



Project:	Australian Financial Reporting Framework	Meeting	AASB 19 February M169
Topic:	Not-for-profit (NFP)/Public Benefit Entity (PBE) Definition	Agenda Item:	6.1
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Objective of this paper

- 1 In this paper, staff ask the Board to decide whether an Exposure Draft (**ED**) should be issued which proposes to:
 - replace the current definition of ‘not-for profit (**NFP**) entity’ in Australian accounting standards with the definition used for public benefit entities (**PBEs**) in New Zealand (but retaining the term NFP entity); and
 - provide guidance to assist an entity that prepares general purpose financial statements (GPFS) to determine whether it is a for-profit (**FP**) entity or an NFP entity for the purpose of applying the accounting standards.
- 2 The attached draft ED is based on the New Zealand *ED 2018 Amendments to XRB A1 Appendix A (When is an Entity a Public Benefit Entity)* (**XRB ED 2018**) issued in December 2018, adapted as necessary for the Australian context.

Reasons for the Board to consider this issue at this meeting

- 3 The Board decided in February 2018 that the term ‘NFP entity’ should be retained as a significant term for accounting purposes but that AASB staff should consider at a

later time amending the definition and guidance through monitoring the New Zealand Accounting Standards Board's (**NZASB**) project on its definition of PBE.¹

- 4 The NZ External Reporting Board (**XRB**) has now issued an exposure draft of proposed amendments to their guidance on the definition of PBE with a comment period until Friday 29 March 2019². If this guidance is also going to be exposed for comment in Australia, it would be useful to do this sooner rather than later, so that feedback received from Australian stakeholders can be passed on to the XRB prior to the NZ proposals being finalised.

Summary of staff recommendations

- 5 Staff recommend that the Board:
- approves the issue of AASB ED in Appendix subject to it being finalised out of session by a Board sub-committee (to ensure all the examples are adapted for the Australian context); and
 - allows for a comment period of 120 days.

Attachments

Agenda Paper 6.2: DRAFT Exposure Draft Not-for-profit Definition and Guidance

Questions for Board members

1. Does the Board agree for Staff to issue an AASB ED proposing:
 - a. to replace the current definition of NFP entity with the definition of PBE (as amended per paragraph 17 below), but retaining the term NFP; and
 - b. include guidance on applying the definition as set out in the attached ED, subject to the ED being finalised out of session by a Board sub-committee to ensure all references and examples are appropriate for the Australian context?
2. Does the Board agree that the proposed definition and proposed guidance be exposed as amendments to AASB 1057 *Application of Australian Accounting Standards* and that the proposed guidance be exposed as 'Implementation Guidance' in AASB 1057 which would form an integral part of AASB 1057, i.e. have mandatory status, when finalised?
3. If the Board agrees to issue the ED referred to in Question 1, does the Board agree with a comment period of 120 days?

¹ See minutes from [Board Meeting 162 – February 2018, Agenda item 11](#)

² [XR Exposure Draft 2018 Amendments to XRB A1 Appendix A \(Invitation to Comment, December 2018\)](#)

Background

- 6 The classification of an entity as a FP entity or a NFP entity is important because the application of the Australian accounting standards can differ depending on whether an entity is classified as a FP or NFP entity. Different recognition, measurement, presentation and disclosure requirements can apply to an entity depending on whether it is a FP or NFP entity.
- 7 The distinction between a FP entity and NFP entity would become even more significant if the AASB develops a separate NFP reporting framework with simplified recognition and measurement criteria and the application of different tiers for NFP entities.
- 8 As part of the consultation undertaken in relation to the AASB's standard setting frameworks³ at the end of 2017, the AASB asked for specific feedback in relation to the definition of NFP entity, and whether there was sufficient guidance on how to distinguish entities as FP entities and NFP entities.
- 9 The majority of respondents supported retaining the term 'NFP', but requested more guidance from the AASB in determining whether an entity is FP or NFP under the accounting standards.⁴
- 10 In addition, a clear majority of respondents supported the AASB monitoring and working with the NZASB on its project to update the definition of a PBE.
- 11 Several respondents noted the potential usefulness of the definition of a PBE as having a greater focus on the nature and purpose of a NFP/PBE. It provides a positive statement of what a NFP/PBE is, rather than what it is not.
- 12 Noting the feedback received, the Board decided in February 2018 to retain the term NFP entity as significant term for accounting purposes, but to consider at a later time amending the definition and guidance through monitoring the NZASB's project on improving the guidance on its definition of PBE.⁵
- 13 In December 2018, the XRB issued the XRB ED 2018 which proposes amendments to Appendix A of XRB A1 *Application of the Accounting Standards Framework*. Appendix A provides guidance to assist an entity in determining whether it is a PBE or an FP entity.

³ ITC 37 *The AASB's Standard Setting Frameworks for For-Profit Entities and Not-for-Profit Entities*

⁴ For detailed summary of the feedback received on ITC 37 see [staff paper 11.1 tabled at the February 2018 meeting \(M162\)](#)

⁵ Refer to: [AASB Action Alert No 189, dated 15 February 2018](#)

- 14 Staff have reviewed the definition of PBE and the associated draft revised guidance and consider that it would generally be appropriate for use under the Australian standard setting framework, subject to limited amendments as noted below.

What we are proposing

- 15 Staff propose to:
- (a) replace the definition of 'NFP entity' as currently included in a number of Australian Accounting Standards with the definition of 'PBE' as included in Appendix A of NZ XBR A1 *Application of the Accounting Standards Framework*, while retaining the term 'NFP entity' (see paras 16 to 19 below);
 - (b) issue the proposed amended guidance from XRB ED 2018 to assist entities applying the revised definition (see paras 20 to 23 below) subject to it being finalised out of session by a Board sub-committee to ensure all the examples are adapted for the Australian context;
 - (c) remove the NFP entity definition from the AASB 102 *Inventories*, AASB 116 *Property, Plant and Equipment* and AASB 136 *Impairment of Assets* and instead include both, the revised definition and the guidance, in AASB 1057 *Application of Australian Accounting Standards* (see paras 24 to 29 below); and
 - (d) issue the exposure draft with a 120 days comment period (see paras 30 to 31 below).

Replacing the definition

- 16 The term 'NFP entity' is currently defined in Australian Accounting Standards⁶ as:

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 it controls.

- 17 Staff propose replacing the definition of 'NFP entity' with the definition used for a PBE in paragraph 3 of XRB ED 2018 (whilst retaining the term NFP), amended as follows:

~~an reporting~~ entity whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders

- 18 The definition is identical to the PBE definition in XRB ED 2018 except for the replacement of 'reporting entity' with 'entity'. Staff do not believe that the reference to 'reporting entity' is necessary or adds anything further in defining 'NFP entity'.

⁶ Refer to AASB 102, para Aus6.1, AASB 116, para Aus 6.1, and AASB 136, para Aus 6.2

Furthermore, a reference to 'reporting entity' may cause confusion in the Australian context, in which it is currently defined differently to the definition contained in the IASB's revised *Conceptual Framework for Financial Reporting*.

- 19 The definition from the XRB ED 2018 aligns with that from the United Kingdom and has a greater focus on the nature and purpose of a NFP entity/PBE. It enables greater guidance to be provided for an entity to determine whether it a NFP or FP entity. In order to use the guidance from the XRB ED 2018, it will be necessary to align the definition of NFP to the NZ definition of PBE.

Issuing the NZ guidance

- 20 The NZ definition of a PBE comprises two interdependent parts:
- (a) the primary objective to provide goods or services for community or social benefit; and
 - (b) the provision of equity to support that primary objective rather than for a return to equity holders.
- 21 The proposed guidance clarifies that both parts of the definition need to be assessed in combination when determining an entity's classification. It sets out several indicators to be considered in determining whether an entity meets the definition of a PBE and discusses each of the indicators in turn. It acknowledges that in many cases it will be unlikely that any one indicator will be conclusive in determining whether an entity meets the definition of a PBE and it may be necessary to consider several indicators together. Professional judgement will be required when considering and balancing the assessment of each indicator.
- 22 The Appendix further provides examples to illustrate the application of the guidance.
- 23 Staff note that XRB ED 2018 contains a number of New Zealand specific references and examples which will need to be adapted to ensure that the ED is appropriate for the Australian context before it is issued. While staff have commenced discussions with stakeholders about possible replacement examples, the attached draft ED does not yet reflect all necessary changes. As the changes will not change the general principles of the guidance, staff consider that the ED can be finalised by a Board sub-committee, provided the Board agrees to proceed with this project.

Question to the Board:

Q1: Does the Board agree issue an AASB ED proposing to:

- (a) replace the current definition of NFP entity with the definition of PBE as amended per paragraph 17 above, but retaining the term NFP; and
- (b) include guidance on applying the definition as set out in the attached ED, subject to the ED being finalised out of session by a Board sub-committee to ensure all references and examples are appropriate for the Australian context?

How should the changes be implemented?

- 24 The definition of a NFP entity is currently included in three separate standards, being AASB 102 *Inventories*, paragraph Aus 6.1, AASB 116 *Property, Plant and Equipment*, paragraph Aus 6.1, and AASB 136 *Impairment of Assets* paragraph Aus 6.2. However, staff consider neither of these to be very obvious or logical. If the definition is to be revised and additional guidance provided, staff recommend that the definition be removed from the accounting standards listed above and instead be included in one standard only, together with the associated guidance.
- 25 Staff have considered the following options of implementing the proposed changes:
- (a) as amendments to AASB 1057 *Application of Australian Accounting Standards*
 - (b) as amendments to AASB 1053 *Application of Tiers of Australian Accounting Standards*; or
 - (c) via a new, separate standard.
- 26 The objective of AASB 1057 is to specify the types of entities and financial statements to which Australian Accounting Standards (including Interpretations) apply⁷. The types of entities referred to in the objective of AASB 1057 would include NFP entities and it would therefore appear appropriate that a NFP entity is defined in the Appendix to AASB 1057, and that the implementation guidance is also separately provided within AASB 1057.
- 27 In contrast, the objective of AASB 1053 is narrower than AASB 1057, being to set out the application of tiers of Australian Accounting Standards to different categories of entities preparing general purpose financial statements. For that reason, staff consider AASB 1057 the better of the two options.
- 28 Staff have also considered whether the definition of NFP and associated guidance should be issued as a separate stand-alone standard rather than an amendment to an existing standard, but believe this is not warranted on the basis that the definition is directly related to the application of accounting standards, and that it would be more confusing for users if it was contained in a separate standard.
- 29 Staff further note that XRB A1 Appendix A notes that “This appendix forms an integral part of XRB A1 Application of the Accounting Standards Framework”, which implies that compliance with the guidance is mandatory in NZ. This is consistent with similar application guidance issued by the AASB in recent years, e.g. AASB 2018-4 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Public Sector Licensors*, AASB 2016-8 *Amendments to Australian Accounting Standards – Implementation Guidance for Not-for-Profit Entities* in relation to AASB 9 and AASB 15 and the Australian implementation

⁷ See paragraph 1 of AASB 1057

guidance for not-for-profit public sector entities that is included in AASB 124 *Related Party Disclosures*. On that basis, staff recommend including a similar statement in the ED.

Question to the Board:

Q2: Does the Board agree that the proposed definition and proposed guidance be exposed as amendments to AASB 1057 and that the proposed guidance be exposed as 'Implementation Guidance' in AASB 1057 which would form an integral part of AASB 1057, ie have mandatory status, when finalised?

Comment period

- 30 Staff recommend that a 120 day comment period is provided in relation to the ED. In this regard, staff have weighed the significance of the proposals and criteria for comment periods along with the advantage of providing the XRB with additional feedback/comments.
- 31 Staff have noted that a three month comment period is provided in relation to the XRB ED 2018 and that a 90-day comment period would also be consistent with the AASB's Policies and Processes⁸. However, the proposals represent a more significant change for Australian stakeholders because constituents have to consider the proposed change in the definition of what is an 'NFP' and whether the proposed guidance and examples are appropriate in the Australian context. On that basis, staff recommend providing a longer comment period of 120 days.

Question to the Board:

Q3: If the Board agrees to issue an AASB ED (Q1), does the Board agree with a comment period of 120 days?

Next steps

Date	Project milestone
19/2/19	<u>February 2019 AASB meeting</u> – staff to obtain Board's approval to issue an AASB ED proposing: <ul style="list-style-type: none">to replace the current definition of NFP entity with the definition of PBE, but retaining the term NFP; and

⁸ [AASB Policies and Processes – May 2011, para 50](#)

Date	Project milestone
	<ul style="list-style-type: none"> guidance on applying the definition as set out in the attached ED subject to it being finalised out of session by a Board sub-committee in relation to ensuring all references and examples are appropriate for the Australian context
12/3/19 (or as decided by the Board)	Board sub-committee finalises ED
15/3/19 - 15/7/19	ED released and open for comment
19/7/19 – 3/9/2019	Staff to collate feedback on ED, recommend next steps to the Board and prepare draft amending Standards to the Board for consideration.
17/9/2019	<p><u>September 2019 AASB meeting</u> – staff to obtain Board’s approval for issue of amending Standards.</p> <p>Any changes advised by the Board to be approved/finalised out of session by Board sub-committee.</p>
17/9/2019- 1/10/19	(If necessary) staff to make changes to the amending Standards based on Board’s directions in September board meeting and to be approved out of session.
8/10/19	Final guidance/amending Standards issued.

<p>Question to the Board</p> <p>Do Board members agree with the proposed plan above, including that the ED is finalised out of session through a sub-committee of the Board?</p>
