



**INTERNATIONAL FEDERATION
OF ACCOUNTANTS**

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DATE: FEBRUARY 6, 2005
MEMO TO: MEMBERS OF IFAC IPSASB
FROM: MATTHEW BOHUN
SUBJECT: REVENUE FROM NON-EXCHANGE TRANSACTIONS

ACTION REQUIRED

The Board is asked to:

- **review** the draft Exposure Draft XX, “Revenue from Non-Exchange Transactions (Including Taxes and Transfers); and
- **provide** staff with instructions for the next stage of drafting.

AGENDA MATERIAL:

8.2 ED XX, “Revenue from Non-Exchange Transactions”

Pages
8.5 – 8.33

BACKGROUND

At the PSC meeting in New Delhi in November 2004, the PSC directed staff to prepare a draft exposure draft of “Revenue from Non-Exchange Transactions” in accordance with the principles established in the Invitation to Comment prepared by the Steering Committee and published by the PSC. The Draft ED at Item 8.2 has been prepared in accordance with the instructions provided to staff and documented in the minutes (see item 2.2).

At this stage, the Specific Matters for Comment have not been included. As has been the case in the past, we will keep these until the end. The minutes from the last meeting suggested a specific matter addressing tax expenses and expenses paid through the tax system, I will keep track of this matter and include it in the next draft.

I have not included as yet the amendments to other IPSASs, the examples, the Basis for Conclusions, or the Comparison with IAS 20, these will be included in the next draft for the New York meeting in July. The examples will be reworked from the examples included in the ITC. The Basis for Conclusions will be drawn from meeting discussions and, to the extent that they are also the IPSASB’s views, the views of the Steering Committee. The IPSAS that develops from this project will be radically different from the approach adopted by the IASC when it developed IAS 20, “Accounting for Government Grants and Disclosure of Government Assistance” and the comparison will reflect the fundamental difference in approach.

Members are requested to review the draft ED and, in particular, consider the issues raised below as you work through the draft.

ISSUES

(a) Contributions from Controlling Entities/Owners/Members

The PSC directed staff to rework the nomenclature of direct contributions to net assets/equity. Members suggested that “Contributions from Controlling Entities/Owners/Members” was more appropriate to the public sector than “contributions from owners”. I have drafted the Exposure Draft accordingly. However, I believe that the term included is unduly lengthy. I would prefer that the IPSASB define the technical term “contribution” with the same definition as the current “contribution from owners”, and that the term “donation” be used for other transfers of assets to reporting entities. Adopting the term “contribution” would resolve the issue of whether there are owners in the public sector. I believe that the terms “controlling entities” and “members” present the same difficulties that “owners” presents.

The requirements proposed in the ITC for the recognition of “contributions from controlling entities/owners/members” have been included in the draft ED. I have also included guidance to require analysis of substance over form.

(b) Tax Expenditures and Expenses Paid Through the Tax System

As directed the draft ED contains proposals to require the separate recognition of expenses paid through the tax system, but no separate recognition of tax expenditures. This is consistent with the proposals in the ITC, and the prohibition on offsetting in IPSAS 1.

In considering this issue further as I was drafting the ED, I have come to the conclusion that this issue is no different to that relating to the components approach in which a single transaction has a number of components that are required to be recognized separately. I would request that as the IPSASB works through the draft, you consider whether this section and the section on the components approach should be merged.

(c) Stipulations

The Steering Committee came to some conclusions regarding restrictions, conditions and time requirements. Whilst the Steering Committee was reasonably comfortable with the conclusions that they had drawn, the respondents to the Invitation to Comment, and members of the PSC expressed a range of views that suggests that the position in practice is not as clear cut as the ITC suggested.

In drafting the ED, I have included the definitions of “condition”, “restriction”, “stipulation” and “timing requirement”. In the proposed requirements of the ED I have included in black letter the requirement not to recognize a liability in respect of a restriction or a time requirement, but to recognize one in respect of a condition. The accompanying commentary explains that a restriction and a time requirement do not meet the definition of a liability and that a condition does. In relation to a time requirement I have, as directed, included in a text box an additional alternative requirement and accompanying commentary so that the IPSASB can revisit the issue of whether entities should be required to recognize a liability in respect of a time requirement. The alternative commentary explains that a time requirement does not meet the definition of a time requirement, but a liability is to be recognized nonetheless.

The commentary also notes in paragraph 51 that in many circumstances the legislation or transfer agreement will be very complex and that the legislation or agreement affecting the transfer may contain all three types of stipulations. The laws and agreements for transfers of substantial assets are typically drafted by teams of legal experts, and it may require a legal opinion or judicial decision to actually determine that a liability exists and should be recognized.

In discussing this issue, the IPSASB should note that in practice, it may not always be clear cut that a stipulation is a restriction, a condition or a time requirement; it may only become clear once the matter is litigated. Even if a stipulation appears to be a restriction or time requirement if there is a legal precedent, or a legal opinion, that indicates that there is a legal liability, IPSAS 19, “Provisions, Contingent Liabilities and Contingent Assets” would require the recognition of a liability.

4(d) Compound Transactions – The Components Approach

The PSC directed staff to include requirements to recognize components of compound transactions separately. This has been done. The way it has been drafted, the components approach encompasses both transactions set at above and below fair value. In respect of those transactions where the consideration is in excess of fair value, the ED proposes that the amount in excess of fair value be recognized as a transfer, whilst the fair value component is recognized as an exchange transaction.

In relation to transactions set at below fair value, the ED proposes that the entity recognize a proportion of the transaction as an exchange transaction, and the balance as a non-exchange transaction that does not generate revenue. For example, a compulsory fee at a public school that represents ten percent of the fair value of the service provided would be recognized as an exchange transaction for the 10%, whilst the balance is a service provided free, which does not generate revenue. This treatment reflects the instructions given to staff, and I am of the view that financial statements prepared this way would give a true and fair view of an entity’s financial performance. The commentary notes that this treatment applies to mandatory fees but not voluntary fees, which are more in the nature of transfers. Please advise if you agree that this statement should be included in the ED.

An alternative view to that drafted is that in respect of transactions set at below fair value, the entity should recognize revenue for the full fair value, and an expense for the imputed subsidy. Such a treatment is suggested by the GFS Manual 2001. For example, where a public school charges a 10% fee, it would recognize 100% of the fair value as revenue, and an expense for 90% as a subsidy. I am of the view that this treatment would mislead users of financial statements, however considering the project on convergence of IPSASs and statistical reporting, this treatment should be considered.

(e) Disclosures

The PSC directed that the ED not require the separate disclosure of revenue from non-exchange transactions. I have drafted the disclosure requirements to require the disclosure of major classes of non-exchange revenue, such as taxes, transfers, donation and fines. I do not believe this is requiring separate disclosure of revenue from non-exchange transactions, merely the major classes of such revenue. I would interpret the IPSAS such that if there was an immaterial class of revenue from non-exchange transactions, it could be included in “Other Revenue” along with immaterial classes of revenue from exchange transactions.

Please advise me if this section of the ED needs modification.

(e) Voluntary Services

The PSC directed that entities not be required or permitted to recognize voluntary services in the general purpose financial statements. Paragraph 5 is included in the scope section and notes that entities are not permitted to recognize voluntary services, but are encouraged to make disclosures about the extent of services received.

ACTION REQUIRED

The IPSASB is requested to provide the Staff with directions for completing the next draft of the Exposure Draft. In addition to the issues raised above, members should raise any additional issues from the exposure draft.

Matthew Bohun
TECHNICAL MANAGER

This Exposure Draft was approved by the International Public Sector Accounting Standards Board of the International Federation of Accountants.

ACKNOWLEDGMENT

This International Public Sector Accounting Standard deals with the impairment of non-cash-generating assets in the public sector. This Standard is partially drawn from IAS 18, "Revenue" which was published by the International Accounting Standards Board (IASB). Extracts from International Accounting Standard IAS 18 (2004), "Revenue" are reproduced in this publication of the International Public Sector Accounting Standards Board of the International Federation of Accountants with the permission of the International Accounting Standards Committee Foundation (IASCF).

The approved text of the IFRSs is that published by the IASB in the English language, and copies may be obtained directly from IASCF Publications Department, 30 Cannon Street, London EC4M 6XH, United Kingdom.

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Information about the International Federation of Accountants and copies of this Standard can be found at its internet site, <http://www.ifac.org>.

The approved text of this Exposure Draft is that published in the English language.

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Commenting on this Exposure Draft

This Exposure Draft of the International Federation of Accountants was prepared by the International Public Sector Accounting Standards Board. The proposals in this Exposure Draft may be modified in the final Standard in the light of comments received before being issued in the form of an International Public Sector Accounting Standard.

Comments should be submitted in writing so as to be received by Month XX 200X. E-mail responses are preferred. Unless respondents to Exposure Drafts specifically request confidentiality, their comments are a matter of public record once a Standard has been issued. Comments should be addressed to:

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INTRODUCTION

Accounting Standards for the Public Sector

The International Federation of Accountants' International Public Sector Accounting Standards Board (IPSASB) develops accounting standards for public sector entities referred to as International Public Sector Accounting Standards (IPSASs). The IPSASB recognizes the significant benefits of achieving consistent and comparable financial information across jurisdictions and it believes that the IPSASs play a key role in enabling these benefits to be realized.

The IPSASB issues IPSASs dealing with financial reporting under the cash basis of accounting and the accrual basis of accounting. The accrual basis IPSASs are based on the International Financial Reporting Standards (IFRSs), issued by the International Accounting Standards Board (IASB), where the requirements of those Standards are applicable to the public sector. They also deal with public sector specific financial reporting issues that are not dealt with in IFRSs.

The adoption of IPSASs by governments will improve both the quality and comparability of financial information reported by public sector entities around the world. The IPSASB recognizes the right of governments and national standard-setters to establish accounting standards and guidelines for financial reporting in their jurisdictions. The IPSASB encourages the adoption of IPSASs and the harmonization of national requirements with IPSASs. Financial statements should be described as complying with IPSASs only if they comply with all the requirements of each applicable IPSAS.

Due Process and Timetable

An important part of the process of developing IPSASs is for the IPSASB to receive comments on the proposals set out in these Exposure Drafts from governments, public sector entities, auditors, standard setters and other parties with an interest in public sector financial reporting. Accordingly, each proposed IPSAS is first released as an Exposure Draft, inviting interested parties to provide their comments. Exposure Drafts will usually have a comment period of four months, although longer periods may be used for certain Exposure Drafts. Upon the closure of the comment period, the IPSASB will consider the comments received on the Exposure Draft and may modify each proposed IPSAS in the light of the comments received before proceeding to issue a final Standard.

Purpose of the Exposure Draft

This Exposure Draft proposes to establish requirements for the recognition, measurement and disclosure of revenue from non-exchange transactions.

Request for Comments

Comments are invited on any proposals in this Exposure Draft by Month XX, 200X. The Committee would prefer that respondents express a clear overall opinion on whether the Exposure Draft in general is supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the issues in the Exposure Draft. Respondents are also invited to provide detailed comments indicating the specific paragraph number or groups of paragraphs to which they relate, clearly explaining the issue and suggesting alternative wording, with supporting reasoning, where this is appropriate.

Specific Matters for Comment

The Committee would particularly value comment on the proposals to:

(a)

(b)

[Specific Matters for Comment will be included as part of the final stage of the development of the ED]

International Public Sector Accounting Standard

IPSAS XX

Revenue from Non-Exchange Transactions

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C. Basis for Conclusions

COMPARISON WITH IAS 18 (2004)

International Public Sector accounting Standard XX, “Revenue from Non-Exchange Transactions” (IPSAS XX) is set out in paragraphs 1 – nn and the Appendix. All the paragraphs have equal authority. IPSAS XX should be read in the context of its objective, the Basis for Conclusions (if any), and the “Preface to the International Public Sector Accounting Standards”. IPSAS 3, “Accounting Policies, Changes in Accounting Estimates and Errors” provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

International Public Sector Accounting Standard

IPSAS XX

Revenue from Non-Exchange Transactions

Objective

1. The objective of this Standard is to prescribe the accounting treatment of revenue arising from non-exchange transactions and events, and disclosures to be made in relation to such revenue.

Scope

2. **An entity which prepares and presents financial statements under the accrual basis of accounting shall apply this Standard in accounting for revenue from non-exchange transactions.**
3. **This Standard applies to all public sector entities other than Government Business Enterprises (GBEs).**
4. This Standard deals with revenue arising from non-exchange transactions. It does not deal with revenue arising from exchange transactions, which are dealt with in other IPSASs, such as IPSAS 9, “Revenue from Exchange Transactions”. Public sector entities may derive revenues from exchange or non-exchange transactions. Governments and other public sector entities typically derive the majority of their revenues from non-exchange transactions such as:
 - (a) Taxes;
 - (b) Transfers;
 - (c) Fines; and
 - (d) Donations.

Voluntary Services

5. Many public sector entities are recipients of voluntary services. For example a rural municipality may operate a volunteer fire brigade, or a public hospital may receive the services of volunteers to distribute food to patients. This standard does not permit entities to recognize revenue in respect of voluntary services. Entities are encouraged to disclose in the notes to the general purpose financial statements the extent of any voluntary services received.

Government Business Enterprises

6. The *Preface to International Financial Reporting Standards* issued by the International Accounting Standards Board (IASB) explains that International Financial Reporting Standards (IFRSs) are designed to apply to the general purpose financial statements of all profit-oriented entities. GBEs are profit-oriented entities, accordingly, they are required to comply with IFRSs.

Definitions

7. The following terms are used in this Standard with the meanings specified:

Assets are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.

A **condition** is a stipulation that specifies that transferred assets must be returned to the donor if not deployed as specified or if a specified future event occurs or does not occur.

A **compound transaction** is one in which two or more separately identifiable transactions are settled net by a single payment.

A **contingent asset** is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

A **contingent liability** is:

- (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or
- (b) a present obligation that arises from past events but is not recognized because:
 - (i) it is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or
 - (ii) the amount of the obligation cannot be measured with sufficient reliability.

Control of an asset arises when the entity can use or otherwise benefit from the asset in pursuit of its objectives and can exclude or otherwise regulate the access of others to that benefit.

An **exchange transaction** is a transaction in which one entity receives assets or services, or has liabilities extinguished, and directly gives

approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange.

Expenses paid through the tax system are items that are available to beneficiaries regardless of whether or not they pay taxes.

A non-exchange transaction is a transaction that is not an exchange transaction. 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.

A restriction is a stipulation that limits or directs the purposes for which a transferred asset may be used, but does not specify that the asset must be returned to the donor if not deployed as specified.

Revenue is the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from a controlling entity/owners/members.

A stipulation is a term, in legislation or a legally binding agreement, imposed upon the use of a transferred asset by entities external to the reporting entity.

Tax expenditures are preferential provisions of the tax law that provide taxpayers with concessions that are not available to others.

A time requirement is a stipulation that prohibits the use of a transferred asset until a specified point in time.

Terms defined in other International Public Sector Accounting Standards are used in this Standard with the same meaning as in those other Standards and are reproduced in the Glossary of Defined Terms published separately.

Non-Exchange Transactions

8. Non-exchange transactions often provide the major source of government revenue, in particular taxation revenue. In distinguishing between exchange and non-exchange transactions, the substance rather than the form of the transaction should be considered. For example, the sale of goods is normally classified as an exchange transaction, however if the transaction is conducted at a subsidized price, that is a price that is not approximately equal to the fair value of the goods sold, that transaction falls within the definition of a non-exchange transaction. In determining whether the substance of a transaction is that of a non-exchange or an exchange transaction, entities exercise professional judgment.
9. Entities frequently receive discounts or other reductions in the price of assets for a variety of reasons. These reductions in price do not mean that the transaction is a non-exchange transaction. In many instances market forces or regulations mean that a public sector entity will always pay a

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lower price than other market participants because the government is the largest participant in the market, or the government's ability to raise taxes reduces the public sector's risk as counterparty. Notwithstanding the discount, in these cases the exchange between the parties is at approximately fair value.

Revenue

10. Revenue includes only the gross inflows of economic benefits or service potential received and receivable by the entity on its own account. Amounts collected as an agent of the government or another government organization or on behalf of other third parties, for example the collection of tax payments by the taxation agency on behalf of the government, are not economic benefits or service potential which flow to the tax agency and do not result in increases in assets or decreases in liabilities of the tax agency. Therefore, they are excluded from revenue of the tax agency. Similarly, in a custodial or agency relationship, the gross inflows of economic benefits or service potential include amounts collected on behalf of the principal and which do not result in increases in net assets/equity for the entity. The amounts collected on behalf of the principal are not revenue. Instead, revenue is the amount of any amount received or receivable for the collection or handling of the gross flows.
11. In the public sector many entities receive inflows of revenue primarily from controlling entities/owners/members, either as transfers, loans or as contributions from controlling entities/owners/members. Such inflows that satisfy the requirements of paragraph 22 are recognized as contributions from controlling entities/owners/members. Where a binding loan agreement is in place the entity recognizes the inflow as a loan. Other inflows are recognized as revenue.
12. The definition states that revenue is the "gross inflow" of resources. In many instances there will be costs associated with the revenue, for example, a government will incur costs to administer a taxation system in order to raise tax revenue. These costs are recognized separately from the revenue in the general purpose financial statements.

Recognition Revenue Arising from Non-Exchange Transactions

13. For revenue from non-exchange transactions to be recognized, an entity must experience an increase in net assets as a result of that non-exchange transaction. This approach requires entities to analyze each transaction to determine which elements of general purpose financial statement must be recognized as a result of the transaction. In practice, entities experience large volumes of identical transaction, and will only analyze the first instance, applying the analysis to all subsequent transactions. For example,

a government will process many millions of income tax transactions, but as they are all identical, one analysis applies to all transactions.

Assets and Revenue

14. To recognize assets arising as a result of a non-exchange transaction all the elements in paragraph 15 must be satisfied. The definition of an asset requires that there be a past event that has resulted in the entity obtaining control of the asset. This past event will vary with each type of transaction. For taxation revenue, the past event will be that event that the taxing authority, for example the legislature, has determined will be subject to tax. The past event indicates the earliest point in time that the entity can recognize an asset. In addition to the past event the entity must control the asset, and it must be probable that the future economic benefits or service potential will flow to the entity.
15. **An inflow of resources from a non-exchange transaction shall be recognized as an asset when:**
 - (a) **It meets the definition of an asset;**
 - (b) **It is probable that the future economic benefits or service potential associated with the asset will flow to the entity; and**
 - (c) **The fair value of asset to the entity can be measured reliably.**
16. **If there is no present obligation in relation to an inflow of resources recognized as an asset, the entity shall recognize revenue in respect of the inflow of resources.**

Probable Inflow of Resources

17. An inflow of resources is “probable” when the inflow is more likely than not. The entity bases this determination on its past experience with similar types of flows of resources and its expectations regarding the counterparty. For example, if past experience has shown that once the national government announces a grant to a local government in its budget, the granted resources are transferred the resources to the local government, then the local government could conclude that any similarly announced grant will probably flow to the entity.
18. In some circumstances, entities announce their intention to transfer resources to a public sector entity, but do not fulfill this intention. For example, if a public school were destroyed by a forest fire and the national government announced its intention to provide funds to rebuild the school, but the legislature failed to appropriate the funds, the national government would be unable to fulfill its announced intention. In circumstances where this may occur, the potential recipient would not recognize the inflow as

probable, until subsequent events confirmed that the government's intention would be fulfilled.

Control of an Asset

19. The ability to exclude or regulate the access of others to the benefits of an asset is an essential element of control that distinguishes an entity's assets from those public goods that all entities have access to and benefit from. In the public sector, governments exercise a regulatory role over certain assets, for example financial instruments or bank accounts, which may enable the government to regulate access to those assets. This regulatory role does not necessarily mean that such regulated assets meet the definition of an asset, or satisfy the criteria for recognition as an asset in the general purpose financial statements of the government that regulates those assets.

Measurement of Revenue from Non-Exchange Transactions

20. **Revenue from non-exchange transactions shall be recognized at the fair value of the increase in net assets recognized by the entity.**
21. When an entity acquires assets through an exchange transaction, the assets are initially recognized at their cost. In a non-exchange transaction, if an entity's net assets increase, any cost to the entity does not reflect the value received.

Contributions from Controlling Entities/Owners/Members

22. **An inflow of resources shall be recognized as a contribution from controlling entities/owners/members when it is evidenced by any of the following:**
 - (a) **A formal designation of the transfer (or a class of such transfers) by the contributor or a controlling entity of the contributor as forming part of the recipient's contributed net assets/equity, either before the contribution occurs or at the time of the contribution;**
 - (b) **A formal agreement, in relation to the contribution, establishing a financial interest in the net assets/equity of the recipient which can be sold, transferred or redeemed; or**
 - (c) **The issuance, in relation to the contribution, of equity instruments which can be sold, transferred or redeemed.**
23. Public sector entities may be structured in a number of ways. Many jurisdictions adopt an arrangement whereby public sector entities are funded by means of transfers from a central government fund which the

individual entity will recognize as revenue. Individual entities in such jurisdictions will not normally recognize contributed net assets/equity in the statement of financial position. Other jurisdictions may adopt a quasi-corporate structure where there is provision for contributions directly to the net assets/equity of a public sector entity. In these jurisdictions, such contributions directly to the net assets/equity of a public sector entity are evidenced by any of the items in paragraph 22 and are recognized as contributions to net assets/equity in the statement of financial position.

24. Paragraph 22 specifies the form that contributions from controlling entities/owners/members takes, however, the entity also considers the substance of the transaction. If, despite the form of the transaction, the substance is clearly that of a loan or revenue, the entity recognizes it as such and makes an appropriate disclosure in the notes to the general purpose financial statements if material.

Taxes

25. **Inflows of resources resulting from taxes shall be recognized as assets and revenue when:**
- (a) **The taxable event has occurred;**
 - (b) **It is probable that an inflow of resources embodying future economic benefits or service potential will occur; and**
 - (c) **The fair value of the resources can be reliably measured.**
26. Taxes give rise to assets and revenue, which under this IPSAS should be recognized when the taxable event has occurred, it is probable that an inflow of resources embodying future economic benefits or service potential will occur, the fair value of which can be reliably measured. The taxable event is the past event that the government, legislature or other authority has determined will be subject to taxation.
27. Similar types of taxes are levied in many jurisdictions. The reporting entity needs to examine the taxation law in its own jurisdiction to determine what the taxable event is for the various taxes levied. Unless otherwise specified in legislation, it is likely that the taxable event for:
- (a) Income tax is the earning of assessable income during the taxation period by the taxpayer;
 - (b) Value added tax is the undertaking of taxable activity during the taxation period by the taxpayer;
 - (c) Goods and services tax is the purchase or sale of taxable goods and services tax during the taxation period;

- (d) Customs duty is the movement of dutiable goods or services across the customs boundary;
- (e) Death duty is the death of a person owning taxable property; and
- (f) Property tax is the passing of the date on which the tax is levied, or the period for which the tax is levied if the tax is levied on a periodic basis.

Measurement of Tax Assets

28. An inflow of resources embodying future economic benefits or service potential arising from the occurrence of a taxable event is recognized when the fair value of that inflow can be measured. For most taxes the entity will be able to reliably estimate the fair value of the inflow of resources in the reporting period in which the taxable event occurs. However, for some taxes, however, the entity will be unable to reliably measure the inflow of resources until cash or its equivalent is received. This may occur for example where tax is levied on the value of a deceased person's estate and the extent of the estate is not measurable for some considerable period of time due to disputes over ownership of assets or the fair value of some non-monetary assets.
29. Reliably measuring the assets, and therefore the revenue, accruing to the government at the time the taxable event occurs can be difficult for many governments. The nature of taxation systems is frequently such that some assets and revenue are difficult to measure due to such factors as:
 - (a) The tax law allowing taxpayers a longer period to file returns than the government is permitted for publishing general purpose financial statements;
 - (b) Taxpayers failing to file returns on a timely basis;
 - (c) Valuing non-monetary assets for tax assessment purposes;
 - (d) Complexities in tax law requiring extended period for assessing taxes due from certain taxpayers;
 - (e) The financial and political costs of rigorously enforcing the tax laws and collecting all the taxes legally due to the government may outweigh the benefits received; and
 - (f) A variety of circumstances particular to individual taxes and jurisdictions.
30. The difficulties associated with reliable measurement may mean that some asset and the related revenue cannot be recognized until some considerable time after the taxable event occurs, for example if a tax base is volatile and

estimation is not possible. In many cases, the assets and revenue may be recognized in the period subsequent to the occurrence of the taxable event. However, there are exceptional circumstances where several reporting periods will pass before a taxable event results in an inflow of resources embodying future economic benefits or service potential that meets the definition of an asset and satisfies the criteria for recognition as an asset.

Tax Expenditures and Expenses Paid Through the Tax System

- 31. Tax expenditures shall not be recognized as expenses in the statement of financial performance.**
- 32. Expenses paid through the tax system shall be recognized as expenses in the statement of financial performance, and the effect of any netting of tax revenue shall be reversed.**
33. In most jurisdictions, governments use the tax system to encourage certain financial behavior and discourage other behavior. For example, in some jurisdictions home owners are permitted to deduct mortgage interest and property taxes from their gross income when calculating tax assessable income. This concession is designed to encourage the population to purchase, rather than rent, their residence. These types of concessions are available only to taxpayers; if an entity (including a natural person) does not pay tax it cannot access the concession. In some instances, a combination of such concessions will enable a taxpayer to entirely eliminate its liability to pay tax – tax expenditures would not normally permit the entity to receive a payment from the government in respect of the negative tax, however, the negative tax liability may be carried forward to the following tax period. Tax expenditures are foregone revenue not expenses.
34. In some jurisdictions, the government uses the tax system as a convenient method of paying benefits to taxpayers, which would otherwise be paid using another payment method, such as writing a check or directly depositing the amount in a taxpayer's bank account, or settling another account on behalf of the taxpayer. For example, a government may pay part of residents' health insurance premiums, to encourage the uptake of such insurance, it may pay this amount by reducing the individual's tax liability, by making a check payment or by paying an amount direct to the insurance company. In these cases, the benefit is payable irrespective of whether the individual pays taxes. Consequently this amount is an expense of the government and should be recognized separately in the statement of financial performance. Tax revenue should be increased for the amount of any of these expenses paid through the tax system.

35. The key distinction between tax expenditures and taxes paid through the tax system is that for expenses paid through the tax system, the benefit is available to recipient entities irrespective of whether they pay taxes, or use a particular mechanism to pay their taxes. IPSAS 1, “Presentation of Financial Statements”, paragraph 55 prohibits the offsetting of items of revenue and expense unless permitted by another standard. This Standard does not permit the offsetting of tax revenue and expenses paid through the tax system.

Transfers

36. **Inflows of resources resulting from transfers shall be recognized as assets and revenue when:**
- (a) **The entity attains control of the transferred resources;**
 - (b) **The fair value of the resources can be measured reliably; and**
 - (c) **The entity has satisfied obligations arising from the transfer that have been recognized as a liability in accordance with paragraph 43.**
37. **As an entity satisfies a present obligation recognized as a liability in respect of an inflow of resources recognized as an asset, it shall reduce the carrying amount of the liability and recognize revenue.**
38. **An entity that recognizes an increase in net assets as a result of a non-exchange transaction shall recognize revenue in respect of that increase provided the increase is not a contribution from owners/controlling entities/of net assets/equity.**
39. “Transfer” is a term used to denote a variety of different transactions that occur in the public sector. Transfers include items such as grants, donations, appropriations, debt forgiveness and fines. All these items have the common attribute that they transfer resources from one entity to another without approximately equal consideration in exchange.
40. An entity obtains control of transferred resources either when the resources have actually been transferred to the entity, or the entity has a legally enforceable claim against the transferor. Many agreements to transfer resources become legally binding on all parties before the actual transfer takes place. Sometimes one entity promises to transfer resources, but fails to do so, consequently only when claims are legally enforceable, and the entity assesses that it is probable that the inflow of resources will occur will revenue be recognized.
41. An inflow of resources that is recognized as an increase in net assets and revenue is measured initially at its fair value. In non-exchange transaction

the cost of an item to the entity is not related to its fair value, therefore the entity recognizes the transaction at the fair value of the inflow of resources. Where the inflow is of cash or cash equivalents, determining fair value is not normally problematic, where the inflow is in the form of non-monetary assets, determining fair value may be more difficult. IPSAS 17, “Property, Plant and Equipment” and IPSAS 21, “Impairment of Non-Cash-Generating Assets” provide guidance on determining the fair value of non-monetary assets.

Present Obligation

42. In many cases it will be clear whether a past event has given rise to a present obligation. In other cases, for example if a donor and recipient are disagreement, it may be disputed whether certain events have occurred or whether those events result in a present obligation. In such cases, an entity determines whether a present obligation exists at the reporting date by taking account of all available evidence, including, for example, the opinion of experts. The evidence considered includes any additional evidence provided by events after the reporting date. On the basis of such evidence:
- (a) Where it is more likely than not that a present obligation exists at the reporting date, the entity recognizes a liability (if the recognition criteria in paragraph 44 are met); and
 - (b) Where it is more likely that no present obligation exists at the reporting date, the entity discloses a contingent liability, unless the possibility of an outflow of resources embodying economic benefits or service potential is remote.

Stipulations

43. **An entity shall analyze any and all stipulations attaching to an inflow of resources to determine whether those stipulations impose a present obligation on the entity that meets the definition of a liability and satisfies the criteria in paragraph 44 for recognition as a liability.**
44. **A present obligation arising from the inflow of resources from a non-exchange transaction recognized as an asset shall be recognized as a liability when:**
- (a) **It meets the definition of a liability;**
 - (b) **The entity has a present obligation (legal or constructive) as a result of a past event;**

- (c) **It is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; and**
- (d) **A reliable estimate can be made of the amount of the obligation.**

If these conditions are not met, no liability should be recognized.

45. An entity shall:

- (a) **Not recognize a liability in respect of a restriction;**
- (b) **Recognize a liability in respect of a condition; and**
- (c) **Not recognize a liability in respect of a timing requirement.**

46. In many instances, assets are transferred to public sector entities in non-exchange transactions pursuant to legislation or legally binding agreements that impose stipulations that they be used for particular purposes and or within particular time periods. This is frequently the case for transfers (including those resulting from appropriations and grants):

- (a) From national governments to provincial, state or local governments;
- (b) To governmental agencies that are created by legislation or statute to perform specific functions with operational autonomy, such as statutory authorities or regional boards or authorities; and
- (c) From donor agencies to governments or other public sector entities.

47. Stipulations may be imposed by a transfer agreement, by legislation or by some other binding authority. These stipulations may direct when or how the transferred resources may be deployed, and may impose penalties for non-compliance. Entities analyze the stipulations that attach to a transfer of resources to determine whether the stipulations are such that control of the asset is retained by the transferor, or whether the entity should recognize a liability in respect of the transfer. If analysis of the stipulations results in the entity concluding that it does not control the transferred resources, it does not recognize an increase in net assets or revenue. This Standard identifies three types of stipulation: condition, restriction and time requirement.

48. The definition of restriction in paragraph 7 states that restrictions do not require the return of the transferred asset if not deployed in accordance with the transfer legislation or agreement, therefore this Standard does not permit the recognition of a liability in respect of conditions. For example, a donor may give a public sector art gallery a painting stipulating that it be

held in perpetuity by the gallery, but does not specify what would happen if the gallery breached the agreement. The public sector gallery would conclude that it has no present obligation to sacrifice future economic benefits or service potential to satisfy the restriction because if it breached the restriction and sold or otherwise disposed of the painting, the agreement does not require the entity to sacrifice the sale proceeds.

49. As stated in the definition in paragraph 7, a condition requires the return of an asset if it is not deployed in accordance with the legislation or agreement. An entity analyzing the substance of an agreement containing a condition will conclude that it has a present obligation to sacrifice future economic benefits or service potential to satisfy the condition. For example, if a local government receives a grant from the national government to establish an elementary school within a three year period or return the grant money, the local government would recognize a liability until the school was established.
50. The definition of time requirements in paragraph 7 states that time requirements do not require the return of the transferred asset if it is not deployed in accordance with the transfer legislation or agreement. An entity analyzing the substance of an agreement containing time requirements is likely to conclude that it does not have a present obligation to sacrifice future economic benefits or service potential to satisfy the time requirements. For example, a local government may receive a grant in 20X1 to provide services to aged persons during the year 20X2, but does not specify what happens if the grant is spent earlier. The local government would likely conclude that it has no present obligation to sacrifice future economic benefits or service potential to satisfy the time requirements because if it breached the time requirements and used the granted asset in a different period, the legislation or grant agreement does not require the local government to return the transferred assets.
51. Paragraphs 45 to 50 are to be interpreted in the light of all the facts of particular transactions and a detailed analysis of the legislation or agreement transferring the assets. Some legislation and agreements are relatively simple and straightforward, however, in many instances, particularly where the transferred assets have substantial monetary value, the stipulations attached to the transfer are complex and a single piece of legislation or agreement may contain conditions, restrictions and time requirements relating to the same transferred asset. The entity examines the substance of the transaction and the legislation or agreement affecting the transaction, to determine whether it recognizes a liability. In some cases, the legislation or agreement is so complex that the entity will have recourse to legal experts to determine whether a liability exists. In other cases, it will only become apparent that a liability exists or does not exist

when a donor and recipient litigate legislation or an agreement in the courts.

Alternative Paragraphs if Timing Requirements are deemed liabilities.

45. (c) Recognize a liability in respect of timing requirements.

50. The definition of a time requirement in paragraph 7 states that a time requirement does not require the return of the transferred asset if it is not deployed in accordance with the transfer legislation or agreement. An entity analyzing the substance of an agreement or legislation containing a time requirement will conclude that it does not have a present obligation to sacrifice future economic benefits or service potential to satisfy the time requirement. However, notwithstanding that a time requirement does not require the return of the transferred asset in the event of a breach of the legislation or agreement, this Standard requires an entity to recognize a liability in respect of a time requirement. For example, a local government may receive a grant in 20X1 to provide services to aged persons during the year 20X2, but does not specify what happens if the grant is spent earlier. The local government would conclude that it has no present obligation to sacrifice future economic benefits or service potential to satisfy the time requirements because if it breached the time requirements and used the granted asset in a different period, the legislation or grant agreement does not require the local government to return the transferred assets. However, the local government entity will recognize a liability in respect of the timing requirement by virtue of this Standard.

52. If analysis of the stipulations results in the entity concluding that it has a present obligation to sacrifice future economic benefits or service potential to satisfy the stipulations imposed in respect of the inflow of resources it recognizes a liability in accordance with paragraph 44. If the entity concludes that the legislation or agreement imposes a condition or timing requirement it recognizes a liability in accordance with paragraph 45. As the entity satisfies the requirements of the stipulations, it reduces the liability and recognizes revenue. For example, a grant agreement may specify that the entity is required to construct a highway, when the resources are received or receivable, the entity recognizes an asset and a liability, as the highway is constructed, the entity reduces the liability and recognizes revenue.

Debt Forgiveness

53. Lenders will sometimes waive their right to collect a debt owed by a public sector entity, effectively canceling the debt. For example, a national government may cancel the debt owed by a local government. In other circumstances, a public sector entity's controlling entity may assume responsibility to satisfy the controlled entity's liabilities. For example a government may assume employee entitlement liabilities recognized by a government department. In such circumstances, the former debtor recognizes an increase in net assets because a liability it previously owed is extinguished.
54. A decrease, including extinguishment, in a provision recognized in accordance with IPSAS 19, "Provisions, Contingent Liabilities and Contingent Assets" is not debt forgiveness, but is recognized as a reversal of a provision in accordance with IPSAS 19. For example, if a public sector university recognizes a provision for decommissioning a nuclear research reactor it controls, and the government passes legislation assuming the obligation to decommission all such facilities, then the university will recognize a reversal of the provision recognized in accordance with IPSAS 19.
55. Entities recognize revenue in respect of debt forgiveness when the former debt no longer meets the definition of a liability or satisfies the criteria for recognition as a liability.

Fines

56. Fines are penalties imposed upon an entity by a court or a quasi-judicial body for violations of laws or administrative rules. Where a defendant reaches an agreement with a prosecutor that includes the payment of a penalty instead of being tried in court. Such a penalty payment is, in substance, a fine. In some jurisdictions law enforcement officials are able to impose fines on individuals considered to have breached the law, the individual will normally have the choice of paying the fine, or going to court to defend the matter. Fines normally require an entity to transfer a fixed amount of cash to the government. Fines are recognized as revenue when the receivable meets the definition of an asset and satisfies the criteria for recognition as an asset set out in paragraph 13.

Compound Transactions – The Components Approach

57. **An entity shall disaggregate compound transactions and recognize the components separately.**
58. Entities sometimes engage in multiple transactions with the same counterparty, in some circumstances the entity may choose, or be required,

to settle net with the counterparty. This Standard requires entities to disaggregate these transactions into their separate components and recognize each transaction separately in the general purpose financial statements. For example, if a public school charges students a mandatory fee that equates to ten percent of the fair value of the educational services provided, then that fee represents an exchange transaction for one tenth of the educational services provided, the balance of which are provided free of charge and do not generate revenue. A voluntary fee is more in the nature of a donation and is recognized as a transfer in accordance with this Standard.

59. Compound transactions typically involve an exchange and a non-exchange component. In some instances, such as that cited in the previous paragraph, the public sector entity provides more value than it receives, in others the situation is reversed. For example, a public hospital may organize a fund raising dinner, for which it sells tickets at CU1,000 per diner. If the fair value of the meal provided is CU50, the entity recognizes that amount as an exchange transaction, and the balance as a transfer.

Disclosures

60. **An entity should disclose:**

- (a) **The accounting policies adopted for the recognition of revenue from non-exchange transactions;**
- (b) **The amount of revenue recognized during the period from each of the significant category of non-exchange transactions recognized including revenue arising from:**
 - (i) **Taxes, disclosing separately major classes of taxes;**
 - (ii) **Transfers, disclosing separately each major source of transfer revenue;**
 - (iii) **Debt forgiveness; and**
 - (iv) **Fines.**
- (c) **For each significant category of revenue from non-exchange transactions, the basis on which fair value of the inflow of resources was determined.**
- (d) **The amount of liabilities recognized in respect of transfers of resources.**

Transitional Provisions

61. **Entities are not required to recognize revenue from non-exchange transactions on an accrual basis for reporting periods beginning on a date within five years following the date of first adoption of this Standard. Entities are encouraged to fully implement this Standard earlier.**
62. Entities that recognize and measure revenue from non-exchange transaction on a basis that is not consistent with the requirements in this Standard, may continue to use that basis for five years after adoption of this Standard. This transitional provision is intended to allow entities a period to develop reliable methods for measuring non-exchange transactions such as income taxes whilst still claiming compliance with IPSASs. It is anticipated that entities will apply this Standard incrementally to different classes of revenue from non-exchange transactions, for example, entities may apply this Standard to fine revenue in the first year of adoption, but not apply it to taxes on deceased estates until the fifth year of implementation.
63. **When an entity takes advantage of the transitional provision in paragraph 61 that fact should be disclosed. An entity shall disclose which classes of revenue from non-exchange transactions have been recognized in accordance with this Standard, and which have been recognized on another basis. When an entity takes advantage of the transitional provisions for a second or subsequent reporting period, details of the classes of revenue from non-exchange transactions that were recognized on another basis, but which are now recognized in accordance with this Standard should be disclosed.**

Effective Date

64. **An entity shall apply this International Public Sector Accounting Standard for annual periods beginning on or after Month XX, XXXX. Earlier application is encouraged. If an entity applies this Standard for an earlier period it shall disclose that fact.**
65. When an entity adopts the accrual basis of accounting, as defined by International Public Sector Accounting Standards, for financial reporting purposes, subsequent to this effective date, this Standard applies to the entity's annual financial statements covering periods beginning on or after the date of adoption.

Appendix

Amendments to Other IPSASs

Appendix B**Measurement of Revenue from Non-Exchange Transactions — Examples**

This appendix illustrates the application of the provisions of the Standard to assist in clarifying their meaning. It does not form part of the Standard. The facts assumed in these examples are illustrative only and are not intended to modify or limit the requirements of the Standard or to indicate the IPSASB's endorsement of the situations or methods illustrated. Application of the provisions of this Standard may require assessment of facts and circumstances other than those illustrated here.

[Examples will be included during the next stage of development.]

Appendix C

Basis for Conclusions

This appendix gives the IPSASB's reasons for supporting or rejecting certain solutions related to the accounting for revenue from non-exchange transactions. It also identifies circumstances in which the requirements of this IPSAS depart from the requirements of IAS 20 and the reasons for such departure. This Appendix does not form part of the Standard.

Introduction

C1.

Comparison with IAS 20 (Year)

International Public Sector Accounting Standard IPSAS XX, “Revenue from Non-Exchange Transactions” deals with the recognition of revenue from non-exchange transactions in the public sector. The main differences between IPSAS XX and International Accounting Standard IAS 18 (Year), “Accounting for Government Grants and Disclosure of Government Assistance” are as follows:

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