

**MFOA/AMCTO JOINT MUNICIPAL ACCOUNTING POLICY  
ADVISORY COMMITTEE**

Comments on PSAB's Proposals re the Accounting  
Treatment of Government Transfers and Operating and  
Capital Grant Revenue Recognition

September 27, 2005

**(1) Should Restricted Assets and Revenues, Section PS 3100, still apply to government transfers received by a government? [You may choose more than 1 answer]**

- Yes - it is critical that grants with time or purpose restrictions still give rise to a liability for a government that receives such a grant
- Yes - it is critical that capital transfers received be able to be recognized in revenue when the transfer is used to acquire or develop the related capital asset
- No - capital transfers received should be recognized in revenue on the same basis as the related capital asset is amortized to expenses (CICA HANDBOOK-ACCOUNTING, Government Assistance, Section 3800)
- No - the deferred revenue that is created when a transfer is received under Section PS 3100 does not meet the definition of a liability in Liabilities, Section PS 3200)
- No - a government transfer is revenue when it is authorized by the transferring government and any eligibility criteria have been met by the recipient (existing standard in Government Transfers, Section PS 3410)
- No - a government transfer is revenue when received (cash basis)

**EXPLANATION:**

There is consensus within the committee that Section PS 3100 should apply to government transfers and that the caveats we are raising about PSAB's proposals should also apply.

The imposition of restrictions, whether by time or purpose, create a liability for the recipient government since failure to satisfy those restrictions may result in denial of the grant application. As such, the grant should be recognized as deferred revenue (as against a grant receivable) once grant approval has been received. Grant approval is understood to mean that the grant transfer has been authorized by the granting government and eligibility criteria have been met by the recipient entity.

Furthermore, the grant should be recognized as revenue in the period that the funds are used to develop or acquire the related capital assets, NOT on the amortization basis for the related tangible capital asset (see also our response to Question 3 below).

The distinction in terms of the timing between the recording of the deferred revenue followed by the clearing to revenue is seen as appropriate to allow for cases where a grant is awarded by the granting government but the project is cancelled by the recipient government. In that case, the deferred revenue and grant receivable would be closed out on filing the project cancellation with the granting government.

**(2) Should a multi-year operating transfer be recognized by a recipient government in revenue over the time periods specified in the transfer terms?**

- Yes - as required by Restricted Assets and Revenues, Section PS 3100
- No - a government transfer is revenue for a recipient government when it is authorized by the transferring government and the recipient has met any eligibility criteria (existing standard in Government Transfers, Section PS 3410)
- No - a government transfer is revenue when received (cash basis)

**EXPLANATION:**

There is consensus within the committee that revenue should only be recognized once grant restrictions are met. In the case of an operating grant transfer, conditions are generally met by satisfying the eligibility criteria, although in the case of multi-year operating grants, the time restriction can only be met by the passage of time.

As such, the recognition of revenue should follow the same pattern by recording the revenue proportionately to the time periods of the grant (see our response to Question 3 below).

**(3) When should a capital transfer be recognized in revenue by a recipient government? [You may choose more than 1 answer - for example checking both bullets 3 and 4 would reflect agreement with AED2 proposals.]**

- When received (cash basis)
- When the transfer is authorized by the transferring government and any eligibility criteria have been met by the recipient government (existing standard in Government Transfers, Section PS 3410)
- When the specified capital asset is acquired or developed by the recipient government (existing standard in Restricted Assets and Revenues, Section PS 3100 and is also an AED2 proposal in paragraphs PS 3410.27 and .30-.31) - i.e., the transfer terms meet the definition of external restrictions as defined in Section PS 3100 and they require that the transferred resources be used to acquire or develop a specified capital asset
- When the specified capital asset is used to provide specified services in specified time periods (proposals in AED2 paragraphs PS 3410.30-.31) - i.e., when the transfer terms are sufficiently broad and specific that the transfer meets the definition of a liability in Liabilities, Section PS 3200
- All capital transfers should be recognized by a recipient government in revenue on the same basis as the related capital asset is amortized to expenses (CICA HANDBOOK-ACCOUNTING, Government Assistance, Section 3800)

**EXPLANATION:**

There is consensus within the committee that the capital transfer should be recognized into revenue when the capital asset is acquired or developed by the recipient government or when the specified capital asset is used to provide specified services in specified time periods. However there should also be mention that the capital transfer should be recognized on the financial statements as an asset or liability when the eligibility criteria have been met by the recipient government. In addition, if the capital transfer is recognized into revenue at time of receipt, any unspent portion must be reclassified to deferred revenues at year-end."

**(4) Should a capital transfer and a transfer of a tangible capital asset be accounted for in the same way by a recipient government?**

- Yes - both transfers provide assets of a capital nature to the recipient government
- Yes - in either case, the transfer is revenue for the recipient government when received or receivable UNLESS, because of the nature and extent of the transfer's terms (transfer stipulations), the transfer meets the definition of a liability in Liabilities, Section PS 3200
- No (please explain)

**EXPLANATION:**

**Note:**

- Our position here is based on the assumption that PSAB's proposed application of PS 3150—Tangible Capital Assets—to local governments will proceed.

In each case, the recipient government obtains an asset, either in the form of a financial asset (cash/receivable), or in the form of a tangible capital asset, which is reported at fair market as required under Tangible Capital Assets, Section PS 3150.

It would follow that the recipient government, in either case, should use the same guidelines and principles for revenue recognition in the financial statements.

A capital transfer is recognized as revenue when received or receivable, unless the recipient government has not used the funds for the intended purpose as stipulated by the transferring government.

A transfer of a capital asset is recognized as revenue at fair market value when received or receivable, unless the recipient government has not used the capital asset for the intended purpose as stipulated by the transferring government.

PSAB should provide clarification on how fair market value as compared to historical cost should be determined.

**(5) When should a government grant provided by a transferring government be recognized as an asset by the transferring government?**

- Never - a grant is an expense when it is flowed to recipients (cash basis)
- Never - a grant is an expense when it is authorized and any eligibility criteria have been met by recipients (existing standard in Government Transfers, paragraph PS 3410.07)
- When the terms of the grant (transfer stipulations) are broad and specific enough that they change the substance of the grant so that it meets the definition of an asset for the transferor (see AED2, paragraph PS 3410.09)
- Other (please specify)

**EXPLANATION:**

**Note:**

- The committee’s comments on how transfers are treated by the transferring government are limited to transfers by local government entities. We take no position on how transfers should be treated by “senior” levels of government.

The treatment of transfers between local government entities should be consistent for both transferor and recipient. Since our consensus is that the recipient should record the grant transfer as a liability (deferred revenue) until such point that all restrictions have been discharged, the transferring government should similarly record the grant transfer as an asset until all restrictions have been discharged.

Of issue is the definition of when restrictions may be considered to be discharged. There is no distinction between operating and capital grants, but rather the distinction is between conditional and unconditional grants. Operating grants are viewed as unconditional once eligibility criteria are met, with exception of multiyear grants which have time restrictions.

We request that PSAB provide clarification on when a transfer is authorized and meets eligibility requirements (i.e. application process) and what constitutes discharging of restrictions in order to ensure that the trigger to clear the asset (for the transferring government) and liability (for the recipient government) to expense and revenue occurs in tandem. PSAB also needs to clarify whether restrictions can be met on a progress basis or only on completion (see also our response to Question 6).

**6) When should a capital transfer provided by a transferring government be recognized in expenses by a transferring government?**

- Always when the transfer is authorized and any eligibility criteria have been met by transfer recipients (existing standard in Government Transfers, Section PS 3410)
- When the transfer is authorized by the transferring government and any eligibility criteria have been met by transfer recipients UNLESS, because of the nature and extent of the grant's terms (transfer stipulations), the grant meets the definition of an asset - in those cases, the grant would be recognized in expenses by the transferring government in accordance with the transfer stipulations (see AED2 proposals, paragraph PS 3410.09-.10 and .14)
- When the transfer is flowed (cash basis)
- Other (please specify)

**EXPLANATION:**

**Note:**

- The committee's comments on how transfers are treated by the transferring government are limited to transfers by local government entities. We take no position on how transfers should be treated by "senior" levels of government.

There is consensus within the committee that the transfer should be recognized in expenses at the point where the transfer is authorized, eligibility criteria are met, and when all restrictions have been discharged. However, clarification is needed from PSAB on certain points.

In the case where there are no restrictions (single-year operating grants), the grant would be recorded in expenses as it is awarded (transfer is authorized, eligibility criteria met).

In the case where there are restrictions (time or purpose), the grant is recorded as an asset, and only recorded in expense as the restrictions are discharged. Municipalities should not recognize the revenue once the eligibility has been met during the application phase, but only once the conditions/expenditures have been met (i.e. progress claim submitted).

For multi-year capital grants, the grant should be allowed to be recorded in expenses on a progress or milestone basis, rather than waiting for completion of the project. Even though it could be argued that restrictions would not be fully met prior to completion, it is felt that not recording any expense until full completion would introduce new volatility into the financial statements. Allowing for recording of expenses on a progress basis follows much of current practice for local governments, especially in the treatment of development charges.

Clarification is required on what constitutes exercising of transfer authority. Is a transfer authorized during the eligibility/application phase or is a transfer authorized when a progress claim has been filed and/or approved?

**(7) Should a capital transfer and a transfer of a tangible capital asset be accounted for in the same way by a transferring government?**

- Yes - both are expenses for the transferor
- Yes - in either case the transfer is an expense UNLESS, because of the nature and extent of the transfer terms (transfer stipulations), the transfer meets the definition of an asset (see AED2 proposals, paragraph PS 3410.09-.10, .14 and .23)
- No (please explain)

**EXPLANATION:**

**Note:**

- Our position here is based on the assumption that PSAB’s proposed application of PS 3150—Tangible Capital Assets—to local governments will proceed.
- The committee’s comments on how transfers are treated by the transferring government are limited to transfers by local government entities. We take no position on how transfers should be treated by “senior” levels of government.

In each case the transferring government is transferring an asset/economic resource, either in the form of a financial asset (cash), or in the form of a tangible capital asset, which is transferred at net book value.

If there are no transfer stipulations, either transfer results in an outflow or reduction of assets/economic resources, which is reported as an expense in the financial statements of the transferring government.

If there are transfer stipulations, such that the transferring government obtains/retains control of an economic resource, either transfer is reported as an asset in the financial statements of the transferring government.



**(8) When is a transfer authorized such that a local government has little discretion to avoid providing the transfer?**

- When the transfer is announced by the local government
- When an agreement is in place with the transfer recipient(s)
- When the transfer has been approved by the local government council in a by-law or regulation
- When the transfer has been approved by the local government council in a by-law or regulation AND someone with the appropriate level of authority has exercised authority under the by-law or regulation to provide the transfer (see AED2 proposal paragraph PS 3410.33)
- Other (please specify)

**EXPLANATION:**

When they involve the giving up of future economic benefits, items are generally recognized in the financial statements when it is probable that such benefits will be given up. In the case of local governments, approval of a grant by by-law may not necessarily provide sufficient evidence that the benefits are to be provided. Previous actions of Council can be repealed, especially when they related to activities extending beyond the term of a Council. As such, it is reasonable to maintain that a local government has little discretion to avoid a transfer when it has been approved by the government AND when someone in a position of authority has exercised their authority to provide the transfer.

**(9) When is a transfer authorized by a transferring government such that a local government can accrue the transfer in its financial statements?**

- When the transfer is announced by the transferring government
- When an agreement is in place with the transferring government
- When a letter has been received by a recipient government indicating that it will be receiving some grant money
- When each of the evidence in the first three bullets is in place such that the recipient believes that the transferor has little discretion to avoid providing the transfer (see Liabilities, Section PS 3200)
- When the transfer has been approved by the transferring government in legislation, regulations or by-laws
- When the transfer has been approved by the transferring government in legislation, regulations or by-laws AND someone with the appropriate level of authority has exercised authority under the legislation, regulations or by-laws to provide the transfer (see AED2 proposals, paragraph PS 3410.33)
- When a letter has been received from the transferring government indicating that some local governments in the jurisdiction will be receiving some grant money
- Other (please specify)

**EXPLANATION:**

It is generally accepted that revenue may be recognized when it is measurable and the ultimate collection is reasonably assured. For recipients of government transfers, it is reasonable to maintain that the assurance of collection exists when (1) the transferring government has formally approved the transfer (e.g., by law, regulation or by-law) AND (2) someone in a position of authority with the transferring government has taken lawful action to provide the transfer.

The second test is important because it establishes that a previous commitment will be honoured and confirms that the transferring government will not be reversing its previous position. The committee is of the opinion that the current wording related to the second test is vague and that clarification is desirable. In practice, it may be difficult for a recipient government to ever know what actions have been taken internally by another government, which may limit the ability of a recipient to accrue grant revenue.

**ADDITIONAL COMMENTS:**

Further clarification is required for the handling of both conditional and unconditional grants.

Further clarification is required on the determination of when revenue is recognized (i.e. when eligibility has been met in the application process— when the progress claim has been filed, when the progress claim has been approved for payment, when the asset is being developed ( matching principal), when the asset has been completely developed or when the cash is actually received)

Before a decision is made on the proposals for the treatment of Government Transfers and Operating and Capital Grant Revenue Recognition, clarification is needed on the potential impacts of the changes on municipal budgeting and taxation.