The AASB's Not-for-Profit Entity Standard-Setting Framework

Introduction

What is the purpose of this Framework?

1 *The AASB's Not-for-Profit Entity Standard-Setting Framework* sets out how the Australian Accounting Standards Board (AASB) uses International Financial Reporting Standards (IFRS Standards) issued by the International Accounting Standards Board (IASB) to develop, issue and maintain Australian Accounting Standards for the not-for-profit (NFP) sector.

2 This Framework is a basis for the AASB to consider in determining justified modifications to IFRS Standards for the NFP sector and when NFP-specific standards, amendments, guidance or examples are required. This Framework is intended to provide greater transparency of the Board's decision-making process, and facilitate consistency in the Board's future decision-making, including both:

(a) whether it should undertake a project to modify IFRS Standards for NFP entities; and

(b) the form and extent of any modification.

3 This Framework accompanies *The AASB's For-Profit Entity Standard-Setting Framework*, which sets out how the AASB uses IFRS Standards to develop, issue and maintain Australian Accounting Standards for for-profit entities.

What are not-for-profit entities?

4 A not-for-profit (NFP) 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"[1].

5 NFP entities exist in both the private and public sectors. Examples of NFP entities include, but are not limited to:

(a) government entities;

(b) charities;

(c) incorporated associations; and

(d) some large and small proprietary companies.

1 Defined in various AASB Standards, including AASB 102 *Inventories*, paragraph Aus6.1.

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What role does the Australian Accounting Standards Board play in setting accounting standards for NFP entities?

6 Other standard-setters and regulators (eg the Australian Charities and Not-for-profits Commission (ACNC) and public sector finance ministers), typically in legislation, determine which entities are required to prepare and publicly lodge financial statements and which need to comply with accounting standards. For non-regulated entities (eg trusts), consistent documents determine whether financial statements need to be prepared and if they need to comply with accounting standards.

7 The AASB establishes the type and nature of financial statements to be prepared by entities required to report in accordance with Australian Accounting Standards.

8 The AASB is required, under s229 of the *Australian Securities and Investments Commission Act 2001* (ASIC Act), to consider the suitability of a proposed standard for different types of entities, including NFP entities, and to ensure there are appropriate accounting standards for each type of entity that must comply with Australian Accounting Standards[2].

General purpose financial statements

9 The AASB sets standards only for general purpose financial statements (GPFS). The objective of a GPFS is to provide financial information to existing or potential users that is useful in making decisions about providing resources[3].

10 Users of a GPFS are not in a position to require an entity to prepare reports tailored to their particular information needs[4]. The AASB has established a differential reporting framework currently consisting of two tiers of reporting requirements for preparing GPFS[5].

11 For entities not legislatively required to prepare financial statements, if the individuals preparing the financial statements are members of Chartered Accountants Australia and New Zealand (CAANZ), CPA Australia or the Institute of Public Accountants, APES 205 *Conformity with Accounting Standards* requires them to take all reasonable steps to ensure an entity that has general purpose users is preparing a GPFS.

2 For the text of s229, see the Appendix.
3 AASB's *Framework for the Preparation and Presentation of Financial Statements*, paragraph OB2.
4 AASB 101 *Presentation of Financial Statements* defines general purpose financial statements as "… 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".
5 see AASB 1057 *Application of Australian Accounting Standards*.

Special purpose financial statements[6]

12 The AASB currently does not set standards for special purpose financial statements (SPFS)[7], as these financial statements should only be prepared where users can tailor the SPFS to their own information needs, and therefore do not need a standard setter or regulator to require the information for them.

13 Accordingly, those responsible for the preparation of SPFS, such as directors, determine to what extent, if at all, SPFS comply with accounting standards.

14 The AASB has specified in AASB 1057 *Application of Australian Accounting Standards*[8] that some individual disclosure focused accounting standards must be complied with by each entity that is required to prepare financial reports in accordance with Part 2M.3 of the *Corporations Act 2001*. Consequently, these entities are required to apply the specified Standards regardless of whether GPFS or SPFS are prepared. The AASB included this requirement in AASB 1057 as part of moving legacy out of legislation and into Australian Accounting Standards and formed no view as to the suitability or otherwise of these requirements for users of SPFSs.

15 In some instances regulators have also recommended compliance with recognition and measurement requirements of Standards[9].

External reporting beyond financial reporting

16 The AASB's powers and functions are set out under Part 12 Section 227 of the ASIC Act. Section 227 (1)(c)[10] allows the AASB to "formulate accounting standards for other purposes" and it is under this function that the AASB has the mandate to develop Australian Accounting Standards addressing external reporting beyond financial reporting. Further, the AASB's *Corporate Plan 2017-2018*[11] sets out a strategic objective (strategy no. 5) to "influence initiatives to develop standards and guidance that meet user needs for external reporting beyond financial reporting". The AASB considers that this Framework is equally applicable to accounting standards relating to both financial and beyond financial reporting.

Enforcement

17 Enforcement of preparation of financial statements and compliance with accounting standards is the responsibility of other regulators (eg ACNC). It is not the responsibility of the AASB.

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6 The AASB is currently undertaking a project to introduce a revised IASB Conceptual Framework into Australia which would remove Statement of Accounting Concepts SAC 1 *Definition of the Reporting Entity*, the current reporting entity concept and the ability to prepare SPSF when an entity is required to prepare financial statements in accordance with Australian Accounting Standards.

7 AASB 1054 *Australian Additional Disclosures* defines SPFS as financial statements other than GPFS.

8 See AASB 1057 paragraph 7.

9 See ASIC Regulatory Guide 85: *Reporting requirements for non-reporting entities*.

10 For the text of s227, see the Appendix.

11 See *AASB-AUASB Corporate Plan 2017-18*.

What assumptions underpin the NFP standard-setting framework?

18 To maintain confidence in the Australian economy (including the NFP sector), obtain the benefits of comparability within and across sectors, facilitate movement of professionals across sectors, and ensure the cost of complying with Australian Accounting Standards does not outweigh the benefits, this Framework is predicated on the assumptions below.

19 Applying this Framework may result in different requirements for the private and public NFP sectors. It is also likely that NFP-specific examples and guidance will be provided. However, this Framework will not always result in NFP-specific standards, amendments, guidance or examples.

20 When there is evidence these assumptions are no longer appropriate for the Australian context, this Framework will be reconsidered. The AASB and/or its oversight body, the Australian Financial Reporting Council (FRC), periodically consult to determine whether these assumptions remain appropriate[12].

IFRS Standards are appropriate as a base

21 IFRS Standards (including Interpretations) are appropriate as a base for the following reasons:

(a) they are developed by an expert standard-setting board, the International Accounting Standards Board (IASB), and its views represent international consensus on best practice for publicly accountable for-profit entities;

(b) they are developed following a stringent due process which encourages parties interested in financial reporting to express their views;

(c) the AASB is able to participate in the development of the IASB's proposals to the extent it considers appropriate[13]; and

(d) IFRS Standards can be modified appropriately for NFP issues, as demonstrated by the International Public Sector Accounting Standards Board (IPSASB) continuing to base its Standards on IFRS, departing only to the extent appropriate for public sector issues[14].

12 In 2015 the AASB commenced a review of the adoption of IFRS Standards to hear the views and experiences of Australian stakeholders, with the objective of assessing the ongoing relevance of IFRS Standards to Australian for-profit and not-for-profit (NFP) reporting entities (eg charities and public sector entities). AASB Research Report No 4 *Review of Adoption of International Financial Reporting Standards in Australia* summarises the stakeholder feedback received.

13 The AASB's typical involvement in the IASB standard-setting process is set out in the *AASB Policies and Processes*.

14 The AASB is also updating the policy document *AASB's Approach to International Public Sector Accounting Standards*, which will set out the circumstances in which it would be appropriate for the FRC and the AASB to agree to move to IPSASB. These circumstances will be reviewed periodically.

Transaction neutrality

22 Like transactions and events should be accounted for in a like manner for all types of entities, reflecting their economic substance (transaction neutrality), unless there is a justifiable reason not to do so (see below)[15].

15 AASB Research Report No 4 identifies, from the targeted outreach conducted, the common key benefits of the policy of transaction neutrality identified by NFP entities' stakeholders as:

- it facilitates the mobility of accounting professionals from one sector to another (ie moving from the for-profit sector to the NFP sector and vice versa) and facilitates access to reporting expertise across sectors
- where relevant, it enables benchmarking of financial performance and position across sectors.

What is the NFP standard-setting framework?

23 The AASB develops, issues and maintains accounting standards for the NFP sector. The AASB's objectives are to:

(a) use IFRS and transaction neutrality as a starting point, however, when justified, make modifications to address:

(i) user needs;

(ii) Australian-specific legislation;

(iii) prevalence and magnitude of issues specific to the NFP sector;

(iv) NFP application issues;

(v) public interest issues relevant to financial reporting; and

(vi) undue cost or effort considerations;

(b) make justified modifications to IFRS Standards via:

(i) 'Aus' paragraphs amending, adding or deleting an IFRS Standard's scoping, recognition, measurement, presentation or disclosure requirement (eg AASB 15 *Revenue from Contracts with Customers*); and/or

(ii) Australian-specific guidance in additional Appendices or specific examples (eg AASB 10 *Consolidated Financial Statements*);

(c) address in NFP-specific standards, interpretations or guidance, NFP issues that have not been comprehensively or appropriately dealt with in existing IFRS Standards, including where no relevant IFRS Standard exists (eg AASB 1054 *Australian Additional Disclosures*, AASB 1058 *Income of Not-for-Profit Entities*); and

(d) permit GPFS to be prepared using either Tier 1 (compliance with Australian Accounting Standards) or Tier 2 (compliance with Australian Accounting Standards – Reduced Disclosure Requirements)[16].

16 The AASB's project on improving the Australian Financial Reporting Framework may result in additional tiers being developed.

What triggers the AASB to consider NFP issues?

24 The AASB considers the need for NFP-specific standards, amendments, guidance or examples when:

(a) a new IFRS Standard or pronouncement – or amendments to an existing IFRS Standard or pronouncement – is issued;

(b) a new IPSASB Standard or pronouncement is issued, which may include modifications to IFRS Standards;

(c) a post-implementation review (PIR) of an IFRS Standard or Australian Accounting Standard gives a compelling reason to do so;

(d) Australian constituents raise the need with the AASB (via agenda consultation, outreach activities, or written or verbal submissions);

(e) Australian-specific legislation with financial reporting implications is issued;

(f) senate or other legislative enquiries contain financial reporting recommendations; or

(g) evidence of diversity in accounting practices exists, and the prevalence and magnitude of the issue results in entities' reported performance or financial position not reflecting economic reality (eg regulator surveillance program results).

When might NFP-specific standards or guidance be justified?

25 The primary purpose and benefit of NFP-specific standards, amendments, guidance or examples is to improve the information provided to users of an NFP entity's financial statements. NFP issues may affect NFP entities in either the public sector, the private sector, or both.

26 The AASB uses professional judgment in reaching its conclusions about NFP-specific standards, amendments, guidance or examples. As part of it normal standard-setting due process, reasons for conclusions in relation to NFP-specific standards, amendments, guidance or examples will be documented in the related Basis for Conclusions, which will also document the extent the Standard differs from IFRS Standards and IPSASB Standards (where applicable).

27 AASB's disagreement with the IASB's treatment is unlikely to provide a good reason, in and of itself, for changing the requirement in an IFRS Standard.

28 Justifiable circumstances may include:

(a) financial reporting inadequately reflecting the objectives and qualitative characteristics of financial reporting as set out in the *Framework for the Preparation and Presentation of Financial Statements* (Conceptual Framework)[17];

(b) user information needs not addressed – eg NFP reporting not adequately reflecting that:

(i) resource providers and service recipients are users[18] (eg AASB 1058);

(ii) users of an NFP entity's financial statements may also require information on non-financial accountability and stewardship, not just financial returns (eg AASB 1055 *Budgetary Reporting*, and for all NFP entities, service performance reporting, addressing the quality of the goods and services produced and information about outputs/outcomes that may be non-financial); and

(iii) NFP entity assets are generally held for their service potential not cash generation (eg amendments to AASB 136 *Impairment of Assets*, AASB 140 *Investment Property*);

(a) the prevalence and magnitude of NFP-specific transactions, circumstances and events results in NFP entities' reported performance or financial position not reflecting economic reality (eg transfers of assets at significantly less than fair value primarily to enable a NFP entity to achieve its objectives, and for public

17 See Chapter 1 and Chapter 3 in the Appendix to the Conceptual Framework.
18 The AASB Conceptual Framework identifies users as suppliers of resources, whereas the IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* includes both suppliers of resources and service recipients.

sector entities, the provision of social benefits and related sustainability and sovereign power issues);

(b) Australian public interest issues relevant to financial reporting require additional disclosures (eg audit fees). Such disclosures must:

(i) meet the objectives and qualitative characteristics of financial reporting as set out in the Conceptual Framework;

(ii) have strong user support;

(iii) deliver user benefits that outweigh any undue cost or effort for preparers, including impacts on international competitiveness; and

(iv) no other existing legislative or voluntary reporting frameworks provide the information or are more appropriate avenues to obtain the information;

(c) NFP application issues resulting from terminology differences and current practice issues, differences in the accountability or regulatory framework, governance or financial management differences or alignment with other financial frameworks;

(d) undue cost or effort of preparing and disclosing information outweigh the benefits. For example, when there are existing legislative requirements for different but similar information for similar purposes (eg government finance statistics in the public sector), differences in resources available to NFP entities when implementing the requirements, mixed groups with both for-profit and NFP entities needing to amend accounting on consolidation, or the prevalence and magnitude of the transactions in the NFP sector mean the basis for the IASB's considerations of undue cost or effort for for-profit entities is not valid for NFPs; and

(e) incompatibility with existing NFP standards – applying IFRS Standards results in inconsistency with other existing NFP-specific standards and guidance or the Conceptual Framework.

Are the identified issues sufficiently significant to warrant NFP-specific standards, amendments, guidance or examples?

29 The AASB assesses the following for each of the NFP private sector and the NFP public sector, and then together, when deciding whether the identified NFP issue is so significant that a modification to an IFRS Standard is warranted:

(a) the quantitative and qualitative significance of a transaction, event or circumstance on an entity's financial statements taken as a whole, and the likely impact on a user's decision making ability;

(b) the quantitative and qualitative significance of a transaction, event or circumstance on relevant sectors, the Australian economy as a whole and the likely impact on users' decision making ability;

(c) whether a modification will increase or decrease internal consistency within IFRS Standards and/or Australian Accounting Standards, including the Conceptual Framework; and

(d) the costs of the specific change relative to the benefits.

30 The impact of modifying IFRS Standards or developing NFP-specific standards or guidance needs to be considered in relation to the suite of Standards as a whole, in addition to the implications for a specific area of financial reporting. Minimising differences between the financial statements of NFP entities and for-profit entities is beneficial for preparers and users of NFP financial statements whose familiarity with financial statements arises from experience in the for-profit sector, and for entities that are members of mixed groups[19].

19 For the purposes of this Framework, a mixed group is a NFP group that includes at least one material for-profit subsidiary where that for-profit subsidiary applies accounting policies that differ from those of the mixed group and that may need to be adjusted on consolidation.

How are NFP-specific standards and/or guidance developed?

31 Having determined that NFP-specific standards and/or guidance are required, the AASB considers whether to:

(a) modify the existing IFRS through 'Aus' paragraphs, additional appendices for implementation guidance, additional examples; or

(b) develop an additional Australian-specific standard or interpretation.

32 In making this determination the AASB considers the:

(a) extent and importance of Australian-specific legislation, user needs or public interest issues in maintaining confidence in the Australian economy;

(b) impact on international perceptions of Australian Accounting Standards complying with IFRS Standards;

(c) inadvertent or inappropriate use of additional guidance by publicly accountable for-profit entities that may result in non-IFRS compliance;

(d) extent of modifications required.

33 In developing the proposals for new standards or guidance, the AASB considers:

(a) consistency with the Conceptual Framework;

(b) consistency with existing Australian Accounting Standards and interpretations;

(c) other authoritative material that is relevant, such as:

(i) other national standard-setter pronouncements, including the New Zealand Accounting Standards Board; and

(ii) IPSASB Standards, Guidance and Conceptual Framework;

34 The AASB follows its normal due process for setting new standards and guidance.

35 Modifications to IFRS Standards include:

(a) increasing or reducing scoping through 'Aus' paragraphs to maintain consistency with existing NFP standards and guidance, reduce legislative conflict or avoid undue cost or effort;

(b) amending recognition and measurement through 'Aus' paragraphs to better meet the objectives or qualitative characteristics of NFP financial reporting, avoid undue cost or effort in applying the requirements, and the coherence of the NFP suite of standards and guidance is maintained;

(c) eliminating options in accounting treatments if not relevant or inappropriate[20];

(d) disclosures added, amended or deleted where they relate to recognition and measurement modifications or to better meet the objectives or qualitative characteristics of NFP entities' financial reporting, or to avoid undue cost or effort in preparing the disclosures;

(e) specific guidance and examples, generally in a separate Appendix or additional materials, to improve ease of use and consistency of application[21]; and

(f) transitional relief 'Aus' paragraphs to address recognition and measurement modifications or provide sufficient time for the NFP sector to address implementation issues.

20 If an option needs to be added, this generally means the issue is significant enough to warrant development of an Australian-specific NFP standard.

21 The majority of IFRS Standards will require additional guidance and examples.

Appendix

Australian Securities and Investments Commission Act 2001

s227 AASB's function and powers

(1) The functions of the AASB are:
- (a) to develop a conceptual framework, not having the force of an accounting standard, for the purpose of evaluating proposed accounting standards and international standards; and
- (b) to make accounting standards under section 334 of the Corporations Act for the purposes of the corporations legislation (other than the excluded provisions); and
- (c) to formulate accounting standards for other purposes; and
- (d) to participate in and contribute to the development of a single set of accounting standards for world-wide use; and
- (e) to advance and promote the main objects of this Part.

…

s229 Generic and specific standards

(2) Accounting standards made or formulated by the AASB may:
- (a) be of general or limited application (including a limitation to specified bodies or undertakings); and
- (b) differ according to differences in time, place or circumstance.

(3) In making and formulating accounting standards, the AASB:
- (a) must have regard to the suitability of a proposed standard for different types of entities; and
- (b) may apply different accounting requirements to different types of entities; and
- (c) must ensure that there are appropriate accounting standards for each type of entity that must comply with accounting standards.