SECTION PS 3420
inter-entity transactions

Basis for Conclusions

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PURPOSE AND SCOPE

.01 This Section establishes standards on how to account for and report transactions between public sector entities that comprise a government's reporting entity from both a provider and recipient perspective.

.02 This Section does not deal with:

(a) restructuring transactions; and

(b) transactions between a partner and a partnership (see INTERESTS IN PARTNERSHIPS, Section PS 3060).

.03 It may be useful to read this Section in conjunction with RELATED PARTY DISCLOSURES, Section PS 2200.

DEFINITIONS

.04 The following terms are used in this Section with the meanings specified:

(a) **Carrying amount** is the amount of an item transferred, or cost of services provided, as recorded in the accounts of the provider, after adjustments, if any, such as for amortization, impairment or changes in the fair value. For a tangible capital asset, the carrying amount is the net of cost and accumulated amortization. For other assets, the carrying amount may be the net of cost and valuation allowances or fair value, as appropriate.

(b) **Commonly controlled entities** are all public sector entities that comprise a government's reporting entity (see GOVERNMENT REPORTING ENTITY, Section PS 1300).

(c) **Cost allocation and recovery** is the allocation of costs of activities associated with providing goods or services to another entity and the recovery of the costs incurred from the other entities. Recoveries between entities may be a direct exchange of consideration or an accounting entry.

(d) **Exchange amount** is the amount of the consideration given for the item transferred or service provided as established and agreed to by the related parties.

(e) **Fair value** is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable and willing parties who are under no compulsion to act.

(f) **Goods and services** include such items as materials and supplies, services, use of facilities or licences. They do not include financial or non-financial assets (for example, tangible capital assets).

(g) **Inter-entity transactions** are those transactions occurring between commonly controlled entities.

(h) **Provider** is the entity that is transferring an asset or liability or providing goods and services to another entity.

(i) **Recipient** is the entity that is receiving assets or liabilities or receiving goods and services from another entity.

(j) **Unallocated costs** represent the cost of resources recorded by the providing entity in its operating activities that are incurred on behalf of a recipient entity.

RECOGNITION

.05 To achieve their objectives, governments generally conduct activities through a variety of different entities. These entities can include those integral to the operations of government such as government components, government organizations and partnerships.

.06 Governments may establish operating relationships between these entities that allow them to operate together to achieve the government's overall objectives. In some cases, the terms and conditions for inter-entity transactions may reflect the policy objectives, accountability structures and budgetary practices of the government or another controlling entity. These practices may be different than those that would have been adopted if the entities were operating at arm's length. In other cases, inter-entity transactions may reflect similar terms and conditions that would be present if the transaction took place at arm's length.

.07 The terms and conditions for inter-entity transactions may result in assets and liabilities being transferred between commonly controlled entities at amounts different from cost or fair value or for no consideration. A government may have established a central entity (such as a department) responsible for common services (such as debt management, pension administration, procurement and other shared services) that apply across all controlled entities. The central entity may follow a policy of allocating and recovering costs from the other entities. Alternatively, the central entity may not allocate costs to the other entities and fund those costs through its own appropriations or other revenue sources.

Transfers of assets or liabilities

.08 *Inter-entity transactions involving the transfer of assets or liabilities should be recognized by both the provider and the recipient.* [APRIL 2017]

.09 If inter-entity transactions involve the transfer of assets or liabilities, both entities would recognize the transactions. The provider would remove the assets or liabilities from its financial statements and any difference between the net proceeds received, if any, and the carrying amounts transferred would be accounted for as a revenue or expense in the statement of operations. The recipient would recognize assets or liabilities in its financial statements when the items satisfy the definition and recognition criteria for an asset and liability in Chapters 8 and 9 of the Conceptual Framework. A transferred asset that has initially been recognized by a public sector entity as a purchased intangible in applying PUBLIC SECTOR GUIDELINE PSG-8, Purchased Intangibles, continues to be recognized as a purchased intangible by the recipient. 1 [Former paragraph PS 3420.09, amended by the Conceptual Framework, retained in Archived Pronouncements.] [Former paragraph PS 3420.09, amended by the 2022-23 Annual Improvements, retained in Archived Pronouncements.]

Cost allocation and recovery

.10 *When there is a policy of cost allocation and recovery for the provision of goods and services:*

(a) the provider should report all revenues and expenses on a gross basis; and

(b) the recipient should report expenses on a gross basis. [APRIL 2017]

Unallocated costs

.11 It is not unusual that certain activities are undertaken by a central entity to support the activities of other departments and agencies. For example, the providing entity may be responsible for the debt management, pension administration, procurement or other shared services that apply across all government entities. The provider may have a policy of funding expenses related to these common services through appropriations or other revenue sources and not allocating the costs to recipients.

.12 *When there is no policy for allocating costs, the recipient may choose to recognize these costs when they would otherwise have been purchased and a reasonable estimate of the amount involved can be made.* [APRIL 2017]

.13 *When the recipient chooses to recognize unallocated costs it reports these items as revenues and expenses.* [APRIL 2017]

MEASUREMENT

.14 *Inter-entity transactions should be recorded at the carrying amount as determined at the transaction date unless:*

(a) transactions are undertaken on similar terms and conditions to those adopted if the entities were dealing at arm's length;

(b) assets or liabilities are transferred for nominal or no consideration;

(c) transactions are allocated costs and recoveries; or

(d) transactions are unallocated costs. [APRIL 2017]

Transactions similar to arm's length transactions

.15 *Inter-entity transactions should be recorded at the exchange amount when they are undertaken on similar terms and conditions to those adopted if the entities were dealing at arm's length.* [APRIL 2017]

.16 Examples of transactions on similar terms and conditions to those adopted if the entities were dealing at arm's length may include the sale and purchase of utilities and the sale or purchase of an inventory item.

Assets or liabilities transferred for nominal or no consideration

.17 *When inter-entity transactions involve the transfer of assets or liabilities for nominal or no consideration, they should be measured at the carrying amount by the provider and at the carrying amount or fair value by the recipient.* [APRIL 2017]

.18 This does not require symmetrical accounting by the provider and recipient.

Gains or losses on transferred assets and liabilities

.19 *When there is a difference between the exchange amount and the carrying amount of a transferred or exchanged asset or liability, a gain or loss should be reported in the statement of operations.* [APRIL 2017]

Cost allocation and recovery

.20 *Allocated costs and recoveries should be measured at the exchange amount.* [APRIL 2017]

Unallocated costs

.21 *When recognized by the recipient, unallocated costs should be measured at the carrying amount or fair value unless policy, budget practices or accountability structures dictate otherwise.* [APRIL 2017]

.22 If unallocated costs are recognized by the recipient, policy, budget practices or accountability structures may impact how the transactions would be measured. In the absence of such, they would be measured at the carrying amount or fair value.

DISCLOSURE

.23 *An entity should disclose information about inter-entity transactions, whether or not given accounting recognitions, in accordance with RELATED PARTY DISCLOSURES, Section* PS 2200*.* [APRIL 2017]

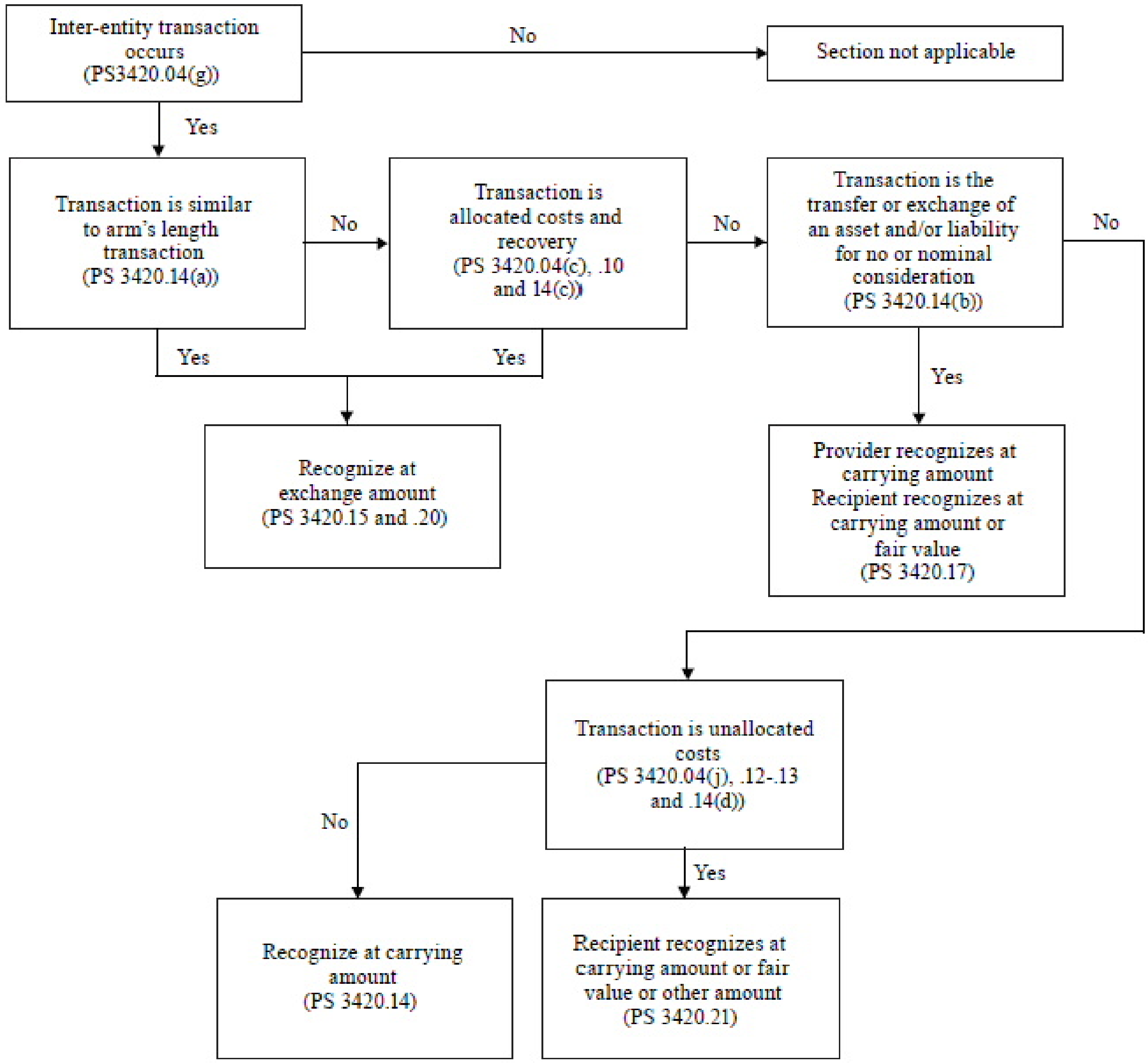
.24 Transactions between commonly controlled entities are related party transactions. Disclosure of information about the transactions and the underlying relationships is necessary for users to understand the effect of those transactions on an entity's assets, liabilities, revenues and expenses.

TRANSITIONAL PROVISIONS

.25 This Section applies to fiscal years beginning on or after April 1, 2017. Earlier adoption is permitted. If application of the Section results in a change of accounting policy, ACCOUNTING CHANGES, Section PS 2120, applies.

APPENDIX A
DECISION TREE — ACCOUNTING

The following decision tree has been prepared to illustrate the accounting treatment specified in this Section. The decision tree is illustrative only and matters of principle relating to particular situations should be decided in the context of the Section.



Footnotes

1. These inter-entity transactions do not give rise to a purchased intangible eligible for asset recognition in accordance with PSG-8:

(a) A non-purchased intangible of one entity in a reporting entity is transferred to another entity within the same reporting entity.

(b) A developed intangible of one entity in a reporting entity is transferred to another entity within the same reporting entity.

(c) A non-purchased or developed intangible of the reporting entity transferred to a party outside the reporting entity and subsequently purchased by an entity within the reporting entity.