BRITISH COLUMBIA

November 1, 2020

396537

John Stanford
Technical Director
International Public Sector Accounting Standards Board
277 Wellington St. West
Toronto, ON M5V 3H2
E-mail: johnstanford@ipsasb.org

Dear John Stanford:

**RE: <u>Exposure Draft 72: Transfer Expenses</u>**

Thank you for the opportunity to provide comments on the exposure draft; *Transfer Expenses*. The views expressed in this letter reflect the views of the Government of the Province of British Columbia, including central agencies, ministries and entities consolidated into the British Columbia Summary Financial Statements. The Summary Financial Statements of the Province are prepared in accordance with Canadian Public Sector Accounting Board (PSAB) standards. We have an interest in the development of International Public Sector Accounting Standards Board's (IPSASB) guidance as it may influence future PSAB standards.

***Comment Period Extension***

Even with a large team of experienced accounting professionals, we found it difficult to review all the material provided in the time allowed, particularly when combined with Exposure Drafts 70 and 71 and the effects of the global COVID-19 pandemic. While we appreciate the original due date extension from September 15, 2020 to November 1, 2020, we are concerned that many stakeholders will not have the resources to adequately review these complex and lengthy documents within the current requested response date. We recommend that an additional extension to the comment period be provided.

…/2

***Alignment with IFRS***

We recognize IPSASB's goal to provide standards that are aligned with International Financial Reporting Standards (IFRS). The objectives of for-profit entities do not align with taxpayer-supported public sector entities and their focus on service delivery. We are concerned that IPSASB's approach does not adequately consider the interests or needs of the public with regards to the impacts of non-exchange transactions.

The proposed views do not consider a government's legislated financial framework, which includes preparing a budget and communicating a government's accountability for actual results against that budget on a line by line basis through the financial statements. It can be difficult to directly compare asset/liability focused financial statements with revenue/expense focused budgets.

***Expense Recognition***

The exposure draft introduces the Public Sector Performance Obligation Approach (PSPOA) for transfers with performance obligations. The PSPOA requires the transferring government to recognize an asset first and the expense is recognized after monitoring activities confirm the transfer recipient satisfied the performance obligation. This approach may result in significant timing delays between the time a decision is made by the transfer provider and the time a recipient fulfills its obligation.

In addition, the PSPOA presents practical difficulties for budgeting purposes, expense forecasting and will increase administrative effort to facilitate monitoring activities. Transfer providers may choose to avoid monitoring activities in order to have more control over timing of expense recognition or to reduce risk due to cut-off issues at year-end. This pressure to modify the agreement in a legislated balanced budget framework is amplified in order to achieve certainty over the timing of expense recognition.

Canadian public sector accounting standards distinguish when a government transfer should be expensed by looking at eligibility requirements of the recipient and authorization of the transfer. These qualities focus on when discretion is lost, and the transfer provider must carry on with the transfer. The timing of the expense is not dependent on when the transfer occurs or when the performance obligations have been completed by the recipient. This accounting treatment primarily results in the transfer provider recognizing the expense in the same period their obligation to the transfer recipient can be enforced.

One of the primary purposes of the Summary Financial Statements in Canada is to provide accountability to the public. Presenting expenses in the period when the decisions are made and become enforceable by the transfer recipient, will help hold the government entity responsible for making the decision to proceed with the transfer.

…/3

***Symmetrical Accounting***

In our view, the Public Sector Performance Obligation Approach (PSPOA) places emphasis on symmetrical accounting specifically for transfers involving performance obligations. In Canada, symmetrical accounting by the parties to a transaction is not part of our conceptual framework. In some cases, when it reflects the substance of the transaction for all parties to a transfer, symmetrical accounting will result. In others, the evidence available to support recognition or the ability to estimate the transfer may vary between the transferor and recipient and symmetrical accounting will not occur. [1]

***Assets***

The standard requires transfer providers to record a 'transfer provider's binding arrangement asset' when performance obligations exist in a binding arrangement. It is our view that funds transferred to a recipient do not meet the definition of an asset because the resources are no longer directly controlled by the entity and the transfer provider does not expect to receive direct future economic benefits or service potential from the asset.

Based on our previous experience, we do not recognize this as a viable approach for public sector entities. Prior to full compliance with generally accepted accounting principles in 2004, the Province presented "prepaid capital advances" on the Statement of Financial Position. The prepaid capital advances represented amounts paid to school districts, health authorities, etc. to acquire capital assets (e.g. buildings). These advances were not expensed in the year they were issued but were treated as a prepaid expense and amortized over the life of the tangible capital asset acquired with the advances. This historic asset category is similar to the properties associated with the proposed "transfer provider's binding arrangement asset".

The past approach led to practical difficulties in verifying the existence of the asset(s) on an annual basis because government did not have direct control of the asset. There were also difficulties with confirming the accurate valuation of the asset(s) at year-end. The carry-forward balance quickly became detached from the original assets they represented and annual adjustments were required to account for unknown transactions (e.g. disposals/write-downs). We recognize a transfer provider's rights to enforce a binding arrangement; however, there is an expectation that the transfer recipient will satisfy the obligation. If a transfer recipient fails to complete a performance obligation, a receivable shall be recorded in the future period when that event occurs.

We recommend the Board consider placing greater emphasis on which entity controls an asset and when an entity loses discretion in an arrangement when providing principles for expense recognition related to non-exchange transactions.

[1] Public Sector Accounting Standards paragraph 3410.09

***Disclosures***

We agree that users of financial statements should understand the nature, amount, timing and uncertainty of revenue and cash flows. However, in some instances the level of detail proposed in the exposure draft may be too specific and onerous to collect for summary level financial statements. We caution against excessive detail in government summary financial statements, which are intended for the broad use of the legislature and the public.

Responses to specific questions posed in the exposure draft are attached. Should IPSAB have any comments or questions, please contact me at: 250-387-6692 or via e-mail: Carl.Fischer@gov.bc.ca, or Diane Lianga, Executive Director, Financial Reporting and Advisory Services Branch, at 778-698-5428 or by e-mail: Diane.Lianga@gov.bc.ca.

On behalf of the Government of British Columbia,

Sincerely,

Carl Fischer, CPA, CGA
Comptroller General
Province of British Columbia

Encl.

cc: Michael Pickup, FCPA, FCA
Auditor General
Province of British Columbia

Diane Lianga, Executive Director
Financial Reporting and Advisory Services
Office of the Comptroller General

**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?**

Yes, the scope of the 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?**

No, we do not agree with the distinction for transfer expenses. It is our view that there should be no distinction between transfer expenses with performance obligations and transfer expenses without performance obligations.

The current distinction, as proposed in the exposure draft, may result in a "transfer provider's binding arrangement asset". In our view, the entity has little to no control over the asset because the transfer recipient has been delegated with the task(s) of delivering on the performance obligations. The transferring government has little control (if any) over how or when the transfer recipient satisfies the performance obligation. In addition, the future economic benefits or service potential of these assets are not expected to flow to the entity and as such, we argue that a "transfer provider's binding arrangement asset" does not meet the definition of an asset.

The current distinction places an emphasis on symmetrical accounting between the transfer provider and the transfer recipient. Symmetrical accounting by the parties to a transaction is not a fundamental principle of accounting theory. Requiring symmetrical accounting may lead to poor financial management if the transfer provider wants to avoid delays in expense recognition to stay within budget for the year, or, if there are issues with monitoring administration.

A transfer expense should be recognized by the transfer provider as an expense in the period the transfer is authorized, and the transfer provider loses discretion over avoiding the settlement of the liability. If it becomes apparent that the recipient does not satisfy performance obligations, a receivable can be set up for the return of funds.

…/6

**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 disagree with this proposal. The decision whether a transfer provider monitors a transfer recipient's performance obligations should not impact the timing of expense recognition of the transfer expense. This requirement could lead to situation where a transfer provider may choose to not monitor a transfer recipient's progress in order to have more control over timing of expense recognition. This could lead to poor financial management.

**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 do not agree with the recognition and measurement requirements for transfer expenses with performance obligations.

a) In our view, the entity has little to no control over the transfer provider's binding arrangement asset ("the asset") because the transfer recipient has been delegated with the task(s) of delivering on the performance obligations. The transferring government has little control (if any) over how or when the transfer recipient satisfies the performance obligation. In addition, the future economic benefits or service potential of these assets are not expected to flow to the entity and as such, we argue that a "transfer provider's binding arrangement asset" does not meet the definition of an asset.
b) We believe the PSPOA approach, with the requirement to monitor progress, makes it difficult to forecast expenses. The approach requires a significant effort to monitor transactions of a separate entity within a timely manner in order to match expense

recognition with the satisfaction of performance obligation. This results in issues with cut-off, completeness and existence of assets and expenses from the perspective of the transfer provider.

We propose transfer expenses should be recognized when eligibility criteria have been satisfied and the transferor has lost discretion over avoiding the obligation. If it becomes apparent that the recipient does not satisfy performance obligations, a receivable can be set up for the return of funds.

**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.**

We believe that there will be significant practical difficulties with applying the PSPOA. The separation of components within a binding arrangement that meet the criteria under PSPOA, and those that do not, is a reasonable concept. However, this could be quite complex for some binding arrangements.

The procedures involved with monitoring activities include the transfer recipient preparing reports after performance obligations have been satisfied. The reports are then provided to the transfer provider. Review of the external reports are likely performed by individuals in direct contact with the transfer recipients and not necessarily accountants responsible for financial statement preparation. This results in significant time delays that may impact the timing of expense recognition to when performance obligations were satisfied.

We suggest that IPSAS move away from these requirements and focus on loss of discretion to avoid the transfer and the ability to measure transfer expenses.

**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?**

Yes, we agree. The recognition and measurement requirements for transfer expenses without performance obligations is reasonable.

We recommend expanding the recognition requirements to include when the transfer provider has lost discretion to avoid the transfer.

**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?**

Yes, we agree. The requirements for symmetrical accounting between unrelated entities is not practical or appropriate. It is also not an objective of the IPSAS Conceptual Framework.

**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, we agree that consideration should be given to whether a present obligation exists.

This alternative could include recognizing the expense if communication and commitment to pay leaves little discretion, even if still subject to appropriation, such as in a multi-year agreement.

Our government has different levels of approvals and appropriation requirements. Loss of discretion in avoiding transfer should be the focus and whether the transfer recipient can reasonably expect the transfer.

**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?**

**a)** No, we do not think additional disclosure requirements should be added. The current disclosure requirements are very detailed. We feel there are too many mandatory disclosures that may not be appropriate for a large government entity reporting in summary financial statements.
**b)** Disclosures that may be unnecessary for summary financial statements:
  - Paragraph 139 – transaction consideration allocated to the transfer recipient's remaining performance obligations. This includes amount allocated to the unsatisfied performance obligations and when they expect to recognize an expense for these amounts.
  - Paragraph 146 – transfer expenses without performance obligations. This includes reconciliation of opening and closing balances of payables from binding arrangements.
  - Paragraphs 135 – 137 – Binding arrangement balances. Includes disclosure of opening and closing balances of binding arrangement assets for transfer expenses with performance obligations, expenses recognized from beginning balances, and from previous periods. Explanations of how timing of recipient's satisfaction of performance obligations impacts timing of payments and transfer provider asset and liability balances. Explanation of changes to the transfer provider asset and liability balances during the year.

In general, disclosures compared to Canadian public sector standards for government transfers are lengthy. Some disclosures may be more appropriate in management discussion and analysis reports rather than the notes to the summary financial statements.

…/10

**Other Comments**

- Paragraph 62(a) – clarify if ‘transfer provider’ should be replaced with ‘transfer recipient’.
- Paragraph 111 – should reference to paragraph 110 be a reference to paragraph 109?
- Paragraph 111 – change the word ‘or’ to ‘of’ in the phrase “promised transfer or resources”.
- Paragraph 154 – the adoption date is not specified.