



10 March 2022

Dr Keith Kendall
Chair
Australian Accounting Standards Board
PO Box 204
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AUSTRALIA

Dear Dr Kendall

Exposure Draft 318 Illustrative Examples for Income of Not-for-Profit Entities and Right-of-Use Assets arising under Concessionary Leases

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to contribute to the limited scope amendments to the implementation examples in AASB 15 *Revenue from Contracts with Customers* and AASB 1058 *Income of Not-for-Profit Entities*. Please find attached the ACAG response to the AASB Exposure Draft 318 *Illustrative Examples for Income of Not-for-Profit Entities and Right-of-Use Assets arising under Concessionary Leases* (ED 318).

ACAG supports clarifying the proposed illustrative examples in AASB 15 and AASB 1058 as we have concerns with the existing examples. ACAG believes that the proposed Example 3A.1 requires additional explanations to support the AASB's rationale for arriving at its conclusions, particularly in relation to the significance of the scholarships being paid at the direction of the alumnus (as opposed to the university having the discretion to determine the scholarships paid). ACAG does not believe Example 3A.1 is common in the public sector and may only be useful in limited circumstances when the recipient does not control the spending of the funds.

The views expressed in this submission represent those of all Australian members of ACAG.

The opportunity to comment is appreciated and I trust you will find the attached comments useful.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Margaret Crawford', written in a cursive style.

Margaret Crawford

Chair
ACAG Financial Reporting and Accounting Committee

QUESTIONS FOR RESPONDENTS

AASB Specific Matters for Comment

Proposed amendments to AASB 15 and AASB 1058 (all not-for-profit entities)

1. Do you agree that the proposed amendments to the AASB 15 and AASB 1058 illustrative examples provide appropriate illustration of the application of the recognition and measurement requirements of the Standards? If not, please explain why.

Illustrative Examples – AASB 15 – Upfront Fees

ACAG agrees that, as the upfront fee is not associated with an activity that relates to a separate performance obligation, the upfront fee is treated as an advance payment for the performance obligation(s) to be satisfied in the future, and therefore recognised as those goods or services are provided.

ACAG suggests that the accounting treatment be reworded to better explain why the fee is treated as an advance payment for future services. That is, because the upfront fee does not relate to a separate performance obligation, the fee is included in the consideration for the performance obligation(s) in the agreement (to provide future services), and therefore treated as an advance payment for those future services. We suggest updating the last paragraph with the following wording:

The organisation concludes that the non-refundable upfront fee does not relate to an activity that represents a separate performance obligation (see paragraph 25). Therefore, the fee is included in the consideration for the performance obligation(s) in the agreement (to provide future services). The effect is that the upfront fee is treated as an advance payment for future services and is recognised as revenue as the future services are provided over the two-year contract period (see paragraphs 30 and B49).

ACAG also suggests that the AASB include in AASB 15 *Revenue from Contracts with Customers* the AASB staff [FAQ](#) example 11 “How does an NFP school account for non-refundable upfront fees charged to place prospective students on a waiting list?”. This example is helpful as it explains the treatment of upfront fees when there is no obligation to provide future services. Alternatively, the AASB should consider developing an alternative contrasting example which can be used by a broader group.

Illustrative Examples – AASB 1058 – Endowment and scholarships

ACAG understands that the intention of AASB 1058 *Income of Not-for-Profit Entities* Example 3 is to demonstrate the interaction of AASB 1058 with AASB 9 *Financial Instruments* and other standards. ACAG agrees with the proposal to amend illustrative Example 3 as the current Example 3A is unclear as to why a financial liability should be recognised. In relation to the proposed changes, ACAG believes that Example 3A.1 requires additional explanations to support the AASB’s rationale for arriving at its conclusions. In doing this, ACAG believes that other examples should be re-visited to ensure that it is clear what facts and circumstances exist which result in differing outcomes.

ACAG’s concerns include:

- Concerns with proposed Example 3A.1 – Definition of a financial instrument
- Proposed Example 3A.1 – Rationale to support conclusions
- Proposed Example 3A.1 – Income from endowment funds
- Concerns with existing Examples 3B and 3C
- Review of existing examples.



Concerns with proposed Example 3A.1 - Definition of a financial instrument

ACAG's comments in this section analyse whether the definition of a financial instrument is met if the university has the discretion to determine the beneficiaries of the cash scholarships.

AASB 9 applies to all financial instruments, except those that are specifically excluded under paragraph 2.1. Under AASB 9 Appendix A, and AASB 132 *Financial Instruments: Presentation* paragraph 11, a "financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity."

ACAG does not believe that on receipt of the endowment funds there is a financial liability, or a contractual obligation to pay cash. Before there is an obligation to pay cash, a suitable student recipient needs to be selected. It is only after the suitable student is selected, and agrees to any scholarship terms, that there is an obligation to pay cash to the student. In practice, such payments are often conditional, as there are conditions associated with receiving a scholarship, such as good behaviour, and achieving suitable grades.

ACAG does not believe that on receipt of the endowment funds any entity has a contractual right to receive cash from the university. A student will have a right to receive cash when they are selected as a suitable recipient by the university.

Consequently, on receipt of the endowment funds, neither the definition of a financial liability of the university, or a financial asset of another entity to receive cash from the university is met. Therefore, the definition of a financial instrument is not met.

ACAG also believes that if such arrangements were accounted for as a financial liability, the outcome would not faithfully represent the activities of the funding recipient, which are to receive funding and use it to give out cash grants or spend on specified projects/eligible expenditure.

Justification given for financial liability view

ACAG understands that there is support from other stakeholders for treating the receipt of the endowment as a financial liability, on the basis of the future obligation to pay cash to successful students. We understand that support for this view is derived from the IFRS Interpretation Committee agenda decision [Classification of liability for a prepaid card in the issuer's financial statements](#) (IAS 32) (March 2016) based on a reference in the associated IFRIC [staff paper](#) that makes the following statement (paragraph 30(c)):

- (c) to meet the definition of a financial instrument, IAS 32 does not require the issuer of a financial liability to identify the specific counterparty that has a financial asset at the time that its obligation arises, nor does it require a counterparty to have recognised a corresponding financial asset. For reference, paragraph AG8 of IAS 32 notes that a contingent right and obligation meet the definition of a financial asset or financial liability, even though such assets and liabilities are not always recognised in the financial statements.

However, that statement needs to be read in the context of the preceding paragraph (paragraph 30(b)):

- (b) if an entity has a contractual obligation to pay cash, this necessarily means that another party must have a contractual right to receive that cash. Both the cardholder and the merchant(s) have contractual rights as follows:
 - (a) the cardholder has the contractual right to direct the issuer to pay cash to the merchant(s) as payment for goods or services; and
 - (b) the merchant(s) has a right to receive cash from the issuer after providing goods or services to the cardholder.



Given that a financial instrument is required to be a contract, then the identification of those entities that have a right to receive cash should be clear.

ACAG also notes the following guidance in AASB 15 as to why a contract asset (that would often represent a right to cash in the future) is not a financial asset:

- 107 If an entity performs by transferring goods or services to a customer before the customer pays consideration or before payment is due, the entity shall present the contract as a contract asset, excluding any amounts presented as a receivable. A contract asset is an entity's right to consideration in exchange for goods or services that the entity has transferred to a customer. ...
- 108 A receivable is an entity's right to consideration that is unconditional. A right to consideration is unconditional if only the passage of time is required before payment of that consideration is due. For example, an entity would recognise a receivable if it has a present right to payment even though that amount may be subject to refund in the future. An entity shall account for a receivable in accordance with AASB 9.

Applying the AASB 15 guidance to the scholarship example, on receipt of the endowment no student or other party has an unconditional right to cash (as a suitable student has not been selected and the scholarship has not been awarded). Also, at the same time, the university does not have an unconditional obligation to pay cash for similar reasons. Therefore, the definition of financial instrument is not met at that time.

Proposed Example 3A.1 – Rationale to support conclusions

ACAG believes that the proposed Example 3A.1 requires additional explanations to support the AASB's rationale for arriving at its conclusions. The proposed changes include references to the payment of cash scholarships by the university being at the direction of the alumnus. This raises the issue of whether the university is acting as principal or agent. ED 318 does not appear to identify or discuss this issue.

Example 3A.1 states that the "endowment gives rise to a financial instrument and, specifically, a financial liability". However, the updated example does not refer to the specific facts and circumstances within the example that results in the AASB's conclusion that a financial liability should be recognised. While ACAG agrees that in the circumstances of the university being an agent that a liability exists, ACAG questions whether there would be a financial instrument, as there does not appear to be another party holding a financial asset (right to receive cash or another financial asset).

Example 3A.1 does not explain the significance of the scholarships being paid at the direction of the alumnus (as opposed to the university having the discretion to determine the scholarships paid) to the conclusion and whether these would vary if the payments were made at the discretion of the university. For example, if the university received an endowment that it was required to direct towards certain scholarships, but the university had the right to determine and approve the scholarship recipients would this have changed the AASB's conclusion regarding recognition of a financial liability?

As stated in the 'Concerns with proposed example 3A.1 - Definition of a financial instrument' above, ACAG does not believe that on receipt of the endowment funds there is a financial liability, or a contractual obligation to pay cash when the university has the right to determine and approve the scholarship recipients. Before there is an obligation to pay cash, a suitable student recipient needs to be selected. It is only after the suitable student is selected, and agrees to any scholarship terms, that there is an obligation to pay cash to the student. In addition, when the university selects the scholarship recipients and awards scholarships, some offices are of the view that recognition in the income statement of the revenue or income from the endowment and the expense for granting the scholarships would more faithfully represent the activities of the university.



ACAG recommends amending the proposed Example 3A.2, to include the alternate scenario where the university has the discretion to determine the scholarship payments. The proposed Example 3A.2 that focuses on the endowment being received for the furtherance of the university's objectives serves no purpose because it is already clear in the Standards (and other illustrative examples) that an endowment provided for such broad purposes would be recognised as income on receipt.

ACAG believes that the AASB should include the applicable journal entries for the recognition of the funds received, and for the disbursement of funds for both examples.

While the public sector receives endowments and grants, ACAG does not believe it is common for a grantor to retain the right to control the spending of those funds. For example, it is very unlikely that a state / territory or the Commonwealth government would provide funds to a local government and retain the right to control the spending of those funds. Therefore, Example 3A.1 may only be useful in limited circumstances when the recipient does not control the spending of the funds.

As stated above, ACAG does not believe that when the university has the discretion to select scholarship recipients and award scholarships, there is a sufficient basis for recognition of a financial instrument and a financial liability under the current standards. ACAG has sympathy that it may be reasonable to recognise a different type of liability or obligation, similar to that currently being discussed by the IPSASB under its Revenue project. If the AASB thinks that recognition of a liability is the right outcome, the AASB should consider making further amendments to the standards following the IPSASB redeliberations.

Proposed Example 3A.1 - Income from endowment funds

The proposed example has added the following fact:

- all income generated from investing the principal can be used by the university to further its objectives at the university's discretion.

This fact does not appear to be referred to in the analysis, and its relevance to the conclusion is not clear. Consequently, questions have been raised as to whether the conclusion in the proposed Example 3A.1 would change if, for example the:

- income generated had to be used by the university for the purposes of the agreement (i.e., increase the amount available to be paid as scholarships)
- asset was not income producing (for example nil or even negative returns in the current low interest environment).

ACAG believes that this fact is important in concluding that the pass-through criteria for derecognition of the financial asset (cash) are not met (AASB 9.3.2.5(c)). The AASB should make this explicit in its analysis.

Concerns with existing Examples 3B and 3C

ACAG is not clear whether the AASB intends to retain Examples 3B and 3C (which are based on facts in the existing Example 3A) without amendments, even though Example 3A is amended.

ACAG suggests that the AASB specifically expose any significant intended changes to these examples to ensure that the concerns raised with the amended Example 3A.1 (see above) are addressed.

ACAG suggests that the accounting in Example 3C be reviewed for consistency with AASB 15 paragraphs 73 to 75 and F32. In particular, Example 3C separates out an income component, even though the requirements for separation do not appear to be met as there is only one performance obligation and there is no separately identifiable donation component.

Review of existing examples

As stated above, it is not clear what facts and circumstances resulted in the AASB concluding that the arrangement was a financial liability and the significance of the scholarships being paid at the direction of the alumnus (as opposed to the university having this discretion). ACAG notes that relevant facts and circumstances may include the obligation to pay cash after undertaking some activities (selecting a variable number of suitable student recipients) and / or the obligation to return any unspent funds (remaining amount of the principal) at the end of the 10-year period.

There are similar facts and circumstances included in other existing examples in AASB 15 Appendix F and AASB 1058 where unspent funding received must be returned to the grantor and the conclusion does not result in the recognition of a financial liability. ACAG believes that a financial liability should not be recognised in these existing examples unless/until a breach of the conditions has occurred or is expected.

The examples identified are:

AASB 15 Appendix F

- Example 2 – Research activities - where there is an obligation to return funds that are either unspent or not spent in accordance with the agreement.
- Example 4 – Research activities – where there is an obligation to return funds that are either unspent or not spent in accordance with the agreement.
- Example 5 – Research activities – no contract with a customer – where there is an obligation to return funds that are either unspent or not spent in accordance with the agreement.

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- Example 6A – Enforceable agreement, no specific performance obligations but restrictions on timing of expenditure – obligation to return unspent funds.
- Example 7D – Obligation to return unspent funds.
- Example 8A – Multi-year cash grant – obligation to return unspent funds.
- Example 9 – Cash grant for the construction of a recognisable asset – income recognised over time – obligation to return unspent funds.
- Example 11 – Cash grant for the construction of a recognisable asset – income recognised over time – obligation to return unspent funds.

Concessionary leases (not-for-profit private sector lessees)

2. In respect of not-for-profit private sector lessees, do you agree with the proposal that the current accounting policy choice in AASB 16 paragraphs Aus25.1–Aus25.2 (for not-for-profit entities to elect to initially measure a class of concessionary right-of-use assets at cost or fair value) should be retained on an ongoing basis (i.e. with no plan to reconsider the accounting policy choice)? If not, please provide your reasons.

ACAG is not commenting on this not-for-profit private-sector issue.

3. Do you agree that the disclosures required by AASB 16 (including the requirements in AASB 16 paragraphs Aus59.1–Aus59.2) provide sufficient information to users of financial statements in the absence of fair value information? Are there any other disclosures regarding concessionary leases that would be useful to users of financial statements without incurring undue cost or effort for preparers? Please provide reasons to support your answer.

ACAG is not commenting on this not-for-profit private-sector issue.

- 4. If in response to Question 2 you consider that not-for-profit private sector lessees should be required to initially measure right-of-use assets arising under concessionary leases at fair value, do you consider that the initial fair value measurement requirement should be applied:**
- a) prospectively, to concessionary leases entered into after the date of application of the removal of the accounting policy choice to measure such right-of-use assets at cost; or
 - b) retrospectively (i.e. requiring existing right-of-use assets arising under concessionary leases to be adjusted to reflect the effect of the initial

Please provide reasons to support your answer.

ACAG is not commenting on this not-for-profit private-sector issue.

Concessionary leases (not-for-profit public sector lessees)

- 5. In respect of not-for-profit public sector lessees, do you agree that, in the absence of fair value information about concessionary leases, the disclosures required by AASB 16 (including the requirements in AASB 16 paragraphs Aus59.1–Aus59.2) provide sufficient information to users of public sector entities' financial statements? Are there any other disclosures regarding concessionary leases that would be useful to users of public sector entities' financial statements without incurring undue cost or effort for preparers? Please provide your reasons to support your answer.**

ACAG is not aware of any significant concerns with the adequacy of the current level of disclosures and does not propose any other disclosures.

AASB General Matters for Comment

- 6. Whether the AASB Not-for-Profit Entity Standard-Setting Framework has been applied appropriately in developing the proposals in this Exposure Draft?**

ACAG agrees that the NFP Framework has been applied appropriately, given the nature and extent of funding arrangements and concessionary leases in the NFP sector.

- 7. Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, including Government Finance Statistics (GFS) implications?**

ACAG is not aware of any additional regulatory or GFS issues to those already in AASB 15 and AASB 1058 that may affect the implementation of the proposals.

- 8. Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals?**

Refer to our response for Question 7.

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



ACAG agrees with the intention of the proposals to reduce the diversity in application of AASB 15 and AASB 1058, and to provide clarity for the public sector on the application of the 'temporary' exemption for fair valuing concessionary leases.

As discussed above, ACAG does not believe the proposed changes to the illustrative examples provide the necessary clarity to reduce diversity.

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

ACAG is not able to comment on whether these proposals are in the best interests of the Australian economy.

11. Unless already provided in response to specific matters for comment 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

ACAG is not able to comment on costs and benefits of the proposals.