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Ms Kris Peach
Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West
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29 April 2016

Invitation to comment on AASB Exposure Draft 270 *Reporting Service Performance Information*

Dear Ms Peach

Ernst & Young Australia ('EY' or 'we') is pleased to provide comments on the AASB's Exposure Draft ('ED') 270 *Reporting Service Performance Information* ('ED 270').

EY is generally supportive of the AASB's project to establish a framework to be used by not-for-profit ('NFP') entities when reporting service performance information for the following reasons:

- Improves accountability of NFP entities in demonstrating that they have met their service performance objectives
- Improves decision-making and may help to resolve inefficiencies within a NFP entity, where consistent outputs/outcomes-based information is available
- Improves consistency of an NFP entity reporting service performance information between reporting periods and between NFP entities with similar activities and similar service performance objectives
- Assists in enhancing comparability of a NFP entity's performance between reporting periods and between NFP entities with similar activities and similar service objectives. However, with the variability in NFP activities and the current level of guidance on how to measure outcomes, challenges will still remain in achieving comparability between all NFP entities.

Having said this, we do note that the draft standard in its current form would be incredibly challenging to implement and a significant amount of additional work and outreach would still be required to make this proposal operational. Specifically, we note the following:

- Additional guidance required: this will be needed to help clarify some of the requirements and to assist NFP entities apply and put these principles into practice in their reporting
- Further cost versus benefits analysis: The time and costs associated with the initial capability to meet the requirements of the draft standard would vary considerably by entity type and size. More outreach with NFP preparers to better understand the benefits and costs of complying would be both beneficial and essential.
- Interaction with other reporting requirements: Given some entities, e.g., some public sector NFP entities, are currently subject to other reporting requirements. Given this, additional work will be required to determine whether the application of the requirements of ED 270 would lead to:
    - Duplication of information
    - Multiple handling of data
    - Increased costs and/or
    - Inefficiencies

  and/or whether it may result in conflicting information being reported. If such additional work would cause a prolonged delay of this standard, the Board could consider using a phased approach, e.g., by mandating application to private sector NFP entities first while completing this additional work for public sector NFP entities.

- Further consideration of the NZASB's service performance reporting proposals: As highlighted by the Board in the BC to the ED, the NZ Accounting Standards Board ('NZASB') has issued a draft proposal on service performance reporting. While there are some deliberate differences from that proposal in the AASB's ED, we do think it would be worth reconsidering this, as feedback suggests that the NZ proposed framework is potentially more user friendly and may be considered less onerous to comply with.

While we would agree that mandatory application of the proposed requirements would be needed if the benefits outlined above are to be realised, we believe that a differential reporting regime with phased application would be worth considering as a way to improve the successful implementation of the standard and to address some of the challenges raised by various parties. For example, we would recommend that for NFP entities below a certain threshold (e.g., in terms of size, type and nature of operations), that the Board considers a less onerous approach and/or allow such entities to be exempt (partially or fully) from the requirements of the proposed standard.

Our detailed responses to specific questions in the invitation to comment are set out in the Appendix to this letter.

We would be pleased to discuss our comments further with you. Please contact Meg Fricke (meg.fricke@au.ey.com, 03 – 9288 8229) or Serene Seah-Tan (serene.seah-tan@au.ey.com, 08 – 9429 2348) if you wish to discuss any of the matters in this response.

Kind regards,

Tracey Waring
Partner, Oceania IFRS desk leader
Melbourne

Appendix – Specific matters for comment

1. Paragraph 20 proposes the principles for reporting service performance information. These principles state that an entity reports service performance information that:

(a) is useful for accountability and decision-making purposes;

(b) shall be appropriate to the entity's service performance objectives;

(c) clearly shows the extent to which an entity has achieved its service performance objectives; and

(d) should enable users to assess the efficiency and effectiveness of the entity's service performance.

Do you agree with these principles? Why or why not?

EY's response:

We agree in general with the principles in the proposed standard. We believe that the proper application of these principles and the associated Qualitative Characteristics will positively assist in meeting the Board's objective of NFP entities providing service performance information on a more consistent basis, which will improve accountability and potentially enhance comparability amongst certain entities. We also consider that the provision of this information will assist NFP entities better satisfy their accountability obligations.

We concur with the view that service performance information reported in accordance with the principles and the associated Qualitative Characteristics and in conjunction with an entity's financial information as reported in its financial statements will provide relevant, reliable and understandable information about a NFP entity's financial and non-financial performance. This will assist key stakeholders and users of this information to better assess a NFP entity's overall performance.

We also note the following considerations in regard to Paragraph 20:

Connection to the Qualitative Characteristics: We would recommend that consideration be given to further align the Qualitative Characteristics (Paragraphs 25-29) with the principles (Paragraph 20). For example, the Qualitative Characteristic of materiality is critical to the overall application of the standard and strongly influences principles (a) and (b). This will assist the NFP entity in understanding the correlation between the two sections and better able to implement the standard.

Public Accountability: We would also recommend that the Board consider discussing *public accountability* for determining when and what service performance information should be reported for public sector NFP entities. In other words, the service performance information reported may be wider than the scope of what an entity is accountable for to its funders.

2. It is proposed that the [draft] Standard will be applicable to NFP entities in both the private and public sector. The performance of these entities cannot typically be evaluated from the financial statements alone. Accordingly, users of NFP entity reporting require further information for accountability and decision-making purposes.

Do you agree that it is appropriate that the [draft] Standard apply to NFP entities in both the private and public sectors? Why or why not?

EY's response:

Public sector considerations:

Yes, conceptually we would agree that the reporting of service performance information is important for NFP entities in both the private and public sectors as the drivers for disclosure and the information needs of users are generally of equal significance across both sectors. Furthermore, for public sector NFPs, the various forms of existing legislation for currently reporting service performance are inconsistent between the states and territories. While some public sector NFP entities are already subject to certain reporting requirements on some aspects of their service performance, it is considered that these current requirements have potentially not been able to sufficiently meet user needs in terms of the type and depth of information and consistency across entities. Given this, it is considered that a consistent framework and more guidance in this area of reporting would be welcomed and some would assert is needed. For instance, it would be easier to make comparisons between the performance of a private institution versus a state-funded institution by looking at their outcomes and outputs if their service performance reports were prepared on a consistent basis.

However, we are not convinced that the draft standard as it currently stands would adequately meet users' needs. For public sector NFP entities with complex and wide-ranging operations, more tailored outcomes reporting would be more relevant for users and hence the requirements of this proposed standard would need to be considered in light of these other needs.

As noted by the Board, some public sector entities may already be subject to service performance reporting requirements imposed by another authority. For example, some public sector entities are required by the *Public Governance, Performance and Accountability (PGPA) Act 2013* to prepare annual performance statements that provide information about the entity's performance in achieving its purpose. Given this, we are cognisant of the concerns expressed by some preparers about the potential overlap of current reporting requirements and the proposed service performance reporting requirements. Duplication of information could increase costs and lead to multiple handling of data which may then lead to inefficiencies, and/or may result in conflicting information being reported. In addition, for public sector NFP entities in jurisdictions without existing service performance reporting, there will be additional upfront work to determine these objectives and associated reporting parameters for efficiency and effectiveness.

Consequently, we believe it would be helpful for preparers and users alike if areas of potential duplication, development and inconsistency are fully considered and addressed in the finalisation of the standard. Having said this, in order to avoid prolonged delay of application of the standard, the Board could also consider implementing the standard using a phased approach. In other words, mandate application for private sector NFP entities in the first phase whilst performing further work to identify, and where possible eliminate, duplicate reporting requirements for the public sector NFP entities.

Private sector considerations:

There will likely be some challenges to consider when making this applicable to private NFP entities. The definition and discussion of service performance objectives, and what has to be reported, assumes that the NFP entity actually has detailed service performance objectives. This might be generally true in the public sector, because of other budgeting/planning/reporting requirements already in place, but it is possible that many private NFP entities (especially smaller ones) will not have detailed service performance objectives. They are more likely to have a few broad social objectives, and may need to create more detailed and specific objectives for the purposes of this proposed standard.

Added to this, there are certain aspects of the requirements that would likely be challenging for private NFP entities to comply with. For example, the requirements to report on efficiency and effectiveness are likely to be particularly onerous and difficult for private NFP entities. This is because the detailed cost allocations needed to report on efficiency, and the range of external factors that will impact on effectiveness, may require processes and capability that the smaller private NFP entities don't have. Therefore, this is likely to make the proposal more costly and difficult to implement for these NFP entities. Given this, as mentioned in our cover letter, we suggest a differential reporting framework be considered to potentially provide entities of a certain size, type and nature either a partial or full exemption from applying this standard either permanently, or over the shorter term. This could go some way to reduce the burden of compliance with the requirements of the proposed standard.

Overall considerations:

As part of the process of working towards an overall framework for reporting service performance information, we recommend that the Board carefully consider the scope and phasing of the final standard both in the short term and over the longer term. Essentially what this means is that rather than go for what might be considered to be the 'gold standard' in one huge step, introducing something which would be considered less onerous might be a good first step, especially to get some service performance reporting in the private NFP sector without overloading them with detailed, prescriptive requirements all at one point in time.

Finally, we would also suggest that in the process of finalising this proposed standard, the Board reconsiders the developments of the NZASB project on service performance reporting. For instance, the NZASB has excluded the requirement to report on efficiency in order to simplify an entity's reporting requirement. In this context, we concur with the Board's objective expressed in BC 14 to continue using similar principles to guide the development of requirements in the respective projects undertaken by the AASB and NZASB.

3. The AASB discussed whether this [draft] Standard could be applied by for-profit entities at a future date. The Board noted that the principle objectives of NFP entities and for-profit entities are different and, therefore, user needs are potentially different. However, the Board is of the view that users of for-profit reporting may also benefit from for-profit entities reporting service performance information.

Do you agree that the application of this [draft] Standard could be extended in the future to include for-profit entities? Why or why not?

EY's response:

While we conceptually agree that there may be some potential benefits from extending application of similar principles to for-profit entities at some point in the future, we do have some strong reservations as whether the proposed standard in its current form would be appropriate.

While there are demands on for-profit entities for non-financial information more generally and specifically around an entity's performance in broader terms than appears in such an entity's financial statements (e.g. sustainability, environmental, social and governance reporting ('ESG') and integrated reporting), we don't consider that this is the same thing as service performance. For example, the current proposal notes that service performance information is useful because NFP entities have the primary objective of providing goods or services for community or social benefit, and this is consistent with the definition of service performance. All of the proposed requirements around reporting outputs, outcomes, objectives, etc, are built around service performance, i.e., a specific type of performance. But for-profit entities have a primary objective of making a profit, and any service performance objectives are very much secondary to the primary profit objective.

Having said this, many for-profit entities are currently reporting non-financial information with regard to performance in relation to purpose and outcomes and are not applying a consistent set of principles. It is difficult to determine if such information is consistently prepared and reported and comparable. Consequently, requiring for-profit entities to apply a consistent set of principles would help to ensure that there is a greater onus on these entities to review their current approach to non-financial disclosures and draw distinction to outcomes and purpose. This would help achieve greater consistency in preparation and reporting and would enable greater comparability with other for-profit entities and NFP entities (where relevant).

While we acknowledge that some of the principles and concepts of the ED could be extended, at a very broad level, to the for-profit sector, we believe that it is not clear whether and how the proposed standard, as currently drafted, could actually be extended. Consequently, we have some reservations as to whether this would be possible without a lot of rework, which would potentially need to occur as a separate project and which would likely result in a very different standard. This would be required given the different objectives and the broader non-financial disclosures already provided by many for-profit entities.

4. The AASB discussed whether the requirements of this [draft] Standard should apply to entities that prepare consolidated financial statements including whole-of-government (WoG) and the general government sector (GGS) financial statements. The Board decided that if the [draft] Standard did not apply to entities preparing consolidated financial statements, some important information might not be reported, particularly if a controlled entity was not required to apply this [draft] Standard. Further, it was noted that some governments prepare a strategic plan for the WoG (not just individual agencies). Therefore, this [draft] Standard could be applied in relation to those WoG plans.

Do you agree that this [draft] Standard should apply to all NFP entities that prepare consolidated general purpose financial statements (including WoG and GGS financial statements)? Why or why not?

EY's response:

We agree that to the extent that the information required by this draft standard is not already reported in other forms of reporting by WoG and GGS, the principles and requirements of this draft standard could be a useful framework for the preparation and reporting of service performance outcomes and output in these types of reports. Although it may be difficult to identify the scope overlap and potential inconsistencies with other reporting requirements, such as the PGPA, and this draft standard, it would be helpful to identify where these may exist and guidance be provided to preparers as to the important incremental information to be reported for users of service performance reports.

Furthermore, it would be helpful to clarify in the final standard whether a controlling entity that prepares consolidated financial statements is required to include service performance information in relation to controlled entities, to the extent the information does not overwhelm and is useful to users, which seems to be a departure from the IPSASB's RPG 3 *Reporting Service Performance Information* (RPG 3 paragraph 28 and BC18).

In addition, we believe that it would also be important to link service performance reporting at different levels of entities within government, to the principles of budgetary reporting. This is because there is a logical connection between the resources that are reported on in budgetary reporting, and the activities those resources are used in and reported on in terms of this draft standard. Without the corresponding budget information as context, it may be difficult to adequately assess entity performance which covers both effectiveness and efficiency.

5. This [draft] Standard proposes that the reporting entity for which service performance information is reported shall be the same as that used for the entity's financial statements.

Do you agree with this proposal? Why or why not?

EY's response:

We agree that in general, service performance information should be (at a minimum) reported at the same level as the reporting entity preparing financial statements. However, we believe there may be instances where information could (and should) be provided at a lower 'segment' level to improve a NFP entity's ability to explain, and a user's ability to assess, performance and the various components that make up that overall performance. Given this, we would therefore recommend that entities be given the option to provide 'segment-type' service performance information if such information is considered relevant.

6. This [draft] Standard allows an entity to present its service performance information in:

(a) the same report as the financial statements;

(b) a separately issued report; or

(c) in a variety of different reports.

Do you agree that this [draft] Standard should not specify the location of service performance information? Why or why not?

If you disagree with the approach proposed in this [draft] Standard how do you consider entities should present service performance information and why?

EY's response:

We agree with the proposal to allow entities the option to select the location of the service performance information which would best suit users' needs. It would also be useful to provide a reference to the service performance information to help users locate the information if an entity chooses not to report this information with its General Purpose Financial Report (GPFR).

7. This [draft] Standard allows for an entity's service performance information to be reported for a different time period to that of the entity's financial statements.

Do you agree with this proposal? Why or why not?

EY's response:

We agree with the Board that such performance information should be reported, at a minimum, on an annual basis, but we do acknowledge that entities could report service performance information for a different time period compared to its financial statements. This is on the basis that service performance programs could be conducted over and at different time periods to that of a NFP entity's financial statements. In addition, there may be some programs that extend beyond an annual period; therefore entities should present a progress report (e.g. milestones report) to users on an annual basis at a minimum.

Having said this, we do consider that if the service performance reports or progress reports were produced at the same time as the GPFRs, this would elevate the importance of the information provided in such non-financial reports as they would be scrutinised more closely and may positively contribute to the transparency and accuracy of this information. This would also mean all reporting on an entity's performance (financial and non-financial) would be made available at the same time and would thus facilitate more efficient and effective assessment of overall performance.

8. The [draft] Standard includes defined terms in Appendix A. Do you agree that the proposed defined terms in Appendix A appropriately explain the significant terms in the [draft] Standard? Why or why not? Do you agree with these defined terms? Why or why not?

Are there additional terms that should be defined in Appendix A to assist application of the [draft] Standard?

EY's response:

We agree that most of the definitions contained in Appendix A appropriately explain the significant terms in the draft standard. However, we have some concerns with the draft definition of "outcomes". The definition currently reads "The impacts on society or segments of society, which occur as a result, or are reasonably attributable to, the entity's outputs. [emphasis added]"

As the service performance report of an entity relates to its achievement of its objectives and utilisation of resources to realise those objectives for the recipients of its services, we have some concerns as to how a NFP entity would track its impact beyond the identifiable recipients/beneficiaries of its activities. Without clearly defined boundaries, the measurement of 'society' based outcomes could be a challenge. We suggest that outcomes be defined more narrowly, and include identifiable recipients and beneficiaries, with clear boundaries for broader societal outcomes.

9. The AASB's view is that this [draft] Standard should be mandatory as it, in conjunction with an entity's financial statements, provides useful information for users to assess the performance of NFPs in relation to an entity's service performance objectives. Providing this information will further assist users for accountability and decision-making purposes.

Do you agree that this [draft] Standard should be mandatory for NFP entities? Why or why not?

EY's response:
We consider that if the benefits of the AASB's project (which we outlined earlier in our response, e.g., increased accountability, better information for decision-making and some improvement of consistency and some enhancement in comparability) are to be fully realised, we consider that mandatory application would be the best way to achieve this. However, such a requirement would not be without challenge.

Before mandating such requirements, the Board would need to undertake additional analysis and consideration of the following matters:

- The overlaps between the requirements of this draft standard and other reporting requirements, e.g., those currently applicable to public sector NFP entities
- Further outreach to assess the costs and benefits of implementing this standard across the various NFP entities to determine whether the cost of implementation could be reduced by introducing a differential reporting regime to allow for the different types of NFP entities, e.g., based on size or nature. For example, a reduced disclosure regime or exemptions from certain disclosures based on size or nature of an entity would help alleviate the disclosure burden on entities with limited users for its reports.
- Further application guidance to help entities apply the standard and measure outcomes, efficiency and effectiveness
- How this draft standard could be further developed to improve consistency in application in, and enhance comparability across, the broad range of NFP entities.

As also mentioned in our cover letter, the Board could consider implementing the requirements using a phased approach while conducting further outreach and cost-benefit analysis of the application of this proposal for the public sector NFP entities, or to provide smaller, less sophisticated NFP entities more time to prepare.

Furthermore, we believe that entities should be able to comply with the requirements of this draft standard by reference, that is, if the required information is available in another report, entities could refer users to that relevant report(s).

10. It is proposed that this [draft] Standard will be applicable for annual reporting periods beginning on or after 1 July 2018. Early application will be permitted.

Do you agree with the proposed application date of 1 July 2018? Why or why not?

EY's response:

We disagree with the proposed application date of 1 July 2018, but instead recommend that the Board consider setting an application date to commence after the application dates of the other major new standards (i.e., AASB 9 *Financial Instruments*, AASB 15 *Revenue from Contract with Customers* and AASB 16 *Leases)*, but provide an option for early application. This is on the basis that the new standards could present varying degrees of complexity for, and impact on, a NFP entity, depending on its size, structure and operations.

Furthermore, we believe that given the significant increase in time, cost and effort, and the likely changes in process that many NFP entities will need to go through to be able to comply with these requirements, that it will be necessary to provide such entities with additional time. Deferring the application date would also provide the AASB with the additional time necessary to develop additional guidance for preparers and to conduct more outreach to identify the overlaps between any existing reporting requirements and this proposal, and to deal more specifically with the information overlaps and/or gaps for public sector NFP entities.

General matters for comment

11. Whether:

(a) there are any regulatory or other issues arising in the Australian environment that may affect the implementation of the proposals by not-for-profit entities, including any issues relating to public sector entities, such as GAAP/GFS implications?

(b) overall, the proposals would result in reporting that would be useful to users?

(c) the proposals are in the best interests of the Australian economy?

EY's response:

(a) No comment

(b) and (c)

As mentioned earlier in our cover letter, for some smaller private and public NFP entities with limited resources and which are not subject to existing legislative requirements to report on service performance, significant time, cost, effort and capability build would be required to meet the requirements of the draft standard both initially and to a lesser extent, on an ongoing basis, and this would vary considerably by entity type and size. Therefore, as outlined above, a differential reporting regime with phased application would be worth considering, due to the concerns around costs of compliance and how these could vary considerably by entity and that these may outweigh the benefits, and the time it may take for certain entities to prepare for such reporting.

Having said that, we believe from the perspective of the reporting entity, the benefits of this proposal are:

- Facilitation of better decision-making with more consistent outputs/outcomes-based information available

- Ability to resolve inefficiencies with better information
- Additional access to capital

From the perspective of various stakeholders of the reporting entity, the benefits of the proposal are:

- Enhancement of accountability and oversight
- Facilitation of the recognition of opportunities for more efficiencies, effectiveness and increased cost awareness
- Provision of more transparent and better information to stakeholders such as state/federal governments which would facilitate better fiscal/budget planning

12. Unless already provided in response to the matters for comment 1-10 above, the costs and benefits of the proposals relative to the current Australian Accounting Standards, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

EY's response

We think that the Board's concerns regarding the cost of implementing the draft standard is justified. This is particularly so given the public concern on the portion of donors' funds spent on meeting social welfare objectives versus the portion of funds spent on compliance and administrative activities.

We are unable to provide any reliable commentary on the estimated amounts of any expected incremental costs. However, we do note that the costs to comply with the draft standard could vary considerably across the population of NFP entities and would depend on the:

- nature and size of the NFP entity
- complexity of the types of information they would need to report upon
- current reporting capabilities of the NFP entity
- complexity of any new or amended processes they would need to introduce to capture and report on such information
- reporting requirements that the NFP entity currently has to comply with

Based on our experience, consistent with the introduction of any new framework, the costs would be more significant upfront in setting up the measurement and reporting framework and then would revert to a lesser annual cost thereafter. However, given the nature of such reporting requirements, for some entities, this will still increase their overall compliance burden and associated costs – which means more of their funding will need to be directed towards compliance.