Snapshot:

AASB Discussion Paper – Development of Simplified Accounting Requirements (Tier 3 Not-for-Profit Private Sector Entities)

Australian Government

Australian Accounting Standards Board

Overview

This Snapshot provides an overview of the Discussion Paper – Development of Simplified Accounting Requirements (Tier 3 Not-for-Profit Private Sector Entities) published by the Australian Accounting Standards Board (AASB) in September 2022.

The Board's objective:

To respond to stakeholder concerns that smaller not-for-profit private sector entities (NFP entities) find the current Australian reporting requirements overly complex to apply. The Board intends to:

- develop a simple, proportionate, consistent and transparent financial reporting framework for application by smaller NFP entities that meets the needs of users of their financial statements; and
- remove the ability of certain NFP entities to prepare special purpose financial statements (SPFS) based on their self-assessment of their financial reporting requirements.

Project stage:

Many stakeholders support having specific reporting requirements for smaller NFP entities. However, there are different views about the requirements and how they could apply. As such, in September 2022, the Board published *Discussion Paper – Development of Simplified Accounting Requirements (Tier 3 Not-for-Profit Private Sector Entities)*. The Discussion Paper contains the Board's preliminary views on key features of the form and content of a proposed third tier of general purpose financial statements (GPFS) relevant to NFP entities.

Who should read this:

Preparers and advisers to NFP entities that are required to prepare financial statements in accordance with the Australian Accounting Standards (AAS) for a regulatory authority, or as directed under a legal document, and the users of those financial statements.

Next steps:

The Board will consider comments it receives on the Discussion Paper before deciding whether and how to develop an Exposure Draft.

Comments due by:

The Board is seeking comments on the Discussion Paper by 31 March 2023.

What is the Board aiming to achieve?

The Discussion Paper is the first step in revising the AASB's differential reporting framework for use by NFP entities.

What is a smaller NFP entity?

In developing its preliminary views, the Board considered NFP entities with revenue between $500,000 and $3 million. The application of the eventual standard is expected to be determined by relevant regulatory requirements.

What are the expected benefits of the Board's proposals?

The expected benefits of the Board's proposals include:

- simplified accounting and reduced costs for smaller NFP entities;
- improved comparability and quality of financial reporting; and
- consistent recognition and measurement requirements to be applied by smaller NFP entities.

What is the expected timing of the Board's proposals?

The Board has not finalised a timeline. The proposals would be subject to further public consultation, such as an Exposure Draft. Typically, the AASB will issue a standard with at least two years of lead time before its effective date and generally permits entities to apply those requirements early should they wish to do so.

For this project, the Board does not intend to:

Develop service performance reporting requirements

Reporting of service performance information will be considered in a separate project.

Change the existing Tier 1 or Tier 2 Australian Accounting Standards

Tier 1 and Tier 2 reporting requirements will continue to be available to NFP entities in their existing form. Tier 1 reporting requirements are 'full IFRS' with some NFP modifications. Tier 2 reporting requirements comprise the same recognition and measurement requirements as Tier 1 but with simplified disclosures.

Establish reporting thresholds

The establishment of appropriate reporting thresholds and any direction of a specific form of GPFS is determined by the relevant regulatory requirements.

Develop a fourth reporting tier

Introducing a further reporting tier would introduce additional complexity for entities when determining regulatory reporting obligations. The AASB considers that a fourth reporting tier, for example, based on cash accounting, might not be fit for purpose.

High-level overview of the proposed Tier 3 accounting requirements

How will the accounting requirements be set out?

The Discussion Paper proposes that:

- the requirements will be set out in a single stand-alone standard;
- the standard will specify accounting requirements relevant to transactions and other events and circumstances that are common to smaller NFP entities;
- the requirements will be expressed in a manner that is easy to understand; and
- guidance, including template financial statements, will accompany the standard.

Items proposed to be excluded from the Tier 3 accounting requirements include:

- biological and agricultural assets;
- insurance contracts issued, reinsurance contracts held and investment contracts with discretionary participation features;
- expenditures incurred in connection with the exploration for and evaluation of mineral resources before the technical feasibility and commercial viability of extracting mineral resources is demonstrable;
- business combinations;
- obligations arising under a defined benefit superannuation plan;
- share-based payment arrangements;
- the accounting by an operator in a service concession arrangement; and
- complex financial assets and financial liabilities.

The Board welcomes feedback on whether the items proposed to be excluded from the Tier 3 accounting requirements are appropriate.

The Board's preliminary views on key topics

The Tier 3 accounting requirements propose simplifications to the presentation, recognition and measurement requirements specified by Tier 1 and Tier 2 AAS. While the Discussion Paper has not included all topics that would be included in a future Tier 3 Standard, the Discussion Paper provides the preliminary views the Board would consider at an Exposure Draft stage.

Some simplifications may result in the absence of some information required by Tier 1 and Tier 2 AAS. However, the Board considered its cost-benefit assessment given that the proposed accounting requirements are being developed with smaller NFP entities in mind.

The Board welcomes feedback on its preliminary views on the Tier 3 accounting requirements for these key topics.

Topics with proposed simplifications to the existing classification, recognition and measurement requirements

Consolidation	A parent entity can choose to prepare: • consolidated financial statements; or • separate financial statements with information about the parent entity's significant relationships.
Non-financial assets acquired at significantly less than fair value	Accounting policy choice: • inventory – initially measured at cost or current replacement cost; and • other non-financial assets (excluding concessionary leases) measured at cost or fair value. An entity is not permitted to subsequently apply the revaluation or fair value model if the donated non-financial assets were initially measured at cost.
Impairment of non-financial assets	Non-financial assets: • subsequently measured at cost or deemed cost (i.e. an amount used as a surrogate for cost or depreciated cost at a given date) are subject to impairment testing; • are assessed for impairment when the asset has been physically damaged or when its service potential is adversely affected; and • are impaired when their carrying amount exceeds the recoverable amount.
Leases	All leases remain off-balance sheet and lease payments are to be recognised on a straight-line basis over the term of the lease unless another systematic basis is appropriate. Do not recognise right-of-use assets arising from concessionary lease arrangements.

The Board's preliminary views on key topics

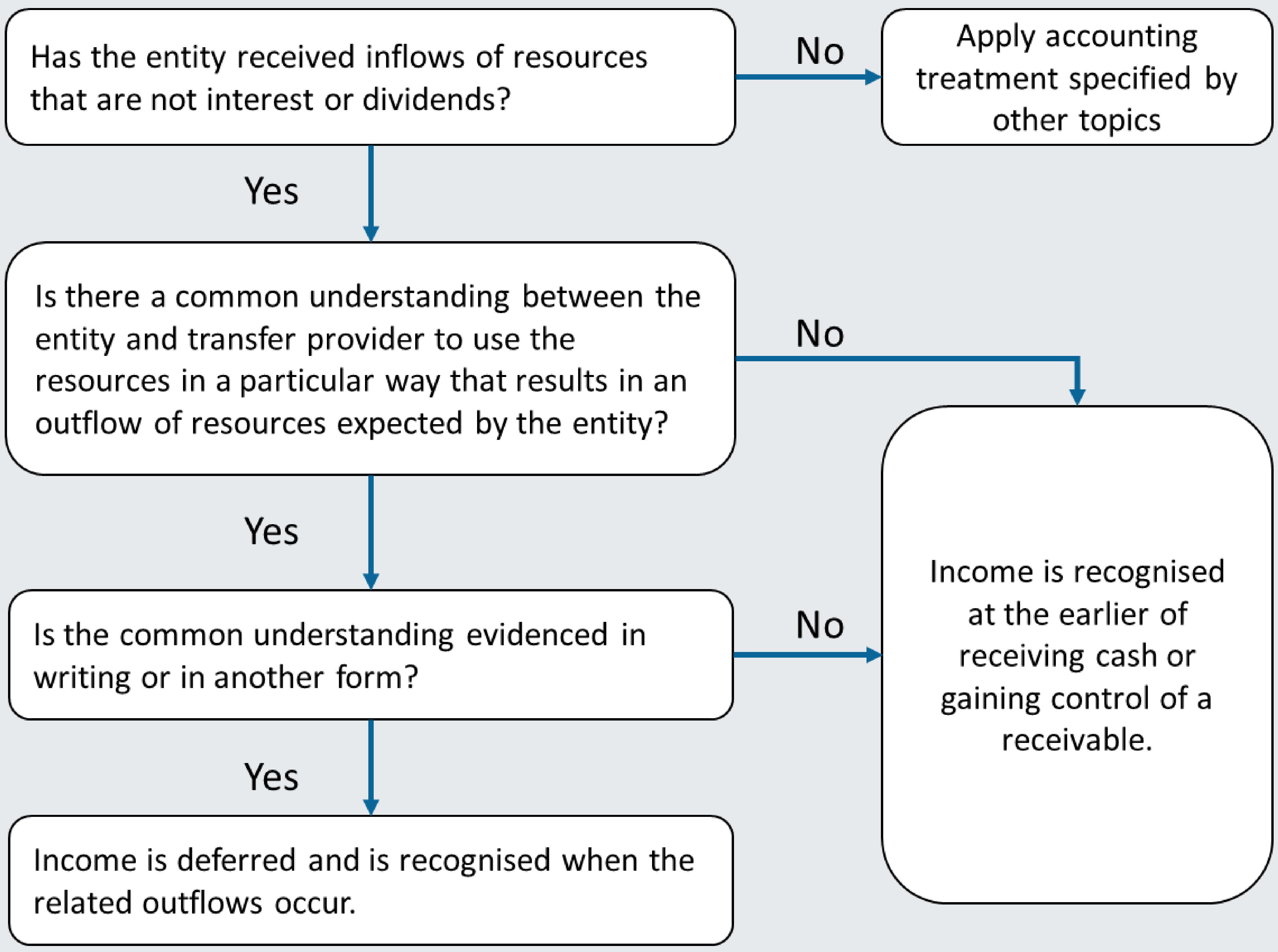
Income (including revenue)

Income is deferred when there is a common understanding that an entity is expected to use the inflows of resources in a particular way (e.g. incurring eligible expenditure for a specified purpose). Income is recognised when the related outflows occur.

The common understanding is evidenced by the transfer provider (i.e. provider of the resources) in writing or in some other form.

For all other income transactions, income is recognised at the earlier of receiving cash or controlling a receivable.

Decision Tree: Income recognition approach for inflows of resources



Employee benefits

Employee benefits are recognised as an expense when the employee has rendered the service. All short-term and long-term employee benefits are to be measured on an undiscounted basis. Long service leave shall reflect the probability that payment will be required. No special requirements developed for accounting of termination benefits and defined benefit plans.

The Board's preliminary views on key topics

Topics with proposed simplifications to recognition and measurement requirements, or restrictions on some accounting policies

Basic financial instruments – include only the most common financial instruments held by smaller NFP entities

All financial instruments – initial measurement	At fair value with immediate expensing of transaction costs.
Financial assets - subsequent measurement	• Financial assets held to generate both income and capital return, such as managed investment schemes, at fair value through other comprehensive income; and • All other financial assets at cost.
Financial liabilities – subsequent measurement	Measured at cost.
Interest income/expenses	Calculated by reference to the instrument's contractual interest rate with any initial premium or discount amortised over the expected life of the instrument.
Impairment	Considered only when it is probable that the carrying amount will not be collectible.
Financial assets – derecognition	Derecognised when either: • the contractual rights to the cash flows from the financial assets expire; or • the entity loses control of the asset.
Financial liabilities– derecognition	Derecognised when the obligation is discharged. A modification of the terms of a financial liability or an exchange of financial liabilities extinguishes the original financial liability and creates a new financial liability.
Other simplification of financial instruments	Hedge accounting is not permitted. Embedded derivatives and certain derivative financial instruments that are not readily identifiable and measurable do not need to be separately recognised.

Basic financial instruments include:

- cash and cash equivalents;
- trade and other receivables;
- security bonds and similar debt instruments;
- term deposits and government bonds;
- units held in managed investment schemes, unit trusts and similar other investment vehicles;
- ordinary shares held in listed and non-listed entities;
- trade and other payables; and
- loans.

Specific more complex financial instruments will be covered by AASB 9 *Financial Instruments*. These may include:

- purchased debt instruments such as listed corporate bonds and convertible notes;
- acquired equity instruments such as preference shares;
- financial guarantee contracts;
- interest rate swaps and forward exchange contracts; and
- commitments to provide a loan at a below market interest rate.

The Board's preliminary views on key topics

Changes in accounting policy/errors and changes in accounting estimates	Voluntary changes in accounting policy and correction of prior period errors are recognised as adjustments to the current period's opening financial position rather than revising comparative financial information. The Board plans to deliberate on mandatory changes in accounting policy and related transitional provisions after considering stakeholder feedback. Changes in accounting estimates will continue to be accounted for prospectively.
Borrowing costs	All borrowing costs are expensed as incurred.

Topics with simplification in terminology and language only

Primary financial statements	The following financial statements form part of Tier 3 GPFS: • a statement of financial position (same as Tier 2, including presentation requirements); • a statement of profit or loss and other comprehensive income (same as Tier 2, including presentation requirements); • a statement of cash flows (using the direct method for 'operating' activities, with no need to separately present 'investing' and 'financing' activities); and • notes to the financial statements.
Separate financial statements	A parent entity presenting separate financial statements can measure its interests in subsidiaries: • at cost; or • at fair value through other comprehensive income; or • using the equity method of accounting.
Inventory	Consistent with Tier 1/Tier 2: • measure inventory at the lower of cost and net realisable value; and • measure inventories held for distribution at cost adjusted for impairment for any loss of service potential.

The Board's preliminary views on key topics

Fair value measurement	Definition and measurement to be consistent with AASB 13 *Fair Value Measurement*. The basis for estimating the fair value of an item will be expressed in a manner that is easier for preparers to follow. Cost may be an appropriate estimate of fair value (at initial or subsequent measurement) when there is a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range, or when there is insufficient recent information available to measure fair value.
Assets held for sale	No special requirements will be developed for accounting of property, plant and equipment or other non-current assets that an entity intends to sell rather than hold for its continuing use.
Investment in associates and joint ventures	In relation to the measurement of interest in associates and joint ventures: • for a parent entity preparing consolidated financial statements — apply the equity method of accounting; • for a parent entity preparing separate financial statements — either at cost or at fair value through other comprehensive income; and • for an investor — at cost or fair value through other comprehensive income in separate financial statements, in addition to preparing equity-accounted financial statements.
Property, plant and equipment	Purchased and internally constructed property, plant and equipment are initially measured at cost and subsequently measured using either the cost model or revaluation model, consistent with Tier 1/Tier 2 reporting requirements.
Volunteer services	An accounting policy choice to recognise volunteer services at fair value, if fair value can be measured reliably.

The Board's preliminary views on key topics

Other topics	The following topics would be accounted for in accordance with the Tier 1/Tier 2 reporting requirements: • foreign currency translations*; • income taxes**; • commitments (in the notes to financial statements); • events after reporting period; • expenses; • going concern; • offsetting; and • provisions, contingent liabilities, and contingent assets. * For foreign currency translations, entities would apply the rate at the transaction date or at the end of the reporting period for monetary assets and liabilities. ** Tax expenses would be based on income tax payable without any allowance for deferred tax assets or deferred tax liabilities.

Tier 3 accounting requirements for which preliminary views have yet to be determined

Statement of changes in equity	The Board will determine the requirement to present a statement of equity changes after considering stakeholders' feedback regarding the usefulness of the information in an NFP context.
Intangible assets	The Board will determine the accounting for intangible assets after considering feedback from stakeholders on the extent of use and types of intangible assets relevant to smaller NFP entities.

Proposed Tier 3 disclosure requirements

The Board welcomes feedback on the approach to the disclosure illustrated in Section 6 of the Discussion Paper for property, plant and equipment; investment property; leases; and changes in accounting policies and correction of errors.

Proposed approach to determine disclosure requirements for topics covered in Tier 3 accounting requirements

Is there a recognition or measurement difference between the Tier 2 and Tier 3 reporting requirements for NFP entities?

No → Use the disclosure requirements from AASB 1060 → Consider further simplification based on stakeholder feedback and benchmarking with selected overseas jurisdictions (e.g. New Zealand)

Yes → Are there any comparable recognition and measurement requirements in other jurisdictions/frameworks?

- Yes → Adopt the appropriate disclosure requirements from comparable jurisdictions/frameworks, and tailor for consistency with Tier 3 Standard
- No → Develop fit forpurpose disclosure requirements (e.g. use the existing disclosure requirements for topics whose requirements are similar to the Tier 3 topics as the base)

Consider the principles for development of Tier 3 accounting requirements

Disclosure examples

Leases

Lessee

- Adopt IFRS for SMEs Standard disclosures for operating leases

Lessor

- Adopt AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-profit and Not-for-profit Tier 2 Entities* disclosures for operating leases with simplification of the language

Changes in accounting policies and correction of errors

Changes in accounting policies

- Develop fit for purpose disclosures based on AASB 1060 and removing non-applicable disclosures

Correction of errors

- Adopt relevant disclosure requirements in the *New Zealand Public Benefit Entity Simple Format Reporting – Accrual (Not-for-Profit)*

Property, plant and equipment and investment property

Initial measurement of donated non-financial assets:

- Develop fit-for-purpose disclosures based on AASB 1060 as required for concessionary leases

Subsequent measurement of property, plant and equipment and investment property:

- Adopt AASB 1060 disclosures with simplification of the language

No specific disclosures for borrowing costs.

Interactions with other reporting tiers

How will the Tier 3 accounting requirements interact with other reporting Tiers?

Smaller NFP entities can elect to 'opt-up' to Tier 1 or Tier 2 AAS in their entirety. However, the Board is yet to decide whether to permit entities preparing Tier 3 GPFS to opt up on a policy-by-policy basis to Tier 1 or Tier 2.

For topics in the scope of the Tier 3 accounting requirements, the Board welcomes feedback on whether to:

- *always allow 'opt-up' to a recognition or measurement policy permitted by Tier 1 or Tier 2 AAS ('free choice')*
- *only allow 'opt-up' when specifically permitted ('cross-reference')*
- *not permit 'opt-up' on a policy-by-policy basis.*

What if the Tier 3 Standard does not cover a certain transaction/balance?

For transactions and other events and conditions that are scoped out from the Tier 3 Standard, an entity should:

- first apply Tier 2 reporting requirements; and
- in the absence of Tier 2 reporting requirements for the specific transaction, apply judgement to develop an accounting policy by reference to:
    - principles and requirements in Tier 3 accounting requirements dealing with similar or related issues; and
    - the definitions, recognition criteria and measurement concepts in the Australian Conceptual Framework that do not conflict with Tier 3 accounting requirements.

When developing an accounting policy, an entity may also consider principles and requirements in Tier 1 and Tier 2 reporting requirements, or pronouncements of other standard-setting bodies with a similar conceptual framework, other accounting literature and accepted industry practices.

How often are the Tier 3 accounting requirements likely to be updated?

It is proposed that revisions will be made:

- no more than once every AASB agenda consultation cycle (5 years); and
- in accordance with *AASB Due Process Framework for Setting Standards*.

Where can I find more information?

How do I provide feedback?

We encourage all stakeholders to provide feedback using any of the following methods:

- online survey (www.surveymonkey.com/r/AASBTIER3NFP)
- e-mail: standard@aasb.gov.au
- formal submission: written submission by lodging online via our 'Open for comment documents' (www.aasb.gov.au/current-projects/open-for-comment/)

The AASB will be conducting outreach during the consultation period. To find out more information, including when and how to register for these events, go to Not-for-Profit Financial Reporting Framework (https://aasb.gov.au/research-resources/hot-topics/not-for-profit-financial-reporting-framework/)

Comments to the AASB are due by 31 March 2023.

Where do I go for more information?

The full version of the Discussion Paper contains:

- the Board's preliminary proposals for the form and accounting requirements of a proposed revised differential reporting framework for NFP entities; and
- the Board's proposal to extend the application of AAS to NFP entities currently not a 'reporting entity' as defined by SAC 1 *Definition of a Reporting Entity*.

Here, you can access the Discussion Paper — *Development of Simplified Accounting Requirements (Tier 3 Not-for-profit Private Sector Entities)*.

To support consultation on the Discussion Paper proposals, the AASB staff have updated Research Report 10 *Legislative and Regulatory Financial Reporting Requirements*. Research Report 10 aims to help with the identification of the entities with financial reporting obligations under Federal and State/Territory legislation that will or may be captured by the Board's proposals.

This document

This Snapshot has been compiled by staff of the AASB for the convenience of interested parties. The views expressed in this Snapshot document should not be considered as an authoritative document issued by the Board.