



Project: Not-for-Profit Private Sector
Financial Reporting Framework

Meeting: M184

Topic: Project overview

Agenda Item: 7.1

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Project Priority: High
Decision-Making: High
Project Status: Initial deliberations

Objective of this agenda item

- 1 The objective of this agenda item is, for the purposes of the Not-for-profit Financial Reporting Framework (NFP FRF) Discussion Paper (DP), for the Board to:
 - (a) **receive** project update including interaction with cross-cutting projects and the timeline (this Agenda Paper);
 - (b) **decide** its preliminary views on Tier 3 accounting requirements for:
 - (i) primary financial statements (Agenda Paper 7.2); and
 - (ii) leases other than 'peppercorn'/concessionary leases (Agenda Paper 7.3).

Attachments

- | | |
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| Agenda paper 7.2 | Tier 3 - Primary financial statements |
| Agenda paper 7.3 | Tier 3 - Leases |
| Agenda paper 7.4 | Research studies and articles (in Board-only supplementary folder): <ol style="list-style-type: none">7.4.1. <i>Faulty Scripting and the Standardization of Non-financial Reporting: the Case of Service Performance Reporting in Australia</i>7.4.2. <i>Financial Reporting by Charities: Why Do Some Choose to Report Under a More Extensive Reporting Framework?</i>7.4.3. <i>The effect of members on charities' annual reporting: evidence from companies limited by guarantee in Australia</i> |

Background

- 2 At its 20-21 February 2021 meeting, the Board agreed to develop a further reporting Tier (Tier 3) for application by not-for-profit (NFP) private sector entities. This reporting Tier is intended to be a proportionate response for application by some (but not all) NFP private sector entities that are currently preparing special purpose financial statements (SPFS) on the basis that the entity is not a reporting entity as defined in SAC 1 *Definition of the Reporting Entity*. In addition, this reporting Tier might be applied by some (but not all) NFP private sector entities that are currently preparing Tier 2 general purpose financial statements (GPFS).
- 3 A number of staff paper have been presented including the approach to simplification agreed by the Board at its 4 August 2021 Board meeting ([Minutes of the 182nd meeting of the AASB](#)) as presented in [Appendix A](#). The staff papers will assist the Board in forming its preliminary views on detailed reporting aspects of the proposed reporting Tier 3, for inclusion in its discussion paper. Developing preliminary views in this regard will enable the Board to obtain useful feedback to inform it as to whether its proposed views should be further developed as part of a future Exposure Draft.
- 4 The Board has decided on a number of tentative decisions to date in developing the Tier 3 accounting requirements:
 - (a) at its 20-21 February 2021 meeting, the Board agreed to develop a further reporting Tier (Tier 3) for application by NFP private sector entities;
 - (b) at its 20-21 April 2021 meeting, the Board decided on the principles against which it will form its views on Tier 3 accounting requirements, for inclusion in the DP;
 - (c) at its 21-22 June 2021 meeting, the Board made decisions on the setting of Tier 3 requirements in the context of Australian Accounting Standards and on accounting for controlled entities;
 - (d) at its 4 August 2021 meeting, the Board considered the primary objective in setting Tier 3 proposals and decided on the accounting for changes in accounting policies and correction of errors; and
 - (e) at its 8-9 August 2021 meeting, the Board decided on the application of accounting policies for omitted topics and application of higher tier requirements where the accounting policy option is not included within Tier 3 requirements.

[The Not-for-Profit Private Sector Financial Reporting Framework Project Summary](#) provides the overview of the Board's tentative decisions to date in respect of the project.

Project timeline and milestones

- 5 Following the Board's discussion at the September 2021 meeting, an updated project timeline and milestones is provided in paragraphs 16 – 18 of this Agenda Paper.
- 6 Subject to the Board's decisions at this meeting, staff will continue analysis of NFP private sector Tier 3 differential reporting topics to discuss at forthcoming Board meetings.

Tier 3 primary financial statements (Agenda Paper 7.2)

- 7 Objective of Agenda Paper 7.2 is to provide the Board with the staff analysis and recommendations on Tier 3 reporting requirements for an NFP entity's primary financial statements. Specifically, the primary financial statements to be presented by Tier 3 entities and the presentation approach for the face of those primary financial statements.

Tier 3 accounting requirements for Leases (Agenda Paper 7.3)

- 8 Objective of Agenda Paper 7.3 is for the Board to consider staff analysis and recommendations on possible Tier 3 proposals for the accounting requirements for leases other than ‘peppercorn’/concessionary leases. Considerations for concessionary lease for Tier 1 and Tier 2 will be covered in Agenda Paper 11.2 and therefore was not considered for Tier 3 proposals at this stage.

Project update

Stakeholder outreach update

- 9 The AASB NFP Project Advisory Panel met on 18 October 2021. At that meeting, staff sought to obtain Panel members’ input into initial staff considerations on the topics that staff planned to discuss with the Board at its November 2021 meetings:
- (a) Tier 3 reporting requirements on primary financial statements (as referenced in AP 7.2 paragraph 14)
 - (b) Tier 3 accounting requirements for leases (as referenced in AP 7.3 paragraphs 21 – 26)
 - (c) Income of Not-for-Profits Entities (AASB 1058 and AASB 15 NFP guidance) – narrow scope amendments (as referenced in AP 11.1 paragraph 10)
 - (d) Right-of-use assets under concessionary leases (as referenced in AP 11.2 paragraph 9)
- and incorporated the feedback into the respective staff analysis. Staff will continue to seek feedback from NFP Project Advisory Panel throughout the project.
- 10 Staff also sought feedback about aspects of this project at the October 2021 ACNC Sector and Advisor forums which comprises of practitioners, advisors and users within the charitable sector. The feedback from these forums have been incorporated into the respective papers for the November 2021 meeting.

Project environmental update including interaction with cross cutting projects

Project	Update
Australian Charities and Not-for-profits Commission Amendment (2021 Measures No. 3) Regulations 2021	<p>The Government issued an exposure draft legislation (comment closed on 15 October 2021) which will implement two reforms in the Australian Charities and Not-for-profits Commission Legislation Review 2018 (Review). The Regulations will give effect to:</p> <ul style="list-style-type: none"> • Recommendation 12 which will increase the revenue threshold defining small, medium and large registered charities. Reporting thresholds for small charities will increase to less than \$500,000 annual revenue and medium-sized charities will increase to less than \$3 million annual revenue, reporting against the 2021-22 financial year) • Recommendation 14 which will require all registered charities to disclose: <ul style="list-style-type: none"> • Related party transactions relating to disclosure of compensation of key management personnel, in accordance with AASB 124 <i>Related Party Disclosure</i>, reporting against the 2021-22 financial year. Exemptions will be provided for medium and large charities with one remunerated key management personnel from disclosing aggregated remuneration paid to responsible persons and senior executives; and

	<ul style="list-style-type: none"> related party transactions relating to any other matters, in accordance with AASB 124 <i>Related Party Disclosures</i>, reporting against the 2022-23 financial year. <p>The AASB already submitted its comments to the Treasury Thresholds Working Group in relation to the consultation on increasing financial reporting thresholds for ACNC-registered charities on 19 March 2021 and therefore did not comment on this consultation. AASB staff have also discussed the topic with Treasury staff.</p>
<p>NZASB’s post-implementation review (PIR) of Tier 3 and Tier 4</p>	<p>At its NZASB Board meeting in September 2021 staff proposed recommendations to address the PIR feedback considered by NZASB at its meeting on 23 June 2021 to broaden the deferral of revenue recognition criteria of grants and donations as well as proposing a number of amendments to the NZ Tier 4 Standards through a process of shortening and simplifying the language and other amendments</p> <p>At its NZASB Board meeting on 19 October 2021, the NZASB Board discussed four issues including amendments to better align wording in the NZ Tier 3 and 4 service performance reporting requirements with PBE FRS 48 <i>Service Performance Reporting</i>, as well as the following issue:</p> <ol style="list-style-type: none"> (1) Accumulated funds for Tier 3: support the proposal, and consider further options, to introduce requirements for entities to provide narrative information about an entity’s general approach to managing reserves (if any) and assets with restrictions with guidance on the circumstances an entity may choose to create a reserve (whether restricted or unrestricted). NZASB also proposed changes to include terminology specific to trust and to reduce the prominence of the term ‘owners’. (2) Opting up in Tier 3: to recognise the effect of specific transactions that results in OCI instead directly in accumulated funds and not in the statement of financial performance and to present cumulative effect of similar transactions as a separate reserve within accumulated funds. No additional guidance on opting up to be developed outside of NZ Tier 3 Standards (3) Tier 3 grant and donations revenue recognition – proposed wording: in line with decision made in NZXRB Board meeting in September to broaden the deferral of revenue recognition criteria, NZXRB Board members have differing view on whether the revenue recognition criteria should be to: <ol style="list-style-type: none"> a. recognise grant and donations revenue in the same accounting period which associated obligations over use are satisfied when there are expectations over how the transferred resources will be used (but no requirement to assess enforceability) b. recognise grant and donation revenue when matching expenditure is incurred. i.e., matching principle <p>The NZXRB Board consequently decided to propose to include both options as part of an exposure draft for stakeholder feedback.</p> <p>Staff have considered the outcome of the PIR for the topics analysed to date and will continue to monitor the project and consider implications of the PIR feedback on the respective topics expected to be included in the DP.</p>
<p>IFR4NPO</p>	<p>Consultation on Phase 1 (General reporting issues) concluded on 13 August. Project further proposes phased approach to the Exposure Draft focusing on NFP guidance with non-NFP specific guidance based on <i>IFRS for SMEs</i>. ED batches are expected in Sep ‘22, May ‘23 and Nov ‘23 with final guidance expected April ‘25. At its October ‘21 meeting the Technical Advisory Group considered the following feedback from Phase 1 consultation:</p> <ul style="list-style-type: none"> support for a broad characteristics approach to describing entities that the IFR4NPO is expected to primarily benefit. The need to define primary users specifically from the perspective of financial reporting/statements

	<ul style="list-style-type: none"> • Broad support for accrual-based accounting but recognising practical challenges for smaller less complex NFOs, and initial focus on high level principles in relation to non-financial reporting rather than any detailed prescriptive work • High level of support to base guidance on existing international framework, particularly the benefit of <i>IFRS for SMEs</i> remains the most appropriate foundational framework for the Guidance <p>Staff will continue to monitor the project and consider implications of the consultation feedback on the respective topics expected to be included in the DP.</p>
<p>IPSASB consulting on possible project on differential reporting</p>	<p>IPSASB' Mid-Period Work Program Consultation proposes to add Differential Reporting project to explore which financial reporting principles best meet the needs of "less complex public sector entity" and ease the financial reporting burden on "less complex public sector entities" through a cost-benefit approach. A major portion of this project would identify the characteristics of "less complex public sector entities" and determine what guidance in IPSAS should be modified and simplified.</p> <p>Staff will monitor the project to identify any useful stakeholder feedback or considerations for the project noting that focus of IPSAS differential reporting project is public sector.</p>
<p>Second Comprehensive Review of the IFRS for SMEs Standard</p>	<p>IASB is currently in the process of assessing whether to align the <i>IFRS for SMEs</i> Standard with IFRS Standards and working towards publishing an exposure draft, proposing amendments to <i>IFRS for SMEs</i> Standard for new requirements that are in the scope of the review. Proposals to align the <i>IFRS for SMEs</i> with IFRS 16 was considered at the SME Implementation Group meeting on 9 September 2021 as referenced in AP 7.1 (paragraph 19).</p> <p>Staff also noted IASB staff recommendation for October IASB Board meeting to amend <i>IFRS for SMEs</i> to remove the existing fallback option to IAS 39, without replacing it with a fallback to IFRS 9, to retain unaligned hedge accounting requirements with IFRS and to align requirements with IFRS 15 principles and language.</p> <p>Staff will continue to monitor the project and consider implications for <i>IFRS for SMEs</i> as one of the reference points when analysing respective topics expected to be included in the DP.</p>

Research update

- 11 In addition to the research noted at prior Board meetings, staff noted further three research studies (Agenda Paper 7.4 in Board-only supplementary folder):
- (a) *Faulty scripting and the standardization of non-financial reporting: case of service performance reporting in Australia* (not yet published) (Agenda Paper 7.4.1):
 - (i) Staff understands that this study expands on the research study presented at the 2019 AASB Research Forum. The study attempts to highlight potential issues with due process, the use of financial reporting concepts and the rigidity of new standards by analysing the AASB's development of ED 270 *Reporting Service Performance Information*. The analysis is expected to show that ideas about the 'perceived' users and preparers in the process of developing ED 270 did not match the realities of real users (donors) and preparers (NFPs). The study suggests that the existing knowledge base and due process of financial accounting standard-setting may not transfer easily to non-financial reporting and could even hinder standard-setters' efforts to develop workable standards, especially where 'users' are not sophisticated investors and/or do not have an active representative body to provide input. This can potentially hinder the standard setter from gaining the

insights of experienced practitioners that are important for standard-setting in non-financial reporting.

- (b) *Financial Reporting by Charities: Why Do Some Choose to Report Under a More Extensive Reporting Framework*¹ (Agenda Paper 7.4.2) finds that:
- (i) the economic importance of the charity, its funding sources, and level of indebtedness are significant factors in explaining charities choosing a more comprehensive financial reporting framework;
 - (ii) a substantial increase in the proportion of large charities electing to disclose Tier 2 GPFS over the period 2014 to 2016; and
 - (iii) the choice of large audit firm (Big 4 and mid-tier audit firms) is significantly associated with charities both lodging more comprehensive GPFS, and reporting GPFS in accordance GPFS -Tier 2 framework.
- (c) *The effect of members on charities' annual reporting: evidence from companies limited by guarantee in Australia*² (Agenda Paper 7.4.3) finds that:
- (i) members as a salient stakeholder group that acts to encourage the disclosure of financial and non-financial information in the annual report;
 - (ii) the extent of reporting of financial and non-financial information and the number of members is positively associated with the level of future revenue; and
 - (iii) information asymmetry between the charity and its contributors - that the disclosure of information about charities' performance is critical to the decision-making of donors.
- 12 Staff consider that the findings suggest that users such as members find financial disclosures and non-financial information is important to their decisions making process. Large charities tend to prepare GPFS, which supports the development of a differential reporting tier (Tier 3) for smaller NFP entities which would be disproportionately impacted if the ability to prepare special purpose financial statements would be removed in the future.
- 13 Staff are also aware of three Australian research currently being conducted and the final reports on the results of those research have not yet been published:³
- (a) *Decision Usefulness: A re-examination of the information needs of non-profit GPFR users* – noted in April 2021 [Agenda Paper 7 Research update](#). This research is intended to communicate information needs of users of NFP GPFS. Staff understand it is expected to communicate the research participants' view that:
- (i) having comparability between like entities is important. Factors identified as impairing comparability included having accounting policy choices, subjectivity in applying accounting requirements, and an entity's ability to tailor its financial statements to meet its funding-imposed reporting obligations. It will also examine the users that NFP organisations are accountable to and information that users consider decision useful, as well as identifying possible areas of complexities in the existing accounting requirements for NFP preparers and auditors.
- (b) *Presentation prominence: Does it matter to non-professional investors? The case of 'Other Comprehensive income*. This research looks at the presentation prominence of other comprehensive income and its influence on the decisions of non-professional investor-users. Staff understand it is expected to communicate that:

1 Published in Abacus, 2020

2 Published in Accounting & Finance, 2021

3 Research studies noted in paragraph 11(a) and 11(b) will be presented at the AASB November 2021 Virtual Research Forum

- (i) clearer labels will help financial statement users reduce their information processing cost and increase the likelihood of use of such information.
- (c) *Adoption of AASB 16 Leases: Post-implementation review in the not-for-profit sector* - Staff are aware of an Australian research study currently being conducted which aims to assess the impact of AASB 16 on the NFP sector. Though the study is yet to be finalised and published, staff understand that it is expected to communicate the research participants' views that:
 - (i) the challenges associated with the implementation of AASB 16 have been specifically high among NFPOs;
 - (ii) the effort that went into implementing AASB 16 and then explaining it to the members of NFPOs was very difficult, particularly in relation to the on-balance sheet recognition of leased assets and liabilities;
 - (iii) NFPOs had difficulty in finding the right team or professional to prepare accounts in compliance with AASB 16 without considerable errors; and
 - (iv) there are concerns that the value AASB 16 brings to end-users in the NFP sector may not justify the significant increase in costs associated with compliance.

Discussion Paper development and outreach plan

- 14 Staff are progressing drafting of the DP as the Board forms its views on the remainder of the topics, with consideration given to the target audience. Staff are exploring the use of:
- language more commonly used in the NFP sector and preparers/users of smaller NFP entity financial statements; and
 - tools to 'reduce' the length of the DP and improve stakeholder engagement, for example, the use of more diagrams and the presentation of information in a way that distinguishes the 'must know' from the 'more information'.
- 15 Staff are mindful how outreach and communication strategy are important success factors for the project and are considering about the most effective approach to reach stakeholders. Staff will bring to a future Board meeting the communication strategy plan to support the release of the DP

Question 1 to the Board

Do Board members have any comments on the project update summarised above?

Project timeline and milestones

- 16 As noted at the August 2021 AASB meeting ([Agenda Paper 4.1](#)), staff are actively considering the project timeline. Subject to the Board's decisions at this meeting, the table in paragraph 18 below provides an updated timeline and key milestones for the project. The timeline reflects the decisions made by the Board to date, as well as consideration of the extent of analysis required for the remaining topics.
- 17 Since the last Board meeting in August, staff have included a specific item to consider the main aspects of disclosures requirements for Tier 3 for the topics covered by the DP, taking into account the simplification approaches to disclosure criteria and understandability as presented in [Agenda Paper 4.2](#) at the 4th August 2021 Board meeting.

Updated project timeline and milestones

- 18 The updated project timeline and milestones are as follows:

TIMELINE	PROJECT MILESTONES	TOPIC
NOV 2021	Board's deliberations on DP preliminary views	Key topics <ul style="list-style-type: none"> • Primary financial statements • Leases
H1 2022	Board's deliberations on DP preliminary views Board to review working draft of the DP	Key topics <ul style="list-style-type: none"> • Revenue/Income • Financial instruments • Investment property • Impairment of non-current assets • Employee benefits • Disclosures for the key topics to be included in the DP Other topics to be considered in the DP⁴
Q3 2022	Board's deliberations on DP preliminary views Board to review final draft DP and appoint subcommittee to finalise out of session DP exposed for public comment	<ul style="list-style-type: none"> • Sweep issues

Question 2 to the Board

Do Board members agree with the updated project timeline and milestones presented in paragraph 18 above?

4 Other possible future Tier 3 topics to be discussed in the DP as presented in [AP 4.1 at the 4th August 2021 Board meeting](#) that have not been identified as an area of significant interest by stakeholders beyond terminology and language are: intangible assets; property plant and equipment; inventory; associates and joint ventures; provisions, contingent liabilities and commitments; income taxes; fair value; foreign currency transactions; offsetting; expenses; borrowing costs; going concern; and events after reporting date. Staff plan to bring suggested high-level drafting for these topics – primarily based on the NZ External Reporting Board's *Public Benefit Entity Simple Format Reporting – Accrual (Not-for-Profit) Accounting Standard* – for the Board's consideration in H1 2022 as part of the working draft of the Discussion Paper.

Appendix A – Approach to simplification agreed by the Board at its 4 August 2021 Board meeting

