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| <b>Project:</b>    | <b>Accounting for revenue from licences issued by not-for-profit public sector entities</b>   | <b>Meeting</b>           | AASB August 2017 (M159) |
| <b>Topic:</b>      | <b>What are licences?</b>   | <b>Agenda Item:</b>      | 5.1                     |
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|                    |   | <b>Decision-Making:</b>  | High                    |
|                    |   | <b>Project Status:</b>   | Preliminary research    |

## Introduction and objective of this paper

- 1 Staff plan to explore the issues relating to the accounting for revenue from licences issued by not-for-profit (NFP) public sector entities through a series of papers. The objective is to help facilitate Board decisions as to whether the principles in AASB 15 *Revenue from Contracts with Customers* could provide an appropriate basis for the accounting for revenue from any licences that are outside, or unclear whether they are within, the scope of current Australian Accounting Standards (including AASB 15).
- 2 Staff intend to seek Board input through the following papers:
  - (a) Paper 1 (this paper): Clarification of scope: The nature of licence arrangements (whether contractual or non-contractual, intellectual property (IP) or non-IP, referred to as licences or permits) as distinct from other arrangements (such as taxes), to help identify the scope of this project (the subject of this agenda paper 5.1. It is necessary to distinguish taxes from licence arrangements, as income from taxes are accounted for in accordance with AASB 1058 *Income of Not-for-Profit Entities* whereas revenue from licences are accounted for in accordance with AASB 15 or other standards where relevant;
  - (b) Paper 2: Clarification of the accounting standards ‘gap’: Further clarification of the nature of licence arrangements within the scope of current AASBs and therefore outside the scope of this project, to help identify the exact nature of the accounting standards ‘gap’ (building on the work of the June 2017 Agenda Paper 8.1). Paper 2 also throws light on whether the principles in AASB 15 could (and should) be extrapolated to

appropriately reflect the economic substance of transactions in accounting for revenue from licences issued under statute and other licences issued by NFP public sector entities not within the scope of current AASBs (the subject of agenda paper 5.2<sup>1</sup>; and

- (c) Paper 3: Clarification of the application of AASB 15: Testing the principles in AASB 15 that appear to be most suitable for licences within the scope of this project against particular types of licences found in practice that are considered to be currently outside (or it is unclear whether they are within) the scope of current AASBs (intended to be presented at the October 2017 Board meeting).<sup>2</sup>

3 The remainder of this paper is structured as follows:

- (a) Summary of staff recommendations (paragraph 4);
- (b) Background and past Board considerations (paragraphs 5-7);
- (c) Results of staff research, principally regarding distinguishing licences and taxes (paragraph 8);
- (d) Appendix A: Supporting staff analysis (paragraphs A1-A28); and
- (e) Appendix B: Extracts from the ABS GFS Manual (for information only).

### **Summary of staff recommendations**

4 Staff recommend:

- (a) The distinguishing features of licences from other arrangements, particularly taxes should be clearly identified. The distinguishing features would be important in identifying arrangements that are licences within the scope of AASB 15, AASB 16 or other relevant standards; and those falling in the accounting standards ‘gap’ to be addressed within the scope of this project. Therefore, in identifying the features of a ‘licence’ for the purpose of this project, the definition of ‘taxes’ in AASB 1058 is used as a starting point in differentiating licences from taxes as the accounting outcomes between licences and taxes may be different.
- (b) The table below, in the first column, sets out the characteristics that are useful in identifying a licence and illustrates how the characteristics could

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1 It is conceivable that, after analysis, the AASB will conclude that all licences within the scope of this project are within the scope of current AASBs. However, despite this, the AASB might conclude that further implementation guidance is needed for particular kinds of licences issued by NFP public sector entities.

2 As AASB 15 and AASB 1058 *Income of Not-for-Profit Entities* are effective from 1 January 2019, the aim is to issue any amendments to AASBs (in particular, AASB 15) necessary to address the accounting for revenue from licences issued by NFP public sector entities to be available for adoption by this time.

distinguish between a licence and a tax (as defined in AASB 1058) and identifies the research source of each feature:

| Characteristic  | Licence   | Tax  |
|---|---|--|
| (a) Is the arrangement discretionary rather than compulsory (based on AASB 1058 definition of 'taxes')?   | Discretionary   | Compulsory                                     |
| (b) What is the primary purpose of establishment (based on AASB 1058 definition of 'taxes')?  | Non-financial purpose (e.g. equitable allocation of a public resource)    | Generating income for the public sector entity |
| (c) Does the arrangement create rights of a payer and, depending on the type of arrangement, obligations of a payee (based on AASB 16 <i>Leases</i> , AASB 1059 <i>Service Concession Arrangements: Grantors</i> )?   | Creates rights of a licensee, and could create obligations for a licensor | No   |
| (d) Does the arrangement give the payer specific permission that must be obtained prior to performing an activity or using or accessing an asset of the payee that would otherwise be unlawful (based on dictionary definitions and other common licence attributes)? | Yes   | No   |
| (e) Does the arrangement transfer control of a payee's underlying asset (based on common law principles)  | No  | Not relevant                                   |
| (f) Does the arrangement convey to the payer a right to use or access an asset of the payee or a right to perform an activity (based on AASB 15 and dictionary definitions)   | Yes   | No   |

- (c) The identified features of a licence should not be included in AASBs. Indeed, consistent with the AASB's approach to IFRS adoption and transaction neutrality, it may not be appropriate to include such features in AASBs, given that IFRSs use the term 'licence' without definition or clarification of its features.

#### Questions to Board members

Q1 Do Board members agree that it's important to identify distinguishing features between licences and taxes?

|    |  |
|----|--|
| Q2 | Do Board members agree that the factors identified in the table in paragraph 4(b) are useful in identifying an ‘in-substance’ licence? |
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### **Background and past Board considerations**

- 5 At the June 2017 Board meeting, staff presented an issues paper (Agenda Paper 8.1) outlining a high level analysis of the need to further consider the accounting for revenue from licences issued by NFP public sector entities, including the accounting issues to be addressed in progressing the project.
- 6 In summary, the Board decided that, due to the magnitude of non-contractual and non-IP licence transactions and current diversity in accounting practice, the following accounting issues need to be addressed through further research and outreach with NFP public sector constituents:
  - (a) whether the scope of AASB 15 should be expanded to encompass licences issued under statute and/or licenses not relating to IP; and
  - (b) whether different accounting treatments under AASB 15 are appropriate for revenue from licences (deferral or upfront recognition) depending on the nature of the right created by the licence, for example depending on whether the licence confers the right to use or access an asset, or confers a right to perform an activity.
- 7 In this regard, the Board asked staff to clarify the accounting standards ‘gap’, by defining/circumscribing the nature of licencing arrangements (and permits) to be addressed by this project and identifying the principles in AASB 15 that could (and should) apply in filling that ‘gap’.

### **Results of staff research, principally regarding distinguishing licences and taxes**

- 8 Staff note from previous outreach that public sector constituents commonly refer to a wide range of arrangements as licences (and permits), notwithstanding possible differences in economic substance. Current AASBs do not explicitly define ‘licence’. Accordingly, consistent with the Board’s deliberations at its June 2017 meeting, attempting to clarify the features of what constitutes a licence with regard to the economic substance of an arrangement is an appropriate first step in refining the scope of this project.

The following table sets out the results of staff research with respect to identifying the features of a ‘licence’ (as summarised in paragraph 4(b) above) that should be adopted for the purpose of this project. The table identifies the resources we analysed to help us come to our views and summarises the main insights we drew from those resources (the table also cross-references to the supporting staff analysis contained in Appendix A of this paper):

| Resource                                 | Key points   | Supporting analysis: paragraphs in Appendix A |
|--|--|---|
| <i>Current AASBs</i>                     |  |   |
| AASB 1058                                | <ul style="list-style-type: none"> <li>• AASB 1058 defines and prescribes the accounting for taxes. It uses but does not define the term ‘licences’. This infers that, under AASBs, a licence is not a tax</li> <li>• The distinction between ‘licences’ and ‘taxes’ primarily pivots on whether an arrangement is “compulsorily paid or payable” and, to a lesser extent, on whether it is “established to provide income to the government”. In analysing these factors, in contrast to a tax, a licence fee: <ul style="list-style-type: none"> <li>○ can be evaded (the notion of compulsion should be considered in terms of the different consequences of evading a tax vs a licence fee. Evading a tax leads to a compulsion to pay the tax and any penalties; evading a licence fee only leads to a compulsion to pay any penalties); and</li> <li>○ is established for a non-financial primary purpose (eg to regulate social behaviour, or to allocate a public resource equitably).</li> </ul> </li> <li>• Therefore, AASB 1058 is useful in identifying at least some features of licences for the purpose of this project.</li> </ul> | A5 – A10                                      |
| AASB 15                                  | <ul style="list-style-type: none"> <li>• AASB 15 unequivocally includes revenue from at least IP licences within its scope.</li> <li>• However, it does not explicitly define the term ‘licence’ and therefore is of limited use in identifying features of licences for the purpose of this project, other than suggesting that a licence might involve a right to use or access a licensor’s asset.</li> </ul>   | A11   |
| AASBs 16, 116, 138 & 1059                | <ul style="list-style-type: none"> <li>• The use of the term ‘licence’ within these AASBs does not help identify the features of a licence for the purpose of this project.</li> </ul>   | A12   |
| <i>Other accounting standard setters</i> |  |   |
| IPSASB                                   | <ul style="list-style-type: none"> <li>• IPSASB is currently conducting project work on the accounting for revenue transactions, but has not yet considered accounting for revenue from licences issued by public sector entities.</li> <li>• ‘Licence’ is not defined in any IPSASs.</li> <li>• Therefore, IPSASB is of limited use in identifying features of licences for the purpose of this project.</li> </ul>   | A13   |
| Canadian PSASB                           | <ul style="list-style-type: none"> <li>• Canadian PSASB is currently undertaking a project with respect to revenue recognition, however it has not clarified or defined licences in its Exposure Draft <i>Revenue, Proposed Section PS 3400</i> issued in May 2017 that addresses accounting for revenue from licences and permits.</li> <li>• Therefore, the Canadian PSASB’s work is of limited use in identifying features of licences for the purpose of this project.</li> </ul>  | A15   |
| US GASB, NZASB                           | <ul style="list-style-type: none"> <li>• Other accounting standard setters (US GASB, NZASB) are also of limited use in informing us of features of licences for the purpose of this project.</li> </ul>  | A15   |
| <i>Other resources</i>                   |  |   |
| ABS GFS                                  | <ul style="list-style-type: none"> <li>• GFS defines the term ‘licence’ widely, and infers that although a</li> </ul>  | A18 – A20                                     |

| Resource                            | Key points  | Supporting analysis: paragraphs in Appendix A |
|-------------------------------------|---|---|
| Manual                              | <p>variety of arrangements could constitute licences, revenue from these arrangements could be taxes or administration fees.</p> <ul style="list-style-type: none"> <li>• The GFS approach is inconsistent with the implied approach in AASB 1058 that differentiates between licences and taxes. For example, GFS does not consider compulsion or purpose of establishment, and does not consider rights of the licensee.</li> <li>• Relevant extracts from the ABS GFS Manual are included at Appendix B (for information only).</li> <li>• We found that GFS is of limited use in informing us of features of licences for the purpose of this project.</li> </ul>   |   |
| Dictionary definitions              | <ul style="list-style-type: none"> <li>• Dictionary definitions of ‘licence’ highlight the requirement to obtain explicit permission prior to performing an activity or using or accessing an asset of the licensor.</li> <li>• Therefore, these definitions are useful in distinguishing a licence from a tax – for example, in contrast to a licence, no explicit permission is required before undertaking a taxable activity.</li> </ul>  | A21 – A23                                     |
| Definitions in law                  | <ul style="list-style-type: none"> <li>• The common law definition of ‘licence’ is consistent with dictionary definitions – it implies a licence provides explicit permission for an action.</li> <li>• It also articulates a characteristic of an ‘in-substance’ licence as being that a licence does not transfer an underlying asset that may be the subject of the licence.</li> <li>• Therefore, definitions in law are useful in identifying features of licences for the purpose of this project.</li> </ul>   | A24 – A26                                     |
| Other common attributes of licences | <ul style="list-style-type: none"> <li>• Temporal considerations: Tax relates to a past activity of an entity (e.g. income tax is imposed on past earnings); whereas a licence relates to a future activity the licensee intends to undertake – to perform a desired activity, the licensee is first legally required to obtain permission from an authority (e.g. marriage licences, drivers licences).</li> <li>• Licensor obligations: A licence may give rise to specific obligations for the licensor, whereas a tax does not usually give rise to a specific obligation (although there may be an indirect obligation to use funds for social benefit as a whole).</li> <li>• We think these common attributes are useful in identifying features of licences for the purpose of this project.</li> </ul> | A27 – A28                                     |

## Appendix A: Supporting staff analysis

A1 This Appendix provides an analysis that supports the results of staff research reported in the table in paragraph 8 of this paper.

### Features of a licence

A2 In identifying the features of a licence, staff considered:

- (a) the extent to which current AASBs define, or at least throw light on a definition of, 'licence'. In particular, we looked at AASBs that refer to licences and at the Bases for Conclusions (BC) relating to AASB 1058 and AASB 15 (albeit the IASB's BC);
- (b) the extent to which other accounting standard setters throw light on a definition. For example, we looked at the International Public Sector Accounting Standards Board's (IPSASB) project work with respect to the accounting for revenue transactions; as well as any insights provided by the US Governmental Accounting Standards Board (GASB), the New Zealand Accounting Standards Board (NZASB) and the Canadian Public Sector Accounting Standards Board (PSASB);
- (c) other related resources. For example, the ABS GFS Manual refers to licences in the context of taxes, administration fees, fees for services, leases and permits. We also looked at dictionary definitions and legal definitions; and
- (d) common features of different kinds of licences issued by NFP public sector entities.

### *The definition of a 'licence' implicit in current AASBs*

A3 The following AASBs explicitly refer to 'licence':

- (a) AASB 1058 *Income of Not-for-Profit Entities*;
- (b) AASB 15 *Revenue from Contracts with Customers*;
- (c) AASB 116 *Leases*;
- (d) AASB 138 *Intangible Assets*; and
- (e) AASB 1059 *Service Concession Arrangements: Grantors*.

A4 Even though none of them explicitly define 'licence', some of them throw light on the characteristics of licences. Each is considered in turn below.

*AASB 1058 Income of Not-for-Profit Entities*

- A5 AASB 1058.2<sup>3</sup> makes it clear that accounting for income from taxes is within the scope of AASB 1058. Appendix A defines ‘taxes’ as:<sup>4</sup>
- “Economic benefits **compulsorily paid or payable** to public sector entities in accordance with laws and/or regulations **established to provide income to the government**. Taxes exclude fines.” (emphasis added)*
- A6 AASB 1058 also makes it clear in paragraph 7(d) that licences outside the scope of AASB 15 are not within the scope of AASB 1058 (see paragraph A3 of Agenda Paper 5.2).
- A7 As a consequence of AASB 1058 including income from taxes in its scope whilst excluding licences outside the scope of AASB 15 from its scope, it can be inferred that a ‘licence’ is not a ‘tax’. In interpreting the definition of ‘taxes’ with the intention of distinguishing it from licences, the distinction pivots on whether an arrangement is “compulsorily paid or payable” and/or “established to provide income to the government”.
- A8 In exploring the meaning of ‘compulsion’: although a licence fee is compulsorily payable upon issue, a prospective licensee has the discretion of whether to seek a licence. It could be argued that a taxpayer similarly has discretion as to whether to undertake the activity that will be taxed. However, for it to be a useful discriminator between a licence and a tax, the notion of compulsion needs to be considered in relation to the consequences of evading a licence fee or a tax. If an entity attempts to evade a licence fee and is caught, it would not be compulsory for the entity to retrospectively obtain the licence – rather any penalty for undertaking unlicensed activities would be in the nature of a fine/penalty. In contrast, an entity that evades a tax and gets caught would be compelled to pay the tax, in addition to penalties and interest on late payments. From this perspective, compulsion versus discretion seems to be an essential factor in distinguishing a tax from a licence.
- A9 In exploring the meaning of ‘established to provide income to the government’: whilst a tax is defined in AASB 1058 as an economic benefit that is established for governmental income purposes<sup>5</sup>, the policy intent of a licence seems to be much broader than that. Arguably, a licence arrangement is established with another, non-

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3 “...governments are entitled to non-contractual receivables arising from statutory requirements such as taxes and rates without providing consideration to the other party. Those receivables provide income to the government to further its objectives. This Standard addresses the accounting for the income arising from such transactions.”

4 IPSAS 23 defines the term ‘taxes’ similarly to the AASB 1058 definition. Refer to paragraph A14 for the IPSASB definition.

5 We note that economists might argue that a tax is not established to provide income to the government; rather it is established to facilitate redistribution of wealth in the economy. However, in the context of an accounting standard (AASB 1058) specifying income recognition requirements from taxes, those taxes being regarded as established to provide income to the government has validity.



financial, primary purpose in mind e.g. to regulate social behaviour, or to allocate a public resource equitably.

- A10 Although this analysis of AASB 1058 may throw significant light on the features of ‘licence’, it is not sufficient as it would not be appropriate to conclude that all arrangements falling outside the definition of taxes would be ‘in-substance’ licences. However, the definition of tax does provide a useful starting point in differentiating the discretionary nature of licences and their purpose of establishment as factors indicative of ‘in-substance’ licences.

*AASB 15 Revenue from Contracts with Customers*

- A11 AASB 15 sets out the accounting treatment that entities must adopt with respect to recognising and measuring revenue from contracts with customers and explicitly extends to the accounting for revenue from IP licences. However, neither AASB 15 nor the IFRS 15 BC explicitly define or identify the features of licences. Rather, the IFRS 15 BC focuses on explaining the IASB’s rationale for the timing of revenue recognition with respect to IP licences.<sup>6</sup> Therefore, AASB 15 of itself is of limited use in identifying the features of a licence for the purpose of this project – other than to the extent it indicates a right to use or access a licensor’s asset.

*AASB 16 Leases, AASB 1059 Service Concession Arrangements: Grantors, AASB 116 Property, Plant and Equipment and AASB 138 Intangible Assets*

- A12 Some arrangements referred to as licences in practice might be in the nature of a lease (AASB 16), a service concession (AASB 1059), or may constitute the sale of an asset (AASB 116 and AASB 138). Indeed, AASB 16 and AASB 138 refer to some transactions within their scope as ‘licences’. Agenda paper 5.2 considers the range of licences within the scope of these Standards to help narrow down the types of licences that might not currently have adequate guidance. However, the use of the term ‘licence’ within these AASBs is not helpful in clarifying the features of a licence for the purpose of this project; except to the extent it is clear that the licences within their scope convey a right to a licensee and an associated obligation of the licensor.

*Other accounting standard setters*

- A13 Staff also considered the thinking of the IPSASB with respect to the accounting by NFP public sector entities for licences they issue, in the context of the IPSASB’s current project work on the accounting for revenue transactions. Staff reached out to IPSASB staff and were informed that although the IPSASB aims to issue a Consultation Paper setting out preliminary views with respect to the accounting for exchange and non-exchange revenue transactions, the IPSASB has not yet considered accounting for revenue from licences issued by public sector entities. Staff also note that the term ‘licence’ is not defined in any IPSASs.
- A14 IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)* defines the term ‘taxes’ similarly to AASB 1058. Paragraph 7 of IPSAS 23 defines ‘taxes’ as:

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6 See Agenda Paper 8.1 presented at the 27 June 2017 Board meeting for a discussion regarding the IASB’s rationale for providing guidance limited to IP licences in the Basis for Conclusions to IFRS 15.

*“... economic benefits or service potential compulsorily paid or payable to public sector entities, in accordance with laws and or regulations, established to provide revenue to the government. Taxes do not include fines or other penalties imposed for breaches of the law.”*

- A15 Staff also considered the current project work of the GASB in the US, the NZASB and the Canadian PSASB and did not identify any publicly documented thinking regarding the definition of the term ‘licence’. Staff note that the Canadian PSASB is currently undertaking a project with respect to revenue recognition, and has considered the accounting for revenue from licences issued by public sector entities in an Exposure Draft *Revenue, Proposed Section PS 3400* issued in May 2017. However, the Canadian PSASB has not clarified or defined licences in the Exposure Draft.
- A16 Accordingly, none of the work of the other accounting standard setters we researched throw much light on features of licences for the purpose of this project.

#### *Other resources*

- A17 Staff reviewed the following non-accounting resources to identify other possible definitions of the term ‘licence’:
- (a) the Australian Bureau of Statistics Government Finance Statistics (ABS GFS) Manual;
  - (b) Dictionary definitions; and
  - (c) Definitions in law.

#### *ABS GFS Manual*

- A18 Staff considered the discussion of licences as set out in the ABS GFS Manual. Paragraph 13.122 of the ABS GFS Manual states:

*“...licences exist to provide a regulatory function for common activities undertaken by the general population. If the issue of such licences involves little or no work for the government, then the revenues raised are recovered as taxation revenue. However, if the government uses the issue of licences to exercise some sort of regulatory function, such as checking the competency or qualifications of a would-be licensee, then the revenues raised are recorded as administrative fees... unless they are clearly disproportionate to costs of providing the services...”<sup>7</sup>*

- A19 The ABS GFS Manual appears to define the term ‘licence’ widely, and infers that although a variety of arrangements could constitute licences; revenue from some of these arrangements could be taxes or administration fees. The GFS definition states that licences exist to provide a regulatory function for common activities undertaken

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7 We acknowledge this ABS GFS Manual paragraph delves into the accounting treatment of licences, which is beyond the scope of this paper. However, the GFS accounting treatment is inextricably linked to definitional issues.

by the general population and suggests that the accounting for the revenue from licences (for example as taxes or administration fees) depends on the level of work involved for the government (i.e. the licensor) in the issuance of a licence.

- A20 Accordingly, the ABS GFS Manual’s approach to defining a licence differs from the approach in AASB 1058. Furthermore, the ABS GFS Manual does not identify ‘compulsion’ or ‘purpose of establishment’ as a basis for distinguishing a tax from a licence (see the discussion in paragraphs A8 and A9 above). The ABS GFS Manual also adopts a licensor’s perspective in determining the economic substance of the transaction. Staff think the GFS approach is of limited use for the purpose of identifying features of a ‘licence’ for the purpose of this project as it does not consider the rights afforded to the licensee under the licence arrangement.

#### *Dictionary definitions*

- A21 The *Oxford Dictionary of English* defines a licence as:

*“A permit from an authority to own or use something, do a particular thing, or carry on a trade (especially in alcoholic drink).”*

*“Formal or official permission to do something.”*

- A22 The *Merriam-Webster Dictionary* defines a licence as:

*“A permission granted by competent authority to engage in a business or occupation or in an activity otherwise unlawful.”*

- A23 Staff think the common themes of the dictionary definitions above are useful in distilling an important feature of licences. These definitions highlight the requirement to obtain explicit permission prior to performing an activity or using or accessing an asset of the licensor. This is useful in distinguishing a licence from a tax – for example, in contrast to a licence to earn income from driving a taxi, no explicit permission is required in order to earn income on which income tax is imposed.

#### *Definitions in law*

- A24 Staff conducted limited research in relation to determining whether any Australian legislation in force defines the term ‘licences’. Although some legislation defining licences was identified, the definitions are narrow and specific in the context of the subject matter of the law. For example, the *Radiocommunications Act 1992* defines a licence as a spectrum licence, an apparatus licence, or a class licence.
- A25 Staff also considered whether any definitions of the term ‘licence’ have been made in common law, and identified two cases<sup>8</sup> that cited a definition of the term ‘licence’ propounded by Vaughan CJ in *Thomas v Sorrell (1673)* as:

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8 *National Provincial Bank Ltd v Ainsworth [1965] 2 All ER 472 (UK Case)*  
*Radaich v Smith 101 CLR 209 [1959] (Australian Case)*

*“A dispensation or licence properly passeth no interest, nor alters or transfers property in any thing, but only makes an action lawful, which without had been unlawful.”*

A26 Staff think the common law definition is potentially useful, as it is consistent with the dictionary definitions in that it implies a licence provides explicit permission for an action through the words “... but only makes an action lawful, which without had been unlawful.” The definition also articulates an important feature of an ‘in-substance’ licence in that a licence does not transfer the underlying asset that may be the subject of the licence. This feature is also helpful as a distinguishing feature between arrangements that constitute asset sales (e.g. asset sales under AASB 116 or AASB 138) from arrangements that constitute ‘in-substance’ licences.

*Common features of licences not identified above*

A27 In addition to the characteristics of ‘in-substance’ licence arrangements identified above, for completeness, staff identified other possible features of licences based on commonly observed attributes of different kinds of arrangements that are typically referred to as licences in Australia. These attributes, and staff thinking regarding their relevance in identifying features of a licence for the purpose of scoping the project, are discussed in the following:

- (a) The existence of an underlying asset: Licence arrangements can be associated with an asset of the licensor (eg a software licence relates to the software of a licensor), or no asset of the licensor (eg a marriage licence or a drivers licence).
- (b) Refundability: Some licence arrangements may be refundable (eg a drivers licence issued in Victoria may be refundable if cancelled) others may not (eg a marriage licence).
- (c) Transferability: Some licence arrangements may be transferable to other entities after issue to the licensee by the public sector entity (eg taxi licence) whereas others may not (eg drivers licence).
- (d) The period of the arrangement: some arrangements are short term (eg annual), others are long-term (eg multi-year).

A28 Staff do not think these attributes, of themselves, are relevant in determining whether an arrangement constitutes an ‘in-substance’ licence – although they may have some relevance in determining the accounting treatment (to be discussed in a later paper). However, staff think the following three features might throw some light on features of a licence:

- (a) temporal considerations: Tax relates to a past activity of an entity (e.g. income tax imposed on earnings); whereas a licence relates to a future desired activity the licensee intends to undertake – the licensee is first legally required to obtain permission from an authority to engage in such activities (e.g. marriage licences, drivers licences). This temporal characteristic can be distinguished from a tax as defined in AASB 1058 (see paragraph A5 above), where an economic benefit would be

compulsorily paid or payable to public sector entities in accordance with laws and/or regulations as a consequence of engaging in an activity (e.g. land tax payable as a consequence of purchasing land, or income tax payable as a consequence of earning income);

- (b) licensor obligations: A licence may give rise to obligations for the licensor, whereas a tax does not; and
- (c) The existence of licensee rights: Arrangements can represent the right to access an asset, use an asset, transfer ownership in an asset, or, as noted above, not involve an asset; whereas taxes do not convey such rights to a taxpayer.

## **Appendix B: Extracts from the ABS GFS Manual (for information only)**

Staff reviewed the following paragraphs from the ABS GFS Manual in developing the analysis (see paragraphs A18-A20 of this paper) underpinning the suggested features of a licence as set out in paragraph 4(b) of this paper:

6.9 Governments may regulate certain activities by issuing licences, for which fees are payable. The service may include activities such as checking the competency or qualifications of a would-be licensee. If the service charge is clearly out of all proportion to the cost of providing the service then the revenue raised is deemed to be taxation revenue rather than revenue from the sales of goods and services. In certain circumstances it may be conceptually justifiable to split the payment, e.g. treating a portion of the payment as the sale of goods and services and the remaining portion as a tax. It may be appropriate to adopt this treatment in situations where a product of measurable benefit is provided to the payer and the case is economically significant. The treatment of sales of goods and services is further discussed in Chapter 13 Part J of this manual.

6.97 Taxes on the use of goods and performance of activities (ETF 1114, TC 5) are other taxes on production consisting of fees levied for the issuance of a licence or permit that are not commensurate with the cost of the control function of government. Paragraph 5.72 of the IMF GFSM 2014 notes that governments provide permission to use certain goods or perform certain activities to individual units directly in the form of a licence, permit, certificate of registration or other authorisation in return for payment. This payment forms part of a mandatory process that ensures proper recognition of ownership, or ensures that activities are performed under the correct authorisation of the law.

6.122 Administrative fees (ETF 1122, COFOG-A, SDC) are a type of revenue which consist of fees and charges for compulsory licences and other administrative fees that make up a part of sales of services. If the government exercises a regulatory function, such as checking the competency or qualifications of a would be licensee, then such fees are treated as revenues from sales of goods and services. In this case, the payment is taken to be proportional to the cost of producing the service. If there is little or no work involved on the part of the government in the processing or granting of the licence, permit or other service, or if the revenues raised are clearly out of all proportion to the cost of providing the service, then the fee is classified as other taxes on use of goods and performance of activities (ETF 1111, TC 539, SDC). Examples of administrative fees include drivers' licence fees, court fees, and radio and television licence fees when public authorities provide general broadcasting services. Paragraph 5.138 of the IMF GFSM 2014 notes that fees payable for voluntary participation in deposit insurance or other guarantee schemes that do not qualify to be a standardised guarantee scheme are also included in this classification category. For further information on the boundary between taxes and the purchases of services, see Chapter 13 of this manual.

### *Licences*

13.122. In GFS, licences exist to provide a regulatory function for common activities undertaken by the general population. If the issue of such licences involves little or no work for the government, then the revenues raised are recorded as taxation revenue

(ETF 111). However, if the government uses the issue of licences to exercise some sort of regulatory function, such as checking the competency or qualifications of a would be licensee, then the revenues raised are recorded as administrative fees (ETF 1122) as part of sales of goods and services by government unless they are clearly disproportionate to the costs of providing the services. Examples of licences issued by government include fishing licences, marriage licences, drivers licences, and dog owners licences. Further information on the classification of tax versus payment for services can be found in Box 13.5 of this manual.

13.123. The difference between a lease and a licence is that governments issue licences in order to regulate certain activities that are common to the general population, whereas government leases often involve a specialised activity, such as mineral extraction.

*Permits to undertake a specific activity*

13.124. In addition to leases and licences, governments may issue permits that give individuals or entities permission to engage in a particular activity in exchange for a fee. Permits are designed to limit the number of individual units entitled to engage in an activity. Often the government is required to check the competency and / or qualifications of permit holders. If the government performs this type of regulatory function, then the fees that are associated through the issue of permits will be recorded as administrative fees (ETF 1122) as part of sales of goods and services (ETF 112). Examples of permits issued by governments include gambling permits, food and beverage permits, and taxi-plate permits.

*Determining whether a licence represents the sale of an asset or rent from natural resources*

13.125. Sometimes it can be difficult to determine whether payments received under certain licensing arrangements actually constitute the sale of an asset, or whether they represent rents received from natural resources under Box A4.1 of the IMF GFSM 2014 lists a number of criteria designed to determine whether payments received under a licence represent an asset sale or rent from natural resources. These criteria have been reproduced in Box 13.4 below:

Box 13.4 - Criteria used to determine whether a licence represents an asset sale or rent from natural resources

a. Costs and benefits assumed by licensee: the greater the extent of the risks and benefits associated with the right to use an asset incurred by the licensee, the more likely the classification of a transaction as the sale of an asset as opposed to rent. Pre-agreement on the value of payments (whether by lump sum or by instalments) effectively transfers all economic risks and benefits to the licensee and points therefore, to the sale of an asset. If, on the other hand, the value of payment is contingent on the results from using the licence, risks and benefits are only partially transferred to the licensee and the situation is more readily characterised as payment of rent. In the case of mobile phone licences, the total amount payable is often pre-agreed. An additional indication of the degree to which commercial risks have been passed to the licensee is to examine the hypothetical case where a licensee goes bankrupt. If, in such a case, the licensor reimburses none of the up-front payment

made by the licensee, this would constitute a strong case against a characterisation of the transaction as rent, as apparently the licensee has incurred all the risks involved.

b. Up-front payment or instalment: as with other indicators, the mode of payment is in itself not conclusive for a characterisation as a transaction in assets or rent payment. Generally, the means of paying for a licence is a financial issue and not a relevant factor in determining whether or not it is an asset. However, business practice shows that upfront payments of rent for long periods (15-25 years in the case of mobile phone licences) are unusual and this favours an interpretation as sale of an asset.

c. Length of the licence: licences granted for long periods suggest the transaction should be treated as the sale of an asset, for shorter periods a treatment as payments for rent. The time frame involved in mobile phone licensing (15-25 years) is considered rather unusual as a period for which to conclude a fixed payment of rent and therefore a further indication favouring an interpretation as sale of an asset.

d. Actual or de facto transferability: the possibility to sell the licence is a strong indication of ownership and if transferability exists, this is considered a strong condition to characterise the licensing act as the sale of third-party property rights. In practice, mobile phone licences are often transferable either directly (by the corporation selling the licence to another corporation) or indirectly (through the corporation being acquired through a takeover).

e. Cancellation possibility: the stronger the restrictions on the issuer's capacity to cancel the licence at its discretion, the stronger the case for treatment as a sale of an asset. Conversely, when licences can easily be cancelled at the discretion of the issuer, ownership over benefits and risks has not been fully transferred to the licensee and the transaction qualifies more readily as rent.

f. Conception in the business world and international accounting standards: businesses, in accordance with international accounting standards, often treat a licence to use the spectrum as an asset. Again, in itself this does not lead to treatment as an asset in the national accounts, and there are other areas where companies choose to present figures in.

#### Box 13.5 - Taxes vs Fees for Service in GFS

One of the regulatory functions of governments is to prohibit the ownership or use of certain goods or the pursuit of certain activities, unless specific permission is granted by issuing a licence or other certificate for which a fee is demanded. To decide whether such a fee constitutes taxation revenue (ETF 1111) or a component within the category of sales of goods and services (ETF 112) the following recommendations apply:

Fee payments are recorded as taxation revenue when:

The government unit performs little or no work in return for payment (such as performing a check of the legal capacity of an applicant of a permit to confirm the applicant has not been convicted of a crime). Examples of this are:



- A licence or a permit is automatically granted by the government as a mandatory condition to perform an activity or acquire an asset.
- The payer of the levy is not the receiver of the benefit, such as a fee collected from slaughterhouses to finance a service provided to farmers.
- The government is not providing a specific service commensurate with the levy (even though a licence may be issued to the payer), such as a hunting, fishing, or shooting licence that is not accompanied by the right to use specific government owned natural resources. Other examples include dog registration, marriage licences, payments by persons or households for licences to own or use vehicles (such as the renewal of a drivers' licence), boats or aircraft;
- The benefits are received only by those paying the fee but the benefits received by each individual may vary in proportion to the payments, such as a milk marketing levy paid by dairy farmers and used to promote the consumption of milk;
- If beneficiaries cannot opt out of a compulsory scheme (such as fees paid to government for deposit insurance and other guarantee schemes if they are compulsory), if the payment is clearly out of proportion to the service provided, if the payment is not set aside in a fund, or if it can be used for other purposes.
- In certain circumstances it may be conceptually justifiable to split the payment into a revenue generation and a full cost recovery component, therefore treating a portion of the payment as the sale of goods and services and the remaining portion as a tax. It may be appropriate to adopt this treatment in situations where a product of measurable benefit is provided to the payer and the case is economically significant.

Fee payments are recorded as the sale of goods and services when:

- The issuing of a licence or permit involves a proper regulatory function of the government by exercising control on the activity, checking the competence or qualifications of the persons concerned, etc. Examples include the assessment process involved with the application of a drivers' licence, pilot's licence, television broadcast licences, radio licences, firearm licences, and payments for airport fees, court fees, etc.

Source: Based on paragraphs 5.73 and 5.74 International Monetary Fund Government Finance Statistics Manual, 2014