

Income of Not-For-Profit Entities

Staff Paper: Exclusion of For-Profit Government Departments

Introduction

- 1 For the purpose of developing an ED on Income of Not-For-Profit Entities (NFPEs), this paper addresses Specific Matter for Comment (k) in AASB ED 180 *Income from Non-exchange Transactions (Taxes and Transfers)*. That matter is:

“the exclusion of for-profit government departments from the scope of the ED – are requirements for such entities still required?”

Summary of Staff Recommendation

- 2 Staff recommend excluding for-profit government departments¹ from the scope of the ED on Income of NFPEs.

Background

- 3 The Basis for Conclusions on ED 180 included the following background to the ED’s proposal to exclude for-profit government departments from its scope:

“Prior to the December 2007 amendments, AASB 1004 applied only to NFPEs. However, the public-sector-specific requirements added at that time to AASB 1004 also applied to for-profit government departments.² As the focus of this ED is NFPEs, whether in the public sector or the private sector, the AASB concluded that the scope of the ED should not be extended to any for-profit entities.” (paragraph BC33)

¹ Staff are not aware that any for-profit government departments currently exist but, given the definition of ‘government department’ in paragraph Aus7.2 of AASB 101 [namely, “a government controlled entity, created pursuant to administrative arrangements or *otherwise designated as a government department* by the government which controls it” (emphasis added)], note that they might exist in the future.

² The additional requirements were in respect of:

- (a) recognition of parliamentary appropriations by government departments;
- (b) accounting for liabilities of government departments assumed by other entities;
- (c) contributions of services to local governments, government departments, GGSs and whole of governments;
- (d) contributions by owners and distributions to owners of local governments, government departments and whole of governments;
- (e) restructures of administrative arrangements of government controlled NFPEs and for-profit government departments;
- (f) disclosure of contributions to local governments, government departments, GGSs and whole of governments; and
- (g) for government departments only, disclosure of appropriations and liabilities assumed by another entity, and of compliance with parliamentary appropriations and other externally-imposed requirements.

Guidance specific to local governments, government departments, GGSs and whole of governments was also added to AASB 1004 at the time.

Comments by Respondents to ED 180

- 4 Of the eleven respondents who commented on ED 180's proposal to exclude for-profit government departments from the scope of the proposed Standard, seven³ agreed and four⁴ disagreed.⁵
- 5 The reason given for supporting the proposal is that it would be consistent with transaction neutrality between for-profit government departments and other for-profit entities.
- 6 Reasons given for disagreeing with the proposal are that:
- (a) for-profit entities and NFP entities should be subject to similar requirements;
 - (b) the treatment of non-exchange transactions in ED 180 is preferable to that in AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*; and
 - (c) for-profit government departments should be subject to the same requirements for restructures of administrative arrangements as other government departments.
- 7 Two respondents who agreed⁶ also expressed the view that:
- (a) grants should be accounted for consistently by for-profit entities and NFPs (repeating the comment noted above in paragraph 6(a)); and
 - (b) where for-profit government departments apply AASB 120 when accounting for government grants, consideration should be given to the potential impact on consolidation within the GGS and whole of government as part of the AASB project on consolidation of for-profit entities into NFP groups.

Analysis of Comments

Arguments Supporting the Scope Proposal in ED 180

Transaction neutrality between all for-profit entities

- 8 Staff think achieving transaction neutrality between any for-profit government departments and other for-profit entities is the most important consideration in this issue, and provides a compelling reason for supporting ED 180's scope proposal.

³ Joint Accounting Bodies, KPMG (Aust.), Ernst & Young, PwC (Aust.), HoTARAC, South Aust. Treasury and Aust. Dept. of Finance and Deregulation

⁴ VTUSFOG (Victorian/Tasmanian Universities Group), Western Aust. Dept. of Local Govt., ACAG and Aust. Universities Group

⁵ 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 57 – 58. A copy of that paper can be obtained from staff at jpaul@aasb.gov.au

⁶ HoTARAC and Aust. Dept. of Finance and Deregulation

Arguments Against the Scope Proposal in ED 180

Consistency between for-profit and NFP entities; and flaws in AASB 120

- 9 Paragraph 10 discusses jointly the concerns noted in paragraphs 6(a) and 6(b).
- 10 Staff note that for-profit government departments (if any exist) would apply a different treatment of government grants received under AASB 120 than NFPs applying the proposed requirements in the ED on Income of NFPs. Nevertheless:
- (a) staff observe that this difference in the treatment of government grants affects all for-profit entities vis-à-vis NFPs, and think the Board's previous decision that for-profit entities should apply AASB 120 should apply equally to any for-profit government departments; and
 - (b) staff think the rationale for NFPs departing from AASB 120 in respect of government grants—namely, that governments grants are generally much more significant to NFPs than to for-profit entities and therefore the deficiencies of AASB 120 are likely to have a more serious impact on NFPs—should be less applicable to any for-profit government departments. This is because any for-profit government departments should, by their nature, be less dependent on government grants to finance their activities.

Restructures of administrative arrangements

- 11 AASB 1004 *Contributions* requires restructures of administrative arrangements to be accounted for as contributions from owners or distributions to owners, and specifies various disclosures about such restructures. ED 180 proposes retaining those requirements for NFPs. (A future staff paper will discuss whether to confirm that proposal in ED 180.) The respondent's view noted in paragraph 6(c) is that any for-profit government departments should be subject to the same requirements for restructures of administrative arrangements as other government departments.
- 12 Whilst staff agree it would be desirable for all government departments to treat such restructures consistently, staff consider it more important to conform to the general principle that all for-profit entities account in conformity with IFRSs, especially as the number of for-profit government departments seems (at most) very small. If consistency between government departments were the overriding principle, the modifications made to IFRSs in Australian Accounting Standards would be based on the sector rather than whether an entity is for-profit or NFP. Therefore, on balance, staff disagree with the contention that for-profit government departments should be subject to the same requirements for restructures of administrative arrangements as other government departments. Whether applying the for-profit entity text in Australian Accounting Standards to restructures of administrative arrangements (given AASB 3 *Business Combinations* scopes out combinations of entities or businesses under common control) would lead to a different treatment to that presently in AASB 1004 is not explored in this paper.
- 13 The staff view set out in paragraph 12 does not have immediate implications for the application of AASB Interpretation 1038 *Contributions by Owners Made to Wholly-Owned Public Sector Entities*. This is because paragraph 3 of AASB

Interpretation 1038 says the Interpretation does not apply to restructures of administrative arrangements, which are to be accounted for under AASB 1004. Paragraph BC27 of the Basis for Conclusions on ED 180 noted that the AASB intends to reconsider the role of and need for AASB Interpretation 1038 once the outcome of that ED's proposals has been determined. Specific Matter for Comment (n) in ED 180 asked for comments on the role of AASB Interpretation 1038 once a Standard based on the ED is issued. A future staff paper will discuss the comments received on that issue.

Other Issue: Consolidation of For-Profit Entities into NFP Groups

- 14 Regarding the comment noted in paragraph 7(b), staff disagree with basing the requirements for for-profit government departments on the potential impact on consolidation within the GGS and whole of government, at least until the AASB project on consolidation of for-profit entities into NFP groups is progressed. The current policy of the Board regarding all types of reporting entities is that they apply the for-profit or NFP requirements of Australian Accounting Standards according to the nature of that reporting entity, regardless of whether the entity's financial statements are consolidated in group financial statements of an entity of a different nature.

Staff Recommendation

- 15 For the reasons discussed in paragraphs 8 – 14, staff recommend excluding for-profit government departments from the scope of the ED on Income of NFPs. Staff think that, consistent with ED 180, it would be unnecessary to explicitly refer to the exclusion of for-profit government departments in the scope section of the ED on Income of NFPs (although the Basis for Conclusions on that forthcoming ED should briefly explain the exclusion). The ED would simply apply only to NFPs.

Question for Board Members

- Q1** Do you agree with the staff recommendation in paragraph 15?