

Financial Reporting Alert

ACCOUNTING STANDARDS FOR PRIVATE ENTERPRISES (ASPE) AND NOT-FOR-PROFIT ORGANIZATIONS (NFPO)

NOVEMBER 2022

2022 Amendment to *Revenue*, Section 3400 in Part II of the CPA Canada Handbook

Highlights

On November 15, 2022, the Accounting Standards Board (AcSB) issued an amendment to *Revenue*, Section 3400 in Part II of the CPA Canada Handbook. This amendment defers 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 also applies to not-for-profit organizations (NFPOs) applying the standards in Part III of the Handbook, as relevant.

This CPA Canada *Financial Reporting Alert* highlights the amendments to Section 3400 and related implications.

Background

The AcSB issued amendments to *Revenue*, Section 3400 in Part II of the CPA Canada Handbook in December 2019. The amendments included additional guidance on the complex revenue topics for which many stakeholders expressed concerns, including determining when to recognize revenue from upfront non-refundable fees or payments. Section 3400 and the additional guidance are applicable to not-for-profit organizations to the extent the organization earns revenue from the sale of services or goods (i.e., revenue that is not a contribution).

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.

EIC-141, *Guidance – Request for Additional Guidance*

The additional application guidance and illustrative examples pertaining to upfront non-refundable fees or payments were derived from the superseded Emerging Issues Committee Abstract (EIC) 141, *Revenue Recognition*.

The upfront non-refundable fees or payments 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 With the lack of guidance in Section 3400, entities referred to the superseded guidance in EIC-141 on how to account for these types of arrangements.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.

EIC-105, *Guidance on Non-Refundable Initiation Fees*

However, the AcSB did not incorporate in the amendments similar guidance to that contained in EIC-105, *Revenue Recognition of Non-Refundable Initiation Fees in Not-for-Profit Organizations*.

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:

- the not-for-profit organization grants the use of its facilities and services to the new members;
- 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
- there are no other material unfulfilled conditions affecting completion of the transaction.

Many entities collecting non-refundable initiation and life membership fees (e.g., golf clubs) applied the guidance in EIC-105 prior to the introduction of Part III of the Handbook and recognized revenue upfront. 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.

New Guidance in Section 3400 Related to Non-Refundable Fees

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.

Feedback Received

As entities started to apply these amendments, the AcSB has received mixed feedback on this potential change in practice. Some 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.

Other 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. These stakeholders were also concerned 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 proposed 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.

Effective Date of the Amendments of November 2022

The amendments to paragraphs 3400.A45 - A48 apply to annual financial statements relating to fiscal years beginning on or after January 1, 2025.

Earlier application is permitted. This will allow entities to apply the amendments to their December 31, 2022, financial statements if they choose to. Alternatively, entities can continue to apply their current accounting policy until the Board completes its project on upfront fees.

Scope of the Board's Research

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 charging non-refundable initiation or life membership fees that have expressed the most concern with the amendments 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 licences, 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.

ASPE Briefing: Additional Guidance Added to Section 3400, Revenue

In May 2021, CPA Canada issued ASPE Briefing: *Additional Guidance Added to Section 3400, Revenue*. Following the new amendment to Section 3400 issued in November 2022, the transition section is amended to clarify that the amendments to paragraphs 3400.A45 – A48 apply to annual financial statements relating to fiscal years beginning on or after January 1, 2025. The transition date described in the Briefing should be amended consequently.

What Resources Are Available to Help Me?

CPA Canada

- [ASPE briefing: Section 3400, Revenue \(cpacanada.ca\)](https://cpacanada.ca)

Accounting Standards Board

- Section 3400, *Revenue*
- [Meetings and Events \(frascanada.ca\)](https://frascanada.ca)

Comments

Comments on this *Financial Reporting Alert*, or suggestions for future Financial Reporting Alerts should be sent to:

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