Note to Board members

The work-in-progress draft Tier 3 ED includes the sections that the Subcommittee members have reviewed to date. Agenda Papers 4.6–4.17 contain the staff analysis and recommendation for drafting each section of the Tier 3 ED and the feedback received from Subcommittee members which staff have transposed into this Agenda Paper.

To navigate this paper, staff have:

- presented 21 questions to the Board in a text box shaded in grey at the start of each section based on:
  - a staff analysis and recommendation to the Board; or
  - staff or Subcommittee member's suggestions for further amendments and simplifications that may differ from the DP proposals and the Board's decisions to date where supported by Subcommittee members.
- presented notes to the Board in a text box shaded in blue and also as comment boxes against relevant paragraphs based on the feedback received from the Subcommittee; and
- shaded paragraphs 23.6–23.17 within Section 23 *Impairment of Assets* which is subject to the Board decision in question 16. Paragraphs 20.3A–20.3C within the Section 20 *Revenue* are shaded to indicate the draft text that staff intends to remove based on the feedback from Subcommittee members; and
- presented edits to drafting as strikethrough and underlined text based on draft Sections staff presented to the Subcommittee and feedback received. Edits are only made where they do not change the Board's decisions made to date.

This work-in-progress draft aims to facilitate the Board's discussion on whether the drafting of the Tier 3 ED reflects appropriately the Board's decisions to date. Editorial review including formatting and cross-references to paragraph numbers have not yet been completed. Staff will complete editorial reviews prior to finalising the Tier 3 ED. Staff have only included limited illustrative examples, as staff are focusing on drafting the mandatory requirements of the Standard first. Staff are seeking the Board's feedback on the overall length of the draft sections and any suggestions for further amendments including simplification of language and otherwise.

AASB Exposure Draft

ED 3XX
Month 202x

General Purpose Financial Statements – Simplified Accounting for Not-for-Profit Private Sector Tier 3 Entities

Comments to the AASB by xx Month 202x

Question 1 to Board members

As noted in Agenda Paper 3.2.1 at the August 2022 Board meeting, staff noted that some stakeholders were concerned that describing the additional financial reporting Tier as 'Tier 3' may confuse smaller preparers given 'Tier' is used by other legislation or regulators to identify an entity's reporting obligation. However, the Board decided it would be beneficial to continue to describe the additional Tier as Tier 3 to distinguish it from the existing Tier 1 and Tier 2 and for the title of the Standard to identify the entities (i.e. Tier 3 NFP Private Sector Entities) that may apply the Standard in the future.

Staff analysis and recommendation

Staff did not receive any stakeholder feedback on the DP that referring to Tier 3 as the future additional financial reporting Tier is confusing and following the outreach, NFP stakeholders are well accustomed to referencing Tier 3 as the potential Tier being developed by the AASB with simplified accounting requirements for smaller entities. Staff consider the title of the Standard should clearly reference Not-for-Profit private sector entities as staff received some feedback on whether the Standard should apply to NFP public sector entities. Staff noted the Board developed this Standard with only smaller NFP private sector entities in mind and also noted that there will be a separate project for the NFP public sector framework.

As such, staff recommend the title of the additional reporting Tier as *General Purpose Financial Statements – Simplified Accounting for Not-for-Profit Private Sector Tier 3 Entities*, being in line with AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*.

Do Board members agree with the name of the potential Tier 3 Standard? If not, what do Board members suggest?

Commenting on this AASB Exposure Draft

Comments on this Exposure Draft are requested by xx Month 202X.

Formal Submissions

Submissions should be lodged online via the "Current Projects – Open for Comment" page of the AASB website (www.aasb.gov.au/current-projects/open-for-comment) as a PDF document and, if possible, a Word document (for internal use only).

Other Feedback

Other feedback is welcomed and may be provided via the following methods:

E-mail: standard@aasb.gov.au
Phone: (03) 9617 7600

All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chair of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

Commented [A1]: **Note to Board members**
Staff are liaising with respective standard-setters regarding copyright agreements on reference materials such as *IFRS for SMEs* and the INPAG. As such, the copyright will be updated in due course.

ISSN 1030-5882

Introduction

Australian Accounting Standards

The Australian Accounting Standards Board (AASB) develops, issues and maintains Australian Accounting Standards.

The AASB is a Commonwealth entity under the *Australian Securities and Investments Commission Act 2001*. AASB 1053 *Application of Tiers of Australian Accounting Standards* explains the two tiers of Australian Accounting Standards. This Exposure Draft proposes a third tier for not-for-profit private sector entities.

Exposure Drafts

The publication of an Exposure Draft (ED) is part of the due process the AASB follows before making a new Australian Accounting Standard or amending an existing one. Exposure Drafts are designed to seek public comment on the AASB's proposals for new Australian Accounting Standards or amendments to existing Standards.

Why we are making these proposals

These proposals are being made in conjunction with Exposure Draft ED XXX *Removal of Special Purpose Financial Statements for Certain Not-for-Profit Entities* (referred to in this document as the ED on the proposed removal of SPFS) to:

(a) provide Tier 3 financial reporting requirements for those not-for-profit (NFP) entities that would be prohibited from preparing Special Purpose Financial Statements (SPFS) under the AASB's proposals that would appropriately balance the needs of financial statement users with the costs of moving from SPFS to other tiers;

(b) reduce the reporting burden of smaller NFP private sector entities where the existing Tier 1 and Tier 2 reporting requirements for preparing General Purpose Financial Statements (GPFS) may be overly complex for application; and

(c) remain consistent with other government red tape reduction initiatives to lessen the financial reporting burden for entities.

Background

AASB 1053 currently sets out the application of two tiers of GPFS with the same recognition and measurement (R&M) requirements, but different levels of disclosures. In this context:

(a) for-profit private sector entities with 'public accountability' (such as listed companies) and governments at the Federal, State/Territory and local levels must apply Tier 1 reporting requirements (full R&M requirements and disclosures) that incorporate International Financial Reporting Standards (IFRS Standards) issued by the International Accounting Standards Board (IASB) and include requirements that are specific to Australian entities; and

(b) other for-profit private sector entities (those without public accountability), NFP private sector entities and public sector entities other than the Australian Government and State, Territory and Local Governments have the option to apply Tier 2 reporting requirements (full R&M requirements with simplified disclosures) instead of Tier 1.

Although there is a need for GPFS to cater for the information needs of a wide range of users, the Board, consistent with the *AASB Not-for-Profit Entity Standard-Setting Framework*, considers that modifications to Australian Accounting Standards for Tier 3 entities can be justified because:

(a) existing requirements impose cost or require effort by preparers that might not be proportionate to the entity's significance and extent of operation; and/or

(b) the needs of users of financial statements of smaller NFP private sector entities are not the same as those of users of financial statements of Tier 1 or Tier 2 entities, and information that provides a relevant and faithfully representative depiction of the entity that is easier to understand would benefit the users of financial statements of such smaller entities.

Since the issue of AASB 1053, the Board has continued to monitor developments, progress research and engage with stakeholders concerning various aspects of the reporting framework, either as part of the work of its Research Centre or as part of the Board's Australian Financial Reporting Framework standard-setting project. In 2016, the Board observed that many stakeholders providing feedback on the Board's work program for the period 2017–2019 (as part of Invitation to Comment ITC 34 *AASB Agenda Consultation 2017–2019*) recommended the Board continue its Australian Financial Reporting Framework project as a high-priority project, and the project scope should consider NFP entities and small-to-medium sized private sector entities. This feedback included suggesting the Board consider the possibility of a third differential reporting tier and reconsidering the criteria for classifying entities as subject to Tier 1 or Tier 2 reporting requirements. Stakeholders also encouraged the Board to continue its work on reviewing the suitability of the reporting entity concept and the prevalence of SPFS.

In developing AASB 1053 *Application of Tiers of Australian Accounting Standards* (which introduced Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements), the Board applied 'user needs' and 'cost/benefit' considerations to identify the extent to which disclosure requirements applicable to Tier 1 entities should be relaxed for Tier 2 entities. 'User needs' and 'cost/benefit' considerations were also implicit in the development of the simplified disclosures in AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*, which replaced the Reduced Disclosure Requirements. Similarly, such considerations were also applied by the IASB to determine the less onerous recognition and measurement requirements of the IASB's *IFRS for SMEs* Standard. Accordingly, the Board similarly decided its proposals on Tier 3 accounting requirements should be developed through considering 'user needs' and 'cost/benefit' overarching principles.

Proposed removal of SPFS for certain not-for-profit entities

Commented [A2]: **Note to Board members**
This section will be updated to reflect decisions the Board will make regarding NFP Conceptual Framework project (including SAC 1 amendments). Staff will bring the revised draft for Board's consideration at a future Board meeting when considering the draft ED on the amendments regarding NFP Conceptual Framework, SAC 1 and other consequential amendments.

Currently, not-for-profit entities may self-assess that they are not a reporting entity as defined in Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity*, and therefore elect to prepare SPFS.

The ability of entities to self-assess their reporting requirements under the Australian reporting entity concept has led to the fundamental SPFS problem, that two similar entities might prepare very different sets of financial statements. This has, in certain cases, resulted in some inappropriate reporting outcomes, including limited comparability between NFP private sector entities in similar economic circumstances.

Considering resource limitations and noting that recommendations arising from the 2017-2018 review of Australian Charities and Not-for-profits Commission (ACNC) legislation were likely to inform the Board's work on the NFP private sector, the Board in 2018 elected to progress its Australian financial reporting framework project in stages, beginning first with the review and revision of the reporting framework for for-profit private sector entities.

In 2018, the Board published Invitation to Comment ITC 39 *Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems* (May 2018). ITC 39 was intended to be a step to improving the quality of financial statements of both for-profit and NFP entities through Board actions to extend the population of entities preparing GPFS.

The work on for-profit private sector entities was completed with the issue of AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* (March 2020) and AASB 2020-2 *Amendments to Australian Accounting Standards – Removal of Special Purpose Financial Statements for Certain For-Profit Private Sector Entities* (March 2020). The outcome of that stage of the Board's project was to require many for-profit entities required by legislation or their constituting document or another document to prepare financial statements that comply with Australian Accounting Standards to prepare GPFS.

However, following feedback on ITC 39, the Board became aware that it may be necessary to develop one or more further reporting tiers (sets of accounting requirements) for use by NFP private sector entities. The Board recognises that there is likely to be a larger population of smaller NFP private sector entities that are required to prepare GPFS, compared to for-profit private sector entities, because the relevant legislation often sets a lower threshold for requiring NFP private sector entities to prepare financial statements that comply with the requirements specified by Australian Accounting Standards.

Consequently, the Board decided that there is a need to develop a further reporting tier for NFP private sector entities at the same time as it supersedes the SAC 1 reporting entity concept for NFP private and public sector entities. This further reporting tier will serve as a proportionate response for smaller-sized entities with less complex transactions and events that are required to prepare financial statements that comply with Australian Accounting Standards. As the Board's review of the Australian financial reporting framework is being conducted in phases, a project considering the appropriateness of the existing reporting framework for public sector entities is being conducted separately on a different timeline to the timeline for NFP private sector entities.

Tier 3 Discussion Paper proposals

In September 2022, the Board issued Discussion Paper *Development of Simplified Accounting Requirements (Tier 3 Not-for-Profit Private Sector Entities)* (Discussion Paper) on its preliminary views about an additional (third) tier for use by NFP private sector entities, being Tier 3 GPFS, and the key features of that further reporting tier (Tier 3 Standard). The Board developed its proposals for the Tier 3 Standard based on the revised ACNC 'medium' size charities (revenue of

$500,000 to less than $3 million) as a reference point for identifying transactions and balances of smaller NFP private sector entities that may be able to prepare Tier 3 GPFS. The matters forming part of the Discussion Paper were those which:

(a) were identified as topics of significant interest or concern to stakeholders – for example, the accounting requirements for subsidiaries and recognition of income;

(b) could have an overarching impact on the development of the Tier 3 reporting requirements – for example, the accounting requirements for changes in accounting policies or correction of errors; and/or

(c) have otherwise been identified as a common transaction, other event or condition of a Tier 3 entity for which the accounting requirements could be simplified – for example, the requirements for property, plant and equipment and employee benefits.

In considering the proposed Tier 3 reporting requirements, the Board had regard to the accounting requirements applying to smaller NFP private sector entities in several other jurisdictions. The selected other jurisdictions were considered on the basis of the international pronouncements compared in the AASB Staff Paper *Comparison of Standards for Smaller Entities* that were reviewed in the AASB Research Report 5 *Financial Reporting Requirements Applicable to Charities* in consideration of the different approaches that already exist for particular areas of financial reporting for the purpose of developing the Tier 3 reporting requirements. The selected jurisdictions and relevant pronouncements are:

- the *International Financial Reporting Standard for Small and Medium-sized Entities* (*IFRS for SMEs* Accounting Standard);
- United Kingdom – FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (FRS 102), FRS 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* and *Accounting and Reporting by Charities: The Statement of Recommended Practice* (Charities SORP);
- Hong Kong – *Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard;*
- New Zealand – *Tier 3 (NFP) Standard Reporting Requirements for Tier 3 Not-for-Profit Entities* (NZ Tier 3 (NFP) Standard);
- Canada – *CPA Canada Handbook Part III – Accounting Standards for Not-for-Profit Organizations*;
- Singapore – *Charities Accounting Standard*; and
- United States of America – *Financial Accounting Standards Board Accounting Standards Codification, Topic 958 Not-for-Profit Entities.*

The Board also had regard to the *International Non-Profit Accounting Guidance* (INPAG) proposals developed by the Chartered Institute of Public Finance and Accountancy.

In the Discussion Paper, the AASB proposed:

(a) Tier 3 reporting requirements with simplified R&M requirements and a disclosure approach that complements the R&M requirements for topics that will be included in the proposed Tier 3 Standard;

(b) not to establish any reporting thresholds and that any specification of a particular form of GPFS is more appropriately within the remit of a regulatory authority that determines whether financial statements must be prepared by regulated entities in accordance with Australian Accounting Standards; and

(c) its intention to extend the general application of Australian Accounting Standards to the broader NFP sector, which may result in certain NFP private and public sector entities no longer being able to prepare special purpose financial statements.

The Board was also informed by Research Report 19 *Common Financial Statement Items: Charities with $0.5-$3 million in revenue* (April 2023), which analysed 260 financial statements of ACNC-registered charities with annual revenue ranging from $0.5 million to $3 million to identify the financial statements line items that are commonly recorded in financial statements of medium-sized charities.

Feedback on the proposals in the Discussion Paper was sought through various outreach activities from October 2022 to March 2023, including virtual outreach sessions, an online survey and submissions. The Board considered the stakeholder comments and assessed the feedback with reference to the principles for developing simplified accounting requirements. The Board decided to proceed with developing a stand-alone accounting standard for a third reporting tier for use by smaller NFP private sector entities, thus extending the application of Australian Accounting Standards to the broader NFP sector.

What we are proposing

This Exposure Draft proposes:

(a) a new Tier 3 Australian Accounting Standard to be titled *General Purpose Financial Statements – Simplified Accounting for Not-for-Profit Private Sector Tier 3 Entities* that applies to smaller not-for-profit (NFP) private sector entities with features including:

  (i) new Tier 3 recognition and measurement requirements that apply to all Tier 3 NFP private sector entities; and

  (ii) new Tier 3 disclosures that accompany the Tier 3 recognition and measurement requirements that apply to all Tier 3 NFP private sector entities; and

(b) to provide relief from restating and presenting comparative information in the year of transition for entities transitioning to the Tier 3 Australian Accounting Standard.

The consequences of the proposals in this ED would be the minimum requirements proposed for GPFS is a new Tier 3 GPFS framework which requires compliance with simplified recognition and measurement requirements in Australian Accounting Standards, and simplified disclosure requirements that complement the simplified accounting requirements. An entity may voluntarily elect, unless otherwise required by legislation or by their constituting document or another document, to prepare:

(a) Tier 1 GPFS, complying with the full recognition, measurement and disclosure requirements in Australian Accounting Standards; or

(b) Tier 2 GPFS, complying with the full recognition and measurement requirements and with simplified disclosure requirements.

In developing the Tier 3 GPFS framework, the Board determined a new set of principles and methodology to make this new Tier 3 Standard applicable to Tier 3 NFP private sector entities, considering 'user needs' and 'cost/benefit' as overarching considerations and the following principles:

(a) the development of Tier 3 reporting requirements is subject to the *AASB Not-for-Profit Entity Standard-Setting Framework*;

(b) Tier 3 financial statements are GPFS. As such, Tier 3 financial statements need to provide useful financial information to users of the financial statements;

(c) consistency with the accounting principles specified by Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable, but might not always be warranted, since Tier 3 requirements are being developed as a proportionate response to the costs incurred by certain entities while still meeting the needs of users of the financial statements for this cohort of entities. For example, opportunities for departure from Tier 2 accounting principles that could give a similar outcome to users of the financial statements while reflecting an appropriate cost/benefit balance could include disclosure requirements instead of a Tier 2 measurement requirement or an approach of specifying minimum 'prescriptive' disclosures;

(d) where possible, leverage the information management uses to make decisions about the entity's operations. The ability to leverage information management uses is made within the context of the Board's Conceptual Framework relevant to NFP entities and user needs and cost/benefit considerations, and the objective of comparability of applying Tier 3 requirements across entities; and

(e) an accounting requirement does not impose disproportionate costs for preparers when compared to the benefits of that information for financial statement users.

In drafting the Tier 3 R&M and disclosure requirements for this ED, the Board considered simplifications based primarily on the NZ Tier 3 (NFP) Standard and the following approaches:

(a) for transactions with the same or similar R&M requirements to the Tier 2 NFP private sector entities, the R&M and disclosure requirements would be drafted with reference to the corresponding Tier 2 requirements. The *IFRS for SMEs* Accounting Standard requirements are also used as a starting point, with modifications based on consideration of the INPAG proposals, FRS 102 or the Charities SORP to the extent the requirements align with Tier 2 requirements; and

(b) for transactions where there is an R&M difference between the Tier 2 and Tier 3 requirements, consideration should be given to:

  (i) adopting, to the extent possible, appropriate requirements in other jurisdictions or frameworks as a starting point; or

  (ii) in other cases, developing requirements based on the *IFRS for SMEs* Accounting Standard and the INPAG proposals as a starting point.

Application date

It is proposed that the amendments would apply to annual periods beginning on or after X Month 202X, with earlier application permitted.

Who will be affected

The proposals are developed for application by not-for-profit private sector entities that are required by legislation to prepare financial statements that comply with either Australian Accounting Standards or "accounting standards" or else required by their constituting document or another document to prepare financial statements that comply with Australian Accounting Standards. These entities may elect to prepare Tier 1 or Tier 2 GPFS instead of Tier 3 GPFS.

Public sector

Although not-for-profit public sector entities are not affected by the proposals in the ED, those not-for-profit public sector entities that are required by legislation to prepare financial statements that comply with either Australian Accounting Standards or "accounting standards", or else required by another document to prepare financial statements that comply with Australian Accounting Standards, will no longer be able to prepare SPFS based on the proposals in [ED XXX] to extend the application of the Australian Accounting Standards to the public and private not-for-profit sector.

What happens next

The AASB will consider feedback on this Exposure Draft at future meetings and, based on the information received, will determine whether the proposals should be implemented, with or without amendment. Depending on the nature and extent of the feedback, the AASB may publish another Exposure Draft or a Fatal-Flaw Review Draft to enable further consultation with stakeholders.

We need your feedback

Comments are invited on any of the proposals in this Exposure Draft by x Month 2025. Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or otherwise, on the major issues. The AASB regards supportive and non-supportive comments as essential to a balanced review of the issues and will consider all submissions, whether they address some or all specific matters, additional issues or only one issue (whether an issue specifically identified below or another issue).

Specific matters for comment [TBU]

Commented [A3]: Note to Board members
Staff have not yet developed the specific matters for comment as staff are seeking whether the drafting of the Tier 3 ED reflects appropriately the Board's decisions to date. Staff will bring the draft specific matters for comments for Board's consideration at a future Board meeting.

The AASB would particularly value comments on the following:

1. Do you agree with the proposals [TBU] .
2. Do you think any unintended consequences might arise from the proposals? If yes, please explain what they are.
3. Do you have any other comments on the proposals?

General matters for comment

The AASB would also particularly value comments on the following general matters:

1. Has the *AASB Not-for-Profit Entity Standard-Setting Framework* been applied appropriately in developing the proposals in this Exposure Draft?
2. Are there any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals?
3. Do the proposals create any auditing or assurance challenges and, if so, please explain those challenges?

4. Would the proposals result overall in financial statements that are useful to users?

5. Are the proposals in the best interests of the Australian economy?

6. Unless already provided in response to specific matters for comment above, what are the costs and benefits of the proposals whether quantitative (financial or non-financial) or qualitative, and are they appropriate relative to the existing requirements? In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

Contents

[Draft] Australian Accounting Standard AASB 10XX *General Purpose Financial Statements – Simplified Accounting For Not-for-Profit Private Sector Tier 3 Entities* is set out in paragraphs 1.1–X and Appendices A–C. All the paragraphs have equal authority. AASB 10XX is to be read in the context of other Australian Accounting Standards as set out in paragraph 1.3. In the absence of explicit guidance, Section 9 Accounting Policies, Estimates and Errors provides a basis for selecting and applying accounting policies.

Preface

Introduction

This Australian Accounting Standards Board (AASB) develops, issues and maintains Australian Accounting Standards including Interpretations. The AASB is a Commonwealth entity under the *Australian Securities and Investments Commission Act 2001*.

AASB 1057 *Application of Australian Accounting Standards* identifies the application of Standards to entities and financial statements. AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of three tiers of reporting requirements for preparing general purpose financial statements.

Main features of this [draft] Standard

Main requirements

This Standard sets out new, separate recognition, measurement, presentation and disclosure requirements for a new tier, Tier 3, which is applicable to certain not-for-profit private sector entities. This Standard has been developed through applying a new methodology and principles based on considering preparer costs and user needs to determine the modified recognition, measurement, presentation and disclosure requirements that are appropriate for Tier 3 entities. The methodology and principles applied are outlined in the Basis for Conclusions.

This Standard does not specify which entities are permitted to apply Tier 3 reporting requirements. That is a matter for other regulatory authorities to determine. The recognition, measurement, presentation and disclosure requirements that are relevant to Tier 3 entities are set out in this separate Standard.

Application date

This Standard applies to annual reporting periods beginning on or after … [1 January 202X]. Earlier adoption of this Standard is permitted.

[Draft] Accounting Standard AASB 10XX

The Australian Accounting Standards Board makes Accounting Standard AASB 10XX *General Purpose Financial Statements – Simplified Accounting for Not-for-profit Private Sector Tier 3 Entities* under section 334 of the *Corporations Act 2001*.

Keith Kendall
Chair – AASB

Dated … [date]

[Draft] Accounting Standard AASB 10XX
General Purpose Financial Statements – Simplified Accounting for Not-for-Profit Private Sector Tier 3 Entities

Note to Board members

In Agenda Paper 4.11 for this meeting, staff asked Subcommittee members whether they agreed with the draft text in paragraphs 1.1–1.2 on the objective and scope of the entities that shall, as a minimum, apply Tier 3 reporting requirements in preparing GPFS below. The Subcommittee members that provided comments agreed with the paragraph 1.2 wording.

Subcommittee members were asked if they consider that a single approach should be applied in making all references to higher Tier(s) than Tier 3 (and, if so, should Tier 2 alone be referred to) in relation to paragraph 1.3 below. Subcommittee members prefer the general principle to refer to higher Tier(s) and only as an exception (where required) refer to Tier 1 or Tier 2.

Subcommittee members have also reviewed the drafting for going concern and offsetting that will be included in the Section 2 on financial statement presentation and a Subcommittee member provided feedback relating to going concern disclosures as noted in paragraphs 2.X3–2.X7 below.

Section 1: Objective, Scope and Application

Objective

1.1 The objective of this Standard is to specify proportionate, simplified financial reporting requirements for general purpose financial statements prepared by Tier 3 not-for-profit private sector entities, to require the reporting of useful, consistent and transparent information by those entities in a manner that achieves an appropriate balance of costs and benefits.

Intended scope of this Standard

1.2 Not-for-profit private sector entities without public accountability and qualifying as 'Tier 3 entities' under the relevant regulatory regime shall, as a minimum, apply Tier 3: ~~reporting requirements in preparing general purpose financial statements~~ Australian Accounting Standards – Simplified Accounting under AASB 1053 *Application of Tiers of Australian Accounting Standards*. These types of entities may elect to apply Tier 1 or Tier 2 reporting requirements in their entirety, instead of Tier 3 reporting requirements, in preparing general purpose financial statements, subject to regulatory requirements.

Commented [A4]: Note to Board members
The Subcommittee members did not provide any comments on the drafting of this paragraph in Agenda Paper 4.11 for this meeting but staff have edited this draft to be consistent with the reference to other Tiers as referred to in AASB 1053.

Application of this Standard

1.3 A not-for-profit private sector entity that is eligible for, and is required to or elects to apply, the Tier 3 reporting requirements in preparing general purpose financial statements shall apply:

(a) ~~Sections 1 – 29, the effective date and transition requirements in Appendix A and the glossary of defined terms in Appendix B~~this Standard; and

(b) the ~~following~~ recognition, ~~and~~ measurement and presentation requirements of the following Australian Accounting Standards and Interpretation, ~~subject to applying the~~ and any related disclosure requirements ~~of~~ in AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities*:

(i) AASB 2 *Share-based Payment*, in relation to share-based payment arrangements;

(ii) AASB 4 *Insurance Contracts* and AASB 1023 *General Insurance Contracts*, or AASB 17 *Insurance Contracts*, in relation to insurance contracts;

(iii) AASB 5 *Non-current Assets Held for Sale and Discontinued Operations*, in relation to assets held for sale;.

(iv) AASB 6 *Exploration for and Evaluation of Mineral Resources*, in relation to exploration for, and evaluation of, mineral resources;

(v) AASB 9 *Financial Instruments*, in relation to complex financial instruments identified in Section 10 *Financial Instruments* of this Standard;

(vi) AASB 119 *Employee Benefits*, in relation to obligations arising under a defined benefit plan;

(vii) AASB 141 *Agriculture*, in relation to biological assets, and agricultural produce at the point of harvest; and

(viii) AASB Interpretation 12 *Service Concession Arrangements* as identified in AASB 1048 *Interpretation of Standards*, in relation to accounting by an operator in a service concession arrangement.

Commented [A5]: Note to Board members
A Subcommittee member has provided comments that an asset held for sale could be considered an indicator of impairment which will be discussed further in Question 15 of Section 23 *Impairment of Assets*.

Section 2: Financial Statement Presentation [TBU]

Commented [A6]: Note to Board members
The Subcommittee has reviewed the drafting for going concern requirements and offsetting presented in Agenda Paper 4.11 for this meeting. Staff will include the remainder of the drafting for the Section on Financial Statements Presentation after Board's deliberation in Agenda Paper 4.2 at this meeting for the Subcommittee to review and subsequently include the drafting in the next iteration of the draft ED at a future Board meeting.

Scope

2.1 xxx

Measurement

2.2 xxx

Going concern

2.X3 When preparing financial statements, the entity's management shall assess the entity's ability and willingness to continue as a going concern. An entity is a going concern unless management either intends to liquidate the entity or to cease its operations, or has no realistic alternative to doing so. In assessing whether the going concern assumption is appropriate, management takes into account all information available about the future, looking forward at least twelve months from the end of the reporting period.

Disclosures

2.X4 Where management is aware of material uncertainties about future events or conditions that might cast significant doubt upon the entity's ability or willingness to continue as a going concern, the entity shall disclose those uncertainties. The statement of accounting policies in the notes shall disclose whether the financial statements were prepared on a going concern basis. When the entity does not prepare financial statements on a going concern basis, it shall also disclose:

(a) a statement that the entity intends to cease operating or that it is unlikely the entity will be able to continue operating, together with the reason(s) why; and

(b) the basis on which the financial statements were prepared.

2.X5 The effect of ~~such a change~~ the change in the entity's ability to continue as a going concern on the amounts of the entity's assets and liabilities at the end of the reporting period will depend upon the entity's particular circumstances. For example, that effect will depend upon whether operations are to be transferred to another entity, sold in an orderly manner, or liquidated in a rushed sale. Judgement is required in determining whether a change in the carrying amounts of assets and liabilities is required. It is also necessary to consider whether the change in circumstances leads to additional liabilities or triggers clauses in debt contracts that will lead to the reclassification of those debts as current liabilities.

Commented [A7]: Note to Board members
A Subcommittee member considered it was not clear to the reader what "such a change" is referring to. I.e. whether it is that the entity is no longer a going concern or the change in basis on which the financial statements were prepared, or both. The member considered this need be clarified.

Staff revised the wording to clarify that the change relates to the entity's ability to continue as a going concern in the drafting.

Offsetting

2.X6 Users of financial statements should be given as much relevant information as possible about the entity's transactions and balances. Therefore, the entity shall report gross amounts for transactions and balances, and not offset (net off) separate transactions or balances. This means that:

(a) assets and liabilities shall not be offset against each other; and

(b) revenue and expenses shall not be offset against each other

unless required or permitted to do so by this [draft] Standard.

2.X7 The following practices do not involve offsetting:

(a) measuring assets net of valuation adjustments such as obsolescence or impairment write-downs of items of inventory or property, plant and equipment;

(b) netting amounts due from and payable to the same counterparty if the entity is legally entitled to do so in settlement of those amounts;

(c) presenting a gain or loss on the sale of an item of property, plant and equipment or investment by deducting from the asset's sale consideration the asset's carrying amount and related selling expenses; and

(d) presenting on a net basis gains and losses arising from transactions or other events of a similar nature (eg foreign exchange gains and losses).

Section 3: Statement of Financial Position [TBU)

Scope of this section

3.1 xxx

Section 4: Statement of Comprehensive Income and Income Statement [TBU]

Scope of this section

4.1 xxx

Section 5: Statement of Changes in Equity and Statement of Income and Retained Earnings [TBU]

Scope of this section

5.1 xxx

Section 6: Statement of Cash Flows [TBU]

Scope of this section

6.1 xxx

Section 7: Notes to the Financial Statements [TBU]

Scope of this section

7.1 xxx

Section 8: Consolidated and Separate Financial Statements

Note to Board members

In Agenda Paper 4.16 for this meeting, staff asked Subcommittee members whether they agreed with:

(a) The length of the draft sections Consolidation and Separate Financial statements being appropriate.

Feedback from Subcommittee: The members that commented were agreeable with the length of the draft section considering the Board's decisions to date.

(b) The draft requirement being sufficiently clear for a reporting entity:

(i) with one or more subsidiaries that elects to present consolidated financial statements (paragraph 8.2(a) applying requirements in paragraphs 8.15 – 8.27);

(ii) with one or more subsidiaries that elects not to present consolidate financial statements (paragraph 8.2(b) applying requirements in paragraphs 8.34–8.36 and disclosures in paragraph 8.32);

(iii) that has one or more notable relationships but is uncertain whether any of them are its subsidiaries (apply only disclosure requirements in paragraphs 8.28–8.32); and

(iv) that has one or more notable relationships (e.g. associates) that are not subsidiaries (applying requirements in paragraphs 8.28–8.32).

Feedback from Subcommittee: The members that commented consider the drafting of paragraph 8.3 is not clear and requires rewording. One member suggested possible improvements could be to cross-reference to paragraphs 8.2(a) and (b), and educational materials or application guidance such as a decision tree diagram may be helpful. Refer to paragraph 8.3 for further Subcommittee comments. Staff agree with the Subcommittee members' feedback and have reworded the sentence as per the Subcommittee member's suggestion as shown by strikethrough and underlined text in paragraph 8.3.

(c) Staff's suggestion to add to paragraph 8.16 of the *IFRS for SMEs* Accounting Standard requirements that any difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall not exceed three months, and also that both the length of the reporting periods and differences between the dates of the financial statements shall be the same from period to period. Staff suggested the additional text because, if a parent entity elects to prepare consolidated financial statements, its obligations in respect of uniform reporting periods should be no less onerous than the obligations applying to Tier 2 entities. The additional text would also align with AASB 10 requirements (refer to paragraph B93).

Feedback from Subcommittee: The members that commented agree with staff's suggestion.

(d) Staff's suggestion to omit the text of the *IFRS for SMEs* Accounting Standard requirements regarding when a parent loses control of a subsidiary, the parent shall account for all amounts previously recorded in other comprehensive income for that subsidiary (i.e. paragraph 8.21). Staff suggested the removal based on the proposal to remove a parallel requirement on the procedure to follow when discounting application of the equity method in the draft section on Investment in Associates and Joint Arrangements. As such, in the interest of brevity, staff consider it proportionate to omit the draft paragraph 8.21.

Feedback from Subcommittee: The members that commented agree with staff's suggestion.

Question 2 to Board members

Staff asked Subcommittee members whether 'notable relationships' is the best term for such relationships. The term notable relationships was suggested by the Board at its November 2023 meeting when discussing Agenda Paper 5.2, where staff previously referred to these relationships as 'significant relationships'.

Of the Subcommittee members that commented, one member agreed with the term, considering it is sufficiently different from other terms to avoid confusion while another member prefers the term 'important relationships'.

Staff note that the term 'notable' is not used in any AAS, so it would be unique within the Tier 3 Standard. The term 'important' is used in various AAS, such as in AASB 110 *Events after the Reporting Period* (in paragraph 18 it states: *It is important for users to know when the financial statements were authorised for issue.*). Staff do not have particular leanings which term to use but consider the term 'important' to be plainer English and familiar than 'notable'. If the Board prefers the term 'important', staff will update the drafting accordingly.

Do Board members prefer to retain the term 'notable relationships' in the draft Tier 3 ED? If not, do Board members prefer the term 'important relationships' or have any other suggestions?

Question 3 to Board members

A Subcommittee member suggested the relocation of paragraph 8.12 relating to power in reference to voting rights to follow paragraph 8.5 which refers to when an investor has control.

While staff agree that paragraph 8.12 refers to when an investor has power over an investee, it also provides references to paragraph 8.13 relating to potential voting rights. As such, staff recommend that paragraph 8.12 to remain as per staff drafting.

Do Board members agree with staff's recommendation not to relocate paragraph 8.12 to follow 8.5? If not, do Board members prefer it relocated under paragraph 8.5 or any other paragraph?

Question 4 to Board members

Paragraph 8.27(b) proposes an entity shall make disclosures in consolidated financial statements, the basis for concluding that control exists when the parent does not own, directly or indirectly through subsidiaries, a majority of the voting rights of the other entity. A Subcommittee member considers whether it is appropriate, given the staff's suggestion not to include the rebuttable presumption from the *IFRS for SMEs* Accounting Standard requirements that control exist when an investor own a majority of the voting rights of an investee, to change the reference of 'control' to 'power' instead.

Staff continue to think the term 'control' is appropriate given power is only one element in assessing whether an investor controls an investee, and the disclosure required in paragraph 8.27(b) relates to the basis on which an entity assesses that control exists when an investor may not have a majority of voting rights of the investee.

Do Board members agree with staff recommendation to retain the term control in the draft paragraph 8.27(b)? If not, do Board members prefer the term be changed to power as per the Subcommittee member's suggestion?

Scope of this section

8.1 This section defines the circumstances in which an entity applying this Standard presents consolidated financial statements and the procedures for preparing those statements in accordance with this Standard. It also includes:

(a) disclosure requirements about notable relationships in separate financial statements; and

(b) guidance on how to prepare separate financial statements in accordance with this Standard, if they are prepared.

Presentation of consolidated financial statements

8.2 A reporting entity that, in applying paragraphs 8.4 – 8.14, identifies it has subsidiaries shall either:

(a) present consolidated financial statements in which it consolidates its subsidiaries, by including the parent, all its subsidiaries and no other entities, in accordance with paragraphs 8.15 – 8.27; or

(b) present, as its only financial statements, separate financial statements that:

(i) do not consolidate its subsidiaries;

(ii) are prepared in accordance with paragraphs 8.34 – 8.36; and

(iii) disclose the information about its notable relationships specified in paragraph 8.32. 'Notable relationships' are defined in paragraph 8.29.

8.3 If a reporting entity prepares consolidated financial statements in accordance with paragraph 9.2(a), it may also elect to ~~present~~prepare separate financial statements ~~that do not consolidate its subsidiaries but instead record its investments in its subsidiaries~~ in accordance with paragraph 8.2(b)~~.~~; except ~~Those separate financial statements do not need to make~~ the disclosures about notable relationships ~~referred to in~~ under paragraph 8.2(b)(iii) are not required.

Assessing control of an investee

8.4 A subsidiary is an entity (an investee) controlled by another entity (an investor). An investor, regardless of the nature of its involvement with the investee, shall determine whether it is a parent by assessing whether it controls the investee.

8.5 An investor controls an investee if, and only if, the investor has all the following:

(a) power over the investee;

(b) exposure, or rights, to variable returns from its involvement with the investee; and

(c) the ability to use its power over the investee to affect the amount of the investor's returns.

8.6 The investor shall reassess whether it controls an investee if circumstances indicate there are changes to one or more of the three elements of control listed in paragraph 8.5.

8.7 An investor has power over an investee when the investor has existing rights that give it the current ability to direct the relevant activities, that is the activities that significantly affect the investor's returns. Relevant activities include, but are not limited to:

Commented [A8]: **Note to Board members:**
Two Subcommittee members that provided comments considered paragraph 8.3 needs to be reworded as it was unclear. One of the members proposed that the paragraph could be reworded to:
"If a reporting entity prepares consolidated financial statements in accordance with paragraph 9.2(a), it may also prepare separate financial statements in accordance with paragraph 9.2(b); except the disclosure requirements under paragraph 9.3(b)(iii) are not required".

Staff agree with the Subcommittee members' feedback and have reworded accordingly as per strikethrough and underlined text.

(a) selling and purchasing goods or services;

(b) selecting, acquiring or disposing of assets;

(c) providing services in accordance with the investor's objectives;

(d) fundraising; and

(e) developing budgets in relation to the activities in (a) – (d).

8.8 An investor with the current ability to direct the relevant activities has power even if its rights to direct have yet to be exercised. Evidence that the investor has been directing relevant activities can help determine whether the investor has power, but is not, in itself, conclusive in determining whether the investor has power over an investee.

8.9 An investor is exposed, or has rights, to variable returns from its involvement with the investee when the investor's returns from its involvement have the potential to vary as a result of the investee's performance. The investor's returns can be only positive, only negative or both positive and negative.

8.10 An investor's returns from its involvement with an investee are broad in nature, encompassing financial, non-financial, direct and indirect benefits, such as when the furtherance of the investee's financial and non-financial objectives contributes to the furtherance of the investor's financial and non-financial objectives. For example, the provision of goods or services by the investee to its beneficiaries might further the achievement of the investor's social policy objectives. These returns to the investor would reflect factors such as the efficiency and effectiveness of delivery of the goods and services and changes in the outcomes for beneficiaries.

8.11 When an investor with decision-making rights (a decision-maker) assesses whether it controls an investee, it shall determine whether it is a principal or an agent. An investor shall also determine whether another entity with decision-making rights is acting as an agent for the investor. An agent is a party primarily engaged to act on behalf and for the benefit of another party or parties (the principal(s)) and therefore does not control the investee when it exercises its decision-making authority. Thus, sometimes a principal's power may be held and exercisable by an agent, but on behalf of the principal. A decision-maker is not an agent simply because other parties can benefit from the decisions it makes.

8.12 An investor can have power even if it holds less than a majority of the voting rights of an investee, for example, through:

(a) a contractual arrangement between the investor and other vote holders;

(b) rights arising from other contractual arrangements;

(c) the investor's voting rights;

(d) potential voting rights (see paragraph 8.13); or

(e) a combination of (a)–(d).

8.13 When assessing control, an investor considers its potential voting rights as well as potential voting rights held by other parties, to determine whether it has power. Potential voting rights are rights to obtain voting rights of an investee, such as those arising from convertible instruments or options, including forward contracts. Those potential voting rights are considered only if the holder of the right has the practical ability to exercise that right.

8.14 If an investor also has voting or other decision-making rights relating to the investee's relevant activities, the investor assesses whether those rights, in combination with potential voting rights, give the investor power.

Consolidation procedures

8.15 Consolidated financial statements present financial information about the group as a single reporting entity. In preparing consolidated financial statements, an entity shall:

(a) combine the financial statements of the parent and its subsidiaries line by line by adding together like items of assets, liabilities, equity, income, expenses and cash flows.

(b) eliminate the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary.

(c) eliminate in full intragroup assets, liabilities, equity, income, expenses and cash flows (including dividends). Profits and losses resulting from intragroup transactions that are recorded in assets, such as inventory and property, plant and equipment, are eliminated in full. Intragroup losses may indicate an impairment that requires recording in the consolidated financial statements (see Section 23 *Impairment of Assets*).

(d) measure and present non-controlling interest in the profit or loss of consolidated subsidiaries for the reporting period separately from the interest of the owners of the parent.

(e) measure and present non-controlling interest in the net assets of consolidated subsidiaries separately from the parent shareholders' equity in them. Non-controlling interest in the net assets consists of:

   (i) the amount of the non-controlling interest at the date of the original combination calculated in accordance with [*TBU Section 17 Business Combinations and Goodwill]*; and

   (ii) the non-controlling interest's share of changes in equity since the date of the combination.

8.16 The proportions of profit or loss and changes in equity allocated to the owners of the parent and to the non-controlling interest are determined on the basis of existing ownership interests and do not reflect the possible exercise or conversion of potential voting rights.

Uniform reporting date

8.17 The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements shall be prepared as of the same reporting date unless it is impracticable to do so. If it is impracticable to prepare the financial statements of a subsidiary as of the same reporting date as the parent, the parent shall consolidate the financial information of the subsidiary using the most recent financial statements of the subsidiary, adjusted for the effects of significant transactions or events that occur between the date of those financial statements and the date of the consolidated financial statements. In any case, the difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall not exceed three months, and both the length of the reporting periods and any difference between the dates of the financial statements shall be the same from period to period.

Uniform accounting policies

8.18 Consolidated financial statements shall be prepared using uniform accounting policies for like transactions and other events and conditions in similar circumstances. If a subsidiary uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements in preparing the consolidated financial statements to ensure conformity with the group's accounting policies.

Acquisition and disposal of subsidiaries

8.19 The income and expenses of a subsidiary are included in the consolidated financial statements from the acquisition date until the date on which the parent loses control of the subsidiary.

8.20 If a parent loses control of a subsidiary, the parent:

(a) ceases recording:

   (i) the assets (including any goodwill) and liabilities at their carrying amounts at the date control is lost in the former subsidiary from the consolidated statement of financial position; and

   (ii) the carrying amount of any non-controlling interests in the former subsidiary at the date when control is lost (including any components of other comprehensive income attributable to them);

(b) records:

   (i) the fair value of the consideration received, if any, from the transaction, event or circumstances that resulted in the loss of control; and

   (ii) any investment retained in the former subsidiary at its fair value on the date control is lost; and

(c) records the gain or loss associated with the loss of control attributable to the former controlling interest.

~~8.21 If a parent loses control of a subsidiary, the parent shall account for all amounts previously recorded in other comprehensive income for that subsidiary, on the same basis as would be required if the parent had directly disposed of the related assets or liabilities.~~

8.22 If a parent loses control of a subsidiary but continues to hold an investment in the former subsidiary, that investment shall be accounted for in accordance with other sections of this Standard. If the retained interest is a financial asset, Section 11 *Financial Instruments* applies; and if it is an interest in an associate or a ~~joint~~ly ~~controlled entity~~ venture, Section 14 *Investments in Associates and Joint Arrangements* applies. The fair value on the date control is lost shall be regarded as the fair value on initial recording of a financial asset or the cost on initial recording of an investment in an associate or joint~~ly controlled entity~~ venture, if applicable.

Commented [A9]: Note to Board members
As per staff's suggestion in paragraph (d) in the Note to Board members at the beginning of Section 8, reflecting on the feedback from Subcommittee members, staff removed paragraph 8.21 based on the suggestion to remove a parallel requirement on the procedure to follow when discounting application of the equity method in the draft section on Investment in Associates and Joint Arrangements.

Non-controlling interest in subsidiaries

8.23 An entity shall present non-controlling interest in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent, as required by [*TBU: Section X Statement of Financial Position paragraph 4.2(q)*].

8.24 An entity shall treat changes in a parent's controlling interest in a subsidiary that do not result in a loss of control as transactions with owners in their capacity as owners. Accordingly, the carrying amount of the non-controlling interest shall be adjusted to reflect the change in the parent's interest in the subsidiary's net assets. Any difference between the amount by which the non-controlling interest is so adjusted and the fair value of the consideration paid or received, if any, shall be recorded directly in equity and attributed to owners of the parent. An entity shall not record any gain or loss on these changes. Also, an entity shall not record any change in the carrying amounts of assets (including goodwill) or liabilities as a result of such transactions.

8.25 An entity shall disclose non-controlling interest in the profit or loss of the group separately in the statement of comprehensive income, as required by [*TBU: Section X Statement of Comprehensive Income and Income Statement paragraph 5.6 (or in the income statement, if presented, as required by paragraph 5.7)*].

8.26 Profit or loss and each component of other comprehensive income shall be attributed to the owners of the parent and to the non-controlling interest. Total comprehensive income shall be attributed to the owners of the parent and to the non-controlling interest even if this results in the non-controlling interest having a deficit balance.

Disclosures in consolidated financial statements

8.27 The following disclosures shall be made in consolidated financial statements:

(a) the fact that the financial statements are consolidated financial statements;

(b) the basis for concluding that control exists when the parent does not own, directly or indirectly through subsidiaries, a majority of the voting rights of the other entity;

(c) any difference between the reporting dates of the financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements; and

(d) the nature and extent of any significant restrictions (for example resulting from borrowing arrangements or regulatory requirements) on the ability of subsidiaries to transfer funds to the parent in the form of cash dividends or to repay loans.

Disclosures about notable relationships in financial statements other than consolidated financial statements

8.28 If the reporting entity has a notable relationship with another entity (see paragraph 8.29), it shall make the disclosures specified in paragraph 8.32, except that it may elect not to make those disclosures when:

(a) the notable relationship entity is incorporated in consolidated financial statements presented by the reporting entity for the period because:

(i) it is included as a subsidiary; or

(ii) it is an associate or a joint~~ly~~ ~~controlled~~ ~~entity~~ venture of a reporting entity with one or more subsidiaries and the reporting entity's investment in it is included in the consolidated financial statements; or

(b) the reporting entity has no subsidiaries and the notable relationship entity is an associate or a joint~~ly~~ ~~controlled entity~~ venture in which the reporting entity's investment is measured in separate financial statements at fair value (through profit or loss or in other comprehensive income) or by applying the equity method.

8.29 A notable relationship of the reporting entity with another entity ('notable relationship entity') exists when the reporting entity has at least significant influence over that entity (with or without holding an investment in the other entity's equity instruments, if any exist). This includes, but is not limited to, having control or joint control over that other entity. Significant influence is the power to participate in the financial and operating policy decisions of an entity, without having control or joint control over those policies.

8.30 If the reporting entity holds, directly or indirectly (eg through entities it controls), 20 per cent or more of the voting power of another entity, it is presumed to have significant influence over that entity, unless it can clearly be demonstrated that this is not the case based on other factors. Conversely, if the reporting entity holds, directly or indirectly, less than 20 per cent of the voting power of another entity, it is presumed not to have significant influence over that entity, unless significant influence can clearly be demonstrated based on other factors. In assessing a reporting entity's voting power over another entity, the existence and effect of potential voting rights currently exercisable or convertible (including potential voting rights held by other entities) are considered.

8.31 An entity applies judgement in assessing whether it has significant influence over another entity. The existence of a reporting entity's significant influence over another entity is usually evidenced by one or more of the following factors:

(a) representation on the board of directors or equivalent governing body of that other entity;

(b) participation in policy-making processes, including participation in decisions about distributions of any surpluses;

(c) material transactions between the two entities;

(d) interchange of managerial personnel between the two entities; and

(e) exchange of essential technical information between the two entities.

8.32 In respect of each notable relationship entity, an entity shall disclose:

(a) its name;

(b) a description of its relationship with the reporting entity;

(c) a clear and concise description of its primary purpose and an indication of the nature of its operations; and

(d) whether the notable relationship entity prepares audited or reviewed financial statements.

Separate financial statements

Presentation of separate financial statements

8.33 This Standard does not require presentation of separate financial statements for a parent entity or individually for its subsidiaries, unless a parent entity selects the option in paragraph 8.2(b).

8.34 Separate financial statements are:

(a) a second set of financial statements presented in addition to consolidated financial statements prepared by a parent; or

(b) financial statements prepared by a reporting entity that has one or more notable relationships and does not prepare consolidated financial statements.

Commented [A10]: Note to Board members
A Subcommittee member suggested drafting to specify the reporting 'has one or more notable relationships'.

Staff agree with the suggestion as per drafting in the underlined text.

Accounting policy election

8.35 When a reporting entity with one or more notable relationships prepares separate financial statements and describes them as conforming to this Standard, those statements shall adopt a policy of accounting for its investments in notable relationship entities in its separate financial statements either:

(a) at cost;

(b) at fair value through profit or loss, unless the entity makes an irrevocable election at initial recording of a particular investment to present changes in its fair value in other comprehensive income; or

(c) by applying the equity method following the procedures in paragraph 8.15.

The entity shall apply the same accounting policy for all investments in a single class (subsidiaries, associates or joint~~ly controlled entities~~ venture), but it can elect different policies for different classes. When an entity presents changes in the fair value of particular investments in other comprehensive income, those changes shall not subsequently be transferred to profit or loss.

Disclosures in separate financial statements

8.36 When an investor in a notable relationship entity prepares separate financial statements, those separate financial statements shall disclose, in addition to the disclosures in paragraph 8.32:

(a) that they are separate financial statements; and

(b) a description of the methods used to account for the investments in notable relationship entities.

Commented [A11]: Note to Board members
A Subcommittee member considered it would be helpful to include in paragraph 8.36 that in addition to the disclosures outlined in paragraph 8.36, reporting entities would also disclose what is specified in paragraph 8.32. This would ensure preparers would not misinterpret or overlook the disclosure requirement drafted in paragraph 8.2(b) earlier.

Section 9: Accounting Policies, Estimates and Errors [TBU]

Commented [A12]: **Note to Board members**
The Subcommittee member has reviewed the drafting for the hierarchy approach presented in Agenda Paper 4.11. Staff will include the remainder of the drafting for the Section on accounting policies, estimates and errors for the Subcommittee to review and include the drafting in the next iteration of the draft ED at a future Board meeting.

Scope of this section

9.1 xxx

Accounting policies

9.X2 If this Standard (encompassing the requirements referred to in paragraph 3(a)) does not specifically address a transaction, other event or condition to which paragraph 3(b) does not apply, an entity's management shall use its judgement in developing and applying an accounting policy that results in information that is:

(a) relevant to the information needs of users of financial statements; and

(b) reliable, in that the financial statements:

(i) represent faithfully the financial position, financial performance and cash flows of the entity;

(ii) reflect the economic substance of transactions, other events and conditions, and not merely their legal form;

(iii) are neutral, ie free from bias;

(iv) are prudent; and

(v) are complete in all material respects.

9.x3 In making the judgement described in paragraph 4, management shall refer to, and consider the applicability of, the following sources in descending order:

(a) the principles and other reporting requirements in this Standard dealing with similar and related issues; and

(b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Conceptual Framework, to the extent that they do not conflict with this Standard.

In making this judgement, management may also consider the requirements and guidance in Tier 2 reporting requirements dealing with similar and related issues.

9.x4 If an accounting policy permitted or required for a transaction, other event or condition by Tier 1 or Tier 2 reporting requirements is not included in this Standard, an entity applying Tier 3 reporting requirements may apply that accounting policy only where the transaction, other event or condition is not specifically addressed by this Standard. Consequently, an entity applying Tier 3 reporting requirements shall not apply Tier 1 or Tier 2 reporting requirements that conflict with the Tier 3 requirements.

Section 10: Financial Instruments

Question 5 to Board members

In Agenda Paper 4.17 at this meeting staff asked Subcommittee members:

a) whether they agree with the staff draft text for initial measurement of concessional loans, which would require the recognition of 'day one' gains or losses, is consistent with the Board's proposals in the DP that financial assets and financial liabilities are initially to be measured at their fair value with interest measured using the contractual rate of interest (refer to draft paragraphs 10.5 and 10.5A); and

b) their views regarding the three options for the measurement of concessional loans identified below? In particular, which of them would they prefer, and whether there are any other alternatives they suggest identifying for the Board's consideration.

Staff analysis and recommendation

The DP proposed that loans (and all other financial assets and financial liabilities) are initially measured at fair value, which typically would be the same as the transaction price (para. 5.83), and that loans are subsequently measured at historical cost (para. 5.86(b)). The DP also proposed that interest income and interest expense are measured using the contractual interest rate (para. 5.101(b)) and therefore that "referencing amortised cost is likely unnecessary" (para. 5.104). Therefore, under the Board's proposals in the DP, the cost of a loan for subsequent measurement would be the loan's original measurement minus payments of principal, plus/minus any outstanding/prepaid interest measured at the contractual rate. A benefit noted in the DP (paras 5.98–5.104) is that using the contractual interest rate avoids the need to perform discounted cash flow calculations to measure the loan. Where a loan is provided at the market rate of interest or a highly similar rate (i.e. the contractual rate equals or approximates the market rate), the same or highly similar amounts of interest will be recognised, but any adjustments affecting the effective interest rate can be disregarded.

An issue that staff consider should be clarified is how to apply the Board's proposals when the contractual rate of interest for a loan is materially less than the market rate of interest for that loan, as occurs with concessional loans, the granting of which is compatible with a NFP environment. Such circumstances would be the exceptions to the rule noted by the Board in the DP that initial fair value and transaction price typically are the same.

To illustrate the issue, assume a loan's principal is $500,000, lent at a contractual rate of interest of 5% per annum, with no coupon payments during the loan term and a sum of $650,000 to be repaid at the loan's maturity date (comprising principal of $500,000 and interest of $150,000). Assume also that the loan's fair value at initial recognition is $400,000, reflecting an 8% market rate of interest on the loan at initial recognition. In market terms, on initial recognition the discount from the total amount of loan payments is $250,000.

If the loan was measured on initial recognition at its fair value ($400,000), a 'day 1' gain of $100,000 would be recognised by the borrower and a 'day 1' loss would be recognised by the lender if it were applying the Tier 3 Standard (the remainder of this discussion focuses on the borrower). If interest were measured using the loan's contractual rate of 5%, as proposed for simplicity in the DP, the carrying amount of the loan immediately prior to its maturity (repayment) would be $400,000 + $150,000 = $550,000. That is, the carrying amount of the loan would be understated by $100,000. On settlement of the loan, cash would be credited by $650,000; the liability would be debited by $550,000 (its carrying amount) and a charge of $100,000 to profit or loss would be necessary. Usually, any 'day 1' gain on a loan is in effect offset over the term of the loan by accruing interest at the higher market rate of interest (compared with the contractual rate of interest), which would avoid this outcome.

Staff identified three main options for addressing this issue, which is to specify the following requirements for concessional loans only:

a) **Option A**: making an exception to the requirement to measure the loans initially at fair value and the consequent requirement to recognise a 'day 1' gain for the borrower. Under this exception, a concessional loan would initially be measured at its transaction price (the loan principal) and the accretion of interest at the contractual rate of interest (as proposed in the DP) would result in the loan's carrying amount immediately before maturity equalling its settlement amount. In the example above, that amount would be $500,000 + $150,000 = $650,000. *Staff consider Option A is simple to apply and easy to understand but lacks transparency regarding the nature of the loan and adopts a different principle for the initial measurement of concessional loans*;

b) **Option B**: requiring concessional loans to initially be measured in the same manner as any other financial instrument (i.e. at fair value, with a consequential 'day 1' gain for the borrower when the loan is concessional). As per Option A retain the requirement for accretion of interest at the contractual rate of interest. However, in addition, amortise the amount of the 'day 1' gain to expense over the term of the loan using a straight-line basis (with a corresponding credit to the loan's carrying amount), effectively as an adjustment to interest but without requiring application of the effective interest rate method. In the example above, the loan would initially be measured at $400,000, to which loan interest of $150,000 and the reversal (amortisation) of the 'day 1' gain of $100,000 would be added. This would result in the loan being measured at $650,000 immediately before maturity. *Staff consider Option B conforms to the Board's proposal in the DP regarding both the initial measurement of financial instruments and the interest rate to use to measure interest income and expenses, and provides greater transparency compared to Option A about the concessional nature of the loan. However, it may be difficult to understand and more complex than Option A and Option C*; or

c) **Option C**: repeating the requirement in Option B to initially measure the loan at its fair value (with a consequential 'day 1' gain for the borrower) and requiring the accretion of interest at the market rate of interest existing on 'day 1' of the loan, in effect reintroducing the use of the effective rate of interest (note that the market rate of interest used is that existing on 'day 1' of the loan only; there would be no remeasurement of the loan for changes in the market interest rate during the term of the loan, consistent with applying the cost approach to measure all loans). In the example above, the loan would initially be measured at $400,000, to which loan interest of $250,000 would be added, resulting in the loan being measured at $650,000 immediately before maturity. *Staff consider Option C to be similar to Option A in that it provides mutually consistent requirements and is easy to understand, but also provides greater transparency of the concessional nature of the loan compared to Option A.*

Staff had mixed views between Option B and C and noted that all three options have the disadvantage of requiring the definition and separate identification of concessional loans (through consideration of the relationship between the contractual and market rates of interest at initial recognition), contrary to the Board's general policy for the Tier 3 ED to avoid categorisation of transactions by nature for the purpose of specifying their recognition and measurement requirements. In the draft Tier 3 ED, staff included text reflecting the DP proposals literally (i.e. Option B), with alternative text (shaded) for Option A above (chosen for its simplicity of illustration).

<u>Feedback from Subcommittee members</u>

The Subcommittee members who commented had mixed views. One Subcommittee member preferred Option A as they consider it would be very difficult for NFP entities in this Tier to establish an equivalent rate (very few, if any, have borrowings from commercial institutions). In addition, imputing a market rate and interest different to the contractual rate will be confusing to users and preparers of Tier 3 financial statements.

Another Subcommittee member preferred Option B as it is consistent with the treatment of all other financial instruments and records the concessionary nature of the loan.

Do Board members prefer:

a) Option A making an exception to the requirement to measure the loans initially at fair value and the consequent requirement to recognise a 'day 1' gain for the borrower; or

b) Option B to requiring concessional loans to initially be measured in the same manner as any other financial instrument?

If Board members do not prefer Option A or Option B, do Board members prefer Option C or any other possible options?

Question 6 to Board members

In Agenda Paper 4.17 for this meeting, staff asked Subcommittee members whether they consider premium or discounts on originating loans would be sufficiently common and/or significant to warrant including draft paragraph 10.15 (shaded in grey) in the Tier 3 ED. The draft text of paragraph 10.15 reflects the Board's proposal in paragraph 5.101(c)) of the DP for when premiums and discounts on acquiring or originating loans are to be recognised in profit or loss. The Board's proposal is consistent with the corresponding Tier 2 requirement in AASB 9 paragraph B5.4.4 and the proposed requirement in the *IFRS for SMEs* Accounting Standard. Premiums and discounts referred to in the Board's proposal do not relate to differences between the transaction price and fair value of a financial instrument on initial measurement; for example, differences arising on concessional loans. A compromise between retaining the paragraph as drafted, or omitting it, would be to require amortisation of premiums and discounts on a straight-line basis only (bearing in mind the potentially complex assessments necessary under para. B5.4.4 of AASB 9).

Feedback from Subcommittee: the Subcommittee members who commented consider it not common for Tier-3-sized entities to warrant inclusion of the draft paragraph 10.15 regarding premium or discounts in the Tier 3 ED. As such, staff also recommend the Tier 3 ED exclude paragraph 10.15 to further reduce the length of the Tier 3 ED. Staff will amend the paragraph numbering accordingly subject to the Board's decision.

Do Board members agree to delete paragraph 10.15 which provides guidance on premium or discounts on originating loans? If not, what do Board members suggestion.

Question 7 to Board members

In Agenda Paper 4.6 at this meeting, staff asked Subcommittee members whether they agreed when a reliable measure of the fair value of an investment in an unlisted equity instrument is unavailable as at measurement date, the drafting should be based on an indication of whether close consistency with the generally applicable criteria for reliable measurement of fair value might be workable. Staff hypothetical drafting presented to the Subcommittee were:

a) *The market price of the equity instrument, or a similar equity instrument, close to the measurement date is not observable.* Staff consider it would seldom occur that a similar equity instrument with an observable price would be available to use as an input to a reliable measure of the fair value of the equity instrument being measured. As such, staff propose not to include this criterion in (a) as an indication for when a reliable measure of the fair value of an investment in an unlisted equity instrument is unavailable.

b) *The range of reasonable fair value measures is significant and the probabilities of the various measures cannot be reasonably assessed.* Staff consider it might not be proportionate to require Tier 3 NFP entities to assess the range of reasonable fair value measures and the probabilities of those measures, especially in view of the limited nature of the cash flow information that might be available for pricing an unquoted equity instrument and the complexities of valuing entities on the basis of cash flow modelling.

c) *Consider only the reasons such as (but not limited to) those listed in paragraph B5.2.6B* for when cost might not be a reliable measure of its fair value should be retained to draft the requirements in Tier 3.

As such, staff recommend the drafting only to retain criteria (c) and not criteria (a) and (b) as an indication for when a reliable measure of the fair value of an investment in an unlisted equity instrument is unavailable.

The Subcommittee members that commented agreed with the staff view.

A Subcommittee member noted that, for unlisted equity instruments, a reliable measure of fair value is not available for subsequent measurement if cost is not a reliable measure of fair value. If that is the case, its new cost becomes the carrying amount at the last date the asset was reliably measurable. They queried whether this presumes, at some point in time, cost was a reliable measure of fair value. They also consider whether further guidance may be needed to clarify how entities would subsequently measure their unlisted equity instruments when paragraphs 10.12(a) or (b) below suggest cost in instances listed would never be a reliable measure of fair value.

Staff analysis and recommendation

Staff note that paragraph 10.11 provides guidance when a reliable measurement of fair value of unlisted equity is not available such as the scenarios listed in paragraph 10.12, in which case the instrument's carrying amount measured at cost less accumulated impairment with the cost being the carrying amount of the asset at the last date its fair value was reliably measured until a reliable measure of fair value becomes available. This paragraph is present in the *IFRS for SMEs* Accounting Standard requirements but not contained in AASB 13. Staff note that the IASB's Basis for Conclusions on IFRS 13 notes that 'inability to measure reliably' exceptions to using fair value measurements are specified in individual Standards other than IFRS 13 (AASB 13); similarly, it states that: "… IFRS 13 specifies *how* an entity should measure fair value and disclose information about fair value measurements. It does not specify when an entity should measure an asset, a liability or its own equity instrument at fair value" (paragraph BC8). Also, paragraph 10.12(c) refers to paragraph 10.9 for instances when the cost is not reliable measure of fair value but other reliable fair value measurement might be available. If they are not available, then paragraph 10.11 applies. Therefore, staff consider that no further guidance is needed to clarify how entities would subsequently measure their unlisted equity instruments when cost is not a reliable measure of fair value.

Do Board members agree with staff recommendation not to develop any further guidance to clarify how entities would subsequently measure their unlisted equity instruments when cost is not a reliable measure of fair value?

If not, what do Board members suggest?

Scope of this section

10.1 A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

10.2 Section 10 applies to the recording, measurement and disclosure of financial assets and financial liabilities arising from basic financial instruments or financial instruments commonly held by Tier 3 not-for-profit private sector entities. Those financial instruments include:

(a) cash and cash equivalents;

(b) trade and other receivables ('debtors');

(c) security bonds (eg residential bonds);

(d) term deposits;

(e) government and listed corporate bonds;

(f) units held in managed investment schemes, unit trusts and similar investment vehicles;

(g) non-convertible ordinary and preference shares held in listed and non-listed entities, including shares redeemable for a known amount of cash or the cash equivalent of their share of the investee's net assets;

(h) trade and other payables ('creditors'); and

(i) loans (whether bearing interest at fixed or variable rates, interest-free or including terms that create leverage). Loans may be amounts borrowed or lent.

10.3 An entity applying this [draft] Standard shall apply the requirements of AASB 9 *Financial Instruments* to account for more complex financial instruments and financial instruments not commonly held by Tier 3 not-for-profit private sector entities, such as the following financial instruments:

(a) unlisted purchased debt instruments such as unlisted corporate bonds and convertible notes;

(b) acquired equity instruments other than non-convertible ordinary and preference shares;

(c) financial guarantee contracts;

(d) derivatives such as interest rate swaps and forward exchange contracts; and

(e) commitments to provide a loan at a below-market interest rate. However, loans provided at a below-market interest rate are within the scope of this [draft] Standard (see paragraph 10.2(i)).

However, the entity shall apply the disclosure requirements of AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* instead of the disclosure requirements of AASB 7.

Initial recording of financial assets and liabilities

10.4 An entity shall record a financial asset or a financial liability when and only when:

(a) cash is received; or

Commented [A13]: **Note to Board members:**
A Subcommittee member considered using the term 'or' indicates that paragraph 10.2 applies to two alternative types of financial instruments: 'basic financial instruments' and 'financial instruments commonly held by Tier 3 entities'. Based on Agenda Paper 5.3 at the November 2023 Board meeting, they consider it should read 'basic financial instruments that are commonly held by Tier 3 NFP public sector entities'.

Staff use of the term 'or' is intentional to represent two alternative types of financial instruments based on the Board's discussion at the November 2023 Board meeting where some Board members emphasised the need to distinguish the two alternative types of financial instruments which are based on findings from Research Report 19, feedback from stakeholders on the DP and NFP PAP members and analysis of requirements of other jurisdictions' pronouncements and frameworks. The November 2023 meeting minutes also reflect the Board's decision to reflect the two alternative types of financial instruments for inclusion in the scope of the Tier 3 ED. As such, staff do not suggest any amendments in paragraph 10.2.

Commented [A14]: **Note to Board members:**
Similar to the comment above for paragraph 10.2, a Subcommittee member considered using the term 'and' indicates applies to two alternative types of financial instruments: 'complex financial instruments' and 'financial instruments not commonly held by Tier 3 entities'.

As per the comment above, staff use of the term 'and' is intentional to represent two alternative types of financial instruments based on the Board's discussion at the November 2023 Board meeting and as reflected in the November 2023 meeting minutes. As such, staff do not suggest any amendments in paragraph 10.3.

(b) the entity becomes a party to the contractual provisions of the instrument. This occurs when:

(i) the entity creates an entitlement to receive cash from a debtor by transferring goods or services to the debtor;

(ii) the entity creates a loan receivable by lending money to a borrower;

(iii) the entity acquires (through purchase or donation) an investment that is a financial asset (eg an equity instrument);

(iv) the entity receives borrowed cash (including when it draws down cash under a bank overdraft facility); or

(v) the entity receives goods or services from a supplier and incurs a liability to pay for them.

Initial measurement

10.5 Subject to paragraph 10.5A, when a financial asset or financial liability is recorded initially, an entity shall measure it at its fair value (excluding transaction costs and fees incurred by the entity). Guidance on measuring the fair value of debtors is set out in Section 20 *Revenue*.

10.5A When a concessional loan is recorded initially, an entity shall measure it at its transaction price (ie the amount of cash lent). A concessional loan is a loan with a contractual interest rate significantly less than the market rate of interest for similar loans as at the date of initial recording, where that lower rate is contracted principally to enable the borrower to further its not-for-profit objectives.

Subsequent measurement

10.6 At the end of each reporting period, an entity shall measure financial assets and financial liabilities as follows, without any adjustment for transaction costs:

(a) financial assets acquired or originated by the entity to generate both income and a capital return for it (including all investments in equity instruments) shall be measured at fair value as at each measurement date, except when a reliable measure of the fair value of an investment in an unlisted equity instrument is unavailable as at a particular measurement date (see paragraphs 10.11 – 10.12). Changes in the fair value of such financial assets shall be presented in profit or loss, unless the entity elects to apply the treatment in (i):

(i) an entity may elect irrevocably, on initial recording of the first asset in a class of financial assets, to present changes in the fair value of that class in other comprehensive income;

(b) all other financial assets shall be measured at cost (determined in accordance with paragraphs 10.14 – 10.15) less any accumulated impairment losses (determined in accordance with paragraphs 10.17 – 10.21); and

(c) all financial liabilities shall be measured at cost (determined in accordance with paragraphs 10.14 – 10.15).

When an entity presents changes in the fair value of a class of financial assets in other comprehensive income, those changes shall not subsequently be transferred to profit or loss.

Hedge accounting

10.7 Hedge accounting, which causes the gain or loss on a designated hedging instrument and a related hedged item to be recorded concurrently in profit or loss, is not permitted for entities applying this [draft] Standard. This is the case regardless of whether the financial instrument(s) in the hedging relationship is (are) accounted for in accordance with the requirements of this [draft] Standard or of AASB 9.

Cost as estimated fair value of investments in equity instruments

10.8 In accordance with paragraphs 10.5 and 10.6(a) and subject to the exception in paragraph 10.11, all investments in equity instruments must be measured at fair value, using valuation techniques that maximise the use of relevant observable inputs. On subsequent measurement of an investment in unquoted equity instruments, in limited circumstances, cost (excluding transaction fees and other costs incurred by the entity) might be an appropriate estimate of the investment's fair value. That may be the case if insufficient more recent information is available to measure fair value, or if there is a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range.

10.9 Examples of indicators that cost might not be a reliable measure of fair value include:

(a) the transaction to acquire the share investment was between related parties. However, the price in a related party transaction might be used as an input to a fair value measurement if the transaction was conducted on commercial terms;

(b) the acquisition transaction occurred under duress or the seller was forced to accept the sales price in the transaction (eg the seller was experiencing financial difficulty); and

(c) any significant unexpected changes or other developments since the investment was acquired, whether favourable or unfavourable, in:

(iv) the investee's operating performance, strategy or economic environment (including its outputs or market demand for its outputs); or

(v) valuations implied by the overall market (eg due to changes in market interest rates).

10.10 Cost is never the best estimate of fair value for investments in quoted equity instruments.

10.11 A reliable measure of the fair value of an equity instrument will always be available for a quoted equity instrument. If a reliable measure of fair value of an investment in an unlisted equity instrument is unavailable as at the measurement date, its carrying amount at the last date the asset was reliably measurable becomes its new cost. An entity shall measure the asset at this cost amount less any accumulated impairment losses until a reliable measure of fair value becomes available.

10.12 For the purposes of paragraph 10.11, a reliable measure of the fair value of an investment in an unlisted equity instrument is unavailable as at the measurement date if:

(a) the market price of the equity instrument, or a similar equity instrument, close to the measurement date is not observable;

(b) the range of reasonable fair value measures is significant and the probabilities of the various measures cannot be reasonably assessed; and

(c) for reasons such as ~~(but not limited to)~~ those listed in paragraph 10.9, the cost of the equity instrument is not a reliable measure of its fair value.

Commented [A15]: Note to Board members
A Subcommittee member provided comments that this statement in parentheses is not necessary, given the list in para X.2 is not exhaustive.

Staff agree to remove these terms to further streamline the sentence.

Dividend income

10.13 Dividends are recorded as amounts receivable and income in profit or loss only when:

(a) an investee of the entity has declared a dividend payable to the entity for a determinable amount; and

(b) publicly available information does not indicate the investee is experiencing financial difficulties that might jeopardise payment of the dividend to the entity.

Cost of a financial asset or financial liability

10.14 The cost of a financial asset or financial liability at each reporting date (before any reduction, directly or through the use of an allowance account, for impairment of a financial asset in accordance with paragraphs 10.17 – 10.21) is the net of the following amounts:

(a) the amount at which the financial asset or financial liability is measured initial recording;

(b) minus any repayments of the principal; and

(c) plus or minus any prepayments or overdue payments of contractual interest.

10.15 The cost of a loan includes any premiums or discounts on acquisition of the asset or incurrence of the liability. Those premiums or discounts shall be amortised over the shorter of:

(a) the expected life of the instrument; and

(b) any other period to which the premiums or discounts relate. This will be the case when the variable to which the premiums or discounts relate is repriced to market rates before the expected maturity of the instrument.

The premiums or discounts shall be amortised using a straight-line basis unless another systematic basis reflects more faithfully the time pattern of their reduction.

Interest expense/income

10.16 The interest expense (income) in a period equals the carrying amount of the financial liability (asset) at the beginning of a period multiplied by the contractual interest rate for the period.

Impairment of debtors and financial assets measured at cost

Recording

10.17 At the end of each reporting period, an entity shall assess whether there is objective evidence of impairment of any financial asset, or group of financial assets, in the following categories:

(a) debtors within the scope of Section 20 on *Revenue*; and

(b) any financial assets measured at cost in accordance with paragraph~~s~~ 10.6(b).

If there is objective evidence of impairment, the entity shall record an impairment loss in profit or loss immediately.

10.18 Objective evidence that a financial asset or group of assets is impaired includes observable data that come to the attention of the holder of the asset about the following loss events:

(a) significant financial difficulty of the issuer or obligor;

(b) a breach of contract, such as a default or delinquency in interest or principal payments;

(c) the creditor, for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the creditor would not otherwise consider;

(d) it has become probable that the debtor will enter bankruptcy or other financial reorganisation; or

(e) observable data indicating that there has been a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recording of those assets, even though the decrease cannot yet be identified with the individual financial assets in the group, such as adverse national or local economic conditions or adverse changes in industry conditions.

10.19 Other factors may also be evidence of impairment, including significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the debtor or issuer operates.

10.20 An entity uses judgement to determine whether to assess financial assets for impairment either individually or grouped on the basis of similar credit risk characteristics.

Measurement

10.21 An entity shall measure an impairment loss for a financial asset measured at cost as the difference between the asset's carrying amount and the present value of estimated cash flows discounted at the asset's contractual interest rate.

Ceasing to record a financial asset

10.22 An entity shall cease recording a financial asset only when either:

(a) the contractual rights to the cash flows from the financial asset expire or are settled; or

(b) the entity otherwise loses control of the financial asset.

Ceasing to record a financial liability

10.23 An entity shall cease to record a financial liability (or a part of a financial liability) only when it is extinguished — ie when the obligation specified in the contract is discharged, is cancelled or expires.

10.24 A modification of the terms of a financial liability or an exchange of a debt instrument~~s~~ for a different debt instrument shall be accounted for as an extinguishment of the original financial liability.

Disclosures

Statement of financial position—categories of financial assets and financial liabilities

10.25 An entity shall disclose the nature and carrying amount~~s~~ of each of the following categories of financial assets and financial liabilities at the reporting date, in total, either in the statement of financial position or in the notes:

(a) financial assets measured at fair value through profit or loss (paragraph 10.6(a));

(b) financial assets measured at fair value through other comprehensive income (paragraphs 10.6(a)(i) and (ii));

(c) financial assets measured at cost less any accumulated impairment losses (paragraph 10.6(b)); and

(d) financial liabilities measured at cost (paragraph 10.6(c)).

10.26 In respect of individually significant loans payable or receivable, an entity shall disclose additional information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance. For example, for individually significant long-term debt, such information would normally include the terms and conditions of the debt instrument (such as interest rate, maturity and, for debt payable, restrictions that the debt instrument imposes on the entity).

10.27 For all financial assets and financial liabilities measured at fair value, the entity shall disclose separately the fair value amounts that are, and are not, based on a quoted price in an active market.

Collateral

10.28 When an entity has pledged financial assets as collateral for liabilities or contingent liabilities, it shall disclose the following:

(a) the carrying amount of the financial assets pledged as collateral;

(b) the nature and amount of the liabilities for which the financial assets have been pledged; and

(c) the terms and conditions relating to its pledge.

Defaults and breaches on loans payable

10.29 For loans payable recorded at the reporting date for which a breach of terms or a default of principal, interest, sinking fund or redemption terms has not been remedied by the reporting date, an entity shall disclose the following:

(a) details of that breach or default;

(b) the carrying amount of the related loans payable at the reporting date; and

(c) whether the breach or default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorised for issue.

Items of income and expense, and gains or losses

10.30 An entity shall disclose the following items of income and expense, and gains or losses:

(a) income, expense, gains or losses, including changes in fair value, recorded on:

(i) financial assets measured at fair value through profit or loss;

(ii) financial assets measured at fair value through other comprehensive income;

(iii) financial assets measured at cost less any accumulated impairment losses; and

(iv) financial liabilities measured at cost;

(b) total interest income and total interest expense (calculated using the contractual interest rate) for financial assets or financial liabilities that are not measured at fair value through profit or loss; and

(c) the amount of any impairment loss for each class of financial asset.

Section 11: Fair Value Measurement

Note to Board members

In Agenda Paper 4.12 for this meeting (and previously presented to the Board in Agenda Paper 10.2.1 at the June 2023 Board meeting) staff asked Subcommittee members whether they agreed with:

(a) the NFP clarification and simplification of guidance regarding an asset's 'financially feasible use' in identifying its highest and best use (refer to draft paragraph 11.16(c) in this draft ED). As drafted in paragraphs BC15–BC16, staff consider an asset's "financially feasible use" presents a challenge for application and understandability in an NFP environment because of its emphasis solely on a market return on investment. When the Board developed AASB 2022-10 to provide guidance for public sector NFP entities on fair value measurement, it decided a case had not been made to modify AASB 13 for application by private sector NFP entities (largely because the Board did not receive requests for such guidance). However, if the Board includes guidance on 'highest and best use' in its Tier 3 Standard, the counter-intuitive reference to 'market return on investment' in respect of an asset's 'financially feasible use' might be quite confusing for Tier 3 entities, which would tend to be less well-resourced than larger NFP entities to interpret such guidance or obtain advice about it. Therefore, staff think consideration should be given to modifying the guidance to by referring to 'financially feasible use' as 'financial sense' in the Tier 3 wording, to use plainer English instead.

Feedback from Subcommittee: The Subcommittee members that commented were agreeable with the simplification. However, a Subcommittee member queried what if the assets were donated.

Staff consider paragraph 11.6 provides guidance more generally regarding highest and best use for non-financial assets regardless of how the assets were acquired. Fair value assumes a hypothetical market transaction, therefore the notion of whether assets were donated is irrelevant. As such, staff do not consider there is a need to clarify that paragraph 11.6 would also apply for donated assets. If the Board considers the need to clarify, staff would suggest adding "if not already held" to reinforce this point. Staff is also aware that the INPAG ED may propose some application guidance on the fair value of donated assets, but staff do not consider it necessary to include further guidance given there is already other guidance on donated non-financial assets within Section 15 Property, plant and equipment (subject to the Board's discussion in Agenda Paper 4.2 at this meeting).

(b) adding guidance to provide a practical expedient limiting the circumstances in which a Tier 3 NFP entity would need to consider whether an asset's highest and best use might differ from its existing use. As per draft paragraph BC14, the staff suggested amendments to *IFRS for SMEs* Accounting Standard requirements paragraph 12.12 are a condensed version of the practical expedient provided in AASB 2022-10 (paragraphs Aus29.1 and Aus29.2) for public sector NFPs. Staff consider that this practical expedient should also be available to provide further simplification for Tier 3 NFPs.

Feedback from Subcommittee: The Subcommittee members who commented were agreeable with the simplification. However, one member noted the use of the indicators of impairment beyond their original intention by the Board may pose a risk of departing from the Board's proposals to conform with Tier 2 requirements. That is, the staff suggested including practical expedient in paragraph 11.7 regarding when an entity needs to consider the possibility that no future economic benefits are expected from the use or disposal of an asset to parallel the Boards' analogous proposal in the DP that consideration of potential impairment needs to be considered only upon the occurrence of specified trigger events. While the Subcommittee member noted the use of the indicators of impairment beyond their original intention by the Board could pose a risk of departing from the Board's proposal to conform with Tier 2, however, they noted the risk is not significant.

Question 8 to Board members

In Agenda Paper 4.12, staff asked Subcommittee members whether they agreed with the staff's approach to exclude the fair value hierarchy set out in AASB 13 and *IFRS for SMEs* Accounting Standard requirements. Staff have previously presented this approach in Agenda Paper 10.2.1 at the June 2023 Board meeting to solicit preliminary feedback from Board members. This is despite paragraph 5.117 of the DP stating that: "the Board considers it important for fair value measurement in Tier 3 financial statements to be determined in a manner consistent with the framework set out in AASB 13, including by reference to a specified hierarchy …". However, the *IFRS for SMEs* Accounting Standard requirements paragraph 12.14 (which staff propose including in the Tier 3 ED) requires fair value estimates to maximise the use of relevant observable inputs and minimise the use of unobservable inputs; the fair value hierarchy classifies the outcomes of applying that principle and requires differentiated disclosures for different levels of the fair value hierarchy (the IASB's Basis for Conclusions on IFRS 13, paragraphs BC166–BC221, does not identify any other role for the fair value hierarchy). In addition, the Basis for Conclusions states that "IFRS 13 does not contain a hierarchy of valuation techniques …" (paragraph BC142).

As such, staff consider that a section on the fair value hierarchy would only be necessary if it was decided that disclosure should be made of the levels of the fair value hierarchy at which the fair values of assets are measured. Under the Board's disclosure approach for Tier 3 NFP entities, drafting the proposed disclosures about fair value measurements for Tier 3 NFP entities should start with those in AASB 1060, with consideration of further simplification. However, AASB 1060 includes no disclosure requirements for fair value measurements. Therefore, under the Board's proposals in the DP, disclosures based on the fair value hierarchy would not be included in the Tier 3 ED. In addition, staff observe that applying the fair value hierarchy might involve significant judgements and be costly for Tier 3 NFP entities to apply, without significant apparent benefits to users of financial statements of Tier 3 NFP entities, and therefore suggest that including the fair value hierarchy would be unlikely to be proportionate. Consequently, staff consider there is a case for concluding that it would be compatible with the Board's preliminary decisions (i.e. subject to considering stakeholders' feedback) and therefore, staff recommend excluding any guidance on the fair value hierarchy from the drafting of the Tier 3 ED.

Feedback from Subcommittee members: The Subcommittee members who commented agreed with the approach to exclude the fair value hierarchy from the Tier 3 ED.

Do Board members agree with staff recommendation to exclude the fair value hierarchy from the Tier 3 ED? If not, what do the Board suggest?

Scope of this section

11.1 This section applies when another section requires or permits fair value measurements or disclosures about fair value measurements.

Measurement

11.2 The objective of a fair value measurement is to estimate the price at which an orderly transaction (not a forced transaction) to sell an asset or to transfer a liability would take place between market participants at the measurement date under current market conditions (that is, an exit price at the measurement date from the perspective of a market participant that holds the asset or owes the liability).

11.3 Fair value is a market-based measurement, not an entity-specific measurement. Therefore, it is measured using the assumptions that market participants would use when pricing the asset or liability at the measurement date, taking into account the characteristics of the asset or liability that market participants would take into account. Such characteristics include, for example:

(a) the condition and existing location of the asset; and

(b) legal restrictions, if any, on the sale or use of the asset (see paragraph 12.6(b)).

11.4 The market price used to measure the fair value of the asset or liability shall not be adjusted for transaction costs (ie, costs directly attributable to selling an asset or transferring a liability, such as costs of marketing an asset for sale). Transaction costs are not a characteristic of an asset or a liability; rather, they are specific to a transaction.

11.5 If location is a characteristic of the asset, the asset's market price shall be adjusted for transport costs.

Highest and best use for non-financial assets

11.6 A fair value measurement of a non-financial asset (such as an item of property, plant and equipment) assumes a market participant would use the asset for its highest and best use, which takes into account:

(a) the asset's physical characteristics (for example, the existing location (either existing or new) or size of a property);

(b) any legal restrictions affecting the market participant's use of the asset (for example, the zoning regulations applicable to a property); and

(c) whether the use makes financial sense, i.e. it would generate at least a market rate of return on investing in the asset or sufficient goods/services to beneficiaries to justify buying the asset.

11.7 An entity's current use of a non-financial asset is presumed to be its highest and best use unless market or other factors suggest that it is highly probable that a different use by market participants would maximise the value of the asset. In general, this exception would occur only when it is highly probable that, within one year of the asset's measurement date, the asset will either be sold to a buyer who would use the asset for a different use or be redeployed by the entity.

Valuation techniques

11.8 When a price for an identical asset or liability is not observable, an entity measures fair value using another valuation technique. The entity shall use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

11.9 Three widely used valuation techniques are the market approach, the cost approach and the income approach. An entity shall use valuation techniques consistent with one or more of these approaches to measure fair value:

(a) the market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. This would often be the case for financial assets and non-financial assets such as land, non-specialised buildings and non-specialised motor vehicles.

(b) the cost approach reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost: see paragraph 11.10).

(c) the income approach discounts future cash flows or income and expense items to their present value.

Commented [A16]: Note to Board members
A Subcommittee member suggested to include the definition of exit price in the glossary.

Staff agree and have now included the definition of exit price as defined in Tier 1/Tier 2 requirements in the draft glossary.

Commented [A17]: Note to Board members
A Subcommittee member commented that it may not be clear whether location in subsequent paragraph (e.g. 11.6(a)) refers to existing location or otherwise.

Staff agree with the Subcommittee member's comment and for consistency, to include 'existing' when referring to location in paragraph 11.6 as per underlined text below.

11.10 From the perspective of a market participant seller, the price that would be received for the asset is based on the cost to a market participant buyer to acquire or construct a substitute asset with the same age, technology, service capacity and condition as that of the asset held. That is because a market participant buyer would not pay more for an asset than the cost of replacing its service capacity. One reason the current replacement cost method may be used is that the asset is specialised and without readily observable market evidence.

Reliable measure of fair value

11.11 The fair value of an asset is reliably measurable if:

(a) a market price of an identical or similar asset is observable close to the measurement date; or

(b) either:

(i) the variability in the range of reasonable fair value measures is insignificant for that asset; or

(ii) the probabilities of the various measures within the range can be reasonably assessed and used in estimating fair value.

11.12 For assets for which a market price of an identical or similar asset is not observable, there are many situations in which the variability in the range of reasonable fair value measures is likely to be insignificant. Normally it is possible to estimate the fair value of an asset that an entity has acquired from an outside party. However, if the range of reasonable fair value measures is significant and the probabilities of the various measures cannot be reasonably assessed, the entity is precluded from measuring the asset at fair value.

11.13 If a reliable measure of fair value is no longer available for an asset measured at fair value ~~(or is not available without undue cost or effort when such an exemption is provided~~ (for example, see paragraphs 10.6(a) and 10.11), its carrying amount at the last date the asset was reliably measurable becomes its new cost. An entity shall measure the asset at this cost amount less any accumulated depreciation and any accumulated impairment losses until a reliable measure of fair value becomes available ~~(or becomes available without undue cost or effort when such an exemption is provided)~~.

Commented [A18]: <u>Note to Board members</u>
The text in brackets was carried over in the drafting stage from the *IFRS for SMEs* Accounting Standard requirements which is now removed to align with the Board's decision not to include the notion of undue cost or effort in the Tier 3 ED.

Section 12: Inventories

<u>Note to Board members</u>

In Agenda Paper 4.8, staff asked Subcommittee members whether they agreed with the staff's suggestion to retain (but modify to a limited extent) the guidance in the *IFRS for SMEs* Accounting Standard requirements on the techniques and formulae for measuring the cost of particular items of inventory and to include a specific matter for comment on whether the guidance is considered useful and proportionate. The Subcommittee members that commented agree with retaining the guidance and the approach to seek feedback from stakeholders as a specific matter for comment.

<u>Question 9 to Board Members</u>

Subcommittee members were asked whether they agreed with staff's suggestion to change from mandatory to optional, the allocation of production overheads to inventories' costs of conversion with the election required to be applied to all inventories produced by the entity.

<u>Staff analysis and recommendation</u>

The *IFRS for SMEs* Accounting Standard requirements paragraphs 13.8–13.9 require the allocation of production overheads to inventories' costs of conversion. As presented in staff comments against paragraphs 13.8 and 13.9 in Table 2 in Agenda Paper 4.8 for this meeting, staff consider that requiring capitalisation of production overheads would not be proportionate for Tier 3 NFP entities and consider many of the Tier 3 entities that hold inventories would not produce their own finished goods (based on Research Report 19 that identified Tier 3 entities typically purchase finished goods). However, staff consider that any election whether to capitalise production overheads should be required to be applied consistently to all inventories produced by the entity, to maximise intra-entity consistency in this regard. Staff also suggest omitting other guidance on cost of conversion in paragraph 13.8, to achieve further simplification of the Tier 3 guidance. Staff think this issue is subordinate to whether to mandate a particular treatment of production overheads.

The Subcommittee members who commented agreed with the staff's suggestions.

Do Board members agree with staff recommendation to permit but not require the allocation of production overheads to inventories' cost of conversion with the election required to be applied to all inventories produced by the entity as drafted in paragraph 12.9? If not, what do Board members suggest?

Question 10 to Board members

A Subcommittee member considered paragraph 12.11 should be deleted to align with other drafted sections for PPE, and employee benefits to not require determining financing component based on cost/benefit consideration and complexity for Tier 3 entities.

Staff analysis and recommendation

As noted in Agenda Paper 4.8 at this meeting, staff included this paragraph having considered the wording in *IFRS for SMEs* Accounting Standard requirements paragraph 13.11 is consistent with AASB 116 and AASB 102 where the Board decided the requirements for PPE and inventories to be consistent with Tier 2 except for simplifying language. However, having considered the cost and complexity that may be required by smaller NFP entities to determine the financing component, staff considered further simplification would be warranted to not require determining the financing component as suggested by the Subcommittee member. As such, staff recommend that draft paragraph 12.11 be removed.

Do Board members agree with the staff recommendation to remove paragraph 12.11? If not, what do Board members suggest?

Scope of this section

12.1 This section sets out the principles for recording, measuring and disclosing all inventories. Inventories are assets:

(a) in the form of materials or supplies to be consumed in producing goods or rendering services;

(b) held for sale or distribution in the ordinary course of operations; or

(c) in the process of production for such sale or distribution.

12.2 An entity's inventories might include food, clothing or goods held for distribution, stocks held in charity shops, information brochures, goods purchased for resale, consumable stores, maintenance materials, spare parts for plant and equipment, and work-in-progress, such as education/training course materials under development.

Recording inventories

12.3 Inventories are recorded as an asset from when they are purchased by, or donated to, the entity.

Measurement of inventories

12.4 Subject to paragraphs 12.5 and 12.8, an entity shall measure inventories at ~~the lower of~~ cost ~~and estimated selling price less costs to complete and sell~~. However, ~~An entity shall consider whether the estimated selling price less costs to complete and sell of inventory (or inventories) is less than its (their) cost when, and~~ if, and only if ~~when~~, one or more of the circumstances in paragraph 23.3 of Section 23 *Impairment of Assets* arises, an entity shall measure inventories at the lower of cost and estimated selling price less costs to complete and sell of inventory (or inventories).

12.5 An entity shall measure inventories held for distribution (ie inventories held for distribution for no, or nominal, consideration in return) at cost~~, adjusted for any identified loss of service potential. For the purposes of this [draft] Standard~~. However, if, and only if one or more of the circumstances in paragraph 23.3 of Section 23 *Impairment of Assets* arises, an entity shall consider~~:~~

~~(a) 'inventories held for distribution' are inventories held for distribution for no, or nominal, consideration in return; and~~

~~(b)~~ ~~an entity shall consider~~ whether a loss of service potential of inventory (or inventories) held for distribution has occurred ~~when, and only when, one or more of the circumstances in paragraph 23.3 of Section XX *Impairment of Assets* arises~~.

12.6 If one or more of the circumstances in paragraph 23.3 of Section 23 *Impairment of Assets* arises in respect of inventory (or inventories) held for distribution, an entity would need to use judgment in determining the factors relevant to the circumstances in assessing whether there is a loss of service potential of those inventories. For many inventories held for distribution, a loss of service potential would be identified and measured based on the existence of a current replacement cost lower than the original acquisition cost or other subsequent carrying amount. For other inventories held for distribution, a loss of service potential might be identified and measured based on obsolescence (whether physical or economic). Typically, such obsolescence would also result in a reduction in the inventories' current replacement cost. In accordance with paragraph 23.5 of Section 23 *Impairment of Assets*, the recoverable amount of inventories no longer useful for distribution is measured by reference to the more easily determined of those inventories' cost or current replacement cost.

Commented [A19]: Note to Board members
A Subcommittee member suggested further simplification as follows: *"Subject to paragraphs 12.5 and 12.8, an entity shall measure inventories at cost. However, if, and only if, one or more of the circumstances in paragraph 23.3 of Section 23 Impairment of Assets arises, an entity shall measure inventories at the lower of cost and estimated selling price less costs to complete and sell."*

Staff agree with the revised wording and have amended the drafting accordingly.

Commented [A20]: Note to Board members
A Subcommittee member suggested a similar further simplification in paragraph 12.4 to paragraph 12.5. That is, to begin with the general simple principle (i.e., measure inventory at cost) and then specify that if, and only if, certain circumstances exist (e.g.: indicators of impairment arise) then depart from the general principle (i.e., measure inventory at cost less identified loss of service potential).

Staff agree with the suggestion and have amended the drafting accordingly.

12.7 Different bases for determining whether there has been a loss of service potential and the measurement of that loss may apply to different inventories held for distribution within the same entity.

12.8 For the purposes of applying paragraphs 12.4 and 12.5, if an item of inventory was donated (which might be nil, a nominal amount or another significantly discounted amount) to the entity, that entity may elect to initially measure the cost of that item either at:

(a) its cost to the entity ~~(which might be either nil, a nominal amount or another significantly discounted amount)~~; or

(b) its current replacement cost as at the date of donation, measured in accordance with paragraphs 11.9(b) and 11.10.

When 12.8(b) is selected and the cost of a donated item of inventory is initially measured at its current replacement cost, the resulting increase in net assets is recorded as donation income in the reporting period in which the donated asset is received.

Commented [A21]: Note to Board members
A Subcommittee member queried if a similar requirement to record donation income applies in paragraph 12.8(a) where donated assets were measured at cost.

Staff note paragraph 12.8(a) would not result in donation income that would arise from the difference between the cost of a donated item and its current replacement cost as per paragraph 12.8(b). As such, staff did not make changes to the drafting here. However, staff consider it would be clearer to state earlier in the paragraph that donated inventories cover scenarios including nil, nominal or another significantly discounted amount. Therefore, staff have revised the drafting accordingly.

Cost of inventories

12.9 An entity shall include in the cost of inventories all costs incurred in bringing the inventories to their present location and condition, including costs of purchase and, for inventories produced by the entity, costs of conversion (i.e. costs of converting raw materials, labour and other inputs such as overheads into finished goods). An entity may include in costs of conversion a systematic allocation of production overhead costs incurred in the conversion process, such as a share of depreciation and maintenance costs of buildings and equipment used to produce the inventories. This election shall be applied consistently to all inventories produced by the entity.

Commented [A22]: Note to Board members
A Subcommittee member suggested explicitly stating what "other inputs" might include to provide some clarity for readers.

Staff agreed with the feedback. Paragraph 12 of AASB 102 contains guidance on cost of conversion to include cost directly related to units of production, such as direct labour, or systematic allocation of fixed and variable production overheads. As such, staff provided an example that other inputs 'such as overheads' as per underlined text in the drafting.

Cost of purchase

12.10 The costs of purchase of inventories comprise the purchase price, import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities) and transport, handling and other costs directly attributable to the acquisition of finished goods, materials and services. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase.

~~12.11 An entity might purchase inventories on deferred settlement terms. In some cases, the arrangement effectively contains an unstated financing element, for example, a difference between the purchase price for normal credit terms and the deferred settlement amount. In these cases, the difference is recorded as interest expense over the period of the financing and is not added to the cost of the inventories.~~

Costs excluded from inventories

12.12 Examples of costs excluded from the cost of inventories and recorded as expenses in the period in which they are incurred are:

(a) abnormal amounts of wasted materials, labour or other production costs;

(b) storage costs, unless those costs are necessary during the production process before a further production stage;

(c) administrative overheads that do not contribute to bringing inventories to their present location and condition. ~~(~~However, if an entity elects under paragraph 12.9 to exclude production overhead costs from the costs of conversion of inventories, all administrative overheads would be excluded from the cost of inventories); and

(d) selling costs.

Commented [A23]: Note to Board members
A Subcommittee member suggested for drafting to include the word "however" as per underlined text.

Staff agreed and have included as per suggestion and considered further changes to shorten the sentences for easier reading.

Costs of inventories of a service provider

12.13 To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel and (where the entity elects to include production overhead costs in the costs of inventories) attributable overheads. Labour and other costs relating to sales and general administrative personnel are not included but are recorded as expenses in the period in which they are incurred. The cost of inventories of a service provider does not include profit margins or non-attributable overheads that are often factored into prices charged by service providers.

Costs of agricultural produce harvested from biological assets

12.14 Inventories comprising agricultural produce that an entity has harvested from its biological assets shall initially be measured at their fair value less estimated costs to sell at the point of harvest. This becomes the cost of the inventories at that date for application of this section.

Techniques for measuring cost, such as standard costing, retail method, most recent purchase price and specific identification

12.15 An entity may use techniques such as the standard cost method, the retail method or most recent purchase price for measuring the cost of inventories if the result approximates cost. Standard costs take into account normal levels of materials and supplies, labour, efficiency and capacity utilisation. They are regularly reviewed and, if necessary, revised in the light of current conditions. The retail method measures cost by reducing the sales value of the inventory by the appropriate gross margin percentage. Where feasible (e.g. for different items that ordinarily are not interchangeable) an entity may measure the cost of inventories by using specific identification of their individual costs.

Cost formulae

12.16 An entity shall measure the cost of inventories, other than those measured using specific identification of their individual costs, by using the first-in, first-out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulae may be justified. The last-in, first-out (LIFO) method is not permitted by this [draft] Standard.

Recording as an expense

12.17 When inventories are sold, the entity shall record the carrying amount of those inventories as an expense in the period in which the related sales revenue is recorded.

12.18 When inventories held for distribution are distributed, the carrying amount of those inventories shall be recorded as an expense. The amount of any write-down of inventories for loss of service potential and all losses of inventories shall be recorded as an expense in the period in which the write-down or loss occurs.

12.19 If an item of inventory was donated without charge to the entity, and the entity elected under paragraph 12.8 to initially measure the cost of that item at the cost to the entity (nil), no expense is recorded on sale or distribution of the item.

Disclosures

12.20 An entity shall disclose the following:

(a) material accounting policy information about the measurement of inventories, including the cost formulae used;

(b) the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity;

(c) the amount of inventories recorded as an expense during the period;

(d) the net amount of impairment losses for inventories recorded ~~or reversed~~ in profit or loss in accordance with Section 23 *Impairment of Assets* during the period; and

(a) the total carrying amount of inventories pledged as security for loans (including the nature and amount of loans that are secured).

12.21 An entity shall also disclose the basis or bases on which any loss of service potential of inventories held for distribution is assessed.

Commented [A24]: Note to Board members
A Subcommittee member considered reference to reversal of impairment losses should be deleted for disclosures in light of the drafting in paragraph 12.18 where, as per Agenda Paper 4.8 for this meeting, staff suggested omitting references to reversal of impairment losses consistent with omitting from Section 23 *Impairment of Assets* the guidance in the *IFRS for SMEs* Accounting Standard requirements on reversal of impairment losses.

As noted in Agenda Paper 4.8, in staff drafting analysis, while staff suggested omitting in paragraph 12.18 the recognition of inventory write-down, staff consider that the amount required to be disclosed in paragraph 12.20(d) should reflect (without separate identification) the amount of any reversals of impairment losses for inventories recorded during the period. However, considering Subcommittee feedback, staff agree with deleting reference to reversal of impairment losses in the disclosure requirements to keep with the consistency of recognition requirements otherwise it may cause confusion to readers.

Section 13: Investments in Associates and Joint Arrangements

Note to Board members
In Agenda Paper 4.15 for this meeting, staff asked Subcommittee members whether they agreed with:

(a) Using the *IFRS for SMEs* Accounting Standard requirements as the starting point for drafting the text of the Tier 3 ED regarding investments in associates and joint arrangements before considering further simplification. Staff suggested the *IFRS for SMEs* Accounting Standard requirements as starting point because it proposes the similar measurement options as agreed by the Board in Agenda Paper 5.2 at the November 2023 Board meeting. Staff also suggested merging the *IFRS for SMEs* Accounting Standard requirements on Investment in Associates (section 14) and Joint Arrangements (section 15) to economise text because of the duplication in various areas including the accounting policy election for measuring investments in associate and interest in jointly controlled entities, the measurement models and disclosure requirements. However, merging those sections may have potential disadvantages such as additional complexity in each paragraph which would refer to investments in both associates and jointly controlled entities. Tier 3 readers would also need to consider a longer section, however staff have used subheadings to divide the topics.

Feedback from Subcommittee: The members that commented agreed with the staff suggestion above.

(b) The staff suggestion to conform to the tripartite classification scheme for joint arrangements in the *IFRS for SMEs* Accounting Standard requirements (i.e. classifying joint arrangements into jointly controlled operations, jointly controlled assets and jointly controlled entities) rather than the dual classification scheme (as either a joint operation or a joint venture) in the Tier 1/Tier 2 requirements in AASB 11 *Joint Arrangements* and AASB 128 *Investments in Associates and Joint Ventures.* Staff suggested the tripartite classification scheme as a form of further simplification because there may be significant judgement required to classifying joint arrangements based on paragraph BC121 of the *IFRS for SMEs* Accounting Standard requirements. Staff also considered the tripartite classification scheme should have little effect on the identification and treatment of investment in joint arrangements because 'jointly controlled entity' has a similar role or definition to 'joint venture' in Tier 1/Tier 2 requirements.

Feedback from Subcommittee: The members that commented did not agree with the staff suggestion to require the tripartite classification scheme in the *IFRS for SMEs* Accounting Standard requirements and prefer the dual classification to avoid confusion in application and for consistency with the Tier 1/Tier 2 requirements. One member also considered while dual classification requires judgement, the IASB evidence suggests entities are able to apply that judgement to faithfully represent their interest. Staff have amended the section to address the feedback from the Subcommittee members and made respective changes to reflect IFRS 11 classification of joint arrangements, that is, joint operations and joint ventures as reflected in underlined text and strikethrough in this section as well as Section 8 *Consolidated and Separate Financial Statements* and Section 23 *Impairment of Assets*. Staff did not incorporate all of the Application Guidance in Appendix B to IFRS 11 in paragraphs B12–B33 due to its extent, however, retained guidance in paragraph 13.8 and incorporated guidance in paragraphs B16 and B19– B21 in IFRS 11.

(c) The staff suggestion to omit from the Tier 3 ED the *IFRS for SMEs* Accounting Standard requirements that if the entity did not select the fair value model to measure its investments in associates and/or jointly controlled entities, those investments with published price quotations must be measured using the fair value model. The staff suggestion is based on the fact that such a requirement does not apply to Tier 1/Tier 2 NFP entities, hence adopting the requirement would impose more onerous requirements than that applying to Tier 2 entities.

Feedback from Subcommittee: The members that commented agree with staff's suggestion.

(d) The staff suggestion to add to paragraph 13.15(f) requirements that, when applying the equity method of accounting, any difference between the date of the investor's and investee's financial statements shall not exceed three months, and both the length of the reporting periods and any difference between the dates of the financial statements shall be the same from period to period. Staff's suggestion is aligned with current requirements in AASB 128 as well as the proposal in paragraph 8.16 in Section 8 *Consolidation and Separate Financial Statements.*

Feedback from Subcommittee: The members that commented agree with staff's suggestion.

(e) The overall length of the draft section is appropriate and whether they have any other suggestions for omitting text to achieve further simplification of the draft section of the Tier 3 ED.

Feedback from Subcommittee: The members that commented agreed with the length and did not provide further suggestions for omitting text to achieve further simplification except for their comments in paragraph (b) disagreeing with the staff suggested draft of the tripartite classification scheme for joint arrangements.

Question 11 to Board members

In Agenda Paper 4.15 for this meeting, staff asked Subcommittee members whether they agreed with the staff suggestion to align with the *IFRS for SMEs* Accounting Standard requirements and depart from the Tier 2 recognition and measurement requirements by including an 'impracticability' exemption from needing to align the accounting policies of the investor and investee when applying the equity method of accounting to an investment in an associate or a jointly controlled entity in draft paragraph 13.15(f). Staff consider that, although the inclusion of the 'impracticability' exemption is a departure from the Tier 2 requirement, it is a proportionate simplification for Tier 3 NFP entities, especially because the circumstances in which the strict test of 'impracticability' would be met should be quite limited. Staff note that paragraph 5 of AASB 108 *Accounting Policies, Changes in Accounting Estimates* *and Errors* states that “applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so” and provides examples of impracticability of retrospective requirements, for each of which it is virtually impossible to apply a requirement fully retrospectively. Therefore, staff recommend that the Board aligns with the text of the *IFRS for SMEs* Accounting Standard requirements (and departs from the Tier 2 recognition/ measurement requirements) in this regard. This recommendation is reflected in the draft text of para. 13.15(f).

Feedback from Subcommittee: The Subcommittee members that commented had mixed views. One Subcommittee member that disagreed questioned whether adding the exemption would provide much simplification to Tier 3 preparers who may not fully understand the requirements and it may not be prevalent for Tier 3 preparers to apply the exemption.

Do Board members support the inclusion of the ‘impracticability’ exemption from needing to align the accounting policies of the investor and investee when applying the equity method of accounting to an investment in an associate or a jointly controlled entity in draft paragraph 13.15(f)? If not, staff will remove the ‘impracticability’ exemption in paragraph 13.15(f).

Scope of this section

13.1 This section applies in:

(a) consolidated financial statements to accounting for associates and by participants in joint arrangements (in this section: ‘parties’); and

(b) the financial statements of an entity that is an investor in one or more associates, or a party to a joint arrangement, but in either case is not a parent.

13.2 Paragraph 8.26 establishes the requirements for accounting in separate financial statements for associates and for a party’s interest in a joint~~ly controlled entity~~ venture.

Associates defined

13.3 An associate is an entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor a joint arrangement.

13.4 Significant influence is the power to participate in the financial and operating policy decisions of the associate but is not control or joint control over those policies. In applying that principle:

(a) if an investor holds, directly or indirectly (for example, through subsidiaries), 20 per cent or more of the voting power of the associate, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case;

(b) conversely, if the investor holds, directly or indirectly (for example, through subsidiaries), less than 20 per cent of the voting power of the associate, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated; and

(c) a substantial or majority ownership by another investor does not preclude an investor from having significant influence.

Joint arrangements defined

13.5 Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

13.6 An entity that is a party to an arrangement shall assess whether the contractual arrangement gives all the parties, or a group of the parties, control of the arrangement collectively. However, an entity that prepares separate financial statements in accordance with paragraph 8.2(b) of Section 8 *Consolidated and Separate Financial Statements* is not required to make such an assessment. All the parties, or a group of the parties, control the arrangement collectively when they must act together to direct the activities that significantly affect the returns of the arrangement (that is, the relevant activities). For guidance on the meaning of ‘returns’ in the not-for-profit context of entities applying this [draft] Standard, refer to paragraph 8.10.

13.7 A joint arrangement is an arrangement of which two or more parties have joint control. Joint arrangements can take the form of a joint~~ly controlled~~ operations~~, jointly controlled assets~~ or a joint~~ly controlled entities~~ venture.

13.8 The classification of a joint arrangement as a joint operation or a joint venture depends upon the rights and obligations of the parties to the arrangement.

13.9 An entity assesses its rights and obligations by considering the structure and legal form of the arrangement, the terms agreed by the parties in the contractual arrangement and, when relevant, other facts and circumstances. A joint arrangement that is not structured through a separate vehicle is a joint operation. A

Commented [A25]: Note to Board members
A Subcommittee member noted entities that prepare separate financial statements disclosing their notable relationships should not be required to assess whether contractual arrangements exist or give rise to control of the arrangements collectively.

Staff agree with the feedback and proposed suggested additional text to clarify that these entities would not be required to assess the contractual arrangements as per the underlined text.

joint arrangement in which the assets and liabilities relating to the arrangement are held in a separate vehicle can be either a joint venture or a joint operation. When the parties have structured a joint arrangement in a separate vehicle, the parties need to assess whether the legal form of the separate vehicle, the terms of the contractual arrangement and, when relevant, any other facts and circumstances give them:

(a) rights to the assets, and obligations for the liabilities, relating to the arrangement (ie the arrangement is a joint operation); or

(b) rights to the net assets of the arrangement (ie the arrangement is a joint venture).

Jointly controlled operations

13.10 A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. The operation of some joint arrangements involves the use of the assets and other resources of the parties to the joint arrangement instead of the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the parties themselves. Each party uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations. The joint arrangement activities may be carried out by the party's employees alongside the party's similar activities. The joint arrangement agreement usually provides a means by which the revenue from the sale of the joint product and any expenses incurred in common are shared among the parties. The accounting entries for joint~~ly controlled~~ operations are specified in paragraph 13.19.

~~Jointly controlled assets~~

~~13.9 Some joint arrangements involve the joint control, and often the joint ownership, by the parties of one or more assets contributed to, or acquired for the purpose of, the joint arrangement and dedicated to the purposes of the joint arrangement. The accounting entries for jointly controlled assets are specified in paragraph 13.19.~~

Joint~~ly controlled entities~~ ventures

13.11 A joint~~ly controlled entity~~ venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement ~~that involves the establishment of a corporation, partnership or other entity in which each party with joint control has a net interest. The entity operates in the same way as other entities, except that an arrangement between the parties establishes joint control.~~ The measurement requirements for investments in joint~~ly controlled entities~~ ventures are specified in paragraphs 13.12 and 13.13.

Measurement of investments in associates and jointly ~~controlled~~ entities ventures

Measurement in consolidated financial statements

13.12 In consolidated financial statements (if any) of a parent entity investor, that investor shall account for its investments in associates and joint~~ly controlled entities~~ ventures using the equity method in paragraph 13.16.

Measurement in financial statements that are not consolidated financial statements – accounting policy election

13.13 In financial statements that are not consolidated financial statements of an investor, an investor shall account for all its investments in associates and joint~~ly controlled entities~~ ventures using one of the following:

(a) the cost model in paragraphs 13.14 – 13.15;

(b) the equity method in paragraph 13.16; or

(c) the fair value model in paragraphs 13.17 – 13.18.

Cost model

13.14 An investor in an associate or a joint~~ly controlled entity~~ venture shall measure ~~its~~ those investments ~~in those entities~~ at cost less any accumulated impairment losses recorded in accordance with Section 23 *Impairment of Assets.*

13.15 An investor in an associate or a joint~~ly controlled entity~~ venture shall record dividends and other distributions received from the investment as income without regard to whether the distributions are from accumulated profits of the associate or joint~~ly controlled entity~~ venture arising before or after the date of acquisition.

Equity method

13.16 Under the equity method of accounting, an equity investment in an associate or a joint~~ly controlled entity~~ venture (in either case in this paragraph, an 'investee') is initially recorded at the transaction price (including transaction costs) and subsequently is adjusted to reflect the investor's share of the profit or loss and other comprehensive income of the investee, by applying the following principles:

(a) *distributions and other adjustments to carrying amount*. Distributions received from the investee reduce the carrying amount of the investment. Adjustments to the carrying amount might also be required as a consequence of changes in the investee's equity arising from items of other comprehensive income.

(b) *potential voting rights*. Although potential voting rights are considered in deciding whether significant influence or joint control (as applicable) exists, an investor shall measure its share of profit or loss and other comprehensive income of the investee and its share of changes in the investee's equity on the basis of present ownership interests. Those measurements shall not reflect the possible exercise or conversion of potential voting rights.

(c) *implicit goodwill and fair value adjustments*. On acquisition of the investment in an investee, an investor shall account for any difference (whether positive or negative) between the cost of acquisition and the investor's share of the fair values of the net identifiable assets of the investee in accordance with [*TBU Section X Business Combination and Goodwill paragraphs 19.10M–19.10O and 19.23*]. An investor shall adjust its share of the investee's profits or losses after acquisition to account for additional depreciation or amortisation of the investee's depreciable or amortisable assets on the basis of the excess of their fair values over their carrying amounts when the investment was acquired. However, amortisation of goodwill implicit in the investment's carrying amount ('implicit goodwill') is not permitted; such goodwill is written down only if it is impaired.

Commented [A26]: **Note to Board members**
These paragraphs are a placeholder to reference the *IFRS for SMEs* Accounting Standard requirements paragraph numbers in the Business Combination and Goodwill section. Staff will bring the analysis and recommendation on the respective Tier 3 requirements at a future meeting.

(d) *impairment*. If there is an indication that an investment in an investee might be impaired, an investor shall test the entire carrying amount of the investment, including financial instruments that in substance form part of the investor's net investment in the associate, for impairment in accordance with Section 23, as a single asset. A financial instrument for which settlement neither is planned nor likely to occur in the foreseeable future is, in substance, part of the investor's net investment (for example, this may include preference shares or long-term receivables or loans). An investor shall apply Section 10 *Financial Instruments*] to any such financial instrument before it applies this paragraph or paragraph 13.16(h). Any goodwill included as part of the carrying amount of the investment in the investee is not tested separately for impairment but, instead, as part of the test for impairment of the investment as a whole.

(e) *investor's transactions with investees*. The investor shall eliminate unrealised profits and losses resulting from upstream (investee to investor) and downstream (investor to investee) transactions to the extent of the investor's ownership interest in the investee. Unrealised losses on such transactions might provide evidence of an impairment of the asset transferred.

(f) *date of investee's financial statements*. In applying the equity method, the investor shall use the financial statements of the investee as of the same date as the financial statements of the investor unless doing so is impracticable. If it is impracticable, the investor shall use the most recent available financial statements of the investee, with adjustments made for the effects of any significant transactions or other events occurring between the accounting period ends. In any case, the difference between the date of the investor's and investee's financial statements shall not exceed three months, and both the length of the reporting periods and any difference between the dates of the financial statements shall be the same from period to period.

Commented [A27]: **Note to Board members**
Staff have included the 'impracticability' exemption from the *IFRS for SMEs* Accounting Standard requirements for Tier 3 entities needing to fully align the accounting policies of the investor and investee, subject to the Board's decision to Question 11.

(g) *investee's accounting policies*. If the investee uses different accounting policies from those of the investor, the investor shall adjust the investee's financial statements to reflect the investor's accounting policies for the purpose of applying the equity method unless doing so is impracticable.

(h) *losses in excess of investment*. If an investor's share of losses of an investee equals or exceeds the carrying amount of its investment in the investee, the investor shall discontinue recording its share of further losses. The investment in an investee is the carrying amount of the investment determined using the equity method together with any financial instruments that in substance form part of the investor's net investment in the associate (see paragraph 13.16(d)). After the investor's interest is reduced to zero, the investor shall record additional losses only to the extent that the investor either has incurred legal or constructive obligations and records a provision (see Section 19 *Provisions* *and Contingencies*) or has made payments on behalf of the investee. If the investee subsequently reports profits, the investor shall resume recording its share of those profits only after its share of the profits equals the share of losses not recorded.

Fair value model

13.17 When an investment in an associate or a joint~~ly controlled entity~~ venture is recorded initially, the investor shall measure it at the transaction price. Transaction price excludes transaction costs, such as legal fees or other fees incurred as a direct result of buying the investment.

13.18 At each reporting date, an investor shall measure its investments in associates and joint~~ly controlled entities~~ ventures at fair value, using the fair value measurement guidance in Section 11. Changes in the fair value of the investments shall be recorded in profit or loss, except that if an investment is held for capital return and to generate income, the investor may make an irrevocable election, upon initial recording of a particular investment, to record those changes in other comprehensive income. Any such election must be applied on a class-of-instruments basis. An investor using the fair value model shall use the cost model for any investment in an associate or joint~~ly controlled entity~~ venture for which fair value cannot be measured reliably.

Accounting for interests in joint~~ly controlled~~ operations

13.19 In respect of its interests in joint~~ly controlled~~ operations, a party shall record in its financial statements:

~~(a) the assets it controls and the liabilities it owes; and~~

~~(b) the expenses it incurs and its share of the revenue it earns from the sale of goods or services by the joint arrangement.~~

~~Accounting for interests in jointly controlled assets~~

~~13.19 In respect of its interests in jointly controlled assets, a party shall record in its financial statements:~~

(a) its assets, including its share of the jointly controlled assets, classified according to the nature of the assets;

(b) ~~any~~ its liabilities~~, it owes;~~ including

~~(c)~~ its share of any liabilities owed jointly with the other parties in relation to the joint arrangement;

(c) any revenue from the sale or use of its share of the output of the joint arrangement, together with its share of any expenses incurred by the joint arrangement; and

(d) any expenses it has incurred in respect of its interest in the joint arrangement.

Transactions between a party to a joint arrangement and the joint arrangement

13.20 When a party to a joint arrangement contributes or sells assets to the joint arrangement, recording any portion of a gain or loss from the transaction shall reflect the substance of the transaction. While the assets are retained by the joint arrangement, and provided the party to the joint arrangement has transferred the significant risks and rewards of ownership, the party shall record only the portion of the gain or loss attributable to the other parties' interests. The party shall record the full amount of any loss when the contribution or sale provides evidence of an impairment loss.

13.21 When a party to a joint arrangement purchases assets from the joint arrangement, that party shall not record its share of the profits of the joint arrangement from the transaction until it resells the assets to an independent party. A party to the joint arrangement shall record its share of the losses resulting from these transactions in the same way as profits, except that losses shall be recorded immediately if they represent an impairment loss.

If a party does not have joint control

13.22 A party that participates in, but does not have joint control of, a joint~~ly controlled entity~~ venture shall account for its interest in the arrangement in accordance with Section 10 *Financial Instruments* unless it has significant influence over the joint~~ly controlled entity~~ venture, in which case it shall account for it as an investment in an associate in accordance with this section.

13.23 A party that participates in, but does not have joint control of, a joint~~ly controlled~~ operation ~~involving the use of assets and other resources instead of the establishment of a separate vehicle~~ shall account for its interest in the arrangement in accordance with paragraph 13.19 if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation. If a party that participates in, but does not have joint control of, a joint operation does not have rights to the assets, and obligations for the liabilities, relating to that joint operation, it shall account for its interest in the joint operation in accordance with the Sections applicable to that interest.

~~13.24 When an asset is, or assets are, jointly controlled through joint ownership of the asset(s):~~

~~(a) contributed to, or acquired for the purpose of, a joint arrangement; and~~

~~(b) dedicated to the purpose of that joint arrangement,~~

~~if the entity participates in the asset(s) but does not have joint control of it (them), it shall account for its interest in the arrangement in accordance with paragraph 13.19.~~

Financial statement presentation – investments in associates

13.24 An investor shall classify investments in associates as non-current assets.

Disclosures

13.25 An entity shall disclose the following:

(a) its accounting policy for investments in associates and joint~~ly controlled entities~~ ventures (i.e. whether it uses the cost model, equity method or fair value model);

(b) the total carrying amounts, separately, of investments in associates [TBU: see paragraph X.2(j) in Section X Statement of Financial Position) and investments in joint~~ly controlled entities~~ ventures (see paragraph X.2(k) in Section X Statement of Financial Position];

(c) the total fair values, separately, of its investments in associates and investments in joint~~ly controlled entities~~ ventures for which a market price for the investment is quoted and the entity accounts for the investment using the equity method; and

(d) if the entity is an investor in one or more joint~~ly controlled entities~~ ventures, the aggregate amount of its commitments relating to those entities, including its share of the commitments incurred jointly with other parties.

13.26 For investments in associates accounted for using the cost model, an investor shall disclose the amount of dividends and other distributions recorded as income for the period.

13.27 An investor shall disclose separately for investments in associates, and investments in joint~~ly controlled entities~~ ventures, accounted for using the equity method:

(a) its share of the profit or loss; and

(b) its share of any discontinued operations.

13.28 For investments in associates and joint~~ly controlled entities~~ ventures accounted for using the fair value model, an investor shall make the disclosures required in ~~AASB 1060~~ Section 10 *Financial Instruments* paragraphs 10.27 – 10.29.

Section 14: Investment Property [TBU]

Scope of this section

Section 15: Property, Plant and Equipment

Question 12 to Board members

A Subcommittee member was unclear about inclusion of the term "net" in the references to the revaluation increase/decrease and did not consider it necessary to include the term in paragraphs 15.12 and 15.13.

Staff analysis and recommendation:

Staff referred to net revaluation to clarify that revaluations would be required for a class of assets, any revaluations would be considered in aggregation (i.e. net). Staff consider it would be useful to keep the word net to ensure readers understand that revaluation gains and losses would be netted together for assets of the same class and therefore, recommend to retaining the term "net" in the draft.

Commented [A28]: Note to Board members:
At the time when drafting this Section for Subcommittee members' review, staff have not yet drafted the Section on Financial Instruments where the *IFRS for SMEs* Accounting Standard requirements contained similar disclosures to AASB 1060 paragraph 113 – 115 which contains specific disclosure requirements about carrying amounts of categories of financial assets and financial liabilities. Staff have now included the cross-reference to Section 10 *Financial Instruments* which contains the disclosure requirements for categories of financial assets and financial liabilities in paragraphs 10.27 – 10.29 as per drafting and therefore the reference was updated.

Do Board members agree with the recommendation? If not, do Board members prefer the reference to the term "net" be removed in paragraphs 15.12 and 15.13?

Scope of this section

15.1 This section applies to accounting for:

(d) property, plant and equipment; and

(e) investment property whose fair value cannot be measured reliably on a continuing basis (to which TBU Section 14 *Investment Property* applies).

15.2 Property, plant and equipment are tangible assets that are:

(d) held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

~~(e)~~ expected to be used during more than one period.

Recording an item

15.3 An entity shall record an item of property, plant and equipment as an asset from when it is purchased by, or donated to, the entity.

Initial measurement

15.4 ~~Subject to paragraph 17.5, a~~An item of property, plant and equipment shall initially be measured at its cost.

~~15.5~~ However, ~~I~~if an item of property, plant and equipment was donated to the entity, that entity may elect to initially measure the item either at:

(a) its cost; or

(b) its fair value as at the date of donation, measured in accordance with Section 11.

Commented [A29]: Note to Board members
A Subcommittee member queried whether paragraph 15.5 is consistent with paragraph 15.4 which covers purchased and donated assets, both of which appear to be mutually exclusive. Donated assets could also be of nil, nominal or acquired at significantly less than fair value.

Staff consider paragraph 15.5 specifically refers to donated assets which is based on the NZ Tier 3 Standard terminology for brevity and clarity. As per Agenda Paper 4.12 for this meeting, staff plan to provide the meaning of donated assets to include assets acquired at significantly less than fair value in glossary. In staff's view, paragraph 15.4 would apply to both purchased and donated assets and paragraph 15.5 provides further guidance for donated assets as per the Board's preliminary view, and subject to the Board's decision in Agenda Paper 4.2 for this meeting. However, staff consider further streamlining could be achieved by combining paragraphs 15.4 and 15.5 as per marked up text.

Elements of cost

15.5 The cost of an item of property, plant and equipment comprises all of the following:

(a) its purchase price, after deducting trade discounts and rebates.

(b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management (e.g. legal fees and installation costs).

(c) the initial estimate of any related restoration, rehabilitation or other "make good" obligation.

15.6 The following costs are not costs of an item of property, plant and equipment and shall be recorded as an expense when they are incurred:

(b) costs of opening a new facility;

(c) costs of introducing a new good or service (including costs of advertising and promotional activities); costs of operating in a new location or with a new class of beneficiaries (including costs of staff training); and

(d) administration and other general overhead costs.

Measurement after initial recording

15.7 An entity shall choose either the cost model in paragraph 15.10 or the revaluation model in paragraph 15.11 as its accounting policy and shall apply that policy to an entire class of property, plant and equipment. An entity shall apply the cost model to investment property whose fair value cannot be measured reliably on a continuing basis. An entity shall record the costs of day-to-day servicing of an item of property, plant and equipment in profit or loss in the period in which the costs are incurred.

15.8 Electing to revalue a class of property, plant and equipment after initially recording an item is an accounting policy choice. Therefore, once a class of property, plant and equipment is revalued it shall continue to be measured on the revaluation model thereafter (rather than reverting to being measured under the cost model).

15.9 For the purposes of paragraphs 15.7 and 15.8, a class of property, plant and equipment is a grouping of assets of a similar nature or function. Possible classes of property, plant and equipment are:

(a) land;

(b) buildings;

(c) motor vehicles;

(d) furniture and fixtures;

(e) office equipment;

(f) computers (including software); and

(g) machinery.

Cost model

15.10 An entity shall measure an item of property, plant and equipment after initial recording at cost less any accumulated depreciation and any accumulated impairment losses (which are recorded and measured in accordance with Section 23 *Impairment of Assets*).

Revaluation model

15.11 An entity shall measure an item of property, plant and equipment whose fair value can be measured reliably at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses (which are recorded and measured in accordance with Section 23). Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. Section 11 *Fair Value Measurement* provides guidance on determining fair value.

Recording revaluation increases and decreases

15.12 If the carrying amount of a class of assets is increased as a result of a revaluation, the net revaluation increase shall be recorded in other comprehensive income and accumulated in equity under the heading of revaluation surplus. However, the net revaluation increase shall be recorded in profit or loss to the extent that it reverses a net revaluation decrease of the same class of assets previously recorded in profit or loss.

15.13 If the carrying amount of a class of assets is decreased as a result of a revaluation, the net revaluation decrease shall be recorded in profit or loss. However, the net revaluation decrease shall be recorded in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that same class of assets. The net revaluation decrease recorded in other comprehensive income reduces the amount accumulated in equity under the heading of revaluation surplus.

Depreciation

15.14 An entity shall allocate the depreciable amount of an asset on a systematic basis over its useful life. The resulting depreciation charge for each period shall be recorded in profit or loss unless another section of this Standard requires the cost to be recorded as part of the cost of an asset. For example, the depreciation of manufacturing property, plant and equipment is included in the costs of inventories (see Section 12 *Inventories*). Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

15.15 If the major components of an item of property, plant and equipment have significantly different useful lives or patterns of consumption of economic benefits, an entity shall allocate the initial cost of the asset to its major components and depreciate each such component separately over its useful life. Other assets shall be depreciated over their useful lives as a single asset. Land has an unlimited useful life and therefore is not depreciated.

Depreciable amount and depreciation period

15.16 An entity shall consider all the following factors in determining the useful life of an asset:

(a) the expected usage of the asset, assessed by reference to the asset's expected capacity or physical output.

(b) expected physical wear and tear.

(c) technical or commercial obsolescence arising from changes or improvements in production, or from a change in the external demand for the output (goods or services) of the asset.

(d) legal or similar limits on the use of the asset, such as the expiry dates of related leases.

15.17 If an asset has been damaged physically or its capacity to provide services has been affected adversely as a result of either:

(a) the entity having changed its strategy; or

(b) being affected by a reduction in external demand for its services,

this may indicate that the residual value or useful life of an asset has changed since the most recent annual reporting date. If such indicators are present, an entity shall review its previous estimates and, if current expectations differ, amend the residual value, depreciation method or useful life. The entity shall account for the change in residual value, depreciation method or useful life as a change in an accounting estimate in accordance with [TBU Section 9 *Accounting Policies, Estimates and Errors*].

15.18 Depreciation of an asset ceases when the asset ceases to be recorded. Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.

Depreciation method

15.19 An entity shall select a depreciation method that reflects the pattern in which it expects to consume the asset's future economic benefits. The possible depreciation methods include the straight-line method, the diminishing balance method and a method based on usage such as the units of production method.

15.20 If there is an indication that there has been a significant change since the last annual reporting date in the pattern by which an entity expects to consume an asset's future economic benefits, the entity shall review its present depreciation method and, if current expectations differ, change the depreciation method to reflect the new pattern. The entity shall account for the change as a change in an accounting estimate in accordance with [*TBU* Section 9].

Ceasing recording an item

15.21 An entity shall cease recording an item of property, plant and equipment when:

(a) it is sold or otherwise disposed of; or

(b) no future economic benefits are expected from its use or disposal.

15.22 For the purposes of paragraph 15.21(b), an entity needs to consider the possibility that no future economic benefits are expected from the use or disposal of an asset only when:

(a) the asset has been damaged physically; or

(b) the entity has changed its strategy or been affected by a reduction in external demand for its services and in either case the asset's capacity to provide services might have been affected adversely as a result.

15.23 An entity shall record the gain or loss upon ceasing to record an item of property, plant and equipment immediately in profit or loss ~~(unless Section 18 *Leases* requires otherwise on a sale and leaseback)~~. The entity shall not classify such gains as revenue. ~~Section XX applies to disposal by a sale and leaseback.~~

15.24 An entity shall determine the gain or loss arising from ceasing to record an item of property, plant and equipment as the difference between the net sale proceeds, if any, and the carrying amount of the item.

Disclosures

15.25 An entity shall disclose the following for each class of property, plant and equipment determined in accordance with paragraph 15.9 and separately for investment property carried at cost less accumulated depreciation and impairment:

(a) a description of the asset class (for example, equipment or furniture);

(b) the measurement bases used;

(c) the carrying amount at the beginning and end of the reporting period;

(d) increases or decreases resulting from revaluations under paragraphs 15.15 and 15.16 and from impairment losses recorded ~~or reversed~~ in other comprehensive income in accordance with Section 23;

Commented [A30]: **Note to Board members**
As noted in the note to Board members in Section 18 *Leases*, Agenda Paper 4.9 for this meeting, staff asked Subcommittee members whether they agreed with the staff suggestion to omit the guidance in the *IFRS for SMEs* Accounting Standard requirements on the accounting treatment of sale-and-leaseback arrangements, consistent with the Board's intention not to develop specific requirements on sale and leaseback arrangements (refer to paragraph 5.176 of the DP). Subcommittee members who commented agreed with the staff suggestion. As such, staff have deleted the reference to sale and leaseback as per strikethrough text.

(e) impairment losses recorded ~~or reversed~~ in profit or loss in accordance with Section 23; and

(f) depreciation.

15.27 An entity shall also disclose the following:

(a) the existence and carrying amounts of property, plant and equipment to which the entity has restricted title or that is pledged as security for loans (including the nature and amount of loans that are secured);

(b) the amount of contractual commitments for the acquisition of property, plant and equipment; and

(c) if the entity has investment property whose fair value cannot be measured reliably, it shall disclose that fact and the reasons why fair value cannot be measured reliably for those items of investment property.

15.28 If items of property, plant and equipment are stated at revalued amounts, an entity shall disclose the following:

(a) the effective date of the revaluation; and

(b) whether an independent valuer was involved.

15.29 Where, in accordance with paragraph 15.5(a), an entity elects to initially measure at cost a donated item of property, plant and equipment, it shall disclose information that helps users of financial statements to assess:

(a) the entity's dependence on donations of assets; and

(b) the nature and terms of the donation arrangement, including:

(vi) a description of the donated asset and the class of assets to which it relates;

(vii) any amounts owing to the donor at the reporting date; and

(viii) restrictions on the use of the donated asset imposed by the donor.

15.30 The disclosures in paragraph 15.29 shall be provided for each donated asset that is individually material to assessing the aspects in part (a) or (b) of paragraph 15.29. However, such disclosures shall be aggregated for donated assets of a similar nature. The entity shall consider the level of detail necessary to enable those assessments by users of financial statements. The disclosures shall be aggregated or disaggregated so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items with substantially different characteristics.

Section 16: Intangible Assets other than Goodwill [TBU]

Scope of this section

Section 17: Business Combinations and Goodwill [TBU]

Scope of this section

Section 18: Leases

Note to Board members

In Agenda Paper 4.9 for this meeting, staff asked Subcommittee members whether they agreed with:

(a) the staff suggestion to omit the guidance in the *IFRS for SMEs* Accounting Standard requirements on the accounting treatment of sale-and-leaseback arrangements, consistent with the Board's intention not to develop specific requirements on sale and leaseback arrangements (refer to paragraph 5.176 of the DP). Subcommittee members who commented agreed with the staff suggestion; and

(b) the staff's draft of disclosure requirements for leases under which a lessee obtains donated use of underlying leased assets (i.e. the lessee makes no lease payments or the lease has significantly below-market terms and conditions principally to enable the lessee to further its not-for-profit objectives). The disclosure should help users assess the entity's dependence on donations of the use of underlying lease assets, and the nature and terms of the leases. The Subcommittee members who commented agreed with the staff's proposed disclosure requirements.

Commented [A31]: Note to Board members
Similar to the rationale noted in paragraph 12.20 of Section 12 *Inventories*, staff recommended to delete references to reversal of impairment losses in the disclosure requirements to keep with the DP proposal in paragraph 5.161 not to develop requirements to account for the reversal of impairment losses, otherwise it may confuse readers.

<u>Question 13 to Board members</u>

Subcommittee members expressed mixed views about staff's drafting of paragraph 18.3(b) which was relocated from paragraph 18.2 based on the *IFRS for SMEs* Accounting Standard requirements (refer to Agenda Paper 4.9). Members suggested different approaches including:

a) combining paragraph 18.3(b) into paragraph 18.3(a); or
b) deleting paragraph 18.3(b) entirely; or
c) reinstating the *IFRS for SMEs* Accounting Standard requirements text back into paragraph 18.3.

<u>Staff analysis and recommendation</u>

As per Agenda Paper 4.9 for this meeting, staff relocated the text into paragraph 18.3(b) to clarify the circumstances in which the time pattern of expense recording for lease rentals might differ from the time pattern of lease payments, in applying the principle specified in paragraph 18.2. However, in light of the feedback from the Subcommittee, staff recommend reinstating the *IFRS for SMEs* Accounting Standard requirements back into paragraph 18.2 as per underlined text.

Do Board members agree with staff recommendation to reinstate the *IFRS for SMEs* Accounting Standard requirements in paragraph 18.2 as per underlined text? If not, do Board members prefer the other approaches suggested by other Subcommittee members?

Scope of this section

18.1 This section covers accounting for all leases other than measurement of property held by lessees or lessors that is accounted for as investment property (*TBU see* Section 14 *Investment Property*).

Financial statements of lessees

Recording and measurement

18.2 A lessee shall record lease payments (excluding costs for services such as insurance and maintenance) as an expense over the lease term on a straight-line basis, unless another systematic basis is more representative of the time pattern of the user's benefit from the leased asset (in which case that other systematic basis shall be used)~~.~~<u>, even if the payments are not on that basis.</u>

18.3 For the purposes of paragraph 18.2~~:~~<u>,</u>

~~(a)~~ the costs to be recorded as an expense over the lease term shall be increased by any initial direct costs of the lessee (ie incremental costs directly attributable to negotiating and arranging a lease) and reduced by the benefit of any upfront lease incentive (eg a rental holiday period), with the effect that those costs/incentives are spread over the term of the lease~~; and, similarly,~~<u>.</u>

~~(b) the time pattern of expense recording does not depend on the time pattern of lease payments.~~

Financial statements of lessors

Recording and measurement

18.4 A lessor shall present assets subject to leases in its statement of financial position according to the nature of the leased asset (eg leased building).

18.5 A lessor shall record lease income (excluding amounts for services such as insurance and maintenance) in profit or loss on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern of the lessee's benefit from the leased asset (in which case that other systematic basis shall be used).~~ even if the receipt of payments is not on that basis; or~~

18.6 A lessor shall record as an expense costs, including depreciation, incurred in earning the lease income.

18.7 A lessor shall add to the carrying amount of the leased asset any initial direct costs it incurs in negotiating and arranging a lease and shall record such costs as an expense over the lease term on the same basis as the lease income. ~~Similarly, the amount of any upfront lease incentive provided to the lessee shall be spread over the term of the lease as a reduction in lease income.~~ The time pattern of income and expense recording does not depend on the time pattern of lease payments.

Commented [A32]: <u>**Note to Board members**</u>
Similar to the Note to Board members above, a Subcommittee member considered the original text that the receipt of payments may differ from time pattern of lease receipts should be retained.

Consistent with the staff recommendation above, staff consider reinstating the *IFRS for SMEs* Accounting Standard requirements back into paragraph 20.5 as per the underlined text.

Commented [A33]: <u>**Note to Board members**</u>
A Subcommittee member noted an inconsistency in the staff analysis of drafting in column 3 of paragraph 20.27 in Agenda Paper 4.9 for this meeting where staff considered including, the suggested relocated guidance on the time pattern of lease payments, and with the suggested additional guidance on upfront lease incentives, for lessees in paragraph 20.15A into the lessor section. Staff considered it would be uncommon for Tier 3 NFP lessors to grant upfront lease incentives, and therefore do not suggest adding that guidance about upfront lease incentives in paragraph 18.7. However, in the proposed drafting as per paragraph 18.7, staff have not removed the text.

Staff agree with the feedback and removed the second sentence from paragraph 18.7 in relation to lease incentives based on reasons noted above and reflected as strikethrough text.

Disclosures for lessees and lessors

18.8 A lessee or lessor shall disclose the following for leases:

(c) a description of the underlying leased assets;

(d) the future minimum lease payments under non-cancellable leases for each of the following periods:

(ix) not later than one year;

(x) later than one year and not later than five years; and

(xi) later than five years; and

(e) a general description of the entity's significant leasing arrangements, including, for example, information about contingent rent, renewal or purchase options and escalation clauses, subleases (if a lessee) and restrictions imposed by lease arrangements.

18.9 A lessee shall also disclose the total lease payments recorded as an expense for the period.

18.10 A lessor shall also disclose the total variable lease payments that do not depend on an index, or a rate, recorded as income for the period.

18.11 In addition to making the disclosures required by paragraphs 18.8 and 18.9, where a lessee obtains donated use of underlying leased assets (ie it makes no lease payments or the lease has significantly below-market terms and conditions principally to enable the entity to further its not-for-profit objectives), it shall disclose information that helps users of financial statements to assess:

(a) the entity's dependence on donations of the use of underlying leased assets; and

(b) the nature and terms of the leases, including:

(i) the lease payments;

(ii) the lease term; and

(iii) any amounts owing to the donor at the reporting date.

18.12 The disclosures in paragraph 18.11 shall be provided for each underlying leased asset that is individually material to assessing the aspects in paragraph 18.11(a) or (b). However, such disclosures shall be aggregated for underlying leased assets of a similar nature. The entity shall consider the level of detail necessary to enable those assessments by users of financial statements. The disclosures shall be aggregated or disaggregated so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items with substantially different characteristics.

18.13 In addition, the requirements for disclosure about assets in accordance with the sections covering Property, Plant and Equipment and Investment Property at Cost, Intangible Assets other than Goodwill, and Impairment of Assets apply to lessors for assets provided under leases.

Section 19: Provisions and Contingent Liabilities

Note to Board members

In Agenda Paper 4.10 for this meeting, staff asked Subcommittee members whether they agreed with staff's view to include draft paragraphs 19.3–19.4 to explain the concept of a 'present obligation' and to describe and illustrate a 'constructive obligation' and whether members suggest any examples to be included in the drafting. Members who commented agreed with staff's approach and no further examples were provided to be included in the drafting.

Question 14 to Board members

In Agenda Paper 4.10 for this meeting, staff asked Subcommittee members whether they agreed with staff's suggestion to exclude the Tier 2 requirements for non-recognition of, and disclosure of information about, contingent assets and disclosures of information about possible reimbursement of expenditures required to settle provisions or contingent liabilities, and about excluding the Tier 2 requirements regarding reimbursement. Staff suggested the exclusion because staff consider that:

(a) based on findings from Research Report 19, contingent assets should be uncommon for Tier 3 NFP entities and in line with New Zealand Tier 3 Standard which does not contain guidance on contingent assets.; and

(b) reimbursements of expenditures required to settle provisions would not occur frequently to justify requiring disclosures.

The Subcommittee members who commented agreed with staff's approach to exclude the Tier 2 requirements listed.

Do Board members agree with the staff recommendation to exclude the Tier 2 requirements relating to contingent assets, reimbursements and disclosures of information about possible reimbursements of expenditures required to settle provisions or contingent liabilities?

If not, what do the Board suggest?

Recording provisions

19.1 A provision is a liability of uncertain timing or amount. For example, a provision would exist when an entity's lease of office premises requires the premises to be renovated at the end of the lease.

19.2 A provision shall be recorded as a liability when:

(a) the entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable (ie more likely than not) that the entity will need to transfer assets to another party in settling the obligation; and

(c) the entity can make a reliable estimate of the amount of the obligation.

19.3 Only obligations arising from past events and that the entity has no realistic alternative to avoid settling are present obligations. Present obligations exist independently of the entity's future actions (ie they must be settled in one manner or another, regardless of choices the entity makes about how it operates in the future).

19.4 Regarding paragraph 19.2(a), a constructive obligation is a present obligation that is not legally binding (although it might become legally binding in the future) and derives from an entity's actions, where:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

An example of a constructive obligation is a non-legally binding obligation to remediate an operating site to its original condition where, before the end of the reporting period, the entity disturbed the site and made a public announcement that, consistent with its practices in other jurisdictions, it will remediate the site.

19.5 The use of estimates is an essential part of the preparation of financial statements, and does not undermine their reliability. This is especially true in the case of provisions, which by their nature are more uncertain than most other liabilities. Except in extremely rare cases, an entity should be able to make a reliable estimate of the amount of the obligation and therefore record a provision. Where a reliable estimate of the amount of a provision cannot be made, the liability is not recorded, and instead is disclosed as a contingent liability (see paragraphs 19.9 – 19.12).

Possible future liabilities

19.6 The only liabilities recorded in an entity's statement of financial position are obligations existing at the end of the reporting period as a result of a past event (ie present obligations). Therefore, a provision shall not be recorded for liabilities that might result from a future event, because these liabilities do not yet exist. For example, costs likely to be incurred in the future to continue an entity's activities in the future are not liabilities. Similarly, provisions shall not be recorded for expected future operating losses.

Measurement of provisions

19.7 Provisions shall be measured at the entity's best estimate of the amount to be paid, taking into account current information about conditions existing at the end of the reporting period. For example, where an entity expects to settle its obligations under a provision by engaging a contractor to perform a task (such as cleaning up a site where it held a fundraising event immediately before the end of the reporting period), it would take current contractor rates into account in estimating the cost to settle the provision.

Disclosures

19.8 For each class of provision, an entity shall disclose in the notes:

(a) a brief description of the nature of the obligations;

(b) the expected amount at which the provision is recorded, separated into current and non-current portions;

(c) an indication of the uncertainties about the amount of the future payments made to settle the obligations; and

(d) if significant uncertainty exists about the classification of the provision into its current and non-current portions, the existence of that uncertainty and reason(s) why.

Comparative information for prior periods is not required.

Contingent liabilities

19.9 A contingent liability is:

(a) a possible obligation, the existence of which will be confirmed only by the occurrence or non-occurrence of an uncertain future event outside the entity's control (for example, a court case not yet settled, or a guarantee issued outside a contract with a customer); or

(b) a present obligation that arises from past events but is not recorded because:

(i) it is not probable that a transfer of assets will be required to settle the obligation; or

(ii) the amount of the obligation cannot be measured reliably.

19.10 Contingent liabilities shall not be recorded in the statement of financial position, but information about them shall be disclosed in the notes (see paragraphs 19.11 – 19.12).

Disclosures

19.11 For each class of contingent liability at the end of the reporting period, an entity shall disclose in the notes:

(a) a brief description of the nature of the contingent liability;

(b) a best estimate of the amount of the contingent liability (where this can be estimated); and

(c) an indication of the uncertainties about the amount or timing of any outflow of assets (where this is known by the entity).

19.12 For each guarantee or class of guarantee (as a subset of contingent liabilities) in force at the end of the reporting period, an entity shall disclose in the notes:

(a) the nature of the guarantee;

(b) the maximum amount of any guarantees provided to others; and

(c) the likelihood of the entity being required to make payment under the guarantee.

Commented [A34]: Note to Board members:
A Subcommittee member noted that in paragraph 19.9(a) contains, as an example of a contingent liability, "a guarantee issued outside a contract with a customer", yet paragraph 19.12 guarantees seem different from contingent liabilities.

As set out in Agenda Paper 4.10 for this meeting, the New Zealand Tier 3 Standard references guarantee as being an example of contingent liability and the disclosure regarding guarantees in paragraph 19.12 is specific to New Zealand Tier 3 Standard which staff suggested to include in the Tier 3 ED to elicit feedback on whether this disclosure should be required. Staff have revised the text in paragraph 19.12 to clarify that guarantees are a subset of contingent liabilities as per the revised drafting.

The Board decided at its November 2023 Board meeting on the scope of Financial instruments section of the Tier 3 ED to require complex financial instruments to apply the requirements in AASB 9 *Financial Instruments.* As such, where a guarantee is no longer a contingent liability, entities shall apply the requirements of AASB 9.

Firm commitments

19.13 Firm commitments are binding agreements for the exchange of a specified quantity of assets at a specified price on a specified future date or dates. They are not recorded as liabilities because the counterparty has yet to perform its promises under the binding agreement or satisfy other eligibility criteria, which is necessary for a present obligation of the entity to arise. Information about an entity's firm commitments to purchase goods, services or other assets is useful for users of financial statements in assessing the entity's future funding requirements.

19.14 This [draft] Standard requires disclosure in the notes of information about the timing and estimated amount of any significant firm commitments (both operating and capital). Those requirements are set out in the topic sections to which they relate. For example, those sections include requirements to disclose information about the following types of firm commitments:

(a) commitments to lease or rent assets;

(b) commitments to purchase property, plant and equipment or intangible assets; and

(c) commitments to provide loans or grants.

Section 20: Revenue

Note to Board members
In Agenda Paper 4.13, staff asked Subcommittee members whether they agreed with:

(a) the staff suggestion in relation to a deferred revenue liability being recognised ('recorded') when the provider of an asset to the entity and the entity have a common understanding that the entity will perform in a particular manner, it would not be necessary that evidence exists that the common understanding between the entity and the provider of an asset is specific enough to enable the entity to demonstrate reliably when the deferred revenue obligation has been satisfied. Subcommittee members who commented agreed with staff's suggestion; and

(b) the range of evidence of a common understanding that the entity will perform under a deferred revenue obligation, set out in paragraph 20.7, is adequate to achieve an appropriate extent of revenue deferred.

Feedback from Subcommittee: The Subcommittee members who commented considered the range of evidence listed to be adequate.

In Agenda Paper 4.17 at this meeting, staff asked Subcommittee members whether they agreed with:

(a) the manner in which staff suggest depicting the requirements for initial measurement of accounts receivables as being aligned with the fair value principle proposed by the Board for all financial assets. In particular, staff asked Subcommittee members if they agree:

(i) that accounts receivable should be required to be measured initially at fair value (along with all other financial assets), with the receivables' transaction price deemed to represent fair value at that date (as drafted in paragraphs 10.5 and 20.3B in Section 20 *Revenue*). This issue arises because accounts receivable are financial assets subject to the sections on Financial Instruments and Revenue. AASB 9 excludes trade receivables without a significant financing component from the general initial measurement requirement of 'fair value adjusted for transaction costs' and states that trade receivables are initially measured at their 'transaction price' as defined in AASB 15 (AASB 9, paragraphs 5.1.1 and 5.1.3).

The DP proposed that financial assets should initially be measured at their fair value (excluding transaction costs and fees associated with acquiring and financial assets), and did not scope trade receivables out of that proposal. Staff also previously drafted the Revenue section and staff have now integrated the initial measurement requirements for accounts receivable more overtly with the general 'fair value' principle proposed by the Board for the initial measurement of financial assets (i.e. transaction price of accounts receivable is normally the same as fair value at the date of initial measurement and it would seldom be sufficient evidence of different fair value to 'move off' the transaction price). Staff noted that there may be scenarios where the fair value of an account receivable on initial measurement might differ from its transaction price (e.g. when transaction price includes variable considerations like incentives, penalties and discounts) and a significant component of variable consideration might be excluded from the 'transaction price' because it fails the 'highly probable' test but might nonetheless have a material effect on the fair value of the account receivable. However, the draft section in Section 20 *Revenue* excluded the requirement for variable consideration to meet a 'highly likely' criterion for inclusion in the transaction price of an account receivable. Staff considered that material amounts of variable consideration would be uncommon for Tier 3 NFP entities, and therefore the inclusion of such a requirement is unlikely to be proportionate.

As per Agenda Paper 4.17, whilst acknowledging that the transaction price of a financial asset might differ from its fair value on initial measurement in some circumstances, AASB 9 imposes strict criteria for measuring the fair value of a financial asset at a different amount than transaction price on initial measurement. Staff think a receivable with variable consideration would seldom have Level 1 evidence of fair value or be based on a valuation technique that uses only data from observable markets. However, staff suggest that, instead of referring to the receivable's 'transaction price' and then explaining it as "the gross amount of consideration to which the entity expects to be entitled in exchange for providing specified goods and services to beneficiaries or customers", the Tier 3 ED should simply use the words in quotes. This should assist in minimising the extent of jargon used.

Feedback from Subcommittee: The Subcommittee members who commented agreed with the staff's approach.

(ii) Staff suggest to omit any reference to 'variable consideration' from the initial measurement requirements for accounts receivable in the Revenue section of the Tier 3 ED, on grounds of being uncommon for Tier 3 NFP entities. The draft section on Revenue for the Tier 3 ED excluded the requirement for variable consideration to meet a 'highly likely' criterion for inclusion in the initial measurement of an account receivable. Staff consider that material amounts of variable consideration would be uncommon for Tier 3 NFP entities, and therefore the inclusion of such a requirement is unlikely to be proportionate. However, staff have included hypothetical draft text in paragraph 20.3B should the Subcommittee members consider including variable considerations in the Tier 3 ED. Staff acknowledge that if requirements for the treatment of variable consideration were omitted from the Tier 3 Standard, Tier 3 NFP entities with variable consideration would need to develop an accounting policy for that issue (i.e. for them, the Standard would not be simpler) and their practices might vary. However, this risk arises generally for transactions and other events excluded from the Tier 3 Standard on the grounds of being uncommon (but arising for some Tier 3 NFP entities) and is inherent in developing a simplified Standard. Staff suggest including a Specific Matter for Comment on whether requirements for variable consideration should be excluded from the Tier 3 Standard, supported by an explanation in the Board's Basis for Conclusions on the Tier 3 ED. Staff think this approach would be preferable to including the text in the ED but proposing to exclude it from the Tier 3 Standard, because that approach would lengthen the ED (when limiting its length inherently is difficult).

Feedback from Subcommittee: The Subcommittee members who commented agreed with the staff's approach. One Subcommittee member noted that even in the absence of the Tier 3 Standard addressing this issue, in applying the hierarchy and developing an accounting policy for this issue, entities will consider Tier 2 (i.e. AASB 15) requirements and, given a choice between the 'expected value' and 'most likely amount' options, will likely choose the latter anyway.

(b) Staff's suggestion to exclude from the Tier 3 ED requirements addressing how to account for a significant financing period provided to a customer, when measuring the amounts of accounts receivable arising from a transfer of goods or service to a customer or beneficiary, on grounds of being uncommon for Tier 3 NFP entities. Because staff are not aware that it would be common for Tier 3 NFP entities to provide significant financing to customers or beneficiaries, staff consider it would be unlikely to be proportionate to include such requirements in the Tier 3 ED. This issue is separate from the treatment of loans; it relates only to financing provided implicitly to customers in conjunction with contracts for the provision of goods or services to them. Staff's hypothetical draft text for how the treatment of a significant financing period provided to customers in conjunction with contracts for the provision of goods or services (but suggested to be omitted from the Tier 3 ED) is set out as shaded text in paragraph 20.3C. Staff suggest including a Specific Matter for Comment on whether requirements for significant financing periods provided to customers should be excluded from the Tier 3 Standard, supported by an explanation in the Board's Basis for Conclusions on the Tier 3 ED. Staff think this approach would be preferable to including the text in the ED and proposing to exclude it from the Tier 3 Standard, because that approach would lengthen the ED (when limiting its length inherently is difficult).

Feedback from Subcommittee: The Subcommittee members who commented agree with staff's suggestion.

Scope of this Section

20.1 Revenue is income arising in the course of an entity's ordinary activities. Revenue includes:

(a) recorded inflows of cash and other assets to the entity, other than;

(i) inflows from borrowings, sales of assets, or contributions of capital from owners; and

(ii) inflows that give rise to liabilities to act or perform in a particular way in the future, such as liabilities to transfer goods or render services;

(b) recorded reductions in liabilities to act or perform in a particular way in the future (see paragraph 20.9); and

(c) recorded increases in debtors (accounts receivable) resulting from transfers of goods, or the rendering of services, by the entity.

20.2 Examples of revenue are donations, grants, members' fees, funding or sales consideration earned through the provision of goods or services to beneficiaries or customers (including fundraising events).

Accounting for Revenue

20.3 On initial recording of an asset provided to the entity (i.e. without the entity purchasing it from a supplier):

(a) the entity shall record a deferred revenue obligation (liability) if the entity and that provider have a common understanding that, in response, the entity will perform in a particular manner resulting in the expenditure, transfer or using up of:

(i) that asset; or:

(ii) other assets of the entity with a similar value (see paragraph 20.5); ~~and~~ or

(b) if a 'deferred revenue obligation' liability described in (a) does not exist, record revenue simultaneously with initially recording the asset. This occurs at the earlier of receiving the cash/other asset and obtaining control of a right to receive the cash/other asset.

20.3A The liability in paragraph 20.3(a) and the revenue in paragraph 20.3(b) shall be measured at the same amount as the amount recorded initially for the asset. That amount shall be measured in accordance with:

(a) the measurement requirements in paragraph 20.3B, for debtors; and

(b) the applicable section of this [draft] Standard, for all other assets.

Commented [A35]: Note to Board members
A Subcommittee member considered the drafting for this paragraph confusing as paragraphs 20.3 (a) and (b) are alternatives, the reading should be 'or' rather than 'and'.

Staff agree with the suggestion and have amended the text as reflected in underline and strikethrough.

Measurement of debtors

20.3B Amounts receivable in exchange for goods or services transferred to customers (debtors) shall, subject to paragraph 20.3C, be measured initially and subsequently at fair value, estimated as the amount of consideration to which the entity expects to be entitled. That amount:

(a) includes both:

(i) the fixed amount of consideration receivable; and

(ii) the most likely amount of any variable consideration receivable (eg amounts that might vary as a result of discounts or penalties), but only to the extent it is highly probable that the variable amount will become due when the uncertainty associated with it is subsequently resolved; and

(b) excludes amounts collectible on behalf of third parties (eg goods and services tax).

20.3C If the period between when goods or services are provided to a customer by the entity and when the customer's payment is required represents the implicit provision of a significant period of financing to the customer, the entity shall measure the amount receivable from the customer (debtor) at the present value of that payment. The present value shall be determined by discounting the payment using a market rate of interest for a similar debt instrument as determined at initial recording. The difference between the present value (initial measure of the debtor) and the amount payable by the debtor shall be recorded as interest income over the period of credit.

Deferred revenue obligations

20.4 For the purposes of paragraph 20.3(a), for a deferred revenue obligation to arise from a common understanding that the entity will perform in a particular manner, it is unnecessary for the obligation to be enforceable against the entity by legal or other means.

20.5 Examples of an entity's performance in a particular manner resulting in the expenditure, transfer or using up of either the asset received, or other assets, referred to in paragraph 20.3(a), are:

(a) transferring specified goods or rendering specified services, either to the asset provider in return or to third party beneficiaries;

(b) performing a specified activity (including acquiring or constructing a specific asset e.g. constructing a building under the terms of a capital grant);

(c) incurring eligible expenditure for a specified purpose (e.g. acquiring a specified asset); and

(d) using the asset(s) for a specified period, either for specific programmes or activities, or for the entity's programmes and activities generally.

20.6 Judgement is required to determine when an entity satisfies its deferred revenue obligations that arose from receiving transferred assets and revenue is no longer deferred. Revenue shall be recorded in the manner that most faithfully represents the amount and pattern of the entity's using up of the assets received (or other assets with a similar value). Examples of the events and time patterns for identifying the satisfaction of deferred revenue obligations are:

(a) when goods and services are transferred (identified by reference to the proportion of the total quantity, cost or value of the goods or services expected to be provided, or on a time basis);

(b) when activities are performed;

(c) when eligible expenditure is incurred; and

(d) as time elapses over the specified period, reflected in a systematic allocation basis over that period.

Evidence of a common understanding

20.7 For the purposes of paragraph 20.3(a), evidence of a common understanding that the entity will transfer, expend or use up an asset it received, or other assets of similar value includes written communication~~, in writing or email~~, between the entity and the provider of the asset, or other written/oral representations made to customers, regarding:

(e) the purpose for which the asset, or other assets of the entity, is to be expended, transferred or used up; or

(f) the period over which the transferred asset is to be used.

Commented [A36]: Note to Board members
A Subcommittee member was unclear about the reference to 'in writing or email', since email is a written form of communication.

Staff agreed with the suggestion and removed the reference to 'in writing or email' and included 'written' as a pretext to communication as per underlined and strikethrough text accordingly.

If a deferred revenue obligation is enforceable, evidence of the aspects in (a) or (b) would normally exist. However, enforceability of a deferred revenue obligation is not required to satisfy the evidence requirement of this paragraph.

20.8 For the purposes of paragraph 20.7:

(a) in sales of goods or services, the asset provided to the entity is the sales consideration, and the communication between the customer and the entity can be in writing or email, or other representations (such as advertising) made to the customer regarding the goods or services that will be provided in return for the sales consideration;

(b) where an application for funding sets out how or when the entity expects to use the funds, approval of the application by the funding provider is sufficient to demonstrate that there is common understanding between both parties concerning the expected use of the funds; and

(c) an example of communication is a specific current statement of the entity regarding how it would use assets provided to it, which creates a valid expectation of asset providers that it would discharge its responsibilities to use the assets in the promised manner.

Satisfying deferred revenue obligations

20.9 When paragraph 20.3(a) applies on initial recording of an asset, the entity shall subsequently reduce the liability, and simultaneously record revenue for the same amount, as the deferred revenue obligation is satisfied by the entity (either on the occurrence of a commonly understood event, such as a transfer of a specified good or making a specified expenditure, or progressively over a period, such as where specified services are rendered by the entity).

20.10 An expectation to use assets received to support the general operating costs of the entity over an unspecified period of time is not identified as giving rise to deferred revenue. In these circumstances, revenue is recorded simultaneously with initially recording the asset.

20.11 Internal expectations or decisions by those charged with governance about how or when the entity expects to use funds received from donations, grants and bequests are not relevant when determining whether a deferred revenue obligation of the entity exists.

Principal versus agent considerations

20.12 When another party is involved in satisfying the requirements of an obligation of the entity to a beneficiary or customer, the entity shall determine whether the nature of its obligation is to satisfy the requirements itself (that is, the entity is a principal) or to arrange for those requirements to be met by the other party (that is, the entity is an agent).

20.13 An entity is a principal if it controls the specified good or service before that good or service is transferred to the beneficiary or customer. Indicators that an entity controls the specified good or service before it is transferred to the beneficiary or customer include, but are not limited to, the following:

(a) the entity has the primary responsibility for providing the good~~s~~ or service~~s~~ to the beneficiary or customer, including the primary responsibility for the acceptability of the good or service (such as whether the good or service meets a customer's specifications);

(b) the entity has discretion in establishing the prices, either directly or indirectly, for ~~those~~ the good~~s~~ or service~~s~~; and

(c) the entity has inventory risk in relation to the specified good or service transferred to a beneficiary or customer (e.g. the beneficiary or customer has a right of return).

20.14 An example of the entity as principal is when the entity organises a conference for a group of not for profit entities, receives the conference fees, and is responsible for all the conference content and delivery even though the entity engages external parties to deliver various sessions under its supervision.

20.15 In applying paragraph 20.3B:

(a) an entity that is a principal shall record revenue in the gross amount of consideration to which the entity expects to be entitled in exchange for providing specified goods or services to beneficiaries or customers.

(b) an entity that is an agent shall record revenue in the amount of any management or administration charge, fee or commission to which the entity expects to be entitled in exchange for arranging for the specified goods or services to be provided to beneficiaries or customers. An entity's charge, fee or commission as agent might be the net amount of consideration that the entity retains after paying

Commented [A37]: Note to Board members
A Subcommittee member noted some inconsistencies in the terms used when referring to 'good/s' or 'service/s' and suggested the use of one term throughout.

Staff have edited paragraphs 20.13(a) and (b) to achieve consistency regarding usage of singular/plural references as per strikethrough and underlined text.

another party the consideration for providing specified goods or services to beneficiaries or customers.

20.16 Regardless of whether an entity is a principal or an agent, its debtors exclude amounts collectible on behalf of third parties (eg goods and services tax).

Commented [A38]: Note to Board members
This paragraph would be included if, as staff suggest, shaded draft para. 20.3B(b) were omitted.

Pledges

20.17 A pledge is a promise made by a donor to contribute assets to the entity in the future. Pledged assets and related revenue are not recorded until the promised assets are received.

Volunteer services

20.18 An entity may, as an accounting policy choice, elect to record volunteer services received, or a class of volunteer services received, if the fair value of those services can be measured reliably. If an entity elects to record volunteer services received, it shall measure those services at their fair value.

20.19 The entries for voluntarily recording the fair value of volunteer services shall include that amount in:

(a) revenue or (in rare circumstances, eg when the controlling entity donates legal services to the entity) contributions by owners; and

(b) expenses for the using up of those services as they are received.

Commented [A39]: Note to Board members
A Subcommittee member suggested it would be helpful to include an example of a rare circumstance in which volunteer services would be a contribution by owners, either here or elsewhere.

Staff agree and have included an example of when a volunteer service might be a contribution by owners of a Tier 3 NFP entity.

20.20 Some volunteer services, such as professional services, might have readily observable market prices. In such circumstances, obtaining a reliable measure of their fair value would be relatively straightforward.

Unit of account for deferred revenue obligations

20.21 The unit of account for deferred revenue obligations is each separate documented commonly understood obligation identified. There may be multiple documented obligations attached to an inflow of assets, each of which shall be accounted for separately when reducing the deferred revenue liability balance and recording revenue. However, if a deferred revenue obligation arise~~s~~ and ~~is~~ are fully satisfied in the same reporting period, there is no need to disaggregate the deferred revenue obligations; the entire amount of the asset(s) received is recorded as revenue in that period.

Commented [A40]: Note to Board members
A Subcommittee member proposed wording changes to this sentence to read better by restating it to "However, if one or more deferred revenue obligations arise and are fully satisfied…" to keep consistent with the latter part of the sentence, which refers to multiple obligations.

Staff agree with the suggestion and amended this sentence to refer to more than one deferred revenue obligation.

20.22 Judgement will be required to determine an appropriate revenue recording approach for determining the point in time at which, or the period over which, the documented commonly understood obligation is satisfied. The following are examples of documented commonly understood obligations and the different revenue recording approaches that may be used, consistent with the requirements of paragraph 23.6:

(a) Deliver specified goods or services to beneficiaries (e.g. to deliver 1,000 school lunches) – revenue could be recorded as the specified goods or services are delivered.

(b) Purchase an asset (e.g. a vehicle) as stipulated under a funding agreement – revenue could be recorded when the asset is purchased.

(c) Construct an asset (e.g. building) – revenue could be recorded over the construction period (e.g. on a stage of completion basis).

(d) Support general operating costs (over a specified time period, e.g., three years) – revenue could be recorded on a straight-line basis over the three-year period.

(e) Host an event or deliver a specific programme or activity – revenue could be recorded on a stage of completion basis as the costs to host the event or deliver the specified programme or activity are incurred.

Disclosures

20.23 An entity's total revenue for the period shall be disaggregated into categories that help users of its financial statements assess the nature, amount, timing and uncertainty of each dissimilar type of revenue recorded. At a minimum, the amounts recorded for the following categories shall be disclosed separately if they were received by the entity:

(a) donations, bequests and other revenue from general fundraising activities, apart from those disclosed under (c) below;

(b) grants ~~specified~~ stipulated to be used for the provision of goods or services consistent with the entity's mission, ~~in general~~ without specification of which goods or services are to be provided;

(c) grants and donations specified to be used for the construction or purchase of assets;

Commented [A41]: Note to Board members
A Subcommittee member considered the reference to 'in general' adds confusion to readers, because it seems contradictory to the earlier term 'specified'.

Staff agree with the suggestion and have amended paragraph 20.23(b), as per marked up text.

(d) revenue from providing specified goods or services sold to customers (including governm0ents as purchasers of those goods or services);

(e) membership fees and subscriptions;

(f) interest, dividends and other investment revenue, disaggregated where required by para. 10.30(a) of Section 10 *Financial Instruments*; and

(g) other revenue.

In relation to any amounts of revenue disclosed under (d), a general description of the nature of the goods and services provided to customers shall also be disclosed.

20.24 The categories may be described using terminology appropriate for the entity and need not use the titles used in paragraph 20.23, provided that the separate categories are still disclosed.

20.25 If there is difficulty in determining the category that should be used for a particular transaction, the entity shall use judgement to determine an appropriate classification. This classification shall then be used consistently in future periods so that the information reported is comparable over time.

Volunteer services

20.26 In relation to any volunteer services (such as free professional services) provided to the entity during the reporting period, the entity shall disclose:

(a) a description of those services; ~~and~~

(b) any amount recorded as revenue under the option to do so in paragraph 20.18; and~~.~~

(c) any other information necessary to satisfy the disclosure objective in paragraph 20.27

20.27 The entity shall disclose sufficient descriptive information about volunteer services to enable users of its financial statements to understand the effects of volunteer services on the entity's operations, including the entity's dependence on volunteer services for the achievement of its objectives and any known information about impending significant changes to the nature and amount of volunteer services. The entity shall consider the level of detail necessary to satisfy this disclosure objective, and shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items with substantially different characteristics. Meeting this disclosure objective does not require an entity to quantify the value of volunteer services received.

Deferred revenue obligations

20.28 An entity shall disclose the amount recorded as liabilities in respect of deferred revenue obligations at the reporting date, disaggregated according to:

(a) its current and non-current portions; and

(b) the nature of the transfers, expenditures or using up of assets that is expected to occur in settling the obligations (e.g. transfers of inventories, expenditures to be incurred in rendering services, and expenditures to construct or purchase assets).

Section 21: Expenses

21.1 Expenses are decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims. Expenses shall be recorded upon the recording of a decrease in assets, or an increase in liabilities, of the nature referred to above. Recording expenses is based on accrual accounting, where not all cash payments give rise to an expense (eg purchases of assets or settlements of liabilities paid for with cash, neither of which decreases equity), and some expenses arise in the absence of a cash payment (eg liabilities incurred to pay for employee services consumed, and using up of assets recorded as depreciation). The timing of the recording of various types of expense is specified in topic sections of this [draft] Standard.

21.2 Expenses include only amounts paid and payable by the entity with resources it controls. Amounts paid on behalf of others (that is, as agent of another entity, using resources controlled by that entity) are not expenses of the entity (see paragraphs 20.12 – 20.16).

Commented [A42]: Note to Board members
These marked-up suggested edits are changes since the draft section on *Revenue* was presented to the Subcommittee members to incorporate the drafting of the Section on Financial Instruments to take into account the disclosures required for other investment revenue separately from other items of income or expenses according to the subsequent measurement bases permitted for financial assets held by Tier 3 NFP entities.

Commented [A43]: Note to Board members
A Subcommittee member suggested that, to assist readers, it might be worthwhile clarifying whether paragraph 20.27 is the type of information to be included per paragraph 20.26(a) (i.e., it satisfies "a description of volunteer services") or whether what is required under paragraph 20.27 is in addition to paragraph 20.26.

Considering the feedback, staff have added sub-paragraph 20.26(c) and added "descriptive" to the first line of paragraph 20.27.

Staff consider the information in paragraph 20.27 extends beyond a description of volunteer services, but would also include that description. However, paragraph 20.27 does not wholly encompass paragraph 20.26 because it does not include the information in paragraph 20.26(b). This is reflected in the text of new draft paragraph 20.26(c). Adding "descriptive" to the first line of paragraph 20.27 reinforces that paragraph 20.27 does not require disclosure of the value of volunteer services received.

Section 22: Borrowing Costs

22.1 Borrowing costs are interest and other costs that an entity incurs in connection with the borrowing of funds. An entity shall record all borrowing costs as an expense in profit or loss in the period in which they accrue.

Section 23: Impairment of Assets

Note to Board members

(a) In Agenda Paper 4.7, Subcommittee members were asked whether they consider 'impairment', or a substitute term, should be used in the Tier 3 ED. Subcommittee members that commented agree that the term impairment should be kept for consistency with Tier 2 and other jurisdiction requirements. One member also noted that using a substitute term, even if more intuitive, will cause problems since all the literature is using the term "impairment" and practitioners will be familiar with it. The Tier 3 Standard would need to develop an explanation to a substitute term for impairment, adding volume to the Tier 3 Standard.

Based on the feedback, staff have retained the term 'impairment' in the draft Tier 3 ED.

(b) Subcommittee members considered the second sentence in paragraph 23.1 that staff drafted may be complex to the reader. They propose to simplify the sentence to confine to the scenarios that the Board agreed as being indicators for impairment assessment in the Tier 3 Standard. One Subcommittee member queried if the two scenarios mentioned are the only two in which an impairment is recognised under this standard, and if not, to include them as examples.

Staff agreed with the feedback and revised the sentence as per strikethrough and underlined text. Staff have referred to these indicators in paragraph 23.1 as examples given obsolescence due to technological change or the asset is damaged are examples of paragraph 23.3(a) only.

Question 15 to Board members

A subcommittee member considered that there may be a case for an asset held for sale to be an indicator of impairment which is in line with the Board's thinking for assets that are physically damaged or no longer planning to use at full capacity as impairment indicators. The example they provided was, if a building which cost $1 million and the entity no longer plan to use the building to provide services but intend to sell it and the likely sale price is $800,000, then it's reasonable to expect the asset to be impaired.

Staff analysis and recommendation

As per the staff drafting of impairment requirements in Agenda Paper 4.7 for this meeting, the Board decided at its September 2023 Board meeting to require Tier 3 entities to apply AASB 5 for assets held for sale. However, staff think there is merit to include assets that become held for sale as another indicator of impairment and staff also noted a stakeholder comment received on the DP that an asset that is held for sale should be identified as an indicator of impairment, consistent with *IFRS for SMEs* Accounting Standard requirements. As considered by one Subcommittee member, disposing of an item is arguably similar to an asset that is damaged and no longer planning to use at full capacity. As noted in paragraphs BC 118–BC 119 of the *IFRS for SMEs* in 2009, IASB considered not to require a separate held-for-sale classification for cost-benefit reasons, and considered that an accounting result similar to that of IFRS 5 could be achieved more simply by including intention to sell as an indicator of impairment would ensure that assets are not overstated in the financial statements and disclosure requirement will provide relevant information to users of SMEs' financial statements. As such, staff recommend that asset that are or plan to be held for sale would be included as an impairment indicator. Staff also recommend:

1) that a paragraph, based on the *IFRS for SMEs* Accounting Standard requirements, to reference PPE that are held for sale should be included to cross-reference to the impairment requirements within the draft Standard; and

2) removing the requirement to apply AASB 5 in relation to any assets held for sale in paragraph 1(b)(iii) of Section 1 *Objective, Scope and Application*.

Do Board members agree with staff recommendation that assets that are or plan to be held for sale should be included as an impairment indicator? If not, what do Board members suggest?

Question 16 to Board members

In Agenda Paper 4.7 for this meeting, staff asked Subcommittee members whether they consider it would be proportionate to omit from the Tier 3 ED the requirements of value in use and cash-generating units that would otherwise be included under the Board's proposal in the Tier 3 ED. For the Subcommittee members that commented, they consider it would be proportionate to omit from the Tier 3 ED the requirements of value in use and cash-generating units. However, one member noted the inconsistency that a decline in value in use is an indicator of impairment (due to decline in external demand), yet it would be proposed that value in use would not be considered when calculating recoverable amount. When drafting this section, staff presented two possible options, that is:

Option A: Add the related modifications of Tier 2 requirements proposed in the DP (namely including rebuttable presumption that fair value less cost of disposal is expected to be most appropriate measure of the recoverable amount of a non-financial asset held by a Tier 3 entity). Option A is further simplified from *IFRS for SMEs* Accounting Standard requirements by omitting the detailed guidance on the calculation of the asset's value in use and adding an in-substance definition of the meaning of a 'cash-generating unit'. Option A is compatible with Tier 2 requirements and with the Board's proposal in the DP.

Option B: omit any reference to value in use or cash-generating units, and therefore require the recoverable amount (and related impairments) to be measured at an individual asset level only. Option B is further simplification to not require an estimation of future cash flows over remaining useful life of the asset and to determine a current market-based risk-adjusted discount rate to apply to those estimated future cash flows. Option B is in line with the Board's rebuttable presumption that fair value less cost of disposal is likely to be the most common measurement for determining recoverable amount. Option B would also lead to the reduction of the section relating to impairment losses of goodwill since recoverable amount of goodwill cannot be calculated on a stand-alone (individual asset) basis.

(Refer to Agenda Paper 4.7 for this meeting for further arguments for and against including the requirements regarding value in use and cash-generating unites for Tier 3 NFP entities.)

Subcommittee members preferred Option B based on the reasons in staff analysis in Agenda Paper 4.7. However, one Subcommittee member noted the inconsistency of not including guidance on value in use when calculating recoverable amount yet decline in value in use (due to decline in external demand) will be considered an impairment indicator.

A Subcommittee member favoured not including impairment of goodwill from the Tier 3 Standard given Research Report 19 only found 5% of sampled charities financial statements disclosing intangible assets and goodwill being a subset. Therefore, it is likely goodwill will only impact a few NFP entities, thereby supporting the removal of guidance on impairment of goodwill. Staff will bring analysis of requirements on intangible assets and business combination at a future meeting.

Staff analysis and recommendation

Staff recommend **Option B**, that is, to not include guidance on value in use and cash-generating units within the Tier 3 Standard based on the arguments supporting Option B presented in Agenda Paper as a form of further simplification.

Staff noted the concern from one Subcommittee member about not including guidance on value in use may be inconsistent with the decline in value in use as an impairment indicator. However, as noted in Agenda Paper 4.7, staff consider measuring recoverable amount being its fair value less cost of disposal will be the most likely measurement basis for Tier 3 entities. If the Board agrees with the staff recommendation for Option B, then the effect will mean the shaded text will not be included in the drafting of the ED.

Do Board members agree with staff recommendation, i.e. Option B above? If not, what do Board members suggest?

Objective and Scope

23.1 An impairment loss occurs when the carrying amount of an asset exceeds its recoverable amount. This may occur for example ~~when an asset's carrying amount needs to reduce by a greater extent than any recorded depreciation or amortisation because it is expected to produce less benefits than previously expected~~ if the asset becomes obsolete due to technological change or the asset is damaged.

23.2 This section shall be applied in accounting for the impairment of all assets other than the following, for which other sections of this Standard establish impairment requirements:

(a) financial assets within the scope of Section 11 Financial Instruments, which establishes impairment requirements for those assets; and

(b) non-financial assets regularly revalued to fair value in accordance with paragraph 15.11 or [TBU: XX] [i.e. the paragraphs setting out the revaluation model in the sections on Property, Plant and Equipment and Intangible Assets other than Goodwill].

Commented [A44]: Note to Board members
A Subcommittee member noted the presumption for not including a specific exclusion for when fair value is used as an asset's deemed cost since the paragraph references will capture this.
Staff agree that a specific exclusion for when fair value is used as an asset's deemed cost is not necessary as paragraph 15.4 provides that all items of PPE shall initially be measured at cost with further explanation in paragraph 15.5 being the purchase price and any other considerations. Only donated PPE's cost can either be cost or fair value in accordance with Section 11. Staff consider this is sufficient for Tier 3 entities' guidance without the need to include reference to deemed cost in the Tier 3 ED.

Assessing possibility of impairment of non-financial assets

23.3 At each reporting date, an entity shall assess the possibility that any non-financial assets (such as inventories and property, plant and equipment) are impaired when, and only when:

(a) they have been damaged physically or are perishable items that spoiled or became obsolete; or

(b) the entity has changed its strategy or been affected by a reduction in external demand for its goods or services and in either case the asset's capacity to sell or provide goods or services might have been affected adversely as a result.

If any of the events in (a) ~~and~~or (b) has occurred, the entity shall identify whether the asset's carrying amount is impaired by determining whether it exceeds the asset's recoverable amount (which is measured in accordance with paragraphs 23.4 – 23.5 (if inventory) or paragraphs 23.6 – 23.10 (for assets other than inventory)). If such an excess exists, ~~it shall be removed by reducing~~ the asset's carrying amount shall be reduced to ~~carrying amount to~~ its recoverable amount and the reduction is record~~ing~~ed as an impairment loss in accordance with paragraph 23.11.

Measuring recoverable amount

Inventories

23.4 Subject to paragraph 23.5, the recoverable amount of an item of inventory (or group of similar items of inventory) is the selling price of the item or group less the costs to complete and sell it.

23.5 The recoverable amount of inventories held for distribution is their cost less their loss of service potential. The loss of service potential shall be measured by reference to the more ~~readily evident~~ easily determined of the cost or replacement cost of those inventories held that no longer are useful for distribution, based on the judgement of the entity's management. Examples of inventories held that no longer are useful for distribution are items that are damaged or outdated.

Other non-financial assets

23.6 The recoverable amount of a non-financial asset other than inventory is the higher of its fair value less costs to sell and its value in use. There is a rebuttable presumption that fair value less costs to sell is expected to be the most appropriate measure of such a non-financial asset's recoverable amount. Paragraphs 23.7 – 23.10 apply to non-financial assets other than inventories.

23.7 For some assets, it might be impossible to estimate their recoverable amount as an individual asset because their value in use cannot be measured separately from the value in use of other assets (i.e. the asset does not generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets) and it is necessary to consider their value in use when measuring the asset's recoverable amount (because it cannot be estimated to be close to the asset's fair value less costs to sell, and might exceed that amount). In such cases, recoverable amount is determined for the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets (the asset's cash-generating unit). References in paragraphs 23.8–23.10 to an asset should be read as references also to an asset's cash-generating unit.

23.8 It is not always necessary to determine both an asset's fair value less costs to sell and its value in use if an indicator of impairment in paragraph 23.3 exists. If either of these amounts exceeds the asset's carrying amount, the asset is not impaired and it is not necessary to estimate the other amount.

Fair value less costs to sell

23.9 Section 11 *Fair Value Measurement* provides guidance on fair value measurement.

Value in use

23.10 Value in use is the present value of the future cash flows expected to be derived from an asset. This present value calculation involves the following steps:

(a) estimating the future cash inflows and outflows expected to be derived from:

(i) continuing use of the asset; and

(ii) disposal of the asset at the end of its useful life in an arm's length transaction between knowledgeable, willing parties; and

(b) applying a current market-based risk-adjusted discount rate to those future cash flows.

To estimate the cash flows expected from continuing use of the asset, the entity may elect to use any recent financial budgets or forecasts, if available.

Commented [A45]: Note to Board members
A Subcommittee member noted the word drafted here should be and "or" rather than "and".
Staff agree and revised the drafting accordingly.

Commented [A46]: Note to Board members
Subcommittee members considered possible re-wording of the sentence to, 'If such an excess exists, the asset's carrying amount shall be reduced to its recoverable amount and recording an impairment loss'. The reduction is recorded as an impairment loss. A Subcommittee member also suggested to including or cross-referencing to where the impairment loss would be recognised.
Staff agree and have amended the sentence to combine the suggestion as per the revised drafting.

Commented [A47]: Note to Board members
A Subcommittee member queried whether inventories available for distribution will need to be defined to distinguish from assets listed in paragraph 23.2. They also consider "more readily evidence" can be further simplified such as "more easily determined" or "more easily calculated".
Another member suggested the definitions can be included in the glossary and preferred alignment with existing definitions in Tier 1/Tier 2 requirements if these are already defined terms in the Australian Accounting Standards.
In relation to "inventories held for distribution", paragraphs 13.1 and 13.2 of this draft ED 13.1 provides some guidance of what are inventories held for distribution. Staff have also included a glossary to define inventories held for sale, aligning with Tier 1/Tier 2 definitions.
Staff initially proposed the term readily evidence because the term 'readily' is present in a number of AAS, albeit it is not defined, including:
(a) "readily convertible" when discussing cash equivalents in AASB 1060; or
(b) AASB 13 and AASB 15 use terms 'readily accessible', 'readily available' and 'resources readily available'; or
(c) 'readily determined' in leases.
However, as the term is not defined and may be open to interpretation, staff see merit to further simplifying the term "readily evident" as per Subcommittee members' suggestion and revised the drafting to "more easily determined".

Recording impairment losses

23.11 An entity shall record an impairment loss immediately in profit or loss, unless the asset is carried at a revalued amount in accordance with the revaluation model in Section 15 Property, Plant and Equipment or TBU Section 16 *Intangible Assets other than Goodwill*]. Any impairment loss of a revalued asset shall be treated as a revaluation decrease in accordance with paragraph ~~17.15D [*cross-reference to be updated to align with revised numbering of section on Property, Plant and Equipment*]~~ 15.13.

Commented [A48]: Note to Board members
A Subcommittee member considered highlighting in the Basis for conclusions how the impairment loss of a revalued asset being a revaluation decrease corresponds with paragraph 23.2(b) which excludes non-financial assets regularly revalued to fair value.

Staff will bring the drafting of Basis for conclusions at a future meeting.

Recording and measuring an impairment loss for a cash-generating unit

23.12 An impairment loss shall be recorded for a cash-generating unit if, and only if, the recoverable amount of the unit is less than the carrying amount of the unit. The impairment loss shall be allocated to reduce the carrying amount of the assets of the unit in the following order:

(a) first, to reduce the carrying amount of any goodwill allocated to the cash-generating unit; and

(b) then, to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the cash-generating unit.

23.13 However, an entity shall not reduce the carrying amount of any asset in the cash-generating unit below the highest of:

(a) its fair value less costs to sell (if determinable);

(b) its value in use (if determinable); and

(c) zero.

23.14 Any excess amount of the impairment loss that cannot be allocated to an asset because of the restriction in paragraph 23.13 shall be allocated to the other assets of the unit pro rata on the basis of the carrying amount of those other assets.

Additional requirements for impairment of goodwill

23.15 Goodwill, by itself, cannot be sold. Nor does it generate cash flows to an entity that are independent of the cash flows of other assets. Consequently, the fair value of goodwill cannot be measured directly; it must be derived from measurement of the fair value of the cash-generating unit(s) of which the goodwill is a part.

23.16 For the purpose of impairment testing, goodwill acquired in a business combination shall, from the acquisition date, be allocated to each of the acquirer's cash-generating units that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

23.17 Part of the recoverable amount of a cash-generating unit is attributable to the non-controlling interest in goodwill. For the purpose of impairment testing a non-wholly-owned cash-generating unit with goodwill, the carrying amount of that unit is notionally adjusted, before being compared with its recoverable amount, by grossing up the carrying amount of goodwill allocated to the unit to include the goodwill attributable to the non-controlling interest. This notionally adjusted carrying amount is then compared with the recoverable amount of the unit to determine whether the cash-generating unit is impaired.

Disclosures

23.18 For each class of assets indicated in paragraph 23.19, an entity shall, subject to paragraph 23.20, disclose the amount of impairment losses recorded in profit or loss during the period and the line item(s) in the statement of comprehensive income (and in the income statement, if presented) in which those impairment losses are included.

23.19 An entity shall disclose the information required by paragraph 23.18 for each of the following classes of asset:

(a) property, plant and equipment (including investment property accounted for by using the cost method);

(b) goodwill;

(c) intangible assets other than goodwill;

(d) investments in associates; and

(e) investments in joint~~ly controlled entities~~ ventures.

23.20 For non-financial assets other than inventories, impairment losses recorded in profit or loss may be disclosed jointly (in a combined total) with depreciation/amortisation expense.

Section 24: Employee Benefits [TBU]

Scope of this section

24.1 [TBU]

Section 25: Income Taxes

25.1 If the entity pays income tax, it shall record income tax expense for the period for the income tax payable for the period. That amount shall, in descending order, be based on the entity's tax assessment for the period (if received by the date the financial statements are authorised for issue), its tax return for the period (if completed by the date the financial statements are authorised for issue) or an estimate of the amounts to be included in that tax return. The entity's recorded liability for income tax at the end of the reporting period shall be measured as the sum of the estimated income tax ~~obligation~~ payable for the period and any income tax assessed in respect of a prior period (or periods) and unpaid at the end of the reporting period.

Commented [A49]: **Note to Board members**
A Subcommittee member noted if income tax payable and income tax obligation are one and the same, then it may be clearer for the reader if "income tax payable" is used here.

Staff agree and have redrafted accordingly.

25.2 The entity's income tax expense recorded for the period shall be presented as a line item in the statement of profit or loss and other comprehensive income. The entity's liability for income tax recorded as at the end of the reporting period shall be presented as a line item in the statement of financial position.

Section 26: Foreign Currency Translation

Note to Board members

In Agenda Paper 4.10, staff asked Subcommittee members whether they agreed with staff's suggestion to include more extensive (but brief) guidance on foreign currency translation than that foreshadowed in the DP, to assist readers of the Tier 3 ED to understand better the Board's proposed requirements. The Subcommittee members that commented disagree with adding the extra paragraph as they do not consider the issue is widespread enough to warrant inclusion in the Tier 3 ED and, if additional guidance/examples are developed, can be included as educational materials instead.

In response to the feedback, staff have redrafted the guidance to conform with the DP proposal for foreign currency translation (see paragraph 5.208 in the DP) based on the NZ Tier 3 Standard. Staff will consider whether to recommend including the additional paragraphs as illustrative examples to accompany Tier 3 requirements.

26.1 All amounts shall be presented in Australian dollars. If the entity has transactions or balances that are not denominated in Australian dollars, it shall translate their amounts to Australian dollars as ~~specified in paragraphs X7.2 – X7.6 and make the disclosures specified by paragraph X7.73.~~ follow:

~~X7.2 Depending on the circumstances, translating transactions and balances denominated in a foreign currency involves one or more of the following steps:~~

(a) ~~translating the changes in assets and/or liabilities, and any related items of income or expense, arising from foreign currency transactions to record those transactions as at the transaction date. These are translated using the spot exchange rate (ie the rate for immediate delivery) between the foreign currency and Australian dollars prevailing on the date of the~~ transaction are to be translated using the exchange rate on the date the revenue, expense or cash flow occurs; and

~~(b) adjustments to the translated amounts of foreign currency receivables and payables (ie amounts receivable or payable for specified amounts of foreign currency) to record the effect of movements in spot exchange rates occurring since the most recent translation of those items into Australian dollars. These adjustments arise upon the following required steps:~~ Monetary asset and liability balances are to be translated using the exchange rate at balance date.

~~(i) translating balances of foreign currency receivables and payables into Australian dollars using the spot exchange rate at the end of the reporting period; and~~

~~(ii) translating transactions that settle all or part of each foreign currency receivable and payable, using the spot exchange rate at each settlement date.~~

~~X7.3 For example, if a charity buys materials for an overseas project that are denominated in a foreign currency, step (a) would be the only foreign currency translation step if the materials were paid for in cash. If the materials were bought on credit (to be settled in a foreign currency), depending on whether the account payable is settled in the same period as that of the purchase, either or both steps (b)(i) and (b)(ii) would need to be performed to complete the foreign currency translations in relation to that purchase. This is because a foreign~~

~~currency payable would arise from the purchase transaction. Translation of foreign currency receivables and payables is discussed in paragraph X7.4.~~

~~X7.4 For any particular foreign currency receivable or payable, depending on the circumstances, either or both of the translations (and resulting translation adjustments) in paragraphs X7.2(b)(i) and (b)(ii) will be required over the term of that item. If the receivable or payable originates and is settled in the same period (eg as may often occur with trade receivables and payables), only the retranslation in paragraph X7.2(b)(ii) will be required. If the receivable or payable originates and is settled in different periods (eg it is a long-term loan), its retranslation in accordance with paragraph X7.2(b)(i) will be required at the end of each reporting period it remains outstanding, and its settlement will be translated in accordance with paragraph X7.2(b)(ii) during the period(s) in which it is settled in full (or in parts).~~

~~X7.5 Upon each retranslation using different exchange rates referred to in paragraph X7.2(b), resulting foreign currency exchange gains or losses are recorded in profit or loss in the period in which those retranslations occurred. Assets bought or originated in return for consideration paid in a foreign currency, other than foreign currency accounts receivable, are not retranslated after the transaction giving rise to their recording. This applies even if the asset (eg an item of inventory or property, plant and equipment) might be sold for consideration receivable in a foreign currency. The foreign currency exchange gain or loss implicit in the total gain or loss on any such sale is not accounted for or disclosed separately.~~

~~X7.6 For practical reasons, an exchange rate that approximates the rate actually prevailing at the date of a transaction may be used (eg an average rate for a week or month may be used for all transactions in a particular foreign currency occurring during that period), provided that exchange rate fluctuations are not so great that applying an approximate exchange rate would give rise to a significant risk of material misstatement.~~

~~**Disclosures**~~

~~X7.7 An entity shall disclose the net amount of exchange differences recorded in profit or loss during the period in accordance with paragraph X7.2(b), except for exchange differences arising on financial instruments measured at fair value through profit or loss in accordance with Section XX [*the section on Financial Instruments*].~~

Section 27: Events occurring after the Reporting Period

27.1 Events occurring after the reporting period are events, favourable and unfavourable, that occur between the end of the reporting period (eg financial year) and the date when the financial statements are authorised for issue by the entity's management.

27.2 An entity shall adjust the amounts recorded in its financial statements and update the related disclosures to reflect events that occur after the reporting period and provide evidence of conditions that existed at the end of the reporting period. The following are examples of events that require an entity to adjust the amounts recorded in its financial statements, or to record items not previously recorded:

(a) the settlement after the end of the reporting period of a court case confirming that the entity had a liability at the end of the reporting period because the disputed event occurred on or before that date.

(b) the receipt of information after the end of the reporting period indicating that an asset was impaired or damaged at that date. For example:

(i) the bankruptcy of a debtor occurring after the end of the reporting period usually confirms that a loss already existed at that date on a receivable account, and that the entity needs to adjust the carrying amount of the receivable account; and

(ii) the disposal of physically damaged inventories or perishable items after the end of the reporting period might provide evidence about their estimated selling price less costs to complete and sell at that date.

(c) the discovery of fraud or errors showing that the financial statements are incorrect.

27.3 An entity shall not adjust the amounts recorded but instead, provide disclosures in accordance with paragraph 27.4 in its financial statements to reflect events after the end of the reporting period indicating conditions that arose after that date. The following are examples of such events ~~(see also paragraph 27.5)~~:

(a) the entity's management decides, after the end of the reporting period, to make further grants to the community;

(b) purchases and disposals of assets occurring after the end of the reporting period; and

Commented [A50]: Note to Board members
A Subcommittee member suggested rephrasing this to "physically damaged inventories", which relates back to the simplified indicators of impairment of non-financial assets.

Staff agree and have amended the drafting including adding perishable items being evidence of assets being impaired.

(c) a decision made by a lender after the end of the reporting period to forgive some amounts borrowed by the entity.

Disclosures

27.4 Where material events occur after the end of the reporting period and indicate conditions that arose after that date (see paragraph 27.3), the entity shall disclose the following information in the notes for each material category of such events:

(a) the nature of the event;

(b) an estimate of its financial effect, or a statement that such an estimate cannot be made; and

(c) the effect, if any, on the entity's ability to continue operating.

The disclosures shall reflect information that becomes known after the end of the reporting period but before the financial statements are authorised for issue.

~~27.5 The following are examples of events of the nature referred to in paragraph 27.4 that, if material, would require disclosure of the information specified in that paragraph:~~

~~(a) the destruction of a building by a fire after the end of the reporting period;~~

~~(b) the entity entering into significant commitments or contingent liabilities after the end of the reporting period, for example issuing significant guarantees after that date; and~~

~~(c) commencement of major litigation against the entity arising solely from events occurring after the end of the reporting period.~~

27.65 An entity is not required to disclose comparative information about events occurring after the end of the previous reporting period.

Commented [A51]: Note to Board members
A Subcommittee member suggested further simplification to combine paragraph 27.3 (a) to (c) on examples where no adjustments would be required with paragraph 27.5 on events that require disclosures of information.

Staff agree and have included in paragraph 27.3 the requirement to provide disclosures in accordance with paragraph 27.4 and removed paragraph 27.5 to further streamline the drafting of the requirements.

Section 28: Related Party Disclosures

Note to Board members

In Agenda Paper 4.17, staff asked Subcommittee members whether they agreed with the overall length of the draft section is appropriate and whether they have any other suggestions for omitting text to achieve further simplification of this draft section of the Tier 3 ED.

The Subcommittee members that commented agreed with the overall length in general but provided comments relating to specific paragraphs within this section.

In addition, a Subcommittee member provided editorial suggestions for paragraph 28.7 to state 'paid, payable or provided' to be consistent with paragraph 28.6. Staff agree and have made editorial changes as per strikethrough and underlined text.

Question 17 to Board members

A Subcommittee member proposed, based on the Board's decision at its November 2023 Board meeting (refer to Action Alert No. 227) not to require the identification of controlling relationships, to consider whether the disclosure of a reporting entity's subsidiaries is necessary and preferred the requirement to be removed from the ED.

Staff analysis and recommendation

As per Agenda Paper 4.17, staff suggested retaining paragraph 33.5 of the *IFRS for SMEs* Accounting Standard requirements because it is the same text as AASB 1060 paragraph 192 and there were no apparent Tier 3 NFP-specific reasons to depart given the Board decided at its November 2023 Board meeting for consistent Tier 2 disclosure requirements, except for donations received from a related party unless there is evidence the donation can influence the entity's activities or use of resources.

Staff also consider that, even though the Board decided to allow entities not to identify controlling relationships and/or elect to prepare separate financial statements, the entities would be required to disclose their notional relationships as per draft paragraph 8.32 which includes the name and nature of the relationship. However, a parent entity that prepares separate financial statements would not be required to make the disclosures in paragraph 8.32. Hence staff consider it would be useful for those parent entities to disclose the subsidiaries that they control. Additionally, the disclosures in paragraph 28.4 would be useful to users to ascertain whether the reporting entity's resources are controlled by another entity.

In light of the feedback, staff consider that there are two possible options to address the concern:

Option A: Delete the disclosure requirements. This option would address the Subcommittee member's feedback and provide further simplification for Tier 3 entities. However, users may be disadvantaged by not being provided information about the subsidiaries of a Tier 3 parent entity that elected to prepare consolidated financial statements or information about the ultimate parent (if any) who controls the Tier 3 reporting entity.

Option B (staff recommendation): retain paragraph 28.3 but specify that a Tier 3 entity disclose its subsidiaries (if identified) or its notable relationships and specify that the disclosure is not necessary if the information has already been disclosed elsewhere in the financial statements. For paragraph 28.4, staff suggest that a Tier 3 entity may elect to provide the disclosures instead. Staff consider Option B would still address the Subcommittee member's concern while ensuring users are still be provided with useful information. If the Board agrees with Option B, staff suggest the draft should be reflected as "*An entity ~~shall~~ may disclose the name of its parent (if identified) and, if different, the ultimate controlling party (if identified). If neither the entity's parent nor the ultimate controlling party produces financial statements available for public use, the name of the next most senior parent that does so (if any) shall also be disclosed.*"

Do Board members agree with the staff recommendation in Option B? If not, what do the Board members suggest?

Question 18 to Board members

A Subcommittee member proposed not to require the disclosures in paragraphs 28.6 and 28.7 as they were persuaded how the disclosure of KMP compensation would be useful to Tier 3 users. Additionally, they consider KMP compensation paid by another entity would not be common for Tier 3 entities. They also consider the disclosure requirements can be mandated by regulators such as the ACNC if deemed necessary.

Staff analysis and recommendation

As per Agenda Paper 4.17 at this meeting, staff suggested retaining the requirement to disclose the total amount of key management personnel (KMP) compensation because it is required by AASB 1060 paragraph 194 and there is no apparent Tier 3 NFP-specific reason to depart given the Board decided at its November 2023 Board meeting on consistent Tier 2 disclosure requirements as noted in question 17 above.

Staff considered that in the government's review of the ACNC legislation (*Strengthening for Purpose: Australian Charities and Not-for-Profits Commission Legislation Review 2018*, pg. 61), the report highlighted a specific concern regarding transparency of the remuneration paid to charity responsible persons and senior executives and recommended the need for KMP remuneration disclosures. However, staff noted that the Government's response to the legislative review, followed by the relevant amendments to ACNC legislation, was to effectively mandate KMP remuneration disclosures (in an aggregated total) for large charities from the 2022 Annual Information Statement reporting period. Staff also note there are exemptions with reporting to the ACNC regarding KMP remuneration disclosures. For medium and large charities that prepare:

(a) SPFS are required to comply with specified accounting standards including AASB 124 or AASB 1060, medium charities are exempt from disclosing KMP remuneration (see paragraph 60.30(4)(a) of the ACNC Regulations);

(b) GPFS (whether Tier 1 or Tier 2) are required to disclose KMP remuneration in accordance with AASB 124 or AASB 1060. No exemption applies; and

(c) large charities preparing SPFS with only one remunerated KMP individual are exempt from disclosing KMP remuneration (see paragraph 60.30(4)(b) of the ACNC Regulations).

However, staff acknowledge that ACNC is only one of the regulators of NFP entities as per Research Report 10 *Legislative and Regulatory Financial Reporting Requirements.* Staff also noted that not requiring KMP remuneration disclosures would be inconsistent with Tier 1/Tier 2 requirements and users may not be provided with useful information.

On balance, considering the feedback, staff recommend deleting the KMP disclosure requirements in paragraphs 28.6–28.7, given they are only required by large registered charities (i.e. annual revenue over $3 million) to provide further simplification for Tier 3 entities. Subject to the Board's decision, staff will remove the disclosure requirements.

Do Board members agree with staff recommendation and, as per feedback from a Subcommittee member, not to require disclosures of KMP compensation in paragraphs 28.6–28.7 for the Tier 3 ED? If not, what do Board members suggest?

Question 19 to Board members

A Subcommittee member questioned the relevance of the exemption for government-related entities to Tier 3 entities in paragraph 28.17.

Staff are not aware if there would be any Tier 3 entities that are controlled by a state government (based on Research Report 19) nor did staff receive any feedback on the DP outreach in this regard.

In view of the Subcommittee member's comment of the relevance to Tier 3 entities and to economise the length of this Section, staff recommend deleting the exemption for government-related entities in the draft Tier 3 ED.

Do Board members agree with staff recommendation to delete the exemption for government-related entities? If not, what do Board members suggest?

Scope of this section

28.1 This section requires an entity to include in its financial statements the disclosures necessary to draw attention to the possibility that its financial position and profit or loss have been affected by related party relationships and transactions and outstanding balances with related parties (eg without a related party relationship, transactions might not have been undertaken on terms and conditions that differed from those prevailing in arm's length transactions).

28.2 In general terms, a person or entity related to the reporting entity ('related party') is related by virtue of a relationship of significant (or greater) influence, being a member of key management personnel or a close family member of a person qualifying as a related party. A 'related party' is defined in the Appendix to this section; that definition applies to all assessments of when a related party of the reporting entity exists.

Disclosures

Disclosure of controlling party relationships

28.3 Relationships between the reporting entity and any entities identified as its subsidiaries shall be disclosed regardless of whether:

(a) related party transactions occurred during the period; and

(b) consolidated financial statements were prepared for the reporting entity and its subsidiaries.

28.4 An entity shall disclose the name of its parent and, if different, the ultimate controlling party. If neither the entity's parent nor the ultimate controlling party produces financial statements available for public use, the name of the next most senior parent that does so (if any) shall also be disclosed.

28.5 In considering each possible related party relationship, an entity shall assess the substance of the relationship and not merely the legal form.

Disclosure of key management personnel compensation

28.6 An entity shall disclose the total amount of compensation paid, payable or provided to key management personnel for their services provided to the entity during the period.

28.7 If an entity receives key management personnel services from another entity (the 'management entity'), the entity is not required to disclose the amount of compensation paid, ~~or~~ payable or provided by the management entity to those personnel. However, the amounts incurred by the entity for the provision of key management personnel services by a separate management entity shall be disclosed.

Disclosure of related party transactions

28.8 A related party transaction is a transfer of resources (whether cash, goods or services) or obligations between a reporting entity and a related party, regardless of whether:

(a) a price is charged; or

(b) it occurs on terms equivalent to those prevailing in arm's length transactions.

28.9 Examples of common related party transactions include, but are not limited to:

(a) transactions between the entity and its principal owner(s);

(b) transactions between the entity and another entity when both entities are under the common control of a single entity or person; and

(c) transactions in which an entity or person that controls the reporting entity incurs expenses directly that otherwise would have been borne by the reporting entity.

28.10 If an entity has related party transactions, it shall, subject to the exemption in paragraph 28.12, disclose information about:

(a) the nature of the related party relationship; and

(b) the transactions, outstanding balances and commitments

necessary for an understanding of the potential effect of the relationship on the financial statements.

Commented [A52]: Note to Board members
A Subcommittee member considers it is unclear whether the minimum disclosure requirements in paragraph 28.11 will meet the requirements specified in paragraph 28.10(a) to disclose the nature of the related party relationships.

Staff agree and have edited paragraph 28.11 to include to subparagraph (b) when referencing paragraph 28.10.

28.11 At a minimum, the disclosures made in accordance with paragraph 28.10(b) shall include:

(a) the amount of the transactions;

(b) the amount of outstanding balances and:

(i) their terms and conditions, including whether they are secured and the nature of the consideration to be provided in settlement; and

(ii) details of any guarantees given or received;

(c) provisions for uncollectable receivables related to the amount of outstanding balances; and

(d) the expense recognised during the period in respect of bad or doubtful debts due from related parties.

Those disclosure requirements are in addition to the requirements in paragraph 28.6 to disclose key management personnel compensation.

33.12 The disclosures in paragraphs 28.10 and 28.11 need not be made for donations received by the entity from a related party, unless evidence indicates the donations could influence the entity's activities or use of resources. An example of such evidence is when a donation is received on the condition that the entity must consequently purchase goods or services from a specified supplier.

28.13 An entity shall make the disclosures required by paragraphs 28.10 and 28.11 separately for each of the following four categories:

(a) entities with control, joint control or significant influence over the entity;

(b) entities over which the entity has control, joint control or significant influence;

(c) key management personnel of the entity or its parent (in the aggregate); and

(d) any other related parties having a notable relationship (as defined in paragraph 8.29 of Section 8 *Consolidated and Separate Financial Statements*) with the reporting entity not categorised under (a) – (c).

If an entity has made some of, or all, these disclosures about notable relationships for the same reporting period in accordance with paragraph 8.32, there is no need to repeat them in complying with this paragraph.

Commented [A53]: Note to Board members
As per Question 17, the Subcommittee considered not requiring separately disclosing the information required in paragraphs 28.10 to 28.11 into the four categories listed if the Board decides not to require entities to disclose the requirements in paragraphs 28.3 and 28.4.

If the Board decides not to require the disclosures in paragraphs 28.3 and 28.4, staff recommend not to require the disaggregation of the disclosures required in paragraphs 28.10-28.11 separately. Staff also think the disclosures required by paragraph 28.10(a) should provide similar information in paragraph 28.13.

28.14 The following are examples of transactions that shall, subject to the exemption in paragraph 28.12, be disclosed if they are with a related party:

(a) purchases, sales or transfers of:

(i) goods (finished or unfinished); and

(ii) property and other assets;

(b) rendering or receiving services;

(a) lease payments;

(b) transfers under finance arrangements (including loans and equity contributions in cash or kind);

(c) provision of guarantees or collateral;

(d) commitments to do something if a particular event occurs or does not occur in the future; and

(e) settlement of liabilities on behalf of the entity or by the entity on behalf of another party.

28.15 An entity shall not state that related party transactions were made on terms equivalent to those that prevail in arm's length transactions unless such terms can be substantiated.

28.16 An entity may disclose items of a similar nature in the aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the entity's financial statements.

Exemption for government-related entities

28.17 An entity is exempt from the disclosure requirements of paragraphs 28.10 and 28.11 in relation to:

(a) a state (a national, regional or local government) that has control, joint control or significant influence over the reporting entity; and

(b) another entity that is a related party because the same state has control, joint control or significant influence over both the reporting entity and the other entity.

However, the entity must still disclose a parent-subsidiary relationship as required by paragraph 28.4.

Section 29: Transition to Australian Accounting Standards: Simplified Accounting [TBU]

Scope of this section [TBU]

Commencement of the legislative instrument

x For legal purposes, this legislative instrument commences on … [date].

Appendix A
Glossary of terms [TBU]

This Appendix is an integral part of the Standard

accounting estimates	Monetary amounts in financial statements that are subject to measurement uncertainty.
accounting policies	The specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements
~~**accounting profit**~~	~~Profit or loss for a period before deducting tax expenses.~~
accumulating compensated absences	Compensated absences that are carried forward and can be used in future period if the current period's entitlement is not used in full.
~~**active market**~~	~~A market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.~~
acquiree	The business or businesses that the acquirer obtains control of in a business combination.
acquirer	The entity that obtains control of the acquiree.
~~**aggregation**~~	~~The adding together of assets, liabilities, equity, income or expenses that have shared characteristics and are included in the same classification.~~
~~**agricultural activity**~~	~~The management by an entity of the biological transformation of biological assets for sale, into agricultural produce or into additional biological assets.~~
~~**agricultural produce**~~	~~The harvested product of the entity's biological assets.~~
~~**amortised cost of a financial asset or financial liability**~~	~~The amount of which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectability.~~
~~**asset**~~	~~A present economic resource controlled by the entity as a result of past events.~~
~~**associate**~~	~~An entity, including an unincorporated entity such as a partnership, over which the controlling NFP entity has significant influence and that is neither a controlled entity nor an interest in a joint arrangement.~~
~~**bearer plant**~~	~~A bearer plant is a living plant that:~~ ~~(a) is used in the production or supply of agricultural produce;~~ ~~(b) is expected to bear produce for more than one period; and~~ ~~(c) has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales.~~
~~**biological asset**~~	~~A living animal or plant.~~
~~**borrowing costs**~~	~~Interest and other costs incurred by an entity in connection with the borrowing of funds.~~
business	An integrated set of activities and assets that is capable of being conducted and managed for the purpose of: (a) providing goods or services to customers;

Commented [A54]: <u>Note to Board members</u>
Staff have included the work-in-progress glossary based on the *IFRS for SMEs* Accounting Standard requirement of its glossary with markups to definitions to align with the body of the Standard. The glossary contains definitions used in business combination and intangible assets subject to the Board's consideration of the Tier 3 requirements and other topics not yet drafted by staff (i.e. employee benefits and changes in accounting policies and estimates and accounting for prior period accounting errors) that will be updated for the Board to consider at a future meeting. Staff have strikethrough definitions for the following reasons:
(a) To remove definitions that are already defined within the Sections (e.g. the term associate is already defined in Section 13).
(b) The term is not used within the Tier 3 ED (e.g. active market has been removed from the fair value measurement section).
(c) Tier 3 Standard will not include the requirements (e.g. biological assets will apply the Tier 2 requirements)
(d) Definitions and terms defined in the conceptual framework as the Tier 3 Standard does not include a simplified version of the conceptual framework (e.g. assets or enhancing qualitative characteristics are terms defined in the conceptual framework).
Staff also included comment boxes with note to Board members where Subcommittee members provided suggestions for the definitions.

(b) generating investment income (such as dividends or interests); or

(c) generating other income from ordinary activities.

business combination — A transaction or other event in which an acquirer obtains control of on or more businesses.

carrying amount — The amount at which an asset, or liability or equity is recognised in the Statement of Financial Position.

cash — Cash on hand and demand deposits.

cash equivalent — Short-term, highly liquid investment that are readily convertible to known amounts of cash that are subject to an insignificant risk of changes in value.

cash flows — Inflows and outflows of cash and cash equivalents.

cash-generating unit — The smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets

~~**Cash-settled share-based payment transaction**~~ — ~~A share-based payment transaction in which the entity acquires goods or services by incurring a liability to transfer cash or other assets to the supplier of those goods or service for amounts that are based on the price (or value) of equity instruments (including shares or share options) of the entity or another group entity.~~

class of assets — A grouping of assets of a similar nature and use in an entity's operations.

~~**classification**~~ — ~~The sorting of asset, liabilities, equity, funds in net assets, income or expenses on the basis of shared characteristics for presentation and disclosure purpose.~~

close members of the family of a person — Those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity, including:

(a) that person's children and spouse or domestic partner;

(b) children of that person's spouse or domestic partner; and

(c) dependents of that person or that persons' spouse or domestic partner.

~~**combined financial statements**~~ — ~~Financial statements of a reporting entity that comprises two or more entities that are not all linked by a parent-subsidiary relationship.~~

component of an entity — Operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity .

compensation — Compensation includes all employee benefits (as defined in Section 24 *Employee Benefits*). Employee benefits include all forms of consideration paid, payable or provided by the entity, or on behalf of the entity (for example, by its parent or by a shareholder), in exchange for services rendered to the entity. It also includes such consideration paid on behalf of a parent of the entity in respect of goods or services provided to the entity.

~~**compound financial instrument**~~ — ~~A financial instrument that, from the issuer's perspective, contains both a liability and an equity element.~~

~~**consolidated financial statements**~~ — ~~The financial statements of a controlling not-for-profit entity and its controlled entities presented as those of a single economic entity~~

~~**constructive obligation**~~ — ~~An obligation that is not legally binding (although it might become legally binding in the future) and derives from an entity's actions where:~~

~~(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and~~

~~(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.~~

~~**contingent asset**~~	~~A possible asst that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.~~
contingent consideration	Usually, an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquiree as part of the exchange for control of the acquiree if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to return of previously transferred consideration if specified conditions are met.
~~**contingent liability**~~	~~A possible obligation, to pay money that the existence of which will be confirmed only by the occurrence or non-occurrence of an uncertain future event outside the entity's control; or an obligation that has arisen but is not recorded because: (i) it is not probable that the entity will have to settle the obligation; or (ii) the amount of the obligation cannot be estimated reliably (that is, the entity is too uncertain of the amount of the obligation).~~
contract	An agreement between two or more parties that creates enforceable rights and obligations.
~~**contract asset**~~	~~A not-for-profit entity's right to consideration in exchange for goods or services that the not-for-profit entity has transferred to a customer when that right is conditioned on something other than the passage of time (for example, the not-for-profit entity's future performance).~~
~~**contract liability**~~	~~A not-for-profit entity's obligation to transfer good or services to a customer or which the not-for profit entity has received consideration (or the amount is due) from the customer~~
contractual interest rate	The rate that is specified in the contract upon a loan agreement or financial contract between a borrower and a lender. The contractual interest rate does not take into consideration any fees, points paid or received, transaction costs and other premiums or discounts on acquisition of the financial instrument.
~~**control (of an entity)**~~	~~A controlling not-for-profit entity controls an investee (controlled entity) when the controlling not-for-profit entity is exposed or has the rights to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.~~
~~**credit loss**~~	~~The difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (that is, all cash shortfalls), discounted at the original effective interest rate.~~
~~**current tax**~~	~~The amount of income tax payable (recoverable) in respect of the taxable profit (tax loss) for the current period or past periods.~~
~~**customer**~~	~~A party that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for considerations.~~
date of initial application	The date an entity first applies the first edition of the Tier 3 Standard.
date of transition to the Tier 3 Standard	The beginning of the earliest period for which an entity presents full comparative information under the Tier 3 Standard in its first financial statements that comply with the Tier 3 Standard.
~~**deductible temporary differences**~~	~~Temporary differences that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled~~

~~**deferred tax**~~	~~Income tax payable (recoverable) in respect of the taxable profit (tax loss) for future periods as a result of past transactions or events.~~
~~**deferred tax assets**~~	~~The amounts of income tax recoverable in future periods in respect of:~~ ~~(a) deductible temporary differences;~~ ~~(b) the carryforward of unused tax losses; and~~ ~~(c) the carryforward of unused tax credits.~~
~~**deferred tax liabilities**~~	~~The amounts of income tax payable in future periods in respect of taxable temporary differences.~~
~~**defined benefit liability**~~	~~Post-employment benefit plans other than defined contribution plans.~~
~~**defined contribution plans**~~	~~Post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.~~
depreciable amount	The cost of an asset, or other amount substituted for cost (in the financial statements), less its residual value.
~~**depreciation**~~	~~The systematic allocation of the depreciable amount of an asset over its useful life.~~
derecognition	The removal of all or part of a recognised asset or liability from an entity's Statement of Financial Position.
development	The application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, productions, processes, systems or services before the start of commercial production or use.
~~**discontinued operation**~~	~~A component of an entity that either has been disposed of or is held for sale and:~~ ~~(a) represents a separate major lien of business or geographical area of operations;~~ ~~(b) is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or~~ ~~(c) is a controlled entity acquired exclusively with a view to resale.~~
~~**director**~~	~~(a) a person who is a director under the Corporations Act; and~~ ~~(b) in the case of entities governed by bodies not called a board of directors, a person who, regardless of the name that is given to the position, is appointed to the position of member of the governing body, council, commission or authority.~~
dividends	Distributions of profits to holders of equity instruments in proportion to their holdings of a particular class of capital.
~~**economic resource**~~	~~A right that has the potential to produce economic benefits.~~
~~**effective interest method**~~	~~A method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expenses over the relevant period.~~
~~**effective interest rate**~~	~~The rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.~~

Commented [A55]: Note to Board members
In Agenda Paper 4.16 for this meeting, staff suggested including a definition for 'director' in the glossary rather than within the body of the Standard. However, staff have since reconsidered and do not think it is necessary to include such a definition given it is defined by the *IFRSs for SMEs* Accounting Standard requirements. Furthermore, staff noted that NFP regulators already have other defined terms (e.g. ACNC uses responsible person). As such, staff suggest not to include a definition for 'director' to further economise the Standard.

~~**effectiveness of a hedge**~~	~~The degree to which changes in the fair value or cash flows of the hedgd item that are attributable to a hedge risk are offset by changes in the fair value or cash flows of the hedging instrument.~~
employee benefits	All forms of consideration given by an entity in exchange for service rendered by employees.
~~**enhancing qualitative characteristics**~~	~~A qualitative characteristic that makes useful information more useful. The enhancing qualitative characteristics are comparability, verifiability, timeliness and understandability.~~
~~**equity**~~	~~The residential interest in the assets of the entity after deducting all its liabilities.~~
~~**equity claim**~~	~~A claim on the residual interest in the asset of an entity after deducting all its liabilities.~~
~~**equity-settled share-based payment transaction**~~	~~A share-based payment transaction in which the entity:~~ ~~(a) receives goods or services as consideration for its own equity instruments (including shares or share options); or~~ ~~(b) receives goods or services but has no obligation to settle the transaction with the supplier.~~
errors	Omissions from, and misstatement in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that: (a) was available when financial statements for those periods were authorised for issue; and (b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.
~~**executory contract**~~	~~A contact, or a portion of a contract, that is equally unperformed – neither party has fulfilled any of its obligation, or both parties have partially fulfilled their obligations to an equal extent.~~
exit price	The price that would be received to sell an asset or paid to transfer a liability.
~~**existence uncertainty**~~	~~Uncertainty about whether an asset or liability exists.~~
~~**expenses**~~	~~Decreases in assets or increases in liabilities that result in decrease in equity, other than those relating to distributions to holders of equity claims.~~
~~**fair presentation**~~	~~Faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Conceptual Framework for Financial Reporting*.~~
~~**fair value**~~	~~The price that would be received to sell, or paid to transfer a liability, in an orderly transaction (not a forced transaction) between market participants at the measurement date.~~
~~**finance lease**~~	~~A lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. A lease that is not a finance lease is an operating lease.~~
financial asset	Any asset that is: (a) cash; (b) an equity instrument of another entity' (c) a contractual right:

Commented [A56]: Note to Board members
This term is included as suggested by a Subcommittee member. The term is defined in AASB 13

(i) to receive cash or another financial asset from another entity; or

(ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity; or

(d) a contract that will or may be settled in the entity’s own equity instruments and:

(i) under which the entity is or may be obliged to receive a variable number of the entity’s own equity instruments; or

(ii) that will or may be settled other than by exchange of a fixed amount of cash or another financial asset for a fixed number of the entity’s own equity instruments. For this purpose, the entity’s own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity’s own equity instruments.

~~**financial guarantee contract**~~	~~A contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.~~
financial instrument	A contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.
financial liability	Any liability that is a contractual obligation: (i) to deliver cash or another financial asset to another entity; or (ii) to exchange financial asset or financial liabilities with another entity under conditions that are potentially unfavourable to the entity.
financial position	The relationship of the assets, liabilities and equity of an entity as reported in the Statement of Financial Position.
financial statements	Structured representation of financial position, income and expense and cash flows of an entity.
financing activities	Activities that result in change in the size and composition of the equity and borrowings of the entity.
~~**firm commitment**~~	~~A binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.~~
first-time adopter of the ~~IFRS for SMEs Accounting~~ Tier 3 Standard	An entity that presents its first annual financial statements that conform to the Tier 3 Standard, regardless of whether its previous accounting was full IFRS Accounting Standards or another set of accounting standards.
~~**forecast transaction**~~	~~An uncommitted but anticipated future transaction.~~
~~**foreign operation**~~	~~An entity that is a subsidiary, associate, joint arrangement, notable relationship or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity.~~
~~**fundamental qualitative characteristics**~~	~~A qualitative characteristic that financial information must possess to be useful to the primary users of general purpose financial reports. The fundamental qualitative characteristics are relevance and faithful representation.~~
~~**funding (of post-employment benefits)**~~	~~Contributions by an entity, and sometimes its employees, into an entity, or fund, that is legally separate from the reporting entity and from which the employee benefits are paid.~~
~~**general purpose financial report**~~	~~A report that provides financial information about the reporting entity’s economic resources, claims against the entity and changes in those economic~~

~~resources and claims that is useful to primary users in making decisions relating to providing resources to the entity.~~

general purpose financial statements — A particular form of general purpose financial reports that provide information about the reporting entity's assets, liabilities, equity, income and expenses.

going concern — An entity is a going concern unless management either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.

goodwill — An asset representing the future economic benefits arising from other asset acquired in a business combination that are not individually identified and separately recognised.

government — Government, government agencies and similar bodies whether local, national or international.

~~**government grants**~~ — ~~Assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity.~~

~~**grant date**~~ — ~~The date at which the entity and another party (including an employee) agree to a share-based payment arrangement, being when the entity and the counterparty have a shared understanding of the terms and conditions of the arrangement. At the grant date, the entity confers on the counterparty the right to cash, other assets or equity instruments of the entity, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), the grant date is the date when that approval is obtained.~~

~~**gross investment in a lease**~~ — ~~The aggregate of:~~

~~(a) the minimum lease payments receivable by the lessor under a finance lease; and~~

~~(b) any unguaranteed residual value accruing to the lessor.~~

group — A parent and all its subsidiaries.

~~**hedged item**~~ — ~~For the purpose of special hedge accounting by SMEs under Part II of Section 11, a hedged item is:~~

~~(a) interest rate risk of a debt instrument measured at amortised cost;~~

~~(b) foreign exchange or interest rate risk in a firm commitment or a highly probable forecast transaction;~~

~~(c) price risk of a commodity that is holds or in a firm commitment or highly probable forecast transaction to purchase or sell a commodity; or~~

~~(d) foreign exchange risk in a net investment in a foreign operation.~~

~~**hedging instrument**~~ — ~~For the purpose of special hedge accounting by SMEs under Part II of Section 11, a hedging instrument is a financial instrument that meets all of the following terms and conditions:~~

~~(a) it is an interest rate swap, a foreign currency swap, a foreign currency forward exchange contract or a commodity forward exchange contract that is expected to be highly effective in offsetting a risk identified in paragraph 11.65 that is designated as the hedged risk;~~

~~(b) it involved a party external to the reporting entity (ie external to the group, segment or individual entity being reporting on);~~

~~(c) its notional amount is equal to the designated amount of the principal or notional amount of the hedged item;~~

~~(d) it has a specified maturity date not later than:~~

~~(i) the maturity of the financial instrument being hedged;~~

~~(ii) the expected settlement of the commodity purchase or sale commitment; or~~

~~(iii) the occurrence of the highly probable forecast foreign currency or commodity transaction being hedged.~~

~~(e) it has no prepayment, early termination or extension features.~~

highly probable Significantly more likely than probable.

~~**impairment (loss)**~~ ~~The amount by which the carrying amount of an asset exceeds:~~

~~(a) in the case of inventories, its selling price less costs to complete and sell~~ it~~; or~~

~~(b) in the case of other non-financial assets, its recoverable amount.~~

impracticable Applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so.

~~**income**~~ ~~Increases in asset, or decreases in liabilities, that result in increases in net assets, other than those relating to contributions from holders of equity claims.~~

income statement A financial statement that presents al items of income and expenses recognised in a reporting period, excluding the items of other comprehensive income.

income tax All domestic and foreign taxes that are based on taxable profits. Income tax also includes taxes, such as withholding taxes, that are payable by a subsidiary, associate, joint arrangement or notable relationship entity on distributions to the reporting entity.

~~**insurance contract**~~ ~~A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.~~

intangible asset An identifiable non-monetary asset without physical substance. Such as an asset is identifiable when it:

(a) is separable, ie is capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract asset or liability; or

(b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

~~**interest rate implicit in the lease**~~ ~~The discount rate that, at the inception of the lease, causes the aggregate present value of (a) the minimum lease payments and (b) the unguaranteed residual value ot be equal to the sum of (i) the fair value of the leased asset and (ii) any initial direct costs of the lessor.~~

~~**interim financial report**~~ ~~A financial report containing either a complete set of financial statements or a set of condensed financial statements for an interim period.~~

~~**interim period**~~ ~~A financial reporting period shorter than a full financial year.~~

~~**intrinsic value**~~ ~~The difference between the fair value of the shares to which the counterparty has the (conditional or unconditional) right to subscribe or which it has the right to receive, and the price (if any) the counterparty is (or will be) required to pay for those shares. For example, a share option with an exercise price of CU15 on a share with a fair value of CU20 has an intrinsic value of CU5.~~

inventories

Asset:

(a) in the form of materials or supplies to be consumed in ~~the production process or in the rendering services~~ producing goods or rendering services;

(b) held for sale or distribution in the ordinary course of operations; or

(c) in the process of production for such sale or distribution.

inventories held for distribution

Assets:

(a) held for distribution at no or nominal consideration in the ordinary course of operation;

(b) in the process of production for distribution at no or nominal consideration in the ordinary course of operations; or

(c) in the form of materials or supplies to be consumed in the production process or in the rendering of services at no or nominal consideration.

Commented [A57]: Note to Board members
As suggested by a Subcommittee member, staff have included the definition of inventories held for distribution as defined in Appendix A para Aus6.1 of AASB 102 to provide clarity to readers.

investing activities

The acquisition and disposal of long-term asset and other investments not included in cash equivalents.

investment property

Property (land or a building, or part of a building, or both) held by the owner or by the lessee under a finance lease to earn rentals or for capital appreciation or both, instead of for:

(a) use in the production or supply of goods or services or for administrative purposes; or

(b) sale in the ordinary course of business.

~~**joint control**~~

~~The contractually agreed sharing of control of an arrangement. It exists only when decisions about the~~

~~**joint arrangement**~~

~~An arrangement of which two or more parties have joint control. Joint arrangements can take the form of jointly controlled operations, jointly controlled assets, or jointly controlled entities.~~

~~**jointly controlled entity**~~

~~A joint arrangement that involves the establishment of a corporation, partnership or other entity in which each party has an interest. The entity operates in the same way as other entities, except that an arrangement between the parties establishes joint control.~~

key management personnel

persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.

Commented [A58]: Note to Board members:
As per Agenda Paper 4.16 for this meeting, staff have included the definition of KMP here rather than within the body of the Standard, subject to the Board's decision to include KMP remuneration disclosures in Question 18.

lease

An agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.

~~**lessee's incremental borrowing rate of interest**~~

~~The rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.~~

~~**liability**~~

~~A present obligation of the entity to transfer economic resources as a result of past events.~~

loans payable

Financial liabilities other than short-term trade payables on normal credit terms.

market participants

Buyers and sellers in the principal (or most advantageous) market for the asset or liability that have all of the following characteristics:

(a) they are independent of each other, that is, they are not related parties as defined in Section 28;

(b) they are knowledgeable, having a reasonable understanding about the asset or liability and the transaction using all available information;

(c) they are able to enter into a transaction for the asset or liability; and

(d) they are willing to enter into a transaction for the asset or liability, that is, they are motivated but not forced or otherwise compelled to do so.

~~**market vesting condition**~~ ~~A performance condition upon which the exercise price, vesting or exercisability of an equity instrument depends that is related to the market price of the entity's equity instrument (or the equity instruments of another entity in the same group), such as~~

~~(a) attaining a special share price or a specified amount of intrinsic value of a share option; or~~

~~(b) achieving a specified target that is based on the market price (or value) of the entity's equity instruments (or the equity instruments of another entity in the same group) relative to an index of market prices of equity instruments of other entities.~~

~~A market condition requires the counterparty ot complete a specified period of services (that is, a service condition); the service requirement can be explicit or implicit.~~

~~**material**~~ ~~Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.~~

~~**measure**~~ ~~The result of applying a measurement basis to an asset or liability and related income and expenses.~~

~~**measurement basis**~~ ~~An identified feature – for example, historical cost, fair value or fulfilment value – of an item being measured.~~

~~**measurement uncertainty**~~ ~~Uncertainty that arises when monetary amounts in financial reports cannot be observed directly and must instead be estimated.~~

minimum lease payments The payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

(a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or

(b) for a lessor, any residual value guaranteed to the lessor by:

(i) the lessee;

(ii) a party related to the lessee; or

(iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

~~However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payment payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.~~

monetary items Units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency.

Commented [A59]: Note to Board members
As per Agenda Paper 4.9, staff recommend including the definition of minimum lease payments to provide clarity to Tier 3 entities but omit the last paragraph of the *IFRS for SMEs* Accounting Standard requirements from the Tier 3 ED. Staff consider it would not be proportionate to require Tier 3 NFP entities to determine whether an option to purchase the leased asset at a future date (such as the end of the lease term) has an exercise price expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised. Refer to Agenda Paper 4.9 at this meeting for further reasons.

~~**most advantageous market**~~	~~The market that maximises the amount that would be received to sell the asset or minimises the amount that would be paid to transfer the liability, after taking into account transaction costs and transport costs.~~
multi-employer (benefit) plans	Defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that: (a) pool the asset contributed by various entities that are not under common control; and (b) use those assts to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees concerned.
~~**net investment in a lease**~~	~~The gross investment in a lease discounted ta the interest rate implicit in the lease~~
non-controlling interest	The equity in a subsidiary not attributable, directly or indirectly, to a parent.
not-for-profit entity	A not-for-profit entity is an entity whose principal objective is not the generation of profit. A not-for-profit entity can be a single entity or a group of entities comprising the parent entity and each of the entities that it controls.
notes (to financial statements)	Notes contain information in addition to that presented in the statement of financial position, statement of comprehensive income, income statement (if presented), statement of changes in equity and statement of cash flows. Notes provide narrative descriptions or disaggregation of items presented in those statements and information about items that do not qualify for recognition in those statements.
notable relationship	When the reporting entity has at least significant influence over that entity (with or without holding an investment in the other entity's equity instruments, if any exist) and includes, but not limited to, having control or joint control over that other entity.
~~**notional amount**~~	~~The quantity of currency units, shares, bushels, pounds or other units specified in a financial instrument contract.~~
~~**objective of financial statements**~~	~~To provide financial information about an entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity.~~
observable inputs	Inputs that are developed using market data, such as publicly available information about actual events or transactions, and that reflect the assumption that market participants would use when pricing the asset or liability.
offsetting (netting off)	Grouping an asset and liability that are recognised and measured as separate units of account into a single net amount in the statement of financial position.
~~**onerous contract**~~	~~A contract in which the unavoidable costs of meeting the obligation under the contract exceed the economic benefits expected to be received under it.~~
operating activities	The principal revenue-producing activities of the entity and other activities that are not investing or financing activities.
~~**operating leases**~~	~~A lease that does not transfer substantially all the risks and rewards incidental to ownership. A lease that is not an operating lease is a finance lease.~~
orderly transaction	A transaction that assumes exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction (for example a forced liquidation or distress sale).

ordinary share
An equity instrument that is subordinate to all other classes of equity instruments.

other comprehensive income
Items of income and expenses (including reclassification adjustments) that are not recognised in profit or loss as required or permitted by this Standard.

~~**outcome uncertainty**~~
~~Uncertainty about the amount or timing of any inflow or outflow of economic benefit that will result from an asset or liability.~~

owners
Holders of instruments classified as equity

parent
An entity that has one or more subsidiaries.

performance
The relationship of the income and expenses of an entity, as reported in the statement of comprehensive income.

~~**performance condition**~~
~~A vesting condition that requires:~~

~~(a) the counterparty to complete a specified period of service (that is, a service condition); the service requirement can be explicit or implicit; and~~

~~(b) specified performance target(s) to be met while the counterparty is rendering the service required in (a).~~

~~The period of achieving the performance target(s):~~

~~(a) shall not extend beyond the end of the service period; and~~

~~(b) may start before the service period on the condition that the commencement date of the performance target is not substantially before the commencement of the service period.~~

~~A performance target is defined by reference to:~~

~~(a) the entity's own operations (or activities) or the operations or activities of another entity in the same group (that is, a non-market condition); or~~

~~(b) the price (or value) of the entity's equity instruments or the equity instruments of another entity in the same group (including shares and share options) (that is, a market condition).~~

~~A performance target might relate either to the performance of the entity as a whole or to some part of the entity (or party of the group), such as a division or an individual employee.~~

~~**plan assets (of a n employee benefit plan)**~~
~~Asset held by a long-term employee benefit fun and qualifying insurance policies.~~

post-employment benefits
Employee benefits (other than termination benefits) that are payable after the completion of employment.

post-employment benefit plans
Formal or informal arrangements under which an entity provides post-employment benefits for one or more employees.

~~**potential to produce economic benefit**~~
~~Within an economic resource, a feature that already exists and that, in at least one circumstance, would produce for the entity economic benefits beyond those available to all other parties.~~

~~**present value**~~
~~A current estimate of the present discounted value of the future net cash flows in the normal course of business.~~

~~**presentation currency**~~
~~The currency in which the financial statements are presented.~~

~~**primary users**~~
~~Existing and potential investors, lenders and other creditors.~~

~~**principal market**~~
~~The market with the greatest volume and level of activity for the asset or liability.~~

probable — More likely than not.

profit or loss — The total of income less expenses, excluding the components of other comprehensive income.

~~**projected unit credit method**~~ — ~~An actuarial valuation method that sees each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation (sometimes known as the accrued benefit method pro-rated on service or as the benefit/years of service method).~~

promise ~~**(in a contract with a customer)**~~ — An obligation or common understanding between the entity and the provider to transfer goods or services ~~(or bundle of goods or services) that is distinct.~~

property, plant and equipment — Tangible assets that:

(a) are held for use in the production or supply of goods or services, for rental to others or for administrative purposes; and

(b) are expected to be used during more than one period.

prospective application (of a change in accounting policy) — Applying the new accounting policy to transactions, other events and conditions occurring after the date as at which the policy is changed.

provision — A liability of uncertain timing or amount.

provider — A provider of asset or assets to the entity such as:

(a) a customer that has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for considerations; or

(b) a funding provider that provides resources to the reporting entity.

~~**prudence**~~ — ~~The exercise of caution when making judgements under conditions of uncertainty. The exercise of prudence means that assets and income are not overstated and liabilities and expenses are not understated. Equally, the exercise of prudence does not allow for the understatement of assets or income or the overstatement of liabilities or expenses.~~

public accountability — An entity has public accountability if:

(a) it debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional market); or

(b) it holds asset in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (for example, banks credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks often meet this second criterion)..

publicly traded (debt or equity instruments) — Traded, or in process of being issued for trading, in a public market (a domestic of foreign stock exchange or an over-the-counter market, including local and regional market).

~~**recognition**~~ — ~~The process of capturing for inclusion in the statement of financial position or the statement(s) of financial performance an item that meets the definition of one of the elements of financial statements – an asset, a liability, equity, income or expenses. Recognition involves depicting the item in one of those statements – either alone or in aggregation with other items – in words and by a monetary amount, and including that amount in one or more totals in that statement.~~

recoverable amount — The higher of an asset's (or cash-generating unit's) fair value less costs to sell and its value in use.

Commented [A60]: Note to Board members
The reference to value in use is subject to the Board agreeing to include guidance on value in use in Section 23 question 16.

related party A related party is a person or an entity that is related to the reporting entity, taking into account the principle in paragraph (c) ~~preparing its financial statements (the reporting entity)~~:

(a) a person or a close member of that person's family is related to a reporting entity ~~if that person~~ or of a parent of the reporting entity:

(i) is a member of the key management personnel of the reporting entity or a parent of the reporting entity;

(ii) has control or joint control over the reporting entity; or

(iii) has significant influence over the reporting entity.

(b) An entity is related to a reporting entity if any of the following conditions applies:

(i) the entity and the reporting entity are members of the same group (which means that each parent subsidiary and fellow subsidiary is related to the others).

(ii) one entity is an associate or jointly controlled entity of the other entity (or an associate or jointly controlled entity of a member of a group of which the other entity is a member).

(iii) both entities are jointly controlled entities of the same third entity.

(iv) One entity is a jointly controlled entity of a third entity and other entity is an associate of the third entity.

~~(v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.~~

(vi) the entity is controlled or jointly controlled by a person identified in (a).

(vii) the entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.

(viii) a person identified in (a)(ii) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(c) For a person or an entity to be identified as related to the reporting entity, it is unnecessary to identify which particular factor or condition listed in paragraph (a) is satisfied. For example, if the reporting entity is uncertain whether another entity is controlled, or significantly influenced, by it, this uncertainty does not preclude identification of that other entity as a related party.

(d) In the context of this Standard, the following are not necessarily related parties:

(i) two entities simply because they have a director or other member of key management personnel in common;

(ii) two entities simply because they have a director or other member of key management personnel in common;

(iii) any of the following simply by virtue of their normal dealings with an entity (even though they may affect the freedom of action of an entity or participate in its decision-making process):

(A) providers of finance;

(B) trade unions;

Commented [A61]: Note to Board members
To reduce the length of the Standard, staff have included the related party definition in the glossary rather than the body of the Standard. The definition has also been updated to align with the Board's decision regarding the choice to present consolidated or separate financial statements with disclosures of notional relationships.

Commented [A62]: Note to Board members
A Subcommittee member queried whether it is necessary to include paragraph (v) particularly given that staff' suggest omitting sub-paragraph 33(j) of the *IFRS for SMEs* Accounting Standard requirements – "*participation by a parent or subsidiary in a defined benefit plan that shares risks between group entities*" because that example would seem unusual for Tier 3 NFP entities.
In light of the Subcommittee feedback and for consistency with the proposing omission in paragraph 33.12, staff have removed paragraph (b)(v) as per strikethrough text.

(C) public utilities; or

(D) government departments and agencies; and

(iv) a customer, supplier, franchisor, distributor or general agent with whom an entity transacts a significant volume of business, merely by virtue of the resulting economic dependence.

related party transaction	A transfer of resources (whether cash, goods or services) or obligations between a reporting entity and a related party, regardless of whether a price is charged.
~~**relevance**~~	~~Relevant financial information is capable of making a difference in the decisions made by users.~~
relevant activities (of an investee)	The activities that significantly affect the investee's returns.
~~**reliability**~~	~~The quality of information that makes it free from material error and bias and represent faithfully that which it either purports to represent or could reasonably by expected to represent.~~
remuneration	Compensation as defined in this Standard. Although the defined term 'compensation' is used in this Standard rather than the term 'remuneration', both words refer to the same concept
~~**reporting entity**~~	~~An entity that is required, or chooses, to prepare general purpose financial statements~~
reporting date	The end of the latest period covered by financial statements ~~or by an interim financial report~~.
reporting period	The period covered by financial statements ~~or by an interim financial report~~.
research	Original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.
residual value (of an asset)	The estimated amount that an entity would currently obtain from disposal of an asset, after deducting the estimated cost of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.
retrospective application (of a change in accounting policy)	Applying a new accounting policy to transaction, other events and conditions as it that policy has always been applied.
revenue	Income arising in the course of an entity's ordinary activities.
~~**separate financial statements**~~	~~Those presented by an entity, in which the entity could elect, in accordance with paragraphs x – x, to account for its investments in subsidiaries, jointly-controlled entities and associates either at cost less impairment, at fair value with changes in fair value recognised in profit or loss or using the equity method following the procedure in paragraph 14.8.~~
~~**service concession arrangement**~~	~~An arrangement whereby a government or other public sector body contracts with a private operator to develop (or upgrade), operate and maintain the grantor's infrastructure assets such as roads, bridges, tunnels, airports, energy distribution networks, prisons or hospitals.~~
~~**service condition**~~	~~A vesting condition that requires the counterparty to complete a specified period of service during which services are provided to the entity. If the counterparty, regardless of the reason, ceases to provide service during the vesting period, it has failed to satisfy the condition. A service condition does not require a performance target to be met.~~

Commented [A63]: Note to Board members
Staff have included the definition of remuneration in glossary rather than within the body of the Standard, subject to the Board's decision to include KMP remuneration disclosures in the Tier 3 ED in question 18.

~~severe hyperinflation~~

~~The currency of a hyperinflationary economy is subject o severe hyperinflation if it has both the following characteristics:~~

~~(a) a reliable general price index is not available to all entities with transactions and balances in the currency, and~~

~~(b) exchangeability between the currency and a relatively stable foreign currency does not exist.~~

~~share-based payment arrangement~~

~~An agreement between the entity (or another group entity or any shareholder of any group entity) and another party (including an employee) that entitles the other party to receive:~~

~~(a) cash or other assets of the entity for amounts that are based on the price (or value) of equity instruments (i9ncludign shares or share options) of the entity or another group entity; or~~

~~(b) equity instruments (including shares or share options) of the entity or another group entity~~

~~provided the specified vesting conditions, if any, are met.~~

~~share-based payment transaction~~

~~A transaction in which the entity:~~

~~(a) receives goods or services from the supplier of those goods or services (including an employee) in a share-based payment arrangement; or~~

~~(b) incurs an obligation to settle the transaction with the supplier in a share-based payment arrangement when another group entity receives those goods or services.~~

~~Small and medium-sized entities~~

~~Entities that:~~

~~(a) do not have public accountability; AND~~

~~(b) publish general purpose financial statements for external users.~~

~~Entities that public accountability if:~~

~~(c) if files, or it is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; or~~

~~(d) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.~~

state (employee benefit) plan

Employee benefit plan established by legislation to cover all entities (or all entities in a particular category, for example a specific industry) and operated by national or local government or by another body (for example an autonomous agency created specifically for this purpose) which is not subject to control or influence by ethe reporting entity.

statement of cash flows

A financial statement that provides information about the changes in cash and cash equivalents of an entity for a period, showing ~~separately~~ changes during the period from operating separately from investing and financing activities. An entity may present changes from investing and financing activities together or separately.

statement of changes in equity (or statement of changes in net assets)

A financial statement that presents the profit or loss for a period, items of income and expense recognised directly in equity for the period, the effects of changes in accounting policy and corrections of errors recognised in the period and (depending on the format of the statement of changes in equity chosen by the entity) the amounts of transactions with owners acting in their capacity as owners during the period.

statement of comprehensive income

A financial statement that presents all items of income and expense recognised in a period, including those items recognised in determining profit or loss (which is a subtotal in the statement of comprehensive income) and items of other comprehensive income. If an entity chooses to present both an income

	statement and a statement of comprehensive income, the statement of comprehensive income begins with profit or loss and then displays the items of other comprehensive income.
statement of financial position	A financial statement that presents the relationship of an entity's assets, liabilities and equity as of a specific date (also called the balance sheet).
statement of income and retained earnings	A financial statement that presents the profit or loss and changes in retained earnings for a period.
~~**subsidiary**~~	~~An entity that is controlled by another entity.~~
~~**tax base**~~	~~The tax base of an asset or liability is the amount attributed to that asst or liability for tax purposes.~~
tax expense	The aggregate amount included in total comprehensive income ~~or equity~~ for the reporting period in respect of current tax ~~and deferred tax~~.
~~**taxable profit (tax loss)**~~	~~The profit (loss) for a reporting period upon which income taxes are payable or recoverable, determined in accordance with the rules established by the taxation authorities. Taxable profit equals taxable income less amounts deductible from taxable income.~~
~~**taxable temporary differences**~~	~~Temporary differences that will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.~~
~~**temporary differences**~~	~~Differences between the carrying amount of an asset or liability in the statement of financial position and its tax bases.~~
~~**termination benefits**~~	~~Employee benefits payable at the earlier of the following dates:~~ ~~(a) when an entity can no longer withdraw the offer of those benefits; and~~ ~~(b) when the entity recognises costs for a restructuring that is within the scope of Section 21 and involves the payment of termination benefits.~~
~~**timing differences**~~	~~income and expenses that are recognised in profit or loss in one period but, under tax laws or regulations, are included in taxable income in a different period.~~
~~**timeliness**~~	~~Having information available to decision-makers in time to be capable of influencing their decisions.~~
total comprehensive income	The change in equity during a period resulting from transactions and other events, other than those changes resulting from transactions with owners in their capacity as owners (equal to the sum of profit or loss and other comprehensive income).
transaction costs	The cost to sell an asset or transfer a liability ~~in the principal (or most advantageous) market for the asset or liability~~ that are directly attributable to the disposal of the asset or the transfer of the liability such as costs of marketing an asset for sale and meet both the following criteria: (a) they result directly from and are essential to that transaction; and (b) they would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made.
transport cost	The costs that would be incurred to transport an asset ~~from its current location to its principal (or most advantageous) market~~.
~~**treasury shares**~~	~~An entity's own equity instruments, held by the entity or other members of the consolidated group~~

Commented [A64]: Note to Board members:
As noted by staff when developing the Tier 3 drafting, staff consider that differences between the principal and most advantageous markets should be unusual for non-financial assets of Tier 3 NFP entities, which would tend to hold those assets for use rather than sale and not to be traded in different markets. Because of these aspects, staff consider the guidance in *IFRS for SMEs* Accounting Standard requirements relating to principal market would be likely to be confusing, and would not be proportionate for Tier 3 NFP entities.

~~**understandability**~~	~~Classifying, characterising and presenting information clearly and concisely makes it understandable.~~
unit of account	The right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations, to which recognition criteria and measurement concepts are applied.
unobservable inputs	Inputs for which market data are not available and that are developed using the best information available about the assumptions that market participants would use when pricing the asset or liability.
useful life	The period over which an asset is expected to be available for use by an entity or the number of production or similar units expected to be obtained from asset by an entity.
value in use	The present value of the future cash flows expected to be derived from an asset or cash-generating unit.
~~**vest**~~	~~Become an entitlement. Under a share-based payment arrangement, a counterparty's right to receive cash, other assets or equity instruments of the entity vests when the counterparty's entitlement is no longer conditional on the satisfaction .of any vesting conditions.~~
~~**vesting conditions**~~	~~A condition that determines whether the entity receives the services that entitle the counterparty to receive cash, other assets or equity instruments of the entity, under a share based payment arrangement. A vesting condition is either a service condition or a performance condition.~~
~~**vesting period**~~	~~The period during which all the specified vesting condition of a share-based payment arrangement are to be satisfied.~~

Commented [A65]: Note to Board members
Subject to the Board decision to include this term in Tier 3 Standard.

Appendix B
Effective date [TBU]

Appendix C
Amendments to other Standards [TBU]

Question 20 to Board members

Staff's approach to developing non-mandatory illustrative examples is based on whether stakeholder feedback was received on the DP for the need to develop and provide further clarification or examples for a particular aspect of the Tier 3 proposals. Staff will also consider the illustrative examples from other jurisdictions or frameworks and assess whether their inclusion would be helpful to be included in the Tier 3 Standard.

Staff have also previously indicated that staff may consider developing application or implementation guidance to provide further clarification of the Tier 3 requirements. However, staff recommend not to develop any implementation guidance unless they are sufficiently important to be included in the body of the Standard. This is also consistent with the New Zealand Tier 3 Standard which includes illustrative examples only. Staff will also consider whether to recommend the illustrative examples be published as a separate document to the Tier 3 Standard to economise the length of the Standard. Staff have drafted some illustrative examples that the Subcommittee has reviewed and provided feedback on for the Board to consider below.

Do Board members agree with the staff's approach to developing non-mandatory illustrative examples only? If not, what do Board members suggest?

Illustrative examples

These illustrative examples accompany, but are not part of, the Standard.

Assessing loss of service potential

A Loss of service potential due to physical obsolescence

B Loss of service potential due to reduction in external demand for goods or service

C Loss of service potential due to changed strategy

Example A – Loss of service potential due to physical obsolescence

Entity A operates a food bank. It purchases items of food to be included in food parcels, and also receives donations of food from supermarkets and individuals. Because the donations it receives are unpredictable, it can have a surplus of certain food items.

These food items may become limited in their use and so suffer a loss of service potential due to their age as they approach their expiry date. If Entity A has more items than are required for the food parcels, it might need to either sell the items at a discount or dispose of them once the expiry date has passed.

At the reporting date, Entity A assesses whether any purchased food items has suffered a loss of service potential from one of the events identified in paragraph 23.3 (which include that the inventories are perishable items that spoiled or became obsolete). A loss of service potential will not be identified for the food that was donated ~~as~~ if Entity A elected to measure the cost of the donated food at the cost to it (of nil). For those inventories that have been measured at an amount other than nil, as required by paragraph 13.4A, Entity A estimates the amount that it will not be able to use in the food parcels, and reduces the carrying amount of the inventories by this amount, net of any expected sales proceeds, and records a corresponding expense.

Example B – Loss of service potential due to reduction in external demand for goods or services

Entity C, which has the objective of helping long-term unemployed people find work, runs courses on interview preparation. Entity C has prepared course materials that are provided to all participants, and has sufficient stock for the expected life of the current course.

The courses are subsidised by the government, and as a result Entity C is able to offer the courses for no charge.

As a result of a change of government policy, the courses are no longer subsidised by the government. Entity C has insufficient resources to cover all the costs itself, and introduces a small charge for the courses to cover the cost of hiring the venue and providing lunch.

Because of the introduction of the small charge, the number of participants reduces, and Entity C runs the courses less frequently. As a result, it is unlikely that Entity C will be able to use all of the course materials.

At the reporting date, Entity C assesses whether any inventories of the course materials has suffered a loss of service potential from one of the events identified in paragraph 23.3 (which include that the entity has been affected by a reduction in external demand for its goods or services and the entity's capacity to provide services might have been affected adversely as a result). As required by paragraph 13.4A, Entity C estimates the amount of the course materials that it will not be able to use before the course needs to be redeveloped, adjusts the carrying amount of its inventories of course materials in proportion to the amount it estimates will be unused, and records a corresponding expense.

Example C – Loss of service potential due to changed strategy

Entity D is a not-for-profit community centre. One of its programmes was to provide free cooking and nutrition classes to members of the community. Its inventories include purchased groceries, disposable plates and cutlery. Due to difficulties in attracting and retaining a chef for a cost affordable within the amount of grant funding secured for the programme, Entity D decided that, upon the end of the then-current grant period (which was also the end of the reporting period), it would not seek a renewal of grant funding, and wound up the programme. None of the groceries held at the reporting date was nearing its expiry date, and therefore the groceries were not affected by physical obsolescence.

Commented [A66]: Note to Board members
A Subcommittee member suggested expanding the example to also consider what would occur (holding all other facts constant) the groceries were affected by physical obsolescence to provide readers with guidance on what to do when more than one indicator of impairment is present.

Staff have expanded the example as per draft underlined text.

At the reporting date, Entity D assesses whether any purchased inventories for its cooking programme has suffered a loss of service potential from one of the events identified in paragraph 23.3 (which include that the entity changed its strategy and the capacity of inventories to be sold or provide goods or services might have been affected adversely as a result). Entity D concludes that it will neither be able to use or sell those inventories. As required by paragraph 13.4A and Section 23 *Impairment of Assets*, Entity D estimates the recoverable amount of those inventories, which is nil, and writes them off as an expense.

Similarly, if the entity at the reporting date discovered that the groceries held were expired or perished, then the entity would conclude that it will neither be able to use or sell those inventories and estimate the recoverable amount of those inventories as nil and writes them off as an expense.

Question 21 to Board members

Staff have applied the requirements in paragraph 7.8.1 of the *AASB Due Process Framework for Setting Standards* when developing the Basis for Conclusions (BC) which states:

A Basis for Conclusions is prepared for each pronouncement which outlines:

(a) reasons for reaching the conclusions in the final issued pronouncement;

(b) evidence and key factors considered in arriving at the decisions;

(c) consultation processes followed;

(d) AASB responses to comments received from consultation processes;

(e) a detailed consideration of the various options available to address the identified issue or problem, including both regulatory and non-regulatory options, together with the likely benefits and costs to stakeholders under each option for compliance with the RIS requirements;

(f) cost/benefits analysis;

(g) a clear statement of the conclusions reached, the recommended option, a review of that option and a plan for implementation; and

(h) dissenting views.

Staff is in the process of drafting the BC however staff have drafted the BC for Fair Value Measurement, Revenue and Consolidated and Separate Financial Statements Sections for the Board to consider and provide any preliminary feedback on the length of the BC and whether it sufficiently outlines the Board's rationale in developing the Tier 3 requirements. In drafting the BC, staff were conscious of the length of sections as staff considered Tier 3 preparers will mainly focus on the body of the Standard rather than the BC. As such, staff will ask the Board whether the BC should be included with the Standard or in a separate document once further sections of the BC has been drafted when staff bring the next iteration of the ED for further consideration at a future meeting.

Staff previously presented a draft paragraph BC 21 as part of Agenda Paper 4.12 for this meeting for Subcommittee review. One Subcommittee member provided feedback which staff have included as a note to Board members against paragraph BC 21 together with staff suggested edits based on Subcommittee feedback.

Do Board members have any preliminary feedback on the BC drafted for Fair Value Measurement, Revenue and Consolidated and Separate Financial Statements below?

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, AASB 10XX.

Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in this Exposure Draft (ED). It sets out the reasons why the Board developed the Exposure Draft, the approach taken to developing the Exposure Draft and the bases for the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

The need for a new Standard for Tier 3 not-for-profit private sector entities [TBU]

BC2 XXX

BC3 XXX

BC4 XXX

BC5 XXX

BC6 XXX

BC7 XXX

BC8 XXX

Significant decisions made by the Board in developing the Tier 3 requirements

BC9 XXX

Fair value measurement

BC10 The Board expressed preliminary views in the DP that the future Tier 3 Standard should allow or require fair value measurements of particular financial instruments and non-financial assets (such as property, plant and equipment), and that the Tier 3 Standard should be consistent in principle with the Tier 2 framework and guidance for fair value measurements in AASB 13 *Fair Value Measurement.* The Board noted that this approach should avoid costs of misinterpretation and retraining that would potentially be incurred if another source of guidance on fair value measurement were specified for Tier 3 not-for-profit entities. Consequently, the Board expressed a preliminary view in the DP that Tier 3 not-for-profit entities should apply the definition of 'fair value' in AASB 13 and estimate fair value by reference to a specified hierarchy and a non-financial asset's highest and best use but expressed in a manner easier to follow for preparers who are not accounting experts.

BC11 As an alternative to the approach described in paragraph BC10, the Board considered whether to permit Tier 3 not-for-profit entities to use other current value measurement bases as 'shortcuts' to estimate fair value. For example, the Board considered whether it should permit an entity to use, on a stand-alone basis, a rateable or other government valuation or the recent market selling price of a similar asset. However, the Board was concerned that such valuation 'shortcuts' might not represent faithfully the value of the asset held (eg rateable value calculation bases might differ between jurisdictions). In addition, the Board noted that private sector not-for-profit entities are not required to apply a revaluation model to their non-financial assets, which largely negates any need for valuation 'shortcuts'.

BC12 Overall, stakeholders' feedback on the DP agreed with the Board's preliminary views. In response to a view that Tier 3 not-for-profit entities should be permitted to use historical cost as an approximation of fair value to reduce the cost and the potential volatility of fair value measurements, the Board concluded that, whilst historical cost might in particular circumstances (eg for some recently purchased assets) coincide closely with the amount of an asset's or liability's fair value, deeming historical cost to represent fair value often would not result of faithful representation of fair value. In addition, as noted in paragraph BC11, private sector not-for-profit entities are not required to apply a revaluation model to their non-financial assets and they generally could simply elect to measure non-financial assets using the (historical) cost model.

BC13 In light of that feedback, the Board decided to reflect its DP preliminary views in its proposals in this ED. However, the Board decided to propose further simplifications by providing a practical expedient for identifying when a higher and better use of a non-financial asset than its existing use would exist (see paragraph BC14) and excluding guidance on the fair value hierarchy (see paragraphs BC17 – BC19). The Board also proposes to simplify the application of fair value measurements by including guidance specific to Tier 3 not-for-profit entities; the specific reasons for that proposed guidance are set out in paragraphs BC15 – BC16 and paragraphs BC20 – BC21. The Board's reason for excluding the disclosure requirements about fair value measurements in AASB 13 is set out in paragraph BC22.

Highest and best use

Practical expedient

BC14 The Tier 2 requirements in AASB 13 require the fair value measurement of a non-financial asset to be based on the asset's highest and best use (paragraph 27); that Standard also states a rebuttable presumption that an asset's current use is its highest and best use (paragraph 29). To achieve the simplification objectives of the Tier 3 Standard, the Board proposes in paragraph 11.7 of the ED guidance clarifying (and limiting) the circumstances in which the presumption that an asset's current use is its highest and best use may be rebutted. Paragraph 11.7 states that a non-financial asset's current use is presumed to be its highest and best use unless it is highly probable that, within one year of the asset's measurement date, the asset will either be sold to a buyer who would use the asset for a different use or be redeployed by the entity.

Financially feasible use

BC15 The 'financially feasible use' requirement in AASB 13, paragraph 28 (c) for identifying the highest and best use of a non-financial asset held by a not-for-profit public sector entity refers to generating an investment return that market participants would require from an asset. To express that criterion in a manner easier for preparers who are not accounting experts to adapt it to a not-for-profit context, the Board decided to modify the text of paragraph 28(c) of AASB 13 to avoid limiting the fair value of any non-financial asset to the present value of cash inflows generated directly by the asset.

BC16 The proposed text in this ED that would replace paragraph 28(c) of AASB 13 is "whether the use makes financial sense, i.e. it would generate at least a market rate of return on investing in the asset or sufficient goods/services to beneficiaries to justify buying the asset or if not already held".

Fair value hierarchy

BC17 As noted in paragraph BC10, the DP (paragraph 5.117) stated the Board's preliminary view that fair value measurements in financial statements of Tier 3 not-for-profit entities should be determined by reference to a specified hierarchy. For the reasons in paragraphs BC18 – BC19, on redeliberating that preliminary view, the Board decided to propose not to include in the Tier 3 Standard the fair value hierarchy set out in paragraphs 72 – 90 and B35 – B36 of AASB 13.

BC18 AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* includes none of AASB 13's disclosure requirements for fair value measurements. Because the Board proposes that disclosure requirements for Tier 3 not-for-profit entities should not be more onerous than the disclosure requirements for Tier 2 entities, the Board proposes that Tier 3 not-for-profit entities should not be required to make the disclosures about their fair value measurements required by AASB 13, although some disclosures about fair value measurements would be required by various sections of the proposed Tier 3 Standard (consistent with AASB 1060).

BC19 AASB 13 (paragraph 61) and proposed paragraph 11.8 of this ED require fair value estimates to maximise the use of relevant observable inputs and minimise the use of unobservable inputs; the fair value hierarchy classifies the outcomes of applying that principle and requires differentiated disclosures for different levels of the fair value hierarchy (the IASB's Basis for Conclusions on IFRS 13 *Fair Value Measurement*, paragraphs BC166 – BC221, does not identify any other role for the fair value hierarchy). In addition, that Basis for Conclusions states that "IFRS 13 does not contain a hierarchy of valuation techniques …" (paragraph BC142). For the reasons explained above, the Board considers that guidance on the fair value hierarchy would only be necessary if disclosure were required of the levels of the fair value hierarchy at which the fair values of assets are measured. The Board also notes that applying the fair value hierarchy might involve significant judgements and be costly for Tier 3 not-for-profit entities to apply, without significant apparent benefits to users of financial statements of those entities. Consequently, the Board concluded that, since it does not propose adopting the disclosure requirements for fair value measurements in AASB 13 (see paragraph BC22), it would not be proportionate to include the fair value hierarchy in the Tier 3 Standard.

Cost approach

BC20 Paragraph 11.10 of the ED was included to provide brief guidance on the cost approach (also termed the current replacement cost method) to estimating a non-financial asset's fair value. The cost approach is likely to be important to fair value measurements (where used) of a range of non-financial assets held by Tier 3 not-for-profit entities, particularly because the income approach would have limited application when assets are not held primarily to generate net cash inflows.

BC21 Although the objective of a fair value measurement of an asset is to estimate the asset's selling price, sometimes the observable selling price of a similar asset might not represent faithfully the selling price of the asset being measured (in terms of paragraph 11.~~14~~8, it might not be a *relevant* observable input). For example, the only observable selling price for a similar asset to ~~a specialised~~ an asset held by the entity might be for a sale of that similar asset for scrap value at the end of its economic life, eg because the asset is specialised. Where the entity's ~~specialised~~ asset has not reached the end of its economic life, its selling price might be represented more faithfully by, for example, using the cost approach (ie current replacement cost) referred to in paragraphs ~~11.15(b)~~11.9(b) and ~~11.15A~~ 11.10.

Disclosures

BC22 As noted in paragraph BC18, AASB 1060 includes none of AASB 13's disclosure requirements for fair value measurements. Because the Board proposes that disclosure requirements for Tier 3 not-for-profit entities should not be more onerous than the disclosure requirements for Tier 2 entities, the Board proposes that Tier 3 not-for-profit entities should not be required to make the disclosures about their fair value measurements required by AASB 13, although some disclosures about fair value measurements would be required by various sections of the proposed Tier 3 Standard (for example, consistent with AASB 1060, this ED proposes that, for revalued classes of property, plant and equipment, disclosure is made of the effective date of the revaluation and whether an independent valuer was involved).

Commented [A67]: **Note to Board members**
A Subcommittee member commented that:
"In para 12.15A it states current replacement cost may be used when the asset is specialised and without readily observable market evidence. In that context, I raise the following points about this example: (1) it seems that current replacement cost is used not because the asset is specialised in nature but rather because the similar asset is of a different age to the specialised asset (I suggest the example be consistent with the reason for using current replacement cost in the last para of 12.15A; and (2) more conceptually, if an asset is specialised can there be such a thing as a similar asset?"

Staff agree that being specialised is an inessential feature of the asset in the example to justify using the cost approach. However, staff think it would be useful to mention being specialised as an example of why observable evidence of an asset with a similar age might be unavailable. Staff think that, if assets were not specialised, it would be customary for observable market evidence to exist of assets with a similar age. For consistency, staff suggest amending the last sentence of draft para. 12.15A (now 12.10) to: "One reason the current replacement cost method may be used is that the asset lacks readily observable market evidence because it is specialised and comparable assets seldom are traded."
Staff think a specialised asset can have similar assets, because specialisation does not mean uniqueness; other assets can be devoted to the same narrow purpose as that of the subject asset, and have similar characteristics but differ in respect of, for example, their age.

Consolidated and separate financial statements

Choice whether to prepare consolidated financial statements

BC23 In relation to the Tier 2 requirement in AASB 10 *Consolidated Financial Statements* for entities to prepare consolidated financial statements if they have subsidiaries (i.e. entities they control), the Board was informed through previous stakeholder outreach about challenges and costs in identifying a complete set of subsidiaries of Tier 3 not-for-profit sector entities, because of:

(a) information not being readily available to those entities; and

(b) a stakeholder view that consolidated financial statements do not provide useful information compared with entity-level financial statements for each entity in a group, sometimes because of disagreement that some entities identified as subsidiaries are actually controlled by the reporting entity; and

(c) greater costs likely to be incurred by smaller not-for-profit entities in preparing consolidated financial statements.

BC24 In addition, the Board received feedback that avoiding consolidation might be a reason some entities presently elect to prepare special purpose financial statements. In response to the feedback referred to in paragraph BC23, the Board concluded that the costs of requiring (with or without limited exceptions) the preparation of consolidated financial statements by Tier 3 not-for-profit parent entities are likely to exceed the benefits to users of financial statements of those parent entities. Therefore, the Board expressed in its discussion paper a preliminary view to provide an option to Tier 3 not-for-profit parent entities to present either:

(a) consolidated financial statements; or

(b) separate financial statements as their only set of financial statements, with disclosures about each parent entity's significant/notable relationships (‘notable relationships’).

The Board decided not to develop additional guidance on identifying control, because such guidance would not necessarily reduce the complexity of assessing whether control relationships exist and might have unintended implications for Tier 2 not-for-profit entities applying AASB 10. The Board considers that implementation concerns about the guidance on control in AASB 10 affect not-for-profit entities of all sizes, and plans to consider those concerns as part of its post-implementation review of the application guidance for not-for-profit entities in AASB 10, rather than in its project to develop a Standard for Tier 3 not-for-profit entities.

BC25 Overall, the stakeholder feedback supported the Board's preliminary view on consolidation in paragraph BC24. However, some stakeholders disagreed, even if additional compensating disclosures were required. They expressed a view that, to be of a ‘general purpose’ nature, a parent entity’s financial statements need to record all assets the entity controls and all liabilities it incurs (directly, or indirectly through subsidiaries), and changes in those assets and liabilities. They also expressed views that:

(a) preparing consolidated financial statements is important in providing transparent information to users of a parent entity’s financial statements about the resources available to, the financial risk associated with, and the funding provided to, the reporting entity as a whole; and

(b) providing an accounting policy choice about whether to prepare consolidated financial statements might undermine the comparability between financial statements of similar groups of Tier 3 not-for-profit entities.

BC26 The Board considered the feedback received and decided to propose in the ED a policy consistent with its preliminary view in the discussion paper because:

(a) it is generally expected that few Tier 3 not-for-profit entities would be parent entities;

(b) separate financial statements, supplemented by disclosures of key information about notable relationship entities, can provide useful information about the reporting entity and its notable relationships without requiring assessments of whether control exists and requiring all the information necessary for the preparation of consolidated financial statements. Requiring disclosure of information about the identity of ‘notable relationship entities’ (see paragraphs BC27 – BC29) should enable users of the financial statements of Tier 3 not-for-profit entities to obtain general purpose financial statements, if available, of those notable relationship entities; and

(c) exceptions to preparing consolidated financial statements exist in AASB 10 (e.g. in respect of investment entities); where exceptions are utilised, the financial statements nevertheless are referred to as general purpose financial statements.

Disclosures about notable relationships

BC27 As noted in paragraphs BC24 and BC26, the Board proposes requiring disclosures of information about notable relationships in separate financial statements (but not if the reporting entity presents consolidated financial statements). This ED's proposed definition of a 'notable relationship entity' is an entity:

(a) over which the parent entity has at least significant influence (i.e. it would also include any instances of control or joint control, without requiring identification of whether the relationship is one of control, joint control or just significant influence); but

(b) that is not identified as an associate. Disclosure requirements for associates are specified separately in Section 13 of this ED on Investments in Associates and Joint Arrangements.

BC28 The proposed definition of a 'notable relationship entity' being the entity over which the parent entity has at least significant influence responds to feedback from previous outreach with stakeholders, who indicated few concerns with identifying relationships of significant influence although identifying control relationships has been problematic (e.g. stakeholder feedback suggested it might often be straightforward to determine whether a church has significant influence over a religious school but highly problematic to determine whether the church controls the school).

BC29 The Board proposes that disclosure would be required of the name of the entities with which the reporting entity has a notable relationship and a description of those relationships, together with other descriptive (non-quantitative) information. The Board considered whether to also propose requiring disclosure of key metrics about significant relationship entities, such as their total assets. The Board concluded that making such disclosures would be likely to reduce considerably the cost savings ensuing when a parent entity elects not to prepare consolidated financial statements in respect of its subsidiaries. This is because:

(c) the range of notable relationship entities that are the subject of the disclosures would be broader than controlled entities (because they include all entities over which the entity has at least significant influence); and

(d) requiring disclosure of key metrics might prove almost as costly as requiring consolidated financial statements (i.e. the cost savings from having to disclose only key metrics would pertain mainly to cost savings relating to disaggregating and presenting information, without reducing the cost of record-keeping and calculating financial statement elements of controlled entities).

BC30 Therefore, the Board is not proposing to require disclosure of key metrics about significant relationship entities.

Measurement basis subsequent to initial recording for interests in notable relationship entities reported in separate financial statements

BC31 The Board expressed a preliminary view in the discussion paper that a parent entity that presents separate financial statements should have the choice of measuring, subsequent to initial recording, its interests in subsidiaries either:

(a) at cost;
(b) at fair value through other comprehensive income; or
(c) using the equity method of accounting.

BC32 Overall, the stakeholder feedback supported the Board's preliminary view. Some stakeholders expressed concern that too many measurement choices are provided, which might reduce the consistency of subsequent measurement; some others argued that investments in subsidiaries should be measured only at cost in separate financial statements of the parent. Regarding consistency of measurement, the Board noted in the discussion paper that:

(a) it expects that Tier 3 not-for-profit entities presenting separate financial statements will, in the main, measure any interests in subsidiaries at cost;

(b) permitting a parent entity to measure its interests in subsidiaries at fair value through other comprehensive income in its separate financial statements should promote consistency of measurement by treating those interests in the same manner as the treatment under the Board's preliminary views regarding financial assets held to generate both an income and a capital return for the entity (note that, under the Board's proposals in the ED [*to be covered in future drafting of section of the Basis for Conclusions regarding financial instruments*], an entity could make an irrevocable election at initial recording of the first asset in such a class of financial assets to measure the class at fair value through other comprehensive income). This measurement basis could provide relevant information where the entity determines the substance of its interests in its subsidiaries is a financial investment, ie a financial asset held to generate both an income and a capital return for the entity;

(c) where a parent determines that the substance of its interests in its subsidiaries is more akin to that of an associate interest, despite the entity controlling those subsidiaries, permitting the parent entity to measure its interests in subsidiaries using the equity method in its separate financial statements would allow the parent entity to measure its interests in subsidiaries consistently with its investments in associates (for which, under the Board's preliminary view in the discussion paper, reaffirmed in its corresponding proposal in the ED, application of the equity method would be required); and

(d) restricting the accounting policy choice for subsequent measurement of interests in subsidiaries in separate financial statements may impose a stricter requirement than that currently required under Tier 2 reporting requirements, which allow a choice for a parent entity to select the measurement basis for its interests in subsidiaries.

BC33 The Board extended the scope of the preliminary view regarding measurement requirements in paragraph BC31 to encompass interests in any significant relationship entities reported in separate financial statements. In addition, the Board decided to propose that interests in significant relationship entities should, if not measured at cost or using the equity method of accounting, be measured at fair value through profit or loss unless the entity makes an irrevocable election at initial recording of a particular investment to present changes in its fair value in other comprehensive income. This option is consistent with the Board's proposed subsequent measurement basis for financial assets acquired or originated by the entity to generate both income and a capital return for it (including all investments in equity instruments). The proposed option to make an irrevocable election at initial recording regarding the presentation of subsequent changes in fair value (i.e. through other comprehensive income, rather than profit or loss):

(a) responds both to concerns about the potential volatility of fair changes affecting the reported profit or loss and concerns about the unfamiliarity of some users of financial statements of Tier 3 not-for-profit entities with the concept of other comprehensive income;

(b) has a precedent in AASB 9 *Financial Instruments*, paragraphs 4.1.4 and 5.7.5 of which provide an option to make an irrevocable election at initial recording to measure financial assets meeting particular criteria at fair value through other comprehensive income instead of fair value through profit or loss; and

(c) would apply consistently to all interests in a single class of interests (interests in subsidiaries, associates or jointly controlled entities) and therefore, in effect, would be made on initial recording of the first interest in a class (TBU subject to the transitional provisions for initial application of this [draft] Standard: see paragraph XX).

BC34 The proposed measurement requirements for a parent entity's investments in associates and jointly controlled entities included in its consolidated financial statements (if any) are specified in Section 13 of this ED on *Investments in Associates and Joint Arrangements*, rather than in Section 8 on *Consolidated and Separate Financial Statements.*

Revenue

BC35 After considering stakeholders' feedback during preliminary outreach, the Board expressed preliminary views in the Discussion Paper that Tier 3 not-for profit entities:

(a) should not be required to apply two different Standards (AASB 15 *Revenue from Contracts with Customers* and AASB 1058 *Income of Not-for-Profit Entities*) to account for their various types of income (as is required of Tier 2 not-for profit entities) or, similarly, to account for income based on the nature of the transaction (e.g. donations, sales or grants); and

(b) should defer recording income from inflows of resources if there is an unsatisfied common understanding of the manner in which the entity is expected to use those resources (eg to transfer goods or services to customers or beneficiaries, or to use the resources over a specified period). A common understanding does not require a documented explicit stipulation by a transferor of a resource, an enforceable right of the transferor (eg a right of return of a resource if not used as expected) or a mandated threshold of specificity regarding how the resources are to be used.

BC36 Other approaches to the recording of income considered by the Board are noted below, together with the key reasons why the Board did not advocate them in its preliminary views in the discussion paper:

(a) not requiring a distinction for the accounting for inflows of resources. This simple approach may not reflect faithfully that some transferred resources are expected to be spent or used in a future period and should be accounted for differently from other donations;

(b) basing the distinction for the accounting for inflows of resources on either the nature of transactions or whether the resource provider imposed documented explicit stipulations on the expenditure or use of those transferred resources. The Board noted that the distinction by the nature of the transaction would appear to involve a similar two-step process as applied in AASB 15 and AASB 1058, rather than a simplification. Requiring a distinction based on documented explicit stipulations may be challenging to understand for smaller not-for-profit entities that lack detailed financial knowledge and might not result in deferral of recording income even though the not-for-profit entity is expected to spend or use the resources in the future;

(c) requiring a not-for-profit entity to assess whether the common understanding between it and the resource provider about the future expenditure or use of transferred resources is 'sufficiently specific' based on a simplified version of the criteria for that principle in AASB 15. Stakeholder feedback on outreach before the discussion paper indicated that those criteria are inherently complex and require judgements that would often be prone to inconsistent application; and

(d) requiring deferral of recording income on when there are conditions attached to the inflows of resources that are enforceable by the transferor, such as a 'use or return' condition or other means of enforcement. The Board considered that this approach would not reduce the current complexity of accounting for income and would not align with stakeholders' expectations that recording income should be deferred when transferred resources are expected to be spent or used in a future period, regardless of whether enforceable conditions exist.

BC37 Overall, stakeholders agreed with the Board's preliminary views. In light of that feedback, the Board decided to reflect its preliminary views in its proposals in this ED. Clarifications of terms used in the discussion paper, such as 'common understanding', were included in the ED as suggested by some stakeholders who responded to the discussion paper. In addition, as suggested by some stakeholders, proposed guidance on principal vs agent considerations (eg when a charity receives a grant on behalf of another charity and then forwards it to that other charity) was included in the ED.

BC38 The Board expressed in the Discussion Paper a preliminary view that the Tier 2 approach of permitting, but not requiring, a not-for-profit entity to record as income volunteer services received (or a class thereof) if the fair value of those services can be measured reliably should also be applicable to Tier 3 entities. Overall, the stakeholder feedback supported the Board's view; in light of that feedback, the Board decided to propose that policy in this ED. The Board also decided to include a proposed requirement to disclose sufficient information about volunteer services to enable an understanding of the effects of volunteer services on the entity's operations, including the entity's dependence on volunteer services for the achievement of its objectives and any known information about impending significant changes to the nature and amount of volunteer services. This would not require quantifying the value of volunteer services received.

Updating of Tier 3 reporting requirements

BC39 The AASB expects to propose amendments to the Tier 3 reporting requirements by publishing occasionally an exposure draft. Such exposure drafts would be developed only when there is a substantive case for amendments, in application of the *AASB Due Process Framework for Setting Standards*, and would take into account the findings of the latest post-implementation review of those requirements and feedback from agenda consultations. In developing those exposure drafts, the AASB would consider new and amended Tier 1/Tier 2 reporting requirements as well as specific issues brought to its attention regarding the application of the Tier 3 reporting requirements.

BC40 The AASB expects that amendments might be made to the Tier 3 requirements in accordance with a five-year periodic review cycle. However, on occasion the AASB might identify an urgent matter for which amendment of the Tier 3 reporting requirements needs to be considered outside the periodic review process. Such occasions are expected to be rare.

BC41 Unless and until the Tier 3 reporting requirements are amended, any changes the AASB might make or propose regarding Tier 1 or Tier 2 reporting requirements do not apply to the Tier 3 reporting requirements. The Tier 3 Standard is a stand-alone document. Entities applying the Tier 3 reporting requirements would not be able to anticipate or apply changes made to Tier 1 or Tier 2 reporting requirements unless and until those changes are incorporated into the Tier 3 reporting requirements. However, this would not preclude an entity that applies the Tier 3 reporting requirements from applying the most recent accounting policy in a Tier 2 reporting requirement pursuant to applying paragraphs 9.3 and 9.4 of the Standard (ie in the absence of specific guidance in the Tier 3 reporting requirements, an entity elects to consider the requirements and guidance in Tier 2 reporting requirements dealing with similar and related issues).