Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Post-Implementation Reviews**	**Meeting:**	M199
Topic:	**Income of Not-For-Profit Entities - Differences between management accounts and statutory accounts and alternative revenue recognition models**	**Agenda Item:**	3.2.2
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		Project Priority:	Medium
		Decision-Making:	Low
		Project Status:	Initial consideration of stakeholder feedback

Objective of this paper

1 The objective of this Staff Paper is for the Board to:

(a) **consider** the feedback received on Topic 3: Difference between management accounts and statutory accounts and alternative revenue recognition models included in ITC 50 *Post-implementation Review – Income of Not-for-Profit Entities* (ITC 50); and

(b) **discuss** the feedback, staff analysis and preliminary views in relation to ITC 50 Topic 3. The Board will not be asked to make any decisions at this meeting but rather to provide feedback and suggestions for further analysis. Following the discussion at this meeting staff will develop recommendations and ask the Board to decide on possible next steps[1] at a future meeting.

This paper is carried over from the AASB September 2023 meeting agenda item 8.2.2 amended for editorial references without any substantial modifications, other than to accommodate that agenda papers 8.2.3 *PIR Income of Not-for-Profit Entities – Sufficiently specific criterion* and 8.2.4 *PIR Income of Not-for-Profit Entities – Termination for convenience clauses* will be considered by the Board at a future meeting.

Structure

2 This paper is structured as follows:

(a) Background (paragraphs 3 to 9)

1 Subject to the Board decision at the October 2023 meeting, staff plan to use the framework included in Agenda Item 3.1 *Decision-making process* of this meeting to determine their recommendation whether, how and when to address the feedback from the PIR.

(b) Analysis of respondents' feedback (paragraphs 10 to 82)

(c) What the AASB has done so far (paragraphs 83 to 108)

(d) Staff analysis and preliminary views (paragraphs 109 to 138)

Background

3 AASB 1058 *Income of Not-for-Profit Entities* and AASB 15 *Revenue from Contracts with Customers* Appendix F *Australian implementation guidance for not-for-profit entities* contain specific requirements for recognising income of not-for-profit (NFP) entities. In some cases, entities are required to recognise income on receipt, whilst expenses are recognised when incurred, which could be in a subsequent reporting period or periods.

4 Income recognition of NFP entities is complex (Gilchrist, West and Zhang 2023).[2] As summarised in Agenda Paper 3.2.1 providing an overview of the feedback by topic, when developing ITC 50, feedback from some preparers indicated that recognising income on receipt for some agreements (for example, where an agreement is not within the scope of AASB 15) is unhelpful for users of the NFP entity's financial information. In some cases, the entity believes activities, subject to the receipt of funding, are still to be performed. Where this is the case, some NFP entities are preparing internal reports based on the activities carried out rather than in accordance with Australian Accounting Standards (AAS) (i.e. entities are recognising revenue based on when expenses are incurred) because this information is perceived to be what those charged with governance and management of the entity find most useful.

5 Feedback also indicated that a management-preferred basis (management accounts) is often used when preparing financial information for donors unless the information is prepared for statutory purposes, especially in cases when income is being recognised upfront and the agreement requires the activities to be performed in future periods. It is also understood that most acquittal statements for funding received are prepared on a cash basis.

6 Some stakeholders also noted that where funds are received, particularly in the form of a grant, it is their view that because certain activities have to be performed, recognising revenue based on when expenses are incurred would provide more useful information to users. Further, they argue that matching revenue and expenses is consistent with AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*, which applies only to for-profit (FP) entities.

7 ITC 50 asked the following questions on differences between management accounts and statutory accounts and alternative revenue recognition models:

Questions for respondents

9. Do you have any comments regarding the timing of revenue recognition required by AASB 15 and AASB 1058 of NFP entities? If so, please provide your views on those requirements, relevant circumstances and their significance. Examples to illustrate your responses are also helpful.

10. Do you have any views on alternative approaches to recognising revenue in the NFP sector? For example, should an NFP entity initially recognise a liability and recognise revenue:

2 Gilchrist, D.J., West, A. and Zhang, Y. (2023), Barriers to the Usefulness of Non-profit Financial Statements: Perspectives From Key Internal Stakeholders. Australian Accounting Review, 33: 188-202. https://doi.org/10.1111/auar.12401

(a) based on a common understanding between the entity and the transfer provider of the manner in which the entity is expected to use the inflows of resources;[3]

(b) where there are terms in law or regulation, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity;[4]

(c) on a systematic basis over the periods in which the entity recognises as expenses the related costs for which a grant is intended to compensate;[5] *or*

(d) where the outflows of resources are incurred in accordance with the requirements set out in a binding agreement.[6]

If so, please provide your views on your preferred alternative(s) above or another alternative approach.

8 Following the issue of the ITC, during the outreach phase of the post-implementation review (PIR), staff actively engaged with stakeholders to seek feedback on this topic.[7] In addition to formal comment letters being submitted, stakeholders could also provide feedback on this topic via a survey and discussion during the various roundtable events held by staff. Stakeholders were also invited to discuss the topic further during one-on-one meetings with staff where they requested this.

9 This Staff Paper is part of the 'feedback and next steps' phase of the PIR process. Agenda Paper 3.1 *Decision-making process* sets out a suggested framework to support the Board in considering stakeholder feedback and determining what action, if any, may be required.

Analysis of respondents' feedback

ITC 50 questions 9 and 10: Timing of revenue recognition required by AASB 15 and AASB 1058 of NFP entities and views on alternative approaches to recognising revenue in the NFP sector

10 Twelve respondents[8] gave feedback relevant to questions 9 and 10.[9] Staff have summarised this under the following themes:

(a) Challenges with the accounting requirements of AASB 15 and AASB 1058;

(b) Support for a principles-based approach;

(c) Inconsistency with AASB 120 for-profit accounting requirements;

(d) Upfront income recognition;

(e) Management and statutory accounting records;

(f) Preference for 'matching' income with expenses;

(g) Disclosures as a possible solution; and

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3 AASB Discussion Paper *Development of Simplified Accounting Requirements (Tier 3 Not-for-Profit Private Sector Entities)* paragraph 5.182.

4 International Public Sector Accounting Standard IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)* paragraph 7: definitions of stipulations on transferred assets and conditions on transferred assets.

5 AASB 120 paragraph 12.

6 IPSASB Exposure Draft ED 71 *Revenue without Performance Obligations* paragraph 10: definition of eligible expenditure.

7 See Agenda Paper 3.2 *Cover Memo: Income of Not-for-Profit Entities* for more details.

8 See submissions 1, 2, 3, 4, 5, 7, 8, 9, 10, 12, 13 and 14.

9 Staff noted that comments made by respondents as part of their feedback to other questions may be relevant to question 9. This feedback has been included where staff consider it most relevant.

(h) Measures already taken by the AASB and possible future measures.

11 Comments made at the NFP Advisory Panel meeting, Roundtables 1 to 3 and individual meetings are consistent with feedback received in the comment letters. Specific comments have been included in this paper where relevant.[10]

12 Overall, in line with the feedback received prior to the issue of ITC 50, many stakeholders provided feedback on the preparation of management accounts, with the need for these increasing where income is being recognised upfront and this not necessarily reflecting the reality of the agreement (i.e. activities to be performed in future periods). Some entities may also use financial statement disclosures to communicate what funding is restricted (as encouraged by AASB 1058). However, some did not think it was necessary to overhaul or redesign the existing revenue recognition model because it is principles-based and a lot of effort went into developing it including public consultation.

13 There were mixed views on the alternative approaches noted in ITC 50 without a clearly preferred model by a majority with some respondents preferring a particular model while others provided comments on why adopting it would not be suitable.

Challenges with the accounting requirements of AASB 15 and AASB 1058

14 Seven respondents (Pitcher Partners (PP), PwC, Sydney University Sport & Fitness Ltd (SUSF), HoTARAC, ACAG, CAANZ and CPA Australia and KPMG) noted:

(a) significant judgement is required to apply the requirements of AASB 15 Appendix F and AASB 1058 (the Standards) and there is difficulty in navigating between them, with both giving different outcomes on the timing of revenue recognition;

(b) ambiguity of the sufficiently specific term. In SUSF's view, the sufficiently specific term is not adequately defined within AASB 15;

(c) that the complexities of applying the Standards have resulted in frustration and significant costs for NFP entities, practitioners and auditors, with each applying their own judgements. In acknowledging the complexities of the Standards, PwC commented that this is not unusual with new standards and is a result of the principles-based rather than a rules-based approach to standard-setting;

(d) that the current guidance in Appendix F to AASB 15 appropriately follows the transaction neutrality principle and should be applied where an arrangement involves the transfer of goods or services. However, where the transfers of goods or services is not present, KPMG would be supportive of exploring whether an alternative income recognition approach, that considers the cost the grants are intended to compensate, to meet the needs of users;

(e) that the Standards have not addressed the lack of comparability issue that existed under the previous accounting standards. Comparability is still not achieved if two similar entities (with similar agreements) report their income differently depending on how they assessed the sufficiently specific criterion. HoTARAC provided the specific example of infringement notices, with the auditor's view that they should be accounted for applying AASB 15 while the preparer's view that they should be accounted for applying AASB 1058; and

(f) ITC 50 correctly identified the major and diverse challenges being experienced and the difficulty of resolving them.

10 Detailed comments are included in Agenda Paper 3.2.6 *ITC 50 outreach meeting notes* [Board only].

Support for a principles-based approach

15 Following on from PwC's comments in paragraph 14(c), PwC commented that the principles underlying AASB 1058 were discussed at length by the AASB and decisions were carefully made to ensure the outcome is a standard that is consistent with the underlying [Conceptual Framework](). A member of the NFP Advisory Panel at the virtual meeting, CAANZ and CPA Australia and HoTARAC also expressed support for a principles-based approach. PwC are supportive of the current model and do not recommend that the Board go back to the drawing board and start anew. The NFP Advisory Panel member expressed that it may not be effective or a good option to start again or the best use of resources.

16 In general, the existing recognition criteria in the Standards are supported by HoTARAC, because they are mostly consistent with the definition and recognition criteria for assets, liabilities, and income in the Conceptual Framework. HoTARAC commented that the existing income recognition criteria in the Standards is also consistent with other accounting standards, including AASB 9 *Financial Instruments* and AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*. Consequently, this framework is generally well understood by preparers which gives rise to the more efficient preparation of statutory reports. A member of the NFP Advisory Panel at the virtual meeting, when discussing ITC 50 Topic 2: Capital Grants, said that judgement is not necessarily bad and they would not like to move to a rules-based standard. A certain level of judgement needs to be accepted.

Inconsistency with AASB 120 for-profit accounting requirements

17 One respondent (RSM) highlighted the inconsistency with the treatment of government grants in the FP sector under AASB 120.

18 HoTARAC commented that while stakeholder feedback provided to the AASB has previously argued that matching incomes and expenses is consistent with AASB 120, it is difficult to determine the conceptual underpinning for differential recognition between AASB 120 paragraph 12 (matching revenue with expenses) and AASB 1058 paragraph 10 (recognising income on establishment of control). They further noted that the receivable for compensatory government grants for financial support, per AASB 120 paragraph 20, should only be recognised once the government has no practical alternative to avoid making the grant. The private sector recognition of revenues ought to be informed by grant program best practice. Best practice includes establishing eligibility, assessing the grant aggregate, and approving the grant applicant for payment.

19 HoTARAC also commented that given IAS 20 was initially effective for 1 January 1984 and has only been amended for below market-rate of interest loans (effective on or after 1 January 2009), it appears that it is timely to review IAS 20/AASB 120 against current international conceptual frameworks applying to generally accepted accounting principles.[11]

20 A member of the NFP Advisory Panel commented that there have been views in the past by the AASB that NFP and FP accounting need to align but they were not convinced that this is a must given there are other NFP and FP accounting differences.

Upfront income recognition

21 Four respondents (Stuart Brown (SB), SUSF, ACAG, and RSM) commented that the upfront income recognition requirements of AASB 1058 do not necessarily reflect the reality of the funding position of NFP entities:

11 Staff note in paragraph 99, that following its most recent Agenda Consultation, the IASB has not added a project relating to IAS 20 to its 2022-2026 work plan.

(a) SB and RSM commented that this requirement potentially gives rise to the unintended consequence of generating an artificially inflated surplus in one year, followed by deficits in future years when the recognition of the related expenses occur. This is even where funds are provided for a specific multi-year period and where there is an obligation to refund any unspent funds; and

(b) SUSF are now required to account for 35%-40% of their revenue applying AASB 1058 even though the funds are allocated to specific programs and it is not possible to transfers the funds from one program to another. Other funding is accounted for under AASB 15. SUSF commented that this brings into question the reliability of the financial information reported given the two ways of accounting for revenue and the usefulness to users. Similarly, ACAG and RSM commented that there is a perception by preparers that the recognition of revenue upfront results in a decreased understanding of financial information that is not useful to some users and is misleading to their financial results, with a particular impact on non-financially experienced persons.

22 A survey respondent commented that reporting income when received and not drawdown in line with the expenditure for which that income is required makes it difficult to report to management and the Board on the actual income available and results in issues when presenting management accounts because the 'surplus' is due to timing alone.

23 Two stakeholders in separate individual meetings expressed concern that potential donors/funders might decide that no money is needed when grant income is recognised upfront and the entity has a large surplus in that specific financial year. To avoid this, entities are asking grantors to provide the funds in the new year rather than before year-end, with the grantors agreeing to this. One of these stakeholders raised the concern that entities could have had a large sum of money in their bank account receiving interest if it was paid before year-end.

Small NFP entities who receive capital grants and recognition upfront

24 In their submission, Corporate Audit and Assurance Services asked the Board to consider the effects of small NFP entities receiving a capital grant and recognising it as income upon receipt[12] with the depreciation expense recognised over the life of the asset or the remaining lease term.

25 Staff consider that this and similar issues faced by smaller NFP entities may be resolved if and when these entities are able to apply the Tier 3 Standard the AASB is currently developing which, subject to the Board's future decisions, may allow the initial recognition a liability and revenue based on a common understanding between the entity and the transfer provider of the manner in which the entity is expected to use the inflows of resources.[13]

Management and statutory accounting records

26 Seven respondents provided feedback in response to management and statutory accounting records (SUSF, ACAG, RSM, BDO, ACNC, HoTARAC and Deloitte). The need for two sets of accounts is heightened where an entity recognises grant income upfront applying AASB 1058 and the expenditure, subject to the funding, is incurred in a subsequent period(s). Statutory accounts may be seen as unreliable, not useful or the 'mismatch' not understandable by stakeholders[14] and therefore management accounts are produced as the users do not have a sufficient understanding of the accounting requirements. There may be challenges explaining the different approaches taken in the management and statutory accounts, why AASB 15 or AASB 1058 has been applied and why there

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12 Details of the specific scenario are included in submission 11. Staff note there are no specific details included in the submission outlining why the requirements of AASB 1058 paragraphs 15 to 17 have not been met, which would allow for the deferral of income.

13 ITC 50 included Topic 2: Capital grants which will be discussed at a future meeting.

14 Including an entity's board, management, ASIC, the public/users and financial institutions and other funding providers.

may be differences to the operating result between the management and statutory accounts. An attendee at an ACNC Forum commented that the financial reporting requirements may not be understood by entities however they also commented that accrual accounting as such is not easily understood and it is considered complex, and any rules that are adopted need to be as clear and consistent as possible.

27 Producing two sets of accounts is considered a poor use of management time and requires additional work by some respondents who already have limited resources (SUSF, ACNC and RSM). In an individual meeting a stakeholder commented that entities are paying to reconcile the management accounts to the statutory accounts or spending more staff time doing this. However, HoTARAC commented that the level of administrative work associated with the timing of income recognition is anticipated to decline as preparers and auditors develop increasingly mature understandings of the respective Standards.

28 ACAG specifically commented that AASB 15 is not aligned to common funding arrangements in the public sector and there are often differences between internal reporting, internal acquittal processes and statutory reporting. There are a variety of ways this is implemented in practice. For example, some jurisdictions have found many entities appear to use upfront revenue recognition for management accounting, and then make any adjustments needed for statutory reporting. Some entities will make adjustments monthly (to align management and statutory reporting), and others less frequently, at year-end. For many entities, the acquittal process is outside management reporting and statutory reporting.

29 A survey respondent commented that they have had many clients that want to prepare management accounts on a matching basis, and then only make annual adjustments for statutory reporting purposes resulting in increased costs to maintain both management and statutory reporting. A survey respondent and a member of the NFP Advisory Panel at the virtual meeting commented that this practice also creates an issue where the statutory financial outcomes may differ significantly to those reported to those charged with governance due to the year-end adjustments to comply with the accounting standards. Another Panel member agreed that management accounts are being prepared often but noted that this also occurs in the FP sector even though it may relate to areas other than revenue recognition. This stakeholder did not think any action needed to be taken by the AASB to address this issue.

30 In answering ITC 50 question 1,[15] BDO also commented that there are entities that recognise income immediately under AASB 1058 in their statutory financial statements because they do not want to spend the time performing the sufficiently specific assessment. These entities apply the matching principle in their management accounts and are accountable to donors and grantors on this basis.

31 One attendee at Roundtable 2 commented that in the state government area they had not heard that alternative reports were being prepared and there had not been any major requirements for year-end adjustments. However, this may not be the case in the local government with one attendee commenting that they do not do their statutory accounts on a monthly basis and year-end adjustments are made to comply with the Standards.

Preference for 'matching' income with expenses

32 One respondent (ACAG) commented that a lot of funding agreements do not have sufficiently specific performance obligations and the upfront recognition does not align with NFP entities' preference for matching revenue/income and expenses. Similarly, another respondent (HoTARAC) also noted that

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15 'Regarding the term sufficiently specific in AASB 15 Appendix F, do you have any comments about: 1. the application of the term in practice?'

many preparers prefer to match income with expenses per the generally accepted accounting principles that existed before the adoption of International Financial Reporting Standards (IFRS) equivalents.

33 Further, ACNC commented that charities regularly contact them asking how to account for grants. Their interactions with charities suggests that some charities (many of them prepare special purpose financial statements (SPFS)) are recognising grant revenue as grant related expenses are incurred, rather than by strict adherence to the reporting requirements in AASB 15 and AASB 1058. Feedback the ACNC has received indicates that charities and the users of their financial reports consider this approach to be logical, easy to understand and the financial report information is used both externally and internally by charity boards and management. Given that grant funding is very common for charities, this suggests that matching of revenue and expenses, at least in relation to grant funding, may be relatively common in the sector. The ACNC's view is that wherever possible and appropriate, charities should have as much flexibility as possible to recognise grant revenue progressively as they expend grants given that most grants are for a specific purpose, even if they have varying degrees of acquittal/contractual obligations.

34 A survey respondent commented that where there is a common understanding of a pattern of economic outflows, most users expect to see the income recorded in the same period as those economic outflows, and generally find the AASB 1058 application of 'income on receipt' quite confusing. Another survey respondent commented that having expenses accounted for independently from income can cause issues with keeping track of budget especially for large projects over multiple years. Related to this, in an individual stakeholder meeting, a stakeholder commented that entities may be accounting for expenses early to get matching.

Disclosures as a possible solution

35 Paragraph 37 of AASB 1058 encourages an entity to disclose information about externally imposed restrictions that limit or direct the purpose for which resources controlled by the entity may be used. For example, an entity may elect to disclose an explanation of the judgements used in determining whether funds are restricted and any of, or any combination of, the following:

(a) assets to be used for specified purposes;

(b) components of equity divided into restricted and unrestricted amounts; and

(c) total comprehensive income divided into restricted and unrestricted amounts – either on the face of the statement of profit or loss and other comprehensive income or in the notes.

36 The Basis for Conclusions (paragraphs BC126 to BC130) also noted that the Board had not exposed a proposal in this regard, and accordingly, decided to encourage the disclosure of information in this regard as opposed to requiring entities to make that disclosure.

37 Two respondents (Deloitte and BDO) commented that they have observed many entities utilising disclosures in the financial statements to better explain its story to users, rather than keeping a separate set of management accounts – for example, voluntary disclosures around the restrictions of funds or use of a 'special purpose reserve' in the statement of changes in equity to quarantine and keep track of such restricted funds (where income has been recognised upfront but there are future services to be performed or expenses yet to be fully incurred) representing the amount of revenue that would have been deferred had matching been permitted under AASB 1058. The use of the 'restricted funds' disclosures was noted by a few stakeholders in individual and virtual meetings.

38 BDO commented that they understand this approach is followed where statutory financial statements are used to attract funding. That is, they are concerned that a surplus could be understood to mean

that the entity does not require funding. Conversely, a deficit could be understood as being that the entity is not properly managing its projects. As a result of these disclosures, Deloitte commented that they do not see a need for standard-setting to address this issue as it can be addressed, if desired, via voluntary disclosure. Another respondent (HoTARAC) also suggested that additional disclosures by preparers can show the progress of works done for ring-fenced funding without compromising IFRS compliance.

39 One respondent (ACAG) also made comments in relation to Commonwealth Financial Assistance Grants to local governments, which do not set out any obligations or activities to be performed. Some local governments in various jurisdictions include a disclosure in their financial statements for transparency to highlight the financial assistance grants received from the Commonwealth that are recognised in the current year that relate to the following financial year.

40 Staff heard that some local councils have developed an operating surplus ratio disclosed in the notes to the financial statements that communicates the actual surplus but it was noted that the notes do not provide as much visibility as recognition or presentation on the face of the primary financial statements.

41 At Roundtable 3 an attendee commented that disclosures could be used to explain how retained earnings have been quarantined for specific purposes and thought the AASB could provide further guidance on how preparers could disclose the quarantined funds provided for, for example, a specific purpose or a project and the subsequent expenditure to explain the nature of the deficits in future years without necessity of non-GAAP disclosures.

42 An academic from Swinburne University noted that in preliminary research conducted, the findings showed that 22 out of 40 universities disclosed information about restricted assets.[16]

Measures already taken by the AASB and possible future measures

43 One respondent (PwC) acknowledged the efforts of the AASB staff to perform outreach and issue FAQs to support stakeholders in some of the more challenging areas.

44 PwC also noted that some of the difficulties applying the model are due to the technical language used in the Standards as well as the fact that guidance is included in multiple places (i.e., AASB 15, AASB 1058 and FAQs). While PwC appreciate that this is not easily fixed, they recommend considering whether the guidance could be better consolidated into one place. At a minimum, certain guidance (in particular the flowcharts) might be incorporated into the Standards. Also, the AASB might consider collaborating with the ACNC to develop a plain English guide.

45 One respondent (HoTARAC) commented that additional illustrative examples would augment the growing knowledge base of preparers and users, particularly where illustration of the sufficiently specific criterion is enhanced.

46 In contrast, one respondent (CAANZ and CPA Australia) commented that although they support principles-based standards they consider applying the current principles to a diverse range of circumstances is complex and continued refinement to address specific fact-patterns, via standard-setting activity or additional guidance, appears to be of limited value in addressing the interpretational challenges. CAANZ and CPA commented that despite the many implementation concerns that have been raised, feedback they have received indicates that, on a cost/benefit basis, there is insufficient justification for any further amendments to AASB 1058 and AASB 15 Appendix F at this point in time. Many NFP and their advisors have invested considerable effort to implement the

16 Submission 6 from Dr Mark Shying CA, Swinburne University School of Business, Law and Entrepreneurship (academic).

accounting requirements, including modifying their systems and approaches to address key judgement issues. They recommend focusing on the Tier 3 Standard development and implementation which also allows sufficient time to be informed by IPSASB 47 *Revenue* and the IFR4NPO standard (INPAG) proposals when considering amendments to AASB 15 and AASB 1058.

47 A survey respondent commented that modifying the current wording in the Standards would be difficult as it may result in a greater amount of preparer judgement and less comparable financial statements between different entities.

ITC 50 question 10: Do you have any views on alternative approaches to recognising revenue in the NFP sector?

48 One respondent (ACNC) commented that they support all of the suggested alternative approaches to recognising revenue listed in question 10. They also suggested that the purpose of a grant could also be a relevant consideration in some cases.

49 One respondent (KPMG) commented that the current guidance in AASB 15 Appendix F appropriately follows the AASB's principle of transaction neutrality as described in the *AASB Not-for-Profit Entity Standard-Setting Framework*. Where an arrangement involves the transfer of goods or services, KPMG takes the view that the requirements of AASB 15 should be applied to those arrangements. However, where the arrangement does not involve the transfer of goods or services, then KPMG would be supportive of exploring whether an alternative income recognition approach that considers the costs the grant is intended to compensate meets the needs of users. KPMG noted that such an approach continues to require identification of an arrangement that would fall within the scope of AASB 15 and those that do not, with the need for more guidance on identifying sufficiently specific performance obligations.

50 Several respondents did not prefer wholesale changes to the underlying approaches in AASB 15 and AASB 1058 at this point in time, including CAANZ and CPA Australia and HoTARAC. PwC made comments in support of the current recognition model (refer to paragraphs 14(c) and 15), however, suggested the AASB clarify key areas where there are more pervasive areas of diversity which may be more easily addressed.[17] PwC made a specific recommendation included in paragraph 44 on the consolidation of the existing guidance. Deloitte noted that they do not see a need for standard-setting to address this issue and they do not immediately see an alternative approach to recognising revenue in the NFP sector. They commented that it is important for the Board to issue guidance around the assessment of sufficiently specific to assist entities in applying the current requirements consistently to reduce the diversity in practice.

51 ACAG and BDO made comments about some agreements not being able to be deferred under any model given they do not have any obligations for how the funds are to be used. For example, Commonwealth Financial Assistance Grants to Local Governments and ordinary grants not linked to specific expenditure.

Alternative approach (a): based on a common understanding between the entity and the transfer provider of the manner in which the entity is expected to use the inflows of resources

52 This approach, in PP's view, does not meet the definition of a liability. For example, if donors donated funds and there was a common understanding the funds were to be used for a recent flood appeal, this approach would present this as a liability on receipt. PP do not consider that such common understanding would be sufficient to meet the definition of a liability especially when the funds could

17 PwC specifically commented on 'Topic 4: Principal v agent, including the appropriate recognition of financial liabilities' and 'Topic 6: Termination for Convenience Clauses.' Comments will be presented to the Board as part of the specific topic Staff Paper.

in fact be used for any purpose determined by the NFP entity, even though the understood purpose may be in relation to the flood appeal.

53 ACAG raised the following concerns with this approach:

(a) there needs to be an obligation in order to recognise a liability (under the Conceptual Framework) for deferred revenue;

(b) it is open to a high degree of interpretation about what the common understanding actually is to determine the appropriate timing;

(c) it may be more likely to be manipulated to achieve a specific result; and

(d) overreliance may result in a lack of consistency and comparability in reporting.

54 HoTARAC commented that a common understanding between the entity and grantor on the expectation of the use of inflows are subject to considerable judgement, thereby resulting in increased audit times and verification efforts.

55 BDO consider this approach suitable for Tier 3 entities. However, BDO do not believe that such a liberal approach is suitable for Tier 1 and Tier 2 NFP entities as it will reduce comparability.

56 In contrast, Moore Australia, as part of their survey response, encouraged the Board to consider the approach proposed in the Discussion Paper on Tier 3 NFPs as a potential model to be applied by all NFPs because it appears to be clearer and simpler to apply. However, as noted in their response to the Discussion Paper, they caution the Board to consider whether the terminology used will actually alleviate the issues with sufficiently specific and they questioned whether trying to articulate the specified purpose/activity/period will lead to similar confusion. The question might still arise how much detail is required to be able to identify the specified purpose.

57 At the NFP Advisory Panel virtual meeting two members selected this approach as their preferred option. Another member (with another's support) commented that they were not going to answer the polling question because it was not clear to them the differences between approaches (a), (b) and (c). In their view, the wording is very similar and would appear to produce the same outcomes.

58 At Roundtable 1 three attendees selected this approach, one at Roundtable 2 and two at Roundtable 3. One attendee at Roundtable 1 commented that they thought approach (a), (c) and (d) are fairly aligned. An attendee at Roundtable 2, whose preferred approach was not approach (a), commented that a common understanding will make it difficult for an auditor to assess whether a common understanding was established.

Alternative approach (b): where there are terms in law or regulation, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity

59 PP commented that this approach seems reasonably consistent with approach (d).

60 ACAG raised the following concerns with this approach:

(a) the IPSAS requirements in IPSAS 23 were not developed with similar principles to AASB 15 and the IPSAS is developing a new method for recognising revenue in the public sector; and

(b) the AASB highlighted concerns with IPSAS 23 in paragraphs BC12 to BC14 of the Basis for Conclusions accompanying AASB 1058 and considered that basing the income for NFP entities on existing IPSAS would not meet the objectives of the project.

61 At the NFP Advisory Panel virtual meeting two members selected this alternative as their preferred approach. A member commented, noting that approaches (b) and (d) were based on the IPSAS and given that these standards were developed on a similar conceptual basis, these could be viable options. They also made the comments that have been included in paragraph 15.

62 At Roundtable 1 none of the attendees selected this approach, three selected the approach at Roundtable 2 and one at Roundtable 3.

Alternative approach (c): on a systematic basis over the periods in which the entity recognises as expenses the related costs for which a grant is intended to compensate

63 This was one of PP's preferred approaches in addition to the approach (d).

64 SB commented that it would more easily enable the intended consequences of funding multi-year programs if deferral of the funding revenue was allowed to match the corresponding expenditure for the program.

65 ACAG raised the following concerns with this approach:

(a) the recognition principle used by AASB 120 is for grants that are narrow in scope and would not be suitable for the various types of grants that are received by NFP public sector entities; and

(b) the AASB already highlighted concerns with extending the scope of AASB 120 to NFP entities in paragraphs BC15 to BC17 of the Basis for Conclusion of AASB 1058.

66 HoTARAC also raised concerns about the suitability of this approach. Comments are included in paragraph 18 and 19 regarding AASB 120. They expressed that this approach departs from the Conceptual Framework and would introduce a significant element of professional judgment.

67 RSM supports an approach that is fundamentally consistent with the alternative (c) presented in ITC 50. As summarised in paragraph 17 above, in their opinion such an approach and removal of the ambiguity of determining whether sufficiently specific performance obligations exist would reduce the compliance burden of judgement on NFP entities and allow recognition policies in line with the Conceptual Framework and AASB 15 and AASB 120 as applied by FP entities.

68 Alternative (c) is also BDO's preferred approach and they commented that it will simplify accounting because:

(a) no sufficiently specific assessment will be required;

(b) entities will not have to measure progress towards satisfying specific performance obligations (over time or at a point in time);

(c) it will facilitate matching and be simpler for accounting staff to apply in practice;

(d) it will provide more relevant and reliable information to donors and other users about progress on a project/activity;

(e) it will enhance comparability between entities; and

(f) it will be consistent with the requirements in AASB 1058 for capital grants (paragraphs 15 to 17).

69 BDO also commented that by applying approach (c) to the Topic 1 PIR examples in ITC 50, the ambiguity of examples (c), (d), (e), (f) and (g) would be resolved.[18]

70 Deloitte commented that one of the merits of applying this approach not mentioned in the ITC is transaction neutrality for some industries where both FP and NFP entities operate (e.g., aged care and the education sector). However, Deloitte are not of the opinion that this would be sufficiently persuasive to merit the introduction of such an approach.

71 At the NFP Advisory Panel virtual meeting 3 members selected this as their preferred option. However, as included in paragraph 20**,** a member also commented that there have been views in the past that NFP and FP accounting need to align but they were not convinced that this is a must given there are other NFP and FP accounting differences.

72 At Roundtable 1 nine attendees selected this option, eleven at Roundtable 2 and ten at Roundtable 3. One attendee at Roundtable 1 commented that they thought approach (a), (c) and (d) are fairly aligned however approach (c) was their preference because the entity is more in control of the definition of when the money will be expended. One attendee at Roundtable 2 commented that this approach would require less resources.

73 Two attendees at an ACNC forum commented that approach (c) is the easiest approach to apply but may not be the best.

Alternative approach (d): where the outflows of resources are incurred in accordance with the requirements set out in a binding agreement

74 This was one of the two of PP's preferred approaches.

75 CAANZ and CPA, PwC and ACAG suggested the AASB monitor the developments of IPSASB's project on *Revenue without Performance Obligations* to consider whether any finalised outcomes are relevant for consideration in the longer term and consider its appropriateness for adoption in Australia.

76 ACAG further commented that if the change in the Conceptual Framework for the private sector (specifically the definition of liability)[19] is applied to the NFP and public sector (as the IPSASB is doing with their Conceptual Framework), then this is expected to require the recognition of additional obligations. Given the IPSASB approach, such obligations would appear to include obligations (under a binding agreement), to spend funds on specific projects or activities, or eligible/allowable expenditure. This approach would likely result in more grant revenue/income being recognised over time. However, ACAG acknowledged that this would still likely result in judgement being required, of how detailed the requirements in the binding agreement need to be to conclude that outflows have been incurred in accordance with those requirements to determine when to recognise the revenue/income.

77 ACAG also noted that if approach (d) is adopted it may reduce some of the burden of making complex judgements and may bring the revenue recognition closer to the matching concept. However, some jurisdictions:

(a) consider this as a step back, from the revenue recognition model in AASB 15 which is linked to the identification of sufficiently specific performance obligations; and

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18 Feedback on Topic 1: Sufficiently specific criterion will be presented in detail at a future Board meeting.

19 Staff note that IPSAB Conceptual Framework was recently revised to align with the current IASB Conceptual Framework including the definition of a liability as 'a present obligation of the entity to transfer resources as a result of past events.'

(b) will involve educating the constituents on new requirements and may involve significant time and cost.

78 HoTARAC commented that binding agreements are already addressed by AASB 1058 which benchmarks recognition for agreements, ranging from the very vague through to the very specific.

79 At the NFP Advisory Panel virtual meeting one member selected this as their preferred option. Also see paragraph 61, which notes that approaches (b) and (d) were based on the IPSAS and given that these standards were developed on a similar conceptual basis, these could be viable options.

80 At Roundtable 1 none of the attendees selected this option, two preferred this approach at Roundtable 2 and five at Roundtable 3. One attendee commented that they thought approach (a), (c) and (d) are fairly aligned.

Other approaches suggested that were not included in ITC 50

81 PP commented that if any alternative approach is selected to replace AASB 1058, there would still be a need for a clear distinction between AASB 15 and any alternative selected to replace AASB 1058. If such a distinction cannot be made clear, then PP would support creating one combined standard for NFP revenue recognition including income. Rather than wholesale changes to the standards as a result of this PIR, PP also commented that once the INPAG has been finalised, the AASB should explore the appropriateness of its adoption in full or in part in Australia for all NFP entities, including those applying Tier 1 and Tier 2 AAS. CAANZ and CPA Australia also made reference to this project and suggested it may be of assistance in this area.

82 CAANZ and CPA Australia also commented that the feedback they have received indicates that stakeholders have different views on if, and how, issues can be resolved by standard-setting given the diverse nature of circumstances, and interpretations of fact when applying the accounting requirements. Rather than amending the Standards at this time, CAANZ and CPA Australia recommend the AASB focuses on the development of the Tier 3 Standard. By providing a more suitable reporting framework for smaller NFPs they are of the view that many of the practical challenges could be minimised. Once the Tier 3 Standard has been developed and implemented, the AASB could again focus on addressing the challenges faced by Tier 1 and Tier 2 NFP entities. This would facilitate a more informed debate about the way in which the Standards can be best revised or refined. CAANZ and CPA Australia recommend that, in the interim, the AASB considers collating and presenting its guidance materials, illustrative examples, and FAQs relating to income for NFP entities in an Appendix to AASB 1058, or in a similar presentation that gives this existing guidance more authority. This will also make the guidance more readily accessible and adaptable.

What the AASB has done so far

Development of AASB 1058

83 In developing AASB 1058 the Board heard that constituents who are preparers find it difficult to discuss financial information with grantors and donors and challenging to explain why an NFP entity needed additional resources when the financial statements indicated no such need. Users noted they did not think the financial statements were reflective of the economic reality of an NFP entity's financial circumstances. Having regard to the feedback from constituents, the Board decided to undertake a project to conduct a fundamental review of the income recognition requirements applying to NFP entities.[20]

20 AASB 1058 paragraph BC4.

84 From the feedback received prior to issuing ITC 50 and from the feedback received as part of the outreach phase of this PIR (paragraphs 10 to 47), these concerns may not have been resolved. Staff note that the Board considered (paragraph BC30(e) in AASB 1058) that although the standard does not completely address concerns about the representation of NFP entity performance to users, to help manage this the Board encouraged the disclosure of information distinguishing for users amounts that are restricted in their use (but which may have been recognised as income immediately in accordance with AASB 1058).

85 Considering paragraphs BC21 to BC27 in AASB 1058 which are relevant to the feedback received as part of this PIR, about half the respondents to ED 260 *Income of Not-for-Profit Entities* explicitly considered that overall, the proposals would result in financial statements that would be useful to users. However, many respondents qualified their support that a resulting Standard would result in financial statements that would be useful to users. The main concerns raised included:

(a) the proposals would not fully resolve the dissatisfaction with existing income recognition requirements as entities would not be able to fully defer income recognition to such time as related expenses are recognised. The Board noted that responding fully to such concerns would result in liabilities being recognised inconsistent with the Conceptual Framework and that with no conceptual basis it would be difficult to distinguish which receipts should be deferred and which should not. In response, the Board decided to add disclosures encouraging entities to disclose information in the financial statements (including on the face of the financial statements) of externally imposed restrictions on an entity. The Board considered this would go some way to addressing constituent concerns that financial performance is misrepresented to users as it allows preparers to better explain their financial performance to others;

(b) the proposals were presented in an overly complicated manner, and consequently the interaction with other AAS was not necessarily clear. In response, the Board decided to redraft the pronouncements to clarify the specified requirements when finalising AASB 1058 (and AASB 2016-8), and to add further illustrative examples to illustrate the operation of the Standard, including its interaction with AASB 15 and other AAS. As part of this, the Board decided that this Standard should not address the recognition of assets.

86 AASB 1058 paragraph BC118 outlines that in developing the Standard the Board noted that constituents in local governments were particularly concerned about the implications of the revised recognition requirements to certain periodic grant funding received by these entities. The Board considered the application of the underlying principles in this Standard to such grants, and decided there was no conceptual basis for supporting an exception to the general requirements in the Standard.

Alternative approaches

Alternative approach (a): based on a common understanding between the entity and the transfer provider of the manner in which the entity is expected to use the inflows of resources

87 Staff continue to work on the development of the Tier 3 standard. At the August 2023 (M197) meeting, the Board considered the Tier 3 Exposure Draft (ED) timeline and project update. Per the proposed timeline the ED will be issued and open for comment from September 2024.

88 Staff plan to discuss the drafting of the Tier 3 income recognition requirements with the NFP Project Advisory Panel during February 2024. This will include clarifying how different revenue recognition models interact with the determination of size-based regulatory reporting requirements; definition of terms such as common understanding, the need for further guidance and illustrative examples (for example, for donations provided in response to specific campaigns and principal vs agent

considerations). It is planned that the Board will make relevant decisions relating to this at the March 2024 Board meeting.

89 It is also planned that the Board will consider proposals and feedback on financial reporting thresholds at its June 2024 meeting. This will be informed by the outcome of the staff targeted outreach and the Board's decision regarding feedback whether to specify thresholds in AAS and if so, whether within the scope paragraph of the standard or transitional provisions (with subsequent review) or provide guidance on entities most suitable to apply Tier 3 and the most appropriate form of such guidance. The scope of application of the future Tier 3 standard would also determine how many NFP private sector entities will continue to apply the Standards subject to this PIR.

Alternative approach (b): where there are terms in law or regulation, or a binding arrangement, imposed upon the use of a transferred asset by entities external to the reporting entity; and

Alternative approach (d): where the outflows of resources are incurred in accordance with the requirements set out in a binding agreement

90 As outlined in AASB 1058 paragraph BC14, the Board decided not to develop proposals for the development of AASB 1058 based on IPSAS for the following reasons:

(a) at that time, IPSAS was using an exchange/non-exchange distinction to determine the accounting for income; with non-exchange being defined similarly to non-reciprocal in AAS. The Board observed that part of the reason for undertaking the development of AASB 1058 was in response to constituent feedback of challenges in identifying a transaction as a reciprocal/non-reciprocal transaction, and concerns that the consequential accounting did not reflect the true underlying financial performance of the entity. Accordingly, the Board considered that basing its project proposals on existing IPSAS would not meet its objective in undertaking the project; and

(b) the IPSASB was developing new standards-level requirements and guidance on revenue to amend or supersede what was then in IPSAS. IPSASB was not expected to complete its project before 2019 and having regard to the effective date of AASB 15, the Board considered that it was necessary for it to develop guidance to assist NFP entities in implementing AASB 15 in advance of the IPSASB project.

91 The IPSASB has approved IPSAS 47 Revenue which will be effective for periods beginning on or after 1 January 2026. IPSAS 47 replaces the existing three revenue standards (IPSAS 9, IPSAS 11 and IPSAS 23 - proposed alternative approach (b) in ITC 50). IPSAS 47 combines ED 70 *Revenue with Performance Obligations* and ED 71 (proposed alternative approach (d) in ITC 50) into one Standard.

92 Given these developments since the issue of ITC 50, staff consider it necessary to analyse the feedback received on proposed alternative approaches (b) and (d) while considering the requirements of IPSAS 47.

93 IPSAS 47 broadens the approach in IFRS/AASB 15 to address public sector transactions. Two aspects adapted for the public sector are binding arrangements and compliance obligations:

(a) a binding arrangement is broader than a 'contract' in IFRS/AASB 15, to allow for jurisdictions where government and public sector entities cannot enter into contracts (with enforceability through legal means) but do enter into arrangements that are in substance the same as contracts (with enforceability through equivalent means). IPSAS 47 also acknowledges that public sector transactions often involve third-party beneficiaries, which can be an entity, individual or household, receiving those goods or services; and

(b) a compliance obligation is an entity's promise in a binding arrangement to either use resources internally for distinct goods or services or transfer distinct goods or services to a purchaser or third-party beneficiary. A compliance obligation in IPSAS 47 is broader than a performance obligation in IFRS/AASB 15. While both are units of account for the recognition and measurement of revenue, compliance obligations also include any:

(i) present obligations that are legally binding through equivalent means;

(ii) requirements for the entity to use resources internally for distinct goods or services; and

(iii) requirements to transfer distinct goods and services to a party other than the resource provider, such as a third-party beneficiary.

Accordingly, among other requirements, IPSAS 47 requires an entity to recognise a liability for any unsatisfied promise to use resources internally and recognise revenue only when that liability is unwound as the promise is being satisfied.

94 At its meeting in June 2023 (see IPSASB update in Agenda Paper 17.1 *Other business*), the Board noted that staff may consider IPSAS 47 to determine whether there is any useful guidance for Australian NFP entities to address the feedback arising from ITC 50. This would include considering whether and how the accounting treatment for revenue transactions prescribed in IPSAS 47:

(a) relating to revenue arising from a nonbinding arrangement aligns with AASB 1058; and

(b) relating to revenue arising from a binding arrangement aligns with IFRS 15 *Revenue from Contracts with Customers*, noting that the IPSASB replaced the IASB's concept of 'performance obligation' with the concept of 'compliance obligation'.

95 Staff noted that the Board responded to the IPSASB Exposure Drafts related to revenue and transfer expenses in October 2020. At the time, the Board had some concerns about the proposals for both revenue and transfer expenses. The Board did not express firm views on whether it agrees or disagrees with the IPSASB' proposals on revenue because it would have been premature to form views prior to this Board's PIR being performed.

Alternative approach (c): on a systematic basis over the periods in which the entity recognises as expenses the related costs for which a grant is intended to compensate

96 As outlined in the Basis for Conclusions of AASB 1058, the Board considered extending the scope of AASB 120 to NFP entities would allow government grants to be accounted for under a strict transaction-neutral approach however the Board was reluctant to do so.[21] For example, because of the limited scope of transfers addressed by AASB 120 compared to the varied transfers received by a NFP entity and the application of the recognition and presentation requirements in AASB 120 could result in an entity's assets being materially understated.

97 The Board observed that extending the application of requirements in AASB 120 to all transfers of an NFP entity would require an NFP entity to defer income recognition for every form of transfer until there is reasonable assurance that the entity will comply with any conditions attached to the transfer. AASB 120 does not define 'conditions', and consequently, the Board was concerned there would be inconsistency in application of the requirements. The Board also considered it unclear whether the 'conditions' of some transfers, for example, an endowment that must be used to provide an annual

[21] See AASB 1058 BC15 to BC17

scholarship, could ever be said to be met. Accordingly, the Board was not convinced that developing proposals based on AASB 120 would achieve its objectives in undertaking this project.

98 In addition, the Board discussed recent international developments for the recognition of income, and noted AASB 120 was less consistent with current conceptual thinking (compared to AASB 15) as it does not articulate the nature of obligations giving rise to a liability rather than income, or when these obligations can be said to have been satisfied. The Board observed that the principles in IAS 20 had not been reconsidered fully at the time of issue of IFRS 15. However, the IASB considered the approach in IAS 20 when developing the *IFRS for SMEs* Standard. The IASB ultimately decided to adopt an approach that refers to the recognition of income when performance conditions are satisfied. This approach may be considered to be similar to the IFRS 15 performance obligation approach. Further, the Board observed that the IASB had no current plans to review IAS 20. Having regard to the significance of grants, taxes, donations and similar transfers to the income of an NFP entity, the Board decided to confirm again its 2004 decision not to extend AASB 120 to apply also to NFP entities.

99 Staff note that the IASB considered the financial reporting issues that could be added to the Board's work plan in the Request for Information *Third Agenda Consultation*, which included IAS 20. The feedback received by stakeholders was considered by the IASB at its November 2021 meeting. Many respondents rated it as a low priority project. At its March 2022 meeting, it was considered as a potential project however the IASB decided it should not be included on the shortlist for discussion at a future meeting.[22]

Other approaches suggested that were not included in ITC 50

IFR4NPO International Financial Reporting for Non Profit Organisations

100 At its June 2023 meeting, the IFR4NPO Technical Advisory Group discussed the final amendments to the INPAG draft content of Exposure Draft 2 for Revenue (and other items). It is expected that revenue requirements (Section 23) will contain two parts. Part I would cover grants and donations, and will be based on IPSAS 47 *Revenue* and Part II would cover contracts with customers, and be based on the Exposure Draft of the revised Section 23 in the *IFRS for SMEs* Accounting Standard. Both IPSAS 47 and the *IFRS for SMEs* Accounting Standard Exposure Draft incorporated the principles of IFRS 15. Some of the departures from the terminology used in IPSAS 47 are:

(a) The term enforceable grant arrangement has been introduced to replace binding grant arrangements. Enforceable grant arrangement is a grant arrangement that confers both rights and obligations, enforceable through legal and equivalent means, on both the parties to the grant arrangement.

(b) Enforceable grant obligations replace compliance obligations including expanding the concept to include an undertaking by the grant recipient to achieve a specific outcome in addition to the delivery of activities and the internal use or external transfer of distinct services, goods and other assets.

(c) Funding agreement has been defined as an arrangement with an NPO that is not enforceable through legal or equivalent means and does not give both parties rights and includes situations where grant-provider transfers resources to a grant recipient without there being any agreed or implied arrangement in place.

22 IASB Update March 2022. See also *Third Agenda Consultation Feedback Statement*.

(d) Constraint has been referred to as the requirement placed on the grant recipient as to how it uses resources.

101 The INPAG Exposure Draft 2 is expected to be released in September 2023. Staff also note that the INPAG proposals regarding presentation of restricted and unrestricted income, fund accounting and supplementary statement may be useful in informing the AASB whether and how to further improve the revenue and income disclosures of NFP entities.

August 2022 AASB meeting

102 At its August 2022 meeting, the Board decided to consider this topic during this PIR and noted that there were no outputs to date relating to this topic.

IFRS (AASB) 15 Revenue from Contracts with Customers post-implementation review

103 The IASB has issued the Request for Information (RFI) as part of the IFRS 15 PIR and it has been issued by the AASB as ITC 53 *Request for Comment on IASB Request for Information on Post-implementation Review of IFRS 15* Revenue from Contracts with Customers. The Australian comment period closes on 8 September 2023 with all comments to be received by the IASB by 27 October 2023.

104 The IFRS 15 PIR requests feedback on sections that may impact the topics included in ITC 50 including identifying performance obligations in a contract, determining when to recognise revenue over time and principal versus agent.

105 At the time of writing this paper, AASB staff are holding stakeholder meetings to obtain Australian-specific feedback. It is planned that staff will present the draft comment letter to the Board at its October 2023 meeting.

106 The IASB has indicated the RFI feedback will be due in H1 of 2024 on its work plan. Staff will monitor the feedback and outcomes of the IFRS 15 PIR and assess the impact of any changes on NFP entity accounting.

Relevant research

107 Staff performed a literature review on the topics to be considered as part of the PIR process.[23] Key implementation issues noted in academic and non-academic research relevant to this topic included:

(a) income recognition is complex (Gilchrist, West and Zhang 2023),[24] and there is often a mismatch between when cash is received, income is recognised, and expenses are incurred.[25] The mismatch often makes explaining a NFP entity's result to stakeholders challenging;

(b) recognition of grant funding can be challenging;[26] and

(c) inconsistent outcomes have led to increased costs by preparers, their accountants and auditors.[27]

23 See *Agenda Item 9.3 NFP domestic PIRs – academic and non-academic literature reviews.*

24 See note 2.

25 See https://intheblack.cpaaustralia.com.au/accounting/nfp-accounting-revenue-income

26 For example, https://www.charteredaccountantsanz.com/news-and-analysis/insights/perspective-articles/insights-from-the-implementation-of-aasb-1058

27 For example, https://www.pitcher.com.au/insights/ongoing-issues-with-income-recognition-for-nfp-entities/

108 Staff have been monitoring if there are any publications related to the topic and are not aware of any other recent publications.

Staff analysis and preliminary views

109 The table includes staff analysis of the feedback received, preliminary views on whether any action may be required to address the feedback and what may be done to respond to it. Following the Board's consideration and acceptance of the PIR framework[28] to support an objective and consistent decision-making process at this meeting and the Board discussion and feedback as part of this topic, staff plan to formalise the recommendations on the next steps including consideration of the magnitude of the issues identified, likely timeframe of possible actions, and their expected benefits and associated costs and present them to the Board at a future meeting.

Feedback themes/areas	Staff analysis and preliminary views
Challenges with the accounting requirements of AASB 15 and AASB 1058	110 Staff acknowledge the concerns from those stakeholders that commented on this aspect that the interaction between AASB 15 and AASB 1058 is not easy to navigate and the level of judgement applied may be disproportionate for some, especially smaller, NFP entities. These stakeholders also confirmed the diversity in practice, especially regarding the timing of the revenue recognition outcomes. 111 However, staff also noted views that some of these issues may be due to the transition period and may abate over time. Further, some stakeholders confirmed that the principles-based approach is preferred. Staff also note that other areas, such as sufficiently specific criterion will be analysed in separate Staff Papers, to be presented at future meetings. 112 Staff's preliminary view is that for the reasons the Board noted in the Bases for Conclusion in AASB 15 and AASB 1058 including application of the transaction neutrality principle in conjunction with the need to provide specific requirements and guidance in Appendix F to AASB 15 and AASB 1058 to reflect NFP circumstances, it appears that subject to targeted improvements of some areas noted below and other specific topics in the scope of ITC 50, it is not necessary to restructure the two standards, however, further application guidance and clarification may be necessary to improve the application of the Standards by NFP entities.
Support for a principles-based approach	113 Staff noted strong support for continuing with the principles-based approach from those stakeholders commenting on the matter, also noting that some of these respondents did not recommend to completely overhaul the requirements. 114 However, as also noted below, several stakeholders requested consideration of other approaches to revenue recognition, such as the AASB 120, IPSAS 47 or INPAG future requirements. 115 Staff's preliminary view is that, if the Board decides to address the feedback on this topic through either standard-setting or a research project, it would not necessarily require the complete restructure of existing guidance, however, specific amendments to either AASB 15 or AASB 1058 could be investigated to reflect better (if determined necessary) NFP agreements and the needs of users.
Inconsistency with AASB 120 for-profit accounting requirements	116 Some stakeholders considered that alignment with AASB 120 should be considered, noting that it would ensure consistency with accounting for government grants by NFP entities. Some other feedback noted that this would achieve better matching of revenue with related expenses resulting in outcomes that users understand more. 117 On the other hand, other stakeholders noted that AASB 120 is not in line with the current Conceptual Framework. AASB noted this in paragraphs BC15 to BC17 accompanying AASB 1058, as well as the scope of AASB 120 being limited compared to AASB 1058. The AASB also noted when developing AASB 1058 that there could be interpretation challenges. For example, how to interpret the requirement to have reasonable assurance to comply with the transfer conditions for the income to be recognised in relation to the transfer.

28 Refer to Agenda Paper 3.1.

Feedback themes/areas	Staff analysis and preliminary views
	118 Staff note that some of the respondents to the IASB *Third Agenda Consultation* said that IAS 20 is not consistent with the most recent accounting standards and Conceptual Framework and the accounting choices in IAS 20 may resulted in a lack of comparability. Despite the feedback, the IASB did not add the project to its work plan after consideration of the relevant criteria. 119 Staff note that if the Board decide to add or amend the revenue recognition criteria in AASB 15 or AASB 1058, more recent thinking would be available as a potential source including either from IPSAS 47 or future INPAG requirements.
Upfront income recognition	120 One of the most cited issues with the revenue recognition requirements (also mentioned in other aspects of the feedback such as sufficient specific criterion and termination for convenience clauses (both to be considered by the Board at a future meeting) was the upfront recognition of revenue that was considered as inappropriately reflecting the circumstances of the funding arrangements and not understood by the users, especially for the grants and transfers in relation to the activities and expenses expected to be incurred over multiple reporting periods without sufficiently specific performance obligations being identified. 121 On the other hand, staff noted that some other stakeholders commented that existing revenue recognition criteria are mostly consistent with the Conceptual Framework and other AAS and that the preference for the revenue to be matched with the related expenses may also be (at least partially) addressed by the on-going education of the sector on the key accounting principles and for smaller NFP entities, the issue may be addressed by the Tier 3 requirements that the AASB is currently developing. 122 Some stakeholders also recommended to consider the abovementioned international standard-setting projects (IPSAS 47 and INPAG) if the AASB decide to amend the recognition principles beyond the separately identifiable distinct performance obligations in AASB 15 and the residual nature of AASB 1058. However, some of these stakeholders commented that this should be considered carefully and over the longer-term horizon.
Management and statutory accounting records	123 Many stakeholders commented that the complexity of application of the sufficiently specific criterion along with the preference at least by some preparers and users to match revenue with expenses resulted in the practice of supplementing financial statements with management reporting. 124 Some stakeholders noted that the need for this may decrease over time as preparers and users improve their understanding of the Standards. As discussed above, some stakeholders noted the consistency of the existing requirements with the Conceptual Framework and AAS as well as the need to apply the concept of performance obligations consistently with the emphasis on the ability to allocate transaction price to when the promised goods or services are transferred. 125 Staff's preliminary view is that whilst it is not desirable to have the widespread practice of preparing management reporting if the Standards are not perceived to result in understandable outcomes, it is unlikely that any changes to the Standards will remove the need to explain the outcomes completely unless the Board implement the matching principle similar to the one in AASB 120 discussed above. 126 Staff's preliminary view is that further guidance on the sufficiently specific criterion in AASB 15, to be considered by the Board at a future meeting, may go some way in addressing this issue, however, the Board could reconsider the residual' nature of AASB 1058 by leveraging the latest international guidance. However, staff note that the Board noted (paragraph BC30(e)) that although AASB 1058 does not completely address concerns about the representation of NFP entity performance to users, to help manage this the Board encouraged the disclosure of information distinguishing for users amounts that are restricted in their use (but which may have been recognised as income immediately in accordance with AASB 1058). The Board considered that, as there is no contractual liability, the entity has the ability to use the assets acquired in alternative ways if that best reflects the needs of the entity, although the entity may currently have every intention of continuing to use the assets acquired in a designated way.

Feedback themes/areas	Staff analysis and preliminary views
Preference for 'matching' income with expenses	127 Some stakeholders specifically commented on the matching concept, a few noting preference for such concept by preparers and users and that NFP entities should have flexibility to recognise revenue progressively as the funds are being spent which also aligns with the expectations and understanding of the users. 128 On the other hand, several stakeholders noted the conceptual soundness of current requirements and noted that AASB 120, whilst in some cases could result in better alignment of revenue with expenses, is not in line with the latest conceptual thinking and recent AAS. 129 However, given international standard setters have recently extended (or are proposing to extend) the revenue recognition beyond the concept of performance obligations (i.e. IPSASB in IPSAS 47 through the concept of compliance obligation and IFR4NPO in INPAG forthcoming Exposure Draft through the concept of enforceable grant obligation), the AASB could consider whether such concepts could be incorporated, for example, into AASB 1058.
Disclosures as a possible solution	130 Several stakeholders recommended that further and improved disclosures could help to address the needs of the users whilst maintaining the conceptual alignment of the revenue recognition requirements in the Standards. 131 Staff noted that the comments regarding the restrictions of the funds and special purpose reserves in equity are in line with the existing disclosure requirements (albeit in some cases voluntary, such as paragraph 37 in AASB 1058) encouraging an entity to disclose information about externally imposed restrictions that limit or direct the purpose for which resources controlled by the entity may be used. 132 Staff also note that INPAG is likely to contain guidance on presentation and disclosure in relation to the terms and conditions of the revenue transactions, including enforceable grant obligations, revenue with and without restrictions as part of fund accounting requirements as well as guidance on Supplementary Statements that aim to present financial information on a specific grant. Proposals on fund accounting and supplementary statements are expected to be published as part of ED 3 in April 2024. The feedback on the proposals could be useful input for the Board to consider if and when considering how to address the feedback on ITC 50. Staff note that the decision about how grant conditions are treated, whether they have been fulfilled and how they affect revenue recognition will likely require judgment regardless of the revenue recognition model.
Measures already taken by the AASB and possible future measures	133 From the summary of feedback, the following recommendations have been made by respondents: (a) disclosures as a solution (paragraphs 35 to 42), for example mandate AASB 1058 voluntary disclosure requirements for reserved funds; (b) develop a plain English guide with the ACNC (paragraph 44); (c) provide additional illustrative examples (paragraph 45); (d) more education or flowcharts, making guidance more accessible (including combining it into one place) including the guidance clarifying distinction between AASB 15 and AASB 1058 requirements (paragraphs 44 and 81 to 82); and (e) adoption of an alternative approach (paragraphs 48 to 80). 134 Staff have noted that whilst some stakeholders noted the opportunity to consolidate existing guidance and staff educational material into the Standards and that further illustrative examples would help with the application of the Standards, many stakeholders did not recommend wholesale changes of the standards and the underlying approach, not at least at this time. Some stakeholders also recommend the Board to focus on current priorities, namely finalisation of the Tier 3 Standard for NFP entities before considering any significant changes to AASB 15 and AASB 1058. 135 Staff's preliminary view is that whilst the objectives of the Standards were met at least to a significant degree (noting that the Board acknowledged that AASB 1058 will not completely address all stakeholder concerns), the feedback indicates that the benefits to users may be lower than expected when compared to the effort and cost of application for preparers. 136 However, staff also noted mixed views from stakeholders on the possible approaches about how to address the implementation issues summarised in this paper. Some of the approaches

Feedback themes/areas	Staff analysis and preliminary views
	would have the benefit of being closer to current Conceptual Framework, whilst some may be perceived easier to implement and could be easier to understand by the users. Albeit the range of the alternative approaches that could be considered is relatively wide, the most concerns appear to be centred around the issue that the combination of the sufficiently specific criterion in AASB 15 and the residual nature of AASB 1058 does not enable entities to provide useful financial information about the grants provided against identifiable enforceable grant obligations. Staff note that if not all, some of these concerns may be addressed through the further improvement of the guidance on the sufficiently specific criterion in AASB 15 (to be considered by the Board at a future meeting). 137 Staff consider there is merit to explore the alternative approaches and how they could be leveraged off to further improve the application of AASB 15 and AASB 1058. However, staff's preliminary view is that any standard-setting will need to be carefully considered to avoid unnecessary disruption of existing practice and thus additional implementation costs relatively shortly after the Standards were implemented. 138 Staff also note that the Board acknowledged when developing AASB 1058 that it would consider a project to review the accounting specified by AASB 1058 following the completion of the IPSAS Revenue project. Staff's preliminary view is that the Board could consider a research project to explore potential amendments to the Standards leveraging off latest international standard-setting projects in this area such as IPSAS 47 and INPAG, including examining their compatibility with the Conceptual Framework applicable to NFP entities (including any anticipated changes from the AASB NFP Conceptual Framework project). This would include cost/benefit considerations as any approach would require a certain degree of the application of judgement to assess whether requirements for revenue recognition were satisfied.

Question to Board members

Q1: Do Board members have any questions or comments on the feedback, staff analysis or preliminary views on this topic?