

31 October 2019

Australian Accounting Standards Board
Podium Level 14,
530 Collins Street,
Melbourne VIC 3000

Dear Board Members

AASB 2019-X Amendments to Australian Illustrative Examples for Not-for-Profit Entities accompanying AASB 15

We make the following comments and observations on the above exposure draft as well as the related AASB Staff FAQ document.

For the reasons set out below:

- i) We **disagree** with the proposed amendments to Example 4A of AASB 15 as well as the AASB Staff FAQ dealing with the same subject matter; and
 - ii) the AASB should **not proceed** with its amendments to Example 4A of AASB 15.
1. The amendments and Staff FAQ document do not appropriately clarify the operation of AASB 15 and are likely to result in conflict with the requirements of AASB 15.

Flowchart 3 of the Staff FAQ illustrates the requirements of AASB 15 in assessing whether a performance obligation is satisfied over time or a point in time. The AASB has stated that the conditions in paragraph B4 of AASB 15 cannot be considered in making this assessment to research grants where the answer is 'clear' (BC3 of AASB 2019-X).

We note the following paragraphs of IFRS 15:

- BC126 The boards observed that there may be service-type contracts in which it is unclear whether the customer receives and consumes the benefit of the entity's performance over time. This is because the notion of 'benefit' can be subjective. Consider, for example, a freight logistics contract in which the entity has agreed to transport goods from Vancouver to New York City. Many respondents suggested that the customer receives no benefit from the entity's performance until the goods are delivered to New York City. However, the boards observed that the customer does benefit from the entity's performance as it occurs because if the goods were delivered only part way (for example, to Chicago), another entity would not need to substantially re-perform the entity's performance to date—that is, another entity would not need to take the goods back to Vancouver to deliver them to New York City. The boards observed that, in those cases, the assessment of whether another entity would need to substantially re-perform the performance completed to date can be used as an objective basis for determining whether the customer receives benefit from the entity's performance as it is provided.

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In the scenario described in BC126 the IASB acknowledges that there is only one performance obligation – to deliver the goods to New York. This is similar to a research contract that contains only one performance obligation – to deliver (or make publicly available) completed research findings to the customer at the *completion* of the project.

Applying the AASB's logic described in BC3 of AASB 2019-X to this scenario, some audit firms have suggested that it is clear the customer (donor) does not simultaneously receive and consume the research service because the research organisation only satisfies its performance obligation by publishing its research findings and data at the end of the project and, hence, paragraph 35(a) is not satisfied.

However, as the IASB itself notes in BC126, in the scenario described the customer *does* benefit from the entity's performance as it occurs because if the goods were delivered only part way (for example, to Chicago), another entity would not need to substantially re-perform the entity's performance to date. In the same way that if a research organisation ceased the project and transferred all the data and information collected to date to another research organisation to complete the project, the second entity would not have to substantially re-perform the performance completed to date.

As illustrated above, in those circumstances the failure to consider the application of paragraph B4 to the specific facts and circumstances of research contracts can result in an incorrect application of AASB 15.

Appendix B Application Guidance to AASB 15 states "This appendix is an integral part of AASB 15. It describes the application of paragraphs 1–129 and has the same authority as the other parts of AASB 15". Hence, paragraph B4 is authoritative in assessing whether a performance obligation is satisfied over time and cannot be ignored.

In our opinion, contractual terms that result in the transfer of all research data and information obtained to date to a new supplier should the research organisation be either unable to complete the project or agrees to transfer the project to another party for completion must be considered as part of the paragraph 35(a) assessment.

In other words, what might appear *prima facie* as 'clear' still requires entities to consider all relevant facts and circumstances of the contract and apply all relevant guidance (including paragraph B4) within AASB 15 in order to make an appropriate assessment.

Furthermore, as stated in BC127:

The boards decided that an entity should disregard any contractual or practical limitations when it assesses the 'simultaneously receives and consumes' criterion and whether another entity would need to substantially re-perform the performance completed to date. This is because the objective of this criterion is to determine whether control of the goods or services has already been transferred to the customer. This is done by using a hypothetical assessment of what another entity would need to do if it were to take over the remaining performance. Thus, actual practical or contractual limitations on the remaining performance would have no bearing on the assessment of whether the entity has transferred control of the goods or services provided to date. (emphases added)

We note that the IASB makes reference to a hypothetical assessment if the contract was transferred, not whether in practice such transfer requires consent of either the customer or supplier.

Hence, in our opinion, entities must take into account the conditions in paragraph B4 in making each and every assessment of whether paragraph 35(a) is satisfied. Failure to do so may result in incorrect assessments being formed. In our opinion, AASB guidance that conflicts with this view may result in a conflict with, and non-compliance with, IFRS 15.

As not-for-profit entities are unlikely to delve into the Basis for Conclusions of IFRS 15 in order to form their assessment on the application of AASB 15 to individual research contracts, we make the following recommendation.

2. Any amendments to Example 4 of AASB 15 should illustrate a scenario where paragraph B4 of AASB 15 *would* be applied.

BC3 of AASB 2019-X states that “if it is clear the customer (the donor) simultaneously receives and consumes the research service, paragraph 35(a) is satisfied”.

The AASB’s proposed deletion of the phrase “another entity would not need to substantially re-perform the research completed to date by the institute if that other entity were to fulfil the remaining performance obligation to the donor (paragraph B4)” in Example 4A is justified on the basis that the application of paragraph 35(a) to the fact set in the example is ‘clear’.

However, the limited fact set contained in Example 4A has been designed to support that conclusion. Providing illustrative examples that merely restate this principle is not, in practice, helpful to not-for-profit entities.

Notwithstanding our comments at point 1 above:

- i) the AASB’s proposed amendment means that the illustrative examples would no longer illustrate a scenario where paragraph B4 *would* be applied; and
- ii) In our opinion, it would be more useful to not-for-profit entities for the AASB to include a scenario similar to that described in BC126 –BC127 of IFRS 15 where paragraph B4 of the Standard would be applied to a research contract.

3. The amendments illustrate a scenario that is unrealistic or do not occur in practice. Consequently, the amendments are of no practical use.

The AASB has stated that the illustrative examples have been developed by creating hypothetical fact sets that results in each of the outcomes in paragraph 35(a) – (c) and are not designed to reflect circumstances that occur in practice. For example, based on our experience in the research sector, most research agreements do not contain a specific condition that the entity ‘contemporaneously publish’ its findings as they are obtained.

In our opinion, the scenarios described in the Example 4A and the AASB Staff FAQ, if they ever occurred, would result in the conclusions described in those examples. However, some audit firms have approached the logic in reverse. That is, paragraph 35(a) of AASB 15 can *only* be applied where the entity’s actual fact set is identical to fact set described in the illustrative example.

4. The amendments do not incorporate or reflect the explanations and representations provided by the AASB at various roundtables and sector outreach sessions.

We are concerned that explanations provided by the AASB to participants at outreach sessions are not illustrated or reflected in the proposed amendments.

For example, a number of stakeholders are confused by the AASB’s use of the phrase “contemporaneously publish” in the proposed amendment to Example 4A and sought clarification of that term. Although the AASB indicated that the simultaneous receipt and consumption of benefits

could be achieved through other means, those alternatives have not been reflected or explored in either the amendments to Example 4A or the Staff FAQ examples.

In addition, the AASB stated that as long as the underlying deliverables (research data, IP, etc) are made available at the request of the grantor as it is being undertaken, then this can demonstrate continuous transfer and that the entity would not need to demonstrate that the donor requests access, only that it is made available if asked (ie, stand ready to provide it). However, some audit firms believe that the entity has to demonstrate that research findings have been provided to the customer/beneficiary.

These matters have led to interpretation disagreements between parties that attended AASB outreach sessions and those that did not.

In our opinion:

- i) the AASB's activities, although well intentioned, have not achieved its objectives and have increased diversity in practice;
- ii) Example 4A of AASB 15 as previously drafted is not incorrect; and
- iii) the AASB need not proceed with its amending standard to AASB 15.

However, if the AASB intends to amend Example 4A, it should only do so after incorporating the above matters. In such case, it should make those further amendments available for public comment.

Finally, we reiterate our concerns on the Staff FAQ and the Board's direction on this matter which were communicated to the Board on 28 May 2019.

Sincerely

Nexia Australia Pty Limited



Martin Olde
Technical Director