

Transfers of Assets from Customers

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Interpretation of Statutory Board Financial Reporting Standard (INT SB-FRS) 118 *Transfers of Assets from Customers* is set out in paragraphs 1–22 and the Appendix. INT SB-FRS 118 is accompanied by Illustrative Examples and a Basis for Conclusions. The scope and authority of Interpretations are set out in the *Preface to Interpretations of Statutory Board Financial Reporting Standards*.

Interpretation of Statutory Board Financial Reporting Standard INT SB-FRS118 *Transfers of Assets from Customers*

References

- *Framework for the Preparation and Presentation of Financial Statements*
- SB-FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*
- SB-FRS 16 *Property, Plant and Equipment*
- SB-FRS 18 *Revenue*
- SB-FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance*
- INT SB-FRS 112 *Service Concession Arrangements*

Background

- 1 In the utilities industry, an entity may receive from its customers items of property, plant and equipment that must be used to connect those customers to a network and provide them with ongoing access to a supply of commodities such as electricity, gas or water. Alternatively, an entity may receive cash from customers for the acquisition or construction of such items of property, plant and equipment. Typically, customers are required to pay additional amounts for the purchase of goods or services based on usage.
- 2 Transfers of assets from customers may also occur in industries other than utilities. For example, an entity outsourcing its information technology functions may transfer its existing items of property, plant and equipment to the outsourcing provider.
- 3 In some cases, the transferor of the asset 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. However, for convenience this Interpretation refers to the entity transferring the asset as the customer.

Scope

- 4 This Interpretation applies to the accounting for transfers of items of property, plant and equipment by entities that receive such transfers from their customers.
- 5 Agreements within the scope of this Interpretation are agreements in which an entity receives from a customer an item of property, plant and equipment that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services, or to do both.
- 6 This Interpretation also applies to agreements in which an entity receives cash from a customer 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 either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services, or to do both.
- 7 This Interpretation does not apply to agreements in which the transfer is either a government grant as defined in SB-FRS 20 or infrastructure used in a service concession arrangement

that is within the scope of INT SB-FRS 112.

Issues

- 8 The Interpretation addresses the following issues:
- (a) Is the definition of an asset met?
 - (b) If the definition of an asset is met, how should the transferred 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 the entity account for a transfer of cash from its customer?

Consensus

Is the definition of an asset met?

- 9 When an entity receives from a customer a transfer of an item of property, plant and equipment, it shall assess whether the transferred item meets the definition of an asset set out in the *Framework*. Paragraph 49(a) of the *Framework* states that 'an asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.' In most circumstances, the entity obtains the right of ownership of the transferred item of property, plant and equipment. However, in determining whether an asset exists, the right of ownership is not essential. Therefore, if the customer continues to control the transferred item, the asset definition would not be met despite a transfer of ownership.
- 10 An entity that controls an asset can generally deal with that asset as it pleases. For example, the entity can exchange that asset for other assets, employ it to produce goods or services, charge a price for others to use it, use it to settle liabilities, hold it, or distribute it to owners. The entity that receives from a customer a transfer of an item of property, plant and equipment shall consider all relevant facts and circumstances when assessing control of the transferred item. For example, although the entity must use the transferred item of property, plant and equipment to provide one or more services to the customer, it may have the ability to decide how the transferred item of property, plant and equipment is operated and maintained and when it is replaced. In this case, the entity would normally conclude that it controls the transferred item of property, plant and equipment.

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

- 11 If the entity concludes that the definition of an asset is met, it shall recognise the transferred asset as an item of property, plant and equipment in accordance with paragraph 7 of SB-FRS 16 and measure its cost on initial recognition at its fair value in accordance with paragraph 24 of that Standard.

How should the credit be accounted for?

- 12 The following discussion assumes that the entity receiving an item of property, plant and equipment has concluded that the transferred item should be recognised and measured in accordance with paragraphs 9–11.
- 13 Paragraph 12 of SB-FRS 18 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 transfer of an item of property, plant and equipment would be an exchange

for dissimilar goods or services. Consequently, the entity shall recognise revenue in accordance with SB-FRS 18.

Identifying the separately identifiable services

- 14 An entity may agree to deliver one or more 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. In accordance with paragraph 13 of SB-FRS 18, the entity shall identify the separately identifiable services included in the agreement.
- 15 Features that indicate that connecting the customer to a network is a separately identifiable service include:
- (a) a service connection is delivered to the customer and represents stand-alone value for that customer;
 - (b) the fair value of the service connection can be measured reliably.
- 16 A feature that indicates that providing the customer with ongoing access to a supply of goods or services is a separately identifiable service is that, in the future, the customer making the transfer receives the ongoing access, the goods or services, or both at a price lower than would be charged without the transfer of the item of property, plant and equipment.
- 17 Conversely, a feature that indicates that the obligation to provide the customer with ongoing access to a supply of goods or services arises from the terms of the entity's operating licence or other regulation rather than from the agreement relating to the transfer of an item of property, plant and equipment is that customers that make a transfer pay the same price as those that do not for the ongoing access, or for the goods or services, or for both.

Revenue recognition

- 18 If only one service is identified, the entity shall recognise revenue when the service is performed in accordance with paragraph 20 of SB-FRS 18.
- 19 If more than one separately identifiable service is identified, paragraph 13 of SB-FRS 18 requires the fair value of the total consideration received or receivable for the agreement to be allocated to each service and the recognition criteria of SB-FRS 18 are then applied to each service.
- 20 If an ongoing service is identified as part of the agreement, the period over which revenue shall be recognised for that service is generally determined by the terms of the agreement with the customer. If the agreement does not specify a period, the revenue shall be recognised over a period no longer than the useful life of the transferred asset used to provide the ongoing service.

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

- 21 When an entity receives a transfer of cash from a customer, it shall assess whether the agreement is within the scope of this Interpretation in accordance with paragraph 6. If it is, the entity shall assess whether the constructed or acquired item of property, plant and equipment meets the definition of an asset in accordance with paragraphs 9 and 10. If the definition of an asset is met, the entity shall recognise the item of property, plant and equipment at its cost in accordance with SB-FRS 16 and shall recognise revenue in accordance with paragraphs 13–20 at the amount of cash received from the customer.

Effective date and transition

- 22 An entity shall apply this Interpretation prospectively to transfers of assets from customers received on or after 1 July 2009. Earlier application is permitted provided the valuations and

other information needed to apply the Interpretation to past transfers were obtained at the time those transfers occurred. An entity shall disclose the date from which the Interpretation was applied.

Illustrative examples

These examples accompany, but are not part of, INT SB-FRS 118.

Example 1

- IE1 A real estate company is building a residential development in an area that is not connected to the electricity network. In order to have access to the electricity network, the real estate company is required to construct an electricity substation that is then transferred to the network company responsible for the transmission of electricity. It is assumed in this example that the network company concludes that the transferred substation meets the definition of an asset. The network company then uses the substation to connect each house of the residential development to its electricity network. In this case, it is the homeowners that will eventually use the network to access the supply of electricity, although they did not initially transfer the substation. By regulation, the network company has an obligation to provide ongoing access to the network to all users of the network at the same price, regardless of whether they transferred an asset. Therefore, users of the network that transfer an asset to the network company pay the same price for the use of the network as those that do not. Users of the network can choose to purchase their electricity from distributors other than the network company but must use the company's network to access the supply of electricity.
- IE2 Alternatively, the network company could have constructed the substation and received a transfer of an amount of cash from the real estate company that had to be used only for the construction of the substation. The amount of cash transferred would not necessarily equal the entire cost of the substation. It is assumed that the substation remains an asset of the network company.
- IE3 In this example, the Interpretation applies to the network company that receives the electricity substation from the real estate company. The network company recognises the substation as an item of property, plant and equipment and measures its cost on initial recognition at its fair value (or at its construction cost in the circumstances described in paragraph IE2) in accordance with SB-FRS 16 *Property, Plant and Equipment*. The fact that users of the network that transfer an asset to the network company pay the same price for the use of the electricity network as those that do not indicates that the obligation to provide ongoing access to the network is not a separately identifiable service of the transaction. Rather, connecting the house to the network is the only service to be delivered in exchange for the substation. Therefore, the network company should recognise revenue from the exchange transaction at the fair value of the substation (or at the amount of the cash received from the real estate company in the circumstances described in paragraph IE2) when the houses are connected to the network in accordance with in paragraph 20 of SB-FRS 18 *Revenue*.

Example 2

- IE4 A house builder constructs a house on a redeveloped site in a major city. As part of constructing the house, the house builder installs a pipe from the house to the water main in front of the house. Because the pipe is on the house's land, the owner of the house can restrict access to the pipe. The owner is also responsible for the maintenance of the pipe. In this example, the facts indicate that the definition of an asset is not met for the water company.
- IE5 Alternatively, a house builder constructs multiple houses and installs a pipe on the commonly owned or public land to connect the houses to the water main. The house builder transfers ownership of the pipe to the water company that will be responsible for its maintenance. In this example, the facts indicate that the water company controls the pipe and should recognise it.

Example 3

- IE6 An entity enters into an agreement with a customer involving the outsourcing of the customer's information technology (IT) functions. As part of the agreement, the customer transfers ownership of its existing IT equipment to the entity. Initially, the entity must use the equipment to provide the service required by the outsourcing agreement. The entity is responsible for maintaining the equipment and for replacing it when the entity decides to do so. The useful life of the equipment is estimated to be three years. The outsourcing agreement requires service to be provided for ten years for a fixed price that is lower than the price the entity would have charged if the IT equipment had not been transferred.
- IE7 In this example, the facts indicate that the IT equipment is an asset of the entity. Therefore, the entity should recognise the equipment and measure its cost on initial recognition at its fair value in accordance with paragraph 24 of SB-FRS 16. The fact that the price charged for the service to be provided under the outsourcing agreement is lower than the price the entity would charge without the transfer of the IT equipment indicates that this service is a separately identifiable service included in the agreement. The facts also indicate that it is the only service to be provided in exchange for the transfer of the IT equipment. Therefore, the entity should recognise revenue arising from the exchange transaction when the service is performed, ie over the ten-year term of the outsourcing agreement.
- IE8 Alternatively, assume that after the first three years, the price the entity charges under the outsourcing agreement increases to reflect the fact that it will then be replacing the equipment the customer transferred.
- IE9 In this case, the reduced price for the services provided under the outsourcing agreement reflects the useful life of the transferred equipment. For this reason, the entity should recognise revenue from the exchange transaction over the first three years of the agreement.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, INT SB-FRS 118.

Introduction

- BC1 This Basis for Conclusions summarises the considerations in reaching the consensus. It gave greater weight to some factors than to others.
- BC2 Draft Interpretation D24 *Customer Contributions* was released for public comment in February 2008.

Background

- BC3 A request was received 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. It was 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, it was 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 the redeliberations, it was 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 SB-FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
- BC6 In the redeliberations, it was 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. An example was also added 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 view was reaffirmed 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 SB-FRSs such as INT SB-FRS 112 *Service Concession Arrangements* and SB-FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. In the redeliberations, it was noted that in a public-to-private service concession arrangement within the scope of INT SB-FRS 112 the grantor controls the infrastructure, not the operator. Therefore, it was 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 INT SB-FRS 112. It was also clarified that SB-FRS 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 SB-FRS 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, it was noted that this Interpretation might also be relevant to industries other than utilities. The background section of the Interpretation was also clarified by 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 SB-FRS 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 that was 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 the redeliberations, it was discussed regarding the different steps that D24 required an entity to follow to determine whether an asset should be recognised, including the consideration of INT SB-FRS 104 *Determining whether an Arrangement contains a Lease* and SB-FRS 17 *Leases*. It was 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* and the additional guidance in paragraphs 55 and 57 of the *Framework*.

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

- BC14 It was 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 It was noted that both paragraph 24 of SB-FRS 16 *Property, Plant and Equipment* and paragraph 12 of SB-FRS 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 SB-FRS 16 and measure it on initial recognition at its fair value in accordance with paragraph 24 of that Standard. It was 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 for reconsideration of the revenue recognition issue on the basis of an SB-FRS 18 approach.
- BC18 In the redeliberations, it was 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. It was concluded that identifying the separately identifiable services of a single agreement depends on facts and circumstances and that judgement is required. It was also acknowledged that a practical weakness of SB-FRS 18 is that it gives insufficient guidance on agreements that deliver more than one good or service to the customer. Therefore, it was decided to develop guidance based on paragraph 13 of SB-FRS 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 SB-FRS 18, it was 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 SB-FRS 18 should be applied to each service. It was noted that INT SB-FRS 112 *Service Concession Arrangements* and INT SB-FRS 113 *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 INT SB-FRS 112 and paragraphs 5–7 of INT SB-FRS 113). Therefore, it was 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 for clarification 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 It was 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 view was reaffirmed 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 respondents' view was agreed with, and it was noted that paragraph 11 of SB-FRS 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 proposals related to transfers of cash. However, some respondents asked for clarification on the circumstances in which a cash transfer would be within the scope of the Interpretation.
- BC24 In the redeliberations, 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 was discussed. The view in D24 was reaffirmed: 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 It was 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, it was concluded that retrospective application may be impracticable and that the Interpretation should require prospective application to transfers received after its effective date. However, it was 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, it was 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.* It was 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, it was also decided to develop guidance based on paragraph 13 of SB-FRS 18 to help identify the separately identifiable services to be delivered in exchange for the transferred asset.
 - (c) *Title of the Interpretation.* It was noted that in some jurisdictions, the term 'contribution' has the implication of a donation rather than an exchange transaction. In addition, it was noted that this term might be difficult to translate into some languages. For that reason, it was decided to use the term 'transfer' and redrafted the Interpretation accordingly.
 - (d) *Illustrative examples.* It was decided that illustrative examples should accompany, but not be part of, the Interpretation to help entities apply the Interpretation.