



# Technical Advisory Group Issue Paper

AGENDA ITEM: TAGED08-07  
29 and 30 September 2022 – Hybrid

## ED1 –NPO description and reporting boundary

Summary	<p>This paper focuses on the most significant comments raised by TAG members to ED1 in relation to consolidation and the description of NPOs included in Section 1 <i>Non-profit organisations</i>, Section 2 <i>Concepts and Pervasive Principles</i>, and Section 9 <i>Consolidated and separate financial statements</i>. These comments have been grouped under the following headings:</p> <ul style="list-style-type: none"><li>• Broad characteristics and indicators;</li><li>• Public accountability; and</li><li>• Consolidation.</li></ul> <p>For each area we provide an overview of the feedback received from TAG members, the proposed approach taken to updating the ED to reflect this feedback, and any remaining questions to TAG members.</p>
Purpose/Objective of the paper	<p>To provide TAG members with an opportunity to understand comments raised to ED1 in relation to Section 1 <i>Non-profit organisations</i> and Section 9 <i>Consolidated and separate financial statements</i>, to provide feedback on the approach to responding to these comments proposed by the Secretariat, and to respond to the questions that will enable the finalisation of the ED..</p>
Other supporting items	N/A
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Actions for this meeting	<p><u>Comment</u> on the proposed approach to responding to TAG comments raised to ED1 in relation to Section 2 <i>Non-profit organisations</i> and Section 9 <i>Consolidated and separate financial statements</i> and provide; and</p> <p><u>Advise</u> on the questions raised.</p>

# Technical Advisory Group

## ED1 - NPO description and the reporting boundary

### 1. Introduction

- 1.1 The TAG was provided with a full draft of ED 1 in July 2022. This comprised:
- Draft of the invitation to comment with the authoritative guidance;
  - Draft basis for conclusions; and
  - Draft implementation guidance.
- 1.2 This paper focuses on the most significant comments that were raised by TAG members in relation to the description of NPOs and the reporting boundary in Section 1 *Non-profit organisations*, Section 2 *Concepts and Pervasive Principles*, and Section 9 *Consolidated and separate financial statements*. These have been grouped under the following areas:
- Broad characteristics and indicators;
  - Public accountability and societal accountability; and
  - Consolidation
- 1.3 For each area we provide an overview of the feedback received from TAG members and the proposed approach taken to updating the ED to reflect this feedback. Questions are also posed to TAG members to give an opportunity for advice to be provided that will enable the finalisation of the ED.

### 2. Broad characteristics and indicators

- 2.1 Section 1 *Non-profit organisations* proposes a broad characteristics approach to describing NPOs. This descriptive approach was chosen because global diversity in both the types of entities that could be described as NPOs and the legal and regulatory frameworks that apply to them meant that any approach based on a single definition would exclude many entities that could benefit from INPAG. As it will not always be clear whether an entity displays all the broad characteristics, indicators are included in the Application Guidance to provide assistance in making judgements.
- 2.2 A number of TAG members suggested that it is made clear that the broad characteristics are a description of NPOs only for the purposes of INPAG. The Secretariat agrees and has amended the introductory text at G1.2. In addition there was further feedback on the individual broad characteristics and indicators.

*Primary objective of providing benefit to the public and membership organisations*

- 2.3 A number of comments were received from TAG members relating to the broad characteristic of an NPO having the 'primary objective of providing a benefit to the public'. In particular there were questions as to whether the explanation of this broad characteristic would permit membership organisations to be described as NPOs.
- 2.4 The explanation of this broad characteristic includes the statement that 'where an NPO has members or providers of contributed capital or similar ownership claims, they should receive no more than an incidental private benefit from the NPO'. The purpose of this statement is to permit NPOs such as member organisations to provide private benefits to members, but to make sure that where such private benefits are provided, they are incidental to the primary objective of providing a benefit to the public.
- 2.5 For example, a membership organisation that provides fresh fruit and vegetables at a discounted price to members, with membership restricted to individuals from a particular community who otherwise would not be able to afford this food is providing members with a private benefit of cheaper food. But this private benefit is incidental to the primary objective of the NPO of providing a benefit to the public by ensuring that the individuals within this particular community are able to access healthy food.
- 2.6 As with the other broad characteristics, it is necessary to apply judgement to this issue. For membership organisations and other organisations where the section of the public that benefits is restricted, it will in particular be necessary to consider whether a sufficient section of the public benefits. This will need to be based on the NPOs purpose and that any private benefits are incidental to the NPO carrying out its purpose. In other words they are not the primary objective of the NPO.
- 2.7 Given that this was raised by several TAG members, additional wording around incidental private benefits has been included in the description of this broad characteristic in Section 1 *Non-profit organisations* at G1.3.

**Question 1:** Does the additional wording clarify that member organisations can be NPOs provided that private benefits are incidental to the primary objective of providing a benefit to the public?

### *Financial surpluses*

- 2.8 The second broad characteristic 'direct surpluses for the benefit of the public' included the example of a financial surplus being generated from the receipt of donations that are intended to support programmes over multiple financial years. One TAG member commented that this was effectively a 'temporary' surplus and different to the other examples of receiving income from sales and having financial assets earning returns.
- 2.9 The Secretariat agrees with this view and has made the proposed amendments to the broad characteristics at G1.4, subject to agreement from other TAG members.

**Question 2:** Are TAG members content with the proposed change to one of the examples of how an NPO might generate a financial surplus?

### *Not government or public sector that should prepare general purpose financial report under public sector financial reporting standards*

- 2.10 The third broad characteristic aims to make clear that for most government and public sector entities, the accountability and decision-making needs of the users of their general purpose financial reports are likely to be best met by preparing them under public sector accounting standards. This is because government and public sector entities have different characteristics to NPOs, and INPAG does not provide guidance for transactions and economic events that are only relevant to the public sector.
- 2.11 This characteristic stated that entities with the characteristics of public sector entities should not be described as NPOs. This was questioned by TAG members, who noted that such a statement was too broad and could be interpreted as being beyond the purposes of INPAG. The Secretariat agrees with these views and has removed this statement.

**Question 3:** Do TAG members agree with the removal of the statement that entities with public sector characteristics should not be described as NPOs?

### *Indicators*

- 2.12 Indicators were developed to assist entities in determining whether they are within the intended scope of INPAG. The indicators are intended to assist in decision-making where it is not clear if an entity fully displays the broad characteristics of an NPO.

- 2.13 A TAG member requested if the relationship between the individual indicators and characteristics could be explained to help entities determine which factors are relevant.
- 2.14 The individual indicators do not always map directly to individual broad characteristics, but rather can be seen as applying across them. For example “an absence of individuals with rights to financial returns from surpluses” can be used to assist in making a judgement as to whether financial surpluses are directed for the benefit of the public and if there are more than incidental private benefits being provided by an NPO.
- 2.15 While there is not always a direct link to individual broad characteristics, the Secretariat has updated the description of the indicators in AG1.3 to AG1.6 to provide further context as to how they can assist in determining if the broad characteristics have been met.

**Question 4:** Do TAG members support the inclusion of the additional text in AG1.3 to AG1.6 to explain the link between individual indicators and broad characteristics?

- 2.16 Another TAG member questioned whether endowments should be included as an example alongside ‘other assets that are held and used for the benefit of the public’. The intention of this indicator had been to highlight the holding and use of physical assets by NPOs. The Secretariat can see that there may be a case to include financial assets such as endowments in this indicator given that they are important to many NPOs and are ultimately held to provide a benefit to the public. As such the assets included in AG1.6 have been broadened to include financial assets.

**Question 5:** Do TAG members support the broadening of the fourth indicator to include financial assets like endowments?

### 3. Public accountability

- 3.1 The *IFRS for SMEs* Accounting Standard is for use only by entities that do not have public accountability. Section 1 *Non-profit organisations* maintains some of the text on public accountability from the *IFRS for SMEs* Accounting Standard to explain the concept of public accountability and the use of INPAG by entities that have public accountability. Some TAG members questioned the extent to which public accountability is relevant to NPOs and has been tailored to the NPO context.

- 3.2 While it is not expected to be common, there is a possibility given the different legal and regulatory structures in place globally, that an entity considered by a jurisdiction to meet the description of an NPO could also meet the public accountability definition in IFRS (i.e. have either traded shares or debt or hold assets in a fiduciary capacity). Text on public accountability has therefore been retained in Section 1 *Non-profit organisations*. The text says that while entities that have public accountability may find INPAG useful, it is unlikely to meet the needs of their users.
- 3.3 Earlier drafting of the text had stated that entities with public accountability should not use INPAG, but this prohibition was removed at the request of TAG members. This was to reflect the fact that the IFR4NPO project has no authority over jurisdictions or entities that may wish to apply INPAG. Instead an entity with public accountability is required to provide an explanation as to why the use of INPAG meets the needs of users as part of the disclosures required by G3.4-G3.8. However, in paragraph G1.9 it is made clear that needs of NPOs with public accountability are not likely to be entirely met by INPAG. Feedback from one TAG member indicated, however, that there was still some discomfort with an entity with public accountability using INPAG. As such the Secretariat is seeking confirmation from TAG members that they support the approach taken.

**Question 6:** Given that individual jurisdictions will determine which entities apply INPAG, do TAG members still support:

- (i) the inclusion of text on public accountability;
- (ii) text that states that INPAG is unlikely to meet the needs of users of the GPFs of publicly accountable entities; and
- (iii) the requirement that publicly accountable entities that use INPAG

- 3.4 A TAG member noted that the text in G1.6-G1.8 was very for-profit focused and questioned whether examples or context could be included to demonstrate when an NPO might have public accountability.
- 3.5 Public accountability is primarily a private sector concept. It is based on an entity either having debt or equity instruments traded in a public market or holding assets in a fiduciary capacity as a primary business. It is difficult to tailor this definition to the NPO context, with any examples likely to be specific to an individual entity or jurisdiction. Given this difficulty, the Secretariat will update the Basis for Conclusions to provide some additional clarity around its views on the situations in which theoretically an NPO might have public accountability.

**Question 7:** Are TAG members content with the Basis for Conclusions being updated to provide additional clarity around the situations in which theoretically and NPO might have public accountability?



#### 4. Reporting NPO, including consolidation

##### *Mixed groups*

- 4.1 Section 2 *Concepts and pervasive principles* explains that financial reports prepared in accordance with INPAG provide information viewed from the perspective of the reporting entity as a whole, not from the perspective of any particular group of the NPO's users. Section 9 *Consolidated and separate financial statements* sets out guidance on determining which entities (whether NPOs or non-NPS) should be considered part of an NPO group, and how they should be reported upon.
- 4.2 A TAG member asked whether there might be a need for guidance where a group includes NPOs and non-NPOs and the status of the overarching parent entity was not clear. A particular concern was at which level the indicators and criteria should be applied to determine that the group was an NPO to which INPAG could be applied.
- 4.3 The Secretariat tend to think that the indicators and criteria should ideally be applied at the level of the parent entity. However, they recognise that there might be circumstances where this is difficult; for example where the parent NPO exists mainly as a collection of other NPOs or activities. The Secretariat would like TAG's views on whether this is likely to be trivial, and if not, whether guidance should be developed.

**Question 8:** Do TAG members consider that this is an issue on which guidance would be helpful?

##### *Undue cost or effort*

- 4.4 A TAG member indicated that it was unclear to them why at G9.8 consideration of undue cost or effort would be necessary or appropriate when considering if a controlled entity should be excluded from consolidation. This was on the basis that if more relevant information is provided by excluding an entity from consolidation, then consideration of cost and effort is not necessary.
- 4.5 They also indicated that they would not support allowing an investor NPO to exclude an entity from consolidation purely on the basis of undue cost or effort, noting that IFRS for SMEs does not include such an exemption.
- 4.6 The Secretariat notes that issues around cost and effort (in relation to the benefit received from the consolidated information) were raised in the general discussion of whether consolidation of any kind is appropriate. TAG views on the appropriateness of considerations of undue cost and effort and whether they

are relevant to the determination of whether an entity might be excluded from consolidation would be welcome.

**Question 9:** Are TAG members content that consideration of 'undue cost or effort' is relevant to the question of whether a controlled entity should be excluded from consolidation?

#### *Entities excluded from consolidation*

- 4.7 A TAG member questioned whether the disclosures provided per G9.8 when entities are not consolidated were sufficient, and in particular whether it would be appropriate to provide more substantial information which would allow users of the financial statements to perform consolidation if they wish. Given the rationale for non-consolidation is likely to rest on the relevance of the information, this may be unlikely.
- 4.8 The Secretariat is of the view that disclosures should mainly focus on the fact of exclusion, the reason for exclusion, and the relationship of the excluded entity from the consolidated financial statements. In addition paragraph G9.24 requires the carrying value of any entities not consolidated to be disclosed.

**Question 10:** Do TAG members content with the additional disclosures proposed?

#### *Control*

- 4.9 A TAG member queried whether entities whose funding was dominated by a single provider would be controlled (AG9.6), given that the recipient entity could always choose not to accept/receive the funds.
- 4.10 The Secretariat is of the view that where a grant-making NPO is the only fund provider or a very significant fund provider, there may be a control relationship. While non-acceptance may always be theoretically possible, there may in practice be dependency which makes this choice untenable.

**Question 11:** Do TAG members agree that control may arise where a grant-making NPO is the only fund provider, or a very significant fund provide?

#### *Other points*

- 4.11 A TAG member noted that when discussing indicators of power, the reference in G9.4D to 'service or capital budgets' could be shortened without loss of meaning to simply 'budgets'. The Secretariat consider that, while technically superfluous



these references provide useful context which may make the INPAG guidance more readable.

- 4.12 A TAG member queried whether the explanation at G9.11 that a parent entity might comprise 'a complete set of activities', as this might be caught within the definition of a reporting entity. Although discussed in the earlier material on reporting entity, the inclusion of 'complete sets of activities' may be particularly pertinent at the group level. For that reason, Secretariat suggest that providing this full description is helpful.

## 5. Material to review

- 5.1 The ED has been updated to reflect the proposed approach to the feedback from the TAG on these issues and other less substantive issues and editing requests. A full redraft is provided as a separate resource for the meeting. The points addressed in this paper related mainly to Section 1 *Non-profit organisations* and Section 9 *Consolidated and separate financial statements*. Tracked changes will show the edits made.

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