



Exposure Draft

Proposed Accounting Standards for Private Enterprises

Revenue – Upfront Non-refundable Fees or Payments

July 2022

COMMENTS TO AcSB MUST BE RECEIVED BY
August 15, 2022

We value your input and look forward to your feedback on this Exposure Draft. Comment on this document by uploading your response letter via this [online form](#).

Please address your response to:

Katharine Christopoulos, CPA, CA
Director, Accounting Standards
Accounting Standards Board
277 Wellington Street West
Toronto, Ontario M5V 3H2
kchristopoulos@acsbcanada.ca

This Exposure Draft reflects proposals made by the Accounting Standards Board (AcSB). Individuals and organizations are invited to send written comments on the Exposure Draft proposals. Comments are requested from those who agree with the Exposure Draft as well as from those who do not.

Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft should clearly explain the problem and include a suggested alternative, supported by specific reasoning. All comments received by the AcSB will be available on the website shortly after the comment deadline, unless confidentiality is requested. The request for confidentiality must be stated explicitly within the response.

HIGHLIGHTS

The AcSB proposes, subject to comments received following exposure, to amend REVENUE, Section 3400 in Part II of the CPA Canada Handbook – Accounting (the Handbook). This amendment would defer the effective date for the application guidance of upfront non-refundable fees or payments from fiscal years beginning on or after January 1, 2022, to fiscal years beginning on or after January 1, 2025. Earlier application is permitted. This amendment would also apply to not-for-profit organizations (NFPOs) applying the standards in Part III of the Handbook, as relevant.

Background

In December 2019, the AcSB issued amendments to Section 3400. The amendments provided additional application guidance on the requirements in Section 3400 related to various complex revenue topics, including determining when to recognize revenue from upfront non-refundable fees or payments. The effective date for the amendments was initially set for fiscal years beginning on or after January 1, 2021, but was subsequently deferred to January 1, 2022, in response to the COVID-19 pandemic. The amendments are applicable retroactively.

As entities started to apply these amendments, the AcSB heard of application challenges from stakeholders, particularly member-benefit organizations. They were concerned about the decision-usefulness of deferring upfront non-refundable fees over long membership durations. They also expressed concerns about the associated cost of applying the amendments.

The AcSB considered the feedback and decided that more time was needed to research the stakeholders' concerns relating to non-refundable initiation and life membership fees and the underlying contracts. Therefore, the Board proposes to defer the effective date of the amendments relating to upfront non-refundable fees or payments to January 1, 2025, while it researches the effects of previously issued amendments for upfront non-refundable fees or payments. This research will inform the Board's decisions on how to address stakeholders' concerns.

Plans for finalizing the proposals

The AcSB will deliberate the proposals in light of comments received. Part of the deliberation process includes the Board consulting with its [Private Enterprise Advisory Committee](#). The Committee assists the Board in maintaining and improving accounting standards for private enterprises. The Board will also consult with its [Not-for-Profit Advisory Committee](#) for input on circumstances unique to NFPOs when applying the potential changes to the standard.

The AcSB will provide updates about its deliberations in its decision summaries and on the Revenue – Upfront Non-refundable Fees or Payments project page.

Once the deliberation process is complete and the due process procedures for finalizing a standard are carried out, the AcSB plans to issue the amendments in November 2022 if no significant changes are required to the proposals.¹

Comments requested

Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any comments that express disagreement with the proposals in the Exposure Draft should clearly explain the problem and include a suggested alternative, supported by specific reasoning.

¹ Refer to the Due Process Specifically Related to Domestic Standards in the [AcSB's Standard-Setting Due Process Manual](#).

While the AcSB welcomes comments on all aspects of the proposal in this Exposure Draft, it particularly welcomes comments on the question listed below:

1. Do you agree with the proposed change in effective date of amendments to Section 3400, pertaining to upfront non-refundable fees or payments (see proposed paragraphs 3400.37-.37A)? If not, why not?

The deadline for providing your comment letter to the AcSB is August 15, 2022. Comment on this document by uploading your response letter via this [online form](#).

PROPOSAL

The following Section would be amended as indicated below. Additional text is denoted by underlining and deleted text by strikethrough.

REVENUE, SECTION 3400

EFFECTIVE DATE AND TRANSITION

- .37 Amendments to paragraphs 3400.01, 3400.09(a), 3400.09(d), 3400.11, 3400.17 and 3400.23-.24 and new paragraphs 3400.32A-.32B and 3400.A1-.A484, issued in December 2019, apply to annual financial statements relating to fiscal years beginning on or after January 1, 2022. Except as specified in paragraphs 3400.38-.40, an enterprise applies these amendments retrospectively, in accordance with ACCOUNTING CHANGES, Section 1506. Earlier application is permitted.
- .37A Amendments to paragraphs 3400.A45-.A48, issued in December 2019, apply to annual financial statements relating to fiscal years beginning on or after January 1, 2025. An enterprise applies these amendments retrospectively, in accordance with ACCOUNTING CHANGES, Section 1506. Earlier application is permitted.

BASIS FOR CONCLUSIONS

Introduction

1. This document summarizes considerations that were deemed significant by members of the AcSB in reaching their conclusions to amend REVENUE, Section 3400 in Part II of the CPA Canada Handbook – Accounting. This document sets out the reasons the AcSB undertook to develop the amendment, the process of research and deliberation, the key decisions made and the principal reasons for adopting the positions taken and rejecting others.

Background

2. In May 2019, the AcSB issued its Exposure Draft to address stakeholders' concerns with Section 3400. Stakeholders noted a lack of application guidance and illustrative examples in the standard pertaining to certain complex revenue topics, including upfront non-refundable fees or payments.
3. The main proposal in the Exposure Draft was to add an appendix to Section 3400 containing additional guidance on the complex revenue topics for which many stakeholders expressed concerns. This guidance was derived from superseded guidance in Part V of the Handbook (primarily from the Emerging Issues Committee Abstracts (EICs)).
4. The application guidance and illustrative examples pertaining to upfront non-refundable fees or payments were derived from EIC-141, *Revenue Recognition*. With the lack of guidance in Section 3400, many stakeholders referred to EICs and other superseded guidance in the pre-changeover standards. By adding the application guidance to the Handbook, it was formalized as authoritative.
5. The AcSB approved amendments to Section 3400 in October 2019 and issued them in the Handbook in December 2019. The effective date for the amendments was initially set for periods beginning on or after January 1, 2021, but was subsequently deferred to January 1, 2022, in response to the COVID-19 pandemic. The amendments are applicable retroactively.
6. As entities started to apply these amendments, the AcSB heard of application challenges from stakeholders, particularly related to non-refundable initiation and life membership fees. These stakeholders were concerned about the decision-usefulness of deferring upfront non-refundable fees over long member durations and the associated cost of applying the amendments.
7. The AcSB heard that many entities collecting non-refundable initiation and life membership fees (e.g., golf clubs) are currently recognizing revenue upfront. Some of these organizations applied the guidance in EIC-105, *Revenue Recognition of Non-refundable Initiation fees in Not-for-Profit Organizations*, prior to the introduction of Part III of the Handbook. After adopting Part III, these entities continued with their existing revenue recognition policy in the absence of application guidance for upfront non-refundable fees or payments.
8. EIC-105 stated that revenue from non-refundable initiation or life membership fees should be recognized when all material conditions relating to the initiation fees have been substantially performed. Substantial performance is considered to have occurred when:
 - (a) the not-for-profit organization grants the use of its facilities and services to the new members;
 - (b) the not-for-profit organization has no remaining obligation or intent – by agreement, practice or legislation – to refund amounts received or forgive unpaid amounts owing; and
 - (c) there are no other material unfulfilled conditions affecting completion of the transaction.
9. When the application guidance was added to Section 3400, the AcSB did not incorporate similar guidance to that contained in EIC-105.

10. The application guidance added to Section 3400 included the following guidance related to upfront non-refundable fees or payments:
 - A45. ...In some circumstances, the right, product or service provided in conjunction with the non-refundable fee has no utility to the buyer separate and independent of the seller's performance of the other elements of the arrangement. In the absence of the seller's continuing involvement under the arrangement, the buyer would not have paid the fee.
 - A46. Revenue is deferred when the upfront fee is in exchange for products delivered or services performed that have no utility to the buyer separate and independent of the enterprise's performance of the other elements of the arrangement.
11. Given this guidance, most organizations with non-refundable initiation and life membership fees concluded that such fees do not have stand-alone "utility to the buyer" and, therefore, should be deferred and amortized into revenue. Some stakeholders also noted that it is challenging for entities to demonstrate they are providing a service that has stand-alone utility to the buyer in exchange for the initiation fee.
12. Some stakeholders also highlighted that the concept of "utility to the buyer" is not defined in the application guidance, nor is it used anywhere else in Section 3400.
13. The AcSB also heard that the illustrative examples related to upfront fees concluded that the fees should be deferred and none of the examples provided scenarios where upfront fees could be recognized at inception.
14. Feedback that the AcSB has received so far on this potential change in practice is mixed. Some stakeholders said there might be facts and circumstances that would permit recognizing non-refundable initiation and life membership fees in revenue upfront. They think that a deferred revenue balance is not decision-useful because the organization has no remaining performance obligation in exchange for the fee.
15. Other stakeholders said that non-refundable initiation and life membership fees should be deferred. They think that deferring the recognition of revenue results in a more faithful representation of revenue as the entity provides services with utility to the buyer over the life of the membership.
16. Most stakeholders have acknowledged that individual contracts have many nuances that would need to be considered before concluding on the most appropriate accounting treatment.

Deferring the effective date

17. The AcSB considered either delaying the effective date of the amendments or withdrawing the guidance completely. Both options would allow the Board to analyze the amendments further, seek additional feedback and determine whether a standard-setting project is needed to address stakeholders' concerns.
18. In determining whether to delay the effective date or withdraw the guidance, the AcSB considered why the amendments were issued in the first place. Before the Board issued the amendments in December 2019, many entities were asking for more guidance on how to account for upfront non-refundable fees or payments. This fee structure is typical for entities issuing software-licensing agreements. With the lack of guidance in Section 3400, entities referred to the superseded guidance in EIC-141 on how to account for these types of arrangements. By adding this guidance from EIC-141 to the Handbook, it was formalized as authoritative. For these types of entities, the amendments were beneficial and supported their accounting policy for upfront non-refundable fees or payments. By keeping the guidance in the standard, it will continue to support the accounting policies of entities who initially asked for it.

19. The AcSB also considered whether to allow for early adoption of the amendments while it deliberates stakeholders' feedback. The Board heard from its Advisory Committees that many entities are far along in implementing the amendments and find them helpful for their financial reporting. These include entities collecting upfront non-refundable fees as part of software-licensing arrangements. The Board decided that early adoption should continue to be permitted because it results in more decision-useful information for the entities' financial statement users. The Board also encourages these entities to early adopt the amendments.
20. The AcSB also considered whether a specific, new effective date should be set for the amendments to upfront non-refundable fees or payments or whether the deferral should be indefinite. The Board decided to specify a new effective date since this will provide transparency to stakeholders on when the Board anticipates completing a standard-setting project if one is deemed necessary.
21. In setting a new effective date, the AcSB considered the types of entities that will be scoped into its research and any potential standard-setting project. Entities that charge non-refundable initiation or life membership fees have expressed the most concern with the amendments. They include for-profit entities applying Part II of the Handbook and not-for-profit entities applying Part III. The Board thinks its research should focus on these types of entities. The Board noted that entities collecting certain types of upfront non-refundable fees, including fees related to the issuance of software licenses, have benefited from the added application guidance. The Board thinks that these types of arrangements should be excluded from its research, and that any amendments to the standard or guidance should not impact these entities. Due to the limited scope of this research, the Board thinks that it can complete any potential standard-setting project before January 1, 2025.

Effective date

22. The AcSB plans to issue the amendments into Part II of the Handbook on November 1, 2022. The Board chose this date because the current effective date for the application guidance on accounting for upfront non-refundable fees and payments is for fiscal years beginning on or after January 1, 2022. As such, the amendments are already effective.
23. However, most private enterprises and NFPOs only issue year-end financial statements. Therefore, issuing the amendments before December 31, 2022, will allow entities that have not early adopted the amendments to benefit from the deferred effective date.
24. The AcSB also proposes continuing to permit earlier application, which includes financial statements not yet authorized for issue. This will allow entities to apply the amendments to their December 31, 2022, financial statements if they choose to.

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