EXPOSURE DRAFT **ED 144**

November 2005

Proposed Australian Guidance to accompany AASB 1004 *Contributions*

Prepared by the
Australian Accounting Standards Board

Australian Government

Australian Accounting Standards Board

Commenting on this Exposure Draft

Comments on this Exposure Draft should be forwarded so as to arrive by 5 December 2005. Comments should be addressed to:

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A copy of all non-confidential submissions will be placed on public record on the AASB's website: www.aasb.com.au.

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This Exposure Draft is available on the AASB's website: www.aasb.com.au. Alternatively, any individual or organisation may obtain one printed copy of this Exposure Draft by contacting:

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Australian Accounting Standard AASB 1004 *Contributions* is set out in paragraphs 1 to 15. All paragraphs have equal authority. Paragraphs in **bold type** state the main principles. Terms defined in this Standard are in *italics* the first time they appear in the Standard. AASB 1004 is to be read in the context of other Australian Accounting Standards, including AASB 1048 *Interpretation and Application of Standards*, which identifies the UIG Interpretations. In the absence of explicit guidance, AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies.

PREFACE

Reasons for Issuing this Exposure Draft

The Australian Accounting Standards Board (AASB) issued AASB 1004 *Contributions* applicable only to not-for-profit entities in July 2004. The corresponding Standard applicable to for-profit entities is AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* that was also issued in July 2004 as part of implementing the Financial Reporting Council's policy of adopting the Standards of the International Accounting Standards Board (IASB) for application to reporting periods beginning on or after 1 January 2005.

The requirements in AASB 1004 are broadly consistent with the requirements under pre-2005 Australian Accounting Standards. However, there has been a re-interpretation of the requirements in AASB 1004, foreshadowed in ED 125 *Financial Reporting by Local Governments*, that results in some types of contributions that were previously initially recognised as revenue being initially recognised as a liability. In addition, the Board has reconsidered the interaction between AASB 1004 and AASB 118 *Revenue*. The proposed guidance in this Exposure Draft gives effect to the re-interpretation. The guidance is expected to be an interim measure, as explained in the section below on "Current and Future Standards addressing Revenue Recognition", and is expected to be withdrawn in due course when AASB 1004 is subject to a fundamental review.

In addition, the AASB intends to withdraw AAS 27 *Financial Reporting by Local Governments*, AAS 29 *Financial Reporting by Government Departments* and AAS 31 *Financial Reporting by Governments* and will release an Exposure Draft proposing the withdrawal of these Standards shortly. Each of these Standards contain revenue recognition requirements, and in some cases they may result in a different accounting treatment than the requirements in AASB 1004. In due course, the proposed guidance in this Exposure Draft will replace some of the guidance that existed in AAS 27, AAS 29 and AAS 31.

Main Features of this Exposure Draft

The Exposure Draft includes Australian Guidance to accompany, but not form part of, AASB 1004. The Guidance articulates:

(a) circumstances in which a contribution is initially recognised as a liability; and

(b) circumstances in which a contribution is initially recognised as income.

Although AASB 1004 has been included as part of this Exposure Draft, no changes are proposed in this Exposure Draft to the requirements of AASB 1004. However, a forthcoming Exposure Draft on the withdrawal of AAS 27, AAS 29 and AAS 31 may propose changes to AASB 1004.

It is intended that the proposed guidance be available for annual reporting periods beginning on or after 1 January 2005. However, the requirements in AAS 27, AAS 29 and AAS 31 will override the guidance when an inconsistency arises until AAS 27, AAS 29 and AAS 31 are withdrawn.

Current and Future Standards addressing Revenue Recognition

The following three Australian Accounting Standards specifically address revenue recognition:

(a) AASB 118 *Revenue* that is applicable to for-profit and not-for-profit entities and contains requirements for the treatment of revenue arising from the sale of goods, the rendering of services and the use by others of entity assets yielding interest, royalties and dividends;

(b) AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* that is applicable to for-profit entities and contains requirements for government grants received or receivable; and

(c) AASB 1004 *Contributions* that is applicable to not-for-profit entities and contains requirements for contributions received or receivable that are not within the scope of AASB 118[1].

There are a number of projects currently being undertaken by the IASB and the International Public Sector Accounting Standards Board (IPSASB) that will potentially impact on the current Australian Accounting Standards in the short to medium term. These projects include:

(a) the withdrawal of, or amendment to, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* by the IASB. The IASB intends to either withdraw or amend IAS 20 to be more consistent with the government grants requirements in IAS 41 *Agriculture*. IAS 20 contains a deferral and matching approach to recognising grant income, in contrast with the approach in IAS 41 that requires grant income to be recognised when the grantee has fulfilled the “conditions” (if any) associated with the grant. The government

1 For example, contributions received or receivable that arise from the rendering of services are accounted for in accordance with AASB 118.

grant accounting requirements in IAS 41 are more closely aligned with the requirements in AASB 1004. Accordingly, if IAS 20, and consequently AASB 120, are amended to be more consistent with the requirements in IAS 41, consideration would be given to broadening the application of AASB 120 to both for-profit and not-for-profit entities, in respect of government grants. It is expected that revenue from non-exchange transactions not addressed in AASB 118 or a revised AASB 120 will continue to be addressed in AASB 1004; and

(b) the issuance of an Exposure Draft on Non-exchange Revenue by the IPSASB. The IPSASB expects to approve for issue an Exposure Draft addressing non-exchange revenue in 2005. The AASB intends to issue the Exposure Draft as the basis of an Australian Exposure Draft, and consider the position that the IPSASB reaches in developing a final Standard to determine whether AASB 1004 should be amended.

It is expected that the proposed guidance in this Exposure Draft will be issued as an interim measure, to be withdrawn when AASB 1004 is subject to a fundamental review. At this stage, this will only occur when the IPSASB releases a Standard on Non-exchange Revenue. Provided that the AASB agrees with the requirements in the IPSASB Non-exchange Revenue Standard, a revised AASB 1004 based on the IPSASB Standard will be issued, subject to due process.

In addition to the short to medium term projects on revenue recognition, the IASB is currently undertaking long-term research projects that address measurement and revenue recognition. At this stage it is not known what impact these projects will have on the various IASB, and consequently AASB, revenue recognition Standards.

Request for Comments

Comments are invited on any of the proposals in the Exposure Draft by 5 December 2005. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the major issues. The AASB regards both critical and supportive comments as essential to a balanced review of the issues and will consider all submissions, whether they address all issues in this Exposure Draft or only one issue.

Specific Matters for Comment

The AASB would particularly value comments on:

(a) whether guidance should be issued at this stage to accompany AASB 1004, in light of the likelihood of future changes given the various projects being undertaken by the IASB and IPSASB;

(b) the usefulness of the proposed guidance on the circumstances in which a contribution is initially recognised as a liability, rather than income;

(c) whether there are any situations that would result in the guidance leading to a liability being initially recognised, when it is more appropriate for income to be recognised;

(d) whether there are any situations that would result in the guidance leading to income being initially recognised, when it is more appropriate for a liability to be recognised;

(e) whether the distinction between applying AASB 118 and AASB 1004 is sufficiently clear; and

(f) whether, instead of treating contributions in relation to the rendering of services under AASB 1004 and using the proposed guidance, such amounts should be treated in accordance with the rendering of services requirements in AASB 118.

COMPARISON WITH INTERNATIONAL PRONOUNCEMENTS

Compliance with IAS 18 and IAS 20

Not-for-profit entities that comply with the requirements of AASB 1004 may not simultaneously be in compliance with the requirements of IAS 18 *Revenue* or IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. This is because the recognition criteria in AASB 1004 are different from those in AASB 118 and AASB 120.

AASB 1004 and IPSASs

International Public Sector Accounting Standards (IPSASs) are issued by the International Public Sector Accounting Standards Board of the International Federation of Accountants.

There is no specific IPSAS dealing with contributions at present. However, as explained in the section “Current and Future Standards addressing Revenue Recognition” in the Preface, it is expected that the IPSASB will approve for issue an Exposure Draft on Non-exchange Revenue in 2005.

ACCOUNTING STANDARD AASB 1004

The Australian Accounting Standards Board makes Accounting Standard AASB 1004 *Contributions* under section 334 of the *Corporations Act 2001*.

D.G. Boymal
Dated 15 July 2004 Chair – AASB

ACCOUNTING STANDARD AASB 1004

CONTRIBUTIONS

Application

1. This Standard 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 and that is a reporting entity;

(b) general purpose financial reports of each other not-for-profit entity that is a reporting entity; and

(c) financial reports of not-for-profit entities that are, or are held out to be, general purpose financial reports.

2. This Standard applies to annual reporting periods beginning on or after 1 January 2005.

3. This Standard shall not be applied to annual reporting periods beginning before 1 January 2005.

4. The requirements specified in this Standard apply to the financial report where information resulting from their application is material in accordance with AASB 1031 *Materiality*.

5. When applied or operative, this Standard supersedes:

(a) AASB 1004 *Revenue* as notified in the *Commonwealth of Australia Gazette* No S 283, 17 June 1998; and

(b) AAS 15 *Revenue* as issued in June 1998.

6. Both AASB 1004 and AAS 15 remain applicable until superseded by this Standard.

7. Notice of this Standard was published in the *Commonwealth of Australia Gazette* No S 294, 22 July 2004.

Measurement of Contributions

8. Income shall be measured at the fair value of the *contributions* received or receivable.

Recognition of Contributions of Assets

9. Income arising from the contribution of an asset to the entity shall be recognised when, and only when, all the following conditions have been satisfied:

(a) the entity obtains control of the contribution or the right to receive the contribution;

(b) it is probable that the economic benefits comprising the contribution will flow to the entity; and

(c) the amount of the contribution can be measured reliably.

10. A contribution occurs when an entity receives an asset, including the right to receive cash or other forms of asset without directly giving approximately equal value to the other party or parties to the transfer; that is, when there is a *non-reciprocal transfer*. Contributions would, for example, include donated assets. Contributions that are income exclude *contributions by owners*.

11. In some cases it may be difficult to determine whether the entity has control of a contribution or the right to receive a contribution. One such case could be economic benefits expected to be received under a multi-year public policy agreement. The entity does not obtain control of a contribution under such an agreement until it has met conditions or provided services or facilities that make it eligible to receive a contribution. On this basis, under multi-year public policy agreements, income would be recognised only in relation to contributions received or receivable under policy agreements. Another example is where a donor pledges a donation to an entity. If the pledge is not enforceable against the donor, the entity does not control the contribution.

12. In some cases it may be difficult to determine whether the entity is giving approximately equal value to the other parties to a transfer.

This is particularly the case where, for example, fees are charged by a not-for-profit entity for the potential use of a general pool of facilities. In circumstances where clubs and professional associations charge fees in return for contributors being able to enjoy the use of facilities, receive publications or practice in a particular vocation for a defined period, an exchange transaction can be presumed and the fees would not be treated as contributions. The recipient of the fees would have a contractual or constructive obligation to refund some or all fees if it were unable to provide the facilities or services. In circumstances where the benefits to contributors are only nominal, such as acknowledgment letters, general information about the entity's activities and satisfaction of contributors' altruistic goals, the fees are in the nature of contributions.

Liabilities Forgiven

13. The gross amount of a liability forgiven by a credit provider shall be recognised by the borrower as income.

14. Where equity is substituted for a liability, this is not treated as a forgiveness.

Disclosures

15. The following information shall be disclosed:

(a) contributions of assets, including cash and non-monetary assets; and

(b) the forgiveness of liabilities.

APPENDIX

DEFINED TERMS

This appendix is an integral part of AASB 1004.

Contributions	Non-reciprocal transfers to the entity.
Contributions by owners	Future economic benefits that have been contributed to the entity by parties external to the entity, other than those which result in liabilities of the entity, that give rise to a financial interest in the net assets of the entity which: (a) conveys entitlement both to distributions of future economic benefits by the entity during its life, such distributions being at the discretion of the ownership group or its representatives, and to distributions of any excess of assets over liabilities in the event of the entity being wound up; and/or (b) can be sold, transferred or redeemed.
Non-reciprocal transfer	A transfer in which the entity receives assets or services or has liabilities extinguished without directly giving approximately equal value in exchange to the other party or parties to the transfer.

AUSTRALIAN GUIDANCE

Australian Guidance accompanies, but is not part of, AASB 1004.

G1. Amounts received or receivable that meet the definition of "contributions" in the Appendix to AASB 1004 *Contributions* are treated in accordance with AASB 1004. When amounts received or receivable relate to the rendering of services[1] they are accounted for in accordance with AASB 118 *Revenue* (or AASB 111 *Construction Contracts*), but only if they are not contributions.

G2. As defined in AASB 1004, contributions are distinguished from contributions by owners.

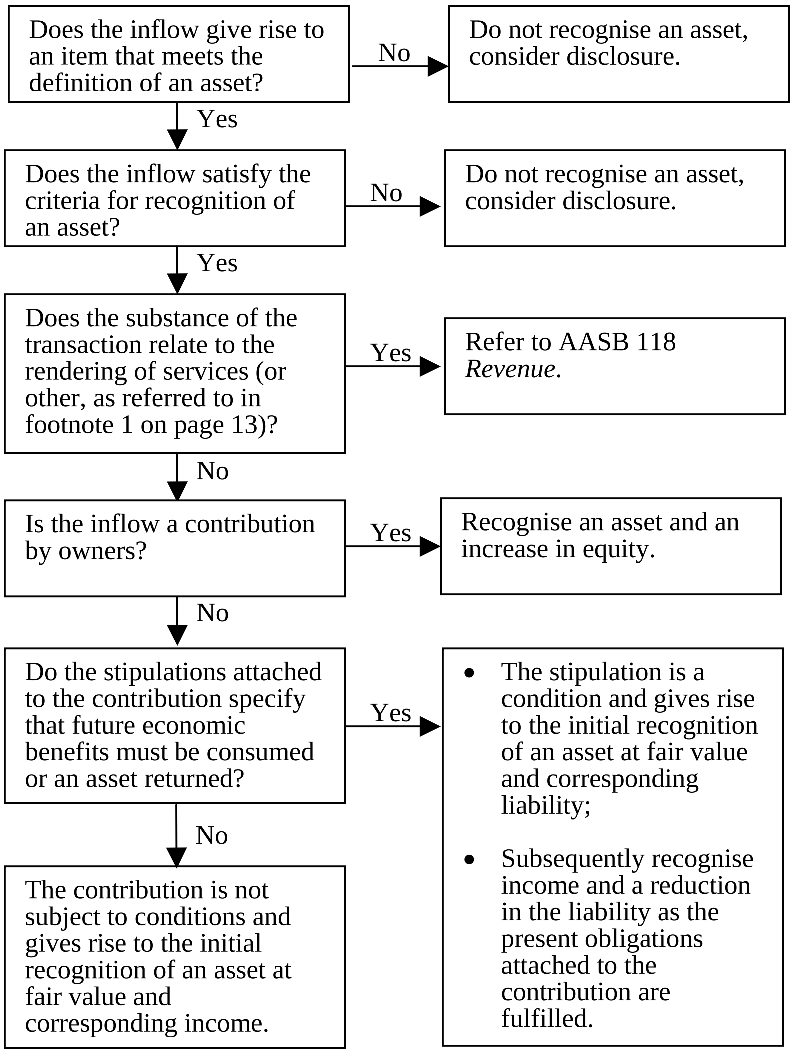
G3. When an amount comprises two components that are different in substance, each component is accounted for separately. For example, an entity holds a fundraising function and charges an attendance fee that partly relates to the rendering of services for the provision of meals and entertainment and partly a donation. The amount relating to the rendering of services is treated in accordance with AASB 118. The amount relating to the donation is treated in accordance with AASB 1004. Similarly, a local government's rates may include a user-pays component to the extent ratepayers are charged a variable amount depending on, for example, the level of garbage collection services they choose to receive. The balance of the rates is treated in accordance with AASB 1004.

G4. Contributions may be subject to stipulations. Stipulations are terms imposed upon the use of a contribution by laws or regulation, or by a binding arrangement with an entity external to the reporting entity, and not controlled by it. Stipulations attached to contributions may be in the nature of conditions. For the purpose of this guidance, a condition is a stipulation which specifies that the future economic benefits or service potential embodied in the asset must be consumed by the recipient entity as specified otherwise an asset must be returned to the donor (see paragraphs G7-G12). If a stipulation specifies the purposes for which future economic benefits or service potential embodied in the asset may be used by the recipient entity, but does not specify that an asset must be returned to the donor if not used as specified, then the stipulation is not a condition (see paragraphs G13 and G14).

1 The expression "rendering of services" is used in this guidance because this is the key activity that not-for-profit entities undertake, but in relevant circumstances should be taken to also encompass the sale of goods and the use by others of an entity's assets yielding interest, royalties and dividends.

G5. The flowchart below summarises how the recipient entity accounts for amounts received or receivable[2].

Flowchart for determining the recognition of inflows



2 When an amount comprises two components that are different in substance, the flowchart is separately applied to each component.

Substance of stipulations

G6. In determining whether a stipulation attached to a contribution is a condition, it is necessary to consider the substance of the stipulation and not merely its legal form. The mere specification that a contribution must be consumed or an asset returned to the donor is, in itself, not sufficient to give rise to a liability when the entity gains control of the asset. When examining the substance of the stipulations attached to a contribution, the recipient entity will consider whether the requirement to return an asset is enforceable, or would be enforced by the donor. If the stipulations attached to the contribution are such that the donor could not enforce them, they do not give rise to a condition. If past experience with the donor indicates that the donor never enforces the stipulations attached to a contribution to return an asset when a stipulation has not been fulfilled, then the recipient entity concludes that the stipulation has the form, but not the substance of a condition. The recipient entity may have no experience with the donor, or no experience of not fulfilling stipulations. In such circumstances and in the absence of evidence to the contrary, the recipient entity assumes that the donor would enforce the stipulation, and therefore the stipulation is a condition.

Contributions with conditions

G7. A condition imposes on the recipient entity a performance obligation and a return obligation. In fulfilling a performance obligation, the recipient entity consumes the future economic benefits or service potential embedded in the contributed asset as specified. In many circumstances, a contribution that contains stipulations relating to a performance obligation relate to the rendering of services. As noted in paragraph G1, any amounts received or receivable that relate to the rendering of services are accounted for in accordance with AASB 118.

G8. When a contribution with conditions requiring the contribution to be transferred to third parties is received or receivable, the recipient entity incurs a present obligation to transfer economic benefits or future service potential to third parties when it initially gains control of the asset subject to the condition. A present obligation arises because the recipient entity is unable to avoid the outflow of resources as it is required to consume the future economic benefits or service potential embodied in the contributed asset in the delivery of particular goods or services to third parties or else to return economic benefits or service potential to the donor. Accordingly, when the recipient entity initially recognises an asset that is subject to a condition, the recipient entity also recognises a liability.

G9. As an administrative convenience, an asset may be effectively returned by reducing the amount of other assets due to be contributed for other purposes. For example, a future contribution might be reduced by the amount of cash or the value of non-monetary assets that would otherwise be returned to the donor. This does not change the underlying substance of the contribution: that gaining control of the asset also gives rise to a liability.

G10. The liability is subsequently decreased and income recognised in accordance with paragraph 9, when the recipient entity performs the action that is required by the condition. Some agreements provide for a return of a proportionate amount of the contributed asset, or its equivalent amount, if the recipient entity partially performs the required action. In these cases, the recipient entity decreases the liability and recognises income as the action is performed, or decreases the liability and decreases the amount of an asset if there is a return of resources to the donor because of non-performance or partial performance.

G11. When the recipient entity does not fulfil a performance obligation required by the contribution the donor may have the option of seeking a penalty against the recipient entity by taking the matter to a court or other tribunal or through an administrative process, such as an appeal to a government minister or other authority. This may result in the recognition of an additional present obligation of the recipient entity to pay a fine.

G12. In some cases, an asset may be contributed subject to it being returned to the donor if a specified future event does not occur but does not entail a performance obligation as described in paragraph G7. This may occur when, for example, the Australian government provides funds to a state government entity subject to the recipient entity raising a matching contribution, or provides funds to a state government entity subject to local area public hospital services being provided free of charge to specific groups of citizens. In these cases, a return obligation does not arise until it is expected that the specified future event will not occur. However, these amounts are in the nature of a prepayment. Such amounts are in the nature of a reciprocal transaction, and would be treated consistently with the treatment of prepayments in accordance with AASB 118.

Contributions without conditions (other than involuntary transfers)

G13. When an entity has a right to receive or receives contributions that have no conditions, the contributions themselves do not give rise to a liability. This is because there is no obligation on the recipient entity to return an asset to the donor and therefore an outflow of future economic benefits is avoidable. Accordingly, the entire amount of the contribution is recognised as income in accordance with paragraph 9 at the time the right to receive the contribution becomes enforceable, regardless of whether the contribution relates to a single year or multiple years.

G14. When the recipient entity does not fulfil a performance obligation associated with the contribution, the donor may have the option of seeking a penalty against the recipient entity by taking the matter to a court or other tribunal or through an administrative process, such as an appeal to a government minister or other authority. This may result in the recognition of a present obligation to pay a fine, however this is a subsequent event, not one that occurs at the time of recognising the contribution received or receivable as an asset.

Involuntary transfers

G15. Involuntary transfers may include items such as taxes, rates or fines. These types of transfers do not arise from the in substance rendering of services because the transfers are imposed through an entity's power to obtain public funds. An entity is not obliged to provide commensurate benefits to the transferor in the form of goods and services provided in return for the transfer imposed. In some circumstances, the public goods and services received by a transferor from the entity may be approximately equal in value to the transfer made or to be made, but this would be coincidental.

G16. The entity analyses the taxation law to determine the taxable event for the various taxes levied. Unless otherwise specified in laws or regulations, it is likely that the taxable event for:

(a) income tax is the earning of assessable income during the taxation period by the taxpayer;

(b) goods and services tax is the purchase or sale of taxable goods and services during the taxation period;

(c) customs duty is the movement of dutiable goods or services across the customs boundary; and

(d) land tax and rates is the passing of the date on which the land tax and rates are levied.

G17. Amounts received in advance of the taxable event are treated consistently with AASB 118. The prepayment reflects an obligation for the recipient entity to reduce the prepayment by future tax obligations incurred by the transferor or refund the excess amount. When the taxable event occurs, the contribution is within the scope of AASB 1004 that requires income to be recognised in accordance with paragraph 9.

G18. Rates are imposed upon an entity (including an individual) by a local government through the local government's power to obtain public funds. Rates are recognised as an asset (cash or rates receivable) when control over the asset arising from rates is obtained. This is at the commencement of the rating period. The asset recognised at the commencement of the rating period gives rise to the recognition of income at that time in accordance with paragraph 9.

G19. Fines are a sacrifice of economic benefits or service potential by a person or other entity for breaching the requirements of laws or regulations, as determined by a court or other law enforcement body. The entity (including an individual) subject to the fine will normally have the choice of paying the fine or going to court to defend the matter. Fines normally require an entity to transfer a fixed amount of cash to the government and do not impose on the government any obligations that would be recognised as a liability. Accordingly, fines are recognised as income in accordance with paragraph 9 when control over the asset is obtained. Control usually arises when fines are levied.