Financial Reporting Advisory Board Paper

IFRS 15 Revenue from contracts with customers:

Work plan for implementation

Issue:	A paper was presented to the Board in November 2014 providing a high level summary of the Standard and initial stage 1 analysis of IFRS 15. Following discussion of the new Standard the Board concluded that there was a need for a working group of the Relevant Authorities to address the introduction of the Standard, and that presentation of a high level implementation plan for the next meeting would be useful to ensure that the necessary work was going to be undertaken. This paper provides an update on the progress of work undertaken by the Relevant Authorities, agreed next steps and a high level work plan towards implementation of the Standard in the public sector. HM Treasury and the other Relevant Authorities ask that the Board provide comment on and agree the forward work plan.
Impact on guidance:	No impact at this stage.
IAS/IFRS adaptation?	None proposed at this stage. This will be considered in a later paper to the Board. IAS 18 is applied without adaptation in the public sector.
Impact on WGA?	Not at this stage.
IPSAS compliant?	Current IPSAS is based on IAS 18 Revenue and consequently adoption of IFRS15 will not be fully IPSAS compliant until relevant IPSAS are updated.
Interpretation for the public sector context?	This will be revisited in a later paper to the Board.
Impact on budgetary regime?	No assessment as yet. This will be considered in a later paper to the Board.
Alignment with National Accounts	No assessment as yet. This will be considered in a later paper to the Board.
Impact on Estimates?	It is possible that there will be an impact on Estimates as the new IFRS has an impact on the timing and recognition of some revenues.
Recommendation:	HM Treasury and the other Relevant Authorities ask that the Board provide comment on and agree the forward work plan.
Timing:	No changes are expected to be made to the FReM until the 2017/18 financial year.

DETAIL

1. This paper provides an overview of work undertaken by the Relevant Authorities, agreed next steps and a high level work plan towards implementation of the Standard in the public sector.

Summary of IFRS 15 and initial view of public sector implications

2. The IASB issued IFRS 15 in May 2014 with an effective date for periods on or after the 1st January 2017, with EU endorsement currently expected in the second quarter of 2015.

3. The disclosure objective of the new Standard is to establish the application principles required for entities to report useful information to the users of financial statements to better understand the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. The disclosure requirements under the new Standard are more extensive than the current requirements included within IAS 18.

4. The core principle in IFRS 15 recognises revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services.

5. To recognise revenue the Standard sets out five steps:

   - Step 1 - Identify the contract(s) with the customer
   - Step 2 – Identify the performance obligations in the contract
   - Step 3 – Determine the transaction price
   - Step 4 – Allocate the transaction price
   - Step 5 - Recognise revenue when a performance obligation is satisfied

6. IFRS 15 also includes requirements for accounting for contract costs. The incremental costs of a contract must be recognised as an asset if the entity expects to recover those costs. However, those incremental costs are limited to the costs an entity would not have incurred if the contract had not been successfully obtained.

7. Whilst for many contracts in the public sector, the accounting for revenue will remain unchanged, for other contracts, including long-term service contracts, there may be changes to the timing and amount of revenue recognised, depending on how entities previously accounted for these contracts.

8. Possible areas where practice may change include:

   - sales with incidental obligations (e.g. equipment sales with maintenance agreements);
   - transfers of goods and services where there is no observable evidence of the stand-alone price of each of the goods and services;
   - licences of intellectual property;
   - situations where there is uncertainty about whether revenue should be recognised at a point in time or over time (e.g. development of a service provided over time or a good transferred on completion);
   - estimates where consideration is variable; and
   - situations where customers pay in advance or arrears and financing of the contract needs to be considered.

9. Public sector budgetary implications may arise due to a potential change to the timing and recognition of some revenues. Where contacts include a variable consideration, this is measured at either expected value (i.e. probability-weighted amount) or the most likely amount, depending on which is the best predictor of the amount of consideration to which the entity is entitled). Further analysis will consider budgetary considerations in more depth.

Initial planning and next steps

10. The Relevant Authorities including HM Treasury, Monitor, Department of Health, CIPFA, and the Department of Finance and Personnel Northern Ireland convened to consider the implementation of the Standard and to agree next steps. HM Treasury are leading on the coordination of this exercise but with significant and meaningful contributions particularly from the Relevant Authorities in the health sector, owing to the expectation that this sector will experience the most significant impact. All Relevant Authorities have agreed to contribute to ensure a coherent, joined up view on the approach to adopting and implementing the standard. This work plan will mirror the timetable for the adoption of IFRS 9 Financial Instruments.

11. Initial analysis of the Standard has identified that there is unlikely to be a significant impact on local authorities due to their main sources of income being non-exchange transactions ie grants, council tax and business rates. Impact is most likely to be seen in the health sector due to the nature of the internal market and the 'Standard Contract' (which forms the basis of contracts between provider trusts and commissioners).

12. In the health sector, the calculation of revenue may differ at a functional level although ultimately such differences will need to be eliminated at group level. The key issues for the health sector to review are those items that define how its internal market operates: specifically, the 'Standard Contract' and the Tariff regime. The Department of Health and Monitor are developing a work programme for health to work with the Department's national bodies and other professionals, to feed into the HM Treasury timetable and working group set out in this paper.

13. More generally, the agreed approach across the Relevant Authorities is to focus on long-term material revenue contracts and the impact of the Standard on the measurement and recognition points in these.

14. Next steps in the programme of impact assessment include:

    a. Securing external technical assistance;

    b. Creation of a technical working group; and

    c. Scoping the public sector landscape.

Securing external technical assistance

15. The Relevant Authorities aim to secure external technical assistance to take advantage of existing experience of planning for implementation of the Standard in the private sector. This will provide a starting point to consider potential factors which may similarly impact on public sector financial reporting entities. It will further assist the Relevant Authorities in identifying and confirming what information needs to be obtained and clarified with public sector

entities during the initial informal consultation over the summer of 2015. The Board are asked to suggest sources of external technical assistance for this project.

Creation of a technical working group

16. The Relevant Authorities will establish a technical working group with representatives from each Relevant Authority and external assistance (as above). The group will set out its terms of reference but will have an initial focus on shaping the consultation to be undertaken over summer 2015, including identify key issues within the Standards that may be important for public sector reporting entities and around the potential burden of implementation.

Scoping the public sector landscape

17. Surveying the departmental and sector landscape will be an important part of an initial impact assessment. The main aims would be to identify the key players for whom the Standard is likely to have the most significant impact, and to more fully understand the current scope of contractual revenue streams and existing accounting practice. The shape of this exercise will be informed by the initial work of the technical working group.

18. Each Relevant Authority will approach their own sectors through an informal consultation, using the most suitable mechanism to them in targeting the required public sector audience. HM Treasury plans to utilise a 'Finance Director letter' from the Deputy Director of Government Financial Reporting. This is considered to be the best instrument to achieve participation in the exercise.

19. The Relevant Authorities agree that it will be important to consult stakeholders early in the process to help identify any potentially significant financial management implications.

20. Following this consultation exercise over the summer, representatives from some of the bodies most affected will be identified and encouraged to bring the issues raised to the technical working group. The use of external assistance at this point may also be valuable in understanding and scoping what interpretations or adaptations for the public sector are genuinely needed.

21. The Relevant Authorities will also consider, through the scoping exercise, the potential financial management implications of implementing the Standard after future year budget settlements have been agreed.

High level work plan and FRAB updates

22. A high level work plan with practical steps towards implementation has been agreed between the Relevant Authorities in the following timeframe:

- March 2015 – Paper on high level work plan to the FRAB
- Spring 2015 – Creation of technical working group (with external assistance)
- Summer 2015 – Initial consultation with public sector stakeholders as part of scoping exercise
- November 2015 – Technical paper to FRAB detailing implications across the public sector and intitial consideration of any interpretations or adaptations (if required)

- March 2016 – Second paper to FRAB addressing any relevant issues and points of clarification, and proposed Exposure Draft

- Summer 2016 – Exposure draft issued inviting comment from stakeholders

- November 2016– Paper to FRAB seeking agreement to adopt the standard on the basis of the Exposure Draft (in light of consultation), with implementation in the 2017/18 FReM.

- January 2017 – IFRS implementation date

- 2017-18 FReM – UK public sector implementation of IFRS 15

Proposed text for the Government Financial Reporting Manual

23. Relevant amendments including any interpretations or adaptations will be drafted for consideration for the 2017-18 FReM.

Recommendation

24. HM Treasury and the other Relevant Authorities ask that the Board provide comment on and agree the high level forward work plan.

HM Treasury

26 March 2015