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**International
Accounting Standards
Board**

This observer note is provided as a convenience to observers at IFRIC meetings, to assist them in following the IFRIC's discussion. Views expressed in this document are identified by the staff as a basis for the discussion at the IFRIC meeting. This document does not represent an official position of the IFRIC. Decisions of the IFRIC are determined only after extensive deliberation and due process. IFRIC positions are set out in Interpretations.

Note: The observer note is based on the staff paper prepared for the IFRIC. Paragraph numbers correspond to paragraph numbers used in the IFRIC paper. However, because the observer note is less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IFRIC meeting: September 2008, London
Project: D24 Customer Contributions: Revised draft
(Agenda Paper 2C)

The following paper is a revised draft of D24 prepared by the staff for discussion at the September 2008 IFRIC meeting. The basis for conclusions will be provided at the next IFRIC meeting if the IFRIC agrees with the basic approach taken in this draft.

References

- *Framework for the Preparation and Presentation of Financial Statements*
- *IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors*
- *IAS 16 Property, Plant and Equipment*
- *IAS 18 Revenue*

Background

- 1 In some industries, entities receive contributions of property, plant and equipment that must be used to connect customers to a network and provide them with on-going access to a supply of goods or services. Sometimes, the entities receive cash contributions for the acquisition or construction of such items of property, plant and equipment. In some cases, the entity that connects the customer to the network and then provides on-going access to a supply of goods or services may not be the supplier of the related goods or

- services. Customers are typically required to pay additional amounts for the goods or services based on usage.
- 2 In some cases, the entity that makes the contribution is not the entity that will eventually have access to the supply of goods or services and will use those goods or services. For example, the property, plant or equipment may be contributed by a property developer in relation to a number of residential houses it is constructing. In this case it is the homeowners that will eventually use the goods or services. However, for convenience this Interpretation refers to the entity making the contribution as the customer.

Scope

- 3 This Interpretation applies to the accounting for contributions by entities that receive such contributions from their customers.
- 4 Agreements in the scope of this Interpretation are agreements in which an entity receives an item of property, plant and equipment (or cash for the construction or acquisition of such item) from a customer that the entity must use to connect the customer to a network and/or to provide on-going access to a supply of goods or services.
- 5 This Interpretation does not apply to agreements in which the contribution is either a government grant as defined in IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* or an infrastructure used in a public-to-private service concession arrangement that falls within the scope of IFRIC 12 *Service Concession Arrangements applies*.

Definitions

- 6 [the definitions of *customer contribution* and *cash contribution* set out in D24 have not been carried over in this revised draft. The staff's view are that such definitions are not necessary with a clarified scope]

Issues

- 7 The Interpretation addresses the following issues:
- (a) Whether the recognition criteria of an asset are met?
 - (b) If the recognition criteria are met, how should the contributed item of property, plant and equipment be measured on initial recognition?
 - (c) If the item of property, plant and equipment is measured at fair value on initial recognition, how should the resulting credit be accounted for?
 - (d) How should an entity account for the receipt of a cash contribution?

Consensus

Recognition and measurement of a contributed item of property, plant and equipment

- 8 When an entity receives a customer contribution in the form of an item of property, plant and equipment, it assesses whether the contributed asset meets the recognition criteria set out in the *Framework*. Paragraph 89 of the Framework states that ‘an asset is recognised in the balance sheet when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably’. In most circumstances, the entity obtains the right of ownership of the contributed item of property, plant and equipment and is responsible for repairs, maintenance, upgrade and replacement of that asset. When assessing whether the recognition criteria are met, the entity shall also consider whether it controls the benefits that are expected to flow from the contributed asset.
- 9 In contrast, if the customer continues to control the use of the asset, the recognition criteria would not be met despite the contribution. The customer controls the use of the asset if either of the following conditions is met:
- (a) the customer has the ability or right to operate the asset or direct others to operate the asset in a manner it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
 - (b) the customer has the ability or right to control physical access to the asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
- 10 If the entity concludes that the recognition criteria are met, it shall recognise the contributed asset as property, plant and equipment and measure it on initial recognition at its fair value in accordance with paragraph 24 of IAS 16 *Property, Plant and Equipment*.

How should the credit be accounted for?

- 11 The following discussion assumes that the entity receiving a customer contribution in the form of an item of property, plant and equipment concluded that the item should be recognised and measured in accordance with paragraphs 8 and 10 of this Interpretation.
- 12 Paragraph 12 of IAS 18 *Revenue* states that ‘when goods are sold or services are rendered in exchange for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue.’ According to the terms of the agreements within the scope of this Interpretation, a contributed item of property, plant and equipment would be exchanged for dissimilar goods or services. Consequently, the entity shall recognise revenue in accordance with IAS 18.

Identifying the components of the transaction

- 13 Goods or services to be provided in exchange for the customer contribution may include connecting the customer to a network and providing on-going access to a supply of goods or services. Regardless of whether the customer contribution is an item of property, plant and equipment or cash, the entity that receives the contribution shall apply the recognition criteria in IAS 18 to the separately identifiable components of a single transaction in accordance with paragraph 13 of that Standard.

- 14 Features that indicate that connecting the customer to the network is a separately identifiable component of the transaction include:
- (a) a service is provided to the customer and represents value for that customer (eg a house connected to an electricity network is more valuable than a non-connected house);
 - (b) the entity receives consideration for this service, either in cash or in the form of an item of a property, plant and equipment and the fair value of that consideration can be measured reliably;
 - (c) the service could be sold separately.
- 15 A feature that indicates that the service to provide on-going access to a supply of goods or services is a component of the transaction is that the goods or services are delivered to the customer in the future at a price lower than would otherwise be charged.
- 16 Conversely, features that indicate that an obligation to provide on-going access to a supply of goods or services is not a component of the transaction include:
- (a) customers are charged a fee for on-going access either as a separate charge or as a minimum periodic charge regardless of usage;
 - (b) customers that make a contribution pay the same price for the on-going service as those that do not;
 - (c) customers have the ability to choose to receive goods or services from suppliers other than the entity, although they must use the entity's network to receive them.

Such features indicate that the obligation to provide on-going access arises from the terms of the entity's operating license or other regulation rather than from the contribution.

Revenue recognition

- 17 When more than one component is identified, the fair value of the total consideration received or receivable for the agreement shall be allocated to each component and the recognition criteria of IAS 18 shall be applied to each component.
- 18 If a service to provide on-going access to a supply of goods or services is identified as a separately identifiable component of the transaction, the period over which revenue shall be recognised for this component is the period over which the related service is provided, but it cannot be longer than the useful economic life of the asset that is contributed or financed by the customer.

Disclosures

- 19 [Should the disclosures already required by IAS 1, IAS 16 and IAS 18 be considered sufficient or should specific additional disclosures be required?]

Effective date and transition

- 20 An entity shall apply this Interpretation for annual periods beginning on or after [date to be set]. If an entity applies this Interpretation for a period beginning before [date to be set], it shall disclose that fact.
- 21 [Changes in accounting policy shall be accounted for retrospectively in accordance with IAS 8].