framework, and that a different term is used to denote the existence of a specified activity and eligible expenditure in ED 71.

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?

We agree that this lack of symmetry is appropriate.

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?

Yes, liabilities should be recognised where there is a binding arrangement, even if this precedes the appropriation being authorised.

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?

While we agree, in principle, that disclosure requirements should mirror the requirements in ED 70 and ED 71, model disclosures from the IPSASB would allow us to better evaluate the practical impact that this is likely to have on preparers. Further outreach may also be needed to gain greater clarity on the reporting burden arising from the disclosures, particularly in the transition period.