EFRAG

European Financial Reporting Advisory Group

The costs and benefits of implementing IFRIC 18 *Transfers of Assets from Customers*

Introduction

1 Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of IFRIC 18 *Transfers of Assets from Customers*.

2 EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of IFRIC 18, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work. (The results of the consultations EFRAG has carried out seem to confirm this.) Therefore, as explained more fully in the main sections of the report, the approach EFRAG has adopted has been to carry out detailed initial assessments of the likely costs and benefits of implementing IFRIC 18 in the EU, to consult on the results of those initial assessments, and to finalise those assessments in the light of the comments received.

EFRAG's endorsement advice

3 EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB and IFRIC against the so-called endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

A SUMMARY OF IFRIC 18

4 Sometimes an entity receives one or more non-cash assets from its customers in return for goods or services that the entity agrees to provide to its customers using the asset(s) it receives. For example, a real estate developer (in this example, the customer) might construct an electricity substation and transfer that substation to an electricity network provider. The customer does that so that the persons to whom it will eventually sell the houses it is building will have a connection to an electricity network and will therefore be in a position to be supplied with electricity.

5 In some other cases, an entity will receive cash from its customers and will be required to use that cash to construct or acquire an asset that it will then use to the provide goods or services to its customers. For example, an alternative arrangement to the one described in the real estate developer/electricity network provider example could be that the real estate developer asks the electricity network provider to build the substation and reimburses the network provider for that work.

6 IFRIC 18 provides guidance on the transfers of assets for entities that receive items of PPE. It addresses three issues: how to account for the transferred item, how to account for the credit side of the transfer transaction, and how to account for a transfer of cash that is used to construct or acquire an item of property, plant or equipment (PPE) in a transfer transaction.[1]

How to account for the transferred item of PPE?

7 IFRIC 18 explains that, if an entity receives an item of PPE in a transfer that falls within the scope of IFRIC 18, it should recognise that item as an asset if both the item meets the definition of an asset under the IASB's Framework and the recognition criteria for PPE are met.

8 IFRIC 18 also explains that, when an entity first recognises such an asset, it shall measure it at its fair value.

How to account for the resulting credit side of the transfer transaction?

9 When an entity receives an asset in a transfer falling within the scope of IFRIC 18, it will do so in return for accepting some sort of obligation to provide goods or services. As such, IFRIC 18 requires the fair value of the asset received to be credited to the statement of comprehensive income as revenue under IAS 18 *Revenue*. When that revenue is recognised will depend on the exact obligation accepted and when that obligation is fulfilled.

10 IFRIC 18 requires the entity that receives the asset to identify which services arise from the transfer transaction.

(a) When only one service is identified, the entity recognises revenue when that service is delivered in accordance with IAS 18 *Revenue*.

(b) If more than one service is identified, the entity is required to allocate the fair value of the asset it receives to each of the identified services, and apply the recognition criteria of IAS 18 to each of those services.

(c) When the service or one of those services is an ongoing type of service—such as ongoing access to a supply of goods or services—revenue is recognised based on the terms of the transfer transaction, although the period over which it is recognised shall not exceed the useful life of the transferred asset.

[1] For ease of reference, an arrangement that involves a transfer of assets from a customer is referred to as a 'transfer transaction' through this document.

How to account for a transfer of cash?

11 Sometimes an entity will receive a transfer in the form of cash from its customer that it must use to construct or acquire an asset that it will use to provide goods or services to its customer using that asset.

12 The accounting for a cash transfer that IFRIC 18 requires is similar to the accounting for a non-cash asset transfer as described above. That is, the entity will recognise the item of PPE it constructs or acquires when the item of PPE meets the recognition requirements under IAS 16. The entity also recognises revenue under IAS 18 when it has delivered the goods or services it has agreed to provide under the transfer transaction.

EFRAG's initial analysis of the costs and benefits of IFRIC 18

13 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IFRIC 18, both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows. The implementation in the EU of IFRIC 18 is likely to:

(a) involve some preparers in some additional year one and ongoing costs. Those costs are however unlikely to be significant;

(b) involve users in no year one or ongoing incremental costs; and

(c) result in some improvements in the comparability of the information provided – and in some cases the relevance – and thus bring benefits to users.

14 EFRAG published its initial assessment and supporting analysis on 26 March 2009. It invited comments on the material by 8 May 2009. In response, EFRAG received eight comment letters. Five respondents agreed with EFRAG's assessment of the benefits of implementing IFRIC 18 and the associated costs involved for users and preparers. The other three respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing IFRIC 18 in the EU, but supported EFRAG's recommendation that IFRIC 18 be adopted for use in Europe.

EFRAG'S EVALUATION OF THE COSTS AND BENEFITS OF IFRIC 18

15 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IFRIC 18 is presented in the paragraphs below.

Costs for preparers

16 EFRAG's assessment is that the requirements in IFRIC 18 concerning the recognition and measurement of any items of PPE deemed to have been transferred as a result of the transaction will involve those preparers either not currently recognising such assets or not measuring them at fair value in some incremental costs in the year of the transfer. If such transfers are a regular part of the entity's business model, this will be an incremental ongoing cost. EFRAG's assessment is however that these costs are unlikely to be significant, particularly as it would appear that the fair value measures required should be reasonably straight-forward to estimate. EFRAG also understands that some entities are currently applying the approach required by the Interpretation, and for them there will be no incremental cost.

17 EFRAG recognises that the requirements in IFRIC 18 concerning the 'credit side' of the transaction might involve some preparers in making changes to their existing accounting, either to recognise revenue that was not previously being recognised (because an asset transfer for value was not being recognised in the financial statements) or to change the pattern of revenue recognition.

(a) EFRAG's assessment is that any incremental costs involved in recognising revenue that was not previously recognised will be insignificant.

(b) EFRAG believes that the incremental ongoing costs involved in any change in revenue recognition pattern could be more significant because of the additional complexity that might arise in identifying the separately identifiable services involved and accounting for each one separately. There might also be some year one costs involved to set up the necessary procedures and systems. However, EFRAG's assessment is that for the vast majority of entities involved these costs are unlikely to be significant.

18 EFRAG's assessment is that the requirements in IFRIC 18 concerning the accounting treatment of transfers of cash will have very similar cost implications for preparers to those described in paragraphs 16 and 17.

19 IFRIC 18 is to be applied prospectively from 1 July 2009, although earlier application is permitted. Thus, there are no costs that entities will be required to incur to transition to IFRIC 18.

20 In summary, EFRAG's assessment is that IFRIC 18 will result in some year one costs and some incremental ongoing costs for some preparers, but that these costs are unlikely to be significant.

Costs and benefits for users

21 EFRAG is not aware of any aspect of IFRIC 18 that will increase the costs users will incur in analysing the financial statements as a result of its adoption.

22 EFRAG also notes that IFRIC 18 will reduce to some extent the diversity of accounting in respect to the accounting for transfers of assets entities receive from their customers and which are within the scope of IFRIC 18. This will benefit users. In some cases, the effect of IFRIC 18 will also be to enhance the relevance of the information being provided by bringing the accounting treatment of the transfers falling within the scope of IFRIC 18 into line with other revenue-generating transactions. Where that is the case, EFRAG believes that the benefit could be significant.

Conclusion

23 Summarising the comments above, EFRAG's assessment is as follows.

(a) IFRIC 18 is likely to involve some preparers in some additional year one and ongoing costs. Those costs are however unlikely to be significant.

(b) IFRIC 18 is likely to involve users in no year one or ongoing incremental costs.

(c) IFRIC 18 is likely to result in some improvements in the comparability of the information provided—and in some cases the relevance—and thus bring benefits to users.

24 EFRAG has found it difficult to assess the costs of implementing IFRIC 18 in the EU relative to the benefits to be derived, because the costs and benefits will vary so much depending on the accounting currently adopted and the frequency of the transactions involved. However, EFRAG's assessment is that the costs are likely to be highest in circumstances in which the benefits are also likely to be the highest and that overall the benefits of implementing IFRIC 18 in the EU are likely to outweigh the costs involved.

Stig Enevoldsen
EFRAG Chairman
27 May 2009