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# Comparative Analysis of International Public Sector Accounting Standard 23 and International Accounting Standard 20

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**Abstract**

International Public Sector Accounting Standard (IPSAS) 23: Revenue from Non-exchange Transactions (Taxes and Transfers) is an accounting standard used to account for taxes and transfers. They are applicable to public sector entities [except for Government Business Enterprises (GBEs)]. The standard is also not applicable to private sector entities. IAS 20: Accounting for Government Grants and Disclosure of Government Assistance is the counterparty accounting standard used in private sector (excluding the SMEs) and GBEs with more than 100 employees. Small and Medium Enterprises (SMEs) are required to apply a set of accounting standards known as International Financial Reporting Standards (IFRSs) for SMEs.

The purpose of this paper is to explore the main areas of differences between the IPSAS 23 and IAS 20 and suggest some improvements to them.

This paper discusses the differences between IPSAS 23 and IAS 20 and suggests areas for improvement in both standards on recognition, presentation, and some disclosures.

The methodology used in this paper is the comparative analysis of financial reporting requirements between IPSAS 23 and IAS 20. A desk work research has been conducted to thoroughly compare the two standards and suggest areas for improvement in both standards.

The paper is beneficial to professional accountants as it provides the 'gaps' existing in the IPSAS 23 and IAS 20 and presenting improvements to plug the 'gaps'. No similar attempts have been published hitherto in the financial reporting literature.

**Keywords** - IPSASs, IFRSs, IASs, Revenue from non-exchange transactions, exchange transactions, recognition, presentation, some disclosures.

## 1. Introduction

International Public Sector Accounting Standards (IPSASs) are applicable to public sector entities that choose to use accrual basis of accounting including but not limited to ministries; regional governments; government departments such as prisons and police force; local governments and parastatals provided they are not Government Business Entities (GBEs), (NBAA, 2009).

On the other hand full International Financial Reporting Standards (full IFRSs) [which include International Accounting Standards (IASs)] are applicable to private sector entities other than those regarded as Small and Medium Entities (SMEs). Entities which apply full IFRSs are publicly accountable entities or entities which represent public interest such as entities that take deposits or loans from the public; offer shares to the public; have essential public responsibility or privilege essential public service or entities which hold assets in fiduciary capacity for a broad group of outsiders. According to (NBAA, 2009) example of entities which should use full IFRSs include but not limited to Listed Companies; Banks and Financial Institutions; Insurance Companies; Pension Funds; Utility Companies; Government Agencies; Mutual Funds; Cooperative Societies (including SACCOSs); Securities brokers/dealers; all entities which receive subvention from the government, except those required to use IPSASs; all entities with 100 or more employees (including GBEs); and all entities with capital investments in non-current assets of above TShs 800,000,000/= (including GBEs).

Also according to (NBAA, 2009) IFRSs for SMEs are applicable to the entities which are not publicly accountable or representing public interest; entities including GBEs with less than 100 employees provided they are not supposed to use IPSASs and full IFRSs as specified above; and entities with capital investment in non-current assets of less than TShs 800,000,000/= (including GBEs) provided they are not supposed to use IPSASs and full IFRSs as specified above.

A GBE is defined as an entity that has all of the following features, (NBAA, 2009) and (IPSASB, 2011a)[12]:

(i) Is an entity with the power to contract in its own name;

(ii) Has been assigned the financial and operational authority to carry on a business;

(iii) Sells goods and services, in the normal course of its business, to other entities at a profit or full cost recovery;

(iv) Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length); and

(v) Is controlled by a public sector entity.

GBEs are supposed to apply either full IFRSs or IFRSs for SMEs as the case may be. IPSAS 23: *Revenue from Non-exchange Transactions (Taxes and Transfers)* prescribes requirements for recognition, measurement, presentation and disclosure regarding revenue from non-exchange transactions.

Revenue is said to be from non-exchange transaction when an entity receives value from another entity without directly giving approximately equal value in exchange, (Deloitte, 2012). Revenue from non-exchange transactions comprises taxes and transfers. Taxes are economic benefits or service potential compulsorily paid or payable to public sector entities, in accordance with laws and/or regulations, established to provide revenue to the government. Taxes do not include fines or other penalties imposed for breaches of the law.

Transfers in the context of IPSAS 23 consists of non-exchange transactions other than taxes and they include grants, debt forgiveness, fines, bequests, gifts, donations, goods and services inkind, and the off-market portion of concessionary loans received.

IAS 20: *Accounting for Government Grants and Disclosure of Government Assistance* prescribes requirements for recognition, measurement, presentation and disclosure of government grants. It also provides disclosure requirements of government assistance.

In the context of IAS 20, government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.

The aim of this paper is to explore the differences in recognition, presentation and disclosure requirements between IPSAS 23 and IAS 20 and suggest the improvements to the standards. On the side of revenue from non-exchange transactions, the author focuses on the revenue in the form of transfers which are similar to grants and governments assistance under IAS 20. The reason for choosing transfers is to make the comparison meaningful since taxes are not discussed in IAS 20 for obvious reason that generally entities applying IAS 20 do not impose taxes.

[1] Part of para 7 of IPSAS 1: *Presentation of Financial Statements*

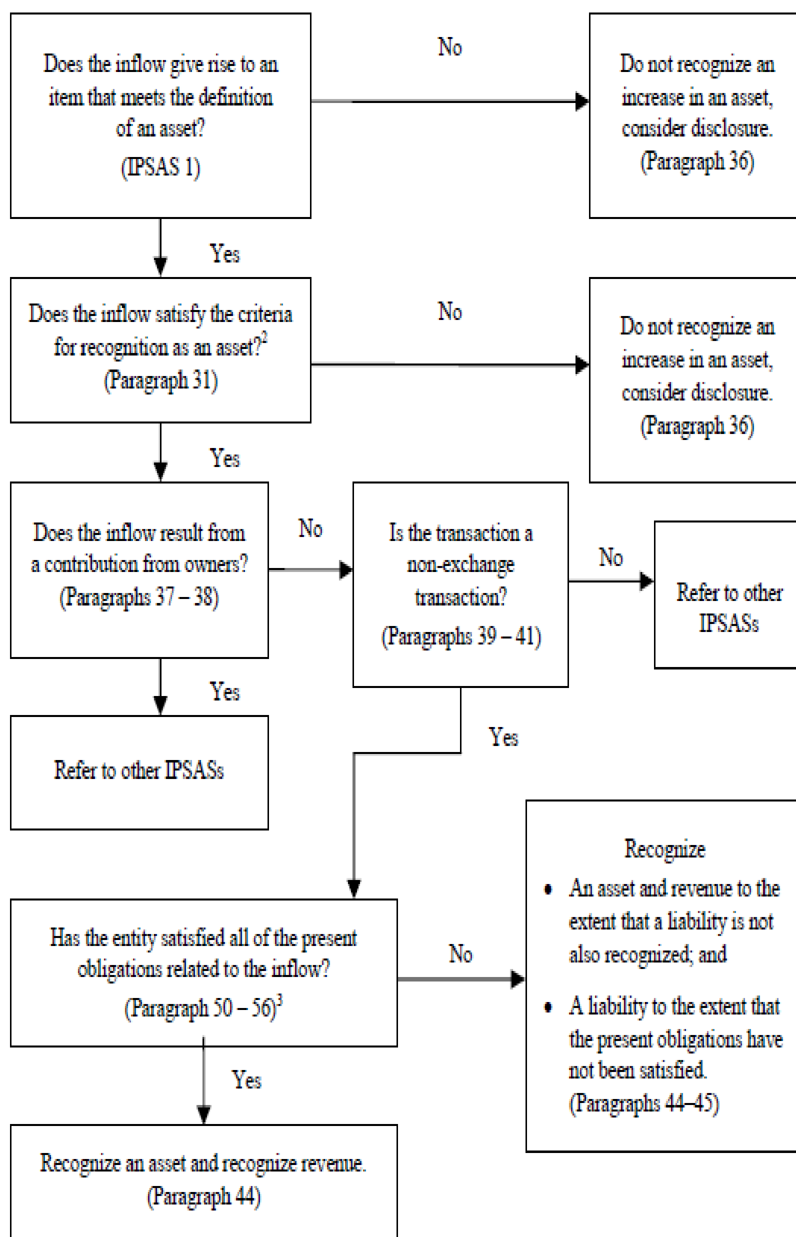
In writing this article the author has mainly used IPSAS 23 and IAS 20 as the main sources of information. The desk work research has been conducted to come up with findings. The financial reporting requirements under the two standards are compared, differences are highlighted and improvements are suggested. The rest of the paper is organized as follows. Part 2.0 covers aspects concerning recognition, presentation and some disclosures under IPSAS 23 and IAS 20; part 3.0 covers suggested improvements to IAS 20 and IPSAS 23 on recognition, presentation and some disclosures and part 4.0 provides the concluding remarks.

## 2. Recognition, Presentation and some Disclosures under IPSAS 23 and IAS 20

### *2.1 Recognition, Presentation and Disclosures under IPSAS 23*

IPSAS 23 requires that when a non-exchange transaction occurs a receiving entity recognizes an asset and at the same time recognizes revenue, except to the extent that a liability is also recognised in respect of the same inflow. The recognition of an asset will be made when an entity gains control of the resources that meet the definition of an asset and satisfy the recognition criteria. Such an entity will also recognise either revenue or liability as the case may be.

The following flowchart provides guidance when recognises the items of assets and revenue or liability.




*Source: IPSAS 23; page 727*

**Figure 1: Illustration of the Analysis of Initial Inflows of Resources**

The flowchart above shows that for an asset to be recognised it must meet both the definition of an asset and recognition criteria for an asset, otherwise consider disclosure of the item.

Assets are defined in IPSAS 1 as resources controlled by an entity as a result of past events, and from which future economic benefits or service potential are expected to flow to the entity, (IPSASB, 2011a)[3].

A resource which meets a definition of as asset will be recognised when it also meets the following recognition criteria, (IPSASB, 2011c)[4]:

[3] Part of para 7 of IPSAS 1: *Presentation of Financial Statements*
[4] Para 3 of IPSAS 23: *Revenue from non-exchange Transactions (Taxes and Transfers)*

(a) It is probable that the future economic benefits or service potential associated with the asset will flow to the entity; and

(b) The fair value of the asset can be measured reliably.

The flowchart also shows that the revenue or liability will be recognised as per IPSAS 23 if the inflow of resource does not come from owners in their capacity as owners. In case the entity has satisfied all the present obligations then an asset and revenue will be recognised. However, an asset and liability will be recognised when there is any unsatisfied obligation.

A resource received in a non-exchange transaction is normally subject to stipulations in the form of either condition(s) or a restriction(s). Stipulations on transferred assets are terms in laws or regulations, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity for example the transferor.

Restrictions on transferred assets are stipulations that limit or direct the purposes for which a transferred asset may be used, but do not specify that future economic benefits or service potential is required to be returned to the transferor if not used as specified. These do not give rise to an obligation to the receiving entity.

Conditions on transferred assets are stipulations that specify that the future economic benefits or service potential embodied in the asset is required to be used by the recipient as specified. In case the recipient of the asset consumes it contrary to the terms then future economic benefits or service potential must be returned to the transferor. For example an entity may be given a bus free of charge for carrying workers to and from the working place with a stipulation that it must be used for that purpose only and that whenever the receiving entity use it for any other purpose it must be returned to the transferor. Such a stipulation is a condition as it creates an obligation to the receiving entity. When a transfer of an asset is attached with a restriction(s) an entity recognises an asset and revenue.

**Example 1**

Temeke Municipal Council (TMC) receives a cheque in terms of a grant of TShs 800,000,000/= from central government to support development in Temeke Municipality. The Council is required to undertake various projects under its jurisdiction according to its priorities spelt out in its strategic plan.

In this case there is a restriction to apply the funds for the development projects which are spelt out in Council's strategic plan. The Council will recognise an asset cash and revenue and will pass the following journal entry:

Dr Bank Account 800,000,000

Cr Revenue 800,000,000

To record the grant received

At the end of the year the Council will present all the above grant revenue to the Statement of Financial Performance[5].

When an entity receives an asset subject to conditions it incurs a present obligation to transfer future economic benefits or service potential to the transferor in case it will not discharge the obligation.

**Example 2**

The Bukoba Municipal Council (BMC) receives a cheque in terms of a grant of TShs 2,000,000,000/= from Ministry of Regional Administration & Local Governments (MRALG) for drilling 100 boreholes. The terms of the grant stipulate that the Council must return immediately the whole amount in case it fails to drill 100 boreholes within one year.

[5] A Statement of Financial Performance is a terminology used in public sector accounting. In private sector we refer to it as A Statement of Comprehensive Income or an Income Statement

In this case the Council recognises the asset cash and a current liability (since it will be required to pay within one year in case it does not fulfill stipulations) and will pass the following journal entry:

Dr Bank Account 2,000,000,000

Cr Current Liability (MRALG) 2,000,000,000

To record the grant received from MRALG

In case the Council completes the drilling exercise within the required time the current liability will be transferred to revenue since there is no longer any obligation. It will pass the following journal entry in this regard:

Dr Current Liability (MRALG) 2,000,000,000

Cr Revenue 2,000,000,000

To record de-recognition of a liability which is now recognised as revenue.

In case the terms stipulate that the Council will return the cash to MRALG equal to unfulfilled portion of the boreholes not drilled within a year it will recognise revenue for fulfilled part only and the unfulfilled remaining part will be repaid to the Ministry as per the terms.

Assume that the Council manages to drill only 50 boreholes. For the fulfilled part of the obligation, it will pass the following journal entry to recognize revenue:

Dr Current Liability (MRALG) 1,000,000,000

Cr Revenue 1,000,000,000

To record de-recognition of a liability on the fulfilled portion of the conditions attached to the grant. This is now recognised as revenue. The remaining balance of TShs 1.000,000/= will be repayable to the Ministry.

IPSAS 23 requires that when an entity receives debt forgiveness it recognises revenue in respect of that debt forgiveness.

**Example 3**

Kinondoni Municipal Council (KMC) has received a debt forgiveness of TShs 30,000,000/= from the Ministry of Regional Administration and Local Governments (MRALG). Upon receiving the documentation for debt forgiveness it will pass the following journal entry:

Dr MRALG 30,000,000

Cr Revenue 30,000,000

To record de-recognition of a liability waived. This is now recognised as revenue.

When a fine becomes receivable it shall be recognised as revenue provided the receivable meets the definition of an asset and satisfies the criteria for recognition as an asset.

**Example 4**

Ilala Municipal Council (IMC) imposes a fine of TShs 2,000,000/= to ABC Ltd for breaching the Municipal's hygiene by-laws. ABC Ltd does not intend to appeal against the decision. IMC shall recognise an asset receivable and revenue. The following journal entry shall be made in this regard:

Dr Receivable (ABC Ltd) 2,000,000

Cr Revenue from fine 2,000,000

To record the fine revenue from ABC Ltd

When an individual writes and communicates a bequest to a public institution naming it to be the beneficiary of his/her wills that public entity shall not recognise such a bequest because the past event for the bequest is the death of the testator (transferor) which has not yet materialised. When the testator dies the entity (recipient) will need to determine if the deceased person's estate is sufficient to meet all claims on it, and satisfy all bequests. If the will is disputed, this will also affect the probability of assets flowing to the entity.[6]

Goods in-kind are recognised as assets when the goods are received, or there is a binding arrangement to receive the goods. If goods in-kind are received without conditions attached, revenue is recognised immediately. If conditions are attached, a liability is recognised, which is reduced and revenue recognised as the conditions are satisfied.

As per IPSAS 23 an entity is permitted but not required to recognise a service in-kind as revenue and as an asset. This requirement is due to the fact that services in-kind are subject to uncertainties including the ability to exercise control over the service in-kind and availability of reliable measure for the same.

However, in case the service in-kind is controlled by a recipient entity and reliable measure exists, the service in-kind may be recognised. It should however, be noted that this kind of asset is immediately consumed, and hence it can be expensed directly[7].

**Example 5**

A public school receives a volunteer service from Education Advisor the fair value of it is determined as TShs 3,000,000/= per month.

The school recognises this as asset and revenue equal to annual fair value and total value for the year will be reflected by the following journal voucher:

Dr Educations Advisor Expense 36,000,000

Cr Revenue 36,000,000

3,000,000 x 12 months

To record annual fair value of education advice received from the Education Advisor.

IPSAS 23 requires non-recognition of a service in-kind for which an entity has insufficient control or reliable measure for it does not exist.

IPSAS 23 encourages an entity to disclose the nature and type of major classes of services in-kind including those recognised. This is just an encouragement but not a requirement. This encouragement is applicable for services in-kind which are material.

Under IPSAS 23 pledges are not recognised because the recipient entity is unable to control the asset until it is received from the donor. However, they may warrant disclosure in case they are material.

### *2.2 Recognition, Presentation and some Disclosures of Government Grants under IAS 20*

Under IAS 20 a government grant is recognised when there is reasonable assurance that[8]:

(a) the entity will comply with the conditions attaching to them; and

[6] Para 91 of IPSAS 23: *Revenue from non-exchange Transactions (Taxes and Transfers)*
[7] Para 99 of IPSAS 23: *Revenue from non-exchange Transactions (Taxes and Transfers)*
[8] Para 7 of IAS 20: *Accounting for Government Grants and Disclosure of Government Assistance*

(b) the grants will be received.

A government grant under IAS 20 includes loan forgiveness which is recognised as revenue when there is reasonable assurance that the conditions attached to the loan forgiveness will be met.

**Example 6**

XYZ Ltd receives documentation for loan forgiveness from the government agency waiving TShs 35,000,000/=. It makes the following journal entry:

Dr Liability (Government Agency) 35,000,000

Cr Revenue 35,000,000

To record de-recognition of a liability waived. It is now recognised as revenue

IAS 20 includes a discussion of two broad approaches of recognising government grants. The approaches are capital approach and income approach. The capital approach is against presentation of government grant in profit or loss part. The arguments for capital approach are as follows[9]:

(a) Government grants are a financing device and should be dealt with as such in the statement of financial position rather than be recognised in profit or loss to offset the items of expense which they finance;

(b) it is inappropriate to recognise government grants in profit or loss, because they are not earned but represent an incentive provided by government without related costs.

Those in support of income approach base on the following arguments:

(a) because government grants are receipts from a source other than shareholders, they should not be recognised directly in equity but should be recognised in profit or loss in appropriate periods;

(b) Government grants are rarely gratuitous. The entity earns them through compliance with their conditions and meeting the envisaged obligations. They should therefore be recognised in profit or loss over the periods in which the entity recognises as expenses the related costs for which the grant is intended to compensate;

(c) as income and other taxes are expenses, it is logical to deal also with government grants, which are an extension of fiscal policies, in the profit or loss.

IAS 20 does not allow the use of capital approach in accounting for government grant. It requires that grants be accounted for by using income approach[10].

IAS 20 requires that grants related to income be presented in the profit or loss (as income or as a reduction to the related expense) part of the statement of comprehensive income in the year in which it meets the recognition criteria.

**Example 7**

On January 2, 2014 ABC Ltd receives TShs 25,000,000/= in a form of a grant from the government of Tanzania to cover part the salaries of its staff.

Assuming that the grant meets the recognition criteria the following journal entry is made:

Dr Bank 25,000,000

Cr Revenue Grant 25,000,000

[9] Paras 13, 14 and 15 of IAS 20: *Accounting for Government Grants and Disclosure of Government Assistance*
[10] Para 16 of IAS 20: *Accounting for Government Grants and Disclosure of Government Assistance*

To record the grant received from government of Tanzania to cover staff salaries

At the end of the financial year the whole amount in revenue account is presented to the profit or loss. The following journal entry will be made:

Dr Revenue Grant 25,000,000

Cr Profit or Loss 25,000,000

To transfer the grant received for meeting salaries to Profit or Loss

Alternatively the amount may be used to reduce the amount of the related expense where the following journal entry is made:

Dr Revenue Grant 25,000,000

Cr Salaries Expense 25,000,000

To record the grant received from government of Tanzania to cover staff salaries

IAS 20 requires that the grant related to asset be presented in the statement of financial position by creating a deferred income account (a non-current liability) or reducing the amount of grant from the amount of a related asset in coming up with the carrying amount of the asset.

As per IAS 20 no revenue is recognised immediately when the grant is related to asset. This practice implies that all stipulations under IAS 20 are regarded as conditions. There are no restrictions under IAS 20. It is therefore, assumed under IAS 20 that all grants related to assets creates obligation(s) to the recipient of the grant.

**Example 8**

On January 2, 2014 ABC Ltd received TShs 300,000,000/= from the government for purchase of modern machinery. The total cost of the machinery purchased is TShs 400,000,000/=. The machinery has an estimated useful life of 10 years with zero residual value.

Under IAS 20 ABL Ltd recognises the grant by making the following journal entry:

Dr Bank 300,000,000

Cr Deferred Income 300,000,000

To record the receipt of a grant from the government for purchasing machinery

On purchase of machinery the company makes the following journal entry:

Dr Machinery 400,000,000

Cr Bank 400,000,000

To record the purchase of the machinery

At the end of each subsequent year the company will make the following journal entries unless it revises the estimates as per the requirements of IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors*:

Dr Deferred Income 30,000,000

Cr Profit or Loss 30,000,000

To allocate the deferred income to the profit or loss

300,000,000/10

Dr Depreciation Expense 40,000,000

Cr Accumulated Depreciation 40,000,000

[400,000,000-0]/10

To record the annual depreciation charge for the machinery

Alternatively, ABC Ltd will make the following journal entry when it initially recognizes the grant:

On purchase of machinery the company makes the following journal entry:

Dr Machinery 100,000,000

Cr Bank 100,000,000

400,000,000 - 300,000,000 = 100,000,000

To record the machinery at an amount net of grant used to purchase the machinery.

At the end of each subsequent year the company will make the following journal entries unless it revises the estimates as per the requirements of IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors*:

Dr Depreciation Expense 10,000,000

Cr Accumulated Depreciation 10,000,000

[100,000,000-0]/10

To record the annual depreciation charge for the machinery

Services in-kind which are referred to as government assistance under IAS 20 are not recognised. IAS 20 requires that they are disclosed in terms of their nature, extent and duration.

## 3. Suggested Improvements to IAS 20 and IPSAS 23 on Recognition, Presentation and some Disclosures

IAS 23 does not require the distinction between a grant related to income and grant related to assets since under IAS 23 it is not the criteria to recognise it either as revenue or liability. Under IAS 20 a grant related to income is recognised as revenue whereas grants related to assets is recognised as a liability (if not deducted to the amount of asset to arrive at the carrying amount of a related asset). Under this requirement of IAS 20 it implies that all grants related to assets are subject to conditions and not restrictions. This assumption of IAS 20 is flawed since the stipulations in the form of restrictions do not give rise to any obligation.

It is suggested that IAS 20 should be revised to introduce the stipulations in its two forms namely restrictions resulting into revenue recognition and conditions resulting into liability recognition.

IAS 20 includes a discussion of two broad approaches namely capital approach and income approach. However, it does not allow the use of capital approach. The discussion of these two broad approaches does not add any value to the standard unless it is appended to it as the Basis for Conclusion (BC) to give the information to readers on the basis for not allowing the capital approach.

IAS 20 allows as an alternative approach to deduct the amount of the grant in order to arrive at the carrying amount of a related asset. This practice leads to understatement of economic resources controlled by an entity and at the same time understates the resources used (expenses). Even if the net effects in the profit or loss (of the statement of comprehensive income) and statement of financial position are the same whether this method is used or deferred income method is used, it leads to the misleading picture. It is suggested that either this method

is deleted from IAS 20 or more specific additional disclosures be required to make the effects of the grant related to asset clearer.

Under IPSAS 23 service in-kind may be recognised as asset and revenue when an entity can exercise control over the service and its measure is reliable. The entity is permitted but not required to recognise the service in-kind. It is suggested that IPSAS 23 be improved by introducing an explicit statement that requires the recognition of a service in-kind when an entity can:

(a) exercise control over the service; and

(b) measure the service reliably.

It is suggested that the disclosure of the nature and type of major classes of service in-kind under IPSAS 23 be made mandatory even if the service in-kind is not recognised. This suggestion is in line with the need to enhance transparency in financial reporting in public sector.

Under IAS 20 a grant related to income may be recognised and presented as income or as a deduction to a related expense. When deducting the grant related to income from the related expense, the net effect to profit or loss is the same as that arrived at when it is recognised as income. However, under this alternative treatment of a grant related to income there is a tendency to understate the resources consumed by an entity and their sources during the respective year. It is suggested that either this alternative treatment of grants related to income is abandoned or full disclosure is made regarding their nature, amounts, duration, effects to financial statements and stipulations attached to them (if any).

In IAS 20 services in-kind are referred to as government assistance whose nature, extent and duration should be disclosed in order that the financial statements may not be misleading. It is suggested that IAS 20 should also be improved to accommodate a situation whereby an entity can exercise control over the service in-kind and fair value of the service in-kind may be measured reliably. For example in case there is a memorandum of understanding, the way the recipient entity may have sufficient control of the service may be spelt out. An entity in some cases may be in the position to determine the existing market value of the service in kind, for example when the volunteer technical advisors' salaries in the market are known.

## 4. Concluding Remarks

In order to improve financial reporting IAS 20 should be improved by differentiating restrictions from conditions. This improvement will avoid recognition of a liability when there is no obligation imposed to the recipient of the grant.

The discussion under IAS 20 of two broad approaches to grant namely capital approach and income approach does not add any value to the standard. However, it may be retained as a Basis for Conclusion appended to the standard.

A grant related to assets should not be deducted from the amount of a related asset (as per IAS 20). It should be treated as part of the assets on the debit side and either as a liability or revenue on the credit side as the case may be. However, the treatment may be maintained but with full disclosure on it nature, amount, effects to financial statements and stipulations attached to it.

IPSAS 23 should be improved to include requirement for recognition when recognition criteria are met. IAS 20 should also be improved to accommodate such a situation.

Disclosure of the nature and type of major classes of service in-kind under IPSAS 23 should be made mandatory in order to enhance transparency if financial reporting.

A grant related to income should not be deducted from a related expense unless full disclosure is made regarding its nature, amount, duration, effects to financial statements and stipulations attached to them (if any).

The suggested improvements will enhance completeness and transparency through financial reporting.

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## About the author

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