

The Institute of Public Accountants
**Comments to AASB on ED 260: Income of
Not-for-profit Entities**

August 2015



IPA INSTITUTE OF PUBLIC
ACCOUNTANTS®

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

Dear Kris

ED 260 “Income of Not-for-Profit Entities”

Thank you for the opportunity to comment on the ED 260 “Income of Not-for-Profit Entities”.

The Institute of Public Accountants (IPA) broadly supports the proposals in relation to the recognition of income for not-for-profit (NFP) entities. The introduction of performance obligations to recognition of income NFPs will result in a more faithful representation of the substance of the activities of NFPs than the existing reciprocal/non-reciprocal transfer concept. As such, the financial statements of NFPs will be more meaningful to users.

Notwithstanding the above, the IPA has two reservations:

1. The IPA broadly supports the concept of specific performance obligations espoused in the proposal. However, the IPA believes a narrow interpretation of performance obligations could result in outcomes inconsistent with AASB 15 “Revenue from Contracts with Customers”. The IPA believes this is particularly evident in the illustrative examples planned to accompany the proposed standard. Our detailed responses in relation to these issues are set-out in our response to Questions 1 and 2 of the Exposure Draft.
2. The IPA believes the application of the control to the contribution of assets needs to be better explained. The IPA has specific concerns in respect of the recognition of income and assets in relation to specific purpose bequests. The guidance currently proposed is restricted in terms of performance obligations and legal form. The IPA believes more specific guidance needs to be provided on how restrictions on the rights and use to assets may affect the recognition of such assets. Furthermore, disclosure should be added for assets recognised by NFPs where there are restrictions in place over the use of such assets. The IPA anecdotally is aware of instances where assets arising from bequests are recognised as assets where the economic substance would indicate significant restriction on the use of the asset; and therefore asset recognition is not met. The IPA is concerned the proposed standard is not sufficiently robust to ensure assets to which the NFP does have control in accordance with accounting concepts are not recognised.

Our comments on the detailed questions asked in the Exposure Draft are in the attached appendix to this letter.

If you would like to discuss our comments, please contact me or our technical advisers Mr Stephen La Greca (stephenlagreca@aol.com) or Mr Colin Parker (colin@gaap.com.au) (a former member of the AASB), GAAP Consulting.

Yours sincerely



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About the IPA

The IPA is a professional organisation for accountants recognised for their practical, hands-on skills and a broad understanding of the total business environment. Representing more than 35,000 members in Australia and in over 65 countries, the IPA represents members and students working in industry, commerce, government, academia and private practice. Through representation on special interest groups, the IPA ensures the views of its members are voiced with government and key industry sectors and makes representations to Government including the Australian Tax Office (ATO), Australian Securities and Investments Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) on issues affecting our members, the profession and the public interest. The IPA recently merged with the Institute of Financial Accountants of the UK, making the new IPA Group the largest accounting body in the SMP/SME sector in the world.

Appendix A

Question 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.*

IPA Response

The IPA supports the recognition of income for NFPs on a basis consistent with the principles of AASB 15 "Revenue from Customers". The IPA supports the development of standards on a sector/transaction neutral basis wherever possible. As such the adoption of an income recognition basis for NFPs consistent with current pronouncements should be the objective. The IPA believes the reciprocal/non-reciprocal transfer distinction in AASB 1004 is no longer consistent with the concepts in relation to revenue recognition espoused in AASB 15 and, therefore, should no longer be applied.

However, we are concerned that a number of examples in the Appendix, including Examples 2, are inconsistent with the principles of AASB 15. The IPA believes in the case of Example 2 a performance obligation exists as the money received has been raised primarily for the provision of clean water in a particular developing country. The fact the money may be used for other purposes, in the IPA's opinion, effectively means the money received is non-refundable. The non-refundable nature of the receipt should not affect the pattern of income recognition under AASB 15. Revenue is not recognised until the performance obligation is met. In the circumstances described in Example 2 where war had made the further execution of the performance obligation non-achievable, when that event occurs (i.e. the war) the balance of monies received can be recognised as income. Similarly, if the drilling program is complete, any surplus funds received would be recognised as income.

The IPA also supports the recognition of income for amounts or assets received that do not give rise to a performance obligation on the basis of control of the asset. However, the IPA believes insufficient explanation and guidance has been provided on how to apply the control concepts in a NFP context. In particular, the IPA believes specific guidance on the application of control concept needs to be incorporated in the proposed standard to deal with bequests.

Furthermore, the IPA does not believe the application guidance at AG9 in relation to performance obligations gives appropriate consideration to the NFPs ability to control the asset in accordance with the accounting concept of control (regardless of the legal form). The IPA is concerned that the proposed standard could result in the recognition of income and assets that a NFP has only limited control over, for example, an amount has been left in a bequest for which the income is available to be used by the NFP but the principal amount is not available for use, or an asset has been provided for a specific use. Guidance needs to be provided for the basis of recognition of such assets and, in the event such assets are recognised, appropriate disclosures relating to restrictions relating to their use, including the ability to use such asset as security or to liquidate them.

Question 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.*

IPA Response

The IPA generally supports the concept of “specificity” of the performance obligation to the extent it assists in the identification of the performance obligation. As such, the IPA believes that certain examples in the proposed guidance are inconsistent with AASB 15, such as, Example 3B. The IPA believes the obligation to provide a service over a period of time is similar to a retainer situation where, for example, a legal firm may receive a retainer to undertake unspecified professional activities over a period. Such income would be recognised over the period of the performance obligation, that is, the period covered by the retainer. This is similar to the Example 3B where a grant has been received for a period to be used in accordance with the charity’s overall objective and income should be recognised in a similar manner. Any refund liability would be recognised at inception in accordance with AASB 15 requirements.

Question 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?

IPA Response

The IPA supports the recognition of a donation component in a contract with customers on an immediate income based on the guidance at IG19-IG30.

Question 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.)

IPA Response

The IPA supports the recognition of volunteer services by all NFPs on the basis set out in paragraph 19 of the proposed standard. The IPA would prefer there to be no distinction between public sector and private sector NFPs in the interest of sector neutrality.

Question 5

Do you agree that 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 of a portfolio or other aggregate level? (See also paragraphs BC50-BC51 of the Basis for Conclusions.)

IPA Response

The IPA supports the proposal at paragraph 31 as a rebuttable position. However, if there are reasonable grounds to believe the donated inventory includes individually material items, the fair value of such items should be assessed on an individual basis and not a transaction basis.

Question 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 owner’ 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.)*

IPA Response

The IPA believes the current definition of “contribution from owners” should be deleted from the proposed standard. The IPA believes the current definition results in non-revenue items being treated as income and would support a wider definition to ensure an appropriate treatment of transfers of assets occurs. The IPA would support a definition based on the IPSASB Public Sector Conceptual Framework.

Question 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-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?*

IPA Response

- (a) As stated in response to Question 6 the IPA supports a definition of contribution from owners based on the IPSASB Conceptual Framework and, as such, the issues arising from the AASB 1004 definition would no longer necessitate the need for the AASB Interpretation 1038.
- (b) The IPA supports the removal of the specific requirements of AASB 1004 relating to administrative restructures to the extent sufficient guidance is available under existing standards, for example, AASB 3 and the Conceptual Framework.
- (c) The IPA supports the removal of the specific requirements of AASB 1004 relating to distributions to owners to the extent sufficient guidance is available under existing standards and the Conceptual Framework.
- (d) The IPA supports the removal of the specific requirements of AASB 1004 relating to the assumption of liabilities to other entities to the extent sufficient guidance is available under existing standards and the Conceptual Framework.
- (e) The IPA is not in a position to express an opinion as to the practical implication of the withdrawal of the definition of “contribution from owner” and the AASB Interpretation 1038. However, the IPA understands that certain contributions from owners would likely not be considered revenue if a definition consistent with the IPSASB Conceptual Framework. In addition, guidance on the matters mentioned in Question 7(b)-(d) would need to be sourced from guidance in other existing standards. If the existing guidance is not sufficient to address the requirements for NFPs then the AASB should include such guidance in the proposed standard and/or as NFP AUS guidance in the relevant standards.

Question 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.)

IPA Response

The IPA supports the proposed changes to disclosure requirements regarding compliance with government department appropriations.

Question 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.)*

IPA Response

The IPA supports transitional requirements in Appendix C of the proposed standard.

General matters for comment

Question 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).*

IPA Response

The IPA is unaware of any regulatory or other issues that may affect the implementation of the proposals.

Question 11

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

IPA Response

The IPA is of the opinion the introduction of performance obligations to the reporting of revenue enhances the usefulness of NFP financial reports.

Question 12

Whether the proposals are in the best interests of the Australian economy,

IPA Response

By increasing the usefulness and accountability of NFP sector financial statements the proposals are in the best interests of the Australian economy.

Question 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.

IPA Response

The IPA is not in a position to estimate the quantitative cost of the proposed standard.