



British Universities Finance Directors Group (BUFDG)

FRED 46, 47 and 48: BUFDG FRG Response

The Financial Reporting Group of the British University Finance Directors Group (BUFDG FRG) fulfils the role of technical working party to the Further and Higher Education SORP Board. In readiness for the introduction of FRS102 the SORP Board have, via BUFDG FRG, commenced work on the development of a new IFRS-based SORP.

BUFDG FRG believes that the proposals set out in FRED 46, 47 and 48 represent a substantial improvement on former proposals and we warmly welcome them. Our response to the ASBs consultation is limited to areas where we wish to make comment.

QUESTION 1

The ASB is setting out the proposals in this revised FRED following a prolonged period of consultation. The ASB considers that the proposals in FREDs 46 to FRED 48 achieve its project objective: To enable users of accounts to receive high-quality, understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.

Do you agree?

BUFDG FRG support the proposals as an optimal solution for the completion of the 'IFRS' project across UK entities. However, we do have reservations about some important aspects relating to revenue recognition, performance conditions and the lack of definition on what constitutes a public benefit entity, which we discuss below in the 'Other Issues' section.

QUESTION 5

In relation to the proposals for specialist activities, the ASB would welcome views on:

- (a) Whether and, if so, why the proposals for agriculture activities are considered unduly arduous? What alternatives should be proposed?
- (b) Whether the proposals for service concession arrangements are sufficient to meet the needs of preparers?

Service Concession Arrangements (FRED48 Section 34, Specialised Activities, para 34.12-34.14)

We have concerns that the proposals for service concession arrangements have not been sufficiently thought through.

Para 34.12-34.14 in FRED48 are based on IFRIC12 – Service Concession Arrangements. This was developed to assist private entities, as grantees, in accounting for ‘public to private’ type arrangements that developed out of PFI-style contractual arrangements.

IFRIC12 strictly applies to grantees (“concession operators”) not grantors (“public bodies”) and so provides detailed requirements on how to account for service concession arrangements by the operator. It provides no information on how to account for such schemes for the grantors. This lack of detail could be open to interpretation and ambiguity if it is to be applied by grantors. Greater clarity is also needed regarding what constitutes a service concession, given that contracts are highly complex and vary greatly and a common type of service concession in the higher education sector (called nomination agreements’) does not fit well in IFRIC12.

IFRIC12 applies to private/public arrangements between private entities and government bodies.

IFRIC12 para 3, states (*our emphasis in bold*):

*“A feature of these service arrangements is the **public service nature of the obligation** undertaken by the operator”*

*“The service arrangement contractually obliges the operator to provide the services to the public on behalf of **the public sector entity**.”*

The first line of FRED48 para 34.12 states “a service concession or other public sector body (the grantor)...”. We are unsure that this can be taken to extend the scope of IFRIC 12 to grantors who are not public sector entities, such as public benefit entities (e.g. universities). Although we think it would be helpful for the standard to be specific as to where the boundary should be drawn as universities are not public sector bodies but are private bodies with a mixed economy of funding, part of which is subject to contractual arrangements with the state.

FRED48 also extends IFRIC12 to private entities who may act as grantors. This is a significant extension and we would wish the ASB to reflect on this and ensure it is what is

intended. We can see logic in grantors adopting an accounting treatment that mirrors that of the grantee, however, IFRIC12 has been developed from a single perspective so we do not believe IFRIC12 should be mirrored without wider consultation. However, we believe that conceptually, it is appropriate to extend IFRIC12 to public benefit entities.

We have no comment on whether private entities who enter service concession arrangements as grantors will be affected adversely or suffer unintended consequences as a result of the way FRED48 widens the scope of IFRIC12. Our concern is more one of governance and consultation given the wider scope of FRED48 compared to IFRIC12.

We do, however, have a more substantive concern. As currently drafted FRED48 (and IFRIC12) does not address a style of service concession arrangement that is now very common in higher education called Nomination Agreements. These agreements are established between universities and private owners/operators of student accommodation. Under such Nomination Arrangements the University underwrites the cost of the service if the operator is unable to attract sufficient demand from students. Such underwriting arrangements range from those that are annual (i.e. the University only provides underwriting for 1 year) or are longer term in nature. These arrangements are qualitatively different from public-private arrangements envisaged under IFRIC12.

One approach that might be adopted by the ASB is to make it clear that FRED48, Section 34, Para 34.12-34.14 applies to grantees (as intended by IFRIC12) and leave it to individual public benefit entity SORPs to address service concession accounting with respect to grantors.

QUESTION 8

Do you agree with the effective date? If not, what alternative date would you prefer and why?

We support the proposed effective date of 1 January 2015.

It is likely that the new SORP will be available in time to enable institutions to prepare 2014-15 accounts in compliance with it, i.e. to adopt early. We believe early adoption across the sector will undermine consistency and will be problematic for regulators. While we believe we could prevent early adoption via the SORP it would be preferable for all public benefit entities to follow the same line and therefore we ask the ASB to deny the option of early adoption for all PBEs from the outset.

QUESTION 9

Do you support the alternative view, or any individual aspect of it?

We do not support the alternative view. While we have sympathy with the thrust of the proposals in driving out complexity, we believe this would be better tackled by targeting the IASB rather than introducing a distinctly different accounting approach to financial reporting for non-listed and public benefit entities. The alternative view, applied solely to

non-listed and public benefit entities would result in the continuation of an inconsistent reporting framework which we could not support.

Other Issues

We would also like to raise some particular issues in relation to the FREDs.

Income Recognition and Performance Conditions

We are concerned with the definitions provided for ‘performance conditions’ and ‘restrictions’ and the way they interact with the requirements for revenue recognition. We do not agree with the accounting treatment proposed for income subject to ‘performance conditions’ (as defined). We do not see that a mere restriction (in the general meaning of this term) placed on the purposes for which a donation was made should result in non-recognition of income. Ultimately, it is wholly within the recipient entity’s control to spend the money received on the purpose for which it is donated and therefore would not seem to meet the definition of a liability.

The definition of performance conditions should not be based on whether funds are repayable to the donor or not but should instead relate to the delivery of a service or an agreed output(s)

We also note that the section dealing with the accounting for grants contains an accounting policy choice (performance or accruals model), whereas the accounting for non-exchange transactions does not (performance model only). However, there does not appear to be anything in FRED 48 to guide an entity as to whether a receipt should be classified as a grant or as a non-exchange transaction. We therefore feel that the guidance should more clearly distinguish between these two types of transaction.”

Public Benefit Entity Definition

The revised FREDs omit the application guidance on the definition of a public benefit entity which appeared in FRED 45. As public benefit entities are a distinct sector we feel that the short definitions provided by the revised FRED should be supplemented by the application guidance provided in FRED45.

Grants and Donations

Section 24 (Grants) links to a definition of a government grant in the glossary, but does not define grants in general, yet section 24 applies to grants “*by government and others*”. Definitions also need to reflect that it is receivables that are accounted for. We propose the following replacement:

FRED48 24.1 This section specifies the accounting for all grants receivable from governments and others.

Glossary 'Grant' A grant is assistance in the form of a transfer of resources to an entity in return for past or future compliance with specified conditions relating to the operating activities of the entity.

Specialist Activities

Section 34.64 (non-exchange transactions) does not help to determine whether donations could be treated as grants under section 24. We propose the following replacement:

FRED48 34.64 Non-exchange transactions include, but are not limited to, donations (of cash, goods, and services) and legacies. A donation receivable which imposes a specified condition relating to the operating activities of the entity is to be treated as a grant in accordance with the requirements of Section 24.