



Project:	Not-for-Profit Private Sector Financial Reporting Framework	Meeting:	M179
Topic:	Possible differential reporting Tiers for not-for-profit private sector entities	Agenda Item:	5.2
		Date:	10 February 2021
Contact(s):	Evelyn Ling eling@asb.gov.au Ao Li ali@asb.gov.au Fridrich Housa fhousa@asb.gov.au	Project Priority:	High
		Decision-Making:	High
		Project Status:	Decide scope of consultation document and key aspects of possible differential reporting framework

Objective of this paper

- 1 The objective of this staff paper is for the Board to consider possible reporting Tiers that might form the basis of a future differential reporting framework for not-for-profit (NFP) private sector entities, and to **form preliminary views** for inclusion in that discussion paper with regards to (1) the number of reporting Tiers, and (2) the associated reporting bases of those reporting Tiers. Specifically, the Board is asked the following questions:
 - Q1 Do Board members want to consult on potentially increasing reporting requirements for certain NFP private sector entities and if so, do Board members support a preliminary position that Tier 1 reporting requirements (full recognition, measurement and disclosure) should form part of a mandatory differential reporting framework for NFP private sector entities?
 - Q2A Do Board members support a preliminary position that Tier 2 reporting requirements (full recognition and measurement, reduced disclosure) should form part of a mandatory differential reporting framework for NFP private sector entities?
 - Q2B Do Board members want to consult more broadly on the form of Tier 2 reporting requirements (for example, reverting to a Reduced Disclosure Regime)?
 - Q3 Do Board members support developing a further Tier of reporting requirements for application by NFP private sector entities?
- 2 For NFP private sector entities, it may be that it is not the needs of users that primarily dictates the reporting requirements in a reporting Tier nor the existence of users that compels the minimum reporting Tier compliance; in part, this is likely to depend on or be informed by the Board's views developed as part of its NFP Conceptual Framework project as to the users and objective of general purpose financial reports of NFP private sector entities. The Board may make decisions about the number of reporting Tiers and their associated reporting requirements based on considerations such as:
 - (a) what information is adequate to discharge management's stewardship responsibilities;
 - (b) the cost-benefit trade-off for smaller entities;
 - (c) what is the Board prepared to describe as general purpose financial statements;

- (d) the priority it places on Trans-Tasman harmonisation; and
 - (e) whether the Board considers its role is to develop accounting requirements for the entire NFP private sector population.
- 3 Previous AASB/staff research and discussion pertinent to the topic of this staff paper have generally taken the approach of stratifying the NFP population (generally, by various quantitative means and focusing on Australian Charities and Not-for-profits Commission (ACNC) regulated entities due to the availability of the data), then considering reporting requirements that might be proportionate to each 'bucket' of NFP entities. However, the approach taken by staff in the current stage of this project (as outlined by the project timeline discussed by the Board at its November 2020 meeting) is reversed; as possible Tiers of reporting requirements that might feature in a differential reporting framework supported by the Board are first discussed before the Board considers the type of entities that might prepare financial statements that comply with the Board's preliminary proposals about the reporting Tiers. The 'direction' taken in the current approach is consistent with the Board's role in setting accounting standards for Australian entities, while acknowledging that it is not specifically charged with specifying which type of financial statements entities must prepare.
- 4 This staff paper is structured as follows:
- (a) background and reasons for bringing this paper to the Board (paragraphs 5 – 6);
 - (b) whether Tier 1 reporting requirements (full recognition, measurement and disclosure) should form part of a mandatory differential reporting Tier for NFP private sector entities (paragraphs 7 – 19);
 - (c) whether Tier 2 (full recognition and measurement, reduced disclosures) should form part of a mandatory differential reporting framework for NFP private sector entities (paragraphs 20 – 22);
 - (d) whether a mandatory differential reporting framework for NFP private sector entities should include one or more further simpler reporting Tiers (a 'Tier 3' / 'Tier 4') (paragraphs 23 – 33);
 - (e) Appendix A: Information about the NFP private sector population
 - (f) Appendix B: Relevant extracts from Australian Accounting Standards; and
 - (g) Appendix C: Summary of requirements applying to NZ NFP PBE entities.

Background and reasons for bringing this paper to the Board

- 5 At its 11-12 November 2020 meeting, the Board decided to progress with a project on developing a revised financial reporting framework for Australian NFP private sector entities. The Board decided that it would issue, as a first step, a consultation document that would explore possible designs for a revised differential reporting framework to apply to NFP private sector entities. The Board's preliminary views on its supported approach to that framework will form part of that consultation document, and feedback on the consultation document will inform the Board to whether it should develop an exposure draft containing proposals to implement any or all of its preliminary views. This staff paper discusses possible alternatives for one of the key aspects of a differential reporting framework: choice of reporting Tiers.
- 6 In ITC 39 *Applying the IASB's Revised Conceptual Framework and Solving the Reporting Entity and Special Purpose Financial Statement Problems* (May 2018), the Board indicated its preliminary view that it intended to no longer limit the application of Australian Accounting Standards to reporting entities as defined by SAC 1 *Definition of the Reporting Entity* (in addition to those entities who elect to present general purpose financial statements). However, to avoid disproportionately taxing NFP private sector entities formerly presenting

special purpose financial statements that might then be required to prepare general purpose financial statements, during the project the Board noted it might need to develop a different response to that for for-profit private sector entities. While over the past several years, staff and the Board have suggested, and sought feedback on, the number and form of possible reporting Tiers a NFP private sector differential reporting framework could take, and the entities that should be applying each Tier, to date, the Board has not, as a follow-up to ITC 39, formally formed preliminary views for inclusion in a public consultation document on the form of that proposed differential reporting framework.

Whether Tier 1 reporting requirements (full recognition, measurement and disclosure) should form part of a mandatory differential reporting Tier for NFP private sector entities

- 7 At the time of developing AASB 1053 *Application of Tiers of Australian Accounting Standards*, the Board decided to make full IFRS as adopted in Australia mandatorily applicable to only publicly accountable entities in the for-profit private sector and to Governments in the public sector. This outcome is consistent with the approach adopted by the IASB which requires only publicly accountable entities to comply with full IFRS in order to claim IFRS compliance (non-publicly accountable entities are able to apply IFRS for SMEs rather than IFRS). While the Board considered whether to apply the notion of public accountability to NFP entities, when making AASB 1053, the Board decided it would require NFP private sector entities to comply with only Tier 2 reporting requirements. Such action was meant to reduce the financial reporting burden of such entities.¹ However, paragraph BC60 of the Basis for Conclusions to AASB 1053 notes:

“The Board concluded that a NFP entity that is eligible to adopt Tier 2 requirements should be permitted to adopt Tier 1 requirements. This is on the basis that, as noted in relation to the for-profit sector in paragraph BC39, in some jurisdictions, a relevant regulator may decide that in certain circumstances it is more beneficial to the users of financial statements, including the public at large, to include more comprehensive information in the general purpose financial statements. A NFP entity may also find it beneficial to choose to apply Tier 1 requirements in order to claim compliance with full IFRSs as adopted in Australia with a view to enhancing its credibility internationally, in particular in relation to major users of financial statements such as donors and governments.”

- 8 For reporting periods before 1 July 2021, AASB 1054 *Australian Additional Disclosures* requires an entity preparing general purpose financial statements that comply with Australian Accounting Standards – or Australian Accounting Standards – Reduced Disclosure Requirements – to make an explicit and unreserved statement of such compliance (AASB 1054.7, RDR7.1). However, it is not clear how many entities across the NFP private sector currently ‘opt up’ to prepare Tier 1 compliant general purpose financial statements. Research conducted as part of AASB [Research Report No. 11](#) *Review of Special Purpose Financial Statements: Large and Medium-Sized Australian Charities* (Sept 2019) indicated that about 51% (8,127) of large and medium-sized charities registered with the ACNC in 2016 described their financial statements as being general purpose financial statements.² Also, AASB [Research Report No. 5](#) *Financial Reporting Requirements Applicable to Charities* (Oct

1 The Board had concluded that a modified definition of the defined term “public accountability” would not provide a robust basis for identifying NFP private sector entities falling under different reporting Tiers since NFP private sector entities, (with the likely exception of smaller member-based entities), are typically seen as having differing degrees of public accountability in the general sense of the term (AASB 1053.BC45).

2 [Agenda Paper 23.1](#) *Presentation on Research Report 11 findings on charities lodging with ACNC*, AASB Meeting 18 September 2019

2017) observed that no regulators researched for the purposes of that report had imposed such requirements on NFP private sector entities under their responsibility.

- 9 The project objective as included in the project plan approved by the Board is to lead the development of a financial reporting framework that is simple, proportionate, consistent and transparent for NFP private sector entities in Australia³. A possible design of proportionate framework could be one that requires certain NFP private sector entities to comply with Tier 1 reporting requirements.
- 10 AASB Staff Discussion Paper [Improving Financial Reporting for Australian Charities](#) (Nov 2017) suggested various forms an Australian differential reporting framework could take. Some of the alternative frameworks contemplated a 4-reporting Tier framework similar to the framework applying to New Zealand NFP public benefit entities (PBE), while others contemplated a 3-reporting Tier framework, depicted as follows:

4 Reporting Tiers	3 Reporting Tiers
<ul style="list-style-type: none"> • Full recognition, measurement and disclosure • Full recognition and measurement, reduced disclosure • Simplified (modified) recognition, measurement and disclosure • Cash accounting financial statements, including a statement of outcomes and outputs / Cash flow statement 	<ul style="list-style-type: none"> • Full recognition, measurement and disclosure • Full recognition and measurement, reduced disclosure • Cash flow statement

- 11 Feedback from outreach sessions in 2017 largely supported a 3-tier differential reporting approach for charities. Staff reported to the Board in December 2017 that there was clear support for the lowest reporting Tier to be based on cash, and the top reporting Tier to require full recognition, measurement and disclosure [i.e. Tier 1].⁴
- 12 In August 2018 and September 2018, the Board discussed implications of ITC 39 and decided to limit the project scope to for-profit entities only. As reported in the AASB Action Alert of the Board’s August 2018 meeting, the Board decided to issue in the meantime a frequently asked question that would outline how the Board might replace special purpose financial statements for NFP entities by introducing a differential reporting framework of the following form:
- “Bottom tier – most likely be cash accounting, with a statement of resources and commitments (for ACNC NFP’s voluntary basis only, supporting completion of the Annual Information Statement);
 - Middle tier either Tier 2 General Purpose Financial Statements (GPFS) [full recognition and measurement with simplified disclosure] or a modified accrual framework [simplified recognition, measurement and disclosure]; and
 - Top tier –either Tier 1 [full recognition, measurement and disclosure] or Tier 2 GPFS framework (depending on where the middle tier lands).” ([AASB Action Alert 15 August 2018](#))
- 13 In November 2018, the Board sought feedback on a 3-reporting Tier framework of the following form:

³ [AASB November 2019 minutes, AASB Agenda Paper 5.1 Australian Financial Reporting Framework – NFP Private Sector Project Plan](#)

⁴ [Agenda Paper 8.1 of the AASB 12 December 2017 meeting](#)

- full recognition, measurement and disclosure
 - NZ PBE Tier 3 reporting requirements
 - NZ PBE Tier 4 reporting requirements.
- 14 The feedback, as communicated to the Board in November 2019 as part of the project plan for the current project, suggested stakeholders preferred a differential reporting Tier framework that might have as its bases:
- Top Tier:
 - full recognition, measurement and disclosure (for publicly accountable entities) – i.e. Tier 1
 - full recognition and measurement, reduced disclosure, i.e. Tier 2
 - modified accrual (possibly based on NZ PBE Tier 3 reporting requirements)
 - annual information statements for ACNC-registered entities / cash accounting financial statements (possibly based on NZ PBE Tier 4 reporting requirements).
- 15 Staff sought further feedback on a framework of this form as part of its targeted outreach August – October 2020. The feedback suggested tentative support for using NZ PBE Tier 3 and Tier 4 reporting requirements as a starting point to develop the Australian NFP private sector differential reporting framework; however, staff did not specifically seek nor receive feedback on whether Tier 2 reporting requirements were a sufficient, proportionate response to providing useful information to general purpose financial statement users for larger NFP private sector entities, or whether Tier 1 reporting requirements should be mandatory for some such entities.⁵ At the same time, it is worth noting that participants in stakeholder outreach did not raise specific objections to the top tier being Tier 2 with voluntary application of Tier 1 requirements.
- 16 In a forthcoming public consultation on a revised differential reporting framework for NFP private sector entities that is proportionate, staff think specific consideration should be given at this opportunity not only to reducing the reporting burden on NFP private sector entities, but also to whether existing requirements are adequate to meet the needs of users of the general purpose financial statements. In this regard, staff think the Board should form a preliminary view as to whether Tier 1 reporting requirements should remain optional to all NFP private sector entities, or whether it should be introduced as a mandatory differential reporting Tier. Staff note the Board member view may be related to the member’s support or otherwise of Option 1 as set out in Agenda Paper 5.3 (whether the Board should specify a minimum reporting Tier of general purpose financial statements that an entity must prepare).
- 17 Staff suggest the following as reasons supporting requiring Tier 1 reporting requirements being specified as part of a mandatory differential reporting framework:
- comparability with the reporting requirements of similar for-profit private sector entities. Staff think there is not a clear reason supporting reduced disclosure for the largest or otherwise significant NFP private sector entities compared to their for-profit counterparts. For example, Ramsay Health Care Limited (ASX listed for-profit entity), St John of God Health Care Inc (NFP private sector entity) and the Epworth Foundation (NFP private sector entity) all provide healthcare services, including operating private hospitals. All three entities generate significant revenue and have large asset holdings.⁶ However, Ramsay Health Care Limited prepares Tier 1 general purpose financial statements, St John of God

5 [Agenda Paper 5.1 of AASB 16-17 September 2020 Meeting](#)

6 Ramsay Health Care Limited year ending 30 June 2020: Revenue ~\$12,160m; Total Assets ~\$18,058m; Net Profit ~\$309m.

St John of God Health Care Inc year ended 30 June 2020: Revenue ~\$1,842m; Total Assets ~\$1,571m; Net Deficit ~\$9m
 Epworth Foundation financial year ended 30 June 2020: Revenue ~\$900m; Total Assets ~\$1,255m; Net Deficit ~\$36m.

Health Care Inc prepares Tier 2 general purpose financial statements, and the Epworth Foundation prepares special purpose financial statements. (Of note: Alfred Health, a NFP public sector health services entity, prepares Tier 1 general purpose financial statements);

- consistency with the level of reporting required of certain New Zealand NFP private sector entities. One of the goals of the trans-Tasman Single Economic Market agenda is for private NFP entities to be able to use a single set of accounting standards and be required to prepare only one set of financial statements.⁷ However, consistency is arguably already present as Australian entities are not prohibited from preparing Tier 1 general purpose financial statements. Further, not many NZ NFP entities are expected to be required to prepare NZ Tier 1 general purpose financial statements;
 - no additional maintenance costs beyond that that would already currently be required if the current status were maintained;
 - recent research suggesting that large NFP entities operating in particular sectors should prepare Tier 1 general purpose financial statements ([Caring For Growth NP Aged Care Report 2](#) by the Centre for International Corporate Tax Accountability and Research, issued July 2020); and
 - feedback from stakeholders from previous outreach suggesting some appetite for certain NFP private sector entities to be subject to full recognition, measurement and disclosure requirements.
- 18 Staff suggest the following as reasons against Tier 1 reporting requirements being specified as part of a mandatory differential reporting framework:
- the Board only recently decided to further reduce the reporting burden of NFP private sector entities as part of the issue of AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* (Mar 2020);
 - a 3-differential reporting Tier approach is consistent with the number of ‘buckets’ into which some Australian NFP regulatory bodies stratify certain NFP entities under their oversight (including many state regulators of incorporated associations and the ACNC). (However, staff note that other NFP entities, including cooperatives and companies, are stratified into two ‘buckets’ to distinguish their reporting obligations);
 - feedback from outreach to date has not revealed a significant concern that the reduced disclosures are of a concern to users.
- 19 **Staff view.** Staff support requiring certain NFP private sector entities to comply with all recognition, measurement and disclosure specified in Australian Accounting Standards. Staff think that doing so would improve comparability between entities in the for-profit and NFP private sector, especially with regards to entities that might be operating much the same business. For many for-profit entities, economic significance is what dictates whether the entity is required to prepare financial statements; while its ‘public significance’ dictates the minimum form of those financial statements. While economic significance may not be as explicit a primary driver for a requirement to lodge financial statements for NFP private sector entities, staff think that the entity’s public significance should continue to be relevant to the reporting it should make.

7 [Memorandum of Understanding Between the Government of New Zealand and the Government of Australia on the Coordination of Business Law](#) (updated 2013)

Question to the Board

- Question 1 Do Board members want to consult on potentially increasing reporting requirements for certain NFP private sector entities and if so, do Board members support a preliminary position that Tier 1 reporting requirements (full recognition, measurement and disclosure) should form part of a mandatory differential reporting framework for NFP private sector entities?

Whether Tier 2 (full recognition and measurement, reduced disclosures) should form part of a mandatory differential reporting framework for NFP private sector entities

- 20 Presently, NFP private sector entities preparing general purpose financial statements in accordance with Australian Accounting Standards must comply with, at a minimum, Tier 2 reporting requirements.
- 21 Until annual reporting periods beginning on or after 1 July 2021, the specified Tier 2 reporting requirements were those specified under the Reduced Disclosure Requirements regime. The Board further reduced the Tier 2 disclosures for all NFP entities through the issue of AASB 1060 (the Simplified Disclosure requirements regime). In its Basis for Conclusions to AASB 1060, the Board noted:
- “BC51 While the disclosures in the IFRS for SMEs Standard are developed specifically for for-profit private sector entities, the Board agreed that AASB 1060 should also be made applicable to not-for-profit private sector entities and public sector entities, other than the Australian Government and State, Territory and Local Governments. Making AASB 1060 applicable to all Tier 2 entities, whether for-profit or NFP, will result in an immediate reduction in disclosures compared to the current RDR framework, and NFP private sector entities will be able to benefit from this reduction in disclosures while waiting for legislative action on the ACNC legislative review recommendations and for a revised NFP Financial Reporting Framework to be developed. Similarly, public sector entities will also benefit while consideration is being given to improving public sector financial reporting. The Tier 2 disclosure framework may still be relevant to NFP entities as one of the tiers of reporting for that sector even after a revised NFP Financial Reporting Framework is developed.*
- BC52 While respondents to ED 295 had suggested deferring the mandatory date of AASB 1060 for NFP entities possibly until the NFP private and public sector financial reporting frameworks have been finalised, the Board decided against different application dates to avoid the confusion for users that would come from having two Tier 2 reporting frameworks in operation at the same time.”*
- 22 **Staff view.** Having regard to the recent decisions made by the Board in this regard, staff think that it would impose undue costs on NFP private sector entities for the reporting requirements of a Tier 2 to be revised again in the short term (except for new Standards). For this reason, staff think that Tier 2 should be maintained in its current form in a proposed differential reporting framework for NFP private sector entities. Further, maintaining Tier 2 in its present form (full recognition and measurement, reduced disclosure) will maintain consistency between reporting requirements for-profit and NFP private sector entities.

Question to the Board

- Question 2A Do Board members support a preliminary position that Tier 2 reporting requirements (full recognition and measurement, reduced disclosure) should form part of a mandatory differential reporting framework for NFP private sector entities?
- Question 2B Do Board members want to consult more broadly on the form of Tier 2 reporting requirements (for example, reverting to a Reduced Disclosure Regime)?

Whether a mandatory differential reporting framework for NFP private sector entities should include one or more further simpler reporting Tiers (a ‘Tier 3’ / ‘Tier 4’)

- 23 At the time of developing AASB 1053, the Board considered whether to develop further reporting requirements for NFP entities. Paragraphs BC22 to BC24 from the Basis of Conclusions to AASB 1053 summarises the Board’s conclusions in this regard (note: a corresponding footnote has been excluded):
- BC22 The Board considered whether a third tier of reporting requirements for general purpose financial statements should be introduced to provide simpler financial reporting requirements for smaller not-for-profit entities since those entities might find the adoption of Tier 2 requirements overly burdensome on cost-benefit grounds. The Board noted that many NFP entities in the private sector are established as companies limited by guarantee under the Corporations Act or as associations under relevant Incorporated Associations Acts in each State and Territory. Moreover, many non-trading cooperatives are regulated by State or Territory Acts. Having regard to this legislation, the Board noted that a reason for contemplating the need for a third tier was that there is generally no NFP equivalent to the outright exemption from reporting that exists for small proprietary companies (see paragraph BC4 above).*
- BC23 The Board noted that while there is some support from constituents for creating a third tier, there are different views about the requirements of such a tier and the way entities applying those requirements should be identified. The Board also considered the proposals for reporting relief in the Discussion Paper published by the Australian Government in June 2007 titled Financial Reporting by Unlisted Public Companies in relation to the creation of a third tier of reporting requirements for companies limited by guarantee.*
- BC24 The Board decided not to introduce a third tier of reporting requirements on the basis that:*
- (a) the Government intended to alleviate the reporting burden of small companies limited by guarantee through amendments to the Corporations Act; and*
 - (b) Tier 2 requirements for preparing general purpose financial statements would help reduce the disclosure burden of NFP entities significantly.”*
- 24 However, since the issue of AASB 1053, various developments have occurred, including those listed below. These have led some to question whether the Board should revisit its conclusions as to whether there is a need for further differential reporting for NFP private sector entities.
- (a) complex IFRSs (incorporated into AASBs) issued since 2010, including IFRS/AASB 9 *Financial Instruments*, IFRS/AASB 15 *Revenue from Contracts with Customers* and IFRS/AASB 16 *Leases*;
 - (b) the need to resolve the inconsistency between use of ‘reporting entity’ in the IASB’s *Conceptual Framework for Financial Reporting* (revised 2018) and SAC 1 *Definition of a Reporting Entity*, which may require the Board to ‘fill the gap’ if it were to act to limit the ability of entities to prepare special purpose financial statements;
 - (c) the government has indicated, in its response to the ACNC Legislative Review 2018, that it intends to increase the thresholds for classification of charities as ‘medium’ and ‘large’, which is expected to result in fewer charities being required to lodge financial statements with the ACNC; and
 - (d) the New Zealand External Reporting Board (XRB) introduced a 4-Tier differential reporting framework for New Zealand NFP public benefit entities (PBE). As set out in XRB A1 *Application of the Accounting Standards Framework* an expenses threshold dictates the form of ‘Tier 2/ Tier 3/ Tier 4’ financial statements applying to NZ NFP PBE entities that are not publicly accountable. NZ NFP PBE entities that are publicly accountable or meet a specified expense threshold are required to prepare general purpose financial statements that comply with NZ Tier 1 reporting requirements.

- 25 Staff have identified the following as reasons why one or more further tiers of reporting requirements might be appropriate:
- feedback from various AASB outreach activities on a potential revised differential framework supporting a demand for one or more tiers of simpler reporting requirements, including support for non-accrual based differential reporting requirements;
 - the need to provide a proportionate response for NFP private sector entities that may no longer be able to present special purpose financial statements. At present, the threshold for requiring NFP private sector entities that are incorporated associations or registered charities to prepare financial statements that comply with Australian Accounting Standards is a lot lower than that specified for companies reporting solely under the *Corporations Act 2001*;
 - a further tier of reporting could be an avenue to addressing areas of accounting complexity such as consolidation and equity accounting which could be reasons why NFP private sector entities are currently not preparing general purpose financial statements; and
 - some of the more recent Australian Accounting Standards specify accounting that might be regarded as overly complex for the operations and abilities of smaller NFP private sector entities. Introducing a third reporting Tier may allow the Board to simplify – for example, in language or in modified requirements – the accounting requirements in complex IFRS/AASBs for application by certain NFP private sector entities.
- 26 Internationally, some other jurisdictions maintain three or four tiers of reporting requirements for charities. The AASB Research Report No.5 *Financial Reporting Requirements Applicable to Charities* (October 2017) included a review of the financial reporting framework applicable to charities in New Zealand, the United Kingdom, Hong Kong, Singapore, South Africa and Canada. The reporting frameworks of New Zealand, Hong Kong and South Africa include a third or fourth reporting Tier.
- 27 Staff have identified the following as reasons why a further tier of reporting requirements might not be appropriate:
- introducing further tiers of reporting requirements may add to reporting complexity for entities, especially those at the ‘edges’ of the tiers;
 - introducing a further tier of reporting requirements may make it more difficult for practitioners to move between entities, to the extent the reporting requirements significantly differ;
 - the Board will be tasked with maintaining a further tier of reporting requirements (e.g. consideration of the applicability of new IFRS requirements for the Tier);
 - inconsistent with accounting for similar transactions in a like manner (maintaining sector neutrality); there is no real difference between small for-profit private sector entities and NFP private sector entities in this regard, yet small for-profit private sector entities wishing to prepare general purpose financial statements might not be able to access any accounting ‘relief’ offered by such further reporting Tier;
 - the Board will need to form a view as to whether these financial statements are general purpose financial statements, and if not, how they are positioned within Australian Accounting Standards and the Australian conceptual framework; and
 - a further tier of reporting requirements responds to costs resulting from the need to prepare financial statements, but does not address whether there is a need for the financial statements in the first place.
- 28 **Staff view.** Staff have mixed views. Some staff support developing a ‘Tier 3’ reporting Tier, noting stakeholder support for a further reporting Tier, the need to provide a proportionate response for non-reporting entities, and to respond to the concern that compliance with existing Australian Accounting Standards may not serve the needs of users of these entities. Other staff do not support developing a further reporting Tier, primarily to maintain consistency with the number of reporting Tiers available to for-profit entities. These staff think

that the concerns about proportionate reporting could be addressed through perhaps the introduction of exceptions or 'practical relief' or limiting accounting policy choices for certain entities, and education and guidance on the concept of materiality. Further, assuming Tier 1 forms part of a proposed mandatory differential reporting framework, staff do not support developing a 'Tier 4' in addition to a 'Tier 3' reporting Tier for the reasons noted in paragraph 28 above (this does not preclude cash as a basis for Tier 3). Staff think that superseding of the SAC 1 reporting entity concept does not necessarily require the Board to specify accounting standards for all NFP private sector entities (that is, the Board could decide that certain (small) NFP private sector entities should continue to be scoped out of Australian Accounting Standards).

Question to the Board

Question 3 Do Board members support developing a further Tier of reporting requirements for application by NFP private sector entities?

Next steps: Possible reporting bases for a Tier 3

- 29 If the Board supports introducing a further reporting Tier, it will need to decide the form of reporting requirements that form the basis of that Tier and whether it will describe such reporting requirements as general purpose financial statements. Possible reporting bases could include:
- (a) Tier 3 Alt A – simplified (e.g. restricted) recognition and measurement, Tier 2-SD disclosure
 - (b) Tier 3 Alt B – modified recognition and measurement (e.g. different measurement criteria or accounting policies), Tier 2-SD disclosure
 - (c) Tier 3 Alt C – based on NZ PBE Tier 3 reporting requirements; i.e. modified recognition and measurement, disclosures relevant to NFP private sector entities including new disclosures limited only to Tier 3 entities (e.g. service performance information, fundraising) in a 'performance report'
 - (d) Tier 3 Alt D – cash basis of accounting, disclosures relevant to NFP private sector entities including new disclosures limited only to Tier 3 entities (e.g. service performance information, fundraising) in a 'performance report'.
- 30 Tier 3 Alt C above is consistent to the approach New Zealand has taken with respect to its Tier 3 reporting requirements and Tier 3 Alt D is consistent to the approach New Zealand has taken with respect to its Tier 4 reporting requirements. Staff have previously sought feedback on adopting reporting requirements that mirror the NZ NFP PBE Tier 3 and NZ NFP PBE Tier 4 reporting requirements, or that uses the NZ NFP PBE Tier 3 or Tier 4 Standard as a starting point. The feedback from the targeted outreach conducted August – October 2020 did not indicate any significant objection to a third reporting Tier being based on NZ NFP PBE Tier 3 requirements.
- 31 A significant difference between Tier 3 Alt C and Tier 3 Alt D, and Tier 1 and Tier 2 reporting requirements, is the extent of disclosures that do not currently form part of the AASB suite of disclosures, including on service performance information (see Agenda Paper 5.4). These Alternatives arguably take an approach that views financial information as being of less importance (and hence, cost-benefit may support different recognition and measurement criteria) to users of the NFP private sector entity compared to information about its stewardship of its not-for-profit objectives. With regards to Alt D, it is arguable whether it is the responsibility of the Board to require disclosure of information about an entity's

stewardship of its not-for-profit objectives to the extent this information is not in the nature of 'explanatory notes' to the cash-based financial statements.

- 32 With respect to Tier 3 Alt D, some jurisdictions (New Zealand, Canada, the United Kingdom) permit certain NFP entities to prepare financial statements using the cash basis of accounting. Staff note that a cash flow statement and other statements need not be described as being 'general purpose financial statements', but that there is precedence for this: the International Public Sector Accounting Standards Board (IPSASB) literature considers that general purpose financial reports might be prepared using the cash basis of accounting. Similarly, the New Zealand External Reporting Board (XRB) Standard A1 *Application of the Accounting Standards Framework* describes all financial reports prepared in accordance with standards issued by the XRB as 'general purpose financial reports'. (Staff note that a Board decision to develop a reporting Tier based on cash accounting may have implications for the Board's project to extend the applicability of its Conceptual Framework for Financial Reporting to NFP entities.)
- 33 Following on from the Board's decisions at this meeting as to whether a further reporting Tier should be proposed as part of the form of a potential differential reporting framework for inclusion in a discussion paper, and the Board's decisions on Agenda Paper 5.4, staff will further develop and analyse the potential reporting bases above for Board consideration at a future meeting.

Appendix A: Information about the NFP private sector population

- 1 A NFP private sector entity with a separate legal structure may be established in a variety of manners; for example, as an incorporated association under a State Act, a company registered under the *Corporations Act 2001* (public company limited by guarantee, proprietary limited company) or as an indigenous corporation or through an Act of Parliament. Some NFP private sector entities may not have a separate legal form, such as unincorporated associations, cooperatives and trusts.
- 2 NFP private sector entities operate across a variety of fields, including as:
 - religious organisations
 - parents and citizens committees or associations
 - universities and research organisations
 - non-government schools (e.g. Melbourne Grammar or the Catholic Education Commission of Victoria)
 - animal welfare organisations
 - domestic and international aid agencies
 - homeless shelters and family violence support organisations
 - aged care centres and childcare groups
 - as museums and galleries
 - environmental protection groups
 - legal aid centres
 - sporting clubs
 - political parties and unions.
- 3 Some social enterprises are NFP entities; other social enterprises are for-profit entities.
- 4 Part of the NFP private sector legal entity population is registered with the ACNC as a registered charity. However, not all entities registered with the ACNC have a separate legal structure (e.g. unincorporated associations, building funds). However, presently, per the ACNC website,⁸ there are approximately 56,000 charities registered with the ACNC:
 - (a) approximately 20,720 of these charities are classified – based on a revenue threshold⁹ – as ‘medium’ (17%) or ‘large’ (19%), and are consequently required to lodge financial statements prepared in accordance with Australian Accounting Standards with the ACNC. The remaining charities are ‘small’ and are not required to lodge financial statements with the ACNC. Approximately one-third of the ‘small’ charities report revenues of less than \$50,000;¹⁰
 - (b) 44% of these charities employ no staff and are entirely volunteer-run;
 - (c) the number of registered charities is presently expected to grow at about 4% annually;
 - (d) some of the 56,000 registered charities are public sector entities (e.g. University of Melbourne);

8 [webpage last accessed 9 February 2021.](#)

9 The ACNC classifies a charity as a ‘medium’ charity if its annual revenue is more than \$250,000 and less than \$1 million, and as a ‘large’ charity if its annual revenue is \$1 million or more. These thresholds are under review and are expected to be increased in 2021.

10 The number of charities required to lodge financial statements is expected to decrease in the near future, following proposed revisions to the revenue threshold arising from recommendations made by the ACNC Legislative Review 2018. The joint media release ‘Easing the regulatory burden on charities’ issued 15 December 2020 by The Hon Josh Frydenberg MP (Treasurer of the Commonwealth of Australia) and Senator the Hon Zed Seselja (Assistant Minister for Finance, Charities and Electoral Matters) suggests that over 5,000 charities will no longer be required to produce financial statements once changes to the financial reporting thresholds are finalised (expected 2021).

- (e) there may be multiple separate charity registrations within an accounting economic entity, which may choose to report to the ACNC together as part of an approved group;¹¹
 - (f) charities must lodge an Annual Information Statement with the ACNC, which includes information about its revenues, expenses, assets and liabilities. Small charities may prepare this information using a cash basis of accounting.
- 5 Whether a NFP private sector entity has to prepare financial statements that comply with Australian Accounting Standards may be dictated by more than one regulatory body; e.g. the regulator with charge of the legislation under which it is incorporated (e.g. Corporations Act 2001, Consumer Affairs Victoria) and also the one or more regulatory bodies that has oversight of the NFP private sector entity's registered status (e.g. ACNC, the Commonwealth Department of Education, Skills and Employment, the Commonwealth Department of Health, or other state/territory government agency). AASB [Research Report No.5 Financial Reporting Requirements Applicable to Charities](#) (Oct 2017) and AASB [Research Report No.10 Legislative and Regulatory Financial Reporting Requirements](#) (Sept 2019) provide more information about an NFP private sector entity's reporting obligations.
- 6 Streamlining activities to remove such duplication of financial reporting obligations for entities that are also registered as a charity with the ACNC have been underway over the past several years. For example, a NFP company limited by guarantee that is a registered charity now only has to lodge financial statements with the ACNC as required by the ACNC; it no longer has to satisfy also *Corporation Act 2001* obligations with respect to preparation of financial statements.¹² In many instances (but not all), the streamlining activity has left the ACNC as the body with responsibility for specifying whether the NFP private sector entity is required to prepare financial statements in accordance with Australian Accounting Standards.¹³ In addition, for periods up to the 2024 reporting period, where there is not yet a streamlined reporting arrangement, the ACNC has indicated that it will accept the same financial report for an incorporated association, cooperative or charitable fundraising organisation as that submitted to the entity's state or territory regulator. However, ACNC streamlining efforts alone will not eliminate the issue of small NFP private sector entities being required to prepare financial statements that are compliant with Australian Accounting Standards, as there remain a significant number of NFP private sector entities that are not registered charities.

11 e.g. the ACNC website notes that the Surf Life Saving Australia group includes 264 separately registered charities.

12 per s.111L of the Corporations Act 2001, Part 2M.1 – 2M.3 do not apply to companies registered under the *ACNC Act 2012* (see <https://asic.gov.au/for-business/running-a-company/charities-registered-with-the-acnc/corporations-act-provisions-that-no-longer-apply-to-charities-registered-with-the-acnc/>)

13 An exception is for indigenous entities registered both with the ACNC and the Office of the Registrar of Indigenous Corporations (ORIC): such entities are not required to submit an Annual Information Statement or financial statements to the ACNC.

Appendix B: Relevant extracts from Australian Accounting Standards

The following extracts from Australian Accounting Standards may be relevant to forming views on a differential reporting framework for NFP private sector entities:

General purpose financial statements are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs.
[AASB1060.Appendix A]

The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity. ... [Conceptual Framework.1.2]

General purpose financial reports are not designed to show the value of a reporting entity; but they provide information to help existing and potential investors, lenders and other creditors to estimate the value of the reporting entity. [Conceptual Framework.1.7]

Other parties, such as regulators and members of the public other than investors, lenders and other creditors, may also find general purpose financial reports useful. However, those reports are not primarily directed to these other groups. [Conceptual Framework.1.10]

General purpose financial reports provide information about the financial position of a reporting entity, which is information about the entity's economic resources and the claims against the reporting entity. Financial reports also provide information about the effects of transactions and other events that change a reporting entity's economic resources and claims. Both types of information provide useful input for decisions relating to providing resources to an entity.
[Conceptual Framework.1.12]¹⁴

The following types of entities shall prepare general purpose financial statements that comply with Tier 1 reporting requirements:

- (a) *for-profit private sector entities that have public accountability and are required by legislation to prepare financial statements that comply with either Australian Accounting Standards or accounting standards; and*
- (b) *the Australian Government and State, Territory and Local Governments.* [AASB1053.11]

Tier 2 reporting requirements shall, as a minimum, apply to the general purpose financial statements of the following types of entities:

- (a) *for-profit private sector entities that do not have public accountability;*
- (b) *not-for-profit private sector entities; and*
- (c) *public sector entities, whether for-profit or not-for-profit, other than the Australian Government and State, Territory and Local Governments.*

¹⁴ The *Conceptual Framework for Financial Reporting* (the *Conceptual Framework*) references above currently apply only to for-profit private sector entities. However, these paragraphs are similarly included in the *Framework for Preparation and Presentation of Financial Statements* (the *Framework*). In addition, the *Framework* contemplates the general purpose financial statements of a NFP reporting entity serving a broader set of users (including donors, taxpayers, beneficiary members of the community and parties performing a review or oversight function on behalf of other users), and acknowledges that users of such financial statements are generally not concerned with obtaining a financial return on an investment in the entity but with the ability of the entity to achieve its objectives, whether financial or non-financial (Framework.AusOB2.1 and AusOB3.1). The extension of the application of the *Conceptual Framework* to NFP entities, including identification of users and the objective of general purpose financial statements of NFP entities is the subject of another current Board project. As noted in Agenda Paper 5.1, staff are conscious that Board decisions on that project may impact its decision making on this project, and are consequently monitoring the progress of that Board project.

These types of entities may elect to apply Tier 1 reporting requirements in preparing general purpose financial statements. [AASB 1053.13]

AASB 1053 Application of Tiers of Australian Accounting Standards applies to:

- (a) each not-for-profit entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;*
- (b) general purpose financial statements of each not-for-profit entity that is a reporting entity;*
- (c) each entity that elects to prepare financial statements that are, or are held out to be, general purpose financial statements;*
- (d) financial statements of GGSs prepared in accordance with AASB 1049; and*
- (e) for-profit private sector entities that are required by legislation to prepare financial statements that comply with either Australian Accounting Standards or accounting standards; and*
- (f) other for-profit private sector entities that are required only by their constituting document or another document to prepare financial statements that comply with Australian Accounting Standards, provided that the relevant document was created or amended on or after 1 July 2021. [AASB 1057.18]*

Appendix C: Summary of requirements applying to NZ NFP PBE entities

Generally speaking, New Zealand law (various Acts and Regulations) specifies which types of NFP entities must prepare financial statements that apply accounting standards set by the New Zealand External Reporting Board (XRB) (or otherwise). For example, the New Zealand *Charities Act 2005* requires all charitable entities to complete an annual return, and for that annual return to be accompanied by financial statements that are prepared in accordance with generally accepted accounting practice (or, where permitted, a non-GAAP standard).¹⁵

However, the XRB standards themselves then state what and how those entities report, by way of reporting thresholds. Reporting thresholds are specified by the XRB in XRB A1 *Application of the Accounting Standards Framework*. These thresholds dictate the type of general purpose financial reporting that a NZ NFP entity needs to comply with, as summarised in the table below:

Tier	NZ NFP entity type	Applicable NZ Standards	Basis
Tier 1	Has public accountability or is a PBE with total expenses > \$30million (a large PBE)	PBE Standards	IPSAS
Tier 2	Has no public accountability, and has total expenses < \$30million but > \$2million, and that elects to be in Tier 2	PBE Standards Reduced Disclosure Regime (PBE Standards RDR)	IPSAS
Tier 3	Has no public accountability and has total expenses ≤ \$2million, that elects to be in Tier 3	PBE Simple Format Reporting Standard - Accrual (SFR-A)	XRB's Simple Format Reporting Requirements
Tier 4	Has no public accountability and is allowed by law to use cash accounting, that elects to be in Tier 4	PBE Simple Format Reporting Standard - Cash (SFR-C)	XRB's Simple Format Reporting Requirements

NZ Tier 1 to Tier 3 reporting requirements are considered GAAP, while NZ Tier 4 is described as being non-GAAP. In addition, PBE Simple Format Reporting Standard - Accrual (SFR-A) and PBE Simple Format Reporting Standard - Cash (SFR-C) require an NFP entity to prepare a 'performance report' which includes a statement of service performance.

In contrast, Australian legislation (various Acts and Regulations) generally distinguishes the financial reporting obligations of Australian NFP entities by way of reporting thresholds specified in the legislation itself. The reporting thresholds differ from Act to Act, although generally speaking entities are sorted in two or three 'Tiers' or 'levels', based on size criteria. Not all legislation requires the preparation of financial statements that are in accordance with Australian accounting standards (or accounting standards).

¹⁵ s41, s42A of the [NZ Charities Act 2005](#)