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Mr John Stanford
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Re: Response to Consultation Paper Accounting for Revenue and Non-Exchanges Expenses

Dear Mr Stanford,

The French Public Sector Accounting Standards Council (CNoCP) welcomes the opportunity to comment on the Consultation Paper *Accounting for Revenue and Non-Exchanges Expenses* published in August 2017.

The CNoCP welcomes the overall approach retained by the IPSASB that focuses on the features of transactions specific to the public sector. In that sense we would strongly recommend that the application of IFRS 15 *Revenue from Contracts with Customers* to relevant transactions in the public sector should be carefully and comprehensively thought through. IFRS 15 is effective as from 1 January 2018 in the private sector; hence as of now, no thorough feedback exists on its application. This makes it difficult to assess the impact and efficiency of its adaptation to the public sector.

On the other hand, the CNoCP understands the need to explore convergence with the principles set out for the private sector on revenue recognition. Because IFRS 15 was commented upon extensively as part of the IASB's process, we will not comment upon its merits or demerits as to

its application to category C transactions¹. We will rather focus on issues that could be raised if the performance obligation approach was retained to account for category B transactions².

In a context of increased attention to performance to evaluate public finance management, we would broadly agree that exploring an approach based on the identification of performance obligations within a transaction is conceptually sound. It provides for a framework that relies on the exercise of judgement. We would support that path forward as long as it allows for various transactions across jurisdictions to be accounted for in a relevant manner taking into account as many elements of context as possible. In that case, we would strongly advise that extensive application guidance should be available to constituents. Category B transactions should definitely be the focal point of future steps for that project.

As much as convergence is a key driver of IPSASs development, we however believe that IPSAS 23 still has merits, though it would need to be revised to ease its application. Current IPSAS 23 fails to provide pragmatic requirements on how to account for stipulations such as time requirements, namely in multi-year funding agreements; this leads to difficulties in identifying the revenue recognition point in time.

With respect to revenue from category A transactions³, we are of the view that a reliable measure of revenue should be a key factor of revenue recognition. This is why in France the government does not recognise estimated revenue from taxable income not fully known until a tax return is filed. Rather, the government recognises revenue upon reception of the tax return. We believe that this is a practical relief that bears a positive cost/benefit ratio while still providing relevant information on a year on year basis.

We would expect further work as to the articulation between conditions as in IPSAS 23 *Revenue from Non-Exchange Transactions* and performance obligations as in IFRS 15. We believe that the performance obligation approach would better reflect the Conceptual Framework's qualitative characteristics. From our standpoint, conditions refer to the legal form of the transactions rather than to its substance. However, before we can perform an in-depth analysis along these lines, we

¹ Category C transactions are transactions that involve the transfer of promised goods or services to customers as defined in IFRS 15, typically transactions similar to those in the private sector.

² Category B transactions are transactions that contain performance obligations (IFRS 15) or stipulations (IPSAS 23), but do not have all the characteristics of transactions within the scope of IFRS 15, typically capital grants.

³ Category A transactions are transactions that with no performance obligation or stipulation, typically taxes and transfers (non-exchange transactions).

would need further insight on the effects on the financial statements of a performance obligation approach on category B transactions.

Finally, we note that the Board decided, at the 2017 December meeting, to phase-in the whole project. They now propose three streams to the project on Revenue and two streams to the project on Non-Exchange Expenses. We understand that that new timeline is meant to fast track those streams where the Board can reach consensus quickly (namely on category A and C transactions), only to allow more time to explore the more complex category B transactions. However, we would recommend that the new requirements should be effective as a whole at one point in time rather than on a stream by stream basis; this is to ensure consistency of accounting treatments between the various categories of transactions once they all have been fully explored.

In that context, we decided that we would provide overall responses to the detailed questions set out in the Consultation Paper. We will expand further upon those points as the various project streams progress and as further consultation documents are published for public comments.

Yours sincerely,

Michel Prada

APPENDIX

Preliminary View 1 (following paragraph 3.8)

The IPSASB considers that it is appropriate to replace IPSAS 9 Revenue from Exchange Transactions, and IPSAS 11 Construction Contracts with an IPSAS primarily based on IFRS 15 Revenue from Contracts with Customers. Such an IPSAS will address Category C transactions that:

- (a) Involve the delivery of promised goods or services to customers as defined in IFRS 15;*
- and*
- (b) Arise from a contract (or equivalent binding arrangement) with a customer which establishes performance obligations.*

Do you agree with the IPSASB's Preliminary View 1? Please give your reasons

We understand that the objective of the new timeline for the Revenue project is to progress quickly on the accounting treatment for category C transactions that are similar to the private sector. However, we would like to stress upfront that category A transactions -and to a lesser extent category B transactions- are not only specificities of the public sector, but are also the most significant transactions in amounts and volumes. We believe that stating, in any communication on the progress of the project, that the Board is well aware of the relative significance of the transactions is critical to the public interest in the project.

We would agree with the IPSAS Board that convergence with IFRS 15 is the right way forward for the revenue recognition of those transactions that are similar to the private sector's because category C transactions are akin to revenue transactions in the private sector and because IPSASs are to converge with IFRSs, except in those instances where the public sector specificities call for departures from IFRSs. We also note that IFRS 15 was already extensively commented on as part of the IASB's due process.

However, we would question the timing of such a convergence project; IFRS 15 is indeed effective from 1 January 2018 and we are aware that private sector entities struggle with its implementation. We would rather the Board wait for implementation in the private sector to settle down before taking a convergence project onto the agenda. Areas of concerns in the private sector include the identification of performance obligations in construction contracts and the determination of the timing of revenue recognition. Unresolved implementation issues in the private sector are likely to arise in the public sector as well, all the more as the cost

benefit ratio is a prevalent constraint; this might be the case for defence construction contracts for instance.

Preliminary View 2 (following paragraph 3.9)

Because Category A revenue transactions do not contain any performance obligations or stipulations, the IPSASB considers that these transactions will need to be addressed in an updated IPSAS 23.

Do you agree with the IPSASB's Preliminary View 2? Please give your reasons.

IPSAS 23 currently requires revenue from category A transactions such as taxes to be recognised when the event giving rise to the taxation took place, as long as measurement is reliable. In several jurisdictions, part or all the amount of taxes to be collected will not be reliably measurable at the point in time when the event giving rise to those taxes occurs. That is mainly because the Inland Revenue department will know of those taxes to collect upon receiving tax payers' returns, only after the taxable event took place.

Therefore, an updated IPSAS 23 should focus on the ability to reliably measure the amount of taxes and on the consequences on the timing of recognition. This is an area of wide implementation issues across jurisdictions where preparers need detailed guidance.

However, because the approach for category B transactions will be addressed last, and because in some cases it might be unclear as to where the drawing line is between transactions with or without performance obligation, we would strongly recommend that the scope of category A transactions should be clearly defined and assessed on the basis of practical examples. There could be an argument that real transactions are a continuum ranging from no performance obligation at all to containing performance obligations. In addition, it could also be useful, in the public sector, to explore performance obligations as being satisfied by the transfer of control of service potential rather than that of economic benefits; as a consequence, one could question the need for different standards.

Specific Matter for Comment 1 (following paragraph 3.10)

Please provide details of the issues that you have encountered in applying IPSAS 23, together with an indication of the additional guidance you believe is needed in an updated IPSAS 23 for:

- (a) Social contributions; and/or*
- (b) Taxes with long collection periods.*

If you believe that there are further areas where the IPSASB should consider providing further guidance in and updated IPSAS 23, please identify these and provide details of the issues that you have encountered together with an indication of the additional guidance you believe is needed.

In France, the general principle for social contributions recognition is upon the realisation of the taxable event, actually in line with the general recognition principle in IPSAS 23. However, some contributions or taxes (it is not always easy to draw the line clearly between the two) remain based on a tax return by individuals or households because the reliable measurement criterion fails to be met. In those instances, and should an updated IPSAS 23 be retained, further guidance on the application of the general recognition principle would be needed.

With respect to taxes with long collection periods, we actually fail to see to what they would refer in practice in our jurisdiction. We would need further explanations as to what transactions are at stake here.

Preliminary View 3 (following paragraph 4.64)

The IPSASB considers that Category B transactions should be accounted for using the Public Sector Performance Obligation Approach.

Do you agree with the IPSASB's Preliminary View 3? If not, please give your reasons.

We would agree with Preliminary View 3 in that we believe that the performance obligation approach conceptually fits better the principle of substance over form than conditions or restrictions that are more of a legal nature. Stipulations are set out in an agreement while performance obligation requires a judgement call on a thorough analysis of the economic effects of a transaction.

Specific Matter for Comment 2 (following paragraph 4.64)

The IPSASB has proposed broadening the requirements in the IFRS 15 five-step approach to facilitate applying a performance obligation approach to Category B transactions for the public sector. These five steps are as follows:

Step 1 - Identify the binding arrangement (paragraphs 4.29 – 4.35)

Step 2 - Identify the performance obligation (paragraphs 4.36 – 4.46)

Step 3 - Determine the consideration (paragraphs 4.47 – 4.50)

Step 4 - Allocate the consideration (paragraphs 4.51 – 4.54)

Step 5 - Recognize revenue (paragraphs 4.55 – 4.58)

Do you agree with the proposals on how each of the IFRS 15 five-steps could be broadened?

If not, please explain your reasons.

While we agree in principle on how each of the IFRS 15 steps could be broadened, we would like to draw attention on the more practical aspect of implementing those steps by reference to the difficulties that private sector entities currently experience. We believe that steps 1 and 2 - that consist in identifying the performance obligation within an identified binding agreement- are critical issues that need to be addressed in priority.

In addition, we note that the step by step approach, while intellectually sound to help analyse a transaction, might also prove to be more fastidious to implement as judgement will have to apply to all and every step.

We understand further research will be performed on that very subject and we will closely follow-up and comment on future developments.

Specific Matter for Comment 3 (following paragraph 4.64)

If the IPSASB were to implement Approach 1 and update IPSAS 23 for Category B transactions, which option do you favor for modifying IPSAS 23 for transactions with time requirements (but no other stipulations):

- (a) Option (b) – Require enhanced display/disclosure;*
- (b) Option (c) – Classify time requirements as a condition;*
- (c) Option (d) – Classify transfers with time requirements as other obligations; or*
- (d) Option (e) - Recognize transfers with time requirements in net assets/ equity and recycle through statement of financial performance.*

Please explain your reasons.

We note that if time requirements were considered conditions as in option (c), the application of IPSAS 23 would lead to the recognition of an asset and a liability that would be settled overtime, hence providing for overtime recognition of revenue. While we would agree on the overtime recognition of revenue that is in line with current practice in our jurisdiction, we would express reservations as to the additional burden to the statement of financial position as long as cash hasn't been received.

Before we can explore further the accounting for time requirements, we would like to get more insights as to the effects on a mirror approach between revenue and expenses. Also, we do not have practical examples in our jurisdiction of agreements containing time requirements only; there are always other stipulations such as the implicit existence of the entity.

In addition, we observe that the fact that time requirements are difficult to classify as conditions or restrictions is a reason why the performance obligation approach would need to be further explored for category B transactions.

Finally, we note that (c) is inconsistent with the Conceptual Framework and that (e) would require the introduction of the concept of Other Comprehensive Income (OCI).

Specific Matter for Comment 4 (following paragraph 4.64)

Do you consider that the option that you have identified in SMC 3 should be used in combination with Approach 1 Option (a) – Provide additional guidance on making the exchange/non-exchange distinction?

(a) Yes

(b) No

Please explain your reasons.

Because the definition of an asset includes a reference to the service potential as well as to the economic benefits, the distinction exchange/non-exchange seems artificial in the public sector.

Preliminary View 4 (following paragraph 5.5)

The IPSASB considers that accounting for capital grants should be explicitly addressed within IPSAS.

Do you agree with the IPSASB's Preliminary View 4? If not please give your reasons.

Capital grants are a major source of financing in the public sector in France. Because they serve the purpose of providing funds to entities to build or acquire long-term assets that will be mainly used to provide a service potential, and because they may take various forms, there is a need to address those transactions explicitly, both from the provider and the beneficiary perspectives.

Also, with a view to consistency with other IPSASs, it could be useful to explore instances where capital grants may take the form of concessionary loans.

In that sense we would agree on the phased-in new timeline for the whole project that would allow for more time to address category B transactions.

Specific Matter for Comment 5 (following paragraph 5.5)

(a) Has the IPSASB identified the main issues with capital grants?

If you think that there are other issues with capital grants please identify them.

(b) Do you have any proposals for accounting for capital grants that the IPSASB should consider?

Please explain your issues and proposals.

We believe that there are other issues with capital grants that the IPSAS Board should consider, for instance from the grantor's perspective, i.e. from the expense side. To illustrate the issue, in France, local authorities may grant subsidies to beneficiary entities for the acquisition or construction of long-term assets, controlled by the beneficiary entities, that serve a service potential as part of a specific public mission. Those subsidies are substantially equivalent to the direct acquisition or construction of the long-term assets by the grant provider; therefore, at the level of the individual reporting entity, grants provided are considered assets of the providing entity that generate service potential, as long as they meet strict recognition criteria.

Specific Matter for Comment 6 (following paragraph 5.9)

Do you consider that the IPSASB should:

(a) Retain the existing requirements for services in-kind, which permit, but do not require recognition of services in-kind; or

(b) Modify requirements to require services in-kind that meet the definition of an asset to be recognised in the financial statements provided that they can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information; or

(c) An alternative approach.

Please explain your reasons. If you favor an alternative approach please identify that approach and explain it.

In our jurisdiction, services in-kind are recognised only if they can be measured reliably. However, we haven't explored that issue further yet in the context of the Consultation Paper.

The new phase-in of the project will probably allow providing additional comments at a later stage.

Preliminary View 5 (following paragraph 6.37)

The IPSASB is of the view that non-exchange transactions related to universally accessible services and collective services impose no performance obligations on the resource recipient. These non-exchange transactions should therefore be accounted for under the Extended Obligating Event Approach.

Do you agree with the IPSASB's Preliminary View 5? If not, please give your reasons.

Notwithstanding the difficulties that may arise from the definition of the scope of the Social Benefits project with respect to universally accessible services, we believe that collective goods and services should be expensed as delivered and future expenses are not a present obligation of the public sector entities. Therefore, we would approve of any approach that would allow for the abovementioned accounting treatment.

Preliminary View 6 (following paragraph 6.39)

The IPSASB is of the view that, because there is no obligating event related to non-exchange transactions for universally accessible services and collective services, resources applied for these types of non-exchange transactions should be expensed as services are delivered.

Do you agree with the IPSASB's Preliminary View 6? If not, please give your reasons.

We agree.

Preliminary View 7 (following paragraph 6.42)

The IPSASB is of the view that where grants, contributions and other transfers contain either performance obligations or stipulations they should be accounted for using the PSPOA which is the counterpart to the IPSASB's preferred approach for revenue.

Do you agree with the IPSASB's Preliminary View 7? If not, please give your reasons

From the perspective of developing consistent mirror approaches, we would agree that the PSPOA is the way forward. However, at this stage of the project, we would need further understanding of how the performance obligation would apply on the revenue side before we can reach an informed decision on the PSPOA.

Preliminary View 8 (following paragraph 7.18)

The Board considers that at initial recognition, non-contractual receivables should be measured at face value (legislated amount) of the transaction(s) with any amount expected to be uncollectible identified as an impairment.

Do you agree with the IPSAS's Preliminary View 8? If not, please give your reasons.

We agree with the use of face value at initial recognition of non-contractual receivables. However, we would not book impairment for uncollectible amount upon initial recognition. We would rather recognise impairment on an incurred loss model basis.

Preliminary View 9 (following paragraph 7.34)

The IPSASB considers that subsequent measurement of non-contractual receivables should use the fair value approach.

Do you agree with the IPSASB's Preliminary View 9? If not, please give your reasons.

As stated in our response to the above question, we recognise impairment at each reporting date based on face value at initial recognition. Therefore, we would not agree with final pronouncements requiring the use of fair value for subsequent measurement of non-contractual receivables.

Specific Matter for Comment 7 (following paragraph 7.46)

For subsequent measurement of non-contractual payables do you support:

- (a) Cost of Fulfillment Approach;*
- (b) Amortized Cost Approach;*
- (c) Hybrid Approach; or*
- (d) IPSAS 19 requirements?*

Please explain your reasons.

We would support a best estimate approach as in IPSAS 19.