Revenue: A Practical Approach to Section PS 3400

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Introduction

Section PS 3400, Revenue, was issued by the Public Sector Accounting Standards Board (PSAB or the "Board") November 2018. It is effective for fiscal years beginning on or after April 1, 2023 which means that March 31, 2024 and December 31, 2024 will be the first year ends impacted. Section PS 3400 applies to all public sector entities following Public Sector Accounting Standards (PSAS). Section PS 3400 was needed as previously the Public Sector Accounting Handbook (PSA Handbook) only provided guidance on accounting for certain types of revenue transactions such as taxation and government transfers. However, there was no overall general revenue recognition guidance. This new standard will fill this gap and provide more consistency in practice for revenue recognition outside of the specific revenue streams already covered by other standards.

This publication will walk through a practical approach to apply Section PS 3400 including: how to determine whether a revenue stream is within the scope of this standard; the 5-step approach to recognizing revenue and the appropriate measurement; a comprehensive example; disclosure requirements; transitional considerations; and practical considerations.

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Two Part Approach

The two parts to this approach are as follows:

Part 1: Identification	Identify revenue streams that are within the scope of Section PS 3400.
Part 2: Applying the 5 Step Approach to Revenue Recognition & Measurement	For each stream in scope, follow the five-step process to determine if revenue can be recognized and appropriately measured.

Let's look at each stage in more detail.

Part 1: Identification of revenue streams that are within scope of Section PS 3400

Part 1 is the most important step since if it is skipped, there is the potential to include revenue streams that are not actually within the scope of Section PS 3400. To appropriately identify revenue streams that are within scope and should be accounted for under Section PS 3400, we need to start by identifying **all** the revenue streams that are present at the public sector entity. It is important to note that not all these revenue streams will end up meeting the criteria to be considered within the scope of Section PS 3400.

To know what is in scope, we need to understand what Section PS 3400 identifies as revenue streams included in the section. Section PS 3400 establishes standards on how to account for revenue transactions for which there is not already specific guidance in other PSA Handbook Sections. Section PS 3400 also specifically differentiates between *revenue arising from transactions that include performance obligations, referred to as "exchange transactions", and transactions that do not have performance obligations, referred to as "non-exchange transactions"*. It should also be noted that some transactions could contain components that combine an element with performance obligations, an element with no performance obligations and/or another form of revenue. These are referred to as hybrid transactions.

Section PS 3400 clearly outlines the following revenue streams are excluded from the scope of PS 3400 as they are accounted for under another PSA Handbook Section.

Excluded Types of Revenue Streams	Relevant PSAS Standard
Contributions that are voluntary and non-reciprocal in nature (i.e. donation)	Section PS 4210, *Contributions - Revenue Recognition*, for public sector entities following the PS 4200 series. Refer to our PSAB at a Glance for more information.
Taxation Revenue (i.e. property tax)	Section PS 3510, *Tax Revenue*. Refer to our PSAB At a Glance for more information.
Government Transfers (i.e. federal gas tax fund)	Section PS 3410, *Government Transfers*. Refer to our PSAB At a Glance for more information.
Inflows of restricted economic resources that are accounted for in accordance with Restricted Assets and Revenues	Section PS 3100, *Restricted Assets and Revenues*. Refer to our PSAB At a Glance for more information.
Interest, dividends and changes in fair value of financial instruments including derivatives or their disposal	Section PS 3450, *Financial Instruments*. Refer to our PSAB At a Glance for more information.
Revenue from Restructuring Transactions	Section PS 3430, *Restructuring Transactions*. Refer to our PSAB At a Glance for more information.
Revenue from Interests in Partnerships	Section PS 3060, *Interests in Partnerships*. Refer to our PSAB At a Glance for more information.

Revenue from Investments in Government Business Enterprises (GBE)	Section PS 3070, *Investments in Government Business Enterprises*. Refer to our PSAB At a Glance for more information.
A transaction that represents a contractual obligation or a contractual right and will eventually result in revenue, is outside the scope of Section PS 3400 until the transaction creates revenue	Section PS 3380, *Contractual Rights* or Section PS 3390, *Contractual Obligations*. Refer to our PSAB At a Glances for more information on this.

Now that we know what's excluded from the scope of Section PS 3400, let's take a look at some examples of revenue streams that would be within the scope of Section PS 3400:

- Goods/services produced by the public sector entity for sale such as municipal water and/or sewer
- Goods/services produced by the public sector entity for resale such as recycling bins, gravel sales, or meal services at a college
- Use of property for a specified period such as rental of space at a community centre
- Services provided such as public transit for a fee
- Standing ready to provide goods or services such as first response operations (i.e. fire, ambulance, police)
- Agreed upon services such as a day care service provided for a fee, student tuition and other ancillary revenues
- Licenses and permits such as business licenses
- An asset constructed, manufactured or developed for a payor such as a water connection to the municipal water system from a private dwelling

The list above is not a comprehensive list of all types of revenue streams that are within scope of Section PS 3400. The revenue streams that are within scope of Section PS 3400 will be specific to the types of revenues each public sector entity earns. Therefore, it is important to understand what streams of revenues the entity earns to determine which streams of revenue are within the scope of Section PS 3400.

The Right Team

In order to identify revenue streams within scope of Section PS 3400, it is important to put together a team of knowledgeable people such as members of the finance department with the relevant experience.

The first step would be to put together a complete list of all revenue streams. While creating this list the team should keep in mind, the most important items to identify are those that could result in a material misstatement to the financial statements.

Once the team has put together a complete list of all revenue streams, the team should then consider if each individual revenue stream is specifically excluded from Section PS 3400 and included in another section of PSAS. If not excluded, then it is within the scope of Section PS 3400.

Part 2: Applying the 5 Step Approach to Revenue Recognition & Measurement

Once it is determined which revenue streams are in scope of Section PS 3400, the second part is to assess whether the recognition and measurement criteria are met. Section PS 3400 is based on a control model instead of the rewards and risk model that many entities may be familiar with from the past.

Under Section PS 3400, revenue recognition and measurement follow a 5 step process as follows:

Step 1: Determine whether the Transaction is an Exchange or Non-Exchange Transaction

Step 2: Identify any Performance Obligations & Assign them to Distinct Goods/Services

Step 3: Determine the Transaction Price

Step 4: Allocate the Transaction Price to Each Performance Obligation

Step 5: Recognize Revenue when Conditions are Satisfied

This process should be followed each time a transaction is considered under Section PS 3400 to ensure the recognition and measurement criteria are appropriately met.

Let's look at these steps in a little more detail.

Step 1: Determine whether the transaction is an Exchange or Non-Exchange Transaction

What does Section PS 3400 say?	Practical Application
Exchange transactions are transactions where goods or services are provided to a payor for consideration. These transactions include performance obligations for a public sector entity arising directly from a payment or promise of consideration by a payor. • **A performance obligation is an enforceable promise to provide specific goods or services to a specific payor.** Exchange transactions are not necessarily exchanges of fair or equal value.	An exchange transaction requires the payor (purchaser) to provide cash (or some other type of consideration) to receive a good or service. The public sector entity has an obligation to provide the good/service upon receiving the consideration. **Example:** *A municipality sells a cemetery plot to a resident in exchange for cash. This would be considered an exchange transaction as the resident is required to provide payment for the cemetery plot and the Municipality is required to provide the plot upon receipt of payment.*
Non-exchange transactions are transactions or events where there is no direct transfer of goods or services to a payor.	A non-exchange transaction requires the payor to provide cash (or some other type of consideration) but there is nothing received in return from the public sector entity. **Example:** *A municipal officer issues a parking ticket to a resident. This would be considered a non-exchange transaction as the resident is required by legislation to pay the fine but there is no transfer of goods/services to the resident by the public sector entity.*
Hybrid transactions: A public sector entity separately accounts for the components of a single transaction that combine: a) an element with performance obligations; b) an element with no performance obligations (for example, a fine or penalty); and/or c) another form of revenue such as a contribution, a government transfer or tax revenue. When accounting for hybrid transactions, the public sector entity accounts for each component of a transaction in accordance with the applicable recognition criteria. When	A hybrid transaction must be split out appropriately based on the components that are present. **Example:** *A College hosts a volleyball tournament. The entry fee for spectators is a total fee of $10 where $8 is charged to watch the game and the other $2 is a voluntary donation to the College's volleyball program.* *The total fee has two components to this transaction. The first component is an exchange transaction with a performance obligation within the scope of Section 3400, where in exchange for paying the fee the College grants access to the spectator to watch the game. The second component is the $2 donation, which is considered another form of revenue outside the scope of*

a component of the transaction is within the scope of another standard, the public sector entity would apply that standard.	*Section 3400 and is accounted for as a donation if the spectator chooses to pay this amount.*

Step 2: Identify any Performance Obligations & Assign them to Distinct Goods/Services

What does Section PS 3400 say?	Practical Application
Performance obligations are enforceable promises to provide **distinct goods or services** to a **specific payor**. Enforceable promises create a **valid expectation** of the payor that the public sector entity **will transfer** a good or service. They can be **written or unwritten**. Performance obligations **must** meet the definition of a liability (refer to our PSAB At A Glance for Section PS 3200, *Liabilities*) • At the **inception** of a transaction, a public sector entity needs to identify if one or more performance obligations exist in the transaction. • In identifying these performance obligations, the public sector entity considers the **characteristics** of the goods or services being provided to the payor in exchange for consideration, whether they are **specific** to the payor and provide a **distinct good or service** to the payor. Performance obligations are attached to **distinct** goods or services. A good or service is considered to be distinct if both of the following criteria are met: a) the payor can benefit from the good or service either **on its own** or together with other resources that are readily available to the payor (i.e., the good or service is capable of being distinct); and b) the public sector entity's promise to provide the good or service to the payor is **separately identifiable** from other promises in the transaction (i.e., the promise to transfer the good or service is distinct in the context of the transaction). In some cases, goods or services may be highly interrelated. In this case, the goods or services are grouped together until there is a	A performance obligation creates the expectation of the payor (purchaser) that they will provide consideration in exchange for the public sector entity transferring a good or service. Performance obligations must always be identified at the start of the transaction. The public sector entity must look at the characteristics (or features) of the goods or service to determine if they are distinct goods or services being provided to the payor and whether the good or service is specific to the payor itself. **Example:** *A public sector entity has a conservation park. It enters into a sale transaction to sell an individual a park pass which allows them to visit the park an unlimited number of times during a one year period.* **Question:** Is there a performance obligation the public sector entity needs to fulfill? **Answer:** *Yes, the public sector entity has made a promise to the payor to provide a service of granting access to the park for a one-year period when a park pass is purchased. The payor is able to use the park pass as often as they wish and whenever they wish.* **Question:** What is the distinct good or service being provided in this transaction? **Answer:** *The public sector entity is providing access to the park as the distinct service being provided. The distinct service is* ***not*** *the physical pass as that cannot be enjoyed without the park.*

bundle of goods or services that is distinct which is then assigned a single performance obligation.	

Step 3: Determine the transaction price

What does Section PS 3400 say?	Practical Application
When dealing with a transaction **without** a performance obligation the transaction price is the **realizable value** of the transaction. Realizable value represents the future economic value the public sector expects to obtain and is the amount of cash or cash equivalents the asset is expected to be converted into in the due course of operations. For transactions **with** performance obligations, the transaction price is the amount of consideration a public sector entity expects to receive in exchange for the promised goods or services. When determining the transaction price, a public sector entity will need to consider the effects of: a) multiple performance obligations; b) variable consideration; c) existence of significant concessionary terms *(expected to be rare situations);* and d) non-cash consideration.	**Multiple performance obligations:** Multiple performance obligations represent more than one performance obligation where the public sector entity must consider how it will allocate the transaction price. **Example:** *A municipality sells a building to a business with a service contract to provide upkeep services for a 2 year period for a total price of $1,000,000.* In this transaction there is two distinct items (building and service) which could be sold separately on their own. **Variable consideration:** When a transaction involves variable consideration the final price of the transaction is not yet known. This could be due to things such as discounts, rebates, incentive programs or price concessions or the final price could depend on the occurrence or non-occurrence of some future event. Therefore, an estimate may be needed. For more information on how to make an appropriate estimate refer to our PSAB At a Glance on Section PS 3400 for guidance. **Example:** *A business enters into an agreement with a public sector entity that allows them to advertise on public structures such as park benches, public transit shelters and public transit busses for a one-year period for $10,000. In addition, the public sector entity can earn an additional $1,000 per special advertising initiative undertaken by the business owner. This could be putting up special posters or additional advertising in public areas that are available for special advertising. The $1,000 would be variable depending on how many special initiatives the public sector entity underwent.* Of the total transaction price, the special advertising portion is considered variable consideration as the end fee is dependent on how many special advertisements the business decides to do. **Non cash consideration**

	Non cash consideration represents consideration received other than cash for a transaction. **Example:** *A public sector entity agrees to sell a business a permit worth $10,000 in exchange for $2,500 cash and a piece of equipment worth $7,500.*

Step 4: Allocate the Transaction Price to Each Performance Obligation

What does Section PS 3400 say?	Practical Application

Allocation Requirement
Once a transaction price is determined (see step 3), then the transaction price must be allocated between the performance obligations that have been identified.
 	
How to allocate the transaction price
• **Use of stand-alone price:** The observable price charged for the goods or services when the same public sector entity sells those goods or services in similar circumstances. When the stand-alone price is available for the good or service underlying each performance obligation , this would be used as the basis of allocation
• **Estimate:** If a stand-alone selling price is not readily available for one or all of the performance obligations, a public sector entity must estimate an amount that faithfully represents the price the individual good or service would be sold for if it was sold separately to the payor. Estimation methods that may be used include, but are not limited to:
  o **Expected cost:** the public sector entity forecasts its expected costs of satisfying the performance obligation
  o **Residual Approach:** When the stand-alone selling price is highly variable or uncertain, then the estimated stand-alone selling price is based on the total consideration less the sum of observable stand-alone selling prices.
  o **Adjusted market assessment:** A public sector entity evaluates the market in which it sells goods or services and estimates the price that a payor would be willing to pay
	If there is only **one** performance obligation the entire transaction price is allocated to the performance obligation.
	
	If there are **multiple** performance obligations the transaction price must be allocated between the performance obligations.
	
	Example: *A public sector entity enters into an agreement to sell a tangible capital asset. In addition to the sale, the public sector entity has agreed to provide service on the asset for the next year. Both are offered for a single transaction price of $500,000.*
	
	In this case the public sector entity identifies that there are two performance obligations identified which are distinct (sale of the tangible capital asset and the service of the asset). Therefore, the transaction price of $500,000 must be allocated between the performance obligations.
	
	The public sector entity does not normally sell the tangible capital asset without the support service, however other entities do provide similar assets for sale.
	
	The public sector entity determines that the best method to allocate the transaction price is to use the residual approach. The observable price of the stand-alone tangible capital asset is $400,000.
	
	Using the residual approach the transaction price is allocated as follows:
	
	Tangible capital asset: $400,000
	Service: $100,000

Step 5: Recognize Revenue when Conditions are Satisfied

What does Section PS 3400 say?	Practical Application
Transactions without performance obligations: Revenue is recognized when: a) There is the authority to claim or retain the economic resources received or receivable; and b) There is a past transaction or event that gives rise to economic resources. Transactions without performance obligations are either voluntary or involuntary. Involuntary transactions arise because the right to the economic resource is attributable to legislation based on constitutional authority or delegated constitutional authority. Legislation, regulations or bylaws authorizing the fine, penalty or fee must be in place for a public sector entity to have the authority to recognize such revenues. The exercise of authority may vary between jurisdictions.	No performance obligations mean the public sector entity is entitled to cash or some other consideration, but there is no obligation for the public entity to provide anything in return. **Example:** *A public sector entity has the authority to issue a parking ticket, in efforts to enforce its approved parking regulations. A security guard issues a $50 parking ticket parked without a pass in one of the public sector entity's parking lots. The public sector entity can recognize revenue when the parking ticket is issued as it has the authority (parking regulations exist) and the past transaction/event has occurred (ticket has been issued to the illegally parked car).*
Transactions with performance obligations: Revenue from transactions with performance obligations should be recognized when (or as) the public sector entity satisfies a performance obligation by providing the promised goods or services to a payor. **Timing of Revenue Recognition** A performance obligation is either settled **at a point in time or over a period of time.** A performance obligation is satisfied and revenue can be recognized when **control** of the benefits associated with the good or service has passed to the payor. **Indicators of Control** **Indicators** that control of the goods or services have passed from the public sector entity to the payor include, but are not limited to, when the payor: a) has the ability to use or direct the use of, sell or exchange and obtain substantially all of the remaining benefits from the good or service; or b) holds the good or service and has the discretion to use it.	Performance obligations are either satisfied over time or at a point in time. The performance obligations are satisfied when control has passed to the payor (purchaser). **Example of performance obligation satisfied over time:** *A college offers a fall term (September – December) course to a student for $2,000. The class will be held twice a week for the duration of the semester.* Given that the College has an obligation to provide the student with a series of lectures and classes over the 4 month semester, the performance obligation would be satisfied over time. The revenue would be recognized over the period of course delivery. **Example of performance obligation satisfied at a point in time:** *A college bookstore sells textbooks to students.* The performance obligation of the college is to provide the student with a textbook in exchange for consideration. Once the consideration has been paid for the textbook, control has passed to the student, the performance obligation has been satisfied at that point in time.

Revenue recognition over time A public sector entity satisfies its performance obligation and recognizes revenue over a period of time when control of the benefits associated with the goods or services passes to the payor over a period of time. A public sector entity satisfies a performance obligation and recognizes revenue over a period of time if any of the following indicators are met: a) the payor simultaneously receives and consumes the benefits provided by the public sector entity's performance as the public sector entity fulfils the performance obligation; b) the public sector entity's performance creates or enhances an asset (for example, work in progress) that the payor controls or uses as the asset is created or enhanced; c) the public sector entity's performance does not create an asset with an alternative use to the public sector entity and the public sector entity has an enforceable right to payment for performance completed to date; d) the public sector entity is expected to continually maintain or support the transferred good or service under the terms of the arrangement; or e) the public sector entity provides the payor with access to a specific good or service under the terms of the arrangement. **Revenue recognition at a point in time** If a performance obligation is not satisfied over a period of time, the public sector entity satisfies the performance obligation at a point in time. The performance obligation is satisfied when the payor obtains control of the benefits associated with the promised good or service.	

Putting it all together – comprehensive example

The following is an example to illustrate how the 5 steps related to recognition and measurement for revenue work together.

Scenario: A College offers parking passes for sale to students attending the institution. A parking pass provides the student the right to park in a designated lot on the college premises for a specific semester. The cost of a parking pass for one semester is $500. A student purchases a parking pass for the fall semester.

Step	Analysis
Step 1: Determine whether the Transaction is an Exchange or Non-exchange Transaction	**Question:** Is the transaction an exchange transaction or a non-exchange transaction? ***Answer:*** *The transaction is an exchange transaction as the student is required to pay for the parking pass and in return the college provides access to a designated parking lot on college premises for a specified period of time.*
Step 2: Identify any Performance Obligations & Assign them to Distinct Goods/Services	**Question:** Are there any performance obligations the public sector entity needs to fulfill? *Answer: Yes, there is one performance obligation in this transaction. The college has made a promise to the payor (student) to provide a service of granting access to a designated parking lot for a semester when a park pass is purchased. The student (payor) is able to use the parking pass as often as they wish and whenever they wish during this period.* **Question:** What is the distinct good or service being provided in this transaction? ***Answer****: The college is providing access to the designated parking lot as the distinct service being provided. The distinct service is not the physical pass as that cannot be enjoyed without the access to the parking lot.*
Step 3: Determine the Transaction Price	Since this is an exchange transactions the following questions should be considered when determining the transaction price: **Question:** Are there multiple performance obligations? ***Answer:*** *No. The only performance obligation that exists is the college providing access to a designated parking lot to a payor for a period of time (i.e. the semester).* **Question:** Is there any variable consideration to consider in the transaction? ***Answer:*** *No, there are no parts of the transaction where the value is not known.* **Question:** Are there any significant concessionary terms? ***Answer:*** *No, there are no concessionary terms present in the arrangement. The student must pay the $500 standard parking pass rate in return for access to the parking lot.* **Question:** Is there any non-cash consideration? ***Answer:*** *No, the college is being paid in cash.* **Summary:** The transaction price is $500.
Step 4: Allocate the Transaction Price to Each Performance Obligation	**Question:** How is the transaction price allocated? ***Answer:*** Since there is only one performance obligation identified, the $500 transaction price is allocated entirely to that performance obligation. *Note that if there were multiple performance obligations then the transaction price would need be allocated between the performance obligations.*
Step 5: Recognize Revenue when Conditions are Satisfied	**Question:** Since this is an exchange transaction, is revenue recognized at a point in time or over a period of time? Revenue is recognized over a period of time if **any** of the following indicators are met:

	a) the payor simultaneously receives and consumes the benefits provided by the public sector entity's performance as the public sector entity fulfils the performance obligation; b) the public sector entity's performance creates or enhances an asset (for example, work in progress) that the payor controls or uses as the asset is created or enhanced; c) the public sector entity's performance does not create an asset with an alternative use to the public sector entity and the public sector entity has an enforceable right to payment for performance completed to date; d) the public sector entity is expected to continually maintain or support the transferred good or service under the terms of the arrangement; or e) the public sector entity provides the payor with access to a specific good or service under the terms of the arrangement. ***Answer**: In this case the student receives and consumes the benefit of the access to the designated parking lot over the period of the fall semester as the college provides this access to the designated parking lot over the semester. Therefore, the revenue is recognized over the period of the semester. For example, if the semester is 4 months long the parking pass revenue may be recognized equally over the period the access to the designated parking lot is provided. Since the criteria to recognize revenue over time is met, revenue cannot be recognized at a point in time.*

Presentation & Disclosures

Section PS 3400 contains presentation and disclosure requirements to ensure financial statement users can understand a public sector entity's various revenues streams.

In terms of presentation, a public sector entity would need to present:

- Disaggregated revenues reported on the statement of operations by source and type, with separate disclosure of revenues that are not related to recurring activities;

In terms of disclosure, some of the key items a public sector entity would need to disclose include:

- Typical performance obligations and the methods and policies that apply when recognizing revenues.
- The nature and amount of continuing performance obligations grouped by category of similar transactions.
- The amounts when a public sector entity has the information necessary to record a transaction but does not expect to collect payment.
- The original amount of the transaction price in circumstances where the terms of the arrangement include significant concessionary terms such that all or a part of the transaction is concessionary in nature.

Providing significant revenue sources and types as well as describing how the revenues are recognized, helps users of the financial statements understand the resources available now to the public sector entity as well as in the future. Additionally, indicating which revenue sources are recurring versus nonrecurring helps financial statement users understand annual surplus' or deficits as well as implications for future years.

Transition

Section PS 3400 comes into effect for fiscal years beginning on or after April 1, 2023 and may be applied in one of the following ways:

- Retroactively – application applies to transactions from their date of origin. Prior year revenues are restated and the balance of the accumulated surplus/deficit is restated at the beginning of the earliest period presented to reflect the cumulative effect of the change on periods prior to that date. The comparability of the financial statements is preserved under this method.
- Prospectively – application applies only to transactions occurring after the effective date and to any outstanding balances existing as of the effective date (This does not mean that the standard is only applied to any new revenue going forward. The standard applies to any revenue contracts in existence at April 1, 2023). The prior year revenues are not restated which may result in the financial statements not being as comparable to the prior year.

Getting Ready – Practical Considerations

As you prepare to adopt new Section PS 3400, there are a few considerations to keep in mind:

- Does your current accounting software track enough information to be able to meet the recognition requirements under Section PS 3400? If the answer is no, is there alternative software that should be considered?
- If the current software doesn't track enough information can the tracking be completed on a manual basis in sufficient detail to meet the requirements under Section PS 3400?
- Are the right people in place with the appropriate knowledge to track the information to meet the requirements under Section PS 3400?
- Will you need more time or resources allocated to accommodate this new standard?
- Will this new standard cause a change in how your day-to-day operations happen?

Next Steps to Affect a Successful Transition

This publication highlights key items to consider in applying new Section PS 3400, but it is not a comprehensive list of all the considerations and guidance in the standard. Revenue can be unique and complex. Each revenue stream within the scope of Section PS 3400 should be analyzed carefully to understand the full impact of the adoption of Section PS 3400. If you have not already, we encourage you to start preparing for the application of Section PS 3400 by creating a list of your revenue streams and the associated revenue recognition policies. Consult with your assurance provider early in the process to help resolve any challenges encountered.

Conclusion

Applying Section PS 3400 can be complex to apply, but by assembling the right team and considering the steps in this publication, the standard can be applied in an efficient manner. If you have questions on how this standard affects your entity or require assistance in undertaking the application of Section PS 3400, reach out to a BDO advisor today to find out the option available to your organization for support.

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