CONSULTATION PAPER PART 1: NON PROFIT ORGANISATION ACCOUNTABILITY LANDSCAPE

Section 1: What are Non Profit Organisations?

1.1 The objective of the International Financial Reporting for Non Profit Organisations (IFR4NPO) project is to develop internationally applicable financial reporting guidance for Non Profit Organisations (NPOs) that will:

- address the most important issues that are common across the NPO sector; and
- meet the general financial reporting requirements of funders and regulators as well as preparers.

1.2 The entities that are potentially within the scope of the Guidance are diverse. They range from small membership organisations funded by and delivering services to a limited number of members to large international relief organisations providing a wide range of services in many countries and in receipt of significant donations and commercial revenue streams.

1.3 As well as diversity in terms of type and size of entity, there is also diversity globally in the legal and regulatory environments in which NPOs operate. In some jurisdictions for example, their status may be formally recognised through special legal and fiscal status and privileges. In others no such recognition may exist with NPOs treated in the same manner as profit making entities.

What is a Non-Profit Organisation? – Insight from academic studies and the approach of different jurisdictions

1.4 There are a number of different ways of defining the NPO sector. Examining academic studies of NPOs, there is often a focus on the structural and operational features of entities. This includes a focus on the extent to which an entity is constituted on a not-for-profit basis, is self-governing, and is established for a public or social benefit.

1.5 Many studies, however, rely on legal definitions that are not applicable internationally (such as the concept of a "charitable" organisation) or which could exclude NPOs with purposes that may be seen as too narrowly focussed on a specific group (such as some membership organisations).

1.6 Different jurisdictions have also taken a number of approaches to defining which entities are within scope for financial reporting guidance that is aimed at NPOs. This often results in a focus on whether organisations meet the definition of a "public benefit entity". It also raises difficult questions such as whether an organisation can be seen as an NPO if as part of meeting their primary objectives they generate some profits and then distribute those profits to owners, members and other resource providers.

Broad characteristics approach to defining Non Profit Organisations

1.7 Highlighted below are examples of approaches that have been taken by a number of jurisdictions to defining NPOs. It shows that each jurisdiction defines the entities to which standards and guidance apply based on their own reporting needs and the broader legal, regulatory and financial reporting framework that is in place.

Canada

Canadian GAAP incorporates a test of public benefit purpose but also focuses more specifically on the not-for-profit characteristics of an entity and in particular financial returns. It defines a not-for-profit private organisation (NFPO) as being:

"*"an entity, normally without transferable ownership interests, organized and operated exclusively for social, educational, professional, religious, health, charitable or any other not-for-profit purpose. An NFPO's members, contributors and other resource providers do not, in such capacity, receive any financial return directly from the organization."*

Preface to the CPA Canada Handbook - Accounting, paragraph 3(c)

New Zealand

In New Zealand's accounting standards framework for for-profit and public benefit entities (both not-for-profit and public sector entities), XRB A1 Appendix A defines public benefit entities

"as reporting entities whose primary objective is to provide goods or services for the general public or social benefit and where any equity has been provided with a view to supporting that primary objective rather than with a view to providing a financial return to equity holders."

External Reporting Board Standard A1 – Application of the Accounting Standards Framework – Appendix A - External Reporting Board New Zealand – May 2019

United Kingdom

1.The Financial Reporting Council in the United Kingdom when developing FRS 102 (which modifies IFRS for SMEs and is designed to apply to the general purpose financial statements and financial reporting of entities including those not constituted as companies and those that are not profit oriented) noted that a public benefit entity is:

"An entity whose primary objective is to provide goods or services for the general public, community or social benefit and where any equity is provided with a view to supporting the entity's primary objectives rather than with a view to providing a financial return to equity providers, shareholders or members."

FRS 102 The Financial Reporting Standard Applicable in the UK and the Republic of Ireland - Financial Reporting Council – March 2018

1.8 In order to ensure that the project meets its objectives, however, there needs to be some determination of the NPOs that the Guidance is aimed at. This will ensure that the Guidance is developed to meet their reporting needs, and does not focus on the more general financial reporting issues of entities which are met by existing guidance aimed at either the for profit private sector or the government and wider public sector.

1.9 For the purposes of this project, the more restrictive the definition of an NPO that is used to the higher the likelihood of putting out of scope entities that might benefit from the Guidance.

1.10 Determining the scope of the public sector entities that it was setting standards for was a challenge faced by the International Public Sector Accounting Standard Board (IPSASB). It met this challenge by focussing on the key features of the public sector and the economic events and transactions relevant to it.

1.11 Given the diverse range of organisations, jurisdictions and legal and regulatory frameworks, it would appear appropriate to adopt a similar approach to defining the NPOs that are potentially within the scope of this project. By focussing on the broad characteristics of NPOs rather than a narrow definition, it will be possible for the Guidance to be developed to address the financial reporting issues that arise from the key economic events and transactions most relevant to a diverse range NPOs.

1.12 Some of the key features of the not for profit sector, as well as relevant economic events and transactions that are highlighted in academic literature, and which lead to the need for the development of internationally applicable financial reporting guidance for NPOs include:

- The significance of donations and grant funding;
- The need to demonstrate to resource providers how funding has been utilised, particularly where there are restrictions;
- The prevalence of assets that are not held to maximise profits or economic returns; and
- The importance of narrative and performance reporting given the primacy of non-financial objectives.

1.13 On the basis of these key features, it is proposed that the Guidance be developed primarily to apply to NPO reporting entities that display the broad characteristics in Figure 1 below.

1.14 While it is expected that an NPO would display all of these broad characteristics to a greater or lesser extent, it is not proposed that the Guidance will explicitly look to exclude entities from scope if they do not meet all of the broad characteristics. This will enable the Guidance to be of use and relevance to entities that may not meet all of the broad characteristics but are faced with similar economic events and transactions that existing financial reporting standards do not provide adequate guidance for.

Figure 1

Service delivery objectives	• The entity's primary objective is to deliver goods and/or services for the general public, community or social benefit and not to generate a financial return for providers of resources • NPOs will and should have financial objectives such as maximising economy, efficiency, and effectiveness in the use of resources.
Use of supluses	• NPOs may generate a financial surplus from some or all of their activities. • Where a surplus is generated this will be directed to furthering the entity’s primary service delivery objectives rather than providing financial benefits to providers of resources.
Funding sources	• Funding through donation, grant or other form of non-exchange transaction is financially significant to the entity • Funding sources may be non-monetary, such as volunteer time, or subject to certain restrictions or conditions that limit how they may be utilised. • NPOs may rely on investment income generated by financial assets provided as a donation in previous years.

1.15 Having acknowledged that there is diversity in the range of organisations that might be described as an NPO, it must also be recognised that there is also diversity in the size and complexity of these organisations. They range from community organisations with no employed staff to international humanitarian organisations, from universities to membership organisations.

1.16 Micro entities, are likely to comprise a significant part of the NPO community in many jurisdictions (depending on local definitions). For example, around 60 percent of NPOs in New Zealand report using the most basic accounting tier and c.50 percent of voluntary organisations in the United Kingdom are designated as micro entities as they have less than £10k per annum in income. Micro entities have basic accountability and reporting requirements that can be satisfied with simple receipts and payments information. The largest

NPOs on the other hand, while having complex accountability arrangements, are more likely to have the resources necessary to meet a wide range of reporting requirements.

1.17 While of relevance to a diverse range of entities the Guidance is expected, however, to be of most benefit to those NPOs that are of sufficient size and complexity to have problems with existing accountability arrangements. Problems with current accountability arrangements are the key driver behind IFR4NPO. In Section 2 we examine what NPOs are accountable for and to who, and the high-level implications of this for NPO financial management and accountability arrangements.

General Matters for Comment 1
This section has developed a broad characteristics approach to defining NPOs that will be in scope when developing and then applying the Guidance. 1.1 - Do you agree with the broad characteristics approach to defining NPOs? If not, why not? What alternative approaches would you propose, and why?

Section 2: Who are Non Profit Organisations accountable to and what are they accountable for?

2.1 Accountability entails an acceptance of responsibility for decisions and actions, and an expectation of being required to explain those decisions and actions when asked by those to whom the relevant individual or entity is accountable. In this section we examine who NPOs are accountable to, what for, and the high-level implications of this for NPO financial management and accountability arrangements.

Who are NPOs accountable to?

2.2 Examining the three characteristics identified in Section 1, it is possible to define two broad groups that NPOs are accountable to. These are:

- service users, who are the direct beneficiaries of the activities provided by the NPO; and
- resource providers, who provide cash funding or donations of goods, services or time.

2.3 The large number of individuals and groups that NPOs are potentially accountable to, and the privileged fiscal and regulatory status they have in many jurisdictions, suggests that they also have a broader public accountability.

Service users

2.4 Service users comprise those who are reliant on the goods and services that are provided by the NPO. Given the diverse range of objectives of NPOs, these goods and services are also diverse. They will range from the free provision of essential public goods such as healthcare and education, through to more commercially focussed activities such as the rent of social housing or the sale of support services. They can also include more intangible goods and services, such as advocacy work.

2.5 An NPO's service users will also be as diverse as the goods and services provided by the NPO. Service users could extend to a large cross-section of the general public, or alternatively could be restricted to a defined section of society or be restricted just to members of the NPOs.

2.6 In addition to those in direct receipt of goods and services, the service user's category can also be expanded to include those who may represent NPOs. This could include elected representatives, government appointed individuals, or others who have been given the responsibility to support and uphold a service user's wellbeing.

Resource providers

2.7 Resource providers comprise those that the NPO relies on for the financial and other resources that it utilises to deliver goods and services. For many NPOs that are reliant on grants and other donations for the majority of their incoming financial resources, donors will be a very important group of resource providers. These donors may be corporate or other institutional entities such as governmental organisations and philanthropic bodies. They may also include volunteers who provide free labour and services to the NPO, and the general public providing financial donations.

2.8 NPOs may also sell goods and services to individuals and other corporate entities. As noted when examining the broad characteristics of NPOs, they may generate financial surpluses from these activities. Generally, however, where NPOs sell goods and services they are at a below market rate designed to support the primary non-financial objectives of the entity rather to achieve profit maximisation. Surpluses are therefore used to support the entity's primary service delivery objective.

2.9 In addition to the direct receipt of financial resources, through both donations and grants and the sale of goods and services, NPOs may also receive financial and other resources from government. These can be through fiscal privileges, such as differential taxation rates and rebates, or a broader legislative and regulatory environment that supports them in the achievement of their objectives.

2.10 NPOs may also receive funding through commercial lending arrangements. These may include specific borrowings, finance leases or bank overdrafts.

Public accountability

2.11 Public accountability is an expansive view of accountability as it recognises not just the accountability relationship between management and the owners of an entity as is commonly seen to apply to many private entities, but also a general accountability of the management and entity to the public at large.

2.12 As will be further highlighted in discussing international financial reporting frameworks in Section 5 some private sector entities are viewed as having public accountability if they are financed by publicly traded debt or equity instruments or they hold financial assets in a fiduciary capacity. Public accountability in this case being seen as essential to the efficient and effective operation of public markets in such financial assets and services.

2.13 In the public sector, services are primarily funded by taxation revenues, or fees and charges set to recover costs where there is no private sector provider of services. Service recipients depend on the provision of these services over the long-term. The prevalence of essential services provided as a result of compulsory taxation and/or in a non-competitive environment results in the need to take a broader perspective of public accountability. As such all government and public sector entities are seen to have public accountability.

2.14 NPOs may be regarded as more akin to public sector entities whose primary function is to provide services to enhance or maintain the well-being of citizens and other eligible residents. So public accountability is also broader for the sector. This has implications for financial reporting as will be discussed further in later Sections of this Consultation Paper.

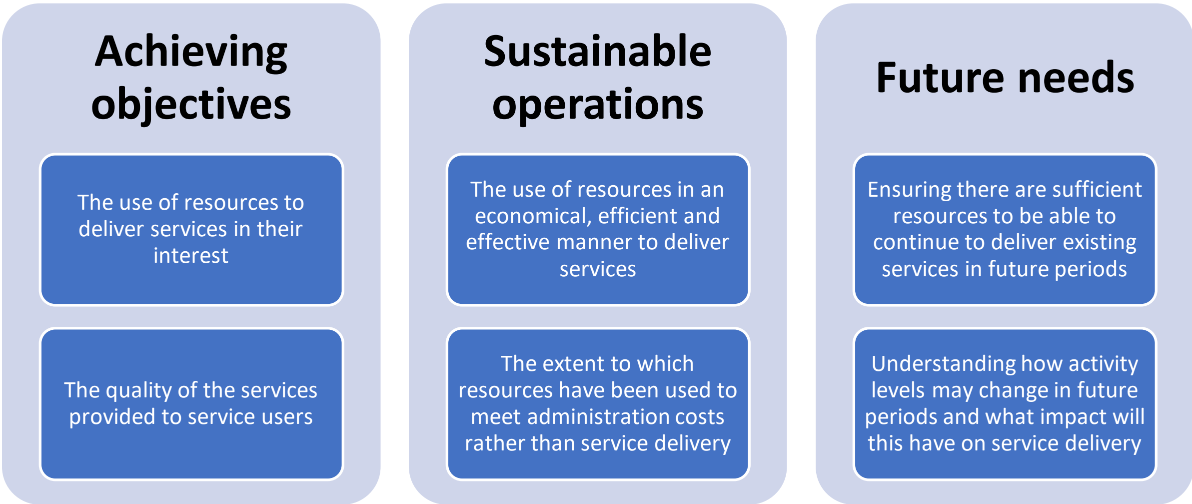
What are NPOs accountable for?

2.15 What NPOs are specifically accountable for will vary depending on what their primary objectives are, what goods and services they provide, and how they are funded.

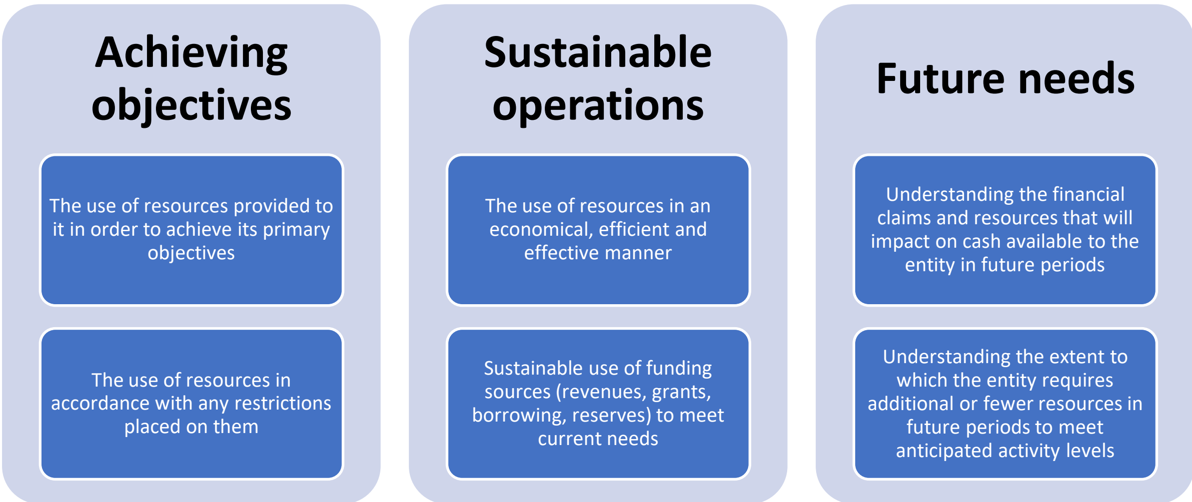
2.16 For service users there would be expected to be a greater focus on the extent to which goods and services have been provided to them. For resource providers, the focus of accountability would be expected to be more on the use of financial resources to deliver on the objectives of the NPO.

2.17 What NPOs are accountable for can be analysed between three broad categories:

2.18 Within these three broad categories, NPOs will be accountable to service users and resource providers for different decisions and actions. For service users, NPOs will be expected to be accountable for, amongst other things:



2.19 For resource providers, by contrast, NPOs will be accountable for, amongst other things, the following:



Financial management accountability

2.20 Good financial management, and the demonstration of this to service users and resource providers is a key aspect of accountability. By providing a transparent overview of how resources have been raised and utilised, service users and resource providers can gain comfort that the NPO is achieving its objectives in a sustainable manner given anticipated future needs.

2.21 Financial resources available to NPOs should be used in a way that maximises value and in accordance with high standards of propriety. Misuse of financial resources, be this from poor financial management at one end of the spectrum or the potential of fraud and corruption at the other, will have a significant impact on the ability of the NPO to achieve its objectives.

2.22 As can be seen from the above discussion, for both service users and resource providers, financial management accountability is therefore important. Although the primary objectives of NPOs will be non-financial, in that they do not exist to maximise profits or financial benefit to resource providers, all NPOs should strive to ensure that they have in place good financial management practices to provide effective stewardship over their resources, and that they deliver value for money.

2.23 This requires NPOs to have in place robust systems and processes to provide a range of service and performance information to demonstrate accountability and, ultimately, to be held accountable. This includes the need to have accurate accounting and quality financial reporting.

2.24 In Section 3 we will focus in more detail on those aspects of financial management accountability most relevant to IFR4NPO.

General Matters for Comment 2
This Section has examined what NPOs are accountable for and to who, with a view that NPOs can be seen to be publicly accountable. 2.1 - Do you agree that NPOs are accountable to service users and resource providers? If not why not? What alternative groups would you propose that NPOs can be seen as accountable to, and why? 2.2 - Do you agree that NPOs can be seen to have public accountability? If not why not? 2.3 - Do you agree that NPOs are accountable for achieving their objectives, operating in a sustainable manner, and ensuring that future needs can be met? If not why not? What other categories of accountability would you propose to highlight as relevant for NPOs, and why?

Section 3: What are the problems with current accountability arrangements for Non Profit Organisations?

3.1 In Section 2 the broad accountability environment of NPOs was examined, including who NPOs are accountable to, and what they are accountable for. This included a high-level examination of accountability with respect to financial management.

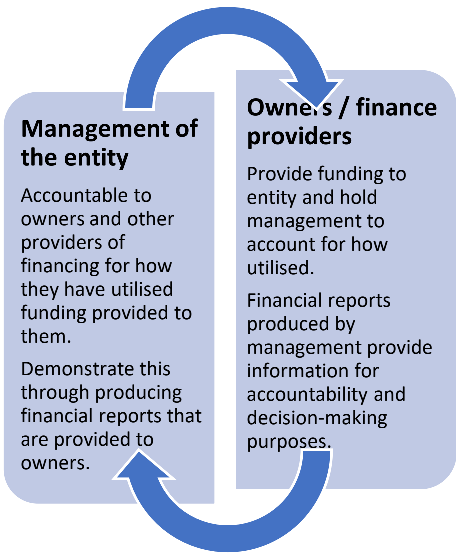
3.2 In this section we focus in more detail on those aspects of financial management accountability most relevant to IFR4NPO. There is a particular focus on problems arising from accountability arrangements to providers of funding and in particular donors as a result of the diversity in financial reporting requirements globally.

Drivers for private and public sector accountability model development

3.3 In the private sector, as organisations began to expand beyond small family owned and managed entities, new forms of financing developed and the management of many entities became divorced from ownership. Owners and other providers of finance therefore needed a way of holding management to account for the financial resources provided to them.

3.4 One aspect of holding management of the entity to account which developed was financial reporting. This allowed the management of an entity to demonstrate accountability to owners and other providers of financing for the resources entrusted to them. It also provided those owners and other providers of financing with the information they needed for decision-making purposes.

3.5 Depending on the size and nature of the entity, a requirement to have the financial reports subject to an independent external audit may also have been required, in order to ensure that all relevant transactions and economic events affecting the entity had been included in the financial statements and that accounting standards had been complied with.



3.6 In implementing this accountability model, the private sector faced problems in determining the appropriate basis for accounting, developing common accounting standards under that basis, and producing annual financial reports in a format that met the needs of users of those reports.

3.7 These financial accountability problems have in the main been answered by ensuring that private sector entities are required to produce annual financial reports which are now commonly produced under accrual-based internationally accepted accounting standards.

3.8 In the public sector though many of these problems are still prevalent. Around the world, government bodies still commonly use cash or modified cash accounting. It is also common for there to be significant differences in the accounting standards used by different parts of the public sector within a jurisdiction and between the same parts of the public sector between jurisdictions, and for reporting formats and frequencies to vary significantly.

3.9 As in the private sector, there has been an increasing recognition of the need to ensure consistency within and between jurisdictions with respect to a common accounting basis, set of standards, and reporting format. To meet this need International Public Sector Accounting Standards (IPSAS) have been developed and these are increasingly being used either directly, indirectly or as the basis of national standards as governments and public sector entities transition to accrual accounting.

NPO financial reporting drivers

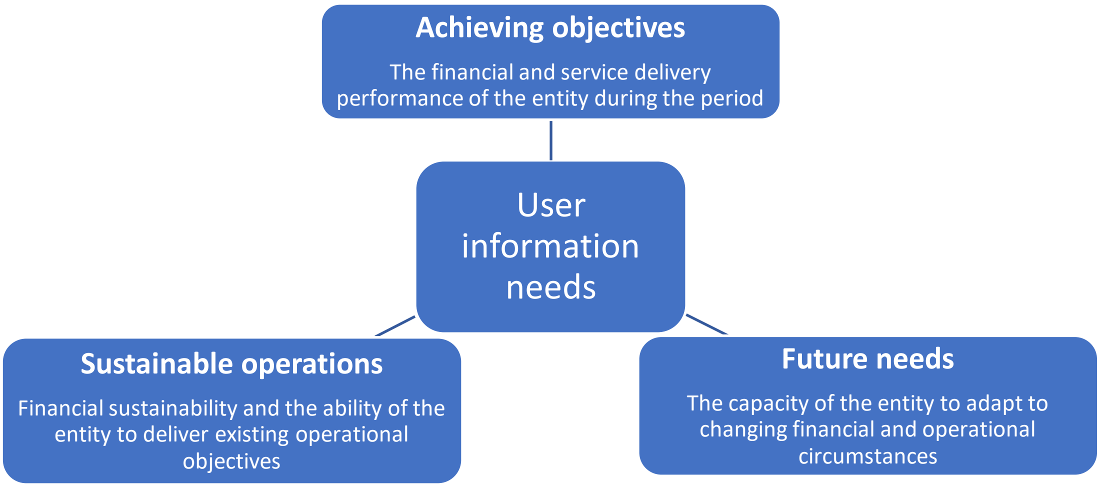
3.10 It is arguable that the objectives of financial reporting by NPOs are the same as those of private and public sector entities, albeit that the key beneficiaries of those reports will be different. Accordingly, the financial reports of NPOs need to provide information that is useful for accountability and decision-making purposes to its users.

3.11 Because of the nature of NPOs and the services they provide, the users of NPO financial reports include service recipients (and their representatives) as well as resource providers.

Service recipients	Resource providers
• Beneficaries and other service users • Members • Community groups and the wider public • Representatives of service recipients	• Funders and donors • Volunteers • The wider public • Those purchasing goods and services from the entity • The Government with respect to fiscal privileges and regulation

3.12 As highlighted in Section 2, the information needs of resource providers and service recipients will often be similar, even though they arise from different perspectives. The scale and complexity of an NPO's activities will also have an impact on its accountability needs. Smaller sized NPOs with simple operational models operating locally will often be funded through donations and local fundraising. In such cases, cash accounting, and simple annual reports may well be sufficient. As their operations increase in scale and complexity, and there is an increased separation between funders, managers and service recipients, as discussed above for the private sector, there is a need for more sophisticated accountability mechanisms, including general purpose financial reports.

3.13 The information needs that NPO users are likely to require from annual reports include:



Diversity of accountability and financial reporting arrangements across individual jurisdictions

3.14 The broader ‘public accountability’ perspective for NPOs reflects their primary objective of delivering services to the general public, community or for social benefit, often in circumstances in which those service recipients are reliant on the provision of these services over the long-term. It also reflects the fact that services are primarily funded through donations and grants, or if fees are charged that these are set to recover costs rather than to generate or maximise profits.

3.15 However, the regulation of NPOs differs significantly globally. Some jurisdictions have, over a long period of time, developed extensive legislative and regulatory provisions governing the operation of the broad sector and individual entities within it. This is often linked to taxation and other financial and operational advantages to which NPOs in these jurisdictions may be entitled. Other jurisdictions have less established provisions, either due to the relatively recent emergence of a formal NPO sector, or a view that such entities should be treated similarly to private entities that are profit oriented.

3.16 This diversity between jurisdictions with respect to regulation extends into financial accountability arrangements, and the financial reporting requirements applicable to NPOs. NPOs will often be required to submit formal financial accounts to authorities to comply with local taxation and other regulatory requirements, and so where they operate internationally and/or locally across borders they may be required to do this in multiple jurisdictions. As highlighted in Section 1, definitional issues as to what constitutes an NPO can also play a part. But there are also broader factors that lead to this diversity. These include:

Legal form	• Financial accountability arrangements may be linked to the legal form of the NPO and the different regulatory regimes that apply to them. • This can for example place financial reporting requirements on NPOs that choose or are required to be legally structured as companies that do not apply to other NPOs that have a different legal form.
Specific NPO standards or none at all	• Some jurisdictions have specific finanical reporting standards that have been developed for NPOs which provide very detailed requirements. • Others require the use of financial reporting standards developed for the private or public sectors which do not address the issues and concepts specific to the NPO sector.
'Size' of NPO and reporting tiers	• A number of jurisdctions have different financial reporting requirements for different sizes of NPOs. • These differnt requirements may be based on financial measures used to determine the 'size' of the NPO such as annual expenditure, or alternatively on other characteristics of the NPO such as the risk or complexity of operations.

3.17 At a jurisdictional level, there are a number of consequences that result from this lack of a common approach to reporting requirements including:

- An NPO operating in one jurisdiction may face significantly different reporting requirements to a similar NPO operating in another jurisdiction;
- An NPO operating in a jurisdiction may face significantly different reporting requirements to an NPO operating in the same jurisdiction that has a different legal form or is judged to be in a different reporting 'tier'; and
- NPOs that are registered in and/or operate in more than one jurisdiction may be required to comply with a number of different reporting regimes.

3.18 Jurisdictional differences can also have a significant impact on accountability and financial reporting arrangements with respect to large donors, as faced with this diversity donors seek to impose their own reporting requirements on NPOs.

Diversity in accountability and financial reporting arrangements by large donors

3.19 In addition to being based and operating in more than one jurisdiction, NPOs are also increasingly operating in a global funding environment, and this is leading to a multiplicity of international grant and funding regimes. These grant and funding regimes bring with them a variety of accountability arrangements, particularly with respect to how NPOs account for and report on the use of financial and other resources provided by donors.

3.20 As highlighted above, accounting and financial reporting arrangements for NPOs can vary significantly both between and within jurisdictions. This can make it difficult for those providing funding to NPOs to use and interpret the financial reports that NPOs prepare under these different arrangements. It may also restrict the ability of donors to gain assurance that funding has been used in an economic and efficient way towards the purposes for which it has been provided. It could also undermine the ability of donors to compare performance between different NPOs, in order to ensure that their financial resources are directed to those entities which are most effectively using donor funding to achieve their objectives.

3.21 It must also be recognised that donors themselves will be accountable to either the public or other stakeholders for the use of funds, including that resources provided to NPOs have been used in a proper manner. As such, detailed information on the use of funding may be sought not just to ensure that the funds provided have been spent on an individual project or programme. There may also be a need to demonstrate compliance with wider corporate governance and procurement standards for the donor, in order to give assurance to its stakeholders that funds have not been misused, or there is no potential for misuse.

3.22 As a result of these challenges, large donors in particular, such as USAID, ECHO, DfID and philanthropic organisations, have developed their own financial reporting requirements, and compliance with these is usually a condition of the funding. These requirements have been developed independently by each organisation to meet their own individual accountability requirements. This drives what is wanted by whom, by when and how, across the community of large donors. An NPO that receives resources from multiple sources is therefore likely to have multiple differing donor reporting requirements.

3.23 Large donors may also require the production of reports in formats that do not relate to how the NPO itself manages a project or programme, or may require financial information to be produced that does not come from the NPOs financial information system.

3.24 In addition, donor reporting timetables may not be aligned with the NPOs own accounting and reporting timetables. This can lead to incomplete information being included in reports as, for example, expenses may not have been updated in financial systems to reflect accruals where an invoice has not yet been received or payment has not yet been made.

3.25 The risk for an NPO with multiple donors there is that there is a significant burden to produce bespoke reports for each donor as well as other financial accountability and broader regulatory requirements of any specific jurisdiction.

How can IFR4NPO help address these issues?

3.26 NPOs are experiencing some of the same problems previously encountered in the private sector regarding differing bases of accounting, the absence of common accounting standards, and the need to produce multiple financial reports in on those different bases and in the varying formats to meet the requirements of the users of those reports. By developing a common set of financial reporting guidance for NPOs, this diversity could be reduced, and with it the compliance costs.

3.27 If accounting and financial reporting arrangements for NPOs were to follow a set of guidance that was common between and within jurisdictions, donors would find it easier to use and interpret the financial reports that the NPOs prepare under that guidance. This would improve their ability to gain assurance that funding has been used in an economic and efficient way towards the purposes for which it has been provided. It would also assist donors in comparing the performance of different NPOs, enabling more effective use of their funding, and ultimately improving financial management.

3.28 Section 4 examines the extent to which two current international governance and financial management improvement initiatives (the 'Good Financial Grant Practice' Standard and the 'Money Where it Counts') can contribute to addressing these NPO accountability issues, the complementary role that IFR4NPO can play, and the resulting key features needed for IFR4NPO guidance.

General Matters for Comment 3
This Section has highlighted the current problems with NPO accountability arrangements, with a particular focus on financial accountability to donors. 3.1 - Do you agree with the problems that have been identified with current accountability arrangements for NPOs? If not why not? Are there any other problems with current accountability arrangements, particularly financial accountability to donors, that you would wish to highlight?

Section 4: How do we strengthen NPO financial management and accountability

4.1 This Section examines two governance and financial management improvement initiatives, namely the 'Good Financial Grant Practice' (GFGP) Standard, and the 'Money Where it Counts' (MWiC) initiative, which aim to provide standardisation in the areas of due diligence and indirect costs in order to improve broader NPO operational and financial management.

4.2 The Section considers the extent to which the initiatives address the issues identified in Section 3 and the role that financial reports based on internationally applicable accrual based guidance for NPOS could play in supporting financial management improvements for NPOs, together with the key features of the guidance required as a result.

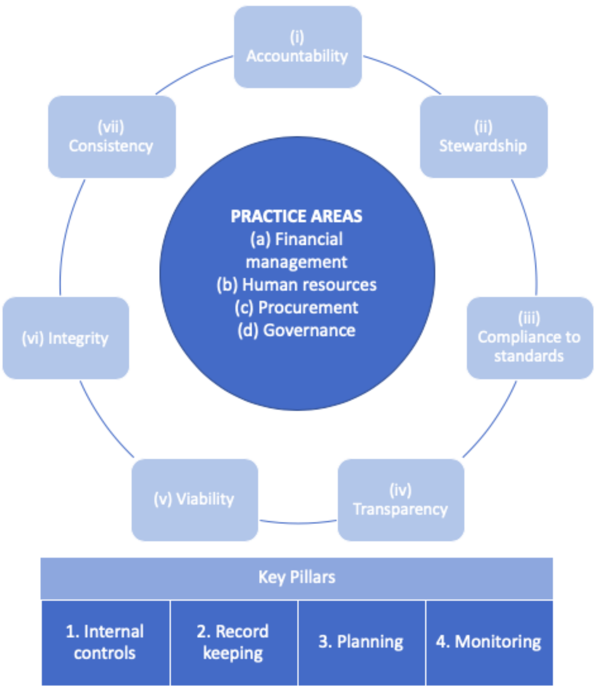
The 'Good Financial Grant Practice' Standard

4.3 The objective of GFGP is to standardise, simplify and strengthen the financial governance of grant funding. By establishing a consistent approach to the management of grants throughout the grant life cycle, GFGP aims to benefit both grantors and grantees. Grantors will be able to use the Standard as a minimum requirement for those in receipt of grants, who will themselves be able to claim compliance with the standard to support applications for grants.

4.4 The programme has three key outputs to date which are collectively called the Global Grant Community (GGC). GGC aims to use technology to digitise, standardise and de-risk the broad due diligence process associated with grant funding for both funders and grant receivers. These three outputs are:

- a new international standard for Good Financial Grant Practice (GFGP);
- a portal based pre-certification scheme to the requirements of GFGP; and
- a Global network of audit firms licensed to undertake site audits for certification that an organisation's day to day operational activities are in compliance to the requirements of the GFGP standard.

4.5 GFGP addresses seven principles of good financial grant practice that are supported by four key pillars of good financial grant management. The standard also specifies requirements to be met by grantees in order to demonstrate GFGP. There are approximately 300 statements of best practice that are categorised into four main practice areas.



(a) Financial management (budgeting process, income and expenditure management, PPE, cash & bank, and inventory management, travel expenses, sub-grantees, financial systems, and financial reporting)

(b) Human resources (recruitment, payroll, timesheets, staff development, process for responding to allegations of corruption)

(c) Procurement (planning and contract management)

(d) Governance (policies, board, compliance, audit and risk)

Principles, pillars and practice areas

4.6 The standard is split into four tiers with a view to catering to the different levels of sophistication required by organisations of different sizes and complexity. An organisation may choose which level they wish to certify to but they are generally aimed at:

Bronze	• Community Based Organisations, Civil Society Organisations, those with regional activities within a country
Silver	• Non-Governmental Organisations, those with activities across one or more countries
Gold	• Larger international non-governmental organisations, research institutes, continental / international activities, makes sub-awards.
Platinum	• Global INGOs or institutes, global activities

4.7 The GFGP standard was developed at the African Academy of Sciences (AAS), with support from many African grantees and international grantors, and technical advice from a range of organisations.

4.8 To support the financial sustainability of the GGC the standard is under copyright and is not available for free. Grantors have visibility of all grantees within the portal, together with their certification status. Achieving certification makes grantees more attractive to potential grantors, and the due diligence process does not need to be duplicated.

Money Where it Counts

4.9 As highlighted in Section 3 one of the key issues for NPO's is reporting to large donors. The Money Where it Counts (MWiC) initiative is a protocol for harmonised cost classification and financial budgeting and reporting. The intention is that it provides standardised information to large donors, rather than the multiple formats that currently exist.

4.10 At a high level, the protocol is a series of trade-offs and benefits for donors and agencies, with commitments from both sides and the overall result summarised below:

Donors give	Donors get / Agencies give	Agencies get
Commit to paying full reasonable and justifiable costs relating to the activities they fund	Transparent and consistent budgets and financial reports	Fully funded projects: reasonable and justifiable direct and indirect costs
Accept harmonised budgets and reports in MWIC format and indirect costs based on audited accounts	Demonstrated financial vigilance and cost control with detailed reports prepared when necessary	Simplified and harmonised approach adopted by funders
Accept cost pooling and apportionment for certain direct costs	Clear and consistent cost charging mechanisms justified with rationale and supported by a third party evidence base	Opportunity to streamline and automate processes
More resources to programmes and beneficiaries		

4.11 MWIC is intended to provide a new, harmonised and simplified approach to cost classification, cost charging for international funding of not-for-profit agencies. It is intended to be a practical way donors and not-for-profit agencies can make the delivery of humanitarian aid and development more efficient and fit for purpose. It is a consolidation of existing good practice, into a common set of principles and processes, which underpin a standardised proposal budgeting and reporting template.

Box 1

Money Where it Counts – summary information

The MWIC protocol includes:

(i) Definitions of types of cost – direct costs, indirect costs and ineligible costs
The protocol defines direct costs as all those necessary and reasonable inputs associated with functions that are directly necessary to deliver a programme or project. These include project and grant management, technical delivery, quality control functions, visibility and communications, human resources and security, compliance and finance, procurement, payroll, information technology and administration.

It also defines indirect costs associated with functions which are necessary to manage the agency as a whole, provide oversight over all its activities and put into place the overarching policies, frameworks and systems that enable it to operate.

Ineligible costs are listed and include items such as losses due to fraud and corruption, the purchase of land and buildings, costs of raising unrestricted or unearmarked funds, and alcohol and entertainment costs.

(ii) Description of allowable cost charging methods, and cost classification and cost charging statement

The MWiC protocol set out how cost charging methods including 100% charge of a direct cost, allocation of a direct cost based on actual use and apportionment of the costs associated with a pooled direct cost (for example the costs of running a regional office which supports a number of projects).

An agency may charge indirect costs, calculated as a percentage (the indirect cost rate) of direct costs. This rate is calculated with reference to the agency's last audited financial statements. The basis for charging allocated and pooled direct costs is transparently explained in a standard format 'Cost Classification and Charging Statement'.

(iii) Harmonised budget and financial report format

The MWIC Protocol adopts a single format for budgets and reports. The single format includes a section where direct costs are classified by nature, but donors may request a detailed breakdown of the figures if required for such costs as staff costs, travel and subsistence, capital expenditure, and downstream partners. It also includes a section showing how total project costs are apportioned to outcomes and results. Other optional annexes may also be requested.

4.12 The protocol is ready to be piloted with a number of donors and agencies for further refinement and proof of concept prior to final release by a wider range of funders. Box 1 provides a summary of the key features of the MWIC initiative. The full MWIC Protocol can be accessed at: https://files.humentum.org/fl/T66AWs9Yf5.

Can these initiatives alone deal with NPO financial management and accountability?

4.13 GFGP and MWiC have a focus on improving financial management to the benefit of funders, NPOs, auditors of these entities and ultimately service users. They both aim to harmonise practices across different entities and jurisdictions, with a focus on alignment to standards that represent best practice.

4.14 While the primary focus of the GFGP Standard is on grant management procedures, processes and policies, a number of the statements relate to the accounting policies and financial statements of the entity. This reflects the variety and lack of transparency around the treatment of issues such as asset valuation, income recognition and sub-grantee expenses recognition and consolidation. The GFGP Standard, whilst requiring accounting policies does not address holistically the accounting issues.

4.15 IFR4NPO can complement GFGP, by providing international guidance on accounting policies. The GFGP standard does stipulate some accounting policies and as the IFR4NPO guidance is developed it would be necessary to ensure that any potential conflicts are identified, and alignment sought where appropriate.

4.16 The MWiC protocol describes various aspects of expenditure classification by type (direct, indirect, ineligible), nature (staff costs, travel costs, etc.) and function. It also utilises audited financial statements in the calculation of indirect cost rates. International financial reporting guidance would aid the implementation of this protocol by increasing consistency in accounting policies and treatments. As part of the development of guidance IFR4NPO will also examine expenditure classification, and the use of ratios such as indirect cost rates as part of broader narrative reporting requirements. Again, it would be necessary to understand the potential for any conflicts between MWiC and IFR4NPO guidance, and to maximise consistency of approaches where appropriate.

4.17 GFGP and MWIC cannot alone address the problems identified in section 3. Whilst improving financial management and donor reporting, they do not provide an international solution to the broader range of financial reporting issues, and they do not cater for all users of NPO financial reports. IFR4NPO can be a key component of improving financial management and accountability for NPOs by providing international financial reporting guidance that meets the needs of a broad range of users. Collectively these initiatives have the potential to significantly strengthen the environment for NPOs.

What should be the key features of IFR4NPO to maximise the benefits?

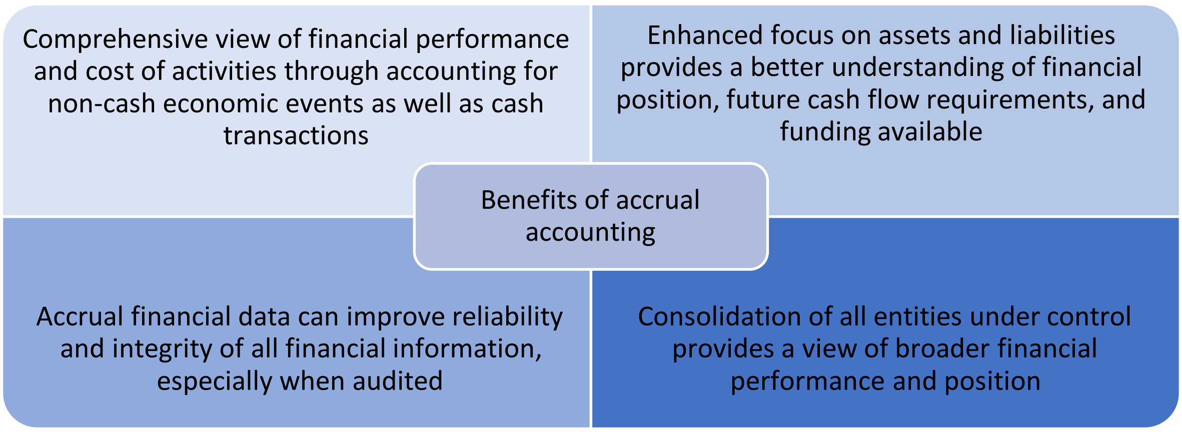
4.18 Section 3 highlighted the diversity in accountability and financial reporting arrangements required by large donors and noted that by developing a common set of financial reporting guidance for NPOs, this diversity can be reduced, so decreasing accountability burdens. The benefit of this approach can be maximised if the IFR4NPO guidance is accrual-based, international, and encompasses broader narrative reporting.

Accrual-based

4.19 The basis of accounting is the method used to determine when economic events and transactions are recognised. The basis of accounting will be one of three methods:

- Cash - where economic events and transactions are recognised when cash is received or paid;
- Accruals – where economic events and transactions are recognised at the time at which they occur (e.g. a service is provided) and not only when any related cash receipts and payments are made; and
- Partial accrual - where some assets and liabilities may be recognised such as when a commitment to pay is made or an entity is provided with an item of property or equipment that will be used over several accounting periods.

4.20 Accrual accounting is recognised as providing significant financial management benefits to both the entity and those who use its accounts for accountability and decision-making purposes. These benefits include:



4.21 Accrual-based financial information provides a more comprehensive view of an organisation's financial position and performance, especially with respect to its assets and liabilities. Not only is it essential for the management of the business, but without it owners and others providing an entity with financing would be unable to hold management to account and make funding and other decisions.

4.22 Cash accounting can be preferred by donors who want to track utilisation of the funds provided to an NPO. Whilst this may often be an effective way of tracking cash spend on an individual project or programme, it is not recognised as the best basis for producing entity financial information. For example, if an NPO is being held to account on the basis only of cash receipts and payments, it may have less incentive to manage the assets and liabilities which ultimately are likely to determine the long-term financial viability of the entity and its ability to continue to deliver services.

4.23 If a partial accrual basis of accounting is being used, where certain commitments to make payments to beneficiaries are reported but broader accrual information is not, this could provide an incomplete picture of financial position and performance, which may impact on future funding decisions. Such approaches are also likely to be inconsistent between entities both within and across jurisdictions.

4.24 Having accrual as the common basis of accounting would not, however, be sufficient on its own. The IFR4NPO guidance would need to be capable of being applied internationally, to ensure commonality over the accounting treatment applied by NPOs for the same transactions and economic events, regardless of where they are operating.

International

4.25 At present NPOs are applying different accounting standards and policies for the same economic events and transactions. National guidance has been developed in a number of jurisdictions, but many jurisdictions have no guidance at all. Where national guidance exists, it has often been developed based on jurisdictional approaches to private and public sector reporting.

4.26 The existence of a single set of international guidance could improve the consistency of financial reporting within and across jurisdictions. Using common high quality international guidance could also improve usability of financial reports to the wide range of users.

4.27 Accrual-based international guidance would be expected to reduce reporting burdens for NPOs while improving accountability. NPOs could no longer be required to run multiple sets of accounts in order to provide financial reports to regulators in different jurisdictions. There could also be benefits in consistency of information provided to donors, both as part of financial reports and through the other financial management improvement projects in the sector.

Narrative reporting

4.28 The primary objectives of many NPOs are non-financial Information on how the entity has performed with respect to service delivery and other non-financial indictors is also needed to demonstrate accountability. The benefits of the guidance would therefore be maximised if it also encompassed narrative reporting.

4.29 General Purpose Financial Reports (GPFRs) present narrative reporting alongside financial information, providing users with a more meaningful understanding of an entity’s nature, objectives, strategy, risks, and performance. They are therefore broader than general purpose financial statements (see Box 2). These are usually backed by a range of performance measures and indicators consistent with underlying financial information to provide a clear view of the impact of the entity's projects, programmes and wider activities on service recipients. This enables entities to demonstrate accountability without having to be constantly reporting to external stakeholders. GPFRs also enable those owners and providers of finance to compare the performance of the entity over time and against other entities more easily.

4.30 It is recognised that such reports produced under accrual-based international standards will not be a panacea for solving all accountability requirements and issues. As they are general purpose they may not be able to provide all the information that the diverse donor community may need. However, by removing differences in accounting basis and providing common financial reporting standards and formats, IFR4NPO guidance could assist in significantly reducing the reporting burden that NPOs face provided it is supported by donors and they accept the financial information produced.

Box 2

General Purpose Financial Reports (GPFRs)

The objective of general purpose financial reporting is to provide information that is useful for accountability and decision-making purposes to those users who do not possess the authority to require an entity to prepare and disclose information to meet their specific needs.

GPFRs are therefore intended to provide a single annual report that includes audited financial information to meet the greatest common needs of the key users of that financial information. For the private sector GPFRs are aimed at meeting the needs of investors and for the public sector where produced GPFRs are aimed at meeting the needs of citizens (as both service users and taxpayers) and the Government.

It is important to note that GPFR are not just General Purpose Financial Statements (GPFS). GPFS comprise the balance sheet, income statement, statement of changes in equity, and cash flow statement and provide information about an entity's assets, liabilities, equity, income and expenses that is useful to financial statement users when assessing prospects for future net cash inflows to the entity and management's stewardship of the entity's resources. GPFR are more expansive, including GPFS but also the management commentary that gives users integrated information that provides context for the financial statements and complements and supplements them through discussion of issues such as:

- the nature of the entity's business;
- its objectives and strategies;
- resources, risks and relationships;
- results and future prospects; and

4.31 The benefits of accrual accounting for financial management, accountability and decision-making purposes are clear. It is the only basis that provides a consolidated and comprehensive view of the financial position and performance of the entity, encompassing non-cash economic events as well as cash transactions, while giving a better understanding of future cash flow and funding requirements.

4.32 Compliance with financial reporting guidance and the production of financial reports can demonstrate the level of financial management competence by the NPO, which can in turn provide donors with some assurance that funding provided will be managed effectively. This is particularly the case when the reports are subject to external audit. Such assurance can go some way to reducing the level of bespoke ongoing reporting and monitoring required.

4.33 This Section has highlighted that by following common standards, rather than requiring financial information to be produced and reported in a variety of different ways depending on the entity, jurisdiction and user, benefits can be delivered. The two initiatives highlighted in this section, together with IFR4NPO guidance could reduce reporting burdens at the same time as improving broader financial management.

4.34 This Section has also concluded that by developing a common set of financial reporting guidance for NPOs, the current diversity in financial reporting can be reduced if this guidance was accrual-based, international, and encompassed broader narrative reporting. Section 5 will examine the options available for the development of international financial reporting guidance for NPOs.

General Matters for Comment 4
This Section has highlighted how IFR4NPO can work with the 'Good Financial Grant Practice' (GFGP) Standard, and the 'Money Where it Counts' (MWiC) initiative, which aim to provide standardisation in the areas of due diligence and indirect costs. It has also noted that by developing a common set of financial reporting guidance for NPOs, the diversity of donor reporting requirements can be reduced and financial management improved. 4.1 – Do you agree with our view that IFR4NPO can support these complementary projects? If yes are there any other potential conflicts that need to be identified and taken into consideration? If not why not? 4.2 – Are there any other NPO financial management projects which IFR4NPO could complement, or potentially be in conflict with? If so which ones and in what ways? 4.3 – Do you agree that the benefit of IFR4NPO can be maximised if the Guidance is: (a) accrual-based; (b) international; and (c) encompasses broader narrative reporting? For each, if you disagree can you note why, and indicate what other approach or approaches you would suggest, and how they could reduce diversity in donor reporting requirements, and improve NPO financial management?

Section 5: How can international financial reporting regimes assist NPOs?

5.1 Section 4 concluded that by developing a common set of international financial reporting guidance for NPOs (the Guidance), diversity of financial reporting can be reduced delivering benefits to NPOs and improving their financial management and accountability arrangements. It also demonstrated the need for the Guidance to be accrual-based, international, and encompass broader narrative reporting.

5.2 Taking this as a start point there are three ‘off the shelf’ international frameworks on which the Guidance could be based. All three provide international, accrual based financial reporting standards. The respective hierarchies, structures and legitimacies for these frameworks, could potentially be used to provide credibility to the Guidance. International Financial Reporting Standards (IFRS) and International Public Sector Accounting Standards (IPSAS) are two of these frameworks. In addition, within the IFRS suite of standards, there is also IFRS for SMEs (Small and Medium Entities), which provides for simplified reporting requirements for for-profit organisations to meet the needs of smaller organisations.

5.3 In this Section we propose three criteria to assess the suitability of these international frameworks as a basis for the IFR4NPO Guidance, and provide a high-level assessment against these for each framework.

Proposed international framework assessment criteria

5.4 There are three proposed criteria for assessing the suitability of the international frameworks as a basis for the development of the IFR4NPO guidance. These are:

(a) Does the framework provide guidance on the most prevalent sector specific issues?

5.5 The first criterion examines the extent to which a framework provides guidance on the most prevalent sector specific issues. As IFR4NPO aims to address those issues that are common across the NPO sector, a framework that already provides solutions to those issues would be of more use than one that is silent on them or requires accounting treatments that are not appropriate for the NPO sector.

(b) Will preparers, auditors and users be familiar with and easily able to use the framework?

5.6 The second criterion focusses on the extent to which preparers, auditors and users will already be familiar with the framework and be easily able to use it and the guidance developed form it. The extent to which frameworks are utilised globally varies significantly, and broader use makes it more likely that preparers, auditors and users would accept a framework as being an appropriate basis for the Guidance. As the project is aiming to reduce the reporting burden on NPOs, the complexity of accounting solutions and significance of disclosure requirements are also important. Those frameworks that provide simplified principles, have reduced disclosure requirements, are easy to understand and are revised only on a periodic basis are likely to be more appropriate in the NPO context.

(c) How feasible will the development and maintenance of Guidance under the framework

5.7 The final criterion focuses on the feasibility of developing and maintaining the Guidance under the framework. This criterion examines the extent to which utilising the framework would be straightforward or require a significant initial and ongoing resource investment to develop and maintain the Guidance. Frameworks that have less complex and fewer accounting solutions, reduced disclosure requirements, and which are subject to less frequent revision would be likely to have a higher development and maintenance feasibility given resource constraints.

Immediate conclusions arising from these criteria

5.8 A solution to the current problems facing NPOs needs to be developed on a timely basis, the sector cannot wait decades. The necessary financial and human resources that it would take to develop a separate full suite of standards means that it is not feasible to develop a separate full suite of international standards specifically for the NPO sector within a reasonable timeframe. By way of comparison, it has taken the IPSASB more than 20 years to develop its conceptual framework and increasingly complete set of financial reporting standards for use by public sector entities.

5.9 Further, preparers, users, auditors and regulators may find it challenging to use a set of Guidance that is based on a set of national guidance that is removed from other accounting guidance in their respective jurisdictions. It is therefore not proposed to base the Guidance on a national suite of accrual standards.

5.10 The next part of this section summarises the key features of each framework including their conceptual basis as well as the similarities and differences between them and provide a high level assessment of each framework against an initial list of sector specific reporting issues that the IFR4NPO project has identified.

International Financial Reporting Frameworks

What are IFRS?

5.11 International Financial Reporting Standards (IFRS) are developed by the International Accounting Standards Board (IASB), the standard-setting body of the IFRS Foundation. The IFRS Foundation is a not-for-profit, public interest organisation established to develop a single set of globally accepted accounting standards and to promote and facilitate adoption of the standards in order to:

- Bring transparency by enhancing the international comparability and quality of financial information, enabling investors and other market participants to make informed economic decisions;

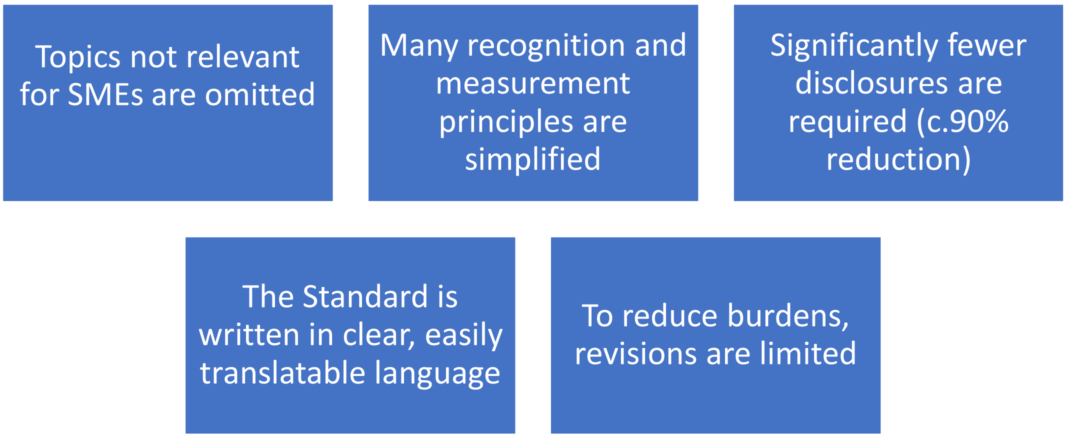
- Strengthen accountability by reducing the information gap between the providers of capital and the people to whom they have entrusted their money. IFRS provide information needed to hold management to account. As a source of globally comparable information, IFRS Standards are also of vital importance to regulators around the world; and
- Contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation. Use of a single, trusted accounting language lowers the cost of capital and reduces international reporting costs for businesses.

5.12 IFRS are developed primarily for use by publicly accountable companies - defined by IASB as those listed on a stock exchange and financial institutions such as banks that hold financial assets in a fiduciary capacity.

What is IFRS for SMEs?

5.13 In addition to full IFRS, the IFRS for SMEs standard provides simplified reporting requirements to meet the less complex needs of smaller for-profit organisations. The IFRS for SMEs Standard is a self-contained Standard (fewer than 250 pages) designed to meet the needs and capabilities of small and medium-sized entities (SMEs), which are estimated to account for more than 95 per cent of all companies around the world.

5.14 Compared with full IFRS Standards (and many national GAAPs), the IFRS for SMEs Standard is less complex in a number of ways:



5.15 The IFRS for SMEs Standard is available for any jurisdiction to adopt, whether or not it has adopted full IFRS Standards. Each jurisdiction must determine which entities should use the Standard. The IASB's only restriction on use is that entities that have public accountability (as defined in IFRS) should not use it. Such entities are required to apply full IFRS if IFRS is adopted.

What are IPSAS?

5.16 International Public Sector Accounting Standards (IPSAS) are developed by the International Public Sector Accounting Standards Board (IPSASB), and independent standard setting Board whose structures and processes are supported by the International Federation of Accounts

(IFAC). IPSASB's mission is to serve the public interest by developing high-quality accounting standards and other publications for use by public sector entities around the world in the preparation of general purpose financial reports. This is intended to help strengthen public sector financial management globally.

5.17 In pursuit of this objective, the IPSASB develops and maintains IPSAS and other high-quality financial reporting guidance for the public sector, as well as raising awareness of IPSAS and the benefits of accrual adoption.

5.18 IPSASB has a formal process to assess the applicability of a relevant IFRS in the public sector context[1]. This alignment process works to minimise the differences between the IFRS and IPSAS financial reporting frameworks, so that as a far as possible a similar transaction or economic event will be accounted for in the same way by a public or private sector entity. It involves determining whether there are public sector issues that warrant modifications of the IFRS (for example terminology changes, changing recognition and measure requirements or eliminating accounting treatments), or instead undertaking a separate public sector project to reflect the public sector context.

5.19 As a result of applying this process, the majority of IPSAS are to a greater or lesser extent aligned with their IFRS counterparts. IPSASB publishes regular 'IPSAS / IFRS alignment dashboard' updates summarising current alignment of its suite of standards against IFRS, as well as the planned impact of project in its work program [2].

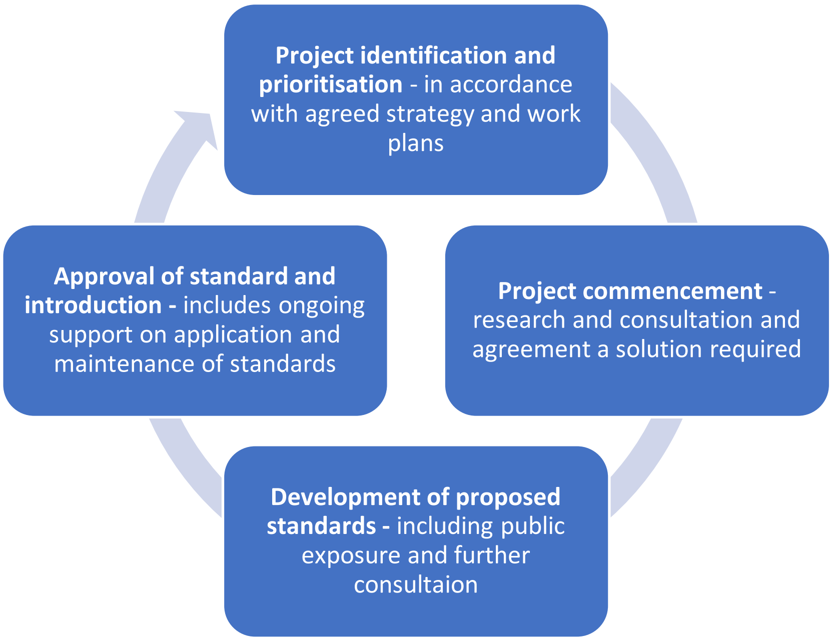
How does international standard setting operate?

5.20 Both IFRS and IPSAS are set using similar thorough, transparent and participatory due processes. The ongoing process of standard setting and maintenance means that the frameworks adapt to user needs through new standards or amendments to existing standards. It does mean however that they can be subject to regular updates which can impact on ease of use.

5.21 In this regard the IFRS for SMEs Standard is different. As indicated to reduce burdens revisions to this Standard are limited, with a commitment from the IASB only to update the entire Standard and to ensure that there are at least three years between revisions. IFRS for SMEs was last amended in October 2015, with an effective date of application of 1 January 2017. A comprehensive review has recently been proposed. Among other activities, the Board is undertaking outreach to gain a broad range of views on the extent to which the IFRS for SMEs Standard should be aligned with full IFRS Standards.

[1] https://www.ifac.org/system/files/publications/files/IPSASB-Rules-of-the-Road-Oct2008.pdf

[2] An example of the alignment dashboard can be found at: https://www.ifac.org/system/files/meetings/files/1-1.5-IPSAS-IFRS-Alignment-Dashboard_Final_0.pdf



How similar are the conceptual frameworks underpinning the frameworks?

5.22 Both IASB and IPSASB have conceptual frameworks that describe the objective of, and the concepts for, general purpose financial reporting. These conceptual frameworks:

- assist the respective Boards in developing Standards that are based on consistent concepts;
- assist preparers in developing consistent accounting policies when no Standard applies to a particular transaction or other event, or when a Standard allows a choice of accounting policy; and
- assist all parties to understand and interpret the Standards.

5.23 While the IPSASB's Conceptual Framework was set for general purpose financial reporting by public sector entities, where appropriate for the public sector context, IPSASB drew on the relevant part of IASB's Conceptual Framework in developing its own. The comparison below of the conceptual frameworks therefore shows the many similarities between IFRS and IPSAS. As can be seen the two conceptual frameworks are in many respects similar, covering most of the same aspects such as the reporting entity, elements of financial statements, recognition, etc. with the same overall purpose.

IASB	IPSASB[3]
Objective of general purpose financial reporting - the objective of general purpose financial reporting, which is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity.	***Objective of financial reporting -*** The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFRs for accountability purposes and for decision-making purposes. Users are service recipients and resource providers who do not possess the authority to require a public sector entity to disclose the information they need for accountability and decision-making purposes.
Qualitative Characteristics of, and the cost constraint on, useful financial information – If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable. Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting.	***Qualitative Characteristics –***The qualitative characteristics of information included in GPFRs of public sector entities are relevance, faithful representation, understandability, timeliness, comparability, and verifiability. Pervasive constraints on information included in GPFRs are materiality, cost-benefit, and achieving an appropriate balance between the qualitative characteristics.
Financial statements and the reporting entity – A reporting entity is an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity. Financial statements are prepared for a reporting period and provide financial information about the reporting entity's assets, liabilities, equity, income and expense.	***Reporting entity -*** A public sector reporting entity is a government or other public sector organization, program or identifiable area of activity that prepares GPFRs. A public sector reporting entity may comprise two or more separate entities that present GPFRs as if they are a single entity–such a reporting entity is referred to as a group reporting entity. GPFRs encompass financial statements and information that enhances, complements and supplements the financial statements. Financial statements present information about the resources of the reporting entity or group reporting entity and claims to those resources at the reporting date, and changes to those resources and claims and cash flows during the reporting period.
Elements of financial statements – Financial statements elements are (a) assets, liabilities and equity, which relate to a reporting entity's financial position and (b) income and expenses, which relate to a reporting entity's financial performance.	***Elements in financial statements –*** The elements are assets, liabilities, revenue, expense, ownership contributions and ownership distributions. This does not preclude IPSASs from requiring or allowing the recognition of other resources or obligations that do not satisfy the definition of these elements when necessary to better achieve the objectives of financial reporting.
Recognition and derecognition – Recognition is the process of capturing for inclusion (in monetary value and words) in the statement of financial position	***Recognition in financial statements –*** Recognition is the process of incorporating and including in amounts displayed on the face of the

[3] The IPSASB has just started a limited scope update of its Conceptual framework , which will include considering the relevance to the public sector of changes made to the IASB's conceptual framework, since the IPSASB's conceptual framework was published in 2014.

IASB	IPSASB[3]
or the statement of financial performance an item that meets the definition of one of the elements of financial statements. Derecognition is the removal of all or part of a recognised asset or liability from an entity's statement of financial position.	appropriate financial statement an item that meets the definition of an element and can be measured in a way that achieves the qualitative characteristics and takes account of the constraints on information included in GPFRs. Derecognition is the process of evaluating whether changes have occurred since the previous reporting date that warrant removing an element that has been previously recognized from the financial statements, and removing the item if such changes have occurred
Measurement – Quantifying elements recognised in financial statements in monetary terms requires the selection of a measurement basis which is an identified feature, such as historical cost or fair value, of an item being measured.	***Measurement of assets and liabilities in financial statements*** – The objective of measurement is to select those measurement bases that most fairly reflect the cost of services, operational capacity and financial capacity of the entity in a manner that is useful in holding the entity to account, and for decision-making purposes.
Presentation and disclosure – The reporting entity communicates information about its assets, liabilities, equity, income and expenses by presenting and disclosing information in its financial statements.	***Presentation in General Purpose Financial Reports –*** Presentation is the selection, location and organization of information that is reported in the GPFRs. Presentation aims to provide information that contributes towards the objectives of financial reporting and achieves the qualitative characteristics while taking into account the constraints on information. Decisions on selection, location and organization of information are made in response to the needs of users. GPFRs are likely to comprise multiple reports, each responding more directly to certain aspects of the objectives of financial reporting and matters included within the scope of financial reporting. In addition to the financial statements, GPFRs provide information relevant to, for example, assessments of an entity's service performance and the sustainability of its finances. The objectives of financial reporting, applied to the area covered by a particular report, guide presentation decisions for that report.
Concepts of capital and capital maintenance – selection of the appropriate concept of capital by an entity based on the needs of the users of its financial statements. A financial concept of capital equates capital to net assets or equity of the entity. A physical concept regards capital as the productive capacity of the entity.	The IPSASB Conceptual Framework does not currently have a chapter on concepts of capital and capital maintenance.

5.24 The table above shows that the IPSASB Conceptual Framework has a broader concept of the nature and extent of General Purpose Financial Reporting and the users of GPFR in the public sector. It explains that the objectives of financial reporting by public sector entities are to provide information about the entity that is useful to the user of GPFRs for accountability and decision-making purposes. Those users include both resource providers **and** service recipients, and so are not limited as under IFRS primarily to existing and potential investors and providers of credit.

5.25 This reflects a view of public accountability that acknowledges that governments and other public sector entities are accountable to those that provide them with resources, and to those that depend on them to use those resources to deliver services. This more expansive approach to public accountability is derived from the primary function of governments and public sector entities, which is to provide services to enhance or maintain the well-being of citizens and other eligible residents.

5.26 The IPSASB Conceptual Framework also addresses concepts such as non-exchange transactions (where an entity receives value from another party without directly giving approximately equal value in exchange) that are not found in the IFRS Conceptual Framework. This is due to the existence in the public sector of powers such as the ability of government to raise compulsory taxes, or the rights of citizens to receive services without direct payment.

5.27 Although the conceptual similarities and the IPSASB's 'rules of the road' process limit differences between the IFRS and IPSAS standards suites, under the criteria on which the frameworks for the development of the IFR4NPO Guidance will be assessed important differences nevertheless do remain. In the remainder of this Section we assess the international financial reporting frameworks against these criteria.

Assessment of international financial reporting frameworks against sector specific issues

5.28 The Guidance being developed under IFR4NPO could comprise a single document covering a range of specific financial reporting issues, which are examined in more detail in Part 2 of this Consultation Paper. The list of sector specific issues to be addressed has been developed from a number of independent sources.

5.29 One key source is the study carried out in late 2013 and early 2014 by the CCAB in the UK[4]. This study attracted a significant number of responses from across the world, with a good geographic representation. Through the consultation responses the report identifies a number of specific areas of difference in accounting treatments globally.

5.30 In addition, issues have been sourced from a working group focused on not-for-profit reporting formed from the International Forum of Accounting Standard Setters (IFASS) in 2016. IFASS is a grouping of national accounting standard-setters from around the world, as well as other organisations that have a close involvement in financial reporting issues formed. This working group has discussed the most pressing issues being encountered by national

[4] https://www.ccab.org.uk/documents/IFRNPO-FullReport-Final-07022014.pdf

standard setters for NPOs, developed a long list of issues and brought together information from working group participants about the various accounting treatments in their jurisdictions.

5.31 Finally, in 2015, the Association of Chartered Certified Accountants (ACCA) in the UK issued a Companion Guide '*Companion guide for Not-for–profits to the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs)'.* The Companion Guide was written in response to the lack of formal guidance to help NPOs prepare financial accounts under a robust, but appropriate framework. This Guide identifies a number of issues for not-for-profit organisations and seeks to provide guidance to sit alongside the IFRS for SME's standard to address those issues.

5.32 The advisory groups to this project have further developed the issues identified from these sources to better reflect and contextualise the groups' understanding of the nature of each of the issues. The specific issues identified have been grouped into five main categories. These are listed below along with a high level description of the main NPO sector specific issues relevant to each category and an assessment of the applicability of existing standards under full IFRS, IFRS for SMEs and IPSAS to each issue. The analysis supporting each assessment can be found in Annex to Part 1 of the Consultation Paper.

5.33 While it is proposed that the initial version of the Guidance will focus on providing solutions for a limited range of the key NPO financial reporting issues, the framework(s) on which the Guidance is based will need to provide a full suite of financial reporting standards, as well as providing guidance on narrative reporting. This will ensure that NPOs are provided with internationally applicable financial reporting guidance that covers all of the economic events and transactions that they are required to account for. It will also ensure that reports provide non-financial information that is consistent with the financial information reported.

5.34 The following key is in use for the table:

Applicability of existing standards to specific NPO reporting issue	**Rating**
The framework is silent on the issues or provides guidance that is largely not applicable in the NPO context	
The framework provides some guidance that could be utilised in the NPO context but it is not tailored to the specific issues	
The framework provides a range of guidance that appears to be directly applicable in the NPO context and to the specific issues	

Category	**High level description of sector specific issues**	**Full IFRS**	**IFRS for SMEs**	**IPSAS**
Accounting for incoming resources	• What are the overarching principles for the recognition and measurement of incoming resources from 'non-exchange' transactions, (of which donations, grants, services in-kind income are all categories)?			
	• Timing of income recognition and definition of performance criteria/obligation for cash donations.			
	• When should services in-kind be recognised and if so how measured?			
	• When should gifts in-kind be recognised and measured?			
	• How should assets financed by capital grants be recognised and measured and the implications for the recognition of the grant income?			
	• When should bequests and endowments be recognised?			

Accounting for outgoing resources	• Should the primary analysis of expenses be based on function or nature of spend?			
	• How should the costs of fundraising be defined (e.g. whether to include business development spend and/or overheads) and how should the costs of fundraising be recognised and/or presented (i.e. on a gross basis or netted against income)?			
	• Recognition and measurement of NPO 'non-exchange' transfers to individuals and other entities?			
	• When is the NPO acting as an agent and when is it acting as principal?			
Accounting for non-financial assets	• How should assets that are held for service potential be measured, both initially and subsequently?			
	• How do you identify impairment where assets are held for service potential and when an impairment has been recognised, what disclosures should be made?			
	• How should heritage assets be accounted for and disclosed?			
	• What is the definition of a concessionary loan and what is the initial and subsequent measurement of special credit conditions?			
	• How should concessionary leases be accounted for?			
	• How to account for service concessions with NPO as grantor?			
	• How to account for service concession with NPO as operator?			
Reporting entity	• How is control defined?			
	• How is a branch defined? Should all branches be accounted for as part of an NPO? What is the status of the financial statements of a branch that is not a separate legal entity?			
	• What is the accounting treatment for the combination of two or more NPOs?			
	• When is income from a subsidiary recognised in the parent NPO's accounts?			

	• What disclosure should be required by both sides of the relationship/transaction when a branch is part of a larger NPO or the NPO is part of a group?			
Form and content of financial reports	• How should financial statements be presented to help the user understanding of an NPO's activities?			
	• What should the narrative/non-financial reporting requirements be?			
	• How should related party transactions be defined and disclosed?			
	• What disclosures should be made for remuneration/pay and who should be included?			

Assessment of international financial reporting frameworks against familiarity and ease of use

5.35 As discussed above, full IFRS are developed primarily for use by publicly accountable companies - defined by IASB as those listed on a stock exchange and financial institutions such as banks that hold financial assets in a fiduciary capacity. Of 166 jurisdictions that have been profiled by the IASB, 144 require IFRS Standards for all or most domestic publicly accountable entities in their capital markets. While this indicates wide adoption internationally, as full IFRS are mainly used by large private sector entities, this will not automatically translate into familiarity for NPO preparers, auditors and users. Amongst smaller or less complex NPOs, it is unlikely that preparers and auditors will have regularly operated with or are familiar with the requirements of full IFRS.

5.36 The requirements of full IFRS are also complex, both in terms of the accounting principles that the standards require entities to apply and the associated disclosure requirements. The focus of the full suite of IFRS standards is necessarily on the financial reporting requirements of large and complex listed companies. NPO preparers would not only need to understand the requirements of the standard but would also have to place reliance on the materiality principle to determine if a standard needs to be applied and the extent of disclosure necessary. This would significantly increase the level of judgements required by NPOs and lead to greater audit work.

5.37 At an entity level, the larger number of SMEs (c. 95% of all companies) when compared to large listed companies or financial institutions is likely to mean that familiarity with IFRS for SMEs will be at least as prevalent as for full IFRS. It also provides for simplified reporting requirements for for-profit organisations to meet the needs of smaller and less complex organisation, including the omittance of irrelevant accounting topics for non-listed entities, reductions in accounting options and reduced disclosure requirements. As it is written in clear easily translatable language and revisions to the entire standard are only made approximately every five years, this could improve the ease with which the framework can be utilised by NPOs. There are gaps in topic coverage may, however, with NPO's potentially having to create their own interpretations, which may impact on ease of use.

5.38 IPSAS are less widely used at present, reflecting the relatively low level of the use of accrual accounting by governments and public sector entities globally. Recent figures indicate that of the 37 governments that currently report on accrual, 19 (51%) are using IPSAS either directly, indirectly or as a basis for their own national standards. However, a large number of governments are currently transitioning to accrual accounting, and in a 2018 report[5] it was estimated that of the 98 government projected to be reporting on accrual by 2023, 72 (73%) will be making use of IPSAS.

5.39 As noted many of the individual IPSAS standards are closely aligned to IFRS which means that for those individuals used to operating with IFRS it is only those standards that deal specifically with public sector specific issues, such as revenue from non-exchange transactions and accounting for social benefits that will be unfamiliar. Ease of use by NPOs is likely,

[5] https://www.ifac.org/knowledge-gateway/supporting-international-standards/publications/international-public-sector-financial-accountability-index-2018-status-report

however, to be impacted by an absence of an IPSAS for SMEs to simplify reporting and disclosure requirements for smaller entities.

Assessment of international financial reporting frameworks against feasibility of developing and maintaining the Guidance

5.40 Full IFRS is a complex suite of standards, with a significant number of different accounting options available in many of the standards and extensive disclosure requirements. As highlighted they are also subject to an ongoing process of change with regular updates for new standards or amendments to existing standards.

5.41 This complexity and frequency of change would necessitate a significant amount of initial work and a process of monitoring for the interpretation and adaption of standards for the NPO context. It would also necessitate the investment of significant resource initially and on an ongoing basis to ensure the development and maintenance of the Guidance was consistent with the underlying framework.

5.42 The IPSAS suite of standards is similar in this respect, as it is also complex, has significant disclosure requirements and is also subject to ongoing development and change as a result of maintaining alignment with new and updated IFRS where appropriate, as well as the development of public sector specific standards.

5.43 IFRS for SMEs, however, is a simplified framework where revisions are limited, with the IASB committed to limiting revisions to the entire Standard and only once every three years and in practice such revision occurring approximately every five years. If Guidance were to be developed using IFRS for SMEs, it would not need to be subject to continual monitoring and update as a result of changes to underlying standards. The initial resources needed to develop any NPO Guidance would be less using IFRS for SMEs than under full IFRS or IPSAS. This would limit the resource required to maintain the Guidance.

International frameworks and the criteria

5.44 This Section has highlighted the options that exist for utilising international frameworks to develop the Guidance so that it can harness their respective hierarchies, structures and legitimacies. It also argues that utilising existing international frameworks could significantly reduce development time and add value most quickly. It has also proposed criteria against which those frameworks can be assessed.

5.45 However, as has been demonstrated, no single existing international framework performs well across all criteria. Full IFRS performs poorly against all criteria. IPSAS better addresses some of the NPO sector specific issues but without a standard for SMEs may not be feasible or easy to implement. IFRS for SMEs provides a more feasible solution and has advantages in ease of use, but does not address a large number of sector specific issues. Section 6 therefore proposes an approach to meeting the objective of addressing the issues that are common across the NPO sector, while also meeting the general financial reporting requirements of funders and regulators as well as preparers.

General Matters for Comment 5
This Section has provided an overview of international financial reporting frameworks that the Guidance can harness and provided three criteria that can be used to assess their suitability. 5.1 – In additional to IFRS, IFRS for SMEs and IPSAS, are there any other financial reporting frameworks that you believe should be considered as part of this project? If so, what are they, and why should they be considered? 5.2 - Do you agree with the criteria that have been used to assess the suitability of the frameworks? If not, why not? What other criteria do you believe could be used and why? 5.3 – Do you agree with the high level assessment of the frameworks against these criteria? If not, why not? What changes would you propose to the assessments and why?

Section 6: Proposed way forward

6.1 Section 5 has highlighted how no single existing international framework performs well across the criteria. Of the three options identified, IPSAS appears to perform best when measured against the provision of guidance on the most prevalent sector specific issues. It is less suitable, however, when judged against feasibility, familiarity, acceptance, and ease of use.

6.2 In those areas, IFRS for SMEs would appear to have a distinct advantage over both IPSAS and full IFRS, particularly given that it provides simplified accounting and disclosure requirements that would permit ease of use by a broader range of entities and is subject to only periodic revision. IFRS for SMEs does, however, face some conceptual issues. While it is backed by the full IFRS conceptual framework, IFRS for SMEs is updated only infrequently following a comprehensive review process. While this results in a standard that is stable over a considerable period of time, it also means that in some respects conceptually, and certainly with reference to specific financial reporting standards, it can lag significantly behind full IFRS and IPSAS. It also does not address a number of topics that have the greatest impact on NPOs.

The case for a hybrid solution and potential issues that would need to be resolved

6.3 As none of the frameworks performs well on their own, rather than utilising a single framework it could be possible to utilise a hybrid solution.

6.4 A hybrid solution could take aspects of different frameworks and bring them together in order to create an integrated framework addressing the issues that are common across the NPO sector, and to meet the general financial reporting requirements of funders and regulators as well as preparers. Such a hybrid solution could provide the opportunity to maximise the advantages of each international framework while minimising the disadvantages that have been highlighted.

6.5 A hybrid solution could see the Guidance based on a foundational framework and utilise other frameworks for developing specific NPO financial reporting standards. This could include IFRS, IPSAS and the broader conceptual frameworks of IFRS and IPSAS. Where international frameworks are silent on an NPO specific issue, relevant national private and public sector accounting standards could be utilised.

6.6 A hybrid solution could also draw on additional narrative reporting guidance that has been developed by the IASB and IPSASB to accompany the suites of standards to support the broader requirements of general purpose financial reporting. The Guidance could be based on existing practice statements and recommended practice guidelines such as:

- IFRS Practice Statement 1 *Management Commentary* – which provides guidance on management commentary to ensure it provide users with integrated information that provides a context for the financial statements and complements and supplements the financial statements by providing integrated information about the entity's financial position and performance and managements view not only about what has happened but also why it happened and what the implications are for the future; and

- IPSAS Recommended Practice Guideline 3 *Reporting Service Performance Information* – which provides guidance on the reporting of service performance information in GPFRs so that when used in combination with the information in an entity's financial statements it enables users to assess the entity's finances in the context of its achievement of service performance objectives and vice versa.

6.7 A hybrid solution does pose a question with respect to conceptual coherence, as it would draw on a range of international and potentially national frameworks. However, as discussed in Section 5, although there are some differences in the conceptual basis of IFRS and IPSAS, in many respects they are similar particularly as a result of the alignment of IPSAS with IFRS where appropriate. This works to minimise the differences between the IFRS and IPSAS financial reporting frameworks, so that as a far as possible a similar transaction or economic event will be accounted for in the same way by a public or private sector entity.

6.8 Timing differences between updates to frameworks would be an issue to be considered. Even where changes to IPSAS to maintain alignment with IFRS are agreed, there are due process requirements for the necessary changes to be implemented, or new standards to be developed. This can lead to temporary differences in accounting treatments between IFRS and IPSAS. IFRS for SMEs has not been amended since 2015. While the Standard is stable over a longer periods of time, it also means that it may not reflect a number of new developments in IFRS.

6.9 It should be noted that a consultation commenced in January 2020 about a proposed update to IFRS for SMEs. If IFRS for SMEs is used as the primary basis of NPO Guidance, the current consultation process introduces some uncertainty. However, the timeframes for updating IFRS for SMEs are not currently inconsistent with the projected Guidance development timeline.

Proposed hybrid solution

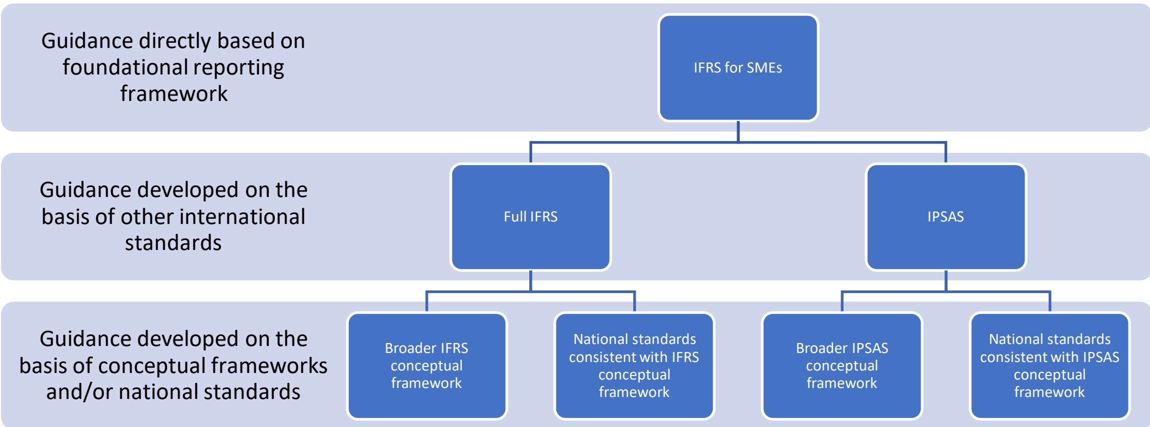
6.10 A number of different hybrid solutions could be developed. The one identified and discussed below maximises a number of advantages from the analysis above while minimising the disadvantages.

6.11 This hybrid solution would adopt IFRS for SMEs as the foundational international financial reporting framework for developing the Guidance on the basis that it:

- provides a simplified standalone set of standards and reduced disclosure requirements;
- is backed by the full IFRS conceptual framework and governance structures;
- is likely to have greater familiarity and acceptance amongst preparers, auditors and users; and
- is most feasible as it would require the lowest level of initial and ongoing resource to develop and maintain the Guidance.

6.12 As discussed above, where IFRS for SMEs is silent on a reporting issue then it is likely that full IFRS will also be silent on this issue. However IPSAS address more of the concepts that could be useful for NPOs. IPSAS could therefore be utilised as the primary source for developing the Guidance where they provide guidance that better meets the needs of users of NPO GPFRs. National private and public sector accounting standards may be referenced where there were still gaps, and these provide appropriate solutions.

6.13 It is envisaged that the use of national standards would be restricted as far as possible to those that are consistent with the conceptual frameworks of IFRS and/or IPSAS. This would assist in maintaining the conceptual integrity of the Guidance even where it drew on a broad range of sources.



6.14 As IFRS for SMEs would be the foundational framework on which the Guidance was based, it is expected that there would be a presumption that it was the requirements of IFRS for SMEs that will be followed where timing differences exist between the frameworks.

6.15 If however this is resulted in GPFRs that do not meet the needs of users, in particular due to the existence of an NPO specific reporting issue that full IFRS standards has not yet incorporated into IFRS for SMEs would assist in meeting, then it might be necessary for IFRS for SMEs be overridden by the requirements of newer IFRS standards.

Assessing the existing international frameworks and the hybrid solution against the criteria

6.16 Assessment of the existing international frameworks and the hybrid solution against the criteria in the table below suggests that the hybrid solution could provide an appropriate foundation for the development of the Guidance.

Criteria	Full IFRS	IFRS for SMEs	IPSAS	Hybrid solution
(a) Does the framework provide guidance on the most prevalent sector specific issues?	Provides some relevant guidance on sector specific issues, but a number of areas where silent. Particularly an issue in relation to areas such as "non-exchange transactions", where entities may give or receive resources without providing or receiving anything of direct financial value in return.	As per full IFRS, IFRS for SMEs provides some relevant guidance on sector specific areas but is silent in others.	Expected to provide relevant guidance in a number of these specific areas, particularly in areas such as non-exchange transactions where IFRS is silent. Some sector specific issues, however, where guidance not currently provided either due to the fact the solutions are currently at Exposure Draft stage (e.g. grant expenditure) or these issues do not impact on government entities (e.g. costs of fundraising).	By including IPSAS in the hybrid solution, it could be possible to utilise the guidance from the IPSAS suite of standards to develop guidance to some of these sector specific issues. Utilising the IFRS and IPSAS conceptual frameworks (and also national standards where these are consistent with those conceptual frameworks) would also maximise the existing guidance available to support the development of sector specific financial reporting standards.
(b) Will preparers, auditors and users be familiar with and easily able to use the framework?	Widely adopted internationally but as this is for large private sector entities, this would not automatically translate into familiarity for NPO preparers, auditors and users. Amongst smaller or less complex NPOs, it is unlikely that preparers and auditors will have regularly operated with full IFRS.	On an entity basis, the larger number of SMEs (c. 95% of all companies) when compared to large listed companies or financial institutions would mean that familiarity with IFRS for SMEs should be at least as prevalent as for full IFRS. Provides for simplified reporting requirements for for-profit	Less broadly used at present than IFRS, reflecting the relatively low level of the use of accrual accounting by governments and public sector entities globally. However, this is rapidly changing. Many of the individual standards closely aligned with IFRS. It is only those standards that deal with public sector specific issues, such as revenue from non-exchange	As primarily based on IFRS for SMEs, could provide financial reporting guidance that more preparers, auditors and users were familiar with. Omitting irrelevant accounting topics for non-listed entities, reductions in accounting options and reduced disclosure requirements would also improve ease of use. Where the Guidance provided sector specific financial reporting

Criteria	Full IFRS	IFRS for SMEs	IPSAS	Hybrid solution
	The focus of the full suite of IFRS on the financial reporting requirements of large and complex listed companies and financial institutions may also lead to questions of ease of use by NPOs. Preparers would have to place reliance on the materiality principle to determine if a standard needed to be applied and the extent of disclosure necessary. This would increase the level of judgements required by NPOs and lead to greater audit work.	organisations to meet the needs of smaller and less complex organisations. This includes the omittance of irrelevant accounting topics for non-listed entities, reductions in accounting options and reduced disclosure requirements. Written in clear easily translatable language. Revisions to the entire standard are only made approximately every five years. This would improve the ease with which the framework can be utilised by NPOs. Gaps in topic coverage could impact on ease of use, with NPO's potentially having to create their own interpretations.	transactions and accounting for social benefits that would be unfamiliar to individuals who are used to operating with IFRS. Ease of use to NPOs might be reduced by an absence of specific standards and reduced disclosure requirements aimed at smaller and less complex entities within IPSAS. Preparers would have to place reliance on the materiality principle to determine if a standard needs to be applied and the extent of disclosure necessary.	solutions based on full IPSAS or national accounting frameworks , these would have been developed from a relatively common conceptual basis so should at least be conceptually familiar. Would also be expected that these would be developed with aim of ensuring ease of use and with reduced disclosure requirements. By providing financial reporting guidance for sector specific issues this should also improve the acceptability of the hybrid solution.
(c) How feasible will the development and maintenance of	Complex suite of standards, with a significant number of different accounting options available in many standards	Simplified framework where revisions are limited, with the IASB committed to limiting	Complex suite of standards, with a significant number of different accounting options available in many standards	Utilising IFRS for SMEs as the foundational framework would limit the initial resources that will need to be devoted to developing

Criteria	Full IFRS	IFRS for SMEs	IPSAS	Hybrid solution
Guidance under the framework be?	and extensive disclosure requirements. Complexity and frequency of change would necessitate a significant amount of initial work and a process of monitoring for the interpretation and adaption of standards for the NPO context. Would require the investment of significant resource, both initially and on an ongoing basis, to ensure the development and maintenance of the Guidance was consistent with the underlying framework.	revisions to the entire Standard and only once every three years. In practice the IASB has limited revision to approximately every five years. Initial resource to develop the Guidance would be less than under full IFRS or IPSAS. Once the Guidance was developed it would not need to be subject to as high a level continual monitoring and update as a result of changes to underlying standards in the framework on which it was based. This would limit the resource required to develop and maintain the Guidance.	and extensive disclosure requirements. Subject to ongoing development and change as a result of maintaining alignment with IFRS where appropriate, and also due to the development of public sector specific standards such as social benefits. Would require the investment of significant resource, both initially and on an ongoing basis, to ensure the development and maintenance of the Guidance was consistent with the underlying framework.	and maintaining the Guidance due to more limited accounting treatments and disclosure requirements and infrequent nature of revisions to IFRS for SMEs. Where specific NPO guidance did utilise other frameworks under the hybrid solution, it would be necessary to monitor developments in these frameworks against the Guidance. This would, however be less onerous than if the framework used full IFRS or IPSAS as its foundation. Conceptual coherence maintained though similarity of conceptual frameworks of IFRS and IPSAS.

6.1 Part 1 of this Consultation Paper has sought to:

- Define which NPOs are in scope for IFR4NPO through a broad characteristics approach;
- Provide an overview of the general accountability landscape for NPOs;
- Focus on aspects of financial accountability, particularly with respect to donors, and how GPFRs based on internationally applicable financial reporting guidance can assist in providing solutions to problems with accountability arrangements;
- Highlight how IFR4NPO can strengthen financial management and accountability and how standardisation can reduce burdens for both NPOs and donors in the areas of due diligence and indirect costs; and
- Examine existing international financial reporting frameworks and the extent to which these frameworks provide guidance relevant to the NPO sector specific issues identified.

6.17 This Section proposes a hybrid solution that draws on the strengths of the current international financial reporting frameworks as a way forward. Assessment of the proposed hybrid solution against the criteria suggests that it could provide an appropriate foundation for the development of internationally applicable financial reporting guidance for NPOs.

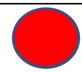
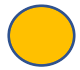
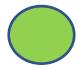
6.18 The current update to IFRS for SMEs introduces some uncertainty about elements of the standard, and complicate delivery of the project. However, the timeframes for the review of the standard are not inconsistent with the development of this Guidance.

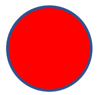
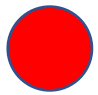
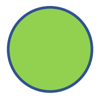
6.19 Guidance developed using the proposed hybrid approach could draw upon a wide range of existing financial reporting standards, and has the best chance of addressing the issues that are common across the NPO sector and meeting the general financial reporting requirements of funders and regulators as well as preparers in an efficient and effective manner.

General Matters for Comment 6
This Section has provided an overview of the proposed way forward using a hybrid solution for developing the Guidance. This solution, rather than using one international framework, would take aspects of different frameworks and brings them together in order to create a framework that addresses NPO sector reporting needs. 6.1 - Do you agree that a hybrid solution should be considered as a means of developing the Guidance? If not, why not? How would you overcome the disadvantages of using a single existing international framework? 6.2 – Do you agree with the hybrid solution proposed? If not, why not? What alternative solution would you propose and why? 6.3 – Do you agree with our assessment of the hybrid solution against the criteria? If not, why not?

ANNEX: Analysis of guidance provided by international financial reporting frameworks against sector specific issues

The following key is in use for the table:

Applicability of existing standards to specific NPO reporting issue	Rating
The framework is silent on the issues or provides guidance that is largely not applicable in the NPO context	
The framework provides some guidance that could be utilised in the NPO context but it is not tailored to the specific issues	
The framework provides a range of guidance that appears to be directly applicable in the NPO context and to the specific issues	

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
Accounting for incoming resources				
Recognition and measurement of incoming resources from external sources	What are the overarching principles for the recognition and measurement of incoming resources from 'non-exchange' transactions, (of which donations, grants, services in-kind income are all categories)? Is there anything sector specific regarding exchange transactions (e.g. provision of services to third parties)?	IFRS provides no specific guidance on non-exchange transactions.  For revenue from exchange transactions IFRS 15 *Revenue from Contracts with Customers* establishes principles for reporting on the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.	IFRS for SMEs provides no specific guidance on non-exchange transactions.  It has also not yet been updated to reflect the principles of IFRS 15, but Section 23 *Revenue* covers accounting for revenue arising from the sale of goods, rendering of services, construction contracts and the use by others of entity assets yielding interest, royalties or dividends.	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on the recognition and measurement of revenue from non-exchange transactions. An exposure draft ED 71 *Revenue without Performance Obligations* was released in February 2020 and will provide additional guidance once it becomes a full standard. 

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
				IPSAS 9 *Revenue from Exchange Transactions* covers accounting for revenue arising from the sale of goods, rendering of services, and the use by others of entity assets yielding interest, royalties, and dividends or similar distributions.
Cash transfers - donations, grants and other contributions with time and purpose requirements and other criteria/performance obligations	Timing of income recognition and definition of performance criteria/obligation. What is the recognition and measurement process when receiving donations that are used to fulfil requirements (including a specific time and purpose requirement) in subsequent periods? When should donations to purchase a capital asset be recognised? What if the donation is repayable if the asset, at some future date, is no longer used for its intended purpose?	IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* provides recognition, measurement and disclosure requirements for income from government grants.	IFRS for SMEs incorporates IAS 20 within Section 24 *Government Grants.*	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on present obligations which may give rise to a liability in respect of any non-exchange transaction.
Services in-Kind (including volunteers)	When should services in-kind be recognised and if so how are they measured? What disclosures should be provided? Recognition and measurement of 'right of use' donations (including	IFRS provides no specific accounting guidance on the recognition of services in-kind.	IFRS for SMEs provides no specific accounting guidance on the recognition of services in-kind.	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on accounting for services-in-kind.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	free use of space and equipment)?			
Gifts in-Kind (non-financial assets and inventory)	When should gifts in-kind be recognised and how should they be measured, including low value items such as inventory (second-hand for sale and new for distribution as part of charitable activities)? How should assets financed by capital grants be recognised and measured (i.e. gross or net), and the implications for the recognition of the grant in income? How should assets that can only be used for a specific purpose and may have to be returned be measured initially and subsequently?	IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* provides guidance if received from a government entity.	IFRS for SMEs incorporates IAS 20 within Section 24 *Government Grants.*	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on accounting for Gifts and Donations, including Gifts-in-Kind.
Recognition of legacy/bequest income and endowments	When should bequests be recognised? What are the considerations involved with perpetual trusts and/or a portfolio of similar smaller assets? How are endowments recognised and classified, including the treatment of the initial contribution, subsequent	IFRS provides no specific guidance on accounting for legacies and bequest income.	IFRS for SMEs provides no specific guidance on accounting for legacies and bequest income.	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on accounting for bequests, gifts and donations.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	changes in the value of the initial contribution and treatment of income earned? How should income from endowments be presented in the operating statement and balance sheet? What disclosures should be required for any restrictions on the entity?			
Accounting for outgoing resources				
Categorisation of expenses – function or nature	Should the primary analysis of expenses be based on function or nature of spend? What should the primary headings be?	IAS 1 *Presentation of Financial Statements* requires that an entity presents, either on the face of the statement of financial performance or in the notes, an analysis of expenses using a classification based on either the nature of expenses or their function within the entity, whichever provides information that most reliable and relevant.	IFRS for SMEs requires a similar categorisation to full IFRS.	IPSAS 1 *Presentation of Financial Statements* requires that an entity presents, either on the face of the statement of financial performance or in the notes, an analysis of expenses using a classification based on either the nature of expenses or their function within the entity, whichever provides information that most reliable and relevant.
Costs of fundraising	How should the costs of fund raising be defined (for example, whether to include business development spend and/or overheads)?	IFRS provides no specific guidance on defining the costs of fundraising.	IFRS for SMEs provides no specific guidance on defining the costs of fundraising.	IPSAS provides no specific guidance on defining the costs of fundraising.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	How should the costs of fundraising be recognised and/or presented (i.e. on a gross basis or netted against income)?			
Grant expenses	Recognition and measurement of NPO 'non-exchange' transfers to individuals and other entities? When is a liability recognised (whether a grant or promise), particularly in a multi-year arrangement?	IFRS provides no specific guidance for accounting for grant expenditure by an entity.	IFRS provides no specific guidance for accounting for grant expenditure by an entity.	There is presently no specific IPSAS on non-exchange expenses related to grants. An exposure draft ED 72 *Transfer Expenses* was released in February 2020 and will provide additional guidance once it becomes a full standard.
Agency relationships	When is the NPO acting as an agent and when is it acting as principal? Is any disclosure required of the gross amounts relating to agency activity or assets in custody, (including cost pass through and assets held on behalf of another entity/person)?	IFRS 15 *Revenue from Contracts with Customers* provides guidance on determining whether an entity is a principal or agent in relation to the provision of goods or services to a customer in relation to revenue recognition. . There is no specific guidance on recognition of accounting for	IFRS for SMEs has not yet been updated to reflect the principles of IFRS 15, but Section 23 *Revenue* also requires an entity to only recognise commission as revenue if it is acting as an agent. There is no specific guidance on recognition of accounting for expenditure in agency relationships.	IPSAS 9 *Revenue from Exchange Transactions* also provides guidance on determining whether an entity is a principal or agent in relation to the provision of goods or services to a customer in relation to revenue recognition. There is no specific guidance on recognition of accounting for expenditure in agency relationships.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
		expenditure in agency relationships.		
Accounting for non-financial assets				
Measurement of tangible and intangible assets held for their service potential	How should assets that are held for service potential be measured, both initially and subsequently? How do you identify impairment where assets are held for service potential (e.g. assets do not generate any income, or generate income at below market rate)? When an impairment has been recognised, what disclosures should be made?	IFRS provides no specific guidance on measurement of tangible and intangible assets held for their service potential.	IFRS for SMEs requires such assets to be held under a cost model or a revaluation model based on fair value with no specific guidance on valuation for assets held for their service potential.	IPSAS 17 *Property, Plant and Equipment* and IPSAS 21 *Impairment of Non-Cash Generating Assets* contains guidance on initial and subsequent measurement, including impairment, and disclosures for tangible and intangible assets.
Heritage assets and/or obligations	Recognition and measurement of heritage assets. What disclosures should be made about the nature and scale of heritage assets and acquisition, preservation etc. of the collection? Recognition and measurement of significant heritage obligations,	IFRS provides no specific guidance on heritage assets.	IFRS for SMEs provides no specific guidance on heritage assets.	IPSASB released a consultation paper on accounting for heritage assets in 2017 and an exposure draft is currently being developed. There is presently, however, no standard.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	and any impact on the measurement of related assets?			
Concessionary loans for social purposes	What is the definition of a concessionary loan? What is the initial and subsequent measurement of special credit conditions? What is the treatment within a group if there is an inter-company loan with a for-profit entity? What disclosures should be made?	IFRS 9 *Financial Instruments* requires that when a loan is not on commercial terms it must be split into a 'below-market' element and a 'loan' element with the below-market element accounting for under the Conceptual Framework if no relevant standard exists.	IFRS for SMEs provides no specific guidance on concessionary loans.	IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers)* provides guidance on recognising non-exchange revenue related to concessionary loans. IPSAS 41 *Financial Instruments* provides guidance on the recognition and measurement of concessionary loans and IPSAS 30 *Financial Instruments: Disclosures* provides guidance on concessionary loan disclosures.
Concessionary leases	How should such arrangements be accounted for?	There is no specific guidance in IFRS on accounting for concessionary leases.	There is no specific guidance in IFRS on accounting for concessionary leases.	There is no specific guidance in IPSAS on accounting for concessionary leases. An exposure draft proposed an accounting treatment with lessees recognising the subsidy inherent in such an arrangement in accordance with IPSAS 23 *Revenue from non-exchange transactions (taxes and transfers) except if a present obligation exists.* Lessors would recognise the subsidy as an expenses on accordance with IPSAS 29 *Financial Instruments: Recognition and Measurement*.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
Accounting for investment/financial assets	Classification, recognition and measurement requirements.	IFRS 9 *Financial Instruments* provides guidance for the classification, recognition and measurement of investments and other financial assets.	IFRS for SMEs provides guidance in Section 10 *Basic Financial Instruments* and Section 11 *Other Financial Instrument Issues*	IPSAS 41 *Financial Instruments* provides guidance for the classification, recognition and measurement of investments and other financial assets.
Service concessions arising in NPOs as grantor	When do these arise in the not-for-profit sector e.g. low income housing? What disclosures are required?	IFRS provides no specific guidance on grantor accounting requirement in service concessions.	IFRS for SMEs provides no specific guidance on grantor accounting requirement in service concessions.	IPSAS 32 *Service Concession Arrangements: Grantor* provides guidance on accounting requirements of grantors in a service concession arrangement.
Service concessions arising in NPOs as operator	When do these arise in the not-for-profit sector e.g. low income housing? What disclosures are required?	IFRIC 12 provides accounting guidance to the operator in a service concession arrangement.	IFRS for SMEs provides no specific accounting guidance for the operator in a service concession arrangement.	IPSAS does not provide specific accounting guidance for the operator in a service concession arrangement.
Reporting entity				
Definition of control (including the treatment of branches)	How is control defined (as NPOs may not be exposed to investee returns in a conventional sense)?	IFRS 10 *Consolidated financial Statements* provides a definition of control that focuses on exposure or rights to variable returns from involvement with an	IFRS for SMEs in Section 9 *Consolidated and Separate Financial Statements* provides guidance on control that focuses on the power to govern the	IPSAS 35 *Consolidated Financial Statements* provides a definition of control that focuses on exposure or rights to variable benefits.

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	How is a branch defined? Should all branches be accounted for as part of an NPO? What is the status of the financial statements of a branch that is not a separate legal entity?	investee and the ability to affect those returns through power over the investee.	financial and operating policies of an entity so as to obtain benefits from its activities.	
Mergers and acquisitions (combinations)	What is the accounting treatment for the combination of two or more NPOs? Should merger accounting be permitted/ required? If the acquisition method is required what is the accounting for a gain/negative goodwill?	IFRS 3 *Business Combinations* provides guidance in determining whether a transaction or other event is a business combination and requires the acquisition method to be applied so that the acquirer recognises assets acquired and liabilities assumed. It also addresses accounting for goodwill.	IFRS for SME Section 19 *Business Combinations and Goodwill* provides guidance on identifying an acquirer, measuring the cost of the business combination and allocating the cost to the assets acquired and liabilities assumed. It also addresses accounting for goodwill.	IPSAS 40 *Public Sector Combinations* provides accounting guidance on public sector combinations based on classification as either an amalgamation or an acquisition.
Intragroup transactions	When is income from a subsidiary recognised in the parent NPO's accounts taking account of legal considerations relating to the way in which the profits of a subsidiary are given to a parent?	IFRS 10 *Consolidated financial Statements* provides guidance on the treatment of intragroup balances and transactions in consolidated statements, including requirements to eliminate.	IFRS for SMEs in Section 9 *Consolidated and Separate Financial Statements* provides guidance on the treatment of intragroup balances and transactions in consolidated statements, including requirements to eliminate.	IPSAS 35 *Consolidated Financial Statements* provides guidance on the treatment of intragroup balances and transactions in consolidated statements, including requirements to eliminate.

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	What disclosure should be required by both sides of the relationship/transaction when a branch is part of a larger NPO or the NPO is part of a group?			
Form and content of financial reports				
Financial statement presentation	How should financial statements be presented to help the user understanding of an NPO's activities? Should there be disclosure of material categories of income and expenditure and/or transactions? How should unrestricted and restricted funds that can be used for specific NPO purposes be presented for the main financial statements and notes (including reserves)? How does this align with donor reporting requirements?	IAS 1 *Presentation of Financial Statements* provides guidance on the reporting requirements for the presentation of financial statement and disclosure of material elements.	IFRS for SMEs Section 3 *Financial Statement Presentation* explains fair presentation of financial statements, what compliance with IFRS for SMEs requires and what a complete set of financial statements is. There are individual Sections providing requirements on: *5 Statement of Financial Position* *6 Statement of Comprehensive Income and Income Statement* *7 Statement of Changes in Equity and Statement of Income and Retained Earnings* *8 Statement of Cash Flows*	IPSAS 1 *Presentation of Financial Statements* provides guidance on the reporting requirements for the presentation of financial statements and disclosure of material elements.
Narrative reporting, (including service reporting)	What should the narrative/non-financial reporting requirements be for NPOs? Should ratios be required for narrative reporting? If they are included, how should costs be	IFRS Practice Statement 1 *Management Commentary provides some* key principles for management commentary, and additional guidance in areas including the nature of the business, objectives and	IFRS Practice Statement 1 *Management Commentary provides some* key principles for management commentary, and additional guidance in areas including the nature of the business, objectives and strategies,	Guidance on narrative reporting requirements is contained within IPSAS Recommended Practice Guideline 1 *Reporting on the long term sustainability of an entity's finances,* Recommended Practice Guideline 2 *Financial Statement*

Topic	Issues	IFRS	IFRS for SMEs	IPSAS
	classified been support costs and those attributable to operational delivery?	strategies, resources, risks and relationships, results and prospects, and performance measures and indicators.	resources, risks and relationships, results and prospects, and performance measures and indicators.	*Discussion and Analysis,* and Recommended Practice Guideline 3 *Reporting Service Performance Information*.
Related party transactions	Definition, required disclosures and presentation of related party transactions. Implications of local legal requirements?	IAS 24 *Related Party Disclosures* provides guidance to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transaction and outstanding balances with such parties.	IFRS for SMES Section 33 *Related Party Disclosures* provides guidance to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transaction and outstanding balances with such parties.	IPSAS 20 *Related Party Transactions* provides guidance on the disclosure of the existence of related party relationships where control exists, and the disclosure of information about transactions between the entity and its related parties in certain circumstances.
Remuneration/pay disclosures	What disclosures should be made and who should be included?	IAS 24 *Related Party Disclosures* provides guidance on the disclosure of key management personnel compensation.	IFRS for SMES Section 33 *Related Party Disclosures* provides guidance on the disclosure of key management personnel compensation.	IPSAS 20 *Related Party Transactions* provides guidance on the disclosure of the remuneration of key management personnel.