

## Income of Not-For-Profit Entities

### Staff Paper: Recognition and Disclosure of Contributed Services

#### Introduction

- 1 For the purpose of developing an ED on Income of Not-For-Profit Entities (NFPs), this paper addresses Specific Matters for Comment (f) and (g) in AASB ED 180 *Income from Non-exchange Transactions (Taxes and Transfers)*. These are, respectively:
- (a) whether to permit, but not require, the recognition of contributions of services; and
  - (b) whether to require disclosure of the nature and type of major classes of services in-kind received.
- 2 ‘Contributions of services’ (referred to in AASB 1004 *Contributions*) and ‘services in-kind received’ [which ED 180 described as “services provided by individuals to NFPEs/PBEs in a non-exchange transaction” (paragraph 100)] are different terms for the same thing. In view of neither of those documents being expected to have a future status, this paper uses the plainer expression ‘donated services’.<sup>1</sup>

#### Staff Recommendations

- 3 Staff recommend proposing in the ED on Income of NFPs that:
- (a) the recognition of donated services to any NFP should be required when the recognition criteria for donated services presently in AASB 1004 *Contributions* are met. These recognition criteria are that:
    - (i) the entity has obtained control of the donated services or the right to receive them;<sup>2</sup>
    - (ii) the fair value of those services can be reliably determined; and
    - (iii) the services would have been purchased if they had not been donated;
  - (b) it should not be necessary to define ‘donated services’ for the purpose of applying the proposal in paragraph 3(a); and
  - (c) disclosure should be required of:
    - (i) the nature and type of major classes of donated services received during the period, whether recognised or unrecognised; and
    - (ii) where income is recognised in respect of a class of donated services during the period, the amount recognised.

<sup>1</sup> Paragraphs 44(b) and 46 of AASB 1004 refer to ‘donated services’, even though ‘contributions of services’ is generally used in that Standard.

<sup>2</sup> This is one of the general recognition criteria for contributions in paragraph 12 of AASB 1004. It is mentioned here to emphasise that services the entity does not control (such as unsolicited services that are not provided under the entity’s direction) are not recognised as assets or income.

## Recognition of Donated Services

### Background

- 4 ED 180 proposed permitting, but not requiring, the recognition of ‘contributions of services’. The Basis for Conclusions on ED 180 includes the following background:

“AASB 1004 (paragraph 44) requires local governments, government departments, general government sectors and whole of governments to recognise contributions of services as income when the fair value of those services can be reliably determined and the services would have been purchased if they had not been donated. ...” (paragraph BC29)

“The proposals in this ED would permit entities to recognise services in-kind, on a class-by-class basis, but would not require them to be recognised. The AASB believes that it is better for this ED to propose a consistent approach to the recognition of contributions of services for all NFPEs, since it does not specify any characteristics of services for which recognition may be most appropriate, following the approach in IPSAS 23. Therefore, the previous requirements for the recognition by certain types of NFPEs in the public sector of some contributions of services would not be retained, but that policy could continue to be applied by such entities, since the recognition of contributions of services is still permitted.” (paragraph BC30)

### Implications of the Change in this Project’s Scope

- 5 Before considering the comments received on ED 180, it is logical to consider whether the change in the project’s scope [from one based on the nature of transactions (non-exchange transactions) to the nature of entities (not-for-profit entities)] contradicts the ED’s proposal to permit non-recognition of services received in non-exchange transactions. In this regard, the AASB decided in February 2011 that:

“assets and liabilities arising from transactions involving revenue of PBEs/NFPs in the public and private sectors should be identified and measured by considering which financial statement elements exist, without being concerned with whether the transaction concerned was ‘exchange’, ‘non-exchange’ or a combination of both.”

- 6 Staff think the Board’s decision quoted in paragraph 5:
- (a) indicates that being ‘exchange’ or ‘non-exchange’ does not determine which financial statement elements arise from a transaction. Therefore, an inflow of services is an asset and income regardless of the nature of the transaction; but
  - (b) does not necessarily indicate whether those elements (assets and income) should be required to be recognised.
- 7 Therefore, staff think the Board’s decision does not, of itself, preclude permitting non-recognition of services received in a non-exchange transaction (donated services) because of, for example, measurement reliability or cost-benefit considerations.
- 8 The merits of the proposal in ED 180 to permit non-recognition of donated services are discussed below, in the light of comments from respondents to that ED.

## Comments by Respondents to ED 180

- 9 Respondents to ED 180 did not strongly support or reject the proposal to permit non-recognition of donated services. Of the twenty-one respondents to ED 180 who commented on this proposal, twelve<sup>3</sup> agreed, eight<sup>4</sup> disagreed and one<sup>5</sup> did not express an overall view.<sup>6</sup>
- 10 Arguments in favour of the ED's proposal (the one made by respondents is asterisked) include:
- (a) \* it is difficult and costly to identify and measure reliably all donated services. For example, volunteer services:
    - (i) tend to be diverse and provided by multiple volunteers;
    - (ii) tend to be subject to less oversight and recording because they do not require outlays by the entity; and
    - (iii) tend not to be the subject of comparable exchange transactions providing market evidence of their fair value;
  - (b) it would achieve the Board's goal at the time to conform to IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)* and thus expedite the replacement of AASB 1004;
  - (c) presently, recognition criteria specific to donated services in AASB 1004 apply only to some types of NFP entity. Removing those recognition criteria would take a consistent approach to the recognition of donated services for all NFPs, because the Standard would not specify any characteristics of services for which recognition may be most appropriate;<sup>7</sup> and
  - (d) modifying the IFRS on *Revenue from Contracts with Customers* to provide this option could be supported on the basis that donated services:
    - (i) occur much more frequently with NFPs than with for-profit entities; and
    - (ii) give rise to special difficulties with recognition and reliable measurement that also raise cost-benefit issues (as noted in subparagraph (a) of this paragraph).

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<sup>3</sup> VTUSFOG (Victorian/Tasmanian Universities Group), FinPro (local government professional association), Joint Accounting Bodies, UHY Haines Norton, Ernst & Young, South Aust. Local Govt Financial Management Group, Aust. Universities Group, PwC (Aust.), PwC (NZ), NZ Not-for-Profit Sector Advisory Committee, Auckland University and Salvation Army

<sup>4</sup> DG & AB Maxwell, ACAG, KPMG (Aust.), KPMG (NZ), HoTARAC, Grant Thornton, South Aust. Treasury and Aust. Dept. of Finance and Deregulation

<sup>5</sup> WA Dept. of Local Govt

<sup>6</sup> For the collation of comments received on this issue, see Agenda Paper B4.2 for the AASB/FRSB meeting on 17 – 18 March 2010, pages 39 – 43. A copy of that paper can be obtained from staff at [jpaul@asab.gov.au](mailto:jpaul@asab.gov.au)

<sup>7</sup> This argument is drawn from paragraphs BC29 and BC30 of the Basis for Conclusions on ED 180 (see paragraph 4 above).

- 11 In addition, the IPSASB argued that some donated services do not meet the definition of an asset because the reporting entity has insufficient control of the services provided (IPSAS 23, paragraph BC25). This argument is not pursued here because the issue is whether services that meet the definition of an asset should be required to be recognised. Other services are irrelevant.
- 12 Arguments made by respondents against the ED's proposal include:
- (a) options in Accounting Standards undermine comparability of financial statements; and
  - (b) non-recognition of donated services omits relevant information about the entity's operations for the period. For some NFPs, donated services can be very significant in value.

### Analysis of Comments

#### Arguments supporting the option proposed in ED 180

##### *Reliability and cost issues*

- 13 Staff agree that donated services often present difficulties with reliable measurement and the cost of recording them. However, staff think those concerns do not necessarily justify permitting non-recognition of all donated services. Some donated services might otherwise be purchased by the entity and have readily available evidence of their fair value (because they are services provided by for-profit entities in market transactions). For example, services provided by teachers' aides (mentioned in paragraph 100 of ED 180) should normally have readily available reliable evidence of their fair value. For donated services that would otherwise be purchased by the entity and have readily available evidence of their fair value, cost-benefit and reliability concerns generally should not be insurmountable.

##### *Conformity to IPSAS 23*

- 14 Staff observe that the argument in paragraph 10(b) above for the option in ED 180 is no longer relevant, because the revised ED will be based on the expected IFRS on *Revenue from Contracts with Customers*. (The argument was noted above to faithfully reflect that it was a significant factor in the AASB's reasoning when it made the proposal in ED 180, and help explain why staff propose departing from the proposal in ED 180.)

##### *Consistent approach for all NFPs*

- 15 Staff note that the proposal in ED 180 would achieve consistent recognition requirements in respect of donated services for all NFPs. However, staff observe that such consistency could also have been achieved by extending the specific recognition criteria for donated services in AASB 1004 to all NFPs. The merits of that approach are discussed below in paragraphs 23 – 29.

### *Modifying the IFRS*

- 16 The argument in paragraph 10(d) indicates there are NFP-specific reasons for modifying the IFRS on *Revenue from Contracts with Customers*. However, it does not necessarily follow that the modification proposed in ED 180 (optional recognition in respect of *any* donated services) is the best alternative to requiring all donated services to be recognised as assets and income.

### Arguments against the option proposed in ED 180

#### *Comparability*

- 17 Staff agree with the respondents' concern that providing optional recognition of donated services, even when reliable measurement is possible, undermines comparability. Staff consider this to be a significant concern.

#### *Relevance*

- 18 The argument by respondents noted in paragraph 12(b), namely, that non-recognition of donated services omits relevant information about the entity's operations for the period, is consistent with the comments in AASB 1004 that:

“... donated services give rise to income and an asset of the recipient and, simultaneously, an expense as the future economic benefits embodied in the asset are consumed. Therefore, the net effect<sup>8</sup> of the contribution of services is the recognition of income and an expense. Such recognition is important if the operating statement is to reflect fully the cost of services provided during the reporting period and the sources and amounts of the entity's income. Such information is useful in assessing the cost efficiency of an entity's performance and the amounts and sources of likely future resource requirements.”  
(paragraph 47)

- 19 Regarding the importance of donated services, a G4+1 paper on non-reciprocal transfers says:

“Many not-for-profit organisations are dependent on donated (volunteer) services for survival. Such services may involve fund-raising activities on behalf of the entity, maintaining club property, developing property for the entity, and acting in official roles such as treasurer or auditor.”<sup>9</sup>

- 20 Based on the points noted in paragraphs 17 – 19, staff consider that recognition of donated services should be required when the fair value of those services can be measured reliably, subject to the additional criterion discussed in paragraphs 23(b) and 25 below. Such an approach is discussed below under the heading ‘Alternative to the Proposal in ED 180’ (see paragraphs 23 – 29).

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<sup>8</sup> Staff think ‘net’ is inappropriate in this context and should be disregarded, because the treatment required is a gross approach.

<sup>9</sup> Mark Westwood and April Mackenzie, Principal Authors, *Accounting by Recipients for Non-Reciprocal Transfers, Excluding Contributions by Owners: Their Definition, Recognition and Measurement*, FASB, Norwalk, 1999, paragraph 2.31.

Staff conclusion on the issues discussed in paragraphs 13 – 20

- 21 On balance, staff do not support retaining the proposal in ED 180 for optional recognition of donated services received. This is because:
- (a) the option permits non-recognition of an important source of income (and related expenses as the services are consumed) of NFPs, and therefore could lead to a loss of relevance and comparability of financial information reported; and
  - (b) the arguments supporting the proposed option do not preclude alternative approaches to accounting for donated services.
- 22 This is an interim conclusion that is extended by the discussion below of an alternative to the proposal in ED 180.

Alternative to the Proposal in ED 180

- 23 The main alternative to the proposal in ED 180 would seem to be to retain the recognition requirement and specific recognition criteria for donated services in AASB 1004, and extend those specific recognition criteria to all NFPs (from their present scope of local governments, government departments, general government sectors and whole of governments). For those entities, AASB 1004 specifically requires donated services to be recognised as income when and only when:
- (a) the fair value of those services can be reliably determined; and
  - (b) the services would have been purchased if they had not been donated. (paragraph 44)
- 24 Criterion (a) in paragraph 23 provides a basis for avoiding the cost and effort involved with measuring donated services lacking evidence of fair value, in addition to specifying a reliability filter consistent with the measurement basis for donated services.
- 25 AASB 1004 explains criterion (b) in paragraph 23 as follows:
- “Some donated services, while useful, may not be central to the delivery of the outputs of the [entity]. In these cases, it is unlikely that the recipient would purchase the services if they were not donated. Recognition of the fair value of those services as income and expenses is not relevant to assessments of the cost of services provided by, or the financial performance of, the recipient.” (paragraph 46)
- 26 Applying the specific recognition criteria for donated services in AASB 1004 (reproduced in paragraph 23) to all NFPs would be another approach (to that in ED 180) to achieving improved consistency in the recognition of donated services for all NFPs. Extending the range of NFPs affected by the specific recognition criteria for donated services might be controversial. Nevertheless, staff think it is not apparent why NFPs other than local governments, government departments, general government sectors and whole of governments should not be subject to those specific criteria.

### Other Literature

- 27 Broadly consistent with FASB Statement No. 116 *Accounting for Contributions Received and Contributions Made*,<sup>10</sup> the G4+1 paper on non-reciprocal transfers referred to in paragraph 19 above proposed requiring recognition of donated services that meet the general recognition criteria in the (then) IASC Framework if they:
- (a) provide specialised skills; and
  - (b) would have had to be purchased by the entity if not donated. (Principle 9, page 41)
- 28 The only substantive difference between those specific criteria and those in AASB 1004 is the G4+1's proposed criterion that the services must provide specialised skills. Neither the Basis for Conclusions on FAS 116 nor the G4+1 paper explain the need for services to provide specialised skills. AASB staff think the 'specialised skills' criterion is similar to a criterion that services would otherwise need to be purchased. However, since an 'otherwise purchase' criterion is separately specified, the 'specialised skills' criterion seems redundant. Staff think that if services would otherwise have been purchased if not donated, it is irrelevant whether those services provide specialised skills, for the purpose of faithfully representing the NFP's dependence on donated services to achieve its objectives. In addition, the meaning of 'specialised' seems subjective and its interpretation might vary (e.g., depending on a particular NFP's employee resources). Therefore, staff do not support including a 'specialised skills' criterion for the recognition of donated services.
- 29 The UK Accounting Standards Board's Exposure Draft FRED 45 *Financial Reporting Standard for Public Benefit Entities* proposes that donated services received should be recognised if they can be reasonably quantified (March 2011, paragraph 7A.8). This proposal differs from the specific recognition criteria in AASB 1004 by not excluding from mandatory recognition donated services that would not otherwise have been purchased. Staff think the 'otherwise purchase' criterion in AASB 1004 is appropriate for the reason given in paragraph 25 above, and because that criterion helps achieve a better balance of costs and benefits associated with the recognition of donated services.

### Other Issue: Defining 'Donated Services'

- 30 Regardless of whether the recognition of any donated services is optional (as proposed in ED 180) or required when specific criteria are met (as recommended by staff), the issue arises whether it would be necessary to define 'donated services' (or an equivalent term like 'services in-kind'). If such a definition were necessary, it could trigger again the Board's concerns regarding the difficulty of distinguishing exchange and non-exchange transactions (see paragraph 33 below for elaboration).
- 31 Although AASB 1004 does not define 'contributed services' or 'donated services', ED 180 describes its equivalent term ('services in-kind') as "services provided by individuals to NFPEs/PBEs in a non-exchange transaction" (paragraph 100). Thus, ED 180 informally defines 'services in-kind'.

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<sup>10</sup> FASB Statement of Financial Accounting Standards No. 116, June 1993, paragraph 9.

- 32 In relation to the concern noted in paragraph 30, staff think it should not be necessary to define ‘donated services’ (for the purpose of permitting non-recognition of some or all donated services) because their meaning should be well understood. The discussion in paragraph 33 applies if the Board disagrees with that view.
- 33 It would seem necessary that any definition of ‘donated services’ (or an equivalent term) would refer to ‘non-exchange transactions’. The Board has already decided that the distinction between exchange and non-exchange transactions, in general, is inherently unclear. Some may counter that a key difficulty of distinguishing exchange and non-exchange transactions relates to transactions involving more than two parties (i.e., a transferor, recipient and beneficiaries), and that donated services do not involve more than two parties. However, another key difficulty of distinguishing exchange and non-exchange transactions relates to difficulties in interpreting exchanges of value that are not ‘approximately equal’. Donated services could be provided in a transaction at below-market rates, in which case an exchange of value that is not approximately equal would occur. Therefore, the Board’s general concern about the difficulty of distinguishing exchange and non-exchange transactions would seem to be an issue if ‘donated services’ were to be defined.

#### Staff Recommendations

- 34 For the reasons discussed in paragraphs 21 – 29, staff recommend retaining the recognition requirement and specific recognition criteria for donated services in AASB 1004, and extending those specific recognition criteria to all NFPs.
- 35 As mentioned in paragraph 32, it should not be necessary to define ‘donated services’ for the purpose of applying the recommendation in paragraph 34, because their meaning should be well understood.

#### **Questions for Board Members**

- Q1** Do you agree with proposing in the ED on Income of NFPs that the recognition of donated services to any NFP should be required when:
- (a) the entity has obtained control of the donated services or the right to receive them;
  - (b) the fair value of those services can be reliably determined; and
  - (c) the services would have been purchased if they had not been donated?
- Q2** Do you agree that, for the purposes of the proposal in Question 1, it should not be necessary to define ‘donated services’?

#### **Disclosure of the Nature and Type of Major Classes of Donated Services**

##### Background

- 36 Paragraph 108(e) of ED 180 proposed requiring disclosure of the nature and type of major classes of ‘services in-kind’ (donated services) received. In contrast, IPSAS 23 only encourages that disclosure.

## Comments by Respondents to ED 180

37 Respondents to ED 180 strongly supported the proposed requirement to disclose information about donated services received. Of the eighteen respondents to ED 180 who commented on the proposal, thirteen<sup>11</sup> agreed and five<sup>12</sup> disagreed.

38 Those who agreed with the proposal and gave their reasons said disclosure of such information would provide useful information about the donated services received on which the NFP relies to carry on its activities. This is consistent with paragraph 116 of ED 180, which says:

“Such disclosures may assist users to make informed judgments about the contribution made by such services to the achievement of the entity’s objectives during the reporting period, and the entity’s dependence on such services for the achievement of its objectives in the future.”

39 Those who disagreed did so because they consider:

- (a) the cost of making the disclosures would exceed the benefits;
- (b) the disclosure requirements should not be more onerous than those in IPSAS 23; and
- (c) only recognised donated services should be required to be disclosed.

## Staff Analysis of Comments in the Light of Developments since ED 180

40 Staff do not support the arguments made against mandatory disclosure of the nature and type of major classes of donated services received. There could be minimal cost associated with disclosing the nature and type of major classes of donated services received, depending on what (if any) related details about those donated services are disclosed to provide additional context. (ED 180 did not propose requiring disclosure of details of those services, such as hours of service or service outputs provided by volunteers. Example 22 of the Implementation Guidance on ED 180, on page 61 of that ED, illustrates disclosures that could be made about unrecognised donated services received.)

41 Since it issued ED 180, the Board decided to base its ED on Income of NFPs on the forthcoming IFRS on *Revenue from Contracts with Customers*, modified where necessary for NFP-specific issues. Therefore, benchmarking to IPSAS 23 is less relevant than considering the likely disclosure requirements of that IFRS. This is considered in paragraph 42 below.

42 IASB ED/2010/6 *Revenue from Contracts with Customers* proposed requiring revenue to be disaggregated into categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors. The ED identified the type of good or service (for example, major product lines) as an example

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<sup>11</sup> Western Aust. Dept. of Local Govt, ACAG, Ernst & Young, Grant Thornton, PwC (Aust.), PwC (NZ), KPMG (Aust.), KPMG (NZ), Auckland University, VTUSFOG (Victorian/Tasmanian Universities Group), South Aust. Treasury, Aust. Universities Group and Salvation Army

<sup>12</sup> Joint Accounting Bodies, HoTARAC, South Aust. Local Govt Financial Management Group, Aust. Dept. of Finance and Deregulation and NZ Not-for-Profit Sector Advisory Committee

of a category of revenue that might be appropriate to meet this requirement (paragraph 74). The AASB generally agreed with this proposal in its submission to the IASB. In addition, staff do not think there are NFP-specific reasons not to require similar disclosures by NFP entities. Therefore, staff think disclosure should be required of:

- (a) the nature and type of major classes of donated services received during the period, whether recognised or unrecognised; and
- (b) where income is recognised in respect of a class of donated services during the period, the amount recognised.

43 This paper does not discuss proposals for Tier 2 disclosure requirements for donated services. Staff plan to base the Reduced Disclosure Regime analysis for Income of NFPs on the analysis that will be performed on the forthcoming Re-Exposure Draft of an IFRS on *Revenue from Contracts with Customers*, and extend that analysis to NFP-specific disclosures. That approach should minimise the risk of making *ad hoc* assessments of which NFP-specific disclosures should not be required for Tier 2 entities.

#### Other Literature

44 FAS 116 (referred to in paragraph 27 above) requires a recipient of contributed services to describe the programs or activities for which those services were used, including:

- (a) the nature and extent of contributed services received for the period; and
- (b) the amount recognised as revenues for the period.

It also encourages entities to disclose the fair value of contributed services received but not recognised as revenues if that is practicable (paragraph 10).

45 The UK Accounting Standards Board's Exposure Draft FRED 45 (referred to in paragraph 29 above) proposes to require disclosure of:

- (a) the nature and recognised amounts of resources received from non-exchange transactions; and
- (b) an indication of other forms of resources from non-exchange transactions from which the entity has benefited (paragraph 7.8).

46 FRED 45 clarifies that an example of the mandatory disclosure proposed in paragraph 45(b) above is disclosure of unrecognised volunteer services (paragraph 7A.11).

47 The G4+1 paper referred to in paragraph 19 above does not discuss whether disclosure of donated services should be required. It says information about unrecognised donated services would also be relevant, including information about the nature of the donated services received and, where known, the fair value of such services (paragraph 4.63).

48 The literature referred to in paragraphs 44 – 47 above is generally consistent with the staff recommendation at the end of paragraph 42.

**Question for Board Members**

- Q3** Do you agree with proposing in the ED on Income of NFPs that disclosure should be required of:
- (a) the nature and type of major classes of donated services received during the period, whether recognised or unrecognised; and
  - (b) where income is recognised in respect of a class of donated services during the period, the amount recognised?