

8 August 2016

GOVERNMENT FINANCIAL REPORTING MANUAL  
(FReM) EXPOSURE DRAFT NO:

(16)02

EXPOSURE DRAFT OF PROPOSED

AMENDMENTS TO THE FReM

Application of IFRS 15 *Revenue from contracts  
with customers*

Comments to be received by 30 September 2016



HM TREASURY

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# 1 Introduction

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**1.1** The Government Financial Reporting team, HM Treasury, has published this exposure draft of proposed amendments to the Government Financial Reporting Manual (FReM) as part of the ongoing work in ensuring that the FReM reflects the latest developments in financial reporting.

**1.2** The proposed amendments to the FReM are published by HM Treasury for comment only. The proposals may be modified in the light of comments received through this consultation process before being presented to the Financial Reporting Advisory Board (FRAB) for its approval. Final proposals approved by the FRAB will be published as amendments to the FReM from the proposed effective date.

## Structure of exposure draft

**1.3** The exposure draft provides details for each FReM chapter for which an amendment is proposed. Each section includes:

- an explanation of why the amendment is proposed
- when necessary any specific additional questions unique to that proposed amendment
- the paragraphs of the FReM chapter that are affected by the proposed amendment
- the proposed effective date of each proposed amendment

## Invitation to comment

**1.4** HM Treasury invites comments on the proposed amendments. It would particularly welcome responses to the questions set out in Chapter 2. Comments are most helpful if they:

- respond to the question as stated
- indicate the specific paragraph or paragraphs to which they relate
- contain a clear rationale
- describe any alternative HM Treasury should consider

**1.5** Comments on this exposure draft should be submitted in writing so as to be received by **30 September 2016**. Respondents are asked to send their comments electronically to [FReM.consultation@hmtreasury.gsi.gov.uk](mailto:FReM.consultation@hmtreasury.gsi.gov.uk).

**1.6** All responses will be published on the gov.uk website unless the respondent requests confidentiality.

**1.7** HM Treasury will consider all comments received in writing by 30 September 2016. In considering the comments, HM Treasury will base its conclusions on the merits of the arguments for and against each alternative, not on the number of responses supporting each alternative.



## 2 General Questions

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### Question 1

Do you agree with the proposed amendments to the accounting for revenue in the FReM to reflect the principles of IFRS 15? If so, why? If not, why not and what alternatives do you propose?

### Question 2

Does your entity expect to recognise assets under IFRS 15 that will not be within the scope of another Standard? If so, what are these assets?

### Question 3

Do you agree with the transition approach for the proposed amendments? If so, why? If not, why not and what alternatives do you propose?

### Question 4

Do you agree with the proposed effective date for the public sector implementation of IFRS 15? If so, why? If not, why not and what alternatives do you propose?

### Question 5

Do you agree with the decision to not adapt the disclosure requirements for the proposed amendments? If so, why? If not, why not and what alternatives do you propose?

### Question 6

Do you agree there should be no changes to the principles of accounting for taxes and duties and fines and penalties? If so, why? If not, why not, and what alternative do you propose?



## 3 Overview of IFRS 15

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**3.1** The International Accounting Standards Board (IASB) issued IFRS 15 *Revenue from Contracts with Customers* in May 2014. This replaces IAS 18 *Revenue*, IAS 11 *Construction Contracts* and related Interpretations. The IASB issued *Clarifications to IFRS 15* in April 2016 to address implementation questions that were discussed by the Joint Transition Resource Group for Revenue Recognition<sup>1</sup>. The clarifications were intended to reduce diversity in practice when the Standard is adopted and decrease the cost and complexity of applying it.

**3.2** The IASB recognised that revenue is an important number to users of financial statements in assessing an entity's financial performance and position. However, previous revenue recognition requirements in IFRS provided limited guidance and, consequently, the two main revenue recognition Standards, IAS 18 and IAS 11, could be difficult to apply to complex transactions. In addition, IAS 18 provided limited guidance on many important revenue topics such as accounting for multiple-element arrangements.

**3.3** The IASB and the US national standard setter, the Financial Accounting Standards Board (FASB), initiated a joint project to clarify the principles for recognising revenue that would:

- remove inconsistencies and weaknesses in previous revenue requirements
- provide a more robust framework for addressing revenue issues
- improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets
- provide more useful information to users of financial statements through improved disclosure requirements
- simplify the preparation of financial statements by reducing the number of requirements to which entities must refer

**3.4** The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity recognises revenue in accordance with that core principle by applying the following steps:

- a Step 1: Identify the contract(s) with a customer
- b Step 2: Identify the performance obligations in the contract
- c Step 3: Determine the transaction price
- d Step 4: Allocate the transaction price to the performance obligations in the contract
- e Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

**3.5** The Standard also includes a cohesive set of disclosure requirements that would result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts with customers.

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<sup>1</sup> <http://www.ifrs.org/About-us/IASB/Advisory-bodies/Joint-Revenue-Transition-Resource-Group/Pages/Home.aspx>



**3.6** IFRS 15 is a residual Standard i.e. it is applied when there are no requirements from other Standards. As well as revenue from leases (IAS 17/IFRS 16), insurance contracts (IFRS 4) and financial instruments (IAS 39/IFRS 9), IFRS 15 does not apply to non-exchange transactions.

**3.7** Entities may apply the Standard to a portfolio of contracts (or performance obligations) with similar characteristics. This is on the basis that an entity reasonably expects that the effects on the financial statements of applying IFRS 15 to the portfolio would not differ materially from applying the Standard to the individual contracts (or performance obligations) within that portfolio.

**3.8** IFRS 15 has an effective date of 1st January 2018. After the IASB has published a new standard the European Union (EU) has a formal process for adoption. The European Commission (EC) requests endorsement advice<sup>2</sup> from the European Financial Reporting Advisory Group (EFRAG) and based on this advice the EC prepares a draft Endorsement Regulation. This Regulation is adopted only after a favourable vote of the Accounting Regulatory Committee (ARC) and favourable opinions of the European Parliament and the Council of the European Union. Following adoption, the Regulation is published in the Official Journal of the European Union, at which time it becomes effective. EFRAG have provided their advice to the European Commission and the Accounting Regulatory Committee have voted positively. The endorsement from the Commission is expected in the third quarter of 2016. The clarifications are expected to be endorsed in the first quarter of 2017.

**3.9** The FReM applies EU adopted IFRS consistent with the requirements of the Government Resource Accounts Act 2000. This means HM Treasury currently expects the new standard to be applied in central government from 2018-19.

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<sup>2</sup> <http://www.efrag.org/Endorsement>

# 4 Applicability of IFRS 15 for public sector reporting entities

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## Introduction

**4.1** With £659.3 billion revenue disclosed in the 2014-15 Whole of Government Accounts<sup>1</sup>, revenue is material within the public sector. £566.7 billion relates to taxation revenue that is obtained primarily by HM Revenue and Customs. The remaining £92.6 billion relates to the sales of goods and services and other revenue by central government, local government and public corporations.

**4.2** The Financial Reporting Advisory Board (FRAB) agreed the high level work plan for the implementation of IFRS 15 in public sector entities in March 2015<sup>2</sup>. The work plan included the creation of a cross-government technical working group, the use of professional accountancy firms to provide technical expertise to the technical working groups and an initial impact assessment undertaken by the Relevant Authorities to scope the landscapes of the various sectors.

**4.3** This section details the discussions of the FRAB, technical working group and initial impact assessment and from these, HM Treasury's proposals for the application of IFRS 15 in the public sector. HM Treasury will continue to review implementation issues in the private sector and consider any corresponding impacts in the public sector.

**4.4** The structure of this section is as follows:

- Five steps
- Contract costs
- Transition
- Implementation
- Disclosures
- Consolidated Fund revenue
- Whole of Government Accounts

## Step 1: Identifying the contract

**4.5** In order for a contract to be within the scope of IFRS 15, all of the following criteria must be met:

- 1 The parties have approved the contract (in writing, orally or in accordance with their customary business practices) and are committed to perform their respective obligations;

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<sup>1</sup> <https://www.gov.uk/government/publications/whole-of-government-accounts-2014-to-2015>

<sup>2</sup> <https://www.gov.uk/government/publications/financial-reporting-advisory-board-minutes-and-associated-papers-17-march-2016>

- 2 The entity can identify each party's rights regarding the goods and services to be transferred;
- 3 The entity can identify the payment terms;
- 4 The contract has commercial substance (i.e. the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and
- 5 It is probable the entity will collect the consideration to which it will be entitled.

**4.6** IFRS 15 (para 15) offers criteria to recognise revenue where the above criteria are not met and consideration is received. The Standard requires there to be a) no further performance obligations to transfer goods or services or b) the contract is terminated. Under both (a) and (b) the consideration is deemed non-refundable.

**4.7** Discussions on the applicability of this step in the public sector have considered a wide range of revenue which includes exchange of physical goods, provision of services, statutory charges, grants, donations and taxes and duties. In some cases, the requirements of other Standards take precedent over IFRS 15, for example IAS 20 *Government Grants* as interpreted by the FRM. In other cases, whilst the process of identifying contracts may be practically challenging initially, there were no significant issues identified in the application of the Standard as written.

**4.8** It was commented that it may be difficult to identify a contract or a customer in the traditional sense in the public sector context in the case of fees, levies and charges. There is often a statutory requirement to pay government rather than it being a choice for the customer. Through discussions it was considered that a "contract" in these circumstances would be the legislation or regulations providing the ability for the entity to impose a charge on the customer and the requirement for the customer undertaking the relevant activities to be liable to pay the charge. The existence of such legislation/regulations and the practice of the government imposing the fee, levy or charge would be deemed akin to customary business practices. The legislation would also provide the enforceability of the obligations on both parties. Box 4.A overleaf provides an illustrative example of this intent.

**4.9** It is recognised however that these principles cannot be applied to general taxation where there is not a specific activity that relates to the tax and is therefore considered outside of the scope of IFRS 15. This is the same principle that was applied under IAS 18 where revenue considered to be a tax by the Office of National Statistics would be reported in Trust Statements rather than Departmental Accounts. Further details on the accounting for taxes and duties is discussed from paragraph 4.48 below.

**4.10** From the "customer's" perspective, IFRIC 21 *Levies* provides the interpretation on when to recognise a liability to pay a levy whose timing and amount is certain or where it is a liability within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. The interpretation states that the obligating event that gives rise to a liability to pay a levy is the activity that triggers the payment of the levy, as identified by the legislation.

## Step 2: Identifying performance obligations

**4.11** IFRS 15 introduces the concept of identifying performance obligations which are promises in a contract to transfer goods or services that are distinct. In determining whether a good or service is distinct, an entity needs to consider if the customer can benefit from the good or service on its own or together with other resources that are readily available to the customer.

**4.12** An entity also needs to consider whether the promise to transfer the good or service is separately identifiable from other promises. If a promised good or service is not distinct, an entity is to combine that good or service with other promised goods or services until it identifies a bundle of goods or services that is distinct. The recognition of revenue will be based on the satisfaction of these individual performance obligations.

**4.13** HM Treasury expects that in most cases obligations can be identified in contracts by virtue of applying the first step of the model. Examples of obligations identified in the public sector include the transfer of physical goods from a sale, production of reports, performing an investigation, providing a licence or permission to undertake certain activities etc.

#### **Box 4.A: Illustrative Example**

Per the Fishing Act 1952 the Department of Fishing (DoF) may impose a levy on persons engaged in fishing activities. Any levy imposed under this section shall be payable by such persons engaged in the sea fish industry, in such proportions and at such times as may be prescribed; and the amount payable by any person on account of the levy shall be a debt due from him to the DoF and recoverable accordingly.

If DoF were to apply the IFRS 15 criteria to identifying a contract for their levy revenue:

- 1 The legislation is considered to be the approved contract which enables the DoF to impose a levy and for the person engaged in fishing activities (customer) to pay the levy. The legislation provides the enforceability on both parties.
- 2 The DoF can identify that they will have rights to consideration from imposing the levy as a result of the customer engaging in fishing activities. There are no other obligations DoF have to perform aside from assuring themselves that the levy is imposed upon the correct persons.
- 3 DoF can identify payment terms as the levies are agreed with Ministers and published on the website each year.
- 4 The contract (i.e. legislative requirements) has commercial substance as the amount of DoF's future cash flows is expected to change as a result of the levy being imposed on persons engaged in fishing activities.
- 5 It is probable that DoF will collect the consideration to which it will be entitled to.

As all the criteria are considered to be met, it is considered there is a contract in place.

### **Step 3: Determining the transaction price**

**4.14** The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. The transaction price is determined under the terms of the contract and the entity's customary business practices.

**4.15** The transaction price may be a fixed amount of consideration or include estimates of consideration that is variable or consideration in a form other than cash. Some or all of the estimated amount of variable consideration is included in the transaction price only to the extent

that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Adjustments to the transaction price are also made for the effects of financing (if significant to the contract) and for any consideration payable to the customer.

**4.16** No significant issues have been raised about determining the transaction price in contracts.

## **Step 4: Allocating transaction price to performance obligations**

**4.17** IFRS 15 requires the transaction price to be allocated to each performance obligation (or distinct good or service) in an amount that depicts the amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to the customer.

**4.18** An entity is required to allocate the transaction price to each performance obligation on the basis of the relative stand-alone selling prices of each distinct good or service. If a stand-alone selling price is not observable, the entity is required to estimate it. IFRS 15 details examples of methodologies an entity could use to determine the stand-alone price. These include adjusted market assessment, cost plus margin or residual approach (in limited circumstances).

**4.19** The transaction price may include a discount or a variable amount of consideration that relates entirely to a specific part of the contract. The requirements specify when an entity should allocate the discount or variable consideration to a specific part of the contract rather than to all performance obligations in the contract.

**4.20** There are likely to be more contracts within the public sector where the department is the sole market provider compared with private sector organisations. This may cause difficulties in establishing a stand-alone price for each distinct good or service. However given the vast array of revenue transactions, HM Treasury judges it not appropriate for the FReM to mandate estimation techniques. Instead entities should adopt suitable methods relating to the individual circumstances of their revenue streams and the markets in which they operate. IFRS 15 provides sufficient scope for entities to choose an appropriate technique and be consistent in its application.

## **Step 5: Satisfaction of performance obligations**

**4.21** IFRS 15 requires revenue to be recognised when (or as) it satisfies a performance obligation by transferring a promised good or service to a customer (which is when the customer obtains control of that good or service).

**4.22** For satisfaction over time, IFRS 15 specifies one of the following criteria needs to be met:

- a. The customer simultaneously receives and consumes the benefits provided;
- b. The entity's performance creates or enhances an asset that the customer controls as it is being created or enhanced; or
- c. The entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.

**4.23** For a performance obligation satisfied over time, an entity is required to select an appropriate single method of measuring progress to determine how much revenue should be recognised as the performance obligation is satisfied.

**4.24** If an entity does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time.

**4.25** The increased guidance, compared to the previous standards, on when revenue can be recognised may result in changes to the timing of revenue recognition. No significant issues have been raised about the satisfaction of performance obligations.

## Contract costs

**4.26** IFRS 15 requires an entity to recognise as assets costs to obtain a contract if the entity expects to recover those costs. These must be the incremental costs incurred in obtaining a contract; costs that would not have been incurred had the contract not been obtained. In addition, if an entity incurs costs in fulfilling a contract that are not within the scope of another Standard (for example, IAS 2 *Inventories*, IAS 16 *Property, Plant and Equipment* or IAS 38 *Intangible Assets*) these should also be recognised as an asset if three conditions are met:

- the costs relate directly to a contract or to an anticipated contract that the entity can specifically identify
- the costs generate or enhance resources of the entity that will be used in satisfying (or continuing to satisfy) performance obligations in the future
- the costs are expected to be recovered

**4.27** If assets are recognised under IFRS 15, they shall be amortised on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the asset relates. Impairment losses shall be recognised to the extent that the carrying amount of an asset recognised exceeds the remaining amount of consideration that the entity expects to receive in exchange for the goods or services to which the asset relates less the costs that relate directly to providing those goods or services that have not been recognised as expenses.

**4.28** Cross government discussions have not identified instances where assets would be recognised that would not be within the scope of another Standard. As a result HM Treasury does not propose any amendments or interpretations on this section. HM Treasury will re-consider this approach if any instances and issues come to light through this consultation.

**Question:** Does your entity expect to recognise assets under IFRS 15 that would not be within the scope of another Standard? If so what would these assets be?

## Transition

**4.29** IFRS 15 is to be applied retrospectively, subject to some transitional reliefs in particular circumstances. There are two options for transition to IFRS 15:

### Option 1: Retrospection application with restatement

**4.30** If an entity restates prior periods, the restated financial statements must exhibit all the requirements of IFRS 15. The Standard permits the use of some practical expedients for contracts that are completed under IAS 11 or IAS 18 at the point of transition and some disclosure exemptions.

**4.31** Disclosures will be required in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. If any practical expedients are used, entities will be required to

disclose which practical expedients have been used and, to the extent reasonably possible, a qualitative assessment of the estimated effect of applying each of the practical expedients.

### **Option 2: Retrospective application with no restatement**

**4.32** If an entity elects not to restate comparative periods, quantification of adjustments is still necessary in order to determine the transition adjustments in the opening balances in reserves/other components of equity, as appropriate; the difference between the previous carrying amounts and the new carrying amounts is recorded in the opening balances of the annual period including the initial application date.

**4.33** Practical expedients on initial adoption are reduced under this option. Additional disclosures are also required with this option which consist of:

- the amount by which each financial statement line is affected in the current reporting period by the application of the Standard as compared to IAS 11, IAS 18 and related interpretations that were in effect before the change
- an explanation of the reasons for significant changes identified in the above

**4.34** Entities will be required to calculate the restated amounts for the prior period comparatives regardless of which method of transition is adopted. This is because the opening balances in the current year's Statement of Financial Position will need to be restated to show the effects of adopting IFRS 15 for the first time.

**4.35** In order to improve consistency across the public sector and to better facilitate the consolidation of public sector entities within the Whole of Government Accounts (WGA), HM Treasury propose the following 'blanket' approach to be applied across the public sector in relation to transition: **Option 2 - Retrospective application with no restatement.**

**Question: Do you agree with the transition approach for the proposed amendments? If so, why? If not why not and what alternatives do you propose?**

## **Implementation**

### **Timetable**

The effective date of IFRS 15 is from 1 January 2018. HM Treasury proposes to apply IFRS 15 effective from 1 April 2018 for the public sector. The implementation timetable HM Treasury is working towards can be found in Box 4.B overleaf.

### **Practical Considerations**

**4.36** IFRS 15 introduces the need for additional data, to support both methodology and disclosure requirements, and infrastructure for developing new processes, systems and controls to ensure entities are able to run the existing IAS 18/IAS 11 and IFRS 15 models concurrently.

**4.37** Public sector entities have a significant number of counterparties and current systems may not have the capacity to consider these individually. As a consequence, IFRS 15 is likely to have resource implications when introduced.

**4.38** In planning for the adoption of IFRS 15 it is important that preparers have a good understanding of how IFRS 15 will impact them on transition and business as usual thereafter. As IFRS 15 requires detailed analysis of individual or portfolios of contracts, it is also important that sales and commercial colleagues also have a good understanding of the impacts of IFRS 15 when writing contracts.

**4.39** No other significant issues have been raised on the implementation considerations.

**Question: Do you agree with the proposed effective date for the public sector implementation of IFRS 15? If so, why? If not, why not and what alternatives do you propose?**

**Box 4.B: IFRS 15 Implementation Timetable**

Summer 2016	Exposure Draft for consultation on the impact of IFRS 15
November 2016	FRAB meeting to review comments from the Exposure Draft consultation
Spring/Summer 2017	Further opportunity to consider adaptations, interpretations, or other amendments to the FReM FRAB meetings for further consideration if needed
November 2017	FRAB meeting to approve the 2018-19 FReM
December 2017	2018-19 FReM published
January 2018	IFRS 15 implementation date
2018-19	UK public sector implementation of IFRS 15

## Disclosures

**4.40** IFRS 15 requires disclosures to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Under the new Standard, entities are required to disclose more information about its contract with customers than currently required under IAS 11 and IAS 18.

**4.41** Discussions have highlighted the burden of the increased disclosure requirements and whether these are aligned to the objectives of the simplification and streamlining project. Similar comments on the burden of the disclosures have been highlighted by the private sector.

**4.42** As explained in the Basis for Conclusions<sup>3</sup>, the IASB found that users of financial statements supported the proposed disclosure requirements because those requirements would have been a

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<sup>3</sup> IFRS 15, Basis for Conclusions, BC327-329



significant improvement over previous requirements. In contrast, other respondents (primarily preparers) noted that, when viewed as a whole, the proposed disclosure requirements would have resulted in voluminous disclosures and they questioned whether the proposed disclosures were justifiable on a cost-benefit basis. IASB observed that, to some extent concerns about the increased volume were the inevitable consequence of addressing the shortcoming in the previous disclosure requirements. This context is considered important when considering the enhanced disclosures in the public sector. Particular considerations for the disclosure requirements and its applicability in the public sector can be found overleaf.

**4.43** The concept of materiality, as it applies to disclosures, is fundamental. It is not appropriate to simply apply the disclosure requirements in IFRS 15 without considering materiality. Specific disclosures are not required under IFRS if the information resulting from that disclosure is not material. IFRS 15 also states that an entity need not disclose information in accordance with this Standard if it has provided the information in accordance with another Standard. Care should be taken to not reduce the understandability of the financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures and functions. The materiality concept should also be applied on a disclosure-by-disclosure basis.

**4.44** HM Treasury considers it appropriate to retain the disclosure requirements in full but to emphasise the materiality considerations that entities are expected to undertake in determining whether they are required to provide particular disclosures.

**4.45** HM Treasury will engage with preparers and issue additional application guidance to improve understanding of the disclosure requirements well in advance of the effective date to support implementation of the Standard in the public sector.

**Question: Do you agree with the decision to not adapt the disclosure requirements for the proposed amendments? If so, why? If not why not and what alternatives do you propose?**

	Disclosure Requirements	Considerations
<b>Disaggregation of Revenue</b>	<p>The Standard requires entities to disaggregate revenue recognised from contracts with customers into categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.</p> <p>In addition, the Standard requires entities to disclose sufficient information to enable users to understand the relationship between the disclosure of disaggregated revenue and revenue disclosed for each reportable segment under IFRS 8 <i>Operating Segments</i></p>	<p>The Standard does not specify how to disaggregate revenue but provides some guidance on potential areas to consider<sup>1</sup>. Some entities may need to use more than one category of disaggregation to fulfil the disclosure requirements. For some bodies, the information is available via the segmental reporting note and repeat disclosures would not be required.</p> <p>Entities should be reminded that disaggregation is only required when revenue from contracts with customers is material. The requirement to disclose is based on whether the amount of revenue is material rather than whether there is a material number of contracts.</p>
<b>Contract Balances</b>	<p>The Standard requires entities to disclose the opening and closing balances of receivables, contract assets and contract liabilities from contracts with customers; revenue recognised in the reporting period that was included in the contract liability balance at the beginning of the period and from obligations satisfied in previous periods; and an explanation of significant changes.</p>	<p>The requirement to disclose contract balances is most similar to the requirements of IAS 11. The objective of this disclosure is to enable users of the accounts to understand the judgements taken in recognising or not recognising revenue. In satisfying this disclosure requirement, entities should consider the requirements of IFRS 9, considering the stability of the customer and whether any impairments would be required.</p> <p>As with all disclosure requirements, entities should take into consideration the materiality of these balances and whether it is required to be disclosed. Contract balances are considered to be most material to those entities that have long term revenue contracts.</p>
<b>Performance Obligations</b>	<p>An entity shall disclose information about its performance obligations in contracts with customers. The Standard provides a list of areas this should cover.</p>	<p>Discussions have considered that it could be appropriate to expand the accounting policy rather than a requirement to disclose details for every contract. This is considered to be in line with the IASB intentions, where in the Basis for Conclusion it stated that in many cases entities provide a boilerplate description of the accounting policy without explaining how that policy relates to the contracts that the entity enters into with customers. The wording of the disclosure requirement also supports the view that this is not expected for every individual contract. Where an entity has one or two material contracts, it is considered presentationally better to provide this detail in the note itself rather than as an accounting policy.</p> <p>Given the introduction of performance obligations is the fundamental basis of the new Standard, HM Treasury considers it appropriate to retain the disclosure requirements in full.</p>

<sup>1</sup> IFRS 15, Application Guidance B87-B89

<b>Transaction price allocated to the remaining performance obligations</b>	<p>The Standard requires disclosure on the aggregate amount of the transaction price allocated to performance obligations that are (partially) unsatisfied and an explanation of when an entity expects to recognise these amounts as revenue.</p> <p>Practical expedients are available if the obligation is part of a contract that has an original expected duration of one year or less or if the revenue is recognised in accordance with B16<sup>2</sup> (e.g. service contracts where there is a fixed amount per hour).</p>	<p>This disclosure requirement has been considered controversial in the public and private sectors as it provides an indication of future revenue streams. However it is for this reason that, from a user's perspective, the disclosure was considered to be useful as it provided an indication of future revenue streams from existing contracts.</p> <p>By virtue of applying the IFRS 15 criteria to the contract in the first place the entity should be able to identify what obligations are outstanding and the remaining transaction price associated with these obligations.</p> <p>Entities should be aware that existing accounting systems may not hold sufficient information to meet this disclosure requirement and work may be required to collate information from other parts of the organisation (commercial).</p>
<b>Assets</b>	The Standards require disclosure of the judgements made in determining the amount of the costs incurred to obtain or fulfil a contract and the method it uses to determine the amortisation.	Cross government discussions have not identified instances where assets would be recognised that were not already within the scope of another Standard. As a result HM Treasury do not propose any amendments or interpretations on this section. HM Treasury will re-consider if any issues come to light through this Exposure Draft process.
<b>Significant Judgements</b>	IFRS 15 provides particular areas of focus for judgements made in applying the Standard on the timing and satisfaction of performance obligations and transaction price and amounts allocated to performance obligations.	Requirements are akin to existing requirements to disclose significant judgments under IAS 1 Presentation of Financial Statements.
<b>Initial Adoption</b>	<p>The following additional disclosures are required if IFRS 15 is applied retrospectively with the cumulative effect in reserves</p> <ul style="list-style-type: none"> <li>• The amount by which each financial statement line item is affected in the current reporting period by the application of this Standard as compared with IAS 11, IAS 18 and related interpretations</li> <li>• An explanation of significant changes identified above</li> </ul>	The requirements are considered appropriate in line with the transition approach proposed.
<b>Practical Expedients</b>	If an entity elects to use practical expedients the entity shall disclose that fact.	The requirements are considered appropriate.

<sup>2</sup> IFRS 15 (B16) As a practical expedient, if an entity has a right to consideration from a customer in an amount that corresponds directly with the value to the customer of the entity's performance completed to date (for example, a service contract in which an entity bills a fixed amount for each hour of service provided), the entity may recognise revenue in the amount to which the entity has a right to invoice

## Consolidated Fund revenue

**4.46** The FReM currently provides the accounting requirements for revenue (and some associated expenditure) collected by entities on behalf of the Consolidated Fund, either by statute or convention, and where the entity undertaking the collection is consequently acting as agent rather than as principal. These revenues are accounted for in Trust Statements rather than Departmental Accounts.

### Taxes and Duties

**4.47** There is no IFRS for the recognition of revenue by government from taxes and duties. Whilst currently based on the principals of IAS 18, IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides a framework which the current FReM is broadly aligned with.

**4.48** The FReM currently requires revenue recognition for taxes and duties “when a taxable event has occurred, the revenue can be measured reliably and it is probable that the economic benefits from the taxable event will flow to the collecting entity. All these elements are required to be satisfied.”

**4.49** Analysing the current accounting requirements to the principles of IFRS 15:

- a taxable event is considered to be the obligation which requires the customer to pay the taxes or duties to government
- *measured reliably* is considered to be with regard to the identification of the transaction price
- economic benefits will flow to the collecting entity (as an agent rather than principal) – the entity is expected to receive the consideration with the underlying legislation providing the entity with the ability to collect the tax
- there are no performance obligations the entity has to perform in order to receive the revenue

**4.50** HM Treasury does not propose to change the accounting for taxes and duties

**4.51** There are some levies, taxation, fines and penalties where, by statute or with Treasury consent, the entity is permitted to keep the income rather than pass it to the Consolidated Fund. These revenues are recorded in accounts rather than Trust Statements. In these circumstances there would be no clear obligations present for government to perform in order to receive the revenue. As such, HM Treasury proposes IFRS 15 (para 15a)<sup>1</sup> will be the criteria to use in order to recognise these revenue streams.

### Fines and Penalties

**4.52** Fines and penalties are economic benefits payable to government for breaches of laws or regulations where there is a statutory obligation to pay. The FReM (para 8.2.9) currently required revenue recognition for fines and penalties “at the time that the fine or penalty is imposed and becomes receivable by the entity”. These are paid into the Consolidated Fund as collecting entities act as an agent rather than a principal and are recorded in Trust Statements.

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<sup>1</sup> IFRS 15 (15) When a contract with a customer does not meet the criteria in paragraph 9 and an entity receives consideration from the customer, the entity shall recognise the consideration received as revenue only when either of the following events has occurred:

(a) the entity has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the consideration promised by the customer has been received by the entity and is non-refundable; or  
(b) the contract has been terminated and the consideration received from the customer is non-refundable.

**4.53** The analysis under IFRS 15 would be similar to that for taxes and duties. There would be no performance obligations the entity has to perform to receive the revenue. HM Treasury does not propose to change the accounting for fines and penalties

**Question: Do you agree there should be no changes to the principles of accounting for taxes and duties and fines and penalties? If so why? If not why not and what alternatives do you propose?**

## **Whole of Government Accounts**

**4.54** The introduction of IFRS 15 is likely to complicate further the elimination of intra-government balances. The criteria for the satisfaction of performance obligations may affect balances and different recognition points by the entities consolidated into WGA.

**4.55** Consistency of reporting methodology and disclosure requirements is preferable from a WGA perspective. However, it is recognised that given the individual nature of each public sector body, it is unlikely to be appropriate to mandate the same disclosures in every account, especially where it would not be material for the organisation.

**4.56** WGA will need to ensure the right data is collected from public sector entities to facilitate the WGA consolidation process. This process and the requirements from entities will need to be considered in advance of the data collection tool being issued. The concept of materiality from a WGA perspective will be important when assessing the impact of the Standard across government and the relevant sectors.

**4.57** From a presentational perspective, WGA will need to explain the movements to opening balances and the impacts on the Statement of Comprehensive Net Expenditure/Income and the Statement of Financial Position as a result of transitioning to IFRS 15. Understanding the movements will be key to forming the narrative for the publication.

**4.58** The WGA team will need to consider these challenges as they develop their implementation plan for IFRS 15. Subject to responses from this consultation, HM Treasury proposes that IFRS 15 will be applied in full to WGA.

# Proposed amendments to the Government Financial Reporting

## 5 Manual

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### Introduction

An amendment to each of the following chapters is proposed:

- Chapter 6, Applicability of Accounting Standards
- Chapter 8, Income and Expenditure

### Why the amendments are proposed

The amendments proposed in this exposure draft seek to amend the FReM to incorporate the financial reporting principles contained in IFRS 15 where it is appropriate for them to be applied.

### Effective date of amendments

The effective date for the proposed amendments is 1 April 2018.

### Proposed amendments

FReM amendments are proposed to reflect IFRS 15 being adopted for the first time.

## 6 Applicability of accounting standards

### 6.1 EU adopted IFRS

6.1.1 A list of EU adopted IFRS is shown in Table 6.1, together with a record of whether they have been adapted or interpreted for the public sector context in this Manual. All standards apply to all reportable activities and reporting entities applying this Manual to the extent that each standard is relevant to those activities and in the light of any statutory requirements or other pronouncements that might from time to time be made by the relevant authorities. Where adaptations or interpretations are different for ALBs this is identified below.

Table 6.1

International Standard	Applies without adaptation	Applies as interpreted for public sector	Applies as adapted for public sector	Different adaptations or interpretation for ALBs
IFRS 15 Revenue from Contracts with Customers	•			

## 8 Further guidance on accounting for income and expenditure

### Retainable and non-retainable income

8.1.5 All income from contracts with customers should be recognised in the Statement of Comprehensive Net Expenditure in accordance with IAS 18 IFRS 15. Entities should refer to other relevant standards for other sources of income. Only income that can be retained and set against resource or capital budgets should be recorded in the Statement of Parliamentary Supply. Departments should refer to Consolidated Budgeting Guidance to determine whether income may be retained and contact the relevant authority where approval to retain is required.

### 8.2 Consolidated Fund revenue

8.2.1 This section deals with revenue (and some associated expenditure) collected by entities on behalf of the Consolidated Fund which by statute or convention are due to the Consolidated Fund and where the entity undertaking the collection is consequently acting as agent rather than principal.

#### Taxes and duties

8.2.2 Taxes and duties are economic benefits compulsorily payable to public sector entities, in accordance with laws and regulations established to provide revenue to the government, excluding fines or other penalties imposed for breaches of laws or regulations.

8.2.3 In preparing their financial statements, entities will not recognise or measure the “tax gap”. The “tax gap” is defined as the difference between the hypothetical amounts of revenues due, based on data on economic activity, and revenues receivable. Revenues receivable include both the tax yield from compliant taxpayers and estimates of amounts due from non-compliant, but known, taxpayers. Where taxes and duties are material, a statement should be included in the accounting policies note that the “tax gap” is not recognised in the financial statements.

8.2.4 Where taxes and duties are recognised on an accrual basis, they will be measured at the fair value of the consideration received or receivable, net of repayments. Revenue is recognised when a taxable

event has occurred, the revenue can be measured reliably and it is probable that the economic benefits from the taxable event will flow to the collecting entity. All these elements are required to be satisfied.

8.2.5 Tax revenues are deemed to accrue equally over the period for which they are due. No revenue is recognised if there are significant uncertainties regarding recovery of the taxes due. The term “probable” means that the flow of revenue should be more likely than not to occur. Revenue should be accrued net of amounts not expected to be collected, which might be determined by reference to past trends in write-offs and remissions, the emerging position in-year, historical debt collection performance or by other appropriate means.

8.2.6 Where, exceptionally and with the consent of HM Treasury, taxes and duties are recognised on a cash basis, they will be recognised in the accounting period in which the tax is received by the entity and are measured at the cash amount received.

8.2.7 In the UK the main form of tax expense is personal tax credits. Tax credits are recognised in the Statement of Comprehensive Net Expenditure of the department which has responsibility for their payment. Where the financing required to fund tax credits may be deducted by statute from tax revenues collected before those revenues are remitted to the Consolidated Fund, the deduction and payment of these amounts is recorded in the trust statement as an appropriation of the revenue received.

### **Fines and penalties**

8.2.8 Fines and penalties are economic benefits payable to government for breaches of laws or regulations where there is a statutory obligation to pay.

8.2.9 Fines and penalties are recognised at the time that the fine or penalty is imposed and becomes receivable by the entity. Where, on appeal, or for other legal reasons, the penalty is cancelled, the amount receivable is derecognised at the date of the successful appeal. Where a financial penalty is imposed, but with an alternative of a non-financial penalty, the financial penalty is recognised initially, but is derecognised if the option of the non-financial penalty is taken up.

8.2.10 Where fines and penalties are uncollectible or, for policy reasons, (other than the imposition of an alternative penalty), the entity decides that it is inappropriate to pursue collection, the amounts not collected are recorded as an expense. The amounts not collectible are estimated from the most appropriate data available to the entity.

### **Trust Statements**

8.2.11 HMRC and certain other receivers of money which is by law payable into the Consolidated Fund are required to prepare accounts in a form to be directed by the Treasury and which are to be examined and reported on by the Comptroller and Auditor General.

8.2.12 The intention of the underlying legislation<sup>14</sup> is to require those entities collecting revenue on behalf of the Consolidated Fund to prepare separate statements (“Trust Statements”), from those for the entity and to include in Trust Statements details of the collection and allocation of that revenue.

8.2.13 The Treasury (or, where appropriate, sponsor department) will issue an accounts direction to each entity producing a Trust Statement. The format of the Trust Statement will be defined in the accounts direction. It will usually follow the principles set out in Chapter 5 “Form and Content of the Annual Report and Accounts” and must be published as part of the Annual Report and Accounts except where the Treasury or sponsor department directs otherwise. The requirement will be based on the underlying legislation of those entities collecting revenue on behalf of the Consolidated Fund and based on section 7 of the Government Resources and Accounts Act for other entities.

8.2.14 Trust Statements shall include the following revenue:

- a) all income classified as taxation by the Office for National Statistics except where by statute the entity is permitted to keep that income;
- b) all amounts which, by statute, are to be surrendered or paid into the Consolidated Fund (either by the entity directly or by passing the collected funds to a third party who then pays over the amounts collected) or to another third party within Government;
- c) all fines and penalties levied except where the entity is permitted by statute or with Treasury consent, to retain the penalties imposed; and
- d) any other income which the Treasury may direct to be included.



8.2.15 Trust Statements shall also include the following expenditure:

- a) the costs of collection and administration where there is express statutory provision for those costs to be deducted from the revenue collected;
- b) the costs of compensating (limited to repayments and interest) those from whom taxes or penalties have been incorrectly collected. Other elements of compensation and related costs shall be accounted for in departmental accounts; and
- c) any allowance for uncollectible amounts measured in accordance with IAS 39.

8.2.16 Where legislation requires or permits part of the revenue collected to be surrendered and part to be retained by the entity, the full amount shall be included in the Trust Statement, and the amount to be retained shall be recorded as an appropriation of net revenue in the Trust Statement (and, equally, as revenue in the Statement of Comprehensive Net Expenditure).

8.2.XX Where by statute or Treasury consent the entity is permitted to keep income from taxation, fines and penalties, this revenue shall be accounted for under IFRS 15 (15). The performance obligation step under IFRS 15 will not apply.