

15 August 2015

EXT2015/63

Ms Kris Peach
Chair
Australian Accounting Standards Board
PO Box 204
COLLINS STREET VIC 8007

By: Submit comments to AASB

Dear Ms Peach

AASB EXPOSURE DRAFT ED 260 APRIL 2015 – INCOME OF NOT-FOR-PROFIT ENTITIES

The Australian Charities and Not-for-profits Commission (the ACNC) would like to thank you for the opportunity to comment on Exposure Draft 260 *Income of Not-for-Profit Entities* (ED 260).

The ACNC is a specialist regulator for charities with a focus on the following key statutory objectives for the Australian not-for-profit sector, as outlined in Part 1-2 of the *Australian Charities and Not-for-Profits Commission Act 2012* (the ACNC Act 2012), to:

- maintain, protect and enhance public trust and confidence in the sector; and
- support and sustain a robust, vibrant, independent and innovative sector; and
- promote the reduction of unnecessary regulatory obligations on the sector.

The ACNC generally supports the proposals in ED 260 given it is an improvement on the current standard, AASB 1004 *Contributions*. The current standard is open to wide interpretation and in our experience is not being applied consistently. However, the ACNC has two key concerns with the proposals, as follows:

- The application date proposed of 1 January 2017 does not provide sufficient time to educate the not-for-profit sector, and the ACNC recommend at least a one year deferral. This would align the application date to that being proposed in ED 263 in respect of AASB 15 *Revenue from Contracts with Customers*.
- The proposed replacement to AASB 1004 uses the term 'income' rather than the term 'revenue'. The ACNC notes that many Commonwealth and State/Territory regulatory agencies use 'revenue' thresholds (determined in accordance with Australian Accounting Standards) to determine reporting obligations. Therefore the ACNC recommends the AASB in the final standard make a clear distinction of what would normally be considered 'revenue' versus 'other income'.





The attached Appendix provides the ACNC's detailed responses to the Specific Matters for Comment as set out in ED 260. Please note that these responses focus on the perspective of private not-for-profit entities and we have not considered the components or examples in ED 260 that relate to public not-for-profit entities (ie government entities).

Please do not hesitate to contact Kerry Hicks, at kerry.hicks@acnc.gov.au should you have any queries in relation to the above.

Yours sincerely

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Appendix – Response to Specific Matters for Comment – ED 260

1. *In relation to the AASB's proposal to replace the reciprocal / non-reciprocal transfer distinction in AASB 1004 with income recognition requirements based on whether a not-for-profit entity needs to satisfy a performance obligation:*
 - (a) *do you agree that this proposal would provide a faithful depiction of a not-for-profit entity's financial performance?*
 - (b) *if not, what alternative approach to income recognition would you recommend for not-for-profit entities? Please provide your reasons.*

While we continue to follow a sector-neutral approach to accounting standards, the ACNC considers that the performance obligation approach that is currently required for the for-profit sector from 1 January 2017, can be made to work for the not-for-profit (NFP) sector. We recognise that under one conceptual framework, with consistent definitions of assets and liabilities any other approach would not be supportive of this framework. Therefore we agree with this approach.

However, the ACNC continues to receive comments from registered charities and their advisors regarding the appropriateness of the sector-neutral approach to accounting standard setting. The ACNC believes that this issue requires further consideration in light of other jurisdictions that have developed separate frameworks and standards specifically for the NFP sector (most recently the developments in New Zealand).

2. *In relation to the AASB's proposal that, to qualify as a performance obligation, a not-for-profit entity's promise to transfer a good or service to a counterparty in a contract must be 'sufficiently specific' to be able to determine when the obligation is satisfied (see paragraph IG13 of Part A):*
 - (a) *do you agree with this proposal?*
 - (b) *if not, what factors or criteria should apply to determine whether a not-for-entity has a performance obligation? Please provide your reasons.*

The ACNC is not convinced of the 'sufficiently specific' criteria in order to determine when the obligation is satisfied. Service contracts vary between different governments and between departments/agencies. This may result in the same service agreement entered into but accounted for differently as a result of a 'specificity' that was not explicit in one funding agreement versus another.

The ACNC understands that many areas of the NFP sector indicate that the 'matching concept' is more appropriate for them. The ACNC does not believe this concept is supported by the current conceptual framework in existence.

However, the ACNC considers that in order to enable the proposed performance obligation approach to work for the sector it will be imperative for the AASB and the sector to ensure grant funding bodies are aware of the changed requirements. Grant funding bodies and government agencies/departments will need sufficient time to build appropriate performance obligations into their funding agreements. Therefore the ACNC considers the AASB should take a proactive approach with



government (Commonwealth as well as State/Territory governments) to explain the changes and the implications for funding agreements. Further, the ACNC considers the application date of the standard should be delayed by at least one year to enable the government departments/agencies sufficient time to consider the impact on funding agreements, and for further education to occur throughout the broader sector on the changes.

The ACNC may be able to facilitate the AASB making the appropriate connections with the relevant government departments/agencies.

3. *Do you agree with the proposal in paragraphs IG19-IG30 of Part A that a not-for-profit entity would recognise a donation component in a contract with a customer as immediate income only if:*
- (a) a qualitative assessment of available evidence indicates that the customer intended to make a donation to the not-for-profit entity; and*
 - (b) the donation component is separately identifiable from the goods or services promised in the contract? (See also paragraphs BC36-BC49 of the Basis for Conclusions.)*

If not, under what circumstances should a not-for-profit entity identify and account separately for a donation that is provided as part of a contract with a customer?

The ACNC does not support the proposed approach to recognising donation components. The ACNC believes a 'customer intention' test is unworkable for the sector due to practicalities of this assessment for many charities. We recommend that refundability should be the key criteria in determining donation components as it is a simpler test to apply. For example, if the goods or services contract was cancelled and the perceived donation component was refundable, then this component would not be accounted for separately and instead included in the transaction price.

However, the ACNC also recognises that if a customer/client of a charity receives a tax receipt for a donation then this would be non-refundable and should be accounted for as a donation upon receipt.

4. *In relation to the AASB's proposals to:*
- (a) permit any not-for-profit entity to recognise volunteer services as income if the fair value of those services can be measured reliably; and*
 - (b) carry forward the requirement in paragraph 44 of AASB 1004 that particular public sector entities must recognise volunteer services if those services would also have been purchased if they had not been donated,*

the AASB seeks views on:

- (a) whether the requirements (if any) for the recognition of volunteer services should be the same for all not-for-profit entities, regardless of whether they operate in the public or private sector; and*



(b) if your answer to (a) is 'yes', whether the recognition of volunteer services should be:

(i) optional, provided that the fair value of those services can be measured reliably; or

(ii) required if those services would also have been purchased if they had not been donated.

(See also paragraphs BC59-BC63 of the Basis for Conclusions.)

The ACNC agrees with the discussion at the AASB Roundtable held in Melbourne in June 2015 that the recognition of volunteer services should be a specific project of the AASB and not addressed in these current proposed changes. Therefore, the ACNC support the existing treatment of accounting for volunteer services to be carried forward from the current AASB 1004. Whilst optionality is not useful in promoting consistent accounting application, the ACNC do not expect this proposal will change current practice.

In relation to a future project, it should be noted that the ACNC is not supportive of differing recognition criteria for volunteering services between the government and non-government sectors. The ACNC consider the test for recognition should be criteria based and not simply based on whether the services would also have been purchased if they had not been donated. The ACNC believe the AASB project should establish common practices in international jurisdictions, to assist in determining a future direction for Australia. The ACNC do not believe that any future proposal should be optional, at least for entities that prepare general purpose financial reports, as the ACNC consider it is important for an entity to recognise the resources it uses in providing services.

5. *Do you agree with the proposal in paragraph 38 of [draft] AASB 10XX that, when inventories are donated to a not-for-profit entity other than as part of a contract with a customer, assessments of whether the donations are material should be made on an individual transaction basis without reassessment at a portfolio or other aggregate level? (See also paragraphs BC50-BC51 of the Basis for Conclusions.)*

The ACNC agrees with the proposal, since anything more is likely to have a significant cost burden to NFPs.

6. *Australian Accounting Standards applicable to for-profit entities do not include a definition of 'contributions by owners'. Further, concerns have been expressed by some that the definition of 'contributions by owners' in AASB 1004 is too narrow. Do you consider that a definition of 'contributions by owners' is still necessary, or appropriate, in Australian Accounting Standards? If so, would you prefer using:*
(a) the definition of 'contributions by owners' presently in AASB 1004; or
(b) the definition of 'ownership contributions' in the Public Sector Conceptual Framework issued by the International Public Sector Accounting Standards Board (IPSASB)? (See also paragraphs BC84-BC91 of the Basis for Conclusions.)



No specific comments are made by the ACNC in this regard.

7. *The AASB also seeks views on the following issues related to contributions by owners:*
- (a) whether, in view of concerns expressed by some that using AASB 1004's definition of 'contributions by owners' in AASB Interpretation 1038 Contributions by Owners Made to Wholly-Owned Public Sector Entities (which includes for-profit public sector entities in its scope) might prevent a for-profit entity in the public sector from making an unreserved statement of compliance with IFRSs, AASB Interpretation 1038 should be:*
 - (i) withdrawn;*
 - (ii) retained but with narrower application [that is, limited to not-for-profit entities in the public sector, and possibly also confined to identifying which not-for-profit public sector entities should account for transfers between them when they are controlled by the same parent (government)]; or*
 - (iii) retained without amendment? (See also paragraphs BC84-BC94 of the Basis for Conclusions.)*
 - (b) whether requirements for restructures of administrative arrangements (presently set out as paragraphs 54-59 of AASB 1004) should still be included in Australian Accounting Standards (see also paragraph BC90(b) of the Basis for Conclusions);*
 - (c) whether requirements for distributions to owners (presently set out as paragraphs 49 and 53 of AASB 1004) should still be included in Australian Accounting Standards (see also paragraphs BC94-BC96 of the Basis for Conclusions);*
 - (d) whether requirements for liabilities of government departments assumed by other entities (presently set out as paragraphs 39-43 of AASB 1004) should still be included in Australian Accounting Standards (see also paragraphs BC97-BC98 of the Basis for Conclusions); and*
 - (e) the practical implications if the definition of 'contributions by owners' and AASB Interpretation 1038 were to be withdrawn?*

No specific comments are made by the ACNC in this regard.

8. *In relation to disclosure requirements regarding compliance by government departments with appropriations, do you agree with:*
- (a) omitting the requirement in paragraph 64(e) of AASB 1004 to disclose the nature and probable financial effect of any non-compliance by the government department with externally-imposed requirements for the period, other than any non-compliance reflected in material variances between amounts appropriated and amounts expended? (See paragraphs BC99-BC103 of the Basis for Conclusions.)*
 - (b) extending the scope of the retained disclosure requirements for government departments (ie those regarding any non-compliance reflected in material variances between amounts appropriated and amounts expended) to also apply to any other public sector entities that obtain part or all of their spending authority*



from parliamentary appropriations? (See also paragraphs BC99-BC103 of the Basis for Conclusions.)

No specific comments are made by the ACNC in this regard.

9. *Do you agree with the proposed transitional provisions in Appendix C of [draft] AASB 10XX? In particular:*
- (a) do you agree with the transitional provisions for non-financial assets and finance lease assets and liabilities, the cost of which was not measured at fair value on initial recognition; and*
 - (b) do any other issues warrant additional transitional provisions and, if so, which transitional provisions do you suggest? (See also paragraphs BC104-BC109 of the Basis for Conclusions.)*

Retrospective adjustments are unlikely to be possible in respect of non-financial assets and/or finance lease assets and liabilities that were acquired in previous years. This is due to the fact that some leases, and indeed some assets may have been initially entered into or acquired many years ago, and records may be unable to be located (although we note that NFPs that are registered charities must keep records for 7 years after the transactions are complete, in order to comply with Part 3-2 of the ACNC Act 2012). NFPs often have volunteer boards which regularly change, therefore there is unlikely to be much historical knowledge in those currently identified as responsible persons.

The ACNC recommends that a transitional option is included to enable fair values of those non-financial assets and/or finance lease assets and liabilities to be established at the initial application date, treated as a cost measure and accounted for directly in equity (or a financial liability if relevant).

Even this measure could have substantial cost implications for NFPs, therefore the ACNC suggests the guidance be made clear that a director valuation is acceptable, with clear supporting guidance included on the minimum requirements for a directors' valuation and evidence required to support such valuation. The ACNC requests that an example of applying this transitional provision, based on a directors' valuation, is included in the guidance.

10. *Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:*
- (a) not-for-profit entities; and*
 - (b) public sector entities, including GAAP/GFS implications (discussed above).*

The proposed replacement to AASB 1004 uses the term 'income' rather than the term 'revenue'. The ACNC recognises that 'revenue' is a component of 'income'. The ACNC considers that the majority of areas the proposed standard deals with, such as grants and donations, are considered 'revenue' under the current standards.



The ACNC does not believe it is the intention of the AASB to reduce 'revenue' and thereby impact on the regulatory reporting obligations of many entities that currently are determined using 'revenue' thresholds. The ACNC notes that reporting obligations based on revenue thresholds in the NFP sector exist for charities under the ACNC Act 2012 (this is specifically defined with reference to accounting standards in section 205-25), other limited by guarantee companies under the *Corporations Law 2001* and many associations under the relevant State/Territories association acts.

Therefore The ACNC recommends the AASB in the final standard make a clear distinction of what would normally be considered 'revenue' versus 'other income'.

No comments are made in relation to GFS harmonisation issues.

11. Whether, overall, the proposals would result in financial statements that would be useful to users.

The ACNC would find the proposed requirements useful in that they would enable more consistent and comparable comparisons to be made of entities operating in the charities sector. The ACNC is also conscious of the need to balance reporting obligations with red-tape reduction. Therefore, in this response the ACNC has proposed some short-cut more practical approaches in the areas of donations, and transitional provisions that may assist in maintaining this balance.

12. Whether the proposals are in the best interests of the Australian economy.

No specific comments are made by the ACNC in this regard.

13. Unless already provided in response to specific matters for comment 1 – 9 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

No specific comments are made by the ACNC in this regard.