

20 November 2017

Mr Warren Allen  
The Chief Executive  
External Reporting Board  
PO Box 11250  
Manners St Central  
Wellington  
6142

Dear Sir

**Requests to comment on Consultation Paper *Accounting for Revenue and Non-Exchange Expenses***

Thank you for the opportunity to comment on the above Consultation Paper.

We are making this submission to you to assist the New Zealand Accounting Standards Board (NZASB) with the above Consultation Paper. We are happy for you to publish our comments publically.

In responding we have addressed the specific questions for respondents in Appendix 1.

More information on BDO is provided in Appendix 2 to this letter.

We hope that our responses and comments are helpful. Should you wish to discuss any of the points we have raised please contact me ([michael.rondel@bdo.co.nz](mailto:michael.rondel@bdo.co.nz)) should you have any queries or require further information.

Yours faithfully,



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## Appendix 1 - Response to questions

### **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? If not, please give your reasons.

**Yes, we agree with Preliminary View 1.**

**Moving to revenue recognition based on IFRS 15 will assist with reducing divergence in accounting treatment between public benefit entities (PBEs) and for-profits here in New Zealand.**

### **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? If not, please give your reasons.

**Yes, we agree with Preliminary View 2.**

### **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 additional guidance in an 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.

**We have no comments on taxes with long collection periods.**

**In terms of social contributions, in the not-for-profit (NFP) sector we have seen significant divergence in practice when entities are receiving funds from the Crown to provide**

**services to members of the public. There is great confusion as to whether or not these social contributions are exchange or non-exchange in nature and thus whether they are in the scope of PBE IPSAS 9 or PBE IPSAS 23.**

**In discussing this issue with clients it is clear that they require significant additional guidance on the differences between exchange and non-exchange revenue, and would greatly benefit from having relevant illustrative examples included in this guidance.**

**We have not identified any other significant areas not covered (elsewhere) by the Consultation Paper.**

### **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.

**Yes, we agree as this approach will lead to consistency of revenue recognition with Category A and Category C transactions. In addition moving revenue recognition for Category B transactions to this approach will reduce divergence between the for-profit and PBE sectors in terms of revenue recognition methodology.**

**However, we do note that this approach will require a significant amount of education and application guidance (including relevant examples) as this approach requires a completely new approach to accounting for revenue than is currently applied.**

**We also note that this approach may be considered onerous for smaller Tier 2 NFP entities that do not have significant accounting resources or the funds to outsource the accounting requirements of their organisations.**

### **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 - Identifying the binding arrangement (paragraphs 4.29 – 4.35);

Step 2 – Identifying 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); and

Step 5 – Recognise 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.

**Yes, we agree with the proposals.**

**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 favour 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) – Recognise transfers with time requirements in net assets/equity and recycle through the statement of financial performance.

Please explain your reasons.

**We have discussed this issue in detail with a number of our NFP clients.**

**The vast majority of these clients would favour option (c). These entities believe that a time requirement stipulation results in a constructive obligation to ensure funds are expended in the specified period. Their operational activity is to ensure that revenues received are matched to the related expenses based on the stipulations of the grantor, and that is how they manage their operations and (if applicable) report to the relevant grantor.**

**These entities believe that option (c) would be easy to implement, cost effective, and would lead to consistency in the sector, even though this option is inconsistent with the IPSASB Conceptual Framework/ PBE Conceptual Framework and IPSAS/PBE Standards.**

**We would favour option (e) as it is a compromise to following a pure framework definition technical approach such as contained in Option (b).**

**It will allow entities to “defer” the revenue received from the Category B transactions in other comprehensive income and expense and recycle the revenue to surplus and deficit once the corresponding expenses are incurred, thus allowing entities to “match” the revenue with the corresponding expenses, which appears to be what is desired by these entities.**

**This option will likely require significant education to be provided as it is a more complex approach and the vast majority of entities in the NFP sector will not have been exposed to option (e) accounting before. However, some of the larger NFP entities that hold financial instruments in the available for sale category will be familiar with this accounting treatment concept and should be able to apply the concepts without significant effort.**

**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.

- a) **Yes, we agree. There is significant confusion as to the understanding of exchange versus non-exchange transactions and this has led to divergence in practice. Additional guidance is definitely required to explain the difference between exchange and non-exchange transactions if the IPSASB follows Approach 1.**

**In particular we would encourage the inclusion of specific illustrative examples for common scenarios in the NFP sector, as this will be of invaluable help, especially for the smaller Tier 2 NFP entities.**

**Preliminary View 4 (following paragraph 5.5)**

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

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

- Yes, we agree with Preliminary View 4.**

**Specific Matter for Comment 5 (following paragraph 5.5)**

- a) Has the IPSASB identified the main issues with capital grants?  
If you think 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 have not identified any other issues with capital grants and have no other proposals.**

**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 achieved the qualitative characteristics and takes account of the constraints on information; or
- c) An alternative approach.

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

**We believe that the IPSASB should follow approach (b). However, significant guidance (including relevant illustrative examples) will need to be provided to assist preparers with determining whether measurement can be made such that the qualitative characteristics are achieved.**

**This is an area where we have seen significant divergence in practice, which is not desirable.**

**In particular we have seen divergence in the accounting treatment of items such as:**

- peppercorn leases;
- loans of artwork for a set period for no consideration;
- secretarial services;
- accounting services

**which can lead to significantly different accounting results for similar entities.**

#### **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.

**Our clients have limited exposure to non-exchange transactions. The Extended Obligating Event Approach is complex and significant education will be required to assist preparers with compliance therewith.**

**From a New Zealand perspective, we would need more guidance on the likely impact of these requirements (if any) on the not-for profit sector if the IPSASB's proposals are adopted. Significant additional guidance will be required in the not-for-profit sector for non-exchange transactions.**

**Although we can see benefit, in principal, the IPSASB's preliminary view, we question whether preparers will encounter difficulty in differentiating between exchange and non-exchange expenditure, as they currently do for exchange and non-exchange revenue. We also question whether a better distinction re accounting treatment should rather be based on whether there is an ongoing performance obligation or not.**

**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, resource 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.

**Please refer to out comment under Preliminary View 5.**

**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.

**Please refer to out comment under Preliminary View 5.**

**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 IPSASB's Preliminary View 8? If not, please give your reasons.

**Yes, we agree with Preliminary View 8.**

**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.

**Yes, we agree with Preliminary View 9.**

**Specific Matter for Comment 7 (following paragraph 7.46)**

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

- a) Cost of Fulfilment Approach;

- b) Amortised Cost Approach;
- c) Hybrid Approach; or
- d) IPSAS 19 requirements?

Please explain your reasons.

**We support (a) as this approach will be relatively straight forward to apply.**



## **Appendix 2 - Information on BDO**

1. BDO New Zealand is a network of eleven independently owned accounting practices, with fifteen offices located throughout New Zealand.
2. BDO firms in New Zealand offer a full range of accountancy services, including business advisory, audit, taxation, risk advisory, internal audit, corporate finance, forensic accounting and business recovery and insolvency.
3. BDO in New Zealand has 89 partners and over 800 staff.
4. BDO firms throughout New Zealand have a significant number of clients in the not-for-profit sector.
5. Five BDO firms in New Zealand (BDO Auckland, BDO Christchurch, BDO Northland, BDO Waikato and BDO Wellington) are registered audit firms and thirteen audit partners are licensed auditors.
6. Internationally, BDO is the fifth largest full-service audit, tax and advisory firm in the world, with over 67,700 people in 1,401 offices across over 158 countries and territories.