

The Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West
Victoria 8007

Email: standard@asb.gov.au

Dear Ms Peach

ED 260 Income of Not-for-Profit 260

Our comments and recommendations regarding ED 260 are provided in this submission. Responses to specific questions as requested by the AASB are provided in the attachment on pages 3-7.

Saward Dawson operates in Melbourne, Australia. Our clients come from a range of industries and comprise a significant number of private sector not-for-profit entities. We are focused on enhancing the relevance, reliability and usefulness of financial reporting for users.

In summary we hold the following views in relation to the attachment:

1. We are supportive of the proposals in relation to the recognition of revenue from customer contracts on the basis of performance obligations criteria and the recognition of voluntary transfers on the basis of obtaining control of the asset.
2. We have concerns in relation to the proposals to allow the recognition of volunteer services at fair value and the example provided. We believe that insufficient guidance exists on determining fair value of such services and the proposals within ED 260 are likely to result in the recording of such services based on simplistic and highly subjective fair value estimates which will reduce the relevance, reliability and comparability of financial reports.
3. We believe that the early adoption of the new standard will be highly attractive to some not-for-profit entities and accordingly the initial application of AASB15 is likely to occur more widely and in earlier reporting periods within the not-for-profit sector than the for-profit sector.

Given the comparatively lower level of financial reporting expertise and resources within the sector, we believe the AASB should implement a broad education process in conjunction with relevant regulators and the accounting professional bodies in order to assist the sector in adopting AASB 15 and the new income of not-for-profit entities standard.

4. We acknowledge the usefulness of the examples contained within ED260 but would emphasise the importance of making sure the terminology does not lead to misinterpretation.

Please do not hesitate to contact us should you wish to discuss further any matters arising from this submission.

Yours Sincerely

A handwritten signature in blue ink, appearing to read "Peter Shields".

P Shields

Partner

A handwritten signature in blue ink, appearing to read "Jeffrey Tulk".

J Tulk

Senior Manager - Technical

Specific Matters for Comment

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.

We broadly agree with approach proposed within ED260.

We agree that certain transfers (usually in the nature of a government or private sector 'grant') for clearly articulated and agreed purposes should be deferred until the requirements of the transfer is met. We consider that the performance obligation criteria is an appropriate method for determining the deferral of income.

We believe that where a transfer (in the nature of a donation) does not clearly articulate the purpose and that is typically for the general operations or the broad objectives of the entity, such transfers should be recognised as income on receipt under the proposed control model.

We do not believe that a deferral of income that does not contain a sufficiently specific performance obligation would be a faithful representation of financial performance.

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-profit entity has a performance obligation? Please provide your reasons.

We agree that determining if a contract is 'sufficiently specific' will require judgement. For example where an entity undertakes a narrow range of activities the performance obligation may be in part implied.

In determining whether a contract is sufficiently specific, in addition to the criteria included within ED260 we believe that the entity having the internal systems to record transactions in order to determine if the performance condition has been satisfied and the transferor having access to the necessary information to determine if the condition has been satisfied may assist in applying judgement in this area.

We do not believe that a clear refund clause or power to demand a refund should be an absolute determining factor. We believe that a contract that contains a sufficiently specific promise would provide rights to the transferor to seek refund, demand performance or another form of compensation. Accordingly we consider that although enforceability is a criteria for determining if a liability exists, judgement may need to be applied in determining if an enforcement condition exists.

- 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?

We agree that the criteria specified above provides a pragmatic method for an entity to determine if the donation component should be separated from the goods or services promised in the contract.

- 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.)

Although ED260 paragraph BC64 states that the "AASB does not plan a fundamental review of the recognition requirements of volunteer services presently contained in AASB 1004", we believe the proposals contained in ED260 and Example 16 will represent a fundamental alteration to current practice within private sector NFPs.

Our experience is that very few private sector NFP's have recorded volunteer services as income on the basis that AASB 1004 contributions paragraph 13 and disclosure requirements in paragraph 18 refer only to the contributions of 'assets' and although 'services' is contained within the definition of a non-reciprocal transfer, it has been broadly considered that items such as volunteer services could not be reliably measured.

We believe that the inclusion of a single simplistic example will be utilised as a method for certain NFPs to adopt a policy of recognising services based on a highly subjective measure of fair value.

We note that the proposal currently provides no guidance or references to the principals contained in AASB 13 framework for measuring fair value. In particular no guidance is provided on how to determine what the 'principle market' and 'most advantageous market' are for typical volunteer services.

In this regard we consider that Example 16 fails to explain the AASB's view on if and when the volunteer labour market of free services would represent an orderly transaction between market participants and accordingly result in the fair value of volunteer services being nil. We believe the proposed standard must provide detailed guidance on determining fair value.

We note that the Australian Bureau of Statistics stated that “the value of the work contributed by volunteers to non-profit institutions in 2006-07 was estimated to be \$14.6 billion.” Given the quantum of volunteer services and the inherent issues in determining fair value we strongly believe that additional research, consideration of the international approach, regulator input and sector education and consultation should occur prior to allowing what would amount to a fundamental change in not-for-profit reporting.

Accordingly, at this time we believe the option to record income from such services should be limited to the current scope of AASB 1004 for the public sector and that any application by private sector NFP’s be limited to the option to only record volunteer services that can be reliably measured and only if those services would have been purchased if they had not been donated.

In addition examples in relation to typical services likely to be recorded under this option should be included within the illustrative examples provided by the AASB and that such examples include instances where a reliable measure criteria is and is not able to be met, the basis for making the determinations and the method of determining a reliable fair value measurement with reference to AASB 13.

We do however believe that private sector NFP’s should be encouraged to disclose the nature and amount (hours) of volunteer services received.

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.)*

We agree that materiality should be made on a transaction level and that reassessment at a portfolio level should not be required.

However we believe that where inventories exist at balance date that would likely be material on a portfolio level, a disclosure requirement that enables a user to understand the nature and estimated amount of such inventories should be required.

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.)

We believe that practical guidance on circumstances where contributions should be recorded directly in equity versus those that should be reflected within the profit and loss would be of benefit to the sector. Typically issues arise in this area as many private sector not for profits do not have ‘owners’ in the traditional sense. In particular clarification in relation to contributions form:

- (i) Entities that are a parent or subsidiary based on the principles of control under AASB 10 even though no equity ownership exists; and
- (ii) Contributions from entities with similar purposes where assets are transferred on wind-up of one entity or on ‘merger’ of the entities.

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 comment.

- 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 comment.

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.)*

We agree that the application of the [draft] AASB 10XX should be applied on a retrospective basis. However where long term assets are held and the determination of fair value at the date of acquisition is not reasonably able to be determined, an option to apply fair value at the beginning of the earliest comparative period should be available.

General matters for comment

The AASB would also particularly value comments on the following:

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).*

Reporting thresholds for charities, companies limited by guarantee and a number of States' incorporated associations reporting and audit requirements are based on revenue thresholds. Accordingly we are concerned that recording of fair value of volunteers services may result in a change in reporting and assurance requirements based on an optional accounting policy choice.

We recommend the AASB discuss these implications with relevant regulators to ensure the application of the thresholds is clearly articulated to the sector as soon as possible after the release of the standard as we believe many entities will seek to early adopt the new proposals.

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

We believe the proposals in relation to income recognition based on a performance obligations will result in a more understandable income statement which currently tend to be volatile based on timing of receipts.

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

We support revisions that improve the relevance, reliability and user understanding of financial reports. In this regard we refer to our comments for items 2 and 4.

As a significant portion of private sector not-for-profit are subject to audit. We have concerns over the ability to substantiate the recording of volunteer services from an audit perspective. It is likely that entities recording volunteer services will be subject to increased assurance costs and potentially audit qualification in relation to these items.