Basis for Conclusions on IFRIC Interpretation 18 *Transfers of Assets from Customers*

This Basis for Conclusions accompanies, but is not part of, IFRIC 18.

Introduction

BC1 This Basis for Conclusions summarises the IFRIC's considerations in reaching its consensus. Individual IFRIC members gave greater weight to some factors than to others.

BC2 The IFRIC released draft Interpretation D24 *Customer Contributions* for public comment in January 2008 and received 59 comment letters in response.

Background

BC3 The IFRIC received a request to issue guidance on the accounting for transfers of items of property, plant and equipment by entities that receive such transfers from their customers. Divergence had arisen in practice with some entities recognising the transferred item at fair value and others recognising it at a cost of nil. Among those that recognised the item at fair value, some recognised the resulting credit as revenue immediately, while others recognised it over some longer service period. The IFRIC decided to develop an Interpretation in response to that divergence in practice.

Scope

BC4 This Interpretation applies to the accounting for transfers of items of property, plant and equipment by entities that receive such transfers from their customers. In developing the Interpretation, the IFRIC decided that it would not address how the customers should account for the transfers because the main issue is how the entity receiving the asset should recognise revenue.

BC5 Some respondents questioned whether transfers of assets other than those within the scope of this Interpretation, ie transfers of intangible assets from customers, would lead to the same answer. In its redeliberations, the IFRIC decided not to expand the scope to assets other than those already considered in D24 but did not prohibit application by analogy in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

BC6 In its redeliberations, the IFRIC clarified in paragraph 3 that, for convenience, this Interpretation refers to the entity transferring the item of property, plant and equipment as the customer even though that entity may not be the entity that will eventually have ongoing access to the supply of goods or services and will be the recipient of those goods or services. The IFRIC also added an example to illustrate such a situation.

BC7 Some respondents commented that, in practice, customers often transfer cash instead of transferring an item of property, plant and equipment. The IFRIC reaffirmed its view that transfers of cash should be within the scope of the Interpretation (see also paragraph BC24).

BC8 Many respondents were concerned that D24 could create unintended overlaps with existing IFRSs such as IFRIC 12 *Service Concession Arrangements* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. In its redeliberations, the IFRIC noted that in a public-to-private service concession arrangement within the scope of IFRIC 12 the grantor controls the infrastructure, not the operator. Therefore, the IFRIC concluded that this Interpretation does not apply to agreements in which the transfer is an item of infrastructure used in a service concession arrangement that is within the scope of IFRIC 12. The IFRIC also clarified that IAS 20 does not apply because transfers of assets from customers do not meet the definition of a government grant in accordance with paragraph 3 of IAS 20.

BC9 Some respondents to D24 questioned the application by analogy to situations other than utility entities providing connection and access to their networks (eg electricity, gas, water or telecommunication networks). In its redeliberations, the IFRIC noted that this Interpretation might also be relevant to industries other than utilities. The IFRIC also clarified the background section of the Interpretation adding an example of an information technology outsourcing agreement.

Issues

BC10 When an entity receives an item of property, plant and equipment from a customer, it should assess whether the transferred item meets the definition of an asset.

BC11 If the entity concludes that the transferred item of property, plant and equipment meets the definition of an asset, it should recognise the transferred item in accordance with paragraph 7 of IAS 16. In that case, the next issues are at what amount it should be recognised on initial recognition and how to account for the resulting credit.

BC12 The last issue the IFRIC considered is how the entity should account for the receipt of cash instead of a transfer of an item of property, plant and equipment.

Consensus

Is the definition of an asset met?

BC13 In its redeliberations, the IFRIC discussed the different steps that D24 required an entity to follow to determine whether an asset should be recognised, including the consideration of IFRIC 4 *Determining whether an Arrangement contains a Lease* and IAS 17 *Leases*. The IFRIC decided to simplify the proposals by focusing on who controls the asset. The Interpretation provides guidance based on the definition of an asset set out in paragraph 49(a) of the *Framework*[1,2] and the additional guidance in paragraphs 55 and 57 of the *Framework*.[3]

1 now paragraph 4.4(a) of the *Conceptual Framework*

2 References to the *Framework* are to IASC's *Framework for the Preparation and Presentation of Financial Statements*, adopted by the IASB in 2001. In September 2010 the IASB replaced the *Framework* with the *Conceptual Framework for Financial Reporting*.

3 now paragraphs 4.10 and 4.12 of the *Conceptual Framework*

How should the transferred item of property, plant and equipment be measured on initial recognition?

BC14 The IFRIC concluded that, in a normal trading transaction, the item of property, plant and equipment is received in exchange for something, ie the provision of services such as connection to a network, provision of ongoing access to a supply of goods or services, or both.

BC15 The IFRIC noted that both paragraph 24 of IAS 16 *Property, Plant and Equipment* and paragraph 12 of IAS 18 *Revenue* lead to the same measurement attribute for such exchange transactions, ie the item received should be measured at fair value on initial recognition. Therefore, if the entity concludes that the definition of an asset is met, it should recognise the transferred asset as an item of property, plant and equipment in accordance with paragraph 7 of IAS 16 and measure it on initial recognition at its fair value in accordance with paragraph 24 of that Standard. The IFRIC also noted that respondents to D24 generally agreed with that conclusion.

How should the credit be accounted for?

BC16 The following discussion assumes that the entity receiving an item of property, plant and equipment from a customer has concluded that the transferred item should be recognised and measured at its fair value on initial recognition. It also assumes that the services to be provided in exchange for the transferred item are part of the ordinary activities of the entity.

Identifying the separately identifiable services

BC17 D24 identified only one service to be delivered in exchange for the transferred item of property, plant and equipment: the provision of ongoing access to a supply of goods or services. Many respondents, including utility entities, questioned whether an entity receiving an asset from a customer always has an obligation to provide ongoing access to a supply of goods or services as a result of the transfer. For example, some respondents argued that when a utility company is required by law or regulation to provide access to a supply of a commodity to all customers at the same price it may have no further obligation once the service connection has been made. They also argued that an obligation to provide ongoing services to the customer who transferred the asset may exist only if the customer obtains in exchange some exclusive right of access to a supply of goods or services, eg a reduced price. Overall, these respondents asked the IFRIC to reconsider the revenue recognition issue on the basis of an IAS 18 approach.

BC18 In its redeliberations, the IFRIC noted that an entity may agree to deliver one or two services in exchange for the transferred item of property, plant and equipment, such as connecting the customer to a network, providing the customer with ongoing access to a supply of goods or services, or both. The IFRIC concluded that identifying the separately identifiable services of a single agreement depends on facts and circumstances and that judgement is required. The IFRIC also acknowledged that a practical weakness of IAS 18 is that it gives insufficient guidance on agreements that deliver more than one good or service to the customer. Therefore, the IFRIC decided to develop guidance based on paragraph 13 of IAS 18 to help identify the services to be delivered in exchange for the transferred asset. This decision resulted in including the indicators in paragraphs 15–17 of the Interpretation and the examples illustrating their application.

Revenue recognition

BC19 In accordance with paragraph 13 of IAS 18, the IFRIC decided that the Interpretation should require that when more than one service is identified the fair value of the total consideration received or receivable for the agreement should be allocated to each service and that the recognition criteria of IAS 18 should be applied to each service. The IFRIC noted that IFRIC 12 *Service Concession Arrangements* and IFRIC 13 *Customer Loyalty Programmes* provide guidance on how to allocate the fair value of the total consideration received or receivable for the agreement to each component (see paragraph 13 of IFRIC 12 and paragraphs 5–7 of IFRIC 13). Therefore, the IFRIC concluded that this Interpretation should include only a reminder in paragraph 19 that such allocation is required if more than one service is identified.

BC20 If a separately identifiable ongoing service is part of the agreement, the entity must identify the period over which revenue should be recognised. Paragraph 20 of D24 stated that 'although the period over which an entity has an obligation to provide access to a supply of goods or services using a contributed asset may be shorter than the useful economic life of the asset, it cannot be longer.' Some respondents asked the IFRIC to clarify whether that period may be determined by the terms of the agreement and why that period cannot be longer than the economic life of the contributed asset.

BC21 The IFRIC clarified that the period over which revenue should be recognised for the ongoing service is generally determined by the terms of the agreement with the customer. If the arrangement does not specify a period, the IFRIC reaffirmed its view that the revenue should be recognised over a period no longer than the useful life of the transferred asset used to provide the ongoing service. This is because the entity can only use the transferred asset to provide ongoing access to a supply of goods or services during its useful life. Any obligation that exists after the asset is replaced does not arise from the original transfer but from the terms of the entity's operating licence or other regulation.

BC22 Almost all respondents disagreed with paragraph BC22 of D24 that the time value of money should be taken into account when measuring revenue. The IFRIC agreed with respondents and noted that paragraph 11 of IAS 18 requires taking the time value of money into account only when payments are deferred.

How should the entity account for a transfer of cash from its customer?

BC23 Respondents were generally supportive of the IFRIC's proposals related to transfers of cash. However, some respondents asked the IFRIC to clarify the circumstances in which a cash transfer would be within the scope of the Interpretation.

BC24 In its redeliberations, the IFRIC discussed the accounting for agreements in which an entity receives a transfer of cash from a customer instead of an item of property, plant and equipment. The IFRIC reaffirmed its view in D24: when that amount of cash must be used only to construct or acquire an item of property, plant and equipment and the entity must then use the item of property, plant and equipment to deliver goods or services to the customer, the economic effect of the transfer of cash is similar to that of a transfer of an item of property, plant and equipment.

Transition

BC25 The IFRIC noted that applying the change in accounting policy retrospectively would require entities to establish a carrying amount for assets that had been transferred in the past. That carrying amount would be based on historical fair values. Those fair values may not be based on an observable price or observable inputs. Therefore, the IFRIC concluded that retrospective application may be impracticable and that the Interpretation should require prospective application to transfers received after its effective date. However, the IFRIC also concluded that earlier application should be permitted provided the valuations and other information needed to apply the Interpretation to past transfers were obtained at the time those transfers occurred.

Changes from draft Interpretation D24

BC26 The most significant changes made from D24 in the light of comments received relate to:

(a) *Recognition of transferred assets*. As stated in paragraph BC13, the IFRIC decided to simplify the requirements. It addressed the issue of which entity controls the asset by giving guidance based on the definition of an asset set out in the *Framework*.

(b) *Revenue recognition*. The IFRIC decided that an entity receiving an item of property, plant and equipment from a customer may not always have an obligation to provide ongoing access to a supply of goods or services as a result of the transfer. Therefore, the IFRIC also decided to develop guidance based on paragraph 13 of IAS 18 to help identify the separately identifiable services to be delivered in exchange for the transferred asset.

(c) *Title of the Interpretation*. The IFRIC noted that in some jurisdictions, the term ‘contribution’ has the implication of a donation rather than an exchange transaction. In addition, the IFRIC noted that this term might be difficult to translate into some languages. For that reason, the IFRIC decided to use the term ‘transfer’ and redrafted the Interpretation accordingly.

(d) *Illustrative examples*. The IFRIC decided that illustrative examples should accompany, but not be part of, the Interpretation to help entities apply the Interpretation.

