Not-for-Profit Financial Reporting Framework Project

Agenda Paper 8.2
Preliminary summary feedback from outreach conducted up to 31 January 2023

AASB M194 Board meeting 2023

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Australian Accounting Standards Board

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Purpose of this paper

- AASB published the Discussion Paper *Development of simplified accounting requirements (Tier 3 Not-for-Profit Private Sector Entities)* (DP) in September 2022 with a 6-month consultation period until 31 March 2023. The DP includes the Board's proposals to develop:
  - a third reporting tier of simplified accounting requirements for smaller NFP entities; and
  - remove the ability to prepare special purpose financial statements by NFP entities.

- Consistent with the outreach plan presented to the Board at its August 2022 (M189) meeting, staff conducted various outreach activities to support the DP including:
  - Online survey;*
  - Virtual outreach sessions;
  - Further stakeholder engagement (these include one on one meetings with individual preparers, regulators and members of accounting professional bodies)

- The purpose of this paper is to summarise the preliminary feedback from outreach activities up to 31 January 2023 for information purposes only and staff do not ask the Board to make any decisions.

- However, Board members' initial thoughts and reactions on any of the material in this Paper would be welcome.

* The survey replicated the questions in the DP except for:
  - Q3 relating to objective and primary users of the *Framework for the Preparation of Financial Statements.* Staff considered stakeholders responding may not adequately understand the current requirements to provide a meaningful response;
  - Q47 – Q49 relating to examples of disclosure requirements for three topics based on the proposed disclosure approach – staff omitted these questions because of the number of questions already included and in keeping with making the survey as simple and user-friendly as possible.
  - Q6 relates to whether to introduce Tier 3 for smaller-sized NFP entities with less complex transactions and Q31 proposed to not include biological assets and agricultural produce at the point of harvest as part of a Tier 3 Standard. Staff considered these questions have already been covered by other questions in the survey.

Overview of outreach conducted up to 31 January 2023

Outreach activity	Number of attendees	Profile of attendees (where identifiable)	Objective of outreach activities
Online Survey	188	• 127 Auditors (68%) • 48 Preparers (26%) • 7 Users (4%) • 5 Other – advisors, a director and mixed (3%) • 1 regulator (1%)	To provide an opportunity to stakeholders who do not have the capacity to submit a comment letter.
5 Virtual outreach sessions	166	Mixed of stakeholders	To provide an opportunity to stakeholders who do not have the capacity to submit a comment letter. The virtual sessions only covered certain questions in the DP due to the limited time allocated per session.
5 Virtual meeting with accounting body NFP committees	47	Mixed of stakeholders	To raise awareness and promote the DP and obtain any initial thoughts
One-to-one individual meetings	6	Preparers	To gather any additional feedback from stakeholders attending virtual sessions
	24	Staff of various regulators	To gather preliminary views on proposals in DP

Outreach activities not included/yet to occur:

February and March 2023 virtual outreach session.

Survey and written submissions received before the end of the comment period.

Contents

- Overall summary (slide 5 – 7)
- Detailed summary of responses for topics with the support rate from the stakeholders below 90% (i.e. less that "almost all agree") relating to the:
  - operationalisation of the proposed Tier 3 Standard (slide 8 – 11); and
  - proposed accounting requirements for topics proposed in DP (slide 12 – 22)
- Staff have applied the following terms to reflect the feedback by percentages of those that agreed to the question from the online survey, virtual outreach and one-to-one meetings.

Term	Extent of response among respondents
Almost all	All except a very small minority (90% or over)
Most	A large majority, with more than a few exceptions (71%-89%)
Many	A small majority or large minority (31%-70%)
Some	A small minority, but more than a few (11%-30%)
A few	A very small minority (10% or less)

Overall summary - Operationalisation of the proposed Tier 3

	Question/Topic from the DP	Agree	Disagree or other
	Q1) Not establishing reporting thresholds within the Australian Accounting Standards	86%	14%
	Q2) Addressing service performance reporting as a separate project	97%	3%
	Q4) Timing of the proposals	93%	7%
	Q5) Extending the Australian Accounting Standards applicable to certain NFP entities*	81%	19%
	Q7) Not developing fourth reporting tier	93%	7%
	Q8) Not change the existing Tier 1 or Tier 2 Australian Accounting Standards	94%	6%
	Q9) Stand-alone standard	96%	4%
	Q10) Opt-up as free choice*	59%	41%
	Q11) Items excluded from Tier 3	87%	13%
	Q12) Hierarchy approach	99%	1%
	Q13) Maintenance cycle	97%	3%

Legend:

Almost all	All except a very small minority (90% or over)
Most	A large majority, with more than a few exceptions (71%-89%)
Many	A small majority or large minority (31%-70%)

Note:
1) The questions to topics that staff consulted at the virtual outreach sessions are marked by *.
2) As noted in slide 2, Q3 of the DP was not included in the online survey.

Overall summary – proposed Tier 3 accounting requirements for key topics

	Question/Topic from the DP	Agree	Disagree	Not applicable
	Q14a & Q15 – Q16) Primary financial statements including presentation*	84%	16%	-
	Q14b) Statement of changes in equity*	57%	42%	1%
	Q17) Consolidation of subsidiaries *	71%	12%	17%
	Q18) Separate financial statements	79%	10%	11%
	Q19 & Q20) Changes in accounting policies and correction of prior period errors	90%	10%	
	Q21) Develop simplified accounting for financial instruments that are common to smaller NFP entities.	97%	-	3%
	Q21) Examples of 'more complex' or uncommon financial instruments *	92%	8%	-
	Q22 – Q27) Accounting for basic financial instruments	88%	11%	-
	Q28) Fair value measurement	95%	2%	3%
	Q29) Cost appropriate for fair value of unlisted share investment	87%	7%	6%
	Q30) Inventory	93%	1%	6%

Note: 1) The questions to topics that staff consulted at the virtual outreach sessions are marked by *.

Almost all	All except a very small minority (90% or over)
Most	A large majority, with more than a few exceptions (71%-89%)
Many	A small majority or large minority (31%-70%)

Overall summary – proposed Tier 3 accounting requirements for key topics

Question/Topic from the DP	Agree	Disagree	Not applicable
Q32 & Q33) Investment in associates and joint ventures	79%	3%	18%
Q34) Property, plant and equipment	94%	4%)	2%
Q35) Initially measurement of non-financial assets acquired at significantly less than fair value*	77%	19%	5%
Q36) Volunteer services	79%	19%	2%
Q37) Borrowing costs	94%	3%	3%
Q38) Impairment of non-financial assets*	90%	6%	4%
Q39) Assets held for sale	92%	2%	5%
Q40) Existence of intangible assets commonly held and recognised*	50%	50%	-
Q41) Leases*	89%	7%	4%
Q42) Income recognition model *	94%	%	1%
Q43 & Q44) Employee benefits (not developing special requirements for termination benefits and defined benefit plans)	93%	6%	1%
Q45) Other topics to apply NZ approach	90%	2%	8%
Q46) Disclosure approach	97%	3%	-

Note: 1) The questions to topics that staff consulted at the virtual outreach sessions are marked by *.
2) As noted in slide 2, Q31 and Q47-Q49 were not included in the online survey.

Almost all	All except a very small minority (90% or over)
Most	A large majority, with more than a few exceptions (71%-89%)
Many	A small majority or large minority (31%-70%)

Operationalisation of Proposed Tier 3 – Not establishing reporting thresholds within the Australian Accounting Standards

	Yes		No	
Q1 of DP. Not establishing the reporting thresholds within the Australian Accounting Standards	Respondents	%	Respondents	%
	105	86	17	14

Arguments supporting proposal

- Specifying thresholds in Australian Accounting Standards could increase complexity and become incompatible with other regulatory requirements if they were to change
- Need to continue discussions among regulators to ensure that consistency is applied

Concerns

- It will increase judgment when determining the type of financial statements to prepare. However, some guidance on which entities should apply the Tier 3 Standard may be helpful
- Tier 3 should only be applied by smaller entities and linked to the ACNC thresholds
- NFP entities with revenue up to $5 M would still be considered small NFP
- Tier 3 should be applicable to all NFP entities

Operationalisation of Proposed Tier 3 – Extending the Australian Accounting Standards applicable to certain NFP entities

Q5 of DP. Extend the set of not-for-profit private sector entities to which Australian Accounting Standards apply by superseding (in part) SAC 1	Yes		No	
	Respondents	%	Respondents	%
	118	81	28	19

Arguments supporting proposal

- Consistency and comparability are important by NFP entities.
- Make Tier 3 Standard available before extending the Australian Accounting Standards to broader NFP entities

Concerns

- General purpose financial statements comes with real cost impact and does not, in the main, provide any significant advantage
- Many smaller NFP entities may still find Tier 3 reporting requirements hard to apply

Operationalisation of Proposed Tier 3 – Opt-up policy

Q10 of DP. Opt-up policy on whether to allow Tier 3 entities to opt up to Tier 1 or Tier 2 reporting requirements for: • all transactions; or • for transactions specifically permitted by the Board only; or • not permit any opt-up*	Free choice to opt-up		Opt-up only when permitted by the Board		Opt-up not permitted	
	Respondents	%	Respondents	%	Respondents	%
	120	59	17	8	65	32

Arguments supporting free choice to opt up

- Provide flexibility to choose an accounting policy that the entity considers would provide appropriate information to users and meets various needs of regulators
- Entities may cross arbitrary revenue thresholds and applying Tier 1 or Tier 2 in its entirety only would increase additional cost and reduce consistency between accounting periods

Concerns

- There is a lack of understanding when electing which accounting policy to apply and entities often rely on the auditors. Hence, limited choices would be easier and limits errors and uncertainties, and also enhances comparability in financial reporting;
- Offering choices on policy by policy basis will revert back to SPFS and create disparity and confusion to users of the financial statements

Operationalisation of Proposed Tier 3 – Items excluded from Tier 3

Q11 of DP. The types of items the Board intends to scope out from the Tier 3 Standard including: a) Biological assets b) Insurance contracts issued; c) Expenditure incurrent in connection with exploration for and evaluation of mineral resources; d) Business combination; e) Obligations arising under a defined benefit superannuation plan; f) Share-based payment arrangements; g) Service concession arrangements; and h) Complex financial instruments	Yes		No	
	Respondents	%	Respondents	%
	202	87	31	13

Arguments supporting proposal

- Have not come across any of the above in over 20 years in the NPO sector.

Concerns

- Guidance for business combination should be developed because of the increasing trend for NFP entities, including smaller entities, to merge or acquire other entities.

Proposed Tier 3 accounting requirements for key topics – Primary financial statements including presentation

Q14a & Q15 – Q16 of DP. Tier 3 general purpose financial statements comprise:	Yes		No	
	Respondents	%	Respondents	%
a) a statement of profit and loss and other comprehensive income and a statement of financial position and presentation requirements consistent with AASB 1060; b) a statement of cash flows presenting operating activities using the direct method and no requirement to separately present investing from financing activities; and c) explanatory notes.	113	84	22	16

Arguments supporting proposal

- Agree but tailor the name of the statements and language to NFP (e.g. Statement of Comprehensive Income, reference to surplus/deficit vs profit/loss)
- While supporting proposals, not requiring the cash flows of financing and investing activities separately does not provide much simplification given entities are already require to present these activities separately and it may be useful to users

Concerns

- The statement of cash flows should also not be required because that statement is challenging for smaller NFP entities to prepare. Board/management may not understand the information presented in the statement

Proposed Tier 3 accounting requirements for key topics – Statement of changes in equity

Q14b of DP. Do you think the statement of changes in equity should also form part of the Tier 3 general purpose financial statements. Should they be required as part of notes to the financial statements?	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	112	57	82	42	3	1

Arguments supporting proposal

- Statement remains useful - NFP entities often have reserves (including restricted reserves or revaluation reserves or private ancillary funds with gift funds for donations received) and show changes in equity, particularly to grantors/donors that resources are set aside for future projects
- The statement is often generated by accounting software and would not require additional resources
- A useful tool to identify errors when journaling retained earnings

Concerns

- The only movement in equity for the year for smaller NFP entities is their profit or loss hence it the statement does not add any additional value to users
- Apply the same requirements as AASB 1060 the statement is required only conditionally, such as movements in reserves, as per the Tier 2 reporting requirement
- If in the notes, it should be mandatory

Proposed Tier 3 accounting requirements for key topics – Consolidation of subsidiaries

Q17 of DP. Do you agree an entity should be allow to present either (a) Separate financial statement as its only financial statements with disclosures of information on the parent's significant relationships; or (b) Consolidated financial statements in accordance with AASB 10?	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	157	71	27	12	37	17

Arguments supporting proposal

- Information provided in a consolidated financial statements where entities have mixed purposes may not be useful especially where users may be interested in the information at the individual entity's level.
- Sufficient disclosures should accompany separate financial statements about controlled entities to provide users with information on the total exposure of the whole entity

Concerns

- Consolidated financial statements are important in providing transparency to users
- Those charged with governance need to see what entities they control. Allowing an accounting policy choice is carrying on special purpose reporting and detracts from the overall purpose of the reporting framework

Proposed Tier 3 accounting requirements for key topics – Separate financial statements

Q18 of DP. A parent that presents separate financial statements measure its interest in subsidiaries either: (a) at cost; (b) at fair value through other comprehensive income; or (c) using the equity method of accounting.	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	104	79	13	10	14	11

Arguments supporting proposal

- Agree, an entity can elect an appropriate method supported by disclosures

Concerns

- If an NFP entity have subsidiaries, it would appear to be a more complex entity and be required to comply with the current requirements
- Too many choices provided and noted the need for a consistent approach for simplicity
- The equity method of accounting should not be an appropriate measurement method given it is not provided by the current IFRS requirements

Proposed Tier 3 accounting requirements for key topics – accounting for basic financial instruments

Q22 - Q27 of DP. Tier 3 accounting for basic financial instruments	Yes		No	
	Respondents	%	Respondents	%
	219	88	28	11

Arguments supporting proposal

- Reasonable proposal
- Subsequent measurement of financial assets held for capital return and investment at fair value through OCI prevents fluctuations in profit for the year and some funding agreement requires test to profit thresholds and avoids volatility in the profit or loss

Concerns

- Mixed views for subsequent measurement of financial assets held for capital return as:
  - Fair value through other comprehensive income (OCI):
    - prevents fluctuations in profit for the year and some funding agreement requires test to profit thresholds
    - is management's preference to separate fair value gains/losses from entity's standard operations
  - Fair value through profit or loss:
    - is a simpler option. Preparers and users lack an understanding of what OCI is. Segmenting between operating and non-operating profits may help to separate these gains from the entity's normal operation

Proposed Tier 3 accounting requirements for key topics – cost as an appropriate measure for fair value of unlisted share investment

Q29 of DP. Cost may be an appropriate estimate for fair value when cost represents the best estimates of fair value within a wide range of possible fair value measurements for unlisted share investments	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	109	87	9	7	7	6

Arguments supporting proposal

- Appropriate measure as long as the disclosure of cost as measure and consideration of impairment remains.

Concerns

- Fair value would be a fairer representation of the investments
- The valuation will depend if the shares were purchased from a related party or under special consideration.
- If cost is an option then it should be cost less any impairment. There is a tendency for NFPs to not assess valuations of unlisted investments when they are held at cost and where investments should be impaired as they sustained heavy losses and have cash flow issues.

Proposed Tier 3 accounting requirements for key topics – investment in associates and joint ventures

Q32 & Q33 of DP. Accounting for investment in associates and joint ventures: (a) For parent entity preparing consolidated financial statements: equity method (b) For parent entity preparing separate financial statements: cost or FVTOCI (c) For investors preparing equity accounted financial statements: cost or FVTOCI	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	97	79	4	3	22	18

Arguments supporting proposal

- Agree but entities with investment in associates and joint ventures may be consider complex, therefore whether existing requirements is applicable for consistency with other entities

Concerns

- Measuring interest in associates and joint ventures at cost is preferred rather than allowing for optionality
- Parent entity preparing separate financial statements should measure interest in associates and joint ventures using the equity method

Proposed Tier 3 accounting requirements for key topics – Initial measurement of non-financial assets at significantly less than fair value at cost or at fair value

Q35 of DP. Accounting policy choice for initial measurement of non-financial assets acquired for significantly less than fair value: a) inventory to be measured at cost or at current replacement cost; and b) other non-financial assets to be measured at cost or at fair value. Not permitted to subsequent apply the revaluation or fair value model if the donated non-financial asset were initially measured at cost.	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	167	77	41	19	10	5

Arguments supporting proposal

- Provides flexibility and calculating fair value can be costly for NFP entities but disclosure is necessary

Concerns

- Disagree with not allowing the subsequent revaluation of non-financial assets. Organisation needs and circumstances may change especially if appropriate and independent evidence is able to support the change in accounting policy that depicts a 'true view'
- Accounting choice reduces comparability
- Allowing significant donated non-financial assets to be measured at cost with no value in balance sheet can be problematic

Proposed Tier 3 accounting requirements for key topics – Volunteer services

Q36 of DP. Permit, but not require, a smaller not-for-profit entity to recognise volunteer services received, or a class of volunteer services, if the fair value of those services can be measured reliably	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	100	79	24	19	3	2

Arguments supporting proposal

- provide an option allows entities that have the resources, to recognise and provide information about volunteer services

Concerns

- Volunteer services should not be recognised in the income statement due to the complexity to measure the fair value of volunteer services reliably especially for smaller entities
- Substantiation would be difficult due to the subjectivity in measuring volunteer services
- Volunteer services should be disclosed in the notes to the financial statements

Proposed Tier 3 accounting requirements for key topics – Existence of intangible assets commonly held and recognised by smaller NFP entities

Q40 of DP. Are you aware of any intangible assets and their type, either internally generated or externally acquired, commonly held and recognised by smaller not-for-profit private sector entities?	Yes		No	
	Respondents	%	Respondents	%
	112	50	113	50

Yes

- Software is the most common type of intangible assets
- Other intangible assets noted were goodwill and trademarks

No

- Most don't have intangibles either because it's not material or not common for smaller entities.

Proposed Tier 2 accounting requirements for key topics – Leases

Q41 of DP. Recognise lease payments as an expense on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern of the user's benefit. Similar requirements apply for lessors. Concessionary lease arrangements are accounted for in the same manner as other leases.	Yes		No		N/A	
	Respondents	%	Respondents	%	Respondents	%
	188	89	15	7	8	4

Arguments supporting proposal

- Current requirements confusing to many smaller NFPs
- Financial statements would be much more user friendly and additional information on key leases can be provided as a narrative in the notes

Concerns

- NFPs had only recently transitioned to adopt AASB 16, as such, transitional issues would need to be considered
- AASB 16 should apply for all NFP entities for consistency and comparability or the entity should be able to apply AASB 16 if the entity considers it appropriate
- Not requiring the right of use assets does not reflect the true value of running the organisation
- It may lead to NFP over committing to lease items

Question 1 to the Board

Do Board members have any questions or comments on the feedback received to date?