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Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
545 Fifth Avenue
14th Floor
NEW YORK NEW YORK 10017
United States of America

Dear Mr Sutcliffe

IPSASB Exposure Draft ED 29 Revenue from Non-Exchange Transactions (Including Taxes and Transfers)

Thank you for the opportunity to comment on the Exposure Draft ED 29 *Revenue from Non-Exchange Transactions (Including Taxes and Transfers)*.

Our comments have been prepared in consultation with members through our Centres of Excellence – Financial Reporting and Governance, and the Public Sector.

The background material to the [draft] International Public Sector Accounting Standard (IPSAS) comments, many public sector entities derive most of their revenue from non-exchange transactions and also receive inflows of resources as a contribution from owners. "These issues have not been addressed by IPSASs and other international guidance does not address these issues from a public sector perspective."

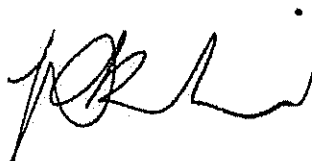
CPA Australia agrees it appropriate that the International Public Sector Accounting Standards Board (IPSASB) address these important issues. We also agree it appropriate that the IPSASB give due consideration to the provisions of relevant International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) – and we note the lack of consistency in approach between IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* and IAS 41 *Agriculture*.

However, CPA Australia is concerned that the approach articulated in the [draft] IPSAS is not consistent with the definition of a liability and is not consistent with the current thinking of the IASB as articulated in paragraph BC11 of ED *Proposed Amendments to IAS 37, Provisions, Contingent Liabilities and Contingent Assets*. Paragraph BC11 comments the IASB tentatively concluded that liabilities arising from contracts derive only from unconditional obligations, and not from conditional obligations. This is because a conditional obligation that may result in an outflow of economic benefits is not a present obligation.

However, although a conditional obligation in a contract does not itself satisfy the definition of a liability, it points to the existence of an accompanying unconditional obligation that may satisfy the definition of a liability. The [draft] IPSASB does not identify a specific public sector reason for the divergence in approach from the definition of a liability and the current thinking of the IASB – and it is our understanding that a working principle of the IPSASB is that a departure from the IASB literature is warranted only when there is a specific public sector reason. CPA Australia would expect the Basis for Conclusions to the [draft] IPSASB to articulate that reasoning.

Our detailed comments to the specific matters identified in the Exposure Draft are attached to this letter. Should you have any queries on our comments, please contact Dr Mark Shying, CPA Australia's Financial Reporting and Governance Senior Policy Adviser, at mark.shying@cpaaustralia.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Geoff Rankin', with a small dot above the final 'i'.

Geoff Rankin FCPA
Chief Executive Officer

Copy: D Boymal
M Shying

CPA Australia's response to IPSASB Exposure Draft ED 29 Revenue from Non-Exchange Transactions (Including Taxes and Transfers):

The attached letter notes CPA Australia's concern that the approach articulated in the [draft] International Public Sector Accounting Standard (IPSAS) is not consistent with the definition of a liability and is not consistent with the current thinking of the International Accounting Standards Board (IASB) as articulated in paragraph BC11 of ED *Proposed Amendments to IAS 37, Provisions, Contingent Liabilities and Contingent Assets*. We would expect the Basis for Conclusions to the [draft] IPSAS to articulate the specific public sector reason for the International Public Sector Accounting Standards Board's (IPSASB) divergence in approach from the definition of a liability and the current thinking of the IASB. Our response is made on the basis that the IPSASB articulates that reasoning.

(a) Exclude entity combinations that are non-exchange transactions from the scope of the Standard (see paragraph 2).

CPA Australia agrees. IFRS 3 *Business Combinations* does not apply to business combinations involving entities under common control – accordingly, for-profit entities have a variety of choices. We consider it appropriate that those entities subject to the [draft] IPSAS have the same variety of choices. Some of our members have identified the variety of available choices as problematic and not consistent with the production of information that is comparable between entities, and accordingly requiring resolution. We encourage the IPSASB to work together with the IASB to specify the required accounting for business combinations involving entities under common control.

(b) Include within the scope of the IPSAS compulsory contributions to social security schemes (e.g. health and disability insurance, aged pensions) which are in the nature of non-exchange transactions. In particular:

(i) Do you think that these compulsory contributions to social security schemes should be explicitly excluded from the scope?

CPA Australia supports the inclusion of these transactions within the scope of the IPSAS. We do not think that compulsory contributions to social security schemes that are non-exchange transactions should be explicitly excluded from the scope.

(ii) Do you think that the ED gives enough guidance in respect of such compulsory contributions? If not, do you think the IPSAS should explicitly address these compulsory contributions and provide specific guidance to assist entities determine to what extent such contributions should be considered as exchange transactions? (See paragraph BC27)

Nothing has come to our attention that would require the inclusion of specific guidance.

(c) Define terms as set out in paragraph 8. These definitions have been developed by the IPSASB for this IPSAS. Please identify any amendments to the definitions that you consider necessary.

"Non-exchange transactions are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange." CPA Australia understands that the entity receiving a cash grant will more often than not be giving approximately equal value to a third party entity (i.e., an entity that is not the entity providing the cash grant). One reading of the definition of non-exchange transactions would appear to not include a transaction of the type we have described.

We think the definition of non-exchange transactions would be improved by the inclusion of the words "that entity" so that the definition is "Non-exchange transactions are transactions that are not exchange transactions. In a non-exchange transaction, an entity either receives value from another entity without directly giving approximately equal value in exchange to that entity, or gives value to another entity without directly receiving approximately equal value in exchange from that entity."

(d) Distinguish exchange and non-exchange components of non-exchange transactions. Paragraphs 11 and 12 note that these transactions may comprise two components, one of which is an exchange transaction, each component of which is recognized separately.

CPA Australia agrees that when an entity receives resources and provides something more than nominal consideration but less than approximately equal value, it might be necessary to componentise the transaction into an exchange transaction component and a non-exchange transaction component.

(e) Include guidance to clarify that restrictions do not give rise to the recognition of a liability on initial recognition of the transferred asset (paragraph 20). Do you agree that restrictions do not give rise to liabilities on initial recognition of the transferred asset?

The [draft] IPSAS comments that:

- constructive obligations do not arise from stipulations. IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* establishes requirements for the recognition and measurement of constructive obligations; and
- restrictions on transferred assets (performance obligations) never cause the recipient entity to incur a present obligation to transfer future economic benefits to third parties when it initially gains control of an asset subject to a restriction.

CPA Australia thinks the inclusion of guidance re restrictions might be useful. We agree that restrictions do not give rise to liabilities on initial recognition of the transferred asset – any restriction that is a constructive obligation is within the scope of IPSAS 19.

(f) Require recognition of assets when resources are transferred or when the reporting entity has an enforceable claim to resources that are to be transferred (see paragraphs 33 – 34 and paragraph 80). The ED notes that before a claim to a resource is enforceable, the resource does not meet the definition of “control of an asset” because the recipient reporting entity cannot exclude or regulate the access of the transferor to the resource.

CPA Australia has been told by some members that there is some confusion about the control concept articulated in the [draft] IPSAS. We support the elimination of this confusion. We understand the confusion arises from the principle articulated in paragraph 34 being interpreted as not consistent with the principle articulated in paragraph 36.

Paragraph 34 states “In circumstances where an appropriation is required before resources can be transferred, a recipient entity will not identify resources as controlled until such time as the appropriation is made because the recipient entity cannot exclude or regulate the access of the government to the resources.” Paragraph 36 states “For example, where a government appropriates funds to a public sector entity (a reporting entity), the appropriation is enforceable and the government has a history of transferring appropriate resources, it is probable that the inflow will occur, notwithstanding that the appropriated funds have not been transferred at the reporting date.”

Some of our members have made known to us their concern as to how the concept of control articulated in the [draft] IPSAS operates for Government reporting entities, such as ministries that are part of the same legal entity. Agreements between these entities are not legally enforceable, as an entity cannot take legal action against itself.

We would expect the [draft] IPSAS to articulate a principle of control that control may exist even where there is no legal control. The IASB *Framework for the Preparation and Presentation of Financial Statements* paragraph 57 states “Although the capacity of an entity to control benefits is usually the result of legal rights, an item may nonetheless satisfy the definition of an asset even when there is no legal control.” CPA Australia believes there should be consistency between the [draft] IPSAS and IFRS unless there is a public sector specific reason for divergence.

(g) Measure assets acquired in a non-exchange transaction at their fair value on initial recognition and amend IPSAS 12, “Inventories”, IPSAS 16, “Investment Property” and IPSAS 17, “Property, Plant and Equipment” to be consistent with this requirement (see paragraphs 38 – 39 and the Appendix). IPSAS 12 currently requires inventory to be initially recognized at cost, and IPSASs 16 and 17 currently require that where assets are acquired for no cost or a nominal cost, their cost is their fair value as at the date of acquisition.

CPA Australia supports the changes to IPSASs 12, 16 and 17 to include a requirement that non-exchange transactions use fair value on initial recognition.

(h) Require that a liability be recognized in respect of an asset transferred subject to conditions upon initial recognition of the transferred asset (paragraph 50). When the condition has been satisfied the liability is reduced, or derecognized, and revenue recognized. Alternatively, do you consider that the IPSAS should only require the recognition of a liability when it is more likely than not that the condition will not be satisfied (see paragraph BC11)? In addition, are you of the view that the requirements relating to the recognition of a liability in respect of a condition applies equally to depreciable and non-depreciable assets?

CPA Australia supports the proposal that a liability be recognised in respect of an asset transferred subject to conditions upon initial recognition of the transferred asset (paragraph 50) and that when the condition has been satisfied the liability is reduced, or derecognised, and revenue recognised.

(i) Require liabilities related to inflows of resources to be measured according to the requirements of IPSAS 19, “Provisions, Contingent Liabilities and Contingent Assets” (paragraph 52).

CPA Australia agrees that the measurement criteria within IPSAS 19 is appropriate.

(j) Require a non-exchange transaction that gives rise to the recognition of an asset to also give rise to the recognition of revenue to the extent that a liability is not recognized (paragraph 54). Are there any non-exchange transactions in which it would be appropriate to initially recognize the gross inflow of economic benefits or service potential represented by the asset as revenue even if a liability is also recognized, with the simultaneous recognition of an expense for the liability?

CPA Australia agrees that revenue should not be recognised to the extent that a liability is recognised, until the obligation is fulfilled.

(k) Require a reporting entity to recognize liabilities in respect of advance receipts related to taxes (see paragraph 67) and advance receipts related to transfers (see paragraph 105).

CPA Australia agrees with the proposal.

(l) Not permit the netting of expenses paid through the tax system (see paragraphs 72 – 76) against taxation revenue. Instead such expenses must be recognized separately on a gross basis. The ED distinguishes between expenses paid through the tax system and tax expenditures, and notes that tax expenditures are foregone revenue, not expenses.

CPA Australia agrees with the proposal.

(m) Permit recognition of services in-kind that satisfy the recognition requirements (see paragraphs 99 – 103) and require disclosure of the nature and type of services in-kind received, whether recognized or not (paragraph 107-108).

CPA Australia considers that services in-kind either meet the requirements for recognition, or they do not. We do not support the recognition of these services in-kind to be at the entity's discretion. We suggest that the International Financial Reporting Interpretation Committee Interpretation SIC-

31 Revenue – Barter Transactions Involving Advertising Services might provide a basis for determining reliable measurement (i.e., involving cash transactions for similar transactions to other parties).

(n) Provide entities a five year period in which to conform their accounting policies in respect of taxation revenue to the requirements of this Standard. (See paragraphs 115 – 122). Do you believe that transitional provisions should be provided in respect of other non-exchange transactions?

Nothing has come to CPA Australia's attention that would require the five year transitional period to be provided in respect of other non-exchange transactions. Some members have told us it is appropriate to provide Governments with relief in regard to taxation revenue recognition – as many Governments currently are unable to meet the accrual requirements of the standard in relation to taxation revenues where there is a high degree of estimation required at balance date.

OTHER COMMENTS

Paragraph 23 Example. Some of our members do not understand the transfer term as being so broad as to not impose on the recipient a performance obligation. We suggest the example be reworded to better convey the intended message.

Paragraph 70. Some of our members suggest that line 2 "may result" be replaced with "will likely result".

Paragraph 98 comments an appraisal of the value of an asset is normally undertaken by a member of the valuation profession. CPA Australia notes that obtaining appraisals from an external valuer will be a case-by-case decision, depending on the cost versus benefit. It is therefore recommended that the [draft] IPSAS replace the words "is normally" with "may be".

Paragraph 108. Some members think disclosure of the monetary value of unrecognised services in-kind should be required.

Example 20. Some of our members read this example as implying that revenue will be recognised on a net basis, as CU55 million was invoiced but only CU53 million was recorded as revenue. This seems inconsistent with the contents of the proposed standard.

Example 21. Some of our members suggest that this example might not be consistent with the latest work of the IASB in the use of fair value in multiple markets.

Example 24. Some of our members suggest that this example would be improved by expanding it so that if a liability is not recognised, a contingent liability may exist that should be disclosed.

Paragraph BC6 first line. "fore the recognition" should read "for the recognition".