Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Post-Implementation Reviews**	**Meeting:**	September 2022 (M190)
Topic:	**NFP domestic PIRs – Summary of feedback on certain NFP topics**	**Agenda Item:**	9.2
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		Project Priority:	Medium
		Decision-Making:	Low
		Project Status:	Initial deliberations

Objectives of this paper

1. The objective of this staff paper is:

   (a) to provide the Board with a summary of feedback received from initial targeted outreach conducted on the following topics in relation to not-for-profit (NFP) entities:

      (i) control/consolidation;

      (ii) the definition of a structured entity;

      (iii) related party disclosures by public sector entities; and

      (iv) special purpose financial statements (SPFS) basis of accounting – compliance with Australian Accounting Standards; and

   (b) for the Board to decide which matters should be included in the Invitation to Comment (ITC).

Structure of this paper

2. This staff paper is set out as follows:

   (a) background and reasons for bringing this paper to the Board;

   (b) summary of feedback

      (i) summary and staff analysis of feedback received from the initial targeted outreach;

      (ii) summary and analysis of implementation issues previously considered by the Board; and

   (c) next steps and project timeline.

Background and reasons for bringing this paper to the Board

3. The Board considered the topics of related party disclosures, SPFS basis of accounting – compliance with Australian Accounting Standards, control and consolidation and the definition of a structured entity at the May and June 2022 meetings. This paper continues the Board's discussions, as set out in the timeline reviewed by the Board at its May 2022 meeting.

4. Staff have since conducted initial targeted outreach with eight stakeholders.[1] In addition to some general feedback, stakeholders also provided specific feedback on the 'known' issues previously discussed with the Board, as well as additional issues they are aware of. Staff have summarised and analysed this feedback as follows:

(a) Control and consolidation:

(i) Table 1 summarises and analyses feedback received from the targeted initial outreach;

(ii) Table 2 summarises and analyses known issues, including additional feedback obtained from targeted outreach;

(b) The definition of structured entities;

(c) Related party disclosures by NFP public sector entities; and

(d) SPFS basis of accounting – compliance with Australian Accounting Standards.

Summary of feedback

Control and Consolidation

5. Stakeholders provided some general feedback on AASB 10 *Consolidated Financial Statements* which has been summarised below:

(a) Almost all stakeholders noted that because AASB 10 is drafted from a for-profit sector perspective, some of the guidance in the Standard does not work as intended for the NFP sector. For example, stakeholders highlighted that one of the key differences between the two sectors is the relationships between entities and the objective and purpose of entities in the NFP sector where transactions are often not at arm’s length.

(b) Most stakeholders indicated that the guidance provided in Appendix E is very specific which can make it difficult to apply the guidance by analogy to entity-specific transactions which have their own facts and circumstances. It was suggested that more generic guidance could be helpful for the NFP sector.

(c) One stakeholder suggested that in their view the guidance provided in AASB 10 Appendix E is more relevant to smaller NFP entities and does not address some of the issues faced by larger NFP entities that have more complex operations and transactions.

(d) One stakeholder suggested that in some cases NFP entities did not understand why AASB 10 applied to them. They suggested more examples to illustrate different scenarios where control is present in the NFP sector and consolidated financial statements are prepared would be helpful.

1 This paper uses the following terms to describe the extent to which particular feedback was provided by respondents:

Term	*Extent of response among respondents*
All	8 Stakeholders
Almost all	7 Stakeholders
Most	5-6 Stakeholder
Some	2-4 Stakeholders
One	1 Stakeholder

PART A: Control/consolidation[2]

Table 1: Topics identified through initial targeted outreach

Feedback	Staff Analysis	Staff Recommendation
a) To be considered as part of the PIR		
Challenges identifying variable returns in the NFP sector		
Feedback indicated that there are challenges identifying variable returns in the NFP sector because the implementation guidance in AASB 10 Appendix E is too broad. Some stakeholders also noted that in the NFP sector, most returns are non-financial returns. Some stakeholders suggested that in most cases, meeting the variable returns criteria is straightforward because demonstrating that a relationship is "achieving or furthering the investors objectives" is easy. It was also suggested that meeting the variable returns criteria is often a default conclusion by NFP entities. This is particularly the case for religious organisations where they can rationalise that any activities of related entities (e.g. schools, aged care facilities or hospitals) are furthering the mission of the religious organisation. Conversely, some stakeholders noted that because the guidance in Appendix E is limited and so broad, the application of the requirements in practice can be	An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (AASB 10 paragraph 6). Paragraph B56[3] describes that variable returns are returns that are not fixed and have the potential to vary as a result of the performance of an investee. Variable returns can be positive, negative or both. Paragraph B57 provides examples of variable financial returns. Paragraph IG18 notes that the examples of returns in paragraph B57 indicate that the scope of the nature of returns is broad. Paragraph IG18 continues to describe that in the NFP Sector returns can be financial, non-financial, direct and indirect benefits and can include the achievement or furtherance of the investor's objectives.	Staff acknowledge there appear to be diverse views about variable returns in the NFP sector and that often judgement will be required. Given the apparent diversity, staff recommend including identifying variable returns in the ITC to seek feedback from stakeholders about whether there is a need for further guidance and clarity about variable returns for NFP entities. **Question for Board members** Q1. Do Board members agree with the staff recommendation to add identification of the variable returns to the ITC?

2 AASB 2013-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities – Control and Structured Entities* added Appendix E to AASB 10

3 The application guidance included in AASB 10 Appendix B (paragraphs denoted with a B prefix) are IFRS-equivalent paragraphs and therefore cannot be amended. The Australian Implementation Guidance included in AASB 10 Appendix E (paragraphs denoted with an IG prefix) are Australian-specific and therefore could be amended by the AASB.

Feedback	Staff Analysis	Staff Recommendation
challenging. They suggested clarity around what a variable return can be is needed. For example, is a variable return fulfilling a mission element of a congregation, notwithstanding that there are no rights to distributions or assets? Or should variable returns be interpreted more narrowly? It was suggested that once variable returns have been identified, it is less complex to understand whether there is control. However, the challenge is identifying variable returns initially. Example *Note: This example focuses on variable returns only and does not consider whether power is present or whether the variability of returns can be affected.* Church A establishes Hospital B to provide health care services. Hospital B is a separate legal entity with an independent Board that comprises 7 members. Church A has the right to appoint 3 directors to the Hospital B Board. Due to the legal structure of Hospital B, Church A has no right to access the net assets of the hospital. However, Hospital B is furthering the objectives of Church A by providing health care services and fulfilling the mission of the church by helping the sick and suffering. In this example, it is complex to understand if Church A has control over Hospital B. Hospital B is furthering the objectives of Church A by providing health care services to the sick and suffering and furthering the objectives of the Church could be considered a	Paragraph IG19 states that an investor's exposure, or rights, to variable returns from its involvement with an investee may give rise to indirect, non-financial returns, such as when achieving or furthering the objectives of the investee contributes to the objectives of the investor. For example, the provision of goods and services by the investee to its beneficiaries may affect the extent to which the investor's social policy objectives are furthered. Paragraph IG20 further provides an example that states that an investor would have the ability to use its power over the investee when it can direct the investee to work with the investor to further the investor's objectives. However, the existence of congruent objectives alone is insufficient for a NFP investor to conclude that it controls an investee (illustrated in Example IG1B).	

Feedback	Staff Analysis	Staff Recommendation
variable return for Church A albeit that the Church has no exposure to financial return.[4]		
Customary Business Practices		
Stakeholders provided feedback that it was unclear what effect customary business practices can have on the assessment of control in the NFP sector. Example *Note: This example focuses on variable returns only and does not consider whether power is present or whether the variability of returns can be affected.* School B establishes the Old School B Association. Old School B Association was established to promote the unity, welfare and advancement of past attendees of School B through a range of services. Each year, Old School B run many events however the annual fundraising gala is the Association's major fundraising event. The Association's Independent Committee of Management comprises seven members two of which are appointed by School B. The rules of the	Customary business practice is not specifically addressed in AASB 10, however AASB 10 and AASB 15 *Revenue from Contracts with Customers* consider similar issues. Control without a majority of the voting rights (de facto control) – AASB 10 When assessing control with less than a majority of voting rights AASB 10 requires investors to consider all facts and circumstances when determining whether the voting rights they hold are sufficient to give them power. AASB 10 paragraph B42(d)[5] notes that voting patterns at previous shareholder meetings is one of the factors an investor needs to consider. However, AASB 10 is clear that past voting patterns are only one of many matters that investors should consider. AASB 10 application example 8 also illustrates how past voting patterns at shareholder meetings can affect control conclusions.	Due to the uncertainty regarding the effect of customary business practices could have on control conclusions in the NFP sector, staff recommend including this issue in the ITC to obtain further feedback on the issue from stakeholders. **Question for Board members** Q2. Do Board members agree with the staff recommendation to add customary business practices to the ITC?

4 When assessing whether control is present, staff note that it is important to consider all facts and circumstances in totality, that is, to understand whether Church A also has power over Hospital B and whether they can affect the variability of the returns that they receive. In this limited fact pattern, it is unlikely that Church A has power as they can only appoint three of the seven directors and the right to appoint directors on its own is not necessarily a substantive right. It is also unclear whether Church A could affect the variability of returns and therefore it is also unclear whether Church A has control over Hospital B.

5 The application guidance included in AASB 10 Appendix B and AASB 15 Appendix B (paragraphs denoted with a B prefix) are IFRS-equivalent paragraphs and therefore cannot be amended.

Feedback	Staff Analysis	Staff Recommendation
Association permit Old School B Association to distribute the proceeds of fundraising activities to any entity they consider worthy. Whilst Old School B Association is permitted to distribute the proceeds of fundraising to any entity, historically they have always been distributed to School B. Despite having the ability to distribute to any entity, School B is unsure whether the Association has established a customary business practice by only distributing to them, which in turn could be considered to expose them to variable returns.[6]	Staff note however, that just because a shareholder has not exercised its voting rights in the past does not mean it will not exercise them in the future and therefore past voting patterns should be considered carefully when determining their impact on possible future voting patterns. <u>Customary business practice – AASB 15</u> Paragraph 10 of AASB 15 *Revenue from Contracts with Customers* states that a contract is an agreement between two or more parties that creates enforceable rights and obligations. Contracts can be written, oral or implied by an entity's customary business practices. The practices and processes for establishing contracts with customers vary across different legal jurisdictions, industries and may even vary within an entity. Paragraph 10 states that an entity shall consider those practices and processes in determining whether and when an agreement with a customer creates enforceable rights and obligations. AASB 15 paragraph 24 also notes that 'promises' can be implied by an entity's customary business practices and that those promises can raise a valid expectation in another party that the entity will do X because they have historically always done X.	

6 As above, when assessing whether control is present, staff note that it is important to consider all facts and circumstances in totality, that is, to understand whether School B also has power over the Association and whether they can affect the variability of the returns that they receive. In this limited fact pattern, it is unlikely that School B has power as they can only appoint two of the seven committee members and the right to appoint committee members on its own is not necessarily a substantive right. It is also unclear whether School B could affect the variability of returns and therefore it is also unclear whether School B has control over Old School B Association.

Feedback	Staff Analysis	Staff Recommendation
	AASB 15 paragraph B12(c) includes an example about needing to consider whether a customary business practice of not enforcing a right to payment renders the right to be unenforceable in a legal sense. AASB 15 paragraph B12(c) states that "an entity's customary business practices of choosing not to enforce a right to payment has resulted in the right being rendered unenforceable in that legal environment. However, notwithstanding that an entity may choose to waive its right to payment in similar contracts, an entity would continue to have a right to payment to date if, in the contract with the customer, its right to payment for performance to date remains enforceable". This suggests there could be circumstances where an established pattern of past practice affects legal rights. In the example of Old School B Association, they too have established a historical pattern of distributing fundraising proceeds to School B. However, the Association has the right to distribute proceeds to any entity in the future. Staff consider that whether and how many times the right to distribute proceeds to any entity has been historically exercised is not relevant, rather it is that the Association has the power to exercise that right. However, this could be affected by an established business practice resulting in the right being considered 'unenforceable'. If the right was considered unenforceable this could affect the control conclusion by School B in relation to the Association.	

Feedback	Staff Analysis	Staff Recommendation
b) No further work is needed		
Veto rights		
Feedback suggested that assessing whether veto rights are substantive or protective in the NFP sector is an area of concern. It was also suggested that entities in the NFP sector have difficulty applying the guidance due to perceived inconsistencies in AASB 10. For example, stakeholders highlighted that AASB 10 notes that veto rights can be indicative of power and are therefore substantive rights. However, in some examples in AASB 10 Appendix E veto rights are illustrated as protective rights and the examples are not well explained. It was noted that veto rights are generally seen as protective rights that are designed to protect the interests of their holder without giving that party power [to direct the relevant activities] over the investee and are therefore often not considered when assessing whether one party has power over another due to AASB 10 paragraphs B27 and IG15-IG17.[7] Example IG2C illustrates a veto right that is exercisable only in exceptional circumstances and concludes it is a protective right because it is a safeguard for the charity. However, if instead of the veto right only being exercisable in exceptional circumstances – that is, when	To have power over an investee, an investor must have existing rights that give the investor the current ability to direct the relevant activities of the investee (AASB 10 paragraph B14). Paragraph B15(d) states that "rights to direct the investee to enter into, or veto any changes to, transactions for the benefit of the investor" is an example of a right that can give an investor power. However, when assessing whether an investor has power, only substantive rights are considered. This requires judgement and the application guidance in AASB 10 paragraphs B22-B28 (relating to substantive rights) is important. Protective rights are defined in AASB 10 as "rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate". Therefore, protective rights are those rights that relate to "fundamental changes to the activities of an investee or apply in exceptional circumstances" (AASB 10 paragraph B26). Because protective rights are designed to protect the interests of their holder without giving that party power over the investee to which those rights relate, an investor that holds only protective	Whilst staff consider veto rights in the NFP sector could be more likely to be protective, for example to ensure reputational risks are minimised, staff acknowledged that assessing whether veto rights are substantive or protective requires judgement and consider that providing additional guidance or examples may not be overly helpful. Instead, staff consider that stakeholder education may be most beneficial. This is because stakeholder education could address the perceived inconsistencies within the Standard, whilst not jeopardising the principal of transaction-neutrality. However, as noted ultimately determining whether a right is protective, or substantive is a matter for judgement after considering all the relevant facts and circumstances. For this reason, staff do not recommend including veto rights in the

7 The application guidance included in AASB 10 Appendix B (paragraphs denoted with a B prefix) are IFRS-equivalent paragraphs and therefore cannot be amended. The Australian Implementation Guidance included in AASB 10 Appendix E (paragraphs denoted with an IG prefix) are Australian-specific and therefore could be amended by the AASB.

Feedback	Staff Analysis	Staff Recommendation
a potential board member is deemed unsuitable, if the veto right was exercisable under any circumstances, would the veto right still be considered protective? It was also noted that example IG2C states that veto right "has only been enforced once, when a proposed board member was found to have a history of fraudulent activities". However, if or how many times a veto right has been exercised does not appear to be relevant, what is relevant is whether an entity has the power to exercise the right. Therefore, the effect of 'established business practices' on veto rights was also raised (see Customary Business Practices above for additional discussion). In example IG1B, it was noted that "decisions made by the association's board are reviewed by the religious organisation, which may offer advice to the association". However, if the religious organisation was able to veto any decision of the Board would the conclusion about the nature of the rights in the example change. It was noted that because AASB 10 is an IFRS-equivalent Standard also applied by for-profit entities, providing specific guidance about how to consider veto rights in the NFP sector is unlikely to be possible due to the AASB's policy of transaction-neutrality as well as concerns it could be considered to be interpreting IFRS-Standards. The following two examples illustrate some of the challenges assessing veto rights in practice. These two examples are based on the same fact pattern however	rights cannot have power or prevent another party from having power over an investee (see paragraph B27). Applying the concepts in IG15 and the examples given in IG17, it is possible that veto rights in the NFP sector are more likely to be protective to ensure reputational risk is minimised. However, staff consider that this is a matter for judgement, and the specific facts and circumstance of each relationship need to be considered.	ITC. However, staff do recommend stakeholder education. **Question for Board members** Q3. Do Board members agree with the staff recommendation not to add veto rights to the ITC? Q4. Do Board members agree with the staff recommendation for stakeholder education?

Feedback	Staff Analysis	Staff Recommendation
the possible conclusion about whether the veto right is considered protective or substantive may differ due to the relationship between the entities and their perceived relatedness. Example: *Note: This example focuses on power only and does not consider whether variable returns are present or whether the variability of returns can be affected.* Church A which operates under the Canon law establishes School B to provide faith-based education to the community. School B is a separate legal entity with an independent Board that comprises seven members. Church A has the right to appoint two members. All Board members have one vote, and a majority is required for decisions to be made. The management of School B is responsible for the day-to-day operations. However, the Board approves the annual budget and business plan. Whilst Church A cannot control the Board of School B with only two votes, when School B was established, the Church was given the ability to veto any decisions made by the Board of School B. In the example, it may be concluded that the veto right is a protective right to ensure that School B is meeting the objectives of Church A and meeting its responsibilities under the Canon Law. Alternatively, the right to veto any decisions made by the Board of		

Feedback	Staff Analysis	Staff Recommendation
School B could also be considered a substantive right since the Church has the power to veto any decision. Example: *Note: This example focuses on power only and does not consider whether variable returns are present or whether the variability of returns can be affected.* University A establishes Sports Association B as a separate legal entity with an independent Committee of Management that comprises seven members, two of whom is appointed by University A. All committee members have one vote, and a majority is required for decision to be made. The management of Sports Association B is responsible for the day-to-day operations. However, the Committee approves the annual budget and business plan. Whilst University A cannot control the Board of Sports Association B with only two votes, when Sports Union B was established, University A was given the ability to veto decisions any decisions about the Association. In this example, it may be concluded the veto right is a substantive right to ensure that Association B is operating as intended due to a greater perceived separation between the University and the Association. However, the right to veto any decisions made by the could also be considered a protective right		

Feedback	Staff Analysis	Staff Recommendation

6. At its May and June 2022 meetings, the Board was provided with a high-level summary of known issues on each of the topics to be considered in this PIR. In the below table, staff have summarised and analysed the known issues, including summarising any additional stakeholder feedback received on these issues during the initial targeted outreach.

Table 2: Implementation issues previously discussed with the Board

Feedback	Staff Analysis	Staff Recommendation
Application of the control model in the NFP sector		
As noted in the June 2022 staff paper, feedback suggests that some stakeholders have concerns about applying the control model in the NFP private sector. Specifically, AASB 10 requires entities to consolidate other entities they do not believe they have 'true' control over (that is, where the parent has 'theoretical' control through constitutional requirements rather than an in-practice exercise of control). Stakeholders also observed that many NFP entity organisational structures do not naturally fit into AASB 10's "control" definition and indicated that preparers and auditors might disagree with some of the control conclusions illustrated in Appendix E of AASB 10. It was noted that some NFP entities do not prepare consolidated financial statements even though they meet the control criteria in AASB 10 because they	The objective of AASB 10 is to outline a single basis for consolidation where an investor controls an investee. The control model in AASB 10 is predicated on the basis that "an investor should consolidate an investee and present in its consolidated financial statements the investee's assets, liabilities, equity, income, expenses and cash flows, if the investor has the current ability to direct those activities of the investee that significantly affect the investee's returns and can benefit by using that ability. An investor that is exposed, or has rights, to variable returns from its involvement with an investee but does not have power over the investee so as to affect the amount of the investor's return from its involvement does not control the investee"[8] Applying the control model in the NPF sector, AASB 10 paragraph IG10 outlines that a NFP investor can have	Whilst staff acknowledge the concerns of some stakeholders that consolidating the financial position and performance of Church A and School B (for example) could be unhelpful as members of the school are unlikely to be interested in the results of the church and vice versa. Staff note that the principle of AASB 10 is that where there is control consolidated financial statements should be presented. However, staff also acknowledge that control in the NFP sector appears to be an area of significant concern, especially with the possible removal of SPFS in the NFP sector. Therefore, staff recommend adding the application of the control model in the NFP sector to

8 IFRS 10 *Consolidated Financial Statements* paragraph BC31

Feedback	Staff Analysis	Staff Recommendation
disagree with the conclusion. To avoid consolidation, they prepare SPFS. In their view, whilst there might be a relationship and shared objectives between the two entities consolidation is not always appropriate because a consolidated financial statement might not meet the user's needs. Feedback also revealed that there were concerns that one entity's financial position and performance may be obscured by the financial position and performance of another entity. Feedback from a NFP Project Advisory Panel member raised concerns over identifying and consolidating a controlled entity because the relevant information may not always be available to the entity due to practices in the sector (e.g. secrecy or lack of documentation). <u>Feedback from targeted outreach</u> Most stakeholders agreed that some entities, including religious organisations, are preparing SPFS to avoid having to prepare consolidated financial statements. This could be for many reasons including, because: • obtaining the necessary information to prepare consolidated financial statements is difficult. At some levels within a 'group' (e.g. a congregation within a church) appropriate books and records might not be kept, completeness of records is a concern and auditability is therefore also affected. Obtaining information might also be difficult due to secrecy which can be common in religious organisations. However, one Stakeholder did note that in their experience, entities are not unable to	power over an investee even if it does not have responsibility for the day-to-day operation of the investee. Paragraph IG19 states that an investor's exposure, or rights, to variable returns from its involvement with an investee may give rise to indirect, non-financial returns, such as when achieving or furthering the objectives of the investee contributes to the objectives of the investor (see discussion in Table B) Paragraph IG20 notes that an investor would have the ability to use its power over the investee when it can direct the investee to work with the investor to further the investor's objectives. However, paragraph IG20 also notes that congruent objectives alone are insufficient for a NFP investor to conclude it controls an investee. When the control criteria in AASB 10 is met, consolidated financial statements must be prepared.	the ITC to seek more information from stakeholders about any difficulties they have applying the control model and any concerns they have. **Question for Board members** Q5. Do Board members agree with the staff recommendation to add application of control model to the ITC?

Feedback	Staff Analysis	Staff Recommendation
prepare consolidated financial statements due to a lack of information, they are not preparing consolidated financial statements because they don't believe they are useful. • the consolidated financial statements are not typically useful to users, with users preferring to review the financial information of the specific operations they are interested in (e.g. a hospital, or a school, or a branch rather than an aggregation of all activities). Feedback also indicated that implementing the concept of control in the local government sector can be challenging. For example, local authorities can find it difficult to implement the concept of control when it comes to organisations and entities they have connections with through constitutions or other agreements. It was noted that even if the legal document or a constructive arrangement indicates potential control from the perspective of AASB 10, there is always a question of whether consolidated financial statements would really represent a fair picture of the councils' business. The stakeholder suggested that in the case of liquidation of a "controlled" party, it is difficult to conclude whether the council would receive any residual interest in that business. Therefore, councils try to avoid complicated consolidation accounting by including additional disclosures or by		

Feedback	Staff Analysis	Staff Recommendation
avoiding it (see also Assessing control without an ownership interest for additional discussion).[9] Another stakeholder was of the view that the issue of control and consolidation can be impacted by the complexities of the legal structures in religious organisations along with how religious organisations operate. One stakeholder thought it was important to consider what the appropriate level is for a possible consolidation and where 'ultimate' control exists. For example, in a religious organisation is the appropriate 'parent' the church, or is it the next 'level' up. Example *Note: This is a very simple example illustrative what staff understand to be a common fact pattern.* Church A establishes School B to provide faith-based education to the community. School B is a separate legal entity with an independent Board that comprises 5 members. Church A has the right to appoint 3 members. Due to the legal structure, Church A is not permitted to access funds of School B to fulfil its operational or day-to-day needs. However, School B is furthering the objectives of Church A by providing faith-based education.		

9 Staff sought to obtain more information about these challenges, however as at the date of this paper had not been able to do so. Therefore, staff will provide Board members with a verbal update on this matter at the September 2022 meeting.

Feedback	Staff Analysis	Staff Recommendation
There is a lease agreement between Church A and School B. However, the terms of the lease agreement are fixed so the lease does not give rise to any variable returns. Church A has power over School B as it controls the Board of the School. Church A has exposure to variable returns in the form of furtherance of objectives. Church A can also affect the variability of its returns through its power over the Board of School B. In this example, all other things being equal, Church A controls School B and consolidated financial statements would be required. However, currently Church A prepares SPFS to avoid preparing consolidated financial statements because in their view the users of the Church and the School have different information needs and consolidated financial statements are not considered to provide useful information. Most stakeholders acknowledged that preparing consolidated financial statements could at times obscure the financial position and performance of some entities. However, where this is a concern, if an entity wished to disclose discrete information for individual operations within a consolidated group for transparency, information similar to that provided by AASB 8 *Operating Segments* segment reporting disclosures would likely be useful to users.		

Feedback	**Staff Analysis**	**Staff Recommendation**
Assessing control without an ownership interest		
As noted in the June 2022 staff paper, stakeholder feedback indicates that assessing whether a NFP entity has rights that give rise to power can be challenging due to the legal structure of some entities. For example, companies limited by guarantee (CLBG) are often prohibited by their constitution from distributing to their members. Instead, the constitution commonly requires any surplus assets to be distributed to a like-minded entity. This prohibition also exists in other structures such as Incorporated Associations. Stakeholder feedback questioned whether the ability to direct distributions on the winding up of a CLBG gives rise to power and an exposure to variable returns. It was noted that assessing control without an ownership interest is equally relevant to Associations and other types of NFP entities. Example Entity A establishes CLBG B. CLBG B is governed by an independent Board of Directors. The Board of CLBG B has six members, one of whom is appointed by Entity A. Entity A also provided an initial investment to enable CLBG B to undertake a particular activity. CLBG B is prohibited for distributing profits to its members and on winding up, CLBG B must distribute any surplus net assets to another like-minded NFP entity. As Entity A provided an initial investment to CLBG B it has the ability to ability to specify which	Appendix E paragraph IG17 provides examples of protective rights, including IG17(e) where a philanthropic trust provides resources to a charity on the condition that the net assets of the charity are distributed to a similar organisation undertaking similar activities if the charity is liquidated. For this reason, the right to direct distributions on winding up of a NFP entity may be considered a protective rather than a substantive right which indicates that Entity A may not have power over CLBG B in the example provided. However, in practice, staff understand that when surplus assets are distributed back to the investor, investors often conclude they have control. Conversely, when surplus assets are distributed to an unrelated entity, determining whether or not the investor has control is less clear, and divergence in practice has emerged. In some cases, investors conclude they have control, whereas, in others, they do not.	Staff note the existence of divergence in practice when assessing the effect distributions can have on determining whether an entity has control. For this reason, staff recommend adding assessing control without an ownership interest to the ITC. **Question for Board members** Q6. Do Board members agree with the staff recommendation to add assessing control without an ownership interest to the ITC?

<table>
<tr><th>Feedback</th><th>Staff Analysis</th><th>Staff Recommendation</th></tr>
<tr><td>like-minded entity should receive the surplus assets on winding up.

When assessing whether Entity A controls CLBG B, Entity A must consider whether its ability to control how CLBG B distributes any surplus assets on winding up is a substantive right or a protective right. This is an important consideration even if Entity A itself is not entitled to the distribution. Whether the right is substantive or protective is also affected by how many members CLBG B has (e.g. the more members CLBG B has the more important the distribution right becomes).

Entity A must also consider whether its ability to direct the distribution of surplus assets also gives rise to an exposure to variable returns.</td><td></td><td></td></tr>
<tr><td colspan="3">Principal versus Agent when determining control</td></tr>
<tr><td>As noted in the June 2022 staff paper, there are situations in the NFP public sector where it is unclear whether or not a party is an agent for the purposes of assessing control. In the public sector, returns are usually in the form of policy outcomes rather than financial outcomes therefore applying the guidance can be difficult.

Feedback noted that there appeared to be inconsistent conclusions in similar situations. It has been suggested that the existing guidance in AASB 10 Appendix E is generally useful as it clarifies/ confirms how to analogise the requirements for the public sector. However, in</td><td>The existing guidance in IG 21 to IG 24 on delegated power has been useful for confirming requirements in the public sector.

According to IG 21, an investor with decision-making rights is required by paragraph B58 to determine whether it is a principal or an agent.

According to paragraph B58, an agent is a party primarily engaged to act on behalf and for the benefit of another party or parties (the principal(s)) and therefore does not control the investee when it exercises its decision-making authority. Thus,</td><td>Staff recommend adding principal versus agent to the ITC.

Question for Board members

Q7. Do Board members agree with the staff recommendation to add principal versus agent to the ITC?</td></tr>
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Feedback	Staff Analysis	Staff Recommendation
some cases, it was necessary to apply the for-profit guidance that applies to managed funds. This was challenging for finance professionals who do not have a background within the finance sector. <u>Feedback from targeted outreach</u> One stakeholder suggested that religious organisations have complex organisation structures and can be governed by the Canon Law for example. It was suggested that where this is the case it could be difficult to understand if an individual is acting in a personal capacity or as an agent for the religious organisation. Feedback from one stakeholder also indicated that there is a need for more examples in scenarios where there could be confusion over who is considered a principal in the NFP private sector.	sometimes a principal's power may be held and exercisable by an agent, but on behalf of the principal. A decision maker is not an agent simply because other parties can benefit from the decisions that it makes. Paragraphs B60–B72 provide guidance on determining whether a decision maker is an agent or a principal. However, the use of for-profit guidance in some scenarios could cause inconsistent conclusions.	

PART B: The definition of a structured entity[10]

Feedback	Staff Analysis	Staff Recommendation
As noted in the June 2022 staff paper, staff were not aware of any implementation issues with applying AASB 12 *Disclosure of Interests in Other Entities* Appendix E by NFP entities. <u>Feedback from targeted outreach</u> Feedback from one stakeholder indicated that the concept of a structured entity is not clear enough for the	-	As only limited feedback has been received, staff recommend adding this matter to the ITC to seek broader stakeholder feedback. **Question for Board members**

10 AASB 2013-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities – Control and Structured Entities* added Appendix E to AASB 12.

Feedback	Staff Analysis	Staff Recommendation
local government industry. One stakeholder suggested more examples are needed to help with the application of this concept.[11]		Q8. Do Board members agree with the staff recommendation to add the definition of structured entity to the ITC?

PART C: Related Party Disclosures[12]

Feedback	Staff Analysis	Staff Recommendation
As noted in the May 2022 staff paper, following the issue of AASB 2015-6, staff recall receiving feedback from constituents voicing concerns about their entity's ability to obtain the information necessary to prepare the disclosures required by AASB 124. This information included: (a) challenges in identifying a complete set of related parties; (b) the completeness of representations made by related parties completing documentation about their engagements with the entity and the entity's ability to compel completion and return of such forms; and (c) the extent of information that related parties were required to provide, in part because of the 'close family member' provisions of the Standard.	To support the implementation of AASB 124 by public sector NFP entities the Board added specific implementation guidance to AASB 124. The guidance was added to assist NFP public sector entities with applying the requirements of AASB 124, noting that AASB 124 was drafted from a for-profit perspective. The guidance was also intended to assist NFP public sector entities with determining the extent of information required to meet the objective of AASB 124. Staff consider that challenges in identifying a complete set of related parties is not a public sector-specific issue and consider the requirements of AASB 124 should be sufficient. However, staff acknowledge that for some public sector entities the assessment may be complex. In response to concerns from stakeholders about the operationalisation of AASB 124 in the public sector, primarily in relation to assessing the materiality of	Whilst no new feedback was obtained during targeted outreach and AASB 124 has been applied by public sector entities for some time it is possible that historical stakeholder concerns have resolved, staff recommend adding this matter to the ITC to seek broader stakeholder feedback. **Question for Board members** Q9. Do Board members agree with the staff recommendation to add related party disclosures in the public sector to the ITC?

11 Staff sought to obtain more information about these challenges, however as at the date of this paper had not been able to do so. Therefore, staff will provide Board members with a verbal update on this matter at the September 2022 meeting.

12 AASB 2015-6 *Amendments to Australian Accounting Standards – Extending Related Party Disclosures to Not-for-Profit Public Sector Entities* extended the scope of AASB 124 *Related Party Disclosures* to apply to NFP public sector entities.

Feedback	Staff Analysis	Staff Recommendation
Staff also heard concerns raised about: (a) data privacy; and (b) the auditability of the related party disclosures. In addition, some constituents queried the appropriateness and value of the requirements in relation to Indigenous Australian-focused or located public sector entities. The concerns stem from the apparent capture of a wide net of peoples and entities when considering the definition of a related party Feedback from targeted outreach No additional feedback was obtained from targeted outreach activities. However, it was noted that one NFP public sector entity has implemented specific procedures to obtain the information needed to support the majority of the related party disclosures required and therefore the concerns raised above were not relevant to them.	transactions with a key management personnel (KMP) related parties (e.g. whether a transaction with a KMP related party that did not occur as part of a public services provider/taxpayer relationship is always material for disclosure in general purpose financial statements), the Board issued an Agenda Decision. The Agenda Decision considered stakeholder concerns, however concluded that it was not necessary to add the issue to the AASB's agenda because existing guidance in Australian Accounting Standards is sufficient to address the issue of whether a transaction with a KMP related party that did not occur as part of a public services provider/taxpayer relationship is always material for disclosure in general purpose financial statements.[13]	

13 Whilst not directly related to related party disclosures by public sector entities, staff note that recent changes to the ACNC requirements providing relief to large charities preparing SPFS with only one Key Management Personnel (KMP) receiving remuneration. The changes provide relief to the entity from disclosing KMP information to provide anonymity for any one remunerated KMP individual. Staff acknowledge these changes however do not consider it is necessary to seek feedback in the ITC on whether similar 'aggregation' relief might be helpful for NFP entities in both the private and public sectors in relation to related party disclosures.

PART D: SPFS basis of accounting – compliance with Australian Accounting Standards[14]

Feedback	Staff Analysis	Staff Recommendation
As noted in the May 2022 staff paper, staff are not aware of any specific implementation issues with the Standard. <u>Feedback from targeted outreach</u> Generally, feedback from almost all stakeholders from targeted outreach activities revealed that entities either: (a) stated compliance because they knew they complied, (b) stated non-compliance because entities were aware that they have not complied with the recognition and measurement requirements of one or more Standards (e.g. not correctly accounting for long service leave); or (c) disclosed that they have not made such an assessment. Initial feedback did not indicate any significant concerns with providing these additional disclosures, nor that any significant costs were incurred by preparers. However, stakeholders acknowledge that the disclosures were only required to be made by part of the NFP population (e.g. Corporations Act and ACNC regulated entities).	Staff note that in response to the proposals in ED 293 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements* (the predecessor to AASB 2019-4), stakeholders raised concern that the costs of the Board's proposals exceeding the benefits of that information The Board decided to include an option for a NFP private sector entity to disclose that they have not assessed whether or not the accounting policies disclosed in the special purpose financial statements comply with all the recognition and measurement requirements in Australian Accounting Standards (except for requirements set out in AASB 10 or AASB 128), because allowing an entity to make such a disclosure would require minimal additional effort … however, would highlight potential instances of non-compliance with the recognition and measurement requirements in Australian Accounting Standards to users of the special purpose financial statements, as well as potential governance issues, and would also allow users of the special purpose financial	Staff consider that initial feedback from stakeholders about how the disclosures have been applied in practice is consistent with expectations. Feedback about their usefulness to users is also consistent with expectations. However, as only limited feedback has been received, staff recommend adding this matter to the ITC to seek broader stakeholder feedback.[15] **Question for Board members** Q10. Do Board members agree with the staff recommendation to add SPFS basis of accounting – compliance with Australian Accounting Standards to the ITC?

14 These requirements were added to AASB 1054 *Australian Additional Disclosures* by AASB 2019-4 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Not-for-Profit Private Sector Entities on Compliance with Recognition and Measurement Requirements*

15 Staff are currently undertaking research examining the common transactions for NFP entities in conjunction with the NFP Private Sector Financial Reporting Framework project. As part of this research, staff also intend to examine the adoption of these disclosure requirements in practice in the NFP sector.

Feedback	Staff Analysis	Staff Recommendation
One stakeholder indicated that from a user perspective, these disclosures provide important information. The stakeholder was concerned that by not providing these disclosures transparency and comparability of SPFS may be compromised.	statements to seek additional information if required.[16]	

16 AASB 2019-4 paragraph BC51