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FOR NON PROFIT ORGANISATIONS

Technical Advisory Group
Issue Paper

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Transition to INPAG

Summary	The paper describes the main considerations in shaping the guidance for NPOs transitioning to INPAG.
Purpose/Objective of the paper	The paper identifies considerations for NPOs who may be transitioning from international GAAP, national GAAP, cash based accounts or no previous requirement for formal accounts. The paper examines the need for adaptations from Section 35 of the *IFRS for SMEs* Accounting Standard and whether additional guidance is required.
Other supporting items	n/a
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Actions for this meeting	**Advise on**: i. the requirement for opening balances ii. the need for comparative information iii. the requirement to disclose grant obligations and constraints on resources provided that exist at the date of transition iv. disclosures for those that partly comply with INPAG but have not yet fully adopted the requirements

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Transition to INPAG

1. Introduction

1.1 Exposure Draft 3 includes the Section that sets out the requirements for NPOs who transition to INPAG. Underpinning this guidance need to be principles that determine what information NPOs are required to include in their first set of accounts under INPAG and also the disclosures that they have to make.

1.2 This Section will need to reflect that some entities will have prepared financial statements using the *IFRS for SMEs* Accounting Standard or other international GAAP, national GAAP, using cash or modified cash principles or may never have produced financial statements before. This variety of start points needs to be acknowledged with the focus on the key information that will be required.

2. Requirements in ED1

2.1 Exposure Draft 1 set out some high-level requirements, particularly in the context of which entities can state that they are in compliance with INPAG. Section G3.3 states that financial statements shall not be described as complying with INPAG unless they comply with all the requirements of INPAG and that where an NPO is transitioning to INPAG, it must comply with the disclosure requirements in Section 36 *Transition to the Guidance* (now Section 38). It also states that an NPO whose financial statements comply with INPAG shall make an explicit and unreserved statement of such compliance in the notes.

2.2 The application guidance states that if exceptions or caveats are needed, then compliance with INPAG cannot be stated. It does, however, allow for INPAG to be adopted over time when permitted by the jurisdiction, or if the NPO determines a transition path that means that full adoption of INPAG takes place over time and not all the requirements are met immediately.

2.3 The application guidance acknowledges that the timeline that an NPO choses to adopt may differ to that permitted by INPAG and that in such circumstances, the disclosure requirements in Section 38 may not be appropriate. It requires an NPO to consider what disclosures will be necessary to enable users to understand the financial statements, in addition to any disclosures that are required by the relevant regulator.

3. NPO specific considerations

3.1 As noted in 1.2 above NPOs may have many different start points, which is likely to mean differing levels of challenge in adopting INPAG for the first time. The transition requirements therefore need to reflect the variety of start points.

3.2 Section 35 of the *IFRS for SMEs* Accounting Standard is based on an entity moving from another framework such as full IFRS, national GAAP or local income tax basis and also provides for those entities that did not previously present financial statements. Section 35 of the *IFRS for SMEs* Accounting Standard requires that at the date of transition to INPAG all entities need to create opening balances to recognise all assets and liabilities required to be recognised in INPAG, but not assets and liabilities not permitted by INPAG.

3.3 It is possible that many NPOs do not have opening balances, particularly if they previously prepared financial statements on a cash basis. The Standard provides for deemed costs to be determined where assets and liabilities were not previously recognised. There may be challenges for NPOs in arriving at these values due to lack of expertise, capability and capacity.

3.4 The existing guidance does not cover grant arrangements that an NPO may have as a grant provider or a grant recipient. Under the proposals in ED2, grant arrangements will need to be assessed to determine whether they are an enforceable grant arrangement (EGA) or an other funding arrangement (OFA). If the principles in Section 35 of the *IFRS for SMEs* Accounting Standard are adopted, NPOs would then need to determine enforceable grant arrangement assets and liabilities, to calculate the opening balance of funds with restrictions and within funds without restrictions, and the extent to which there are any internally or externally imposed constraints over these balances. This will add to challenges on transition.

3.5 Section 35 of the *IFRS for SMEs* Accounting Standard requires that (in equivalent terms) the date of transition to INPAG is the beginning of the earliest period for which the NPO presents full comparative information in accordance with INPAG in its first financial statements that conform to INPAG. In other words, if an NPO is not able to generate comparative information for its first year of using INPAG, it will need to produce 2 years of INPAG based financial statements before being able to state compliance with INPAG. This may extend the period in which an NPO is be able to state that it complies with INPAG.

3.6 An expanded form of financial reporting was proposed in Exposure Draft 1 with the inclusion of narrative reporting. A specific matter for comment was raised about the amount of time needed for an NPO to be able to adopt the narrative reporting requirements and whether an transition period was needed. It was recognised for some NPOs there would already be a significant challenge in adopting the requirements for financial statements, and that the broader scope including narrative reporting could be a barrier to adoption.

Question 1: Are there other NPO specific circumstances that should be considered in determining the transition guidance to INPAG?

4. Proposed adaptions to the *IFRS for SMEs* Accounting Standard

4.1 Section 35 of the *IFRS for SMEs* Accounting Standard sets out a number of requirements for entities that are transitioning to this Standard. It also permits a number of pragmatic exceptions.

4.2 Based on the NPO specific issues identified above, pragmatic exceptions could be made with regard to:

- whether comparatives are required
- determining the value of assets and liabilities to be initially recognised
- how existing grants are recognised on the Statement of Financial Position, particularly if they are expected to be completed within a short period of transition (eg 12 months)
- the amount of time permitted to adopt all of the requirements of INPAG and whether there is an approved adoption path as mooted in the application guidance to Section 3 *Financial statements* included in Exposure Draft 1
- exclusion of narrative reporting from the statement of compliance for a 2 year period after the statement of compliance with the financial statements element of INPAG

4.3 For those entities that have not previously prepared financial statements, there is no information lost in allowing comparatives not to be required as this information was not previously available. A pragmatic exception for this information would not diminish the information available and reduce barriers to adoption. However, for those entities that produced financial statements under an international or national GAAP it would be more reasonable to expect comparatives to be produced.

4.4 Section 35 of the *IFRS for SMEs* Accounting Standard (paragraph 35.10) allows the use of fair value and revaluation as deemed cost for property, plant and equipment, investment properties and intangible assets. It also allows event-driven fair value as a deemed cost for assets and liabilities, where they have been previously measured at a point in time. Section 12 *Fair value measurement* includes application guidance with respect to donated in-kind. This guidance could be broadened to all assets on first time adoption to derive deemed cost where assets or liabilities were not previously recorded.

4.5 Determining the brought forward balance on funds without restrictions, will be important as it is this information that is useful to stakeholders in understanding the resilience of an NPO. As noted above pragmatically grant arrangements that have less than 12 months to complete at the date of transition could be excluded as long as they do not impact the closing balance of funds without restrictions. It might also be possible to allow a (short) period for NPOs to amend these balances based on improved information without the need to recognise an error in the financial statements.

4.6 In terms of ability to express compliance with INPAG, a two step approach could be adopted. An NPO could express compliance with the preparation of financial statements as an initial step. Once narrative reporting is completed the NPO could express compliance with all of the INPAG financial reporting requirements. If such an approach was taken then it would need to be clear whether these statements of compliance could be used in perpetuity or whether the ability to express compliance with the preparation of financial statements is time limited, or some variation on this.

4.7 In addition there could be a statement that an NPO has complied with a minimum set of requirements that could be determined. For any position other than full compliance with the financial reporting requirements an NPO would need to set out which aspects of INPAG are yet to be adopted and the timeframe for their adoption.

Question 2: What are TAG member's views on allowing NPOs that have not previously prepared accrual based financial statements to not provide comparatives in year one?

Question 3: What are TAG member's view on pragmatic approaches to producing opening balances where assets and liabilities have not previously been recognised?

Question 4: What are TAG member's views on the recognition of grant arrangement balances for opening balances including funds with restrictions?

Question 5: What are TAG member's views on statements of compliance over an extended transition period?

Question 6: Are there any other pragmatic exceptions or requirements to be considered for the transition guidance?

5. Next steps

5.1 A draft of Section 38 *Transition to INPAG* reflecting feedback from TAG members will be shared at the meeting on 12 December 2023. Annex A includes draft guidance based on Section 35 of the *IFRS for SMEs* Accounting Standard before taking account of any of the points raised above.

September 2023

Annex A

Section 38 - First time adoption of INPAG

G38.1 This section applies to a **first-time adopter of INPAG**, regardless of ~~whether~~ its previous accounting framework whether this was **IFRS** based **accounting standards** or another set of generally accepted accounting principles (GAAP) such as its national accounting standards or another framework such as the local income tax basis.

G38.2 An entity that has applied INPAG in a previous **reporting period**, but whose most recent previous annual **financial statements** did not contain an explicit and unreserved statement of compliance with INPAG, must either apply this section or apply INPAG retrospectively in accordance with Section 10 *Accounting Policies, Estimates and Errors* as if the NPO had never stopped applying INPAG. When such an NPO does not elect to apply this section, it is still required to apply the disclosure requirements in paragraph G38.13 in addition to the disclosure requirements in Section 10.

G38.3 A first-time adopter of the INPAG shall apply this section in its first financial statements that conform to this Guidance.

G38.4 An NPO's first financial statements that conform to this Guidance are the first annual financial statements in which the NPO makes an explicit and unreserved statement in those financial statements of compliance with the INPAG. Financial statements prepared in accordance with this Guidance are an NPO's first such financial statements if, for example, the NPO:

a) did not present financial statements for previous periods;
b) presented its most recent previous financial statements under national requirements that are not consistent with this Guidance in all respects; or
c) presented its most recent previous financial statements in conformity with ~~**full**~~ **IFRS**

Accounting Standards.

G38.5 Paragraph G3.18 defines a complete set of financial statements.

G38.6 Paragraph G3.14 requires an NPO to disclose, in a complete set of financial statements, comparative information in respect of the previous comparable period for all monetary amounts presented in the financial statements, as well as specified comparative narrative and descriptive information. An NPO may present comparative information in respect of more than one comparable prior period. Consequently, an NPO's **date of transition to INPAG** is the beginning of the earliest period for which the NPO presents full comparative information in accordance with this Guidance in its first financial statements that conform to this Guidance.

G38.7 Except as provided in paragraphs G38.9–G38.11, an NPO shall on its date of transition to INPAG (ie the beginning of the earliest period presented):

a) recognise all **assets** and **liabilities** whose **recognition** is required by INPAG;
b) not recognise items as assets or liabilities if this Guidance does not permit such recognition;

c) reclassify items that it recognised under its previous financial reporting framework as one type of asset, liability or component of **equity**, but are a different type of asset, liability or component of equity under this Guidance; and
d) apply this Guidance in measuring all recognised assets and liabilities.

G38.8 The **accounting policies** that an NPO uses on adoption of this Guidance may differ from those that it used for the same date using its previous financial reporting framework. The resulting adjustments arise from transactions, other events or conditions before the date of transition to this Guidance. Consequently, an NPO shall recognise those adjustments directly in funds without restrictions (or, if appropriate, another category of equity) at the date of transition to this Guidance.

G38.9 On first-time adoption of this Guidance, an NPO shall not retrospectively change the accounting that it followed under its previous financial reporting framework for any of the following transactions:

a) **derecognition** of **financial assets** and **financial liabilities**. Financial assets and liabilities derecognised under an NPO's previous accounting framework before the date of transition shall not be recognised upon adoption of INPAG. Conversely, for financial assets and liabilities that would have been derecognised under INPAG in a transaction that took place before the date of transition, but that were not derecognised under an NPO's previous accounting framework, an NPO may choose (a) to derecognise them on adoption of INPAG or (b) to continue to recognise them until disposed of or settled.
b) hedge accounting. An NPO shall not change its hedge accounting before the date of transition to INPAG for hedging relationships that no longer exist at the date of transition. For hedging relationships that exist at the date of transition, the NPO shall follow the hedge accounting requirements of Part II of Section 11 *Other Financial Instrument Issues*, including the requirements for discontinuing hedge accounting for hedging relationships that do not meet the conditions of Part II of Section 11.
c) accounting estimates.
d) **discontinued operations**.
e) measuring **non-controlling interests**. The requirements of paragraph G5.8 to allocate **surplus or deficit** ~~and **total comprehensive income**~~ between non-controlling interest and **owners** of the **parent** shall be applied prospectively from the date of transition to INPAG (or from such earlier date as this Guidance is applied to restate **business combinations**—see paragraph G38.10(a)).
f) government loans. A first-time adopter shall apply the requirements in Section 11 *Financial Instruments* ~~and Section 24 *Government Grants*~~ prospectively to government loans existing at the date of transition to this Guidance. Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan on a basis that is consistent with this Guidance, it shall use its previous GAAP **carrying amount** of the loan at the date of transition to this Guidance as the carrying amount of the loan at that date and shall not recognise the benefit of any government loan at a below-market rate of interest as a **government grant**.
g) completed contracts with customers. An NPO shall not restate contracts that were completed before the date of transition to INPAG. A completed contract is a contract for which the NPO has transferred all of the goods or services identified in accordance with its previous GAAP.

G38.10 An NPO may use one or more of the following exemptions in preparing its first financial statements that conform to this Guidance:

a) business combinations. A first-time adopter may elect not to apply Section 19 *Business combinations and goodwill* to business combinations that were effected before the date of transition to this Guidance. However, if a first-time adopter restates any business combination to comply with Section 19, it shall restate all later business combinations.

~~(b) **share-based payment transactions**. A first-time adopter is not required to apply Section 26 *Share-based Payment* to equity instruments that were granted before the date of transition to this Standard, or to liabilities arising from share-based payment transactions that were settled before the date of transition to this Standard.~~

b) **fair value** as deemed cost. A first-time adopter may elect to measure an item of **property, plant and equipment**, an **investment property** or an **intangible asset** on the date of transition to this Guidance at its fair value and use that fair value as its deemed cost at that date.

c) revaluation as deemed cost. A first-time adopter may elect to use a previous GAAP revaluation of an item of property, plant and equipment, an investment property or an intangible asset at, or before, the date of transition to this Guidance as its deemed cost at the revaluation date.

d) event-driven fair value **measurement** as deemed cost. A first-time adopter may have established a deemed cost in accordance with its previous GAAP for some or all of its assets and liabilities by measuring them at their fair value at one particular date because of an event, for example, a valuation of the business, or parts of the business, for the purposes of a planned sale. If the measurement date:
   i. is at or before the date of transition to this Guidance, the NPO may use such event-driven fair value measurements as deemed cost at the date of that measurement.
   ii. is after the date of transition to this Guidance, but during the periods covered by the first financial statements that conform to this Guidance, the event-driven fair value measurements may be used as deemed cost when the event occurs. An NPO shall recognise the resulting adjustments directly in funds without restrictions (or, if appropriate, another category of equity) at the measurement date. At the date of transition to this Guidance, the NPO shall either establish the deemed cost by applying the criteria in paragraph G38.10(b)–(c) or measure those assets and liabilities in accordance with the other requirements in this section.

e) cumulative translation differences. Section 30 *Foreign currency translation* requires an NPO to classify some translation differences as a separate component of equity. A first-time adopter may elect to deem the cumulative translation differences for all **foreign operations** to be zero at the date of transition to INPAG (ie a 'fresh start').

f) **separate financial statements**. When an NPO prepares separate financial statements, paragraph G9.26 requires it to account for its investments in **controlled entities, associates** and jointly controlled entities either:
   i. at cost less **impairment**;
   ii. at fair value with changes in fair value recognised in surplus or deficit; or
   iii. using the equity method following the procedures in paragraph G14.8.

If a first-time adopter measures such an investment at cost, it shall measure that investment at one of the following amounts at the date of transition:

i. cost determined in accordance with Section 9 *Consolidated and separate financial statements*; or
ii. deemed cost, which shall be either fair value at the date of transition to INPAG or previous GAAP carrying amount on that date.

g) **compound financial instruments**. Paragraph G22.13 requires an NPO to split a compound financial instrument into its liability and equity components at the date of issue. A first-time adopter need not separate those two components if the liability component is not outstanding at the date of transition to this Guidance.

h) deferred income tax. A first-time adopter may apply Section 29 *Income tax* prospectively from the date of transition to INPAG.

i) **service concession arrangements**. A first-time adopter is not required to apply paragraphs G34.12–G34.16 to service concession arrangements entered into before the date of transition to this Guidance.

j) extractive activities. A first-time adopter using full cost accounting under previous GAAP may elect to measure oil and gas assets (those used in the exploration, evaluation, development or production of oil and gas) on the date of transition to INPAG at the amount determined under the NPO's previous GAAP. The NPO shall test those assets for impairment at the date of transition to this Standard in accordance with Section 27 *Impairment of assets*.

k) arrangements containing a **lease**. A first-time adopter may elect to determine whether an arrangement existing at the date of transition to INPAG contains a lease (see paragraph 20.3) on the basis of facts and circumstances existing at that date, instead of when the arrangement was entered into.

l) decommissioning liabilities included in the cost of property, plant and equipment. Paragraph G17.10(c) states that the cost of an item of property, plant and equipment includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an NPO incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce **inventories** during that period. A first-time adopter may elect to measure this component of the cost of an item of property, plant and equipment at the date of transition to INPAG, instead of on the date(s) when the obligation initially arose.

m) operations subject to rate regulation. If a first-time adopter holds items of property, plant and equipment or intangible assets that are used, or were previously used, in operations subject to rate regulation (ie to provide goods or services to customers at prices/rates established by an authorised body) it may elect to use the previous GAAP carrying amount of those items at the date of transition to this Guidance as their deemed cost. If an NPO applies this exemption to an item, it need not apply it to all items. The NPO shall test those assets for impairment at the date of transition to this Guidance in accordance with Section 27.

n) **severe hyperinflation**. If a first-time adopter has a **functional currency** that was subject to severe hyperinflation:

i. if its date of transition to this Guidance is on, or after, the **functional currency normalisation date**, the NPO may elect to measure all assets and liabilities held before the functional currency normalisation date at fair value on the date of transition to this Guidance and use that fair value as the deemed cost of those assets and liabilities at that date; and

ii. if the functional currency normalisation date falls within a twelve month comparative period, an entity may use a comparative period of less than twelve months, provided that a complete set of financial statements (as required by paragraph 3.17) is provided for that shorter period

G38.11 If it is **impracticable** for an NPO to make one or more of the adjustments required by paragraph G38.7 at the date of transition, the entity shall apply paragraphs G38.7–G38.10 for such adjustments in the earliest period for which it is practicable to do so, and shall identify which amounts in the financial statements have not been restated. If it is impracticable for an NPO to provide any of the disclosures required by this Guidance, including those for comparative periods, the omission shall be disclosed.

G38.12 An NPO shall explain how the transition from its previous financial reporting framework to this Guidance affected its reported **financial position**, financial **performance** and **cash flows**.

G38.13 An NPO that has applied INPAG in a previous period, as described in paragraph G38.2, shall disclose:

a) the reason it stopped applying INPAG;
b) the reason it is resuming the application of INPAG; and
c) whether it has applied this section or has applied INPAG retrospectively in accordance with Section 10

G38.14 To comply with paragraph G38.12, an NPO's first financial statements prepared using this Guidance shall include:

a) a description of the nature of each change in accounting policy;
b) reconciliations of its equity determined in accordance with its previous financial reporting framework to its equity determined in accordance with this Guidance for both of the following dates:
   i. the date of transition to this Guidance; and
   ii. the end of the latest period presented in the NPO's most recent annual financial statements determined in accordance with its previous financial reporting framework.
c) a reconciliation of the surplus or deficit determined in accordance with its previous financial reporting framework for the latest period in the NPOs's most recent annual financial statements to its surplus or deficit determined in accordance with this Guidance for the same period.

G38.15 If an NPO becomes aware of **errors** made under its previous financial reporting framework, the reconciliations required by paragraph G38.14(b) and (c) shall, to the extent practicable, distinguish the correction of those errors from changes in accounting policies.

G38.16 If an NPO did not present financial statements for previous periods, it shall disclose that fact in its first financial statements that conform to this Guidance.