



# Technical Advisory Group Issue Paper

AGENDA ITEM: TAGFG01 - 03  
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## Concepts and Pervasive Principles – Response to ED1

Summary	<p>This paper provides TAG members with:</p> <ul style="list-style-type: none"><li>• a summary of the responses to the specific matters for comment (SMCs) for issues relating to section 2 (Concepts and Pervasive Principles) that were included in INPAG Exposure Draft 1,</li><li>• respondents' views on those issues, and</li><li>• suggested approaches for the final guidance.</li></ul> <p>It also summarises the consultation responses on the SMCs relating to net assets/equity and the reporting of funds with and without restrictions which have also been included in ED3.</p>
Purpose/objective of the paper	<p>The purpose of this paper is to provide a detailed analysis of the responses to the SMCs for ED1 on section 2. It seeks the views of TAG members to further develop the final guidance based on the respondents' views and feedback on specific proposals.</p>
Other supporting items	<p>N/A</p>
Prepared by	<p>Sarah Sheen</p>
Actions for this meeting	<p><b>Advise on:</b></p> <ol style="list-style-type: none"><li>i. the primary users of NPO general purpose financial reports and their information needs</li><li>ii. qualitative characteristics of useful financial information</li><li>iii. the concept of service potential</li><li>iv. the specifications for undue cost or effort</li><li>v. the reporting NPO (including branches)</li><li>vi. any initial views on the comments on net assets/equity and reporting on funds with or without restrictions.</li></ol>

# Technical Advisory Group

## Concepts and Pervasive Principles - Response to ED1

### 1. Introduction

- 1.1 This paper:
- provides a summary and high level analysis of the consultation responses to the Specific Matters for Comment (SMC) relating to Section 2 (Concepts and Pervasive Principles) - see Annexes A and B.
  - sets out initial approaches and responses from the Secretariat.
  - seeks TAG members' advice on a number of the issues raised in the feedback.
  - summarises the consultation responses to the SMCs on net assets, the inclusion of equity and the categorisation funds (and the inclusion of equity claims within those funds) in Annex C, which were considered in the development of ED3.

### 2. Background

- 2.1 Section 2 (Concepts and Pervasive Principles) is based on the equivalent section in IFRS for SMEs but with additional interpretation for NPO circumstances, which was informed by the IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* (IPSASB Conceptual Framework). It covers the following topics:
- the objective of non-profit organisations' general purpose financial reports
  - qualitative characteristics of information in general purpose financial reports
  - general purpose financial reports and the reporting NPO
  - the elements of financial statements
  - assets and liabilities
  - recognition and derecognition
  - measurement, and
  - presentation and disclosure.
- 2.2 There were nine SMCs included in the Exposure Draft and Invitation to Comment. The main body of this report and Annexes A and B include analysis of the SMCs on the primary users and the description of their needs, the qualitative characteristics of useful financial information, the use of the term service potential, the specifications for undue cost and effort and the reporting NPO (including branches).
- 2.3 Annex C considers the SMCs on net assets, the inclusion of equity and the categorisation of funds (and the inclusion of equity claims within those funds). TAG will be aware that these were considered in the development of Exposure Draft 3. Annex C contains a snapshot of the outcomes of the feedback and an overview of the consultation responses. The detailed responses will be combined with the responses to the SMC on Exposure Draft 3 and considered with that analysis.

- 2.4 A survey was carried out that addressed some aspects of the proposals in Section 2. These have been incorporated into the analysis of responses where appropriate.

### **3. Primary Users and the Description of their Needs**

*SMC 3(a) Do you agree with the range of primary users and the description of their needs? If not, what would you propose and why?*

- 3.1 Eighty-three percent, (fifty respondents), agreed with the range of primary users and the description of their needs with seven percent, (four respondents), disagreeing and ten percent, (six respondents), indicating that they neither agreed nor disagreed. Nine respondents provided no response to this SMC.
- 3.2 The respondents that agreed with the range of primary users and the description of their needs commented that:
- the user categorisation (resource providers and the public that depend on the goods and services provided) covers a multitude of different stakeholders that are appropriate for general purpose financial reports (GPFs)
  - it is vital and overdue to see that the needs of 'service users', (ie those that benefit from the activities) of the NPO are given prominence as primary users.
- 3.3 One respondent indicated that there might need to be more discussion on the particular needs of NPO users as opposed to commercial users of the financial statements. However, the Secretariat is of the view that this is provided by paragraphs G2.7 to G2.12 of section 2. Further detail could be developed through educational materials.
- 3.4 There are a range of users under the categorisation presented by INPAG, donors probably being one of the most complicated. Depending on the circumstances they may be primary users but when they require special purpose reports they are not. The Secretariat considers that additional clarifications would assist accounts preparers and other stakeholders in the understanding of the requirements and their application.
- 3.5 A respondent indicated that there are different types of donors or providers of grants. Each type of donor considers that the information about what is being done with the resources provided is important. The respondent was of the view that the specifications in ED2 made the role of donors as a user of the financial information less clear. In particular, Section 2 states that a user that has the authority to require an NPO to disclose information is not considered a primary user. This respondent appeared to recognise the different characteristics of donors who, depending on their approach to the provision of resources (ie whether they request special purpose reports) may or may not be primary users.
- 3.6 A respondent agreed that when donors act like any other resource providers they may be primary users. They commented that although donors that have rights to demand information tailored to meet their particular information needs are

excluded from primary users, they should be encouraged to reduce other information requirements.

- 3.7 A respondent raised a concern about board members being excluded as primary users because they have the rights to request information. This respondent was of the opinion that they should be included because they:
- act in a fiduciary capacity
  - are sometimes the only users of the GPFs, and
  - act as representatives of services users.
- They also noted that the ability to request information is only a theoretical possibility.
- 3.8 International financial reporting frameworks specify that those who possess the authority to require an entity to disclose the information they need are not the primary users of GPFs. However, as set out in ED1, when board members are fulfilling oversight functions on behalf of the public and resource providers they might be acting as primary users. This was previously discussed, with the prevailing view that board members would not by default be primary users. As there are no new considerations, the Secretariat does not propose that board members are explicitly included as primary users.
- 3.9 There were various comments relating to internal stakeholders as needing to be included as primary users including:
- members – a respondent was of the view that these stakeholders need to be regarded as primary users, another noted that they should be explicitly mentioned. It is agreed that members might be primary users if they are resource providers or service recipients.
  - execution partners – it is not clear that these would be primary users; this would depend on their exact function and characteristics.
  - those who fulfil oversight functions (see paragraph 3.8) – these have been addressed in Section 2
  - managers acting stewards – it is not clear that these meet the criteria described in Section 2.
- 3.10 Another respondent commented that it is unhelpful to remove any of the existing 'primary users' envisaged by IFRS for SMEs. They recommended that in addition to the public, resource providers, and those that fulfil oversight functions, the Guidance also lists investors, lenders and other creditors. Two respondents discussed other entities requiring information for due diligence purposes such as banks but also donors or funding agencies.
- 3.11 The Secretariat is of the view that INPAG has not removed investors, and particularly lenders and other creditors, from the list. These are resource providers following a similar model to the IPSASB Conceptual Framework. The Secretariat proposes to include additional text in the application guidance to make clear that such organisations are resource providers.

- 3.12 Similar to donors, for bankers and other entities that are using the information for due diligence, these groups would be primary users when the information they require is used to assist decision making about the provision of resources (and where they do not have the authority to request special purpose financial reports). However, where these users are using this information for administrative purposes (and no decisions to provide resources are taken) then they would not be primary users.
- 3.13 A number of respondents suggested that regulators (including governments) should be included as a primary users, with their responses indicating that information in the financial reports are used to review compliance, monitoring and other decision making analysis. However, most regulators and government by their nature are able to require financial reports from NPOs within their jurisdiction and this might be in a specified format. There might be limited cases where they are not able to do this. In these cases they might be considered resource providers or those that fulfil oversight functions and therefore may meet the definition of primary users. As proposed in paragraph 3.11 of this paper, this could be made clear in the Application Guidance. This is similar to the role of regulators included in the IPSASB Conceptual Framework, (paragraph 2.6).
- 3.14 One of the respondents commented that a paragraph similar to paragraph 1.10 in the IASB Conceptual Framework, which discusses wider users such as the regulators and the general public, should be included. The approach taken in INPAG is similar to the approach taken by IPSASB where entities are accountable for their use of resources and to those who depend on them to provide services. Accountability also originates from an NPO's mission or objects, which will be to deliver services or activities on behalf of specific user groups, or to support the public in general. As a consequence, the Secretariat does not concur with this view.
- 3.15 A respondent that neither agreed or disagreed raised concerns that those fulfilling oversight functions on behalf of the public or resource providers are included as primary users. This respondent commented that this stakeholder group has the authority to prescribe information and hence their need is fulfilled more by a special purpose financial report.
- 3.16 INPAG reflects the approach in the IPSASB Conceptual Framework where elected representatives who act in their capacity of representatives of resource providers and service users are deemed to be primary users. However, the Secretariat will amend the wording to be clearer about these potential users in line with the response to paragraph 3.17. This will take account of the drafting suggestion of a respondent who commented "*in some jurisdictions those charged with oversight functions would be in a position to demand reports tailored to meet their particular information needs and therefore may not be primary users of NPO general purpose financial reports. This could be given as an example in Paragraph G2.6...*".
- 3.17 The Secretariat is of the view that it is appropriate that those fulfilling oversight functions are primary users as in many cases while undertaking this function they

will not have the rights to information.. The term 'oversight', appears to have been interpreted as those more with regulatory type monitoring roles. The Secretariat proposes to add the term 'those representing resource providers and the public that depend on the goods and services provided by NPOs' to make the meaning clearer supported by authoritative guidance which follows the approach to this issue in the IPSAB Conceptual Framework.

- 3.18 Two respondents that disagreed commented that the public should not be a primary user. They were of the view that NPOs are accountable only to the resource providers, and not to those benefiting from the activities of the NPO, on the basis that the service recipients do not provide funds. One commented that if the public is considered as a primary user, then customers should also be considered as the primary users of for-profit entities, which is not the case as per the IASB's Conceptual Framework for Financial Reporting (IASB Conceptual Framework).
- 3.19 One respondent fed back that the specifications were more about who primary users were not, rather than who they were. Two respondents produced their own specifications, with one drawing from the Basis for Conclusions to clarify their understanding of the primary users. The Secretariat proposes to augment the guidance by further describing primary users, and by considering whether any further authoritative guidance on the key characteristics of primary users is needed
- 3.20 Two respondents that agreed proposed that the information needs of each user should be specified and cross referenced to the location where such information is provided to be sure that their needs are met. The information needs of users is discussed in Section 2 (see paragraph G2.7 and G2.8). The Secretariat acknowledges that this is a relatively brief description, which could be enhanced by explaining in the Implementation Guidance how such needs could be met. The Secretariat proposes to develop additional guidance

**Question 1: Do TAG members have any comments on the feedback provided by respondents' on SMC 3(a) about the primary users of the financial statements?**

**Question 2: Are TAG members content with the approach to the description of the primary users of the financial statements and particularly:**

**a) donors and funders;**

**b) the public;**

**c) the approach to resource providers; and**

**d) the approach to those that fill oversight roles or representative functions, including board members, regulators and government.**

**Question 3: What are TAG members' views on adding the term 'those that are representatives of resource providers and the public that depend on the goods and services provided by NPOs' , to make these distinct from those fulfilling oversight roles?**



**Question 4: Are TAG members content with the Secretariat's proposals in response to the SMCs comments?**

**4. Qualitative characteristics of information in general purpose financial information**

*SMC 3(b) Do you agree with the qualitative characteristics of useful financial information? If not, what would you change and why?*

- 4.1 Ninety-two percent, (fifty-five), of those that responded to this SMC agreed with the qualitative characteristics of useful financial information presented in ED1. There were no dissenting views. Eight percent, (five), neither agreed nor disagreed. Nine respondents did not answer this question.
- 4.2 Most of the respondents that agreed provided supportive comments about how the qualitative characteristics of useful financial information allowed NPOs to support the objectives of general purpose financial reports providing decision useful information. One respondent was of the view that the approach would support global consistency for financial reporting. Another respondent commented in detail indicating that it would:
- provide coherent orientation of financial information;
  - assist NPOs with decisions about accounting policy choices;
  - help stakeholders understand INPAG prescriptions;
  - allow like transactions to be treated in a similar way;
  - assist users in making decisions about NPOs based on the information; contained in their general-purpose financial reports;
  - simplify requirements if the same characteristics are used for financial and non-financial information.
- 4.3 A respondent that agreed considered that the language was too "long". They suggested drafting changes to reduce the length of the text and to make it is clearer. It should be noted that these paragraphs replicate the draft Third edition of the *IFRS for SMEs Accounting Standard*, which may be amended in response to its own consultation. The Secretariat will consider these suggestions alongside the final text of the Third edition of the *IFRS for SMEs Accounting Standard*.
- 4.4 One respondent that neither agreed nor disagreed commented that the information is useful but the user needs are different to that in IFRS for SMEs because the users are different with different objectives. The major need for most of the NPO users is accountability. Among the fundamental features, the respondent suggested shifting comparability from enhancing to fundamental and add measurability and attribution which in their view are some of the major risks stakeholders face while reading NPO reports.
- 4.5 The Secretariat agrees that there are different objectives for NPO financial reporting in comparison to "for profit" financial reporting and concurs with the importance of accountability, which is already reflected in Section two. While comparability is a useful characteristic, if financial information is either not relevant or faithfully represented (or neither) then being able to provide comparison of like transactions

or over time is not useful. The Secretariat is of the view that measurability and attribution are aspects of faithfully represented and relevant information and therefore not fundamental characteristics.

- 4.6 A respondent recommended that the wording in the authoritative guidance at paragraph G2.20 should be updated to say that the general purpose financial statements should be free of “material” error rather than “complete, neutral and free from error” as currently drafted. Materiality is an aspect of relevance and as noted in Section 2, faithful representation does not mean accurate in all respects. The Secretariat is not recommending that this is changed.
- 4.7 The same respondent commented that in respect of the enhancing characteristics, “completeness is also included”. Being complete is a part of the description of faithful representation and the Secretariat does not support that this is included as a separate characteristic.
- 4.8 Two respondents commented on the headings and sub headings in the Exposure Draft noting that these appeared not to be appropriate levels. The Secretariat agrees and will ensure that appropriate headings and subheadings reflect the characteristics of useful financial information.

**Question 5: Do TAG members have any further comments or suggestions on the SMC responses in relation to the qualitative characteristics of useful financial information?**

**5. The Use of the Term Service Potential**

*SMC 3(g) Do you agree that ‘service potential’ should be introduced into Section 2? If not, why not?*

- 5.1 Eighty percent, (forty-seven), respondents agreed with the proposals in ED1 for the introduction of service potential in Section 2. Twelve percent, (seven respondents), disagreed, and the remaining eight percent of respondents, (five respondents), neither agreed nor disagreed. Ten respondents did not answer this question.
- 5.2 The survey that was issued along with ED1 showed that over 90% (63 respondents) thought that the concept of service potential was either important or very important.
- 5.3 The respondents that agreed with the inclusion of the concept of service potential in Section 2 commented that:
- it reflected NPOs’ role not to generate profit and provide services without a financial return; and
  - it has been recognised by numerous standard setters over many years as the expectation that a resource will be held for its ability to enable the entity to meet its service objectives.



- 5.4 One respondent that agreed with the concept was of the view that the term ‘service potential’, while taken from IPSAS, is not readily understandable. It suggested that alternatives worthy of consideration include ‘mission potential’, ‘social potential’, ‘potential to deliver social good’ or ‘public benefit potential’. A respondent that disagreed suggested the term “capacity potential”.
- 5.5 In line with previous discussions, the Secretariat is of the view that creating a new term for the same concept should not be pursued as it has the potential to confuse stakeholders. This term is used by standard setters and there has been substantial work by IPSASB, which may be useful in the future development of INPAG. See also the advice given by TAG at its September 2022 meeting on the use of service potential discussed at paragraph 5.9 below.
- 5.6 Another respondent was of the view that a more detailed description of service potential be provided similar to IPSAS 2 *Statement of Cash Flows* which contrasts assets used to provide goods and services (which do not directly generate cash inflows) with those which do usually defined as being held for economic benefits. The respondent was of the view that more description about the application of service potential would be needed in Section 17 *Property plant and equipment*. The Secretariat is of the view that the description as drafted follows the approach in the IPSASB Conceptual Framework and is not proposing any changes.
- 5.7 The respondents that disagreed indicated:

<b>Comment</b>	<b>Secretariat response</b>
Service potential may be misleading because some NPOs provided goods.	The description at paragraph G2.54 is clear that service potential includes the provision of goods.
It is subjective and there is no comprehensive approach related to define, measure, recognise and disclose it. (Note that the subjectivity of service potential was noted by a respondent that agreed and a respondent that a neither agreed nor disagreed.)	Service potential is more subjective than economic resources generated by cash inflows (or a reduction in cash outflows) and measurability can be more challenging. IPSASB has recently issued a standard on measurement (IPSAS 46 Measurement) which includes the measurement of the operational capacity of an asset. This work will inform the discussion of measurement in the future development of INPAG.
Some NPOs use their returns to plough these back into NPOs for financial sustainability	The concept of service potential would not prohibit property, plant and equipment assets held for their financial capacity to be measured.

<b>Comment</b>	<b>Secretariat response</b>
It does not reflect the contributions of volunteers.	Any measurement of volunteer contributions is measuring the service potential contributed by the volunteers.

5.8 A respondent that neither agreed nor disagreed with the proposal agreed with the concept of service potential but disagreed with the proposal to define 'service potential' as a distinct concept from 'economic benefit', and that 'economic benefit' is modified to specify that it relates only to cash inflows and outflows. They were of the view that 'economic benefit' encompasses more than just cash flows, and would include service potential.

5.9 The TAG discussed this issue at its meeting in September 2022. TAG members advice at the time was that service potential should be described as a separate concept and developed in due course so that the relationship with the same or similar terms in other GAAPs remain clear. The Secretariat is of the view that nothing has changed since this discussion and does not support making a change.

**Question 6: Do TAG members have any further comments or suggestions on the SMC responses in relation to the concept of service potential?**

**Question 7: Do TAG members agree that "service potential" should continue to be a distinct concept from "economic benefit"?**

## 6. Undue Cost or Effort

*SMC 3(h) Do you agree that the provisions for 'undue cost and effort' used in the IFRS for SMEs Accounting Standard should be retained? If not, why not?*

- 6.1 Seventy-nine percent, (forty-one respondents), agreed *that the provisions for 'undue cost and effort' used in the IFRS for SMEs Accounting Standard should be retained.* Thirteen percent, (seven) respondents disagreed. Eight percent, (four respondents) neither agreed nor disagreed. Seventeen respondents did not provide an answer to this SMC.
- 6.2 The survey which was issued alongside the consultation on ED1 showed that just over 60 percent (of the 64 respondents) thought it should be retained.
- 6.3 Those respondents that agreed with the use of undue cost or effort commented that it:
- should be retained from the *IFRS for SMEs Accounting Standard* but only applied to the NPO's specific circumstances and appropriately disclosed;
  - is intrinsic to the financial reporting process for any entity; and
  - supports minimising the burden associated with financial reporting.

- 6.4 One of the respondents that agreed commented on the difficulties of applying the exemption, while noting its existence in IFRS and IFRS for SMEs. This included that the benefits do not accrue directly to the NPO but are realised by users that use the NPO's financial report. This requires consideration of how the economic and other decisions of those who are expected to use the financial reports might be affected by not having that information. There is a need for careful evaluation and separate assessment at different points in the transaction (for example, initial recognition and subsequent measurement). This respondent called for implementation guidance to be provided, for example, in the form of decision trees or examples of parameters to ensure objectivity.
- 6.5 A respondent that disagreed was concerned about the technical skills required to apply the exemption. Three of the respondents that disagreed suggested instead that simplifications be provided on the areas where the exemption was available. One respondent was of the view that such simplifications would be infrequent. Another noted the difficulties of application of the exemption in UK GAAP (see paragraph 6.6 below).
- 6.6 A respondent who neither agreed nor disagreed commented that where NPOs needed to apply judgement in determining whether an exemption is available in their circumstances, their experience was that this was not always dealt with, with sufficient rigour. This had led to the exemptions being applied inconsistently in similar circumstances with costs implications for the preparation of financial statements. The respondent commented, however, that on the basis that INPAG is using the IFRS for SMEs Accounting Standard as the foundational framework, they did do not think there was an NPO-specific reason to remove them. Another respondent noted that the use of the exemption is a matter of debate amongst standard setters.
- 6.7 A group response that included individuals that disagreed highlighted that those that disagreed were concerned with the exemption being used inappropriately.
- 6.8 There is significant use of judgement in applying the undue cost or effort exemption. However, it is used for in relatively limited circumstances, including where fair value measurement is required under full IFRS. Examples of transactions where this might be applied include the fair value measurement of investment properties or the fair value measurement of investments in associates or jointly controlled entities.
- 6.9 The Secretariat notes that there is substantial support for the retention of the undue cost or effort exemption particularly to reduce the reporting burden for NPOs. It also notes that this needs to be balanced against whether the technical skills and resources required to apply it consistently and correctly does not negate the reduction in the reporting burden.
- 6.10 As its use is permitted only under specified circumstances, this should limit inappropriate use, and as there are no NPO specific reason not to apply them the Secretariat is of the view that they should be retained. The Secretariat will consider

whether further support could be provided through implementation guidance to reduce difficulties or inconsistent approaches.

- 6.11 The simplifications suggested in the feedback may be able to be developed over time. The Secretariat proposes that this is considered in a future version of INPAG.
- 6.12 A further respondent used this SMC to seek views on the status of INPAG ie as to whether it is a guidance or a standalone standard. INPAG has been developed using the international protocols for standard setting that allows it to be considered a standalone standard. However, INPAG is currently proposed to be issued as guidance.

**Question 8: Do TAG Members agree with the approach to the undue cost or effort exemption?**

**Question 9: Do TAG Members consider that there are benefits to considering opportunities for simplification in a subsequent version of INPAG?**

**Question 10: Are TAG Members of the view that further implementation guidance would be beneficial to assist NPOs with the use of the exemption?**

## 7. The Reporting NPO (including branches)

*SMC 3(i) Is the NPO as a reporting entity clear? Does the process for identifying branches in the Application Guidance support the principles? If not, what would be more useful?*

- 7.1 Eighty-eight percent, (fifty-two), respondents agreed that the specifications for a reporting NPO and the process for identifying branches are clear. Three percent, (two respondents), disagreed. Nine percent, (five respondents), neither agreed nor disagreed. Ten respondents did not provide an answer to this SMC.
- 7.2 Respondents that agreed indicated:
- this was a good example of how the structure of INPAG would work;
  - the indicators are useful to assist with the identification of branches.
- 7.3 Although the indicators were deemed to be useful one respondent suggested that it should be supported by a conceptual framework because jurisdictional issues are often decided based on rules. Most of the specifications of the reporting entity included in Section 2 are from the IASB Conceptual Framework.
- 7.4 The respondent that disagreed was of the view that accountability requires that a reporting NPO should always be a legal entity. The Secretariat accepts that in most cases the reporting NPO is likely to be a legal entity. International financial reporting standards and conceptual frameworks consider the substance and not solely the legal form of an arrangement. Although less frequently the case, other organisational structures for the reporting NPO may exist which would meet the accountability needs of primary users.

- 7.5 A number of respondents provided more detailed comments on the guidance on the reporting NPO in section 2 and associated implementation guidance. These detailed comments and the Secretariat's responses are presented in Annex B.
- 7.6 One respondent that neither agreed nor disagreed commented that consolidation is a procedure for the presentation of financial information typical of entities that pursue financial returns. The extension of this to NPOs might lose the essence of an NPO, which can be complex. They were of the view that a combination of, rather than consolidation of financial reports would be an option to address this issue.
- 7.7 This topic has previously been discussed by both the PAG and the TAG. At its June 2022 meeting TAG advised that consolidated information can result in greater transparency that supports accountability even though there may be practical difficulties. It is important to identify the limitation of the flow of funds between entities within a consolidation group to provide useful information. As consolidation is not a priority topic for this version of INPAG it was agreed that this should be revisited in the future development of INPAG.

**Question 11: Do TAG members have any comments on the individual issues suggested by the comments detailed in Annex B?**

May 2024



## Annex A(i) – Summary of Feedback Responses to SMCs

<b>SMC 3(a) Do you agree with the range of primary users and the description of their needs? If not, what would you propose and why?</b>	<b>Response</b>	<b>Number</b>	<b>% of those who responded (58)</b>
	Agree	50	83%
	Disagree	4	7%
	Neither agree nor disagree	6	10%
	No Response	9	-
		69	100%

<b>SMC 3(b) Do you agree with the qualitative characteristics of useful information? If not, what would you change and why?</b>	<b>Response</b>	<b>Number</b>	<b>% of those who responded (60)</b>
	Agree	55	92%
	Disagree	-	-
	Neither agree nor disagree	5	8%
	No Response	9	-
	Totals	69	100%

<b>SMC 3(g) Do you agree that 'service potential' should be introduced into Section 2? If not, why not?</b>	<b>Response</b>	<b>Number</b>	<b>% of those who responded (57)</b>
	Agree	47	80%
	Disagree	7	12%
	Neither agree nor disagree	5	8%
	No Response	10	-
		69	100%





<b>SMC 3(h) Do you agree that the provisions for 'undue cost and effort' used in the IFRS for SMEs Accounting Standard should be retained? If not, why not?</b>	<b>Response</b>	<b>Number</b>	<b>% of those who responded (52)</b>
	Agree	41	79%
	Disagree	7	13%
	Neither agree nor disagree	4	8%
	No Response	17	-
		69	100%

<b>SMC 3(i) Is the NPO as a reporting entity clear? Does the process for identifying branches in the Application Guidance support the principles? If not, what would be more useful?</b>	<b>Response</b>	<b>Number</b>	<b>% of those who responded (57)</b>
	Agree	52	88%
	Disagree	2	3%
	Neither agree nor disagree	5	9%
	No Response	10	-
		69	100%

## Annex B

Detailed comments made in respect of the reporting NPO SMC 3(i) – Reporting NPO (including branches). Comments made in respect of the other Section 2 SMCs have been substantially incorporated into the body of the TAG paper.

Comment	Secretariat response
<b>Reporting NPO</b>	
G2.47 appears to have a word missing?	Agree. <i>The Secretariat proposes to redraft G2.47:</i>  <i>"Determining <del>what</del> the appropriate reporting boundary of a reporting NPO can be complex where the potential reporting NPO is not a legal entity or where it does not include legal entities that are governed by controlling NPO-controlled entity relationships."</i>
The "reporting NPO" should instead be described as the "accounting entity" to make it clearer for NPOs that the issue is accountability rather than just reporting for the sake of reporting.	This term is intended to be similar to IFRS for SMEs and conceptual frameworks' references to the report entity. The Secretariat notes that accountability underlines many of the reporting concepts and reporting requirements of INPAG. <i>The Secretariat is of the view that no change is needed.</i>
Guidance should be developed and included in the Application Guidance to Section 2 on scenarios where a reporting NPO is a parent that controls for-profit entities.	<i>The Secretariat is of the view that specific guidance on this issue is not needed.</i>
The definition of "reporting NPO" in the Glossary of Terms does not envisage a group that includes for-profits. This should be amended to reflect such mixed groups.	Agree that it should be changed.  <i>The Secretariat proposes amend the text as follows:</i>  <i>"A reporting NPO is a single NPO, part of an NPO or a combination of entities that is required, or chooses, to prepare general purpose financial reports. Where more than one entity comprises an NPO this may be all non-profit organisations or a combination of for-profit and non-profit organisations"</i>



<i>Branches</i>	
The phrase “is not required to provide separate general purpose financial reports” being reworded as “is not required either by regulations or internal requirements, to provide separate general purpose financial reports”.	The Secretariat wishes to avoid being too restrictive about the reasons that an NPO might be required to provide separate general purpose financial reports. <i>The Secretariat is of the view that no change is a necessary.</i>
There may be unintended consequences of the proposals. Where there is an incorporated subsidiary who is required to separately produce general purpose financial statements, but meets the other indicators. It is possible that these may be judged to be treated as a branch rather than a subsidiary.	The Secretariat is of the view that an incorporated subsidiary is unlikely to be mistaken as an internal branch as described in INPAG. <i>The Secretariat proposes to consider whether any clarification of the position is needed in the Application Guidance.</i>
Branches need more explanation, clearer instructions and more detailed guidance.	INPAG includes implementation guidance to support branches (and other issues relating to the reporting NPO). <i>The Secretariat’s view is that the current guidance is sufficient.</i>
It would be useful to have real life examples.	Real life examples are often too detailed to be included in implementation guidance and would need to be simplified. Educational materials might be more suitable. <i>The Secretariat will consider whether simplified examples would be useful, or a matter for education materials.</i>
Linked charities - In the UK, there is a concept of linked charities whereby charities who provide different aspects of the same service or have the same trustees are linked for administrative purposes. Under the UK Charities SORP (FRS102), it is allowed for a linked charity which is not incorporated, to be treated as a branch. This is to reduce the administrative burden of preparing separate financial statements. Whilst this is not a specific requirement under FRS102, we welcome the INPAG approach of the list of indicators as it, in most situations, will lead to the same conclusion being reached.	No further comments.
We think the term ‘operational structure’ in paragraph AG2.19, which is not used elsewhere in the Guidance or Application Guidance, may be confusing. We think it could be changed to ‘branch’.	The term “operational structure” is used to help NPOs identify branches where they might not be defined or described as such and where such structures may be misinterpreted as more formal operating arrangements. What is intended by the term ‘operational



	<p>structure' could be included in the glossary. <i>The Secretariat proposes not to make changes to the guidance but to consider the inclusion of this term in the glossary.</i></p>
<p>We do not think it is necessary to imply, as paragraph AG2.19 does, that a branch will be either an internal branch of an NPO or a separate reporting entity. Paragraphs AG2.18 and AG2.21 both indicate that whether or not a branch produces a separate general purpose financial report is not determinative of whether it is an internal branch.</p>	<p>The guidance was developed to identify when operational structures, which might take the form of internal branches exist. This is to avoid them being required to produced general purpose financial reports. However, internal branches are not prohibited from preparing general purpose financial reports. <i>The Secretariat does not propose to make changes for this point.</i></p>



## Annex C Net Assets and Funds

### Annex C(i) Components of net assets

SMC 3(c) Do you agree with the components of net assets? If not, why not.	Response	Number	% of those who responded
	Agree	41	69%
	Disagree	11	18%
	Neither agree nor disagree	9	13%
	No Response	8	-
		69	100%

#### Comments by respondents to question 3(c) – Components of net assets

Respondents that agreed indicated:

- Agreement with the overall definition. This would include the founders' deposits, but also other items such as subsidies and special-purpose donations received as a source of financing of fixed assets and the value of fixed assets acquired gratuitously.
- It seeks to eliminate most of the confusion around assets in terms of NPOs as this is a major issue with NPOs.

A number of issues were raised by the respondents that agreed:

- Whether a reconciliation between the carrying amount at the beginning and the end of the period as proposed under para G6.3 simply alludes to the fulfilment of the concepts discussed in section 2 of the ED.
- Temporarily restricted funds should be considered and included, according to the interpretation of the grant and/or funding agreement, under the criteria of the funding condition.
- The differentiation between funds with and without restrictions need not be presented on the face of primary financial statements.

Respondents that disagreed indicated the following:

- That funds are distinct components within net assets (alongside other components); rather, fund accounting is a separate dimension within the financial statements that



### Comments by respondents to question 3(c) – Components of net assets

all transactions are categorised into. Accordingly, every element of the financial statements, including net assets, can be split by fund.

- The term “Net Assets” does not resonate well for NPOs for describing residual funds. The terms “general fund” or “accumulated funds” resonates well with NPOs, which would ideally comprise residual surplus from un-restricted funds i.e. un-restricted funds that are available for used by the NPO.
- The inclusion of the element of equity within net assets of the NPO where the holders of equity claims have established a financial interest in or entitlement to some of the net assets of the NPO should not exist within an NPO.
- Funds with restrictions are actually owed to the donor, so cannot be considered net assets.

Respondents that neither agreed nor disagreed raised the following issues:

- There are some items that require “a direct posting to the books” in the net assets from the start, and that do not result from a simple liability subtraction from the asset.
- The heading itself was deemed unhelpful, as “Net assets” replace equity in the statement of financial position, since it is not common for investors to take an equity position in an NPO.
- “Net assets” is a net debit.

### Annex C(ii) Inclusion of Equity as an Element

SMC 3(d) Do you agree with the inclusion of equity as an element? If not, what would you propose and why. What type of equity might an NPO have?	Response	Number	% of those who responded
	Agree	34	57%
	Disagree	19	32%
	Neither agree nor disagree	7	11%
	No Response	9	-
		69	100%





### Comments by respondents to question 3(c) – Inclusion of equity as an element

Respondents that agreed raised the following issues:

- “The equity an NPO might have is a contribution from trustees for the initial cost of starting and running the organization, or to bridge a critical funding gap that threatens the going concern of the organization.”
- It needs to be included but commentary is required that equity is not the “norm”.
- Suggestions to describe it as “non-profit equity”.
- Commentary that NPOs “do not die” but their resources are transferred to others – although this is not a direct claim by a third party, it needs to be factored into the definition of an NPO.
- There are NPOs around the world with nominal amounts of equity.
- NPOs have reserves of unrestricted funds.
- Consideration be given as to how such funding is reflected in the financial statements if it is not part of equity, including any relevant disclosures.
- There may be considerations for the exercise of control.
- Suggestions describing it as “Shares of Net Assets”; “social equity” or “social capital” or “net assets”.
- Some charities have a legal structure in the form of a company limited by shares, in which shareholders may be other charities.

Respondents that disagreed provided the following comments:

- The term “equity” will likely be misunderstood and should be avoided.
- Equity may represent the accumulated funds or reserves that have been built up over time through donations, grants, or other sources. This equity can be used to support the organization's mission and programs, or to invest in future initiatives
- It introduces “for profit” descriptions.
- NPOs’ net assets are usually made up of accumulated surpluses, reserves and funds where applicable.
- The word equity does not mean the same thing for an NPO as equity is the residual interest in a “for profit” organization.
- The value of a NPO is far beyond the assets.
- Equity implies interest with a view to a private return and not for public benefit.
- It is important to reflect the source of the surplus or deficit whether it is from normal NPO operations or from the economic entities controlled fully by the NPO.
- Most NPOs are not owned by other entities that have legal entitlement to the net assets.
- Jurisdictional or national standard setters should be allowed to define this.
- Entities should be allowed to add “for profit” line items as necessary.
- Equity should be replaced with capital and revaluation reserves.
- Suggestion that the Guidance:
  - uses the term ‘net assets’ to describe the residual interest in the assets of an entity after deducting all its liabilities, replacing ‘equity’ in the IFRS for SMEs Accounting Standard; and



### Comments by respondents to question 3(c) – Inclusion of equity as an element

- uses the term 'equity' to refer to the net of any contributions from, and distributions to, holders of equity claims, which are a claim on the residual interest in the assets of an entity after deducting all its liabilities.
- Where the respondent had NPO clients with equity, it has been a nominal amount, carrying minimal rights with qualitative disclosure only being made in the general purpose financial statements.
- A view should be presented that the concept of holders of equity claims establishing a financial interest in or entitlement to some of the net assets of the NPO should not exist in an NPO this will have a consequential impact on the definitions of income and expenses.
- Residual funds in case of an NPO belong to the NPO itself and in case of its discontinuation are usually passed on to another NPO having similar objectives.

Respondents that neither agreed nor disagreed raised the following issues:

- The term "equity" is referring to ownership. When NPOs are funded by donors, the money left over at the reporting date belongs to the donors. Fund Balance is more appropriate than the term equity as it doesn't work for all types of NPOs.
- Academic study found equity definitions most useful (for cooperatives) when they were not tied to ownership, but recognised the various ways that equity could be built in for-profit and non-profit cooperatives using a wide variety of instruments.
- NPOs usually do not have shareholders who are concerned with this metric.
- The social capital element exists to record the economic contribution of a third party, either to guarantee their contribution with specific remunerations or for potential service of the NPO.
- Suggestions for the following ie of registering operations derived from the transfer of rights in the cases of:
  - Distributions of economic benefits and liquidation of the NPO, and
  - In the case of sale or transfer of the NPO.
- Suggestion to use capital reserve or contribution that was initially injected to start the NPO.



### Annex C(iii) Categorisation of funds between those with restrictions and those without restrictions

SMC 3(e) Do you agree with the categorisation of funds between those with restrictions and those without restrictions in presenting accumulated surpluses and deficits? If not, what would you propose and why?	Response	Number	% of those who responded
	Agree	61	100%
	Disagree	-	-
	Neither agree nor disagree	-	-
	No Response	8	
		69	100%

#### Comments to SMC 3(e) – Categorisation of funds between those with restrictions and those without restrictions

Respondents that agreed indicated:

- It makes for better reporting and analysis.
- This categorisation is commonly used in non-profit organizations to distinguish between funds that have donor-imposed restrictions on how they can be used and funds that do not have any restrictions.
- It would be useful if the disclosures include the type of restriction.
- Fund accounting is not encouraged in New Zealand but academic studies indicate that it should be. Where they exist it is necessary to identify those with externally-imposed restrictions and those without. This should not include those established for internal governance purposes.
- It maintains an audit trail and transparency.
- It is not mandated in UK GAAP (FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*) but is a requirement of the Charities SORP, as an interpretation of the UK GAAP on Section 5 (Statement of Comprehensive Income and Income Statement) on the basis that it is required under trust law in the UK and is useful information for users of those entities' accounts.
- When relevant, an entity should disaggregate restricted funds between those which are to be spent or applied within a reasonable period from their receipt to further a specific purpose of the NPO.
- INPAG should also require NPOs to disclose accumulated surpluses and deficits for designated funds.
- INPAG should also acknowledge that there may be local legal requirements to provide further breakdowns.



### Comments to SMC 3(e) – Categorisation of funds between those with restrictions and those without restrictions

- A third category of funds could be reported for balance from receipts in exchange for goods or services, whether at fair value or at nominal value.
- Consideration should be given to expanding the AG paragraphs to include clarification on some of the practical challenges associated with distinguishing between funds with restrictions and those without restrictions.
- A clear definition of the words “with restrictions” and “without restrictions” should be provided in the standards as well as in application materials and guidance.
- Consideration should be given to whether including a disclosure note to elaborate on the restricted component would suffice.
- There has to be clarity on the classification on the balance sheet. Ideally restricted funds should sit as either long or short term liabilities.
- This should be disclosed on the face of the statement.

### Annex C(iii) Funds set aside from accumulated surpluses for the holders of equity claims can be part of funds with restrictions and funds without restrictions

SMC 3(f) Do you agree that funds set aside from accumulated surpluses for the holders of equity claims can be part of funds with restrictions and funds without restrictions and that they should be transferred to equity prior to distribution? If not, what would you propose and why?	Response	Number	% of those who responded (55)
	Agree	34	61%
	Disagree	18	32%
	Neither agree nor disagree	4	7%
	No Response	13	-
		69	100%

### Comments on SMC 3(f) - Funds set aside from accumulated surpluses for the holders of equity claims can be part of funds with restrictions and funds without restrictions

Respondents that agreed indicated:

- The transfer of funds set aside from accumulated surpluses for the holders of equity claims prior to distribution is generally required by accounting standards, and the



categorisation of these funds as either restricted or unrestricted depends on the specific terms and conditions of the equity claims

- Funds should be transferred to equity prior to distribution as it's for the public benefit.
- It is the correct technical procedure to ensure that equity is not understated after distribution
- AG 2.8, should be modified. Distributions to equity holders are an outflow of NPO resources, distributed to outside parties that return or reduce a financial interest in the NPO's net assets.
- Materiality and scalability should be taken into account when it comes to smallest NPOs as cost/benefit issues.
- Some grant agreements restrict NPOs to recognise unrestricted funds as a liability until the fund are utilised. At the end of the reporting period, any excess of income over expenses from such projects are classified as liabilities rather than a restricted fund balance. The classification in the exposure draft may not address such variations in grant modality.
- It would be much clearer to bring all the fund accounting issues together in one place.

Respondents that disagreed indicated the following:

- Disagreement that INPAG should include equity claims, because equity claims are one of the main characteristics of profit organisations.
- If there is reasonable assurance that these funds set aside will be transferred to a third party, it should be reflected as restricted funds.
- Where such restricted funds are held over period end, they should be held separately in equity/net assets, rather than as a liability.
- Restricted funds should not be comingled with any other funds. However, the surpluses accumulated from non-restricted funds can be appropriated to equity if the holders of that equity call for a refund.
- Transactions with holders of equity claims occur outside the fund accounting concept. It would not be necessary to transfer accumulated surpluses from 'funds' to 'equity' (as defined in INPAG) prior to distribution because the transaction would take place directly from 'retained earnings'/'accumulated surplus', similar to a dividend paid out by a commercial company limited by shares.
- If INPAG is attempting to be inclusive of for profit transactions then "we can stick with IFRS for SMEs". If the NPO performs for profit transactions for sustainability it has to be accounted for under IFRS/IFRS for SMEs then consolidated to the NPO as required by INPAG.
- There should not be any distribution of those surpluses. Accumulated surpluses should also be used for the purpose of the NPO's mission.
- Funds should remain separate in the current year until the providers of funds authorise both the transfer and distribution.
- Due to the specificities of NPOs that the funds from equity be classified aside from funds with restrictions and funds without restrictions.



- References to “distributions to holders of equity claims” in the ED appear to conflict with the description of a NPO set out in paragraph G1.4, which states that “organisations that do have a primary objective of distributing surpluses for private benefit to groups and individuals, such as investors and holders of equity claims, are likely to be for-profit organisations”. Such references need to consistently make it clear that an NPO is not able to have a primary objective of distributing surpluses to holders of equity claims while still addressing circumstances where, for example, a subsidiary NPO may make a distribution to a parent NPO.

Respondents that neither agreed nor disagreed raised the following issues:

- The equity concept should be eliminated if possible and the other approaches of dealing with equity explored. However, if it’s inevitable, then funds set aside from accumulated surpluses for the holders of equity claims should be part of non-current liabilities.
- This is an infrequent occurrence, so not a material issue for NPOs.
- NPO funds transferred to capital or estate must not be distributed or returned to whoever donated them. The patrimony of an NPO must only be distributed in case of cessation of activities or liquidation and the remaining assets and liabilities.
- A disclosure note providing details on the restricted component would suffice as an alternative to reduce reporting burden while enhancing transparency.
- Any distribution to equity holders is subject to an overarching restriction that it must be used to further the NPO's objects, which requires direct surpluses to benefit the public.