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13 August 2015

Ms Kris Peach
Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West
VICTORIA 8007

By email: standard@aasb.gov.au

Dear Ms Peach,

Submission on Exposure Draft ED 260 *Income of Not-for-Profit Entities*

The Association of Independent Schools NSW welcomes the opportunity to provide the Australian Accounting Standards Board with our comments on Exposure Draft (ED) 260 *Income of Not-for-Profit Entities*.

The Association of Independent Schools NSW (AIS) is the peak body for independent schools in NSW. AIS represents over 480 independent schools who together enrol more than 180,000 students. A key function of the AIS is to administer capital grant funding programs on behalf of the State and Commonwealth Governments. Prior to allocation of government grants to facilitate capital works projects, a thorough financial assessment must be carried out on an average 60-70 schools to determine financial need. This process which has been undertaken by this organisation for over 20 years, gives us some insight into the impact of the current accounting treatment for conditional grants and the effects on the reported financial results of recipient schools.

The AIS has no comments on the specific questions contained in the ED. We do, however, wish to express our views on the proposed treatment of capital grants.

Proposed treatment of capital grants

ED 260 proposes that AASB 15 *Revenue from Contracts with Customers* would apply to contracts with customers representing enforceable agreements that contain sufficiently specific performance obligations. Where an entity entered into an agreement with governments to receive a capital grant for the acquisition or construction of property, plant and equipment, and that agreement satisfied the contract criteria in AASB 15, then revenue would be recognised as the entity satisfied those performance obligations. That is, revenue would be recognised at the time the entity acquired or constructed the asset.

Similarly, if a grant was within the scope of [draft] AASB 10XX, income would be recognised at the time the entity acquired or constructed the asset. We note that most specific purpose capital grants from government contain refund obligations if the purpose of the grant is not met.

In both cases, income would be recognised when the entity had satisfied the terms of the grant.

Our major concern with AASB 1004 *Contributions* is related to distortions created in a school's financial performance caused by differences between the timing of the recognition of the capital grants and the recognition of subsequent expenses in the school's income statement. Depending on the timing of receipt of grant funds, an entity may report substantial income (and net profit) in one financial year and substantial depreciation and amortisation expenses in following financial years. We are concerned that this misalignment between the recognition of income and the associated expenses to which it relates does not faithfully depict, and potentially misrepresents, a school's financial performance.

In our opinion, this distortion of the reported financial performance of the entity receiving the capital grants has not been resolved by the proposals in ED 260.

In the above scenario, the proposals in ED 260 would result in income being recognised in relation to the capital grant once the asset has been acquired or constructed. However, the entity would still subsequently recognise annual depreciation over the remaining useful life of the constructed asset. Indeed, the grant funding agreement accompanying the grant stipulates that the constructed educational facility must continue to be used by the school for a minimum period of time, the duration of which is dependent upon the grant amount.

To overcome this distortion in the reported financial performance of the entity receiving capital grants, we believe that not-for-profit entities should have an accounting policy choice to recognise capital grants received from governments in the same manner as described in paragraphs 17 and 26 of AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*.

That is, a not-for-profit entity should be permitted an accounting policy choice (consistent with for-profit recipients of government grants) to recognise the capital grant as deferred income and subsequently recognise income in profit or loss on a systematic basis over the useful life of the asset. This would result in grant income being recognised over the periods and in the proportions in which depreciation expense on those assets is recognised. Thus, readers of those financial statements would not be confused by erratic changes in income and profitability.

Should you wish to discuss the contents of our submission, please contact me at dbuley@aisnsw.edu.au or phone (02) 9299 2845.

Sincerely

David Buley
Chief Financial Officer