

## Basis for Conclusions on AASB 1058

*This Basis for Conclusions accompanies, but is not part of, AASB 1004. The Basis for Conclusions was originally published with AASB 1058 Income of Not-for-Profit Entities.*

### Background

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BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in AASB 1058. It sets out the reasons why the AASB developed the Standard, the approach taken to developing the Standard and the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

#### The need for change

BC2 Prior to the issue of this Standard and AASB 15 *Revenue from Contracts with Customers*, the recognition and measurement requirements for transactions giving rise to income depended on whether the transaction was reciprocal or non-reciprocal in nature. The accounting for income arising from reciprocal transactions was predominantly addressed in AASB 118 *Revenue* and AASB 111 *Construction Contracts*. The accounting for income arising from non-reciprocal transactions was addressed in AASB 1004 *Contributions*.

BC3 The Board observed determining whether a transaction was reciprocal or non-reciprocal in practice was not always straightforward. Entities found it challenging to determine whether approximately equal value had been provided in exchange to the other party or parties to the transfer, and contended that in many instances the immediate recognition of income in a non-reciprocal transaction did not faithfully represent the underlying financial performance of the entity. Diverse interpretations existed, with some entities recognising transactions with return obligations and specified performance outcomes as reciprocal transactions and some not.

BC4 Constituents were particularly concerned about the income recognition requirements as applied to grants, appropriations and other transfers of assets made on the condition that the not-for-profit entity deliver goods or services to nominated third parties. The Board heard that constituents who are preparers find it difficult to discuss financial information with grantors and donors, and challenging to explain why a not-for-profit 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 a not-for-profit 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 not-for-profit entities.

BC5 The Board observed that the International Accounting Standards Board had completed developments in the accounting for revenue with the issue of IFRS 15 *Revenue from Contracts with Customers* in May 2014. The Board noted it still needed to determine what, if any, amendments and guidance would be required to enable not-for-profit entities to apply the equivalent Australian Accounting Standard, AASB 15. In addition, the Board noted that the application of the performance obligation approach to revenue recognition adopted in AASB 15, using a broader concept of customer, had the potential to resolve some of the issues noted with AASB 1004. Consequently, the Board considered that this was an appropriate time to undertake a project to review the income recognition requirements applying to not-for-profit entities.

BC6 As part of its current project, the Board noted there is currently divergence in practice in the accounting for leases with significantly below-market terms and conditions, such as 'peppercorn' leases where a nominal amount is made as payment to the lessor. Some entities consider AASB 117 *Leases* takes precedence over AASB 1004 and accordingly, currently recognise such leases at nominal values; others consider the reverse applies and recognise such leases at fair value, together with a related contribution. The Board decided its project should also clarify the accounting for such leases.

BC7 The Board also observed that various Australian Accounting Standards required a not-for-profit entity to recognise assets received at fair value (or current replacement cost, in relation to inventories) only where the asset had been acquired for no or nominal consideration (for example, AASB 116 *Property, Plant and Equipment* and AASB 138 *Intangible Assets*). The Board perceived there to be a gap in the accounting for those transactions where an asset has been acquired for consideration that is below market but is more than nominal. The Board noted that under existing recognition and measurement rules at that time, an entity would likely not have recognised any income on the transaction, but measured the asset acquired at the amount of the consideration transferred. The Board considered that, in many instances, such transactions were unlikely to be conceptually different to those for which no consideration was transferred, and consequently decided to also consider the accounting for such transactions as part of this project.

## Previous stages of this project

- BC8 In previous stages of this project, the Board had previously exposed proposals on income recognition requirements for similar transactions as part of the following Exposure Drafts:
- (a) ED 125 *Financial Reporting by Local Governments* (October 2003). This ED also addressed other issues;
  - (b) ED 144 *Proposed Guidance to accompany AASB 1004 Contributions* (November 2005);
  - (c) ED 147 *Revenue from Non-Exchange Transactions (Including Taxes and Transfers)* (February 2006); and
  - (d) ED 180 *Income from Non-exchange Transactions (Including Taxes and Transfers)* (June 2009).
- BC9 However, having regard to constituent feedback and developments in accounting internationally subsequent to the issue of each such Exposure Draft, the Board had decided not to finalise those previous Exposure Drafts. The last such Exposure Draft, ED 180, was closely based on IPSAS 23 *Income from Non-exchange Transactions (Taxes and Transfers)*. At that time, the Board decided, having regard to feedback received on the ED and the progress the IASB was making on a project to replace IAS 18 *Revenue*, not to finalise the proposals set out in ED 180, but instead to refocus its project following issue of IFRS 15 *Revenue from Contracts with Customers*.

## Alternative approaches considered

- BC10 In developing this Standard, the Board considered whether to base the income recognition and measurement principles for a not-for-profit entity on those set out in:
- (a) AASB 1004 *Contributions*;
  - (b) IPSAS, including IPSAS 23;
  - (c) AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*; or
  - (d) AASB 15 *Revenue from Contracts with Customers*.
- BC11 The Board decided not to develop proposals based on the accounting specified by AASB 1004 (as in force at that time), having regard to constituent feedback leading to the Board undertaking the project. In addition, the Board observed that the approach in AASB 1004 does not acknowledge that a non-reciprocal transfer may be made on terms and conditions representative of a liability as defined in the *Framework for the Preparation and Presentation of Financial Statements*.
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## Issue of ED 260

- BC21 The Board's proposals with respect to the accounting for income of not-for-profit entities finalised in this Standard were exposed for public comment in April 2015 as part of ED 260 *Income of Not-for-Profit Entities*. In developing ED 260, the Board considered both the feedback received on ED 180 and the requirements of AASB 15. ED 260 proposed both revisions to the income recognition principles in AASB 1004, and development of guidance and illustrative examples to assist not-for-profit entities in implementing AASB 15.
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- BC24 The Board received feedback on its proposals through receipt of 34 formal comment letters on ED 260. The Board also obtained feedback via means such as email, meetings with constituents, presentations to various bodies and social media. About half the respondents to the Exposure Draft explicitly considered that overall, the proposals would result in financial statements that would be useful to users. Many respondents to ED 260 expressed support for no longer basing income recognition requirements on a reciprocal/non-reciprocal transfer distinction as previously specified by AASB 1004, but on requirements based on satisfying a performance obligation.
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## Finalisation of ED 260

- BC28 Following the consultation period, and after considering constituent comments received, the Board decided to proceed with issuing revised principles for the recognition and measurement of income of not-for-profit entities largely as exposed. The Board considered the identified benefits of the revised requirements to exceed the costs of the revised requirements.

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BC32 The Board considered that, overall, its decisions on this project have not significantly departed from those exposed in a manner that adversely affects entities applying the Standard. The Board decided to finalise its proposals exposed in ED 260 by:

- (a) issuing AASB 1058 to address the accounting for income of not-for-profit entities. The Standard establishes principles for not-for-profit entities that apply to transactions where the consideration to acquire an asset is significantly less than fair value principally to enable a not-for-profit entity to further its objectives, and to the receipt of volunteer services;
- (b) issuing AASB 2016-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities* to add implementation guidance and illustrative examples to AASB 15 to assist not-for-profit entities in applying the Standard. In addition, AASB 2016-8 adds implementation guidance to AASB 9 on the initial measurement and recognition of non-contractual receivables arising from statutory requirements;
- (c) retaining AASB 1004 *Contributions*, amended to exclude transactions now addressed by AASB 1058; and
- (d) issuing AASB 2016-7 *Amendments to Australian Accounting Standards – Deferral of AASB 15 for Not-for-Profit Entities* to defer the effective date of AASB 15 for application by not-for-profit entities.

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## Scope

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### Scope exclusions

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BC49 The Board noted that the requirements of AASB 1058 could be interpreted to apply to restructures of administrative arrangements, which are addressed in AASB 1004 (see paragraph BC173 below). To avoid confusion as to which Standard applies to these transactions, the Board decided to exclude them from the scope of AASB 1058.

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## Recognition and measurement

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### Volunteer services

BC107 AASB 1004 (December 2007) required local governments, government departments, General Government Sectors (GGSs) and whole of government reporting entities to recognise services received free of charge or for nominal consideration, provided the fair value of those services could be measured reliably, and the services would have been purchased if they had not been donated. The Board decided to carry forward these aspects into AASB 1058 as it was concerned that a wide-ranging review of the recognition requirements for volunteer services could take significant time and potentially delay the completion of this project.

BC108 AASB 1004 does not specifically indicate the circumstances in which not-for-profit entities other than those specifically identified can recognise volunteer services. Consequently, not-for-profit entities may elect to recognise volunteer services based on an accounting policy developed in accordance with AASB 108. ED 260 proposed clarifying that not-for-profit entities may elect to recognise volunteer services if the fair value of those services can be measured reliably, without necessarily needing to have been purchased had the services not been donated. In forming the proposal, the Board observed the purchase pre-requisite in AASB 1004 was primarily focused on limiting the scope of volunteer services for which recognition by particular public sector not-for-profit entities is required. The Board considered not-for-profit entities should be able to elect to recognise volunteer services with a fair value that can be measured reliably even if those services would not have been purchased if they had not been donated.

- BC109 The Board noted that carrying forward the treatment of volunteer services from AASB 1004 almost unchanged retains an inconsistency between private sector and public sector not-for-profit entities regarding the scope of the recognition requirements for volunteer services. The Board acknowledged the inconsistency reflects the transfer of recognition requirements for volunteer services to AASB 1004 upon the withdrawal of Australian Accounting Standards for specific types of public sector entity (namely, AAS 27 *Financial Reporting by Local Governments*, AAS 29 *Financial Reporting by Government Departments* and AAS 31 *Financial Reporting by Governments*) in 2007, rather than a difference in information needs of users of financial statements of not-for-profit entities in the private and public sectors.
- BC110 Many respondents to ED 260 were of the view that the requirements with respect to the recognition of volunteer services should be the same for all not-for-profit entities. However, many opined that the recognition of volunteer services should be optional, primarily for cost-benefit reasons. Some encouraged the Board to expedite consideration of whether there was differentiation between entities in the sector to justify different accounting requirements. Others suggested that the treatment and location of information about volunteer services be reconsidered by the Board.
- BC111 The Board considered how to progress its consideration of the accounting for volunteer services, having regard to the feedback received. The Board noted further consideration and due process would be required before it could finalise any broad changes to the current accounting requirements in this regard. Accordingly, the Board decided, as a short-term solution, to finalise the recognition and measurement proposals largely unamended from those exposed. (See also paragraphs BC123–BC124 below.)
- BC112 The Board expects to consider the accounting requirements for volunteer services as part of a separate future project.

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## Disclosure

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### **Disclosure of parliamentary appropriations and other related authorities for expenditure**

- BC131 When developing AASB 1004 (December 2007), the Board decided to defer consideration of whether disclosures of parliamentary appropriations should apply to not-for-profit public sector entities other than government departments, given the short-term nature of its project at that time. The Board noted that in due course, it would consider extending the application of the requirements.
- BC132 As part of this project, the Board reviewed the specified disclosures of compliance with parliamentary appropriations and other externally-imposed requirements required of government departments which had been included in AASB 1004 (now deleted from that Standard). The Board decided, in light of changes in public sector financial management arrangements since originally developing these requirements, to propose extending the scope of disclosures in this regard to include other public sector entities that obtain part or all of their spending authority from parliamentary appropriations.
- BC133 In reviewing the disclosures, the Board acknowledged constituent concerns that the interaction between two of the specified disclosures was unclear, as the scope of paragraph 64(e) of AASB 1004 was broader than the scope of paragraph 64(d). The Board decided to clarify its requirements in this regard by proposing in ED 260:
- (a) not to carry forward the text of paragraph 64(e) into AASB 1058; and
  - (b) to require disclosure of the financial consequences of an unauthorised expenditure.
- BC134 Respondents to the ED were generally supportive of the Board's proposals in this regard. In its redeliberations, the Board noted a concern raised that by extending the application of these disclosure requirements beyond government departments some might interpret the disclosure requirements as applying to for-profit entities in the public sector. The Board observed that the scope of AASB 1058 is limited to not-for-profit entities and therefore for-profit public sector entities would not be subject to these disclosures.
- BC135 The Board discussed a concern whether the proposed disclosure requirements duplicate existing disclosures in AASB 1055 *Budgetary Reporting*. The Board reaffirmed its view that these disclosures contain fundamentally different requirements from AASB 1055 and should be retained, as the disclosures are focused on information concerning how appropriations and other advances received have been expended, rather than the more broadly based requirements in AASB 1055 for actual to budget variance analysis (see paragraph BC28 in AASB 1055).

- BC136 In addition, as part of its deliberations, the Board discussed whether to relocate disclosures about a government department's compliance with parliamentary appropriations and other externally-imposed requirements from AASB 1004 to AASB 1054 *Australian Additional Disclosures*, rather than this Standard. The Board concluded it would be more user-friendly to include these disclosure requirements in AASB 1058 given the nexus between the income of government departments and appropriated amounts.
- BC137 Having regard to the feedback received, the Board decided to finalise the disclosure in this regard largely as exposed in ED 260.

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## Other

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### Contributions by owners

- BC168 In developing ED 260, the Board noted the concerns of some constituents with the existing definition of "contributions by owners" (see Appendix A of AASB 1058) and Interpretation 1038 that includes for-profit public sector entities within its scope. The Board observed:
- (a) the IASB has not defined a similar term employed within the definition of 'income' in IFRS Standards; and
  - (b) the IPSASB's Public Sector Conceptual Framework includes a broader definition of 'ownership contributions' than that in Australian Accounting Standards.
- BC169 Acknowledging constituent concerns about application of the term, the Board decided to invite comment on the defined term "contributions by owners" as part of this project. The Board did not make a specific proposal regarding the definition of "contributions by owners". Instead, ED 260 illustrated what a replacement Standard for AASB 1004 would look like without that definition and particular related guidance, and posed related questions including whether a definition of 'contributions by owners' is still necessary, or appropriate.
- BC170 In responding to the ED, constituents noted the definition in AASB 1004 can be problematic, identified a need for a definition of contributions by owners and expressed their support for applying the IPSASB definition or using the IPSASB definition as the basis for an Australian definition. Many respondents considered a definition was necessary to minimise diversity in practice.
- BC171 In addition, the majority of respondents to ED 260 responding on this topic supported the withdrawal of Interpretation 1038.
- BC172 Having regard to the feedback received, the Board considered whether to:
- (a) withdraw and not replace the current definition in AASB 1004 and Interpretation 1038;
  - (b) replace the current definition in AASB 1004 with the definition of ownership contributions adopted by the IPSASB, and separately consider whether to retain an amended Interpretation 1038; or
  - (c) address the accounting for contributions by owners as part of a separate project.
- BC173 The Board was conscious of the need to finalise its proposals on other aspects of its current project in a timely manner. The Board considered that developing any amendment to the definition, including ensuring adequate due process, would delay finalisation of its current project. Accordingly, the Board decided to progress consideration of 'contributions by owners' and the related requirements as part of a separate project. Consequently, the Board decided to retain, for the interim:
- (a) the terms 'contributions' and 'contributions by owners' as presently defined in Australian Accounting Standards;
  - (b) the requirements specified in AASB 1004 and AASB Interpretation 1038 *Contributions by Owners Made to Wholly-Owned Public Sector Entities* with respect to contributions by owners and distributions to owners; and
  - (c) the requirements specified in AASB 1004 with respect to contributions by owners and distributions to owners, including those arising in relation to restructures of administrative arrangements.

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