Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Not-for-Profit Private Sector Financial Reporting Framework**	**Meeting:**	M187
Topic:	**Tier 3 – Revenue/Income – requiring assessment of 'sufficiently specific' criteria**	**Agenda Item:**	5.1.2
		Date:	2 May 2022
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		Decision-Making:	High
		Project Status:	Initial deliberations

The objective of this paper

1 The objective of this staff paper is for the Board to **decide** its preliminary views, for the purpose of the discussion paper (DP), on Tier 3 reporting requirements for not-for-profit (NFP) private sector entities whether to require the assessment of 'sufficiently specific' requirements for accounting of inflows of resources with performance obligations. This paper is only relevant if the Board decides to require the distinction of inflows of resources in Agenda Paper 5.1.1.

2 Agenda Paper 5.1.3 presents six high-level scenarios to provide a comparison of the outcomes of the income recognition options presented in this staff paper and Agenda Paper 5.1.1.

Structure of this staff paper

3 This paper is structured as follows:

(a) Summary of staff recommendations (paragraph 4);

Considering options for simplifications and staff analysis and recommendations

(b) Simplification of options for Tier 3 income recognition model flowchart (**Figure 1** and paragraphs 5 – 7);

(i) Should entities be required to assess 'sufficiently specific' criteria for either explicit stipulations or reciprocal transactions? (**Table 1** and paragraphs 8 – 10);

(ii) Options for the income recognition model for inflows of resources containing explicit stipulations or for reciprocal transactions without the requirement to assess 'sufficiently specific' criteria (**Table 2** and paragraphs 11 – 13); and

(iii) Options for the income recognition model for inflows of resources containing explicit stipulations or for reciprocal transactions with the requirement to assess 'sufficiently specific' criteria (**Table 3** and paragraphs 14 – 16).

Summary of staff recommendations

4 If the Board agrees with the staff recommendation that Tier 3 reporting requirements should require an entity to distinguish for the accounting for different inflows of resources based on whether the inflows of resources contain an explicit stipulation in Agenda Paper 5.1.1, then staff recommend that:

(a) an entity is not required to assess whether the explicit stipulations are 'sufficiently specific';

(b) for inflows of resources with explicit stipulation, an entity is required to identify liabilities (and therefore defer income recognition) whenever:

(i) there are enforceable conditions that the entity must spend or otherwise use the transferred resources as directed or return them to the transferor as referred in AASB 15, Appendix F, paragraph F12(a); or

(ii) the transferor can enforce by other means the explicit stipulations (including specified activities) attached to the inflows of resources (using the guidance on enforceable promises in AASB 15, Appendix F, paragraph F12(b) – F12(d)).

Income is recognised either as the goods or services are provided, activities are performed, or the eligible expenditure incurred. Where a transferor stipulates the time period relating to the use of inflow of resources, income may be recognised either when expenses are incurred or on a systemic allocation basis over the specified period; and

(c) for inflows of resources without explicit stipulation given by a transfer provider or if no liabilities under paragraph 4(b)were identified, income is recognised when cash or other assets are received or receivable.

Options for simplification

5 With reference to the 'Approach to simplification' flowchart in Appendix A of Agenda Paper 5.1.3, the staff analysis considers current practice in Australia and international jurisdictions, feedback received from stakeholders, and the findings summarised in paragraphs 12 – 22 in Agenda Paper 5.1.1. Staff have presented the options for simplification in Figure 1.Figure 1Figure 1 'Simplification options for Tier 3 income recognition model' flowchart presented on the following page for:

(a) whether, and how, an integrated approach can be developed, including whether a distinction for the accounting of inflows of resources is required – considered in Agenda Paper 5.1.1; and

(b) whether to require the assessment of 'sufficiently specific' criteria for the accounting of inflows of resources with explicit stipulation or reciprocal transactions – to be considered in this staff paper. This is represented by the **red box** in the flowchart, including the staff recommended option shaded in **yellow**.

6 Agenda Paper 5.1.3 presents six high-level scenarios to illustrate the differences in the possible income recognition options presented in this staff paper and staff paper 5.1.1.[1] The scenarios cover inflows of resources an entity receives for:

(a) sales of goods and/or services;

(b) operational funding in current year to be spent in the following financial year;

(c) funds to employ staff and fund their salaries;

(d) operational funding to further objectives;

(e) funds to construct a non-financial asset; and

(f) performing a research activity.

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1 The scenarios apply to consideration of Options 3A – 3C and 4A – 4B in this staff paper.

Figure 1: Simplification options for Tier 3 income recognition model

A.P. 5.1.1 Q1: Is distinction required for the accounting for different types of inflows of resources? (Staff propose distinction based on Options 1A, 1B and 1C between type(s) of inflows of resources) **A.P. 5.1.1 Table 1**

Option 1 if Yes

A.P. 5.1.1 Q2: Which option is appropriate to distinguish between different types of inflows of resources?

A.P. 5.1.1 Option 1A: By nature of transactions:
- Sales of goods/services
- Donations/bequests
- Grants

Definitional-based approach – akin to existing NZ Tier 3 Standards. Staff propose Tier 3 accounting requirements for income recognition will also be based on the existing NZ Tier 3 Standards.
"Existing NZ Tier 3 model" (**A.P. 5.1.1 Table 2**)[F4]

A.P 5.1.1 Option 1B: Reciprocal/non-reciprocal[F1]
For reciprocal inflows of resource (**A.P. 5.1.1 Table 2**)

A.P. 5.1.1 Option 1C: Whether an explicit stipulation to use the inflows of resources in a particular way or to act or perform in a particular way[F2] that results in the outflows of resources that are expected to be used by the NFP entity in fulfilling its obligations. (**A.P. 5.1.1 Table 2**)

Option 2 if No

A.P. 5.1.1 Q3: Which option is appropriate if there is no requirement to distinguish types of inflows of resources?

A.P. 5.1.1 Option 2A: Recognise income based on expense or time-based matching that the entity considers to be most representationally faithful of the amount and pattern of consumption/use of the transferred resources
"Expense/time-matching approach". (**A.P. 5.1.1 Table 3**)

A.P. 5.1.1 Option 2B: Recognise income for inflows of resources at the earlier of receiving cash or receiving a right to cash (receivable).
"Receipt-based approach"[F3] (**A.P. 5.1.1 Table 3**)

A.P. 5.1.1 Option 2C: Recognise income for inflows of resources at the completion of the specified activities/services. For capital grants received to construct a non-financial asset, income is recognised when construction of that asset is completed.
"Completion of activities/services approach". (**A.P. 5.1.1 Table 3**)

A.P. 5.1.2 Q1: Is there a requirement to assess 'sufficiently specific' criteria for either explicit stipulation or reciprocal transactions?***A.P. 5.1.2 (Table 1)**

Option 4 if Yes

A.P. 5.1.2 Q3: Which option is appropriate for Tier 3 income recognition model **with** requirement to assess 'sufficiently specific' criteria?

A.P. 5.1.2 Option 4A: recognise income based on paragraph F20 in AASB 15 for determining 'sufficiently specific' promise but all aspects must be present:
a) The nature or type of the goods/services;
b) The cost or value of the goods/services;
c) The quantity of the goods/services; and
d) The period over which the goods/services must be transferred.

If all of the above are not present, then recognise income when cash received/receivable. (**A.P. 5.1.2 Table 3**)

A.P. 5.1.2 Option 4B: rebuttable presumption to recognise income when cash received/receivable unless an entity determines that application of AASB 15 to determine whether the obligation is 'sufficiently specific' provides more faithful representation (**A.P. 5.1.2 Table 3**)

Option 3 if No

A.P. 5.1.2 Q2: Which option (or combinations of options) is appropriate for Tier 3 income recognition model **without** requirement to assess 'sufficiently specific' criteria?

Options 3A – 3C below were presented at the Feb 2022 AASB Board meeting. Of them, the Board directed staff to explore Options 3A and 3B

A.P. 5.1.2 Option 3A: Defer income wherever:
- Enforceable conditions exists that the entity must spend or otherwise use the transferred resources as directed or return to the transferor (i.e. refund right as referred in AASB 15, Appendix F, paragraph F12(a); or
- The transferor can enforce by other means the entity's promise to transfer economic resources using the guidance on enforceable agreement in AASB 15, Appendix F, paragraph F12(b) – F12(d).[F5]

Income is recognised as obligations are satisfied. "Enforceable conditions model". (**A.P. 5.1.2 Table 2**)

A.P. 5.1.2 Option 3B: Expense/time-matching approach (**A.P. 5.1.2 Table 2**)

A.P. 5.1.2 Option 3C: Receipt-based approach[F3] (**A.P. 5.1.2 Table 2**)

* This is only applied when income was not recognised when cash was received/receivable
Note: The questions including options within the red border are covered in this staff paper and the staff recommendation are shaded in yellow.

Footnotes to flowchart:

F1 AASB 1004 defines 'non-reciprocal transfer' as a transfer in which the entity receives assets or services or has liabilities extinguished without directly giving approximately equal value in exchange to the other party or parties to the transfer.

F2 An explicit stipulation to use the transferred resources in a particular way or to act or perform in a particular way, including to:

a) transfer goods and/or services (i.e. akin to performance obligation recognised under AASB 15)
b) perform a specified activity (e.g. akin to construct a non-financial asset under AASB 1058 or conduct a form of research for the entity's benefit);
c) incur eligible expenditure (i.e. incur expenditure for a specified purpose that is not an identifiable specified activity covered by (b)), e.g. funding is provided to a university to employ a marketing manager to promote the university's courses to overseas students; or
d) use the transferred resources in respect of a specified time period as stipulated by the resource transferor.

Any use of transferred resources for general purposes or to fund current operations without a time stipulation from transfer provider will not meet the definition of using resources in a particular way or to act or perform in a particular way.

F3 Whilst the Board indicated in its February 2022 meeting for staff not to pursue this option for the recognition of grants, donations or bequest as income, staff consider it may be an option for recognition of *ad hoc* sales of goods/services as income and for completeness of documenting the options considered.

F4 If the Board prefers Option 1A (i.e. distinction based on nature of transactions), then determining whether to require assessment of 'sufficiently specific' criteria may also be a relevant consideration in Question 1 of this staff paper.

F5 AASB 15, Appendix F, paragraph F12(a) – (d) lists the following examples of terms that result in enforceable agreements:

a) a refund in cash or kind is required when the agreed specific performance has not occurred;
b) the customer, or another party acting on its behalf, has a right to enforce specific performance or claim damages;
c) the customer has the right to take a financial interest in assets purchases or constructed by the entity with resources provided under the agreement; and
d) the parties to the agreement are required to agree on alternative uses of the resources provided under the agreement.

7 Subject to the Board decision regarding whether to require distinction of the accounting of inflows of resources in Agenda Paper 5.1.1, staff have identified the following options, staff analysis and recommendations for Tier 3 reporting requirements on:

(a) whether there is a requirement to assess 'sufficiently specific' criteria for either explicit stipulations or reciprocal transactions (**Table 1**);

(i) if 'sufficiently specific' assessment is not required – the income recognition model for inflows of resources containing explicit stipulations given by a transfer provider to use the inflow of resources or for reciprocal transactions without the requirement to assess 'sufficiently specific' criteria requirements (**Table 2**); and

(ii) if 'sufficiently specific 'assessment is required – the income recognition model for inflows of resources with explicit stipulation given by a transfer provider with expectation and/or understanding to use the inflow of resources with the requirement to assess 'sufficiently specific' criteria (**Table 3**).

Table 1: *Is there a requirement to assess 'sufficiently specific' criteria for either explicit stipulations or reciprocal transactions?*

Possible options for Tier 3 – requirement to assess 'sufficiently specific' criteria for explicit stipulations or reciprocal transactions	Option 3: not require assessment of 'sufficiently specific' criteria for explicit stipulations or reciprocal transactions	Option 4: to require assessment of 'sufficiently specific' criteria for explicit stipulations or reciprocal transactions
	This option does not require an entity to assess if explicit stipulation or reciprocal transaction is 'sufficiently specific'. Staff have developed simplification options for income recognition based on the options presented at the Feb 2022 Board meeting as referenced in Table 2.	This option requires an entity to assess that explicit stipulations or reciprocal transactions must be 'sufficiently specific' (i.e. based on the criterion in paragraphs F20 – F27 in AASB 15). Staff have developed simplification options if sufficiently specific determination remains in Table 3.
Jurisdiction adopting similar approaches (and pronouncement)	• Existing NZ Tier 3[2] • IFRS for SMEs • UK FRS 102/UK Charities SORP • Singapore CAS • HK SME-FRF & SME-FRS Canada ASNFPO	• AASB 15 and AASB 1058 • US ASC NFP 958
Support for this approach	• Responds to many stakeholders' concerns that identifying 'sufficiently specific' promises is difficult for smaller NFP entities and resulting in immediate income recognition for many inflows of resources due to the promise of goods or services not being 'sufficiently specific', which is difficult to understand for the users of the financial statements. • Removes judgement to not require assessment of 'sufficiently specific' promises which many smaller NFP entities may not be well resourced to apply in determining the appropriate treatment. Removing judgement simplifies the accounting requirements and improves comparability between Tier 3 entities. • Proportionate response and consistent with requirements applying to selected other jurisdictions applicable to smaller entities which does not require assessment whether the promise of transfer of goods or services is 'sufficiently specific'. • May improve user understanding of financial statements for promise of goods or services that do not meet 'sufficiently specific' criteria resulting in immediate recognition under AASB 1058, even though the transfer provider may have specified that those resources should be spent over a particular time period.	• Remains largely consistent with higher tier requirements and allows preparers and auditors to more easily move between entities given the consistency with Tier 2 reporting requirements. • Assessing' sufficiently specific' criteria helps an entity to identify when an obligation is satisfied and helps with auditability when an entity extinguished those obligations. • NPF entities may enter into arrangements that may give rise to 'sufficiently specific' performance obligations, constructive obligations or the immediate recognition of income. Retaining the sufficiently specific requirements helps an entity to distinguish the different characteristics in the arrangement. • More consistent with the principles in the Conceptual Framework compared to Option 3.

2 The NZ Tier 3 approach is proposing in their upcoming exposure draft to require that an expectation (as documented), must be 'specific enough' to allow the reporting entity to reliably demonstrate to the resource provider when the expectation has been satisfied (regardless of whether the resource provider monitors the use of the funding provided or not).

Staff recommendation

8 On balance, staff recommend Option 3, that the proposed Tier 3 reporting requirements should not require assessment of 'sufficiently specific' criteria. Staff are persuaded to their view by the following considerations:

(a) this approach simplifies the income recognition model in recognition of smaller NFP entities that likely do not have the resources to assess 'sufficiently specific' criteria in many cases; and

(b) this is a proportionate response to smaller entities as applied by selected other jurisdictions that do not require entities to assess whether an explicit stipulation attached to the inflows of resources is 'sufficiently specific'.

Question to Board members
Q1 Do Board members agree, for the purpose of the DP, with the staff recommendation that Tier 3 reporting requirements should not require an entity to assess 'sufficiently specific' criteria (Option 3)? If not, what approach do Board members support?

9 If Board members agree with the staff recommendation that Tier 3 reporting requirements should not require assessment of 'sufficiently specific' criteria in Question 1, staff presents the simplification options as presented at the February 2022 AASB Board meeting with modifications only to Option 3A[3] in this staff paper in **Table 2** and paragraphs 11 – 13 below.

10 If the Board does not agree with the staff recommendation in Question 1 and prefer that Tier 3 reporting requirements should continue to require the assessment of sufficiently specific criteria, then the simplification options of the income recognition model for Tier 3 NFP entities are analysed in **Table 3** and paragraphs 14 – 16 below.

3 In Agenda Paper 11.4 at the February 2022 Board meeting, the options the staff presented included: Option B: the "enforceable conditions model" and Option C the "enforceable activities/expenditure model" as referenced in paragraph 4 of Agenda Paper 5.1.1. In this paper, staff have combined Options B and C into Option 3A given the introduction of Option 1B (which requires a reciprocal activity for the inflow of the resources) and Option 1C (which requires an entity to consider whether explicit stipulation to use the inflows of resources in a particular way or to act or perform in a particular way as defined in the footnote F2 of Figure 1. This implies that an entity need only consider whether the reciprocal activity or explicit stipulation from transfer provider is enforceable (i.e. Option 3A in this staff paper), rather than re-considering if enforceability was in relation to specified activities or incurring expenditure (i.e. Option C as presented in Feb 2022 Board meeting).

Note: This section is relevant only if the Board agrees with the staff recommendation in Question 1

Table 2: *Summary of possible options and analysis for Tier 3* – the income recognition model for inflows of resources containing explicit stipulations or for reciprocal transactions without the requirement to assess sufficiently specific criteria

Possible options for Tier 3 – accounting requirements for the income recognition model for inflows of resources without requiring an entity to assess sufficiently specific criteria requirement	**Support for the approach**	**Arguments against the approach**
Option 3A: Simplify the income recognition requirements of inflows of resources containing explicit stipulations (or for reciprocal transactions) by also **identifying liabilities** (and therefore deferring income recognition) whenever: (i) **there are enforceable conditions** that the entity must spend or otherwise use the transferred resources as directed or return them to the transfer provider (i.e. refund right as referred to in AASB 15, Appendix F, paragraph F12(a)); or (ii) the transfer provider can **enforce by other means** the explicit stipulations attached to the inflows of resources (using the guidance on enforceable promises in AASB 15, Appendix F, paragraph F12(b) – F12(d)). Staff acknowledge that income can be recognised either as the goods/services are provided, as activities are performed, as the eligible expenditure is incurred (over time) or only after completion of the services/goods delivered (point in time). To further simplify the requirements, staff consider that income should be recognised over time for provision of services. Where a transferor specifies the time period relating to the use of inflow of resources, income may be recognised either when expenses are incurred or on a systemic allocation basis over the specified period, which is similar to the expense or time-based matching in Option 3B below. This option is referred to as "enforceable conditions model". Income is recognised when cash or assets are received or receivable where liabilities are not identified under (i) or (ii) above, or where no explicit stipulation identified or for non-reciprocal inflows of resources.	• Arguably proportionate response to concerns raised by stakeholders. • Removes sufficiently specific criteria which stakeholders report as being difficult to apply. • Differentiates between enforceable and unenforceable stipulations and allows entities to focus resources to determine income recognition for inflows of resources that contain enforceable conditions. • Increases the understandability of financial statements as the recognised liability more closely aligns with the stakeholder view of a liability (e.g. where some obligations that may not meet the criteria in AASB 15 would be recognised as a liability under this option). • Stakeholder feedback indicates that assessing enforceability of a contract is not too onerous, thereby costs might be reduced. • Addresses stakeholder feedback where current accounting treatment for non-refundable enrolment/joining fees may be required to be deferred over the contract period. This option does not require obligations with no enforceability to be deferred.	• Enforceable criteria may be too narrow a principle for deferral.[4] • Stakeholders may be confused about the enforceability of constructive obligations. • Departs from Tier 1/Tier 2 requirements and the Conceptual Framework to certain degree, although certain liabilities would overlap. • The model may not sufficiently leverage management information used in decision making. • As noted in paragraph F13 of AASB 15, agreements may be enforceable even if the particular terms do not include refund or other enforcement provisions, since Australian law generally provides remedies of specific performance or damages for breach of an agreement, as such, judgement would be still required to determine enforceability. • Removal of sufficiently specific means that judgement is required to assess when a liability can be recognised, and it may be difficult to determine when the obligation is satisfied – leading to potentially arbitrary revenue recognition. • Initial costs incurred to understand the new models and terminology not currently present in AAS.

4 As noted in stakeholder feedback from the NZASB Post Implementation Review (PIR) of its Tier 3 and 4 PBE Standards, stakeholders would like revenue deferral to be more widely permitted and considered that the 'use or return' condition requirement in the Tier 3 Standard is too restrictive.

Possible options for Tier 3 – accounting requirements for the income recognition model for inflows of resources without requiring an entity to assess sufficiently specific criteria requirement	Support for the approach	Arguments against the approach
Option 3B: Simplify the income recognition requirements to allow **either expenses or time-based matching** for the transferred resources containing explicit stipulations (or for reciprocal transactions) This approach would be similar to the approach applied in AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* (but extended to all transfers, not just government grants), under which unsatisfied conditions that defer income recognition include unenforceable conditions. This option further simplifies the income recognition without the need to assess the sufficiently specific criteria. Further, it allows either expenses or time-based matching that the entity <u>considers to be most representationally faithful</u> of the amount and pattern of consumption/used of transferred resources received. Inflows of resources related to assets, including non-monetary assets recognised at fair value, may, as a presentation alternative to recognising 'deferred income' liability, deduct the grant amount in arriving at the asset's carrying amount. This means recognising the inflows of resources in profit or loss as a reduced depreciation expense. As such, where the inflows of resources are received for the entire value of the asset, the effect would result in non-recognition of the asset. In this paper, this model is referred to as the "expense/time-based matching model". Income is recognised when cash or assets is received or receivable when no explicit stipulation is identified or for non-reciprocal inflows of resources.	• Consistent with existing IFRS standard – IAS 20 (AASB 120) • Expected to be less costly to apply than the existing AASB 1058 model for Tier 3 entities removing the need to assess enforceability and specificity of conditions. • May increase the understandability of financial statements as the liability more closely aligns with the stakeholder view of a liability. • Leverages management information used in decision-making due to the use of matching. • Proportionate response to issues raised by stakeholders.	• Does not support consistency across NFP tiers but would be consistent with for-profit treatment for recognition of grants. • A liability arising from unenforceable obligations may result in a departure from the Conceptual Framework. • Enforceability is a key characteristic of a liability. This has been removed in this option which may result in difficulty for users to distinguish a liability from a general obligation. • Allows the entity an option to offset funding received against a related asset purchased or constructed which may result in non-recognition of assets – this would reduce information usefulness for users. • This option may be perceived to provide too much flexibility for income deferral and judgement may be required to determine which income should be deferred and may lead to inconsistency between Tier 3 entities.
Option 3C: Simplify the income recognition requirements to recognise income at the **earlier of when cash or asset is received or receivable** for inflows of resources containing explicit stipulations (or for reciprocal transactions). In this paper, this is referred to as the 'receipt-based model'. This approach does not require an entity to consider if there are any conditions including refund rights. This option further simplifies income recognition as income is recognised the earlier of when the cash or other asset is received or receivable.	• Least costly model since an entity is not required to consider any terms and/or conditions within the agreement to determine the appropriate accounting treatment.	• Significant departure from the Conceptual Framework and significant inconsistency with Tier 1/Tier 2 requirements. • Does not reflect the pattern of transfer of specific goods/services funded by the contract. • Causes mismatch between receipt of funds and corresponding expenditure for all contracts which overlap a financial reporting period. • Conflicts with stakeholder feedback in respect of user needs. • Would likely increase volatility of results as income and expenses are more likely recognised in different periods compared to current requirements of AASB 1058.

Evaluation of options against the Tier 3 development principles

11 With reference to the 'Approach to simplification' flowchart in Appendix A of Agenda Paper 5.1.3 and the analysis in Table 2 above, staff also analysed each of the proposed options against the tentative Tier 3 principles previously agreed to by Board members. Staff consider that the proposed options are broadly equally aligned with the Tier 3 principles, except for the following listed below:

Principles	Staff assessment
Tier 3 financial statements are general purpose financial statements. As such, Tier 3 financial statements provide useful information to users of financial statements	Option 3A moderately aligns with the Conceptual Framework because some liabilities may not meet the definition within the Conceptual Framework.[5] As such, the information presented in the general purpose financial statements are useful to users as deferral of income is allowed in certain scenarios. Option 3C does not provide information useful to users as it does not recognise any deferral of income where there are obligations associated with the inflows of resources and does not address stakeholder concerns.
Consistency with the accounting principles specified in Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable but might not always be warranted since Tier 3 requirements are being developed as a proportionate response Accounting requirements do not impose disproportionate costs on preparers compared to the benefits of the information	Option 3A moderately aligns with Tier 2 accounting principles as there may be certain liabilities for deferral of income that would also be consistent with Tier 2 accounting requirements. Options 3B and 3C do not align with Tier 2 accounting principles as Option 3B allows deferral of income in all cases, and Option 3C requires all revenue to be recognised upfront. Option 3B may also impose higher costs on preparers as it requires meticulous record-keeping to match income with related expenditure. Option 3C is the simplest and least costly to apply but conflicts with stakeholder feedback regarding user needs.
Where possible, leverage the information management uses to make a decision about the entity's operations. The ability to leverage the information management uses is made within the context of the NFP conceptual framework, user needs and cost/benefit considerations, and the aim for comparability within Tier 3 reporting requirements.	Option 3B most strongly leverages the information management uses to reflect the reporting to funding providers for grant acquittal purposes. Options 3A and 3C may not always leverage information management uses as some information required is not ordinarily prepared by management and may be inconsistent with information recorded in grant acquittals.

Staff recommendation

12 On balance, if the Board decided that an entity is not required to assess sufficiently specific criteria in Question 1 above, then staff recommend Option 3A. That is, the proposed Tier 3 reporting requirements should require recognition of income by also identifying liabilities (and therefore deferring income recognition) whenever:

5 As noted in AASB submission on IPSAS Exposure Drafts 70 – 72, it is not clear why a requirement to perform a 'specified activity' or to incur 'eligible expenditure' would always give rise to a liability for the transfer recipient, when the transaction is not considered a liability under the IPSASB Standards stated in paragraph 3 of ED 71 (the scope exclusions) and does not have a performance obligation under ED 70.

(a) there are enforceable conditions that the NFP entity must spend or otherwise use the transferred resources as directed or return them to the transfer provider (i.e. refund right as referred in AASB 15, Appendix F, paragraph F12(a)); or

(b) the transfer provider can enforce by other means the explicit stipulations attached to the inflows of resources (using the guidance on enforceable promises in AASB 15, Appendix F, paragraph F12(b) – F12(d)).

Income will be recognised when cash is received or receivable for inflows of resources that do not contain enforceable conditions for any explicit stipulation given by a transfer provider or where the transfer provider cannot enforce the obligations by other means.

13 Staff are persuaded to their view by the following considerations:

(a) respond to stakeholder feedback that an income recognition model to identify liabilities where inflows of resources given or raised for a specific purpose with enforceability from donor or grantor would be easily understood by smaller NFP entities;

(b) the option achieves a balance between the cost to preparers and the usefulness of the financial information for the users; and

(c) staff acknowledge that stakeholder feedback from NZASB PIR of its Tier 3 and 4 Standards considered the enforceable criteria might be too narrow a principle for deferral. However, the approach would simplify the recognition model by only requiring smaller entities to consider those inflows of resources with enforceable obligations that staff consider most likely to be significant to the entity.

Question to Board members

Q2 Do Board members agree for the purpose of the DP, with the staff recommendation that Tier 3 reporting requirements should require Option 3A. That is, require for recognition of income by also identifying liabilities (and therefore deferring income recognition) whenever:

a. there are enforceable conditions that the entity must spend or otherwise use the inflows of resources as directed or return them to the transfer provider; or

b. the transfer provider can enforce by other means the explicit stipulations attached to the inflows of resources (using the guidance on enforceable promises in AASB 15, Appendix F, paragraph F12(b) – F12(d)).

Income is recognised either as the goods or services are provided, activities are performed, or the eligible expenditure incurred. Where a transferor stipulates the time period relating to the use of inflow of resources, income may be recognised either when expenses are incurred or on a systemic allocation basis over the specified period

For inflows of resources that do not contain enforceable conditions or enforcement by other means for explicit stipulation given by a transfer provider, income will be recognised when cash is received or receivable.

If the Board members disagree with the staff recommendation, what approach do Board members support?

Note: This section is relevant only if the Board does not agree with the staff recommendation in Question 1

Table 3: *Summary of possible options and analysis for Tier 3* – the income recognition model for inflows of resources with explicit stipulation or for reciprocal transactions with the requirement to assess sufficiently specific criteria

Possible options for Tier 3 – accounting requirements for the income recognition model for inflows of resources with the requirement to assess sufficiently specific criteria	Support for the approach	Arguments against the approach
Option 4A: Recognise income by determining aspects of the **'sufficiently specific' criterion** based on paragraph F20 in AASB 15 with the modification that **all** aspects below must be present in order for **an enforceable** stipulation/reciprocal activity to be considered sufficiently specific: a) the nature or type of goods/services; b) the cost or value of the goods/services; c) the quantity of the goods/services; and d) the period over which the goods/services must be transferred.[6] If the above aspects of sufficiently specific criterion are present, income is recognised when such a sufficiently specific stipulation is satisfied. If the transaction does not contain sufficient specific stipulation or activity or agreement that is not enforceable, then recognise income when cash is received or receivable.	• More consistent with the requirements for Tier 1 and Tier 2 entities facilitating the movement of professionals between Tiers. • Relatively consistent with the principles in the Conceptual Framework. • Only considers enforceable obligations; hence NFP entities can spend less resources to consider deferral of income for any agreement that is not enforceable. • Narrowly defined requirements where all aspects in determining whether a transaction contains sufficiently specific performance obligations may simplify accounting requirements by removing significant level of judgement required to assess sufficiently specific requirements.	• Requires all aspects as set out in paragraph F20 of AASB 15 to be present which is a narrower requirement than the existing requirements. As such, this may result in more income being recognised immediately than existing requirements. • The model is less likely to leverage management information used in decision making. • Stakeholder feedback indicated that smaller NFP entities with limited resources are spending significant time and effort to determine 'sufficiently specific 'requirements. • Confusion and inconsistences in reporting revenue due to difficulties in identifying whether stipulations in agreements are sufficiently specific may still pertain to some extent. • Narrowly defined requirements may not necessarily be sufficiently flexible to address the concern from stakeholders to allow income to be deferred where there are obligations attached to the inflows of resources entered by Tier 3 entities. • Stakeholder feedback indicates the cost of ongoing implementation exceeds the perceived benefits.
Option 4B: A **rebuttable presumption** to recognise all income transactions when cash is received or receivable unless an entity determines that application of AASB 15 to determine whether the obligation is sufficiently specific provides more faithful representation.	• Income would be recognised immediately as a first step which is simple to apply unless the entity determines that application of AASB 15 results in a more faithful representation.	• Likely leads to inconsistent reporting amongst Tier 3 entities as entities will apply judgement determining when to apply AASB 15 for agreements with performance obligations.

6 Staff have considered to align Option 4A with the proposed NZ Tier 3 approach to replace the aspects 'sufficiently specific' criterion with 'specific enough' requirements, however, staff think this would not sufficiently simplify current requirements in AASB 15 and would not address the feedback from stakeholders with further simplification and guidance. Therefore, staff have decided to specify the 'sufficiently specific' criterion leveraging off the aspects noted in AASB 15 paragraph 20.

Evaluation of options against the Tier 3 development principles

14 With reference to the 'Approach to simplification' flowchart in Appendix A of Agenda Paper 5.1.3, in addition to the analysis in **Table 3** above, staff also analysed each of the proposed options against the tentative Tier 3 principles previously agreed to by the Board members. Staff consider that the proposed options are broadly equally aligned with the Tier 3 principles, except for the following listed below:

Principles	Staff assessment
Tier 3 financial statements are general purpose financial statements. As such, Tier 3 financial statements provide useful information to users of financial statements	Option 4A does not significantly depart from the Conceptual Framework, as such, it would provide useful information to users of financial statements. However, stakeholder feedback suggests that it may not align with stakeholders' view for grants/donations with the expectation to be immediately recognised where the obligations are not sufficiently specific. Option 4B aligns with the Conceptual Framework only if an entity applies AASB 15.
Consistency with the accounting principles specified in Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable but might not always be warranted since Tier 3 requirements are being developed as a proportionate response Accounting requirements do not impose disproportionate costs on preparers compared to the benefits of the information	Option 4A mostly aligns with Tier 2 requirements. Still, stakeholder feedback indicated the model is complex, and Tier 3 entities with limited resources are spending significant time and effort to determine the appropriate income treatment under the current accounting standards for compliance purposes only. Option 4B aligns with Tier 2 principles if the entity applies AASB 15 but allows an entity to immediately recognise income if preparers determine that AASB 15 does not result in the most faithful representation of the transaction.
Where possible, leverage the information management uses to make a decision about the entity's operations. The ability to leverage the information management uses is made within the context of the NFP conceptual framework, user needs and cost/benefit considerations, and the aim for comparability within Tier 3 reporting requirements.	Option 4B allows an entity to leverage management information if the entity has information to apply AASB 15 appropriately. Option 4A may not leverage management information as some information needed is not ordinarily prepared by management, and stakeholders have indicated confusion regarding information based on the income recognition model.

Staff recommendation

15 On balance, if the Board decided that an entity is required to assess sufficiently specific criterion in Question 1 above, then staff recommend Option 4A, that the proposed Tier 3 reporting requirements should recognise income based on paragraph F20 of AASB 15 for determining sufficiently specific criterion with all aspects must be present. If not all aspects of sufficiently specific criterion are present, then income is recognised at the earlier of receiving cash or receiving a right to cash (receivable).

16 Staff are persuaded to their view by the following considerations:

(a) if the Board requires that sufficiently specific determination continues to be required, then income should continue to be based on the aspects in paragraph F20 of AASB 15 as considered by other NFP entities;

(b) judgement increases complexity, as such, providing a more rules-based approach could simplify the accounting requirements; and

(c) while there may be more income recognised when cash is received or receivable under this option, this may eliminate the need for smaller entities to determine when performance obligations are satisfied for many inflows of resources and reduce the cost of preparation.

Question to Board members

Q3 Do Board members agree, for the purpose of the DP, with the staff recommendation that Tier 3 reporting requirements should require Option 4A. That is, income is recognised based on paragraph F20 of AASB 15 for determining aspects of 'sufficiently specific' criterion with all aspects below required to present:

a) the nature or type of goods/services;

b) the cost or value of the goods/services;

c) the quantity of the goods/services; and

d) the period over which the goods/services must be transferred.

If the above aspects are not present, recognise income when cash is received or receivable.

If not, what approach do the Board members prefer?