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Association of Australian Medical Research Institutes

Concerns with the Application of AASB 1058 and AASB 15 Grant Accounting for Medical Research Institutes

The principal concern with application of the new accounting standards (AASB 1058 and AASB 15) pertains to the recognition of grant income for research activities by medical research institutes. Feedback from within the sector is that there are differing views from audit firms as to the application of the new accounting standards in this regard which creates uncertainty and the potential for inconsistent approaches being taken to the recognition of grant income.

A number of medical research institutes are concerned that some of the grant agreements they administer may be determined to not satisfy all of the requirements of AASB 15 so as to permit income to be matched with expenditure over the term of the contract (which may span multiple reporting periods). The impact of this would be that income is recognised up front or at the end of a grant, thereby affecting the bottom line between financial years in a manner which may generate concern from donors and funders about the financial sustainability of the organisation (for example, significant surpluses one year and significant deficits in other years based on when grant income is recognised).

In applying AASB 15, it is understood that the following three requirements must be met in relation to grant funding received by medical research institutes:

A. Contract is in place with a "customer" to provide goods or services.
B. Contract must create enforceable rights and obligations; and
C. Contract must include performance obligations that are sufficiently specific.

A. Contract is in place with a "customer" to provide goods or services

The core business of medical research institutes is undertaking research. In entering contracts for the provision of funding to research institutes, funders and donors (the "customer") are procuring the institute to undertake research in a particular field for the intent of pursuing new discoveries, increasing knowledge and advancing solutions to health problems. Even where a determination is made that the undertaking of research pursuant to a grant agreement constitutes a "service" being undertaken for the customer, this determination may be questioned given that most research projects do not yield outputs which can be sufficiently quantified or qualified so as to be accurately described as being a "service" which is delivered for the customer.

B. Contract must create enforceable rights

It is common for grant agreements with donors and funders to be constituted through legally enforceable contracts that establish rights and obligations on both parties to the contract. Most grant agreements involving medical research institutes and funders, or donors will satisfy this requirement.

C. Contract must include performance obligations that are sufficiently specific

There is some confusion around whether research agreements meet the requirement of having performance obligations pertaining to the delivery of goods or services that are *sufficiently specific*. Determining this requires the use of judgement, the exercise of which creates the potential for differing approaches to be taken. Where the performance obligations are deemed not to be sufficiently specific, the transaction will likely not meet the requirements of AASB 15 and the revenue may need to be recognised immediately rather than over the term of the grant.

In assessing this requirement, AASB 15 para 22 requires that at contract inception an entity considers the goods or services explicitly promised in a contract and identifies as a performance obligation each promise or bundle of promises to transfer a distinct good or service to the customer. There must be a

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promise to transfer a good or service to a customer for a performance obligation to be identified. Stipulation of time is not on its own sufficiently specific to establish the existence of a performance obligation, neither is a statement of intent.

In determining whether grant agreements between medical research institutes and donors, or funders, satisfy the requirement of having a sufficiently specific performance obligation, it has been suggested that one (or more) of the following outcomes must be delivered to the "customer":

- Transfer or license IP to donor;
- Provide good or service to the customer; and/or
- Publish all research for all researchers to use – this may occur during or at the conclusion of a research project depending on the significance of research outcomes. However, this is not always the case and, in many instances, research will not result in the publication of outcomes.

Transfer or license IP to donor

Transfer of IP relating to research undertaken pursuant to a grant does not occur with funders or donors. Licensing (in the form of a research license back) may be required by some funders (e.g. government); however, this is rarely required by donors. Accordingly, the transfer or licensing of IP as the basis for satisfying the requirement for a sufficiently specific performance obligation is unlikely to be able to be relied upon.

Provide good or service to the customer

As stated previously, there has been suggestions that undertaking research pursuant to a grant agreement constitutes a "service" being undertaken for the customer. This determination may prove problematic and be subject to questioning given that most research projects do not yield outputs which could be sufficiently quantified or qualified to accurately represent a "service" that is delivered to the customer.

Publish all research for all researchers to use

Advice received appears to support that the publication of research by a medical research institute for the benefit of all researchers would constitute a sufficiently specific promise. However, it is unclear as to the rationale of this assessment based on the following considerations:

- Publication of research delivers no distinct "good" or "service" to the funder or donor, nor does it provide any benefit or value which reciprocates fully or partially the consideration that has been paid by the funder or donor. Funders and donors will not typically require the publication of research outcomes as a prescribed deliverable within grant agreements;
- Not all research activities undertaken pursuant to grants result in publishable research outcomes. This may be a consequence of the research not being sufficiently progressed as at the end of a funding agreement to justify publication.
- Publishing all research creates a risk of disclosing valuable intellectual property into the public arena which may prevent subsequent commercialisation.

It is evident that funders and donors are generally seeking performance obligations and outcomes from research grants that do not include the publication of research outcomes for the benefit of all researchers. The deliverables sought by funders and donors will normally relate to the application of grant funding towards research which facilitates the pursuit of new discoveries and the advancement of knowledge in relation to specific health problems. Given that positive impacts on the health and wellbeing of patients can take many years of medical research and will usually involves significant collaboration between research organisations (nationally and internationally), it is difficult to identify tangible health outcomes from a single research project which is being funded by a donor or funder. Accordingly, it may be more appropriate to consider other outcomes as measures of whether a grant includes sufficiently specific performance obligations. Potential outcomes which may constitute specific performance obligations for the purposes of AASB 15 include:

- Funds provided pursuant to the grant are exclusively used for a specific research purpose;
- Provision of regular reports to the donor or funder on the progress of research activities;

- Successful performance against agreed research milestones and deliverables;
- Evidence of progress being made towards making new discoveries in a field of research; or
- Evidence of progress being made in the translation of research into outcomes which demonstrate the advancement of knowledge in regards to specific health problems.

APPENDIX: MEDICAL RESEARCH INSTITUTES – FUNDING ARRANGEMENTS

GOVERNMENT RESEARCH COUNCIL FUNDING

Funding source	• Funders are primarily the National Health and Medical Research Council (NHMRC), but occasionally the Australian Research Council.
How funds are awarded	• Researchers from eligible research organisations (MRIs, universities and hospitals) apply to the Funder.. • Researchers nominate an administering research organisation. • Funder makes funding decisions based on scientific quality.
Funds awarded to	• Funding is awarded to the specific researchers named on the funding application. • Researchers can transfer the grant from one administering research organisation to another (permission needed from Funder but nearly always given).
Funding agreement with	• The executed funding agreement is between the funding body and the nominated medical research institute as the administering institution. Researchers are named as Chief Investigators in the funding agreement.
Restrictions associated with funding	• Funding can only be expended on the research activities outlined in the approved funding application. The MRI cannot use the funding for any other purpose. • Funding cannot be used for any MRI overheads incurred in supporting the research (e.g. capital expenditure, IT, HR, and other corporate functions). • Claw-back provision in funding agreement which enables the funds awarded to be recovered by the Funder (e.g. breach of funding rules, failure to achieve performance milestones or discontinuation of project). • Funding is usually staged and is subject to performance objectives and/or milestones being met. • Unspent funds must be returned to the Funder.
Role of MRIs with respect to the funding	• Medical research institute effectively holds the research funding awarded by the funding body for the specific researchers named on the grant application. This is often across multiple financial years. The funds are only recognised as earned income in direct proportion to the expenditure by the specific researcher on direct research activities (eg researcher salaries, research consumables, study participant costs, travel etc). • If the applicable Chief Investigators elect to transfer the research funding to another administering institution, the outgoing research organisation must transfer any and all unexpended funds to the research organisation that is the new administering institution.

GOVERNMENT AND NON-GOVERNMENT RESEARCH GRANTS

Funding source	• Numerous sources including Federal and State Governments, corporates, PAFs, charitable foundations and not-for-profit organisations.
How funds are awarded	• Can be nationally or state competitive process where funder competitively assesses applications and makes funding decisions based on scientific quality and/or delivery of agreed research outcomes.

	• Can be a direct funding arrangement based on scientific quality and/or delivery of agreed research outcomes.
Funds awarded to	• Funding is awarded to the medical research institute.
Funding agreement with	• Executed funding agreement is between the Funder and the medical research institute.
Restrictions associated with funding	• Funding can only be expended on the research activities outlined in the funding proposal. The MRI cannot use the funding for any other purpose. • Direct research funding cannot be used for any MRI overheads incurred in supporting the research (e.g. capital expenditure, IT, HR, and other corporate functions). • Claw-back provision in funding agreement which enables the Funds to be recovered by the Funder (e.g. breach of funding rules, failure to achieve performance milestones, discontinuation of project etc). • Funding is usually staged and subject to performance/milestones being met. • Unspent funds must be returned to the Funder .
Role of MRIs with respect to the funding	• Medical research institute effectively holds thefunding in trust for the researcher until the time it is needed to be expended on medical research activities. This is often across multiple financial years.

CONTRACT RESEARCH AND CONSULTANCY WORK

Funding source	• Numerous sources including government, pharmaceutical companies, other corporates, PAFs, charitable foundations and not-for-profit organisations.
How funds are awarded	• Contract entered into between the Funder and the medical research institute. • Funding is received by the medical research institute.
Funds awarded to	• All or a portion of the funds (including cost recovery and profits) from the contract research or consultancy work are retained by the medical research institute. • For some medical research institutes, a portion of the profits from the contract research or consultancy work belong to the researcher (pursuant to Institute Policy) and are held by the medical research institute in trust for the researcher. These funds can be transferred to another medical research institute should the researcher move to a new research organisation.
Funding agreement with	• The executed contract is between the Funder and the medical research institute.
Restrictions associated with funding	• Funding can only be expended on the research activities specified in the contract. The MRI cannot use the funding for any other purpose. • Claw-back provision in funding agreement which enables the Funds to be recovered by the Funder (e.g. breach of funding rules, failure to achieve performance milestones, discontinuation of project etc). • Funding is usually staged and subject to performance/milestones being met. • For medical research institutes that provide a portion of the profits from the contract research or consultancy work to the researcher, these funds are held by the medical research institute can only be used by the researcher for research related activities.

Role of MRIs with respect to the funding	• Medical research institute holds the funds on behalf of the researcher until the researcher is ready to use them to fund medical research related activities. This is often across multiple financial years. • For medical research institutes that provide a portion of the profits from the contract research or consultancy work to the researcher, where the researcher elects to transfer to another administering institution, the outgoing research organisation must transfer any and all funds which belong to that researcher to the new administering institution.

COMMERCIALISATION INCOME AND ROYALTIES

Funding source	• Commercialisation deals and royalties from licensing agreements. • Researchers are encouraged to undertake commercialisation activities. • Commercialisation agreements are between the MRI and the commercial entity.
How funds are awarded	• Contract entered into between the Funder, the researchers (inventers and co-inventers) and the medical research institute. •
Funds awarded to	• Portion of income / royalties paid to researchers (inventers and co-inventers) as personal income. • Portion of income / royalties retained by the medical research institute. • For some medical research institutes, a portion of the income / royalties are provided to the researcher's project (pursuant to Institute Policy) and are held by the medical research institute in trust for that research project. These funds can be transferred to another medical research institute should the researcher move their research project to a new research organisation.
Funding agreement with	• Initial receipt of funds is from a commercialisation agreement. • How funds are distributed and expended is subject to an MRI's specific policy and guidelines. • MRIs might have employment contracts which specify that researchers (inventers and co-inventers) are entitled to any distributions from commercialisation deals and royalties for medical research activities.
Restrictions associated with funding	• None with respect to the source of the funding, but medical research institutes have their own guidelines on how the funding can be used. For example, funds can only be used to fund new research related activities.
Role of MRIs with respect to the funding	• • For medical research institutes that provide a portion of the profits from the contract research or consultancy work to the researcher, where the researcher elects to transfer to another administering institution, the outgoing research organisation must transfer any and all funds which belong to that researcher to the new administering institution.

PHILANTHROPIC GIFTS

Funding source	• Numerous sources including corporates, family trusts and individuals.
How funds are awarded	• Gift provided on the basis of scientific quality and/or delivery of agreed research outcomes.
Funds awarded to	• Funding is awarded to the medical research institute.

Funding agreement with	• Executed gift agreement is between the Funder and the medical research institute.
Restrictions associated with funding	• Funding pursuant the gift can only be expended on the research activities outlined in the gift agreement and must deliver specific performance outcomes. The MRI cannot use the funding for any other purpose. • Funding related to the gift is often to be expended across multiple financial years. • Claw-back provision in funding agreement which enables the Funds to be recovered by the Funder (e.g. breach of gift agreement, failure to meet performance requirements). • Funding provided as part of the gift may be paid upfront or staged and subject to performance/milestones being met. • Unspent funds may be required to be returned to the Funder.
Role of MRIs with respect to the funding	• Medical research institute effectively holds the funding in trust for the researcher until the time it is needed to be expended on medical research activities. This is often across multiple financial years.