



<b>Project:</b>	<b>Not-for-Profit Private Sector Financial Reporting Framework</b>	<b>Meeting:</b>	M195
<b>Topic:</b>	<b>Tier 3 – Approach to drafting recognition and measurement requirements</b>	<b>Agenda Item:</b>	3.2
		<b>Date:</b>	18 April 2023
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		<b>Decision-Making:</b>	High
		<b>Project Status:</b>	Consider stakeholder feedback and decide next steps of the project

## The objective of this paper

- 1 The objective of this staff paper is, in relation to developing an exposure draft (ED) of a Tier 3 Standard for not-for-profit (NFP) private sector entities, for the Board to **decide** the approach to drafting the proposed recognition and measurement requirements that reflect the Board’s most recent tentative decisions made at the time of drafting.

## Background and reasons for bringing this paper to the Board

### Scope of this paper

- 2 Agenda Paper 3.1 for this meeting provides the Board with the feedback received on the Discussion Paper (DP) on the simplified reporting requirements for NFP private sector entities (NFP entities), including staff preliminary analysis and recommendations thereon, and asks Board members to decide the next steps of the project. Subject to the Board's decision about whether to proceed with developing an ED, staff seek the Board's decision in this paper on the approach to drafting the ED of proposed Tier 3 requirements.
- 3 No decisions on the Tier 3 requirements are sought in relation to this paper. Adopting any of the approaches analysed below does not determine the substance or scope of the recognition and measurement requirements to be proposed in the Tier 3 ED as the Board will determine those when deliberating on the feedback on the preliminary views on those aspects set out in the DP.
- 4 Staff note that the Board’s proposals in its Tier 3 DP received strong support from stakeholders. Therefore, for the topics that did not attract significant disagreement (identified as Category A in Agenda Paper 3.1), drafting of an ED could commence subject to the Board agreeing with the staff suggested next steps in Agenda Paper 3.1. Consequently, the views of Board members on the approach to apply in drafting the proposed recognition and measurement requirements for Tier 3 NFP entities are being sought now.<sup>1</sup>

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1 The Board decided the approach to drafting disclosure requirements in the DP (Section 6), which is noted in paragraph 11 of this paper.

### ***Objectives of determining an approach to drafting***

- 5 The objectives of determining an approach to drafting recognition and measurement requirements are to:
  - (a) achieve an appropriate balance between providing recognition and measurement requirements for the transactions, other events and conditions commonly encountered by Tier 3 NFP entities while limiting the length and complexity of those requirements, and thereby achieve an appropriate balance of costs and benefits; and
  - (b) facilitate efficient and consistent drafting of the ED.
- 6 To achieve those objectives, it is necessary for the Board to make decisions about the following matters:
  - (a) when drafting simplified Tier 3 recognition and measurement requirements with reference to Tier 2 requirements:
    - (i) whether that drafting should utilise the simplification work of other standard-setters, e.g. the IASB;
    - (ii) whether a source pronouncement should be used as the primary basis for the draft proposed recognition and measurement requirements and, if so, which one; and
    - (iii) which complementary source(s) should be considered if the IFRS for SMEs is identified as the primary source in (ii) above; and
  - (b) the approach that should be adopted for drafting simplified Tier 3 recognition and measurement requirements when Tier 3 differs from Tier 2.
- 7 Decisions about those matters will also have implications for:
  - (a) the extent of modification of the wording of source pronouncements used;
  - (b) the length and complexity of the draft proposed Tier 3 requirements;
  - (c) the writing style to employ; and
  - (d) the extent to which the literature of other standard-setters and similar bodies should be considered in drafting the ED text.
- 8 Staff consider that the drafting of the ED will necessarily be an iterative approach, with review/reassessment as the drafting of sections of the ED proceeds to reflect the Board's future decisions on the proposed recognition and measurement requirements.
- 9 Staff seek a *general* direction on the approach to the style of drafting used, i.e. a base drafting style that might need to be modified slightly for some topic sections. This is because staff note that, in respect of different topics, for the primary sources of international precedents followed

by the Board in its DP proposals,<sup>2</sup> the substance of the recognition and measurement requirements differs – and the styles of these sources also differ. Achieving consistency of writing style across the recognition and measurement requirements proposed in the ED might involve some departure from the wording of the multiple sources potentially used in accordance with the decisions the Board makes about the general drafting approach to follow.

### ***Principles for development of Tier 3 reporting requirements***

- 10 Appendix A in Agenda Paper 3.0 for this meeting provides a flowchart of the Board’s ‘approach to simplification’ summarising the principles for development of its proposed Tier 3 reporting requirements. Those principles apply essentially to the selection of proposed Tier 3 recognition, measurement and disclosure requirements, whereas the drafting approach selected is a lower-level consideration. Nevertheless, staff considered whether the main options for drafting approaches discussed in this paper are compatible with those principles – this is discussed in and paragraphs 36 – 37.

### ***Approach to development of disclosure requirements***

- 11 Staff note that the Board already decided its approach to developing disclosure requirements in [Meeting 188](#) (described in paragraph 26 of Agenda item 12.3.1 for that meeting, held in June 2022). That approach is depicted in Figure 1 below. Staff note that the approach to drafting the recognition and measurement requirements recommended in this paper is consistent with the Board’s approach to developing disclosure requirements. This aspect is commented on further in paragraphs 49 – 50.

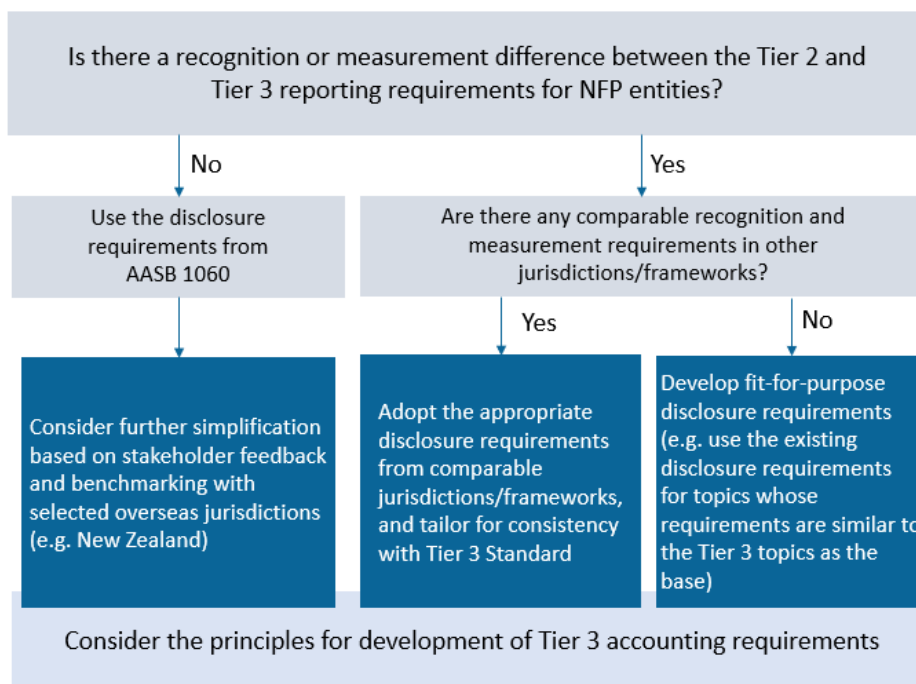
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2 In developing the Tier 3 DP proposals, the Board considered recognition and measurement requirements in the following jurisdictions (reporting frameworks):

- (a) International Financial Reporting Standard for Small and Medium-sized Entities (*IFRS for SMEs*).
- (b) IFRS Standards Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures* (ED/2021/7).
- (c) New Zealand Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit) (NZ PBE SFR – A (NFP)).
- (d) Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland (UK FRS 102).
- (e) Financial Reporting Standard 105 The Financial Reporting Standard applicable to the Micro-entities Regime (UK FRS 105).
- (f) Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland (UK Charities SORP).
- (g) Singapore Charities Accounting Standard (Singapore CAS).
- (h) Hong Kong Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (HK SME-FRF & SME-FRS).

The Board also considered issues highlighted in the IFR4NPO Consultation Paper published by the Chartered Institute of Public Finance and Accountancy, which addressed NFP reporting issues using the IFRS for SMEs as a base.

Figure 1 Approach to developing disclosure requirements for Tier 3 not-for-profit private sector entities for each topic/issue



- 12 The flowchart in Figure 1 reflects that, if the Tier 3 recognition or measurement requirement is consistent with the corresponding Tier 2 (full IFRS) requirement, the Tier 2 disclosure requirements for the topic/issue set out in AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* would be used as a starting point.

### Structure of the paper

- 13 This paper is structured as follows:

- (a) summary of staff recommendations (paragraphs 14 – 17);

*Considering options for approaches to drafting; including staff analysis and recommendations*

- (b) **Issue 1** (related to the matter in paragraph 6(a)(i)): Approach to drafting simplified Tier 3 recognition and measurement requirements when there is no difference in scope or substance between Tier 2 and Tier 3 (paragraphs 18 – 22):
- (i) staff evaluation (paragraphs 18 – 20);
  - (ii) staff recommendation (paragraph 21)
- (c) **Issue 1(a)** (related to the matter in paragraph 6(a)(ii)): Possible primary sources to consider in applying the staff recommendation on Issue 1 (paragraphs 23 – 40):
- (i) staff evaluation, including evaluation of options against the Tier 3 development principles (paragraphs 23 – 37);
  - (ii) staff recommendations (paragraphs 38 – 40)
- (c) **Issue 1(b)** (related to the matter in paragraph 6(a)(iii)): Possible complementary sources to consider if using the IFRS for SMEs for drafting Tier 3 requirements based on the corresponding Tier 2 requirements (paragraphs 41 – 48):
- (i) staff evaluation (paragraphs 41 – 46);
  - (ii) staff recommendation (paragraphs 47 – 48)

- (d) **Issue 2** (related to the matter in paragraph 6(b)): Approach to drafting simplified Tier 3 recognition and measurement requirements when Tier 3 differ in scope or substance from Tier 2 (paragraphs 49 – 53):
  - (i) staff evaluation (paragraphs 49 – 52);
  - (ii) staff recommendations (paragraph 53)

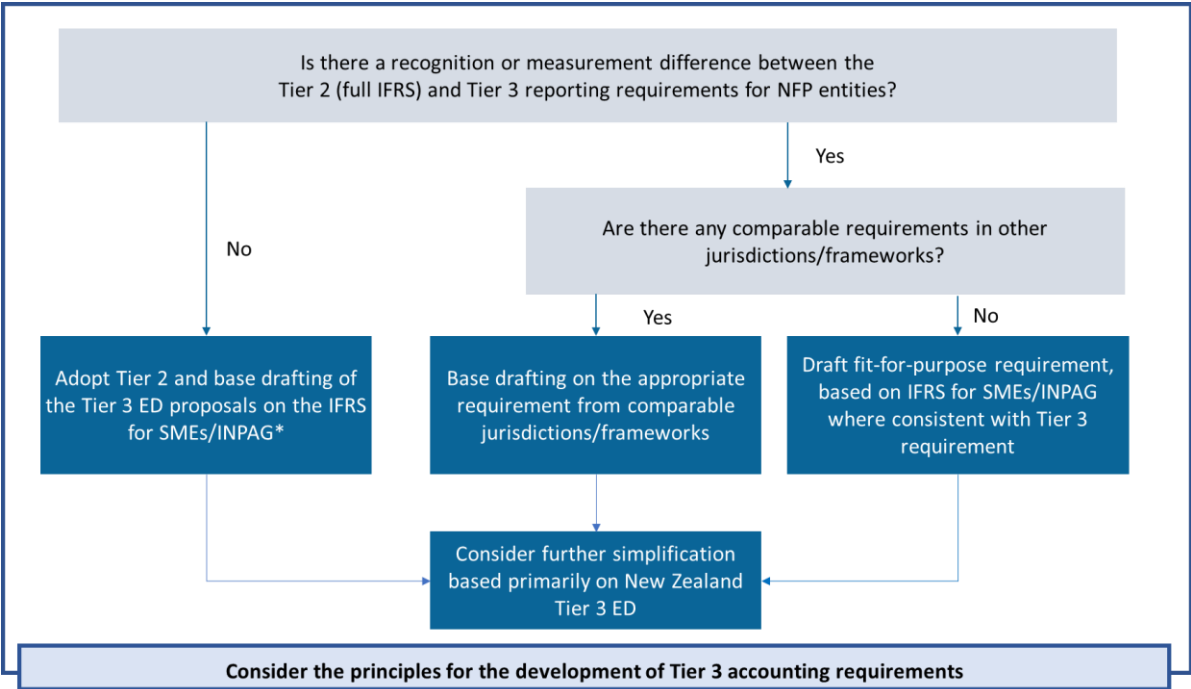
### Summary of staff recommendations

- 14 Staff's recommendations for the approach to drafting the Tier 3 ED with reference to the 'approach to simplification' flowchart referred to in paragraph 10 are summarised in paragraphs 15 – 17. Staff consider that the approach should be reviewed and, where necessary, refined as drafting progresses.
- 15 Staff recommend adopting an approach to drafting the recognition and measurement requirements of the Board's Tier 3 ED for each topic/issue (transaction, other event or condition) within the scope of Tier 3 requirements by commencing with considering whether there is a recognition or measurement difference (whether a difference in the scope or substance of the requirement) between the Tier 2 (full IFRS) requirement and the proposed Tier 3 requirement for NFP entities:
  - (a) When no recognition or measurement difference exists between the Tier 2 and Tier 3 requirements, the proposed Tier 3 requirements would be drafted with reference to the corresponding Tier 2 wording. To achieve this, the IFRS for SMEs<sup>3</sup> should be used as base wording (subject to modification, having regard to the proposals of INPAG publicly available when the Board's ED is drafted (or the requirements of UK FRS 102/Charities SORP if the INPAG ED is not publicly available) – see paragraphs 38 and 47). (This combined source of wording to utilise is referred to hereinafter as "IFRS for SMEs/INPAG".) However, the drafting would amend the IFRS for SMEs/INPAG wording if that combined source is inconsistent in substance or scope with Tier 2 for the aspect where Tier 3 explicitly aligns with Tier 2 (see paragraph 39).
  - (b) When a recognition or measurement difference exists between the Tier 2 and Tier 3 requirements, consideration should be given to whether there are any comparable treatments in other jurisdictions/frameworks and:
    - (i) if there are, the appropriate requirement from those comparable treatments should be selected as the source for drafting the Tier 3 ED proposal; or
    - (ii) if there are not, staff should draft a fit-for-purpose requirement based on the IFRS for SMEs/INPAG where consistent with the substance of the Tier 3 requirement (see paragraph 53).
- 16 Regardless of whether paragraph 15(a) or (b) applies, further simplification of the draft guidance (including language) should be considered, based primarily on the New Zealand Tier 3 Standard, but compatible with the Board's recognition and measurement proposals in its DP (see paragraph 40).
- 17 A flowchart encapsulating the staff recommendations summarised in paragraphs 15 – 16 is set out in Figure 2 below.

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3 References in this paper to the IFRS for SMEs and the New Zealand Tier 3 Standard are to the latest exposure drafts (EDs) for amending those Standards, rather than the wording of those extant Standards. This is because staff expect that many of the proposals of those EDs are likely to be adopted in the respective Standards; therefore, it seems logical to use those ED proposals. If Board members agree with preferring the wording of those EDs to those extant Standards, staff plan to monitor developments in the finalisation of the revised Standards and update the draft wording of the Tier 3 ED in light of those developments.

Figure 2 Flowchart of staff-recommended approach to drafting recognition and measurement requirements for Tier 3 NFP private sector entities (each topic/issue)



\*However, the drafting will amend the IFRS for SMEs/INPAG if inconsistent in substance or scope with Tier 2 for the aspect where Tier 3 explicitly aligns with Tier 2

**Issue 1: Approach to drafting simplified Tier 3 recognition and measurement requirements when there is no difference in scope or substance between Tier 2 and Tier 3**

- 18 The overarching principle already adopted by the Board in its Tier 3 DP is to commence by considering whether there is a recognition or measurement difference (whether a difference in the scope or substance of the requirement) between the Tier 1/Tier 2 (full IFRS) requirement, hereinafter simply “Tier 2 requirement”, and the proposed Tier 3 requirement for NFP entities. Where such a difference does not exist, the ED’s proposed recognition and measurement requirements would be drafted with reference to the relevant Tier 2 requirement, before simplifying it by applying the principles for the development of Tier 3 accounting requirements. This is a given in the design of the approach to drafting the Tier 3 recognition and measurement requirements.
- 19 The first issue to address in applying the fundamental approach described in paragraph 18 to drafting simplified Tier 3 requirements consistently with the Tier 2 text (when consistent with Tier 2 in scope and substance) is whether to refer solely to the Tier 2 text, i.e. without referring to other pronouncements (international or national). Doing so would have the advantage of providing a ‘checklist’ for ensuring no relevant Tier 2 requirements are overlooked. Similarly, it would enable direct tracking between Tier 2 and Tier 3.
- 20 However, adopting this approach would disregard the work of other standard-setters, e.g. the IASB, in considering which reporting requirements should be modified or omitted for smaller entities. Utilising that work of other standard-setters where those sources are consistent with the Tier 3 requirement would be expected to assist the Board in making decisions on the wording of the Tier 3 Standard for NFP entities. Therefore, staff consider that using the Tier 2 requirement guidance as a starting drafting point is likely to be very time-consuming and consequently delay completion of that drafting to an unacceptable extent.

**Staff recommendation on Issue 1**

- 21 For the reason in paragraph 20, staff recommend that, when drafting Tier 3 recognition and measurement requirements by reference to Tier 2 requirements, that drafting should utilise the simplification work of other standard-setters, e.g. the IASB, in considering which reporting requirements should be modified or omitted for smaller entities.
- 22 Issue 1(a), discussed in paragraphs 23 – 40, addresses which primary drafting sources should be considered, subject—if the IFRS for SMEs is used—to modification by having regard to similar sources. Issue 1(b), discussed in paragraphs 41 – 48, addresses which complementary sources should be considered if the primary drafting source is the IFRS for SMEs.<sup>4</sup>

**Question 1 for Board members:**

- (Q1)** Do Board members agree with the staff recommendation in paragraph 21 that, when drafting Tier 3 recognition and measurement requirements by reference to Tier 2 requirements, that drafting should utilise the simplification work of other standard-setters, e.g. the IASB, in considering which reporting requirement guidance should be modified or omitted for smaller entities?
- If not, what do Board members suggest?

**Issue 1(a): Possible primary sources to consider in applying staff recommendation on Issue 1**

- 23 Within the constraints of the Board's decisions about the Tier 3 proposals for recognition and measurement, it would seem desirable to identify a primary source for drafting the proposed Tier 3 ED, to maximise the likelihood of using a consistent drafting style in the ED. As outlined in the disclosure approach discussed in paragraph 11, such a single reference point is available for disclosures, being AASB 1060. That Standard was developed based on the IFRS for SMEs; the Board's DP indicated an intention to simplify further the disclosure requirements of AASB 1060 for Tier 3 NFP entities.
- 24 Staff noted that such a single pronouncement does not exist in Australia for recognition and measurement requirements. However, staff recognises that several international and overseas standard-setters have developed simplified recognition and measurement requirements, including those based on full IFRS, where an 'audit trail' of differences from full IFRS is available.
- 25 Staff identified two main candidates as primary sources for applying the staff recommendation on Issue 1 (to utilise the simplification work of other standard-setters when drafting Tier 3

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4 Issues 1(a) and 1(b) concentrate on four particular jurisdictions/reporting frameworks because consideration of them should largely complete the process of developing an initial complete draft of Tier 3 recognition and measurement requirements, and limiting the number of sources widely referred to should assist in achieving a consistent drafting style in the Tier 3 ED. However, for selected issues, it will be necessary to consider other sources on a case-by-case basis. The possible approaches to the drafting of Tier 3 recognition and measurement requirements in other jurisdictions and reporting frameworks considered in this paper are: (1) those that either embody, or are based on, the IFRS for SMEs and were key sources considered by the Board in deciding its proposed recognition and measurement requirements (these were included because they stem from full IFRS in some manner); and (2) New Zealand's Tier 3 Standard (which was also a key source considered by the Board in deciding its proposed recognition and measurement requirements; is simplified to an extent advocated by many stakeholders who have provided feedback on the Board's Tier 3 project; and is considered as part of the Board's policy on harmonisation of Trans-Tasman standard-setting). Approximately 30% of the proposed Tier 3 recognition, measurement and disclosure requirements developed by the Board are primarily based on the New Zealand Tier 3 reporting requirements and approximately 15% of those proposed requirements are primarily based on the IFRS for SMEs.

recognition and measurement requirements with reference to the corresponding Tier 2 requirements): namely, the IFRS for SMEs and the New Zealand Tier 3 Standard. However, if the IFRS for SMEs were to be preferred as the primary drafting source to consider in the context of Issue 1, it would not be used in isolation: regard would be had to complementary pronouncements developed to modify the IFRS for SMEs to provide NFP-specific guidance and use NFP-specific expression – this is explored in Issue 1(b).

- 26 The recognition and measurement requirements of the IFRS for SMEs were substantially reduced from the corresponding requirements in full IFRS. The requirements were developed broadly based on principles focusing on users' needs and cost-benefit considerations. In that regard, the IASB concluded that “users of financial statements of SMEs may have greater interest in short-term cash flows, liquidity, balance sheet strength and interest coverage, and in the historical trends of profit or loss and interest coverage, than they do in information that is intended to assist in making forecasts of an entity’s long-term cash flows, profit or loss, and value.”<sup>5</sup> Using the IFRS for SMEs where the Board’s Tier 3 requirements are consistent both with Tier 2 requirements and the IFRS for SMEs would provide a drafting link with Tier 2 (full IFRS) and utilise the work of the IASB in simplifying the Tier 2 requirements.
- 27 The recognition and measurement requirements in New Zealand's Tier 3 Standard were developed following the general approach that New Zealand's PBE Standards (which are based on IPSAS) should be simplified for Tier 3 entities by creating a single, short, and simple Standard written in less technical language than is normally found in accounting standards.<sup>6</sup> Using the New Zealand's Tier 3 Standard where the Board’s Tier 3 requirements are consistent both with Tier 2 requirements and the New Zealand Standard would considerably assist in simplifying reporting for Tier 3 NFP entities (because of the conciseness of the New Zealand Tier 3 Standard) and align with the Board’s policy on harmonisation of Trans-Tasman standard-setting.
- 28 The other reason for identifying the IFRS for SMEs and the New Zealand Tier 3 Standard as the main contenders for use as the primary source to commence with, when drafting Tier 3 requirements with reference to corresponding Tier 2 requirements is that, as noted in footnote 4, approximately 30% of the proposed Tier 3 recognition, measurement and disclosure requirements developed by the Board are primarily based on the New Zealand Tier 3 reporting requirements and approximately 15% of those proposed requirements are primarily based on the IFRS for SMEs.
- 29 A comparison of the relative merits of using the IFRS for SMEs or the New Zealand Tier 3 Standard as the primary source for commencing drafting Tier 3 requirements with reference to corresponding Tier 2 requirements is set out in Table 1. Key aspects of that table are discussed further in paragraphs 30 – 35.

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5 IASB Basis for Conclusions on IFRS for SMEs, 2015, paragraph B45.

6 The New Zealand Tier 3 Standard is being updated and amended based on the feedback to an Exposure Draft developed following completion of a Post-Implementation Review on the extant Standard.



**Table 1 Comparison of Approaches using IFRS for SMEs or New Zealand Tier 3 Standard as Primary Source for drafting Tier 3 Recognition and Measurement Requirements when there is no difference between Tier 3 and Tier 2 requirement**

Possible approaches for Tier 3 – approach to drafting recognition and measurement requirements	Support for the approach	Arguments against this approach
<p><b>Approach 1:</b>  <b>Commence with the text of the IFRS for SMEs and modify it, mainly by omitting unnecessary text<sup>7</sup> and modifying the guidance to reflect a NFP entity context (see discussion of Issue 1(b) in paragraphs 41 – 48 for possible sources of NFP modification)</b></p>	<ul style="list-style-type: none"> <li>• Utilises the work of the IASB in considering which requirements of full IFRS should be modified or omitted for smaller entities (i.e. avoids replicating the IASB’s work).</li> <li>• Because the IASB used full IFRS (mostly the same as Tier 1/Tier 2 reporting requirements) as the starting point, it assists in achieving consistency and comparability with Tier 1/Tier 2 reporting requirements where relevant (one of the principles for developing the Tier 3 requirements is to maximise consistency with Tier 2 accounting principles where possible).</li> <li>• Reflects language more familiar to those working in multiple tiers in Australia (which limits the amount of education and knowledge transfer costs required).</li> <li>• INPAG is using the IFRS for SMEs as a base for developing its guidance (based on feedback from its consultation process), indicating the IFRS for SMEs is a good starting point.</li> <li>• A stronger ‘audit trail’ exists of the differences from Tier 1/Tier 2 because of the comparison between IFRS for SMEs and full IFRS already prepared.<sup>8</sup></li> </ul>	<ul style="list-style-type: none"> <li>• If used, it would need to be simplified significantly: <ul style="list-style-type: none"> <li>• The core text of the current IFRS for SMEs ED spans 321 pages, for example compared with the 61-page length of the core text of the current New Zealand Tier 3 ED.</li> <li>• Various SMEs are likely to be larger and undertake more complex transactions than entities used as a reference point for the Board’s proposals in its Tier 3 DP (i.e. entities with revenue of \$500,000 or more but less than \$3 million: as referred to in paragraph 2.12 of the DP) – meaning many requirements of the IFRS for SMEs would not be proportionate for Tier 3 NFP entities. Some sections of the IFRS for SMEs would be wholly inapplicable because their subject matter would be uncommon for Tier 3 NFP entities (e.g. share-based payment)—however, it should be straightforward to identify and omit those inapplicable sections.</li> </ul> </li> <li>• If used, it would need to be modified for NFP-specific issues – in contrast with using the New Zealand Tier 3 Standard. This disadvantage could be ameliorated by using NFP-oriented sources such as those in Issue 1(b) (e.g. INPAG proposals, to the extent they are available on a timely basis for drafting the Tier 3 ED).</li> </ul>

7 Based on initial “sand box” pilot testing of drafting applied by staff, modifying the text of the IFRS for SMEs would mainly involve omitting ‘unnecessary’ text (i.e. text that would not achieve a proportionate response to the need to provide useful information to users of financial statements while achieving an appropriate balance of costs and benefits).

8 The IASB’s Basis for Conclusions on the extant IFRS for SMEs Standard explains (in paragraphs BC99 – BC136) the significant simplifications to the recognition and measurement principles in full IFRS that are reflected in the IFRS for SMEs. In addition, in its Basis for Conclusions on AASB 1060, the Board stated (in paragraph BC44) that: “To identify R&M differences, the Board has referred to: (a) the AASB staff paper *Comparison of Standards for Smaller Entities* prepared and published in April 2018; (b) full IFRS vs *IFRS for SMEs* Standard comparisons included in the *IFRS for SMEs* Standard modules published by the IASB; and (c) individual analyses of Standards, where a topic is covered by neither of these two sources.” Furthermore, during the process of developing AASB 1060, the following comparison was prepared:

[https://www.aasb.gov.au/admin/file/content142/c2/ACCED295\\_08-19\\_Staff\\_Analysis\\_SME\\_RM.pdf](https://www.aasb.gov.au/admin/file/content142/c2/ACCED295_08-19_Staff_Analysis_SME_RM.pdf)

Possible approaches for Tier 3 – approach to drafting recognition and measurement requirements	Support for the approach	Arguments against this approach
<p><b>Approach 2:</b>  <b>Commence with the New Zealand Tier 3 Standard and modify it – mainly by adding proportionate guidance</b></p>	<ul style="list-style-type: none"> <li>• New Zealand Tier 3 Standard is short, relatively simple and written in less technical language than is normally found in Tier 1/Tier 2 requirements (and in various IFRS for SMEs paragraphs). Therefore, it is simpler and easier to understand and apply than the IFRS for SMEs; some language in the IFRS for SMEs is highly technical, despite its greater brevity compared with full IFRS. <ul style="list-style-type: none"> <li>• as noted above in respect of Approach 1, its core text is less than a fifth of the length of the core text of the current IFRS for SMEs ED</li> </ul> </li> <li>• Written for NFP entities, unlike the IFRS for SMEs.</li> <li>• Generally meets the information needs of users of financial statements while achieving a reasonable balance between costs and benefits of the requirements.</li> <li>• Aligns with AASB’s policy on harmonisation of Trans-Tasman standard-setting.</li> <li>• Feedback from adoption of the current New Zealand Tier 3 Standard indicates it is working well and well received by stakeholders.</li> <li>• Approximately 30% of the proposed Tier 3 recognition, measurement and disclosure requirements developed by the Board are primarily based on the NZ Tier 3 reporting requirements<sup>9</sup> compared with approximately 15% for IFRS for SMEs.<sup>10</sup></li> </ul>	<ul style="list-style-type: none"> <li>• Excludes some proportionate guidance found in the IFRS for SMEs, or its equivalent (e.g. it lacks a section providing guidance on fair value measurement; in relation to impairment of property, plant and equipment it does not explain what the “value to the entity” of an asset is (to compare with its carrying amount); and, for example, in initial staff “sand box” pilot testing of drafting a section on Property, Plant and Equipment, it was noted that the NZ Tier 3 Standard does not include guidance on factors for determining an asset’s useful life). Another example is that it does not cater for optional recognition of volunteer services received if their fair value can be measured reliably.</li> <li>• Australian Tier 3 entities are likely to include some entities larger than those to which the New Zealand Tier 3 Standard would apply; this might create a need for increased guidance to cover a wider range of issues.</li> <li>• Expression differs from that used in Tier 1/Tier 2 (to a greater degree than the IFRS for SMEs) because the starting point is the New Zealand PBE Standards (which are based on IPSAS, rather than full IFRS).<sup>11</sup> Therefore: <ul style="list-style-type: none"> <li>• those familiar with Tier 1/Tier 2 might expend greater effort in understanding Tier 3 guidance if based on NZ Tier 3 requirements; and</li> <li>• there would be a risk of inadvertently importing IPSAS differences from full IFRS requirements.</li> </ul> </li> </ul>

9 The topics that the Board had previously preliminarily decided to primarily be based on the New Zealand requirements include: accounting for prior period accounting errors, expensing transactions cost for the initial measurement of financial instruments, accounting for interest income/expenses, impairment of financial instruments, investment in associates and joint ventures, recognition criteria for lessors, revenue recognition model (similar to the NZ Tier 3 recognition for donations/grants/bequests) and other topics.

10 The topics that the Board had previously preliminarily decided to primarily be based on the IFRS for SMEs Standard include subsequent measurement of financial liabilities, derecognition of financial assets and financial liabilities, borrowing costs, measurement criteria for leases (similar to operating leases in IFRS for SMEs),

11 The [Simple Format Reporting for NFP Entities Working Group Report](#) issued by the XRB in November 2011 outlined the development of the multi-standards accounting framework in New Zealand where the XRB proposed to develop standards for public benefit entities (including NFP entities required to prepare GPFR) based on IPSAS.

- 30 Most of the Board’s stakeholders who provided feedback on the length and simplicity of the Tier 3 Standard indicated a preference for a Standard considerably shorter and simpler than the IFRS for SMEs. In light of that feedback and the fact that almost half of the Board’s preliminary views in the DP are consistent with either IFRS for SMEs and NZ Tier 3, staff consider that, in the context of Issue 1, the proposed recognition and measurement requirements for the Tier 3 ED are likely to lie somewhere between the relatively lengthy requirements of the IFRS for SMEs (complemented by other sources such as INPAG—see Issue 1(b)) and the requirements of the New Zealand Tier 3 Standard. Regarding identification of the better starting point for drafting the proposed Tier 3 recognition and measurement requirements, staff note that, overall, the recognition and measurement requirements of the IFRS for SMEs are much more extensive than those of the New Zealand Tier 3 Standard. Staff consider it important that using the IFRS for SMEs wording (complemented by other sources) and simplifying it would:
- (a) minimise the risk of overlooking a potential item of recognition or measurement guidance, because the IFRS for SMEs/INPAG would provide both:
    - (i) an ‘audit trail’ from most Tier 2 requirements; and
    - (ii) at least as much guidance on most recognition and measurement issues as the guidance that would achieve a proportionate response to meeting the information needs of users of Tier 3 entity financial statements while balancing the costs and benefits of the information provided; and
  - (b) utilise the IASB’s work in considering how to modify the text of IFRSs (on which Tier 2 requirements are based) for smaller entities, rather than replicating that work. In that regard, staff consider that using the IFRS for SMEs wording (complemented by other sources) and simplifying it would be likely to save considerable drafting time compared with using the New Zealand Tier 3 Standard, because it is probably faster to summarise and omit guidance than to add guidance to a briefer set of requirements like those in the New Zealand Tier 3 Standard if adding guidance thereto is needed to reflect the Board’s decisions on the recognition and measurement requirements.
- 31 For these reasons, staff consider that commencing with the IFRS for SMEs wording (complemented by other sources) as a primary source for timely drafting of proposed Tier 3 recognition and measurement requirements is likely to be more effective than commencing with the New Zealand Tier 3 Standard, provided that the IFRS for SMEs wording (complemented by other sources) is consistent in substance and scope with the Tier 2 requirement being aligned with in Tier 3.
- 32 Staff consider that, where the recognition or measurement requirements of the IFRS for SMEs are used, the wording should be modified by simplifying it and using NFP-specific terminology or expression where the IFRS for SMEs wording does not reflect (or is incompatible with) the NFP entity environment. In simplifying its wording, subjective judgement would be necessary to summarise/condense the guidance while retaining its key points.
- 33 Staff emphasise that adopting the staff view in paragraph 31 would not necessarily imply that the draft proposed recognition and measurement requirements for the Board’s Tier 3 ED (on issues where it is aligned with Tier 2) would ultimately be more like those in the IFRS for SMEs than the New Zealand Tier 3 Standard. Indeed, the New Zealand Tier 3 Standard is considerably closer in length and simplicity to the Tier 3 ED that would align with the expectations of most of the Board’s stakeholders who provided feedback on those aspects. Nevertheless, the choice between using the IFRS for SMEs and the New Zealand Tier 3 Standard as a primary source is mainly with the process to employ, rather than the outcome of drafting (particularly because further simplification would be necessary).
- 34 Staff has been performing initial “sand box” pilot testing of simplifying some sections of the IFRS for SMEs (using the latest IASB ED) and found that considerable simplification of the IFRS for SMEs seems feasible in application of the Board’s principles for development of its

proposed Tier 3 reporting requirements. Regardless of which approach the Board decides to take to drafting proposed recognition and measurement requirements for Tier 3 NFP entities, staff will provide examples of pilot testing of that approach for consideration at a future Board meeting.

- 35 Accordingly, staff consider that using the IFRS for SMEs wording (complemented by other compatible sources based on the IFRS for SMEs) and should be the preferred primary source before further simplification, subject to considering the impact (if any) of applying the Tier 3 development principles (see paragraphs 36 – 37).

#### ***Evaluation of options against the Tier 3 development principles***

- 36 Staff consider that applying the Tier 3 development principles referred to in paragraph 10 will affect assessments at an individual issue level of the requirements to include, more so than in ranking the relative merits of commencing drafting Tier 3 requirements based on the IFRS for SMEs (complemented by other sources) or the New Zealand Tier 3 Standard. The exception is the principle “Consistency with the accounting principles specified in Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable but might not always be warranted since Tier 3 requirements are being developed as a proportionate response”. Commencing with the New Zealand Tier 3 Standard would not be expected to align as closely with that Tier 3 development principle as commencing with the IFRS for SMEs. This is because the New Zealand Tier 3 Standard was not drafted strictly in accordance with an IFRS-based framework. Nevertheless, it would be feasible to largely overcome that issue by modifying the wording of the New Zealand Tier 3 Standard.
- 37 As noted in paragraph 35, staff consider that the preferred primary source for drafting Tier 3 requirements when the circumstances of Issue 1 exist should be the IFRS for SMEs (subject to complementing it with reference to other sources discussed in Issue 1(b)). Therefore, the exception noted in paragraph 36 does not affect the staff recommendation, which is set out in paragraph 38.

#### ***Staff recommendations on Issue 1(a)***

- 38 For the reasons discussed in Table 1 and paragraphs 30 – 37, staff recommend that, when the circumstances of Issue 1 exist, the IFRS for SMEs wording (complemented by other compatible sources based on the IFRS for SMEs: see Issue 1(b)) should be the preferred primary base source for drafting the proposed recognition and measurement requirements of the Board’s Tier 3 ED for NFP entities, before further simplification. This would:
- minimise the risk of overlooking a potential item of recognition or measurement guidance;
  - be likely to save considerable drafting time compared with commencing with the New Zealand Tier 3 Standard, because it is probably faster to summarise and omit guidance than to add guidance (if needed to reflect the Board’s decisions) to a briefer set of requirements like those in the New Zealand Tier 3 Standard; and
  - maintain consistency and comparability with Tier 1/Tier 2 reporting requirements, where relevant, and provide an ‘audit trail’ of differences<sup>12</sup>. Accounting professionals in the NFP sector are familiar with the existing reporting framework.
- 39 However, the drafting would amend the IFRS for SMEs wording (complemented by other source(s)) if it is inconsistent in substance or scope with Tier 2 for the aspect where Tier 3 explicitly aligns with Tier 2.
- 40 Regardless of the source of requirements on which drafting of the Tier 3 recognition or measurement requirement is based (in accordance with paragraph 38), further simplification of

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12 See the comments on Approach 1 in Table 1 (including footnote 8).

language or otherwise would be based primarily on consideration of the New Zealand Tier 3 Standard, the brevity of which is closest to the brevity of guidance sought by most of the Board's stakeholders who provided feedback on the appropriate length of a Tier 3 Standard. Doing so would also align with the AASB's policy on harmonisation of Trans-Tasman standard-setting. This is reflected in Figure 2 beneath paragraph 17 and applies not only to the circumstances encompassed by Issue 1 but also to the circumstances encompassed by Issue 2.

**Questions 2 and 3 for Board members:**

- (Q2)** Do Board members agree with the staff recommendations in paragraph 38 that, when the circumstances of Issue 1 exist (i.e. when drafting Tier 3 requirements with reference to Tier 2 requirements), the IFRS for SMEs wording (complemented by other compatible source(s)) should be the preferred primary source for drafting the proposed recognition and measurement requirements for Tier 3 NFP entities, before considering further simplification (however, the drafting would amend the IFRS for SMEs wording if it is inconsistent in substance or scope with Tier 2 for the aspect where Tier 3 explicitly aligns with Tier 2)? If not, what do Board members suggest?
- (Q3)** Do Board members agree with the staff recommendation in paragraph 40 that, regardless of the source of requirements on which drafting of the Tier 3 recognition or measurement requirement is based, further simplification of language or otherwise would be based primarily on consideration of the New Zealand Tier 3 Standard? If not, what do Board members suggest?

**Issue 1(b): Possible complementary sources to consider if using the IFRS for SMEs for drafting Tier 3 requirements with reference to the corresponding Tier 2 requirements**

- 41 Two sources of guidance considered by the Board in developing its Tier 3 DP and that were developed based on the IFRS for SMEs are the INPAG EDs and UK FRS 102 read together with the UK Charities SORP (hereinafter: UK FRS 102/Charities SORP). The INPAG EDs and UK FRS 102/Charities SORP share the features of being based on the IFRS for SMEs wording but modifying that wording to the extent considered necessary for NFP considerations.
- 42 The UK Chartered Institute of Public Finance and Accountancy (CIPFA) published an Exposure Draft of International Non-Profit Accounting Guidance ("INPAG"): Part 1 in November 2022. The ED was developed by the INPAG Secretariat as part of the process of developing accrual-based International Financial Reporting guidance for Non-Profit Organisations ("IFR4NPO") by adapting the IFRS for SMEs to respond to the NFP environment. INPAG is expected to include sections developed specifically for NPOs for which corresponding sections do not exist in the IFRS for SMEs, and will use terminology more suited to the NFP environment. Two additional INPAG EDs are planned for issue by the end of the 2023 calendar year. Proposed recognition and measurement requirements for INPAG are planned to be included in both EDs (i.e. the earliest time a complete set of recognition and measurement proposals for INPAG is expected to be publicly available is the fourth quarter of 2023) and a final INPAG is targeted for issue in mid-2025.
- 43 Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (UK FRS 102) was developed based on the IFRS for SMEs, but amended in limited instances to permit accounting treatments in EU-adopted IFRS, unless a non-IFRS-based solution clearly met better the objective of providing high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.<sup>13</sup> It is supported for charities exceeding a size threshold by the Charities SORP

13 Basis for Conclusions on FRS 102, paragraphs A.4 and A.6.

(Statement of Recommended Practice), which is required to be consistent with UK FRS 102 (and therefore is based on the IFRS for SMEs). A Financial Reporting Exposure Draft currently is open for comment on proposed amendments to FRS 102 that would update that Standard based on a second periodic review.<sup>14</sup>

- 44 Because the INPAG EDs and UK FRS 102/Charities SORP are based on the IFRS for SMEs wording but modify that wording to the extent considered necessary for NFP considerations, the use of either source as a complement to the IFRS for SMEs should:
- (a) enable more efficient drafting of proposed Tier 3 requirements compared with using the IFRS for SMEs and developing NFP entity modifications without regard to either of those complementary sources; and
  - (b) use expression and terminology familiar to Australian NFP stakeholders.
- 45 Neither the INPAG EDs nor the UK FRS 102/Charities SORP are targeted at simplifying further the IFRS for SMEs; therefore, if either source were used, considerable work would still be necessary to identify wording to omit (as would be the case if the IFRS for SMEs were used without regard to these complementary sources).
- 46 The main difference between the approaches of the INPAG EDs and UK FRS 102/Charities SORP is that:
- (a) UK FRS 102/Charities SORP are pronouncements issued by a domestic standard-setter; whereas
  - (b) the INPAG EDs are developed as an international response to the IFRS for SMEs, and therefore more relevant from an Australian perspective (and to Australian stakeholders)<sup>15</sup>. Underlining this point, paragraph 43 notes that (in contrast with INPAG) FRS 102 amends the IFRS for SMEs in limited instances to permit accounting treatments in EU-adopted IFRS.

**Staff recommendation on Issue 1(b)**

- 47 For the reason in paragraph 46, staff recommend that, where INPAG proposals have been issued on a particular topic/issue, they should be used in preference to UK FRS 102/Charities SORP as a complementary source to the IFRS for SMEs. However, where INPAG proposals have not yet been issued on a particular topic/issue at the time of drafting the Tier 3 ED, regard should be had to the wording of UK FRS 102/Charities SORP. For simplicity, this approach is referred to hereinafter as “IFRS for SMEs/INPAG”.
- 48 Staff observe that, if complete, the INPAG proposals would provide an international perspective on how the IFRS for SMEs should be modified for a NFP entity context, and therefore arguably would be a better source for drafting than the IFRS for SMEs. However, completion of all INPAG proposals on recognition and measurement issues is unlikely to be sufficiently timely for the Board’s timeline for developing its Tier 3 ED – therefore, waiting for the remaining INPAG EDs to be issued (or the final INPAG, which is targeted for issue in mid-2025) would be likely to delay completion of the Board’s Tier 3 ED to an unacceptable extent. Accordingly, staff do not recommend at this stage that INPAG proposals should be used to the exclusion of the IFRS for SMEs.

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14 Financial Reporting Exposure Draft FRED 82 *Draft amendments to FRS 102* (comment period closes on 30 April 2023).

15 For example, Agenda Paper 3.1 for this Board meeting (Meeting 195) notes, in relation to Topic Q6, that a stakeholder thinks the Board should consider the international developments (IFR4NPO/INPAG) and explore the appropriateness of its adoption in full or in part in Australia for all NFP entities.

**Question 4 for Board members:**

**(Q4)** Do Board members agree with staff recommendation in paragraph 47 that, when the IFRS for SMEs is being used as a primary source of drafting for Tier 3 requirements with reference to the corresponding Tier 2 requirements, the main complementary source of guidance to consider should be the INPAG proposals where they have been issued on a particular topic/issue, and UK FRS 102/Charities SORP where the INPAG proposals have not yet been issued?

If not, what do Board members suggest?

**Issue 2: Approach to drafting simplified Tier 3 recognition and measurement requirements when Tier 3 differs in scope or substance from Tier 2**

49 The next step in developing an appropriate approach to drafting the recognition and measurement requirements of a Tier 3 ED is to consider an approach to drafting when there is a recognition or measurement difference (in scope or substance) between the Tier 3 requirement and the Tier 2 requirement. In such instances, the Tier 2 wording would be inapplicable. Staff consider that, consistent with the approach to disclosures in Figure 1, consideration should be given to whether there are any comparable treatments in other jurisdictions/frameworks providing alternative sources of wording on which to base drafting of the Tier 3 requirement, and:

- (a) if there are, the appropriate requirement selected from those comparable treatments should be selected as the source for drafting the Tier 3 ED proposal; or
- (b) if there are not, a fit-for-purpose requirement would be drafted consistently with the substance of the Tier 3 requirement (see also paragraph 51).

50 Staff also observe that the combination of the steps in paragraph 18 and paragraph 49 is consistent with the combination of steps adopted by the Board in relation to disclosure requirements,<sup>16</sup> as referred to in paragraph 11. If the Board were to adopt a different approach for drafting Tier 3 recognition and measurement requirements, this could imply a need for the Board to revisit its decisions in Meeting 188 (June 2022) regarding the approach to take to identifying proposed Tier 3 disclosure requirements.

***How to draft a fit-for-purpose recognition or measurement requirement in the absence of comparable requirements in other jurisdictions/frameworks***

51 Staff consider that, when paragraph 49(b) applies (i.e. there is a recognition or measurement difference between the Tier 3 requirement and the Tier 2 requirement and no comparable treatments in other jurisdictions/frameworks have been identified), the drafting of the Tier 3 requirement should be based on the IFRS for SMEs/INPAG where consistent with the substance of the Tier 3 requirement. Some of the Board's proposed Tier 3 requirements that differ from

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16 The only non-editorial difference between this approach and the approach adopted by the Board in relation to disclosure requirements (referred to in paragraph 11 and depicted in Figure 1) is that Figure 1 indicates that the Board's approach to disclosures involves "consider(ing) further simplification if appropriate" if the disclosure requirements of AASB 1060 are used (i.e. when there is no recognition or measurement difference between the Tier 2 and Tier 3 reporting requirements). In contrast, this recognition and measurement drafting approach considers further simplification regardless of the requirement on which the drafting is primarily based. (In addition, this recognition and measurement drafting approach refers to basing that further simplification primarily on the New Zealand Tier 3 Standard.) If the Board agrees with the proposal to consider further simplification based primarily on the New Zealand Tier 3 Standard regardless of the requirement on which the drafting of the recognition and measurement requirements is primarily based, staff would also take that step in drafting the proposed Tier 3 disclosure requirements. However, staff consider there would be no need to amend the flowchart of the Board's approach to development disclosure requirements set out in Figure 1.

the corresponding Tier 2 requirement align with differences between the IFRS for SMEs and full IFRS; in these instances, the wording of the IFRS for SMEs would serve as a faithful starting point before considering further simplification (including consideration of INPAG proposals).

- 52 In addition, if the Board supports the staff recommendations in paragraphs 38 and 39, staff expect that widespread use would be made of the IFRS for SMEs/INPAG, e.g. where the proposed Tier 3 requirements are consistent with both the Tier 2 requirements and the IFRS for SMEs. If the IFRS for SMEs/INPAG were used in the circumstances referred to in paragraph 49(b), this would be likely to assist achievement of a consistent drafting style in the Tier 3 ED.

***Staff recommendations on Issue 2***

- 53 Staff recommend that, where when there is a recognition or measurement difference between the Tier 3 requirement and the Tier 2 requirement:
- (a) the drafting should be consistent with the approach to disclosures in Figure 1, as spelled out in paragraph 49; and
  - (b) if no comparable treatments in other jurisdictions/frameworks have been identified, for the reasons noted in paragraphs 51 and 52, the drafting of the Tier 3 requirement should be based on the IFRS for SMEs/INPAG where consistent with the substance of the Tier 3 requirement.

**Question 5 for Board members:**

**(Q5)** Do Board members agree with staff recommendations in paragraph 53 that, when there is a recognition or measurement difference between the Tier 3 requirement and the Tier 2 requirement, consistent with the approach to disclosures in Figure 1, consideration would be given to whether there are any comparable treatments in other jurisdictions/frameworks providing alternative sources of wording on which to base drafting of the Tier 3 requirement, and:

(a) if there are, the appropriate requirement selected from those comparable treatments should be selected as the source for drafting the Tier 3 ED proposal; or

(b) if there are not, a fit-for-purpose requirement should be drafted consistently with the substance of the Tier 3 requirement and based on the IFRS for SMEs/INPAG where consistent with the substance of the Tier 3 requirement?

If not, what do Board members suggest?