

Agenda Item 9: Revenue

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Session Outline

Agenda Item 9

- Proposed Scope.
- Proposed Definitions.
- Identifying the Binding Arrangement with a Purchaser.
- Other Outstanding Items.
- Project Management Proposal – Developing Illustrative Examples

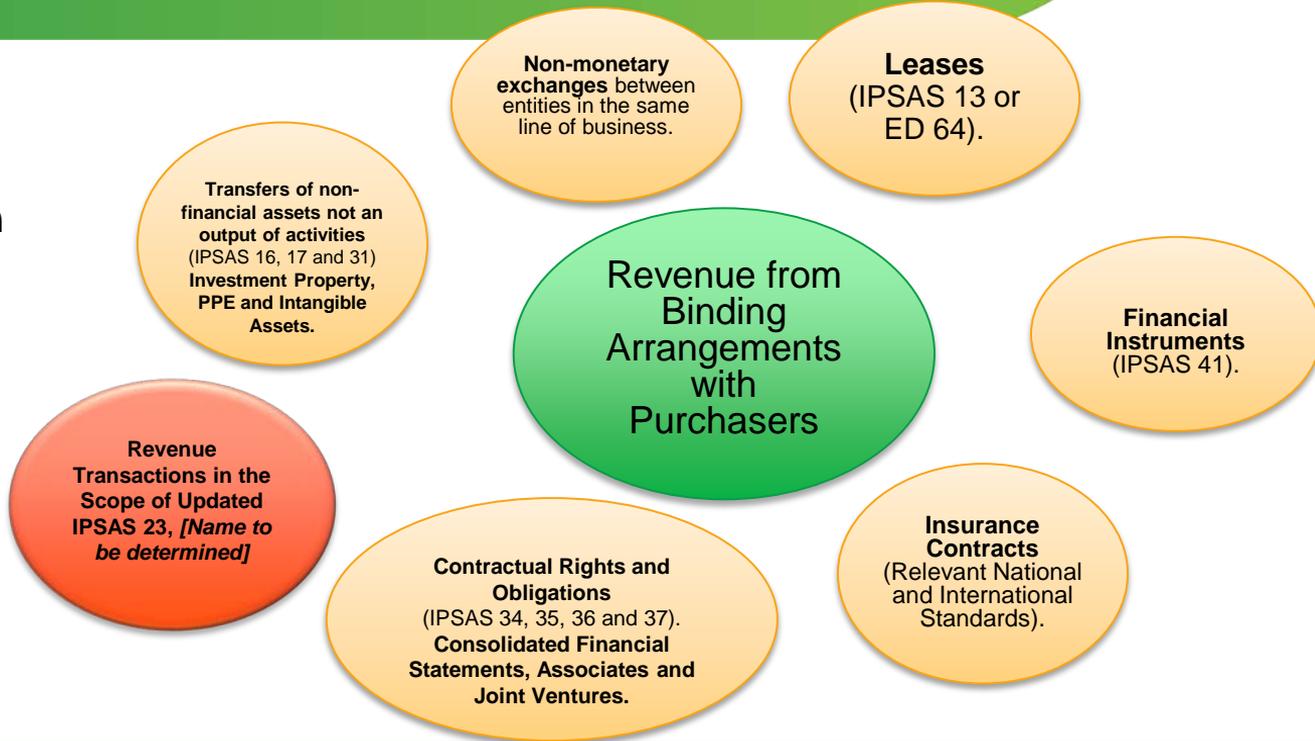
Approved Scope and Scope exclusions at the December 2018 meeting (Agenda Item 9.2.1)

Scope

Scope exclusions

Additional Scope exclusion proposed

- Consistent with IPSAS 9, *Revenue from Exchange Transactions*.
- IPSAS 9 **excludes** non-exchange revenue transactions from its scope as there are addressed in IPSAS 23.



Non monetary Exchanges – Appropriateness of Example (Agenda Item 9.2.1)

Scope exclusion: Non-monetary exchanges

- Some jurisdictions mentioned that the examples used for non-monetary exchanges **are not suitable for the public sector.**
- IFRS 15** refers to non-monetary exchanges of **Oil.**
- IPSAS 9** refers to non-monetary exchanges of **Oil** and **Milk.**
- Staff propose the following examples:

Non monetary Exchanges – Appropriateness of Example (Agenda Item 9.2.1)

| Example | Description of Example | Reason for selecting Example |
|---------|---|--|
| 1. | Government department trades a parcel of land in an industrial area to a private corporation for a different parcel of land of similar value that the government will use as a national park. | Aligned to the GFS. |
| 2. | Nations trade strategic natural resources for another kind of product or service of similar value. | Aligned to the GFS. |
| 3. | Government entities agree to an exchange of commodities to fulfil demand. | Aligned to IFRS - Commodities are general. Incorporates Oil, Milk, and Other products. |
| 4. | Government entities agree to an exchange of electricity to fulfil demand. | Similar to Examples used in IPSAS 41, <i>Financial Instruments</i> . |

Proposed Scope (Agenda Item 9.2.1) - Decisions

1. Does the IPSASB agree with the additional scope exclusion?

2. Does the IPSASB agree to replace the example of non- monetary exchanges?

Proposed Definitions (Binding Arrangements) (Agenda Item 9.2.2)

| Term | Definition |
|--------------------------------|---|
| Binding Arrangement. | A <u>binding arrangement</u> is an arrangement that confers enforceable rights and obligations on the parties to the arrangement. A binding arrangement includes <u>contract</u> . |
| Contract. | A <u>contract</u> is an agreement between two or more parties that creates enforceable rights and obligations. |
| Binding Arrangement Asset. | A <u>binding arrangement asset</u> is an entity's right to consideration in exchange for goods or services that the entity has transferred to a purchaser when that right is conditioned on something other than the passage of time (for example, the entity's future performance). A binding arrangement asset includes a <u>contract asset</u> . |
| Binding Arrangement Liability. | A <u>binding arrangement liability</u> is an entity's obligation to transfer goods or services to a purchaser for which the entity has received consideration (or the amount is due) from the purchaser. A binding arrangement liability includes a <u>contract liability</u> . |

Application Guidance - Binding Arrangements (Agenda Item 9.2.2)

Binding Arrangements

AG6. [draft] IPSAS [X] (ED XX) is underpinned by the definition of binding arrangements, as rights and obligations are enforceable by legal or equivalent means. There are jurisdictions where government and public sector entities cannot enter into legal obligations, because they are not permitted to contract in their own name, but where there are alternative processes with equivalent effect.

AG7. An entity considers the substance rather than the legal form of an arrangement in determining whether it is a binding arrangement for purposes of this [draft] IPSAS [X] (ED XX). Binding arrangements, for the purposes of this [draft] IPSAS [X] (ED XX), are generally evidenced by the following (although this may differ from jurisdiction to jurisdiction):

- (a) The terms of the binding arrangement create rights and obligations for the parties;**
- (b) The remedy for non-performance may be enforceable by law or other mechanisms; and**
- (c) The arrangements may arise from contracts or through other legal means, such as statutory mechanisms.**

Basis for Conclusion - Binding Arrangements (Agenda Item 9.2.2)

Binding Arrangements

Binding Arrangements

BC6. The IPSASB replaced all references to “contractual arrangements” in IFRS 15 with references to the term “binding arrangements”. This change acknowledges that in some jurisdictions, entities may not have the power to enter into contracts but nevertheless may have the authority to enter into binding arrangements. In addition, the IPSASB agreed that binding arrangements, for the purpose of this Standard, should encompass rights that arise from legislative or executive authority.

Binding Arrangement Asset and Binding Arrangement Liability

BC7. The IPSASB replaced all references to “contract asset” and “contract liability”, in IFRS 15, with references to the term “binding arrangement asset” and “binding arrangement liability”, respectively. This change acknowledges that in some jurisdictions, entities applying IPSAS may not have the power to enter into contracts but nevertheless may have the authority to enter into binding arrangements.

Proposed Definitions (Purchaser) (Agenda Item 9.2.2)

| Term | Definition |
|------------|--|
| Purchaser. | A <u>purchaser</u> is a party that acquires goods or services that are an output of an entity under a binding arrangement. A purchaser includes <u>customer</u> . |
| Customer. | A <u>customer</u> is a party that has contracted with an entity to obtain goods or services that are an output of the entity's activities in exchange for consideration. |

Application Guidance - Purchaser (Agenda Item 9.2.2)

Purchaser

AG19. For public sector specific transactions the **purchaser is the party that pays consideration for the goods and services agreed to within a binding arrangement, but is not necessarily the party that receives those goods and services.** The delivery of public services **often involves three parties.** In these three-party (tripartite) arrangements, the purchaser has a binding arrangement with and pays consideration to the entity to deliver public services to a third-party beneficiary. **For example, if a central government provides funding to a regional health department to conduct bone density screening for citizens over 55, the central government is the purchaser and the citizens are the beneficiary of the service.** The purchaser can also enforce delivery of those goods and services or seek recourse if the promises in the binding arrangement were not be fulfilled.

Basis for Conclusion - Purchaser (Agenda Item 9.2.2)

Purchaser

BC8. The IPSASB **acknowledged that, the term, “customer”, may not always suit the public sector and considered the appropriateness of terms**, such as, “another party, buyer, commissioner, commissioning body, contractor, counterparty, payee, payer, resource provider, other party and purchaser”.

BC9. The IPSASB **replaced the term, “customer” with the term, “purchaser”**, because the term is widespread in the IPSAS literature and is more suited for the public sector.

Proposed Definitions (Agenda Item 9.2.2) - Decisions

1. Does the IPSASB agree with the definitions of binding arrangement, binding arrangement asset, binding arrangement liability, contract and purchaser?
2. Does the IPSASB agree whether the definitions of binding arrangement and purchaser incorporates contract and customer respectively?
3. Does the IPSASB agree whether the binding arrangement asset and binding arrangement liability incorporates contract asset and contract liability respectively?
4. Does the IPSASB agree with the explanatory text in the Application Guidance and Bases for Conclusions.

Identifying the Binding Arrangement (Agenda Item 9.2.3)

Paragraph 10a – 10e of [draft] Exposure Draft (ED) - Revenue recognition model is applied when all the following criteria are met:

- 10 (a). The parties have approved the binding arrangement and are committed to perform their respective obligations.
- 10 (b). The entity can identify each party's rights regarding the goods or services to be transferred.
- 10 (c). The entity can identify the payment terms for the goods or services to be transferred
- 10 (d). The binding arrangement has economic substance.
- 10 (e). It is probable that the entity will collect the consideration to which it will be entitled.

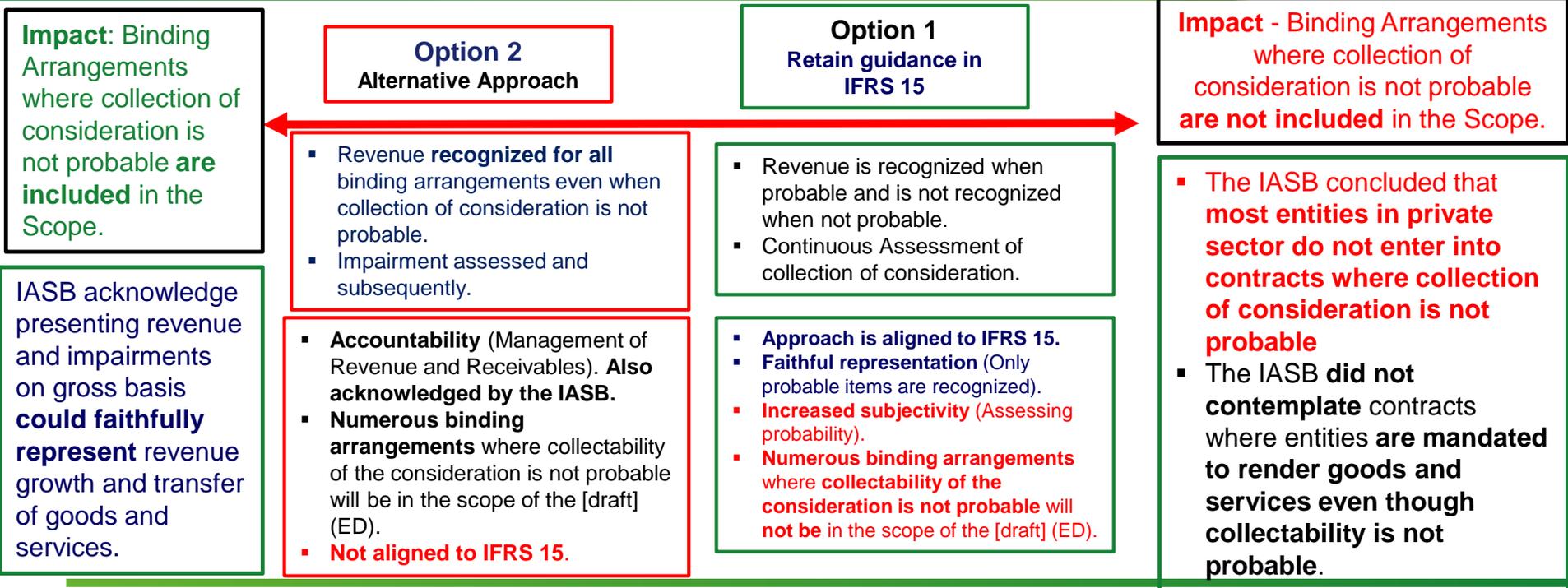
- **The IPSASB agreed to retain the revenue recognition criteria in IFRS 15 at the December 2018 meeting.**
- **The IPSASB also acknowledged that paragraph 10 (e) of the revenue recognition criteria may not be suitable for certain binding arrangements in the Public sector.**

Identifying the Binding Arrangement Continued (Agenda Item 9.2.3)

Implications of the Probability Criterion in Paragraph 10 (e)

1. **The criterion acts as a Collectability Threshold** - Assess the Purchaser's ability and intention of the purchaser to pay the consideration. (Purchaser's Credit Risk).
2. If collection of consideration IS NOT PROBABLE = Not in the Scope of [draft] (ED). **No recognition – Continuous Assessment, Revenue recognized when cash is received.**
3. If collection of consideration IS PROBABLE = **In the Scope of [draft] (ED).**
4. **Private sector entities generally enter into Contracts which are probable to collect payment.** Small Population of Contracts expected to fail to meet the Probability Criterion.
5. **Public sector entities may have numerous contracts where collectability of consideration is not probable but are legislated to provide the goods and services. Does that mean that such binding arrangements are not in the scope of [draft] (ED)?**

Identifying the Binding Arrangement Continued (Agenda Item 9.2.3)



Identifying the Binding Arrangement (Agenda Item 9.2.3) - Decision

1. Does the IPSASB agree with the approach to account for binding arrangements when it is not probable that an entity will collect the consideration to which it will be entitled?

Other Outstanding Items - (Agenda Item 9.2.4)

Location of
Revenue
Definitions

Consequential
Amendments
– *Leases*

Terminology
Changes

Other Outstanding Items – Location of Revenue Definitions (Agenda Item 9.2.4)

- Revenue definitions are located in IPSAS 1 and [draft] (ED).
- IASB definition of Revenue is only located in IFRS 15.
- Staff prefer to include the location of revenue definition in both IPSAS 1 and the [draft] (ED).
- There is a need for consistency with location of the expenses definition.

Other Outstanding Items – Terminology Changes (Agenda Item 9.2.4)

| IFRS 15 | Proposed IPSAS Terminology |
|-------------------------------|--|
| Customary business practices. | <u>Entity's customary practices</u> Consistent with Other IPSASs (IPSAS 40, <i>Public Sector Combinations</i>). |
| Industry. | <u>Sector</u> . Consistent with Other IPSASs (IPSAS 40, <i>Public Sector Combinations</i>). |
| Commercial objective | <u>Economic Objective</u> . The term, 'economic' incorporates both the objectives of profit making and service delivery whilst the term, 'commercial', is for profit making . |

Other Outstanding Items – Consequential Amendments, *Leases* (Agenda Item 9.2.4)

- ❑ IFRS 15, was issued in May 2014. IFRS 16, *Leases* was issued in January 2016 and replaced IAS 17, *Leases*.
- ❑ IFRS 15 was amended when IFRS 16 was issued - The Scope, Treatment of costs incurred to fulfil a contract and Repurchase agreements were amended in IFRS 15 due to IFRS 16 being issued.
- ❑ The IPSASB has a project in place, Exposure Draft (ED) 64, *Leases* to replace IPSAS 13, *Leases*.
- ❑ The [draft] (ED) is based on IFRS 15, staff amended certain paragraphs in the [draft] (ED) to align to IPSAS 13 requirements. The amended paragraphs are in the next slide.

Other Outstanding Items – Consequential Amendments – Leases Continued (Agenda Item 9.2.4)

Proposed Amendments to the [draft] (ED)

Scope

5. An entity shall apply this [draft] Standard to all binding arrangements with purchasers, except the following:

- (a) Lease contracts within the scope of ~~IFRS 16~~, IPSAS 13, Leases;
- (b) ...

Binding Arrangement Costs

...

98. Costs that relate directly to a binding arrangement (or a specific anticipated binding arrangement) include any of the following:

- (a) ...;
- (c) Allocations of costs that relate directly to the binding arrangement or to activities in the binding arrangement (for example, costs of management and supervision incurred as a result of the binding arrangement, insurance and depreciation of tools and equipment ~~and right of use assets~~ used in fulfilling the binding arrangement);
- (d) ...

Other Outstanding Items – Consequential Amendments – Leases Continued (Agenda Item 9.2.4)

Proposed Amendments to the [draft] (ED)

Application Guidance

...

Repurchase Agreements

...

A Forward or a Call Option

AG100. If an entity has an obligation or a right to repurchase the asset (a forward or a call option), a purchaser does not obtain control of the asset because the purchaser is limited in its ability to direct the use of, and obtain substantially all of the remaining benefits or service potential from, the asset even though the purchaser may have physical possession of the asset. Consequently, the entity shall account for the binding arrangement as either of the following:

- (a) A lease in accordance with ~~IFRS 16~~ IPSAS 13, Leases if the entity can or must repurchase the asset for an amount that is less than the original selling price of the asset ~~unless the binding arrangement is part of a sale and leaseback transaction. If the binding arrangement is part of a sale and leaseback transaction, the entity shall continue to recognize the asset and shall recognize a financial liability for any consideration received from the purchaser. The entity shall account for the financial liability in accordance with IPSAS 41, *Financial Instruments*; or~~

Other Outstanding Items – Consequential Amendments – Leases Continued (Agenda Item 9.2.4)

Proposed Amendments to the [draft] (ED)

A Put Option

AG104. If an entity has an obligation to repurchase the asset at the purchaser's request (a put option) at a price that is lower than the original selling price of the asset, the entity shall consider at the inception of the binding arrangement whether the purchaser has a significant economic incentive to exercise that right. The purchaser's exercising of that right results in the purchaser effectively paying the entity consideration for the right to use a specified asset for a period of time. Therefore, if the purchaser has a significant economic incentive to exercise that right, the entity shall account for the agreement as a lease in accordance with ~~IFRS 16~~ IPSAS 13. ~~unless the binding arrangement is part of a sale and leaseback transaction. If the binding arrangement is part of a sale and leaseback transaction, the entity shall continue to recognize the asset and shall recognize a financial liability for any consideration received from the purchaser. The entity shall account for the financial liability in accordance with IPSAS 41.~~

Consequential Amendments (Agenda Item 9.2.4) - Decisions

1. Does the IPSASB agree on the location of the revenue definition?
2. Does the IPSASB agree on the proposed terminology changes?
3. Does the IPSASB agree on the consequential amendments as a result of applying IPSAS 13 and not IFRS 16?

Process for Developing Illustrative Examples (Agenda Item 9.2.5)

Step 1 - Incorporate IASB Guidance

- Evaluate each IFRS 15 example to determine if it should be included in the [draft] (ED).

Step 2 - Incorporate IPSASB Guidance

- Include appropriate IPSAS 9 examples and align them with the [draft] (ED).

Step 3 – Develop specific examples as directed by the IPSASB

- Develop public sector specific examples as identified by the IPSASB.

Step 4 - Task Force review staff developed examples

- See next slide for the Proposed Task Force Plan.

Proposed Task Force Plan (Agenda Item 9.2.5)

March 2019 - Teleconference

- After the IPSASB meeting, Task Force discuss the plan for the approach on the Illustrative Examples.

April 2019 - Teleconference

- Review the Illustrative Examples in IFRS 15 and discuss the changes and updates to the terminology.

Mid-May 2019 – Teleconference

- Development of the Illustrative Examples. Finalize the Illustrative Examples.

June 2019 - Teleconference

- Approval of Illustrative Examples and report back at the June 2019 meeting.

Process for Developing Illustrative Examples (Agenda Item 9.2.5) - Decisions

1. Does the IPSASB agree on the staff proposal for the process to prepare Illustrative Examples?

2. Does the IPSASB agree on the proposed Task Force Plan on working on the Illustrative Examples?



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