THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
(Set up by an Act of Parliament)

April 15, 2023

Ms. Samantha Musoke
Project Director, IFR4NPO

Dear Madam,

Sub: Comments of the Institute of Chartered Accountants of India (ICAI) on the Exposure Draft *International Non-Profit Accounting Guidance (INPAG)- Part 1*

The Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) acknowledges the opportunity to comment on the Exposure Draft *International Non-Profit Accounting Guidance (INPAG)- Part 1* issued by Chartered Institute of Public Finance and Accountancy (CIPFA) and Humentum.

We may mention that in order to formulate comments on the aforesaid Exposure draft, following activities were undertaken by the ASB of ICAI:

- Exposure Draft hosted on ICAI website inviting comments from Indian stakeholders.
- Constituted and conducted meetings of the Study Group to consider the proposals given in the Exposure Draft and formulated views.
- ASB members were also consulted while finalising the comments on the Exposure Draft

On the basis of above, we have formulated the comments on the specific questions asked in the Exposure Draft which are provided in **Annexure 'A'**.

Yours sincerely,

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Chairman,
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Annexure A

Question 1: General comments
a) Is the structure of INPAG helpful? If not, how could it be improved? b) Do you have any other comments (including regulatory, assurance or cost/ benefit) relating to this INPAG Exposure Draft? If so, explain the rationale for any points you wish to make.

Response: a) The structure of INPAG is helpful.

b) **<u>Other Comments</u>**

Foundational Framework for Exposure Draft of INPAG Part-1

Exposure Draft of INPAG Part-1 (ED) states that the foundational framework of INPAG is the IFRS for SMEs Accounting Standard and all the references to the IFRS for SMEs Accounting Standard in this ED are to the Third edition of the IFRS for SMEs Accounting Standard exposed in September 2022 unless otherwise stated.

In this regard, we are of the view that since the third edition of the IFRS for SMEs Accounting Standard is an attempt to move closer to IFRS, **some of the provisions** of the third edition of the IFRS for SMEs Accounting Standard may be onerous and complex for NPOs. Since the IFRS for SMEs Accounting Standard is applicable to for-profit organisations, it may be appropriate to make suitable simplifications from the perspective of NPOs in the forthcoming Exposure Drafts which would prescribe the accounting of various transactions (Part 2 & Part 3) and the final INPAG. Refer responses to Questions 3(c) & (d), Question 5 and Question 12 for the simplifications sought in the ED Part 1. Further, since smaller NPOs are large in number, additional exemptions and relaxations as may be considered appropriate may be provided to them.

Question 2: Description of NPOs and users of INPAG
a) Do you agree with the description of the broad characteristics of NPOs? Does the term 'providing a benefit to the public' include all entities that might be NPOs? If not, what would you propose and why? b) Does Section 1, together with the Preface, provide clear guidance on which NPOs are intended to benefit from the use of INPAG? If not, what would be more useful?

Response: a) **<u>Description of NPOs</u>**

1. *Interpretation of the term 'public'*

   The term 'public' has been used at many places but the same has not been defined in the ED. While what constitutes 'public' becomes clear on reading of other part of ED, such as, Basis for Conclusions and Implementation Guidance to some extent, it is suggested to define the term 'public' or provide characteristics thereof and provide clarity on the same at one place in the ED because of the following reasons:

- The concept of public is fundamental in determining whether the primary objective of providing benefit to the public is met for an entity to be an NPO.
- Clearly defining the term would not leave any scope for varied interpretations.
- NPOs may not have the sufficient skill-set to interpret the meaning of term from different paragraphs of the guidance.

2. *Paragraphs G1.2, 1.3 and G1.4*

We are of the view that considering the nature of NPOs, there cannot be any 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. Therefore, all the surpluses are utilised for the benefit of the public in NPOs and no surplus can be distributed for private benefit to groups and individuals, such as investors and holders of equity claims.

However, from the reading of paragraph G1.2 and G1.4, it can be mis-interpreted that NPOs can distribute some portion of surpluses for private benefit to groups and individuals, such as investors and holders of equity claims. Therefore, the second point of paragraph G1.2 may be redrafted as follows:

- They direct **<u>all</u>** the surpluses for the benefit of the public.

As a result, paragraph G1.4 may also be redrafted as follows:

"……………..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 private sector organisations….."

b) We are of the view that Section 1, together with the Preface, provide clear guidance on which NPOs are intended to benefit from the use of INPAG subject to our above comments.

Question 3: Concepts and pervasive principles

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) Do you agree with the qualitative characteristics of useful information? If not, what would you change and why?

c) Do you agree with the components of net assets? If not, why not?

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?

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?

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?

g) Do you agree that 'service potential' should be introduced into Section 2? If not, why not?

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?

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?

Response: a) While we agree that the NPOs are accountable to the resource providers and to those fulfilling oversight functions on their behalf, however, NPOs cannot be held accountable to the public that depend on the goods and/or services provided by an NPO, i.e., recipients of the goods and services. Considering the nature of NPOs, since they are responsible for the stewardship of resources entrusted to them, they are accountable only to the resource providers and not the general public being benefitted from the activities of the NPO. Moreover, if the public is considered as a primary user, then customers should also be considered as the primary users in case of for-profit entities which is not the case as per the IASB's Conceptual Framework. Therefore, we are of the view that the public that depend on the goods and/or services provided by NPOs should not be considered as a primary user.

Apart from the above, it is suggested that for providing better clarity, a paragraph similar to following paragraph 1.10 of the IASB's Conceptual Framework, with suitable changes, if required, may be considered for inclusion in Section 2:

'*Other parties, such as regulators and members of the public other than investors, lenders and other creditors, may also find general purpose financial reports useful. However, those reports are not primarily directed to these other groups'.*

b) We agree with the qualitative characteristics of useful information.

c) & d) We do not agree with the inclusion of 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. The organisations which have the objective of distributing surplus for private benefits to groups and individuals, such as investors and holders of equity claims are likely to be for-profit private sector organisations and not NPOs. Therefore, we are of the view that the situation where holders of equity claims establish a financial interest in or entitlement to some of the net assets of the NPO should not exist in an NPO, i.e., even if it exists partially, such an entity should adopt IFRS/IFRS for SME standards.

As a result of this view, many consequential amendments would arise. For example, ‘Expense’ has been defined in the ED as decreases in assets or increases in liabilities that result in decreases in net assets, **other than those relating to distributions to holders of equity claims**. In line with the above comment, the definition of expense may be changed to decreases in assets or increases in liabilities that result in decreases in NPO Funds. The definition of income may also be considered for suitable amendments.

We are also of the view that the residual funds (difference between assets and liabilities) in case of an NPO do not belong to any holder of equity claims and are not held for distribution for private benefits. 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. Accordingly it is suggested to rename the net assets as ‘NPO’s funds’.

e) We agree with the proposal of categorisation of funds between those with restrictions and those without restrictions in presenting accumulated surpluses and deficits.

f) In line with the response to question c) and d) above, the question does not arise.

g) We agree with the introduction of ’service potential’ in Section 2 of the ED.

h) We agree that the provisions of ‘undue cost and effort’ should be retained as used in the IFRS for SMEs Accounting Standard.

i) We agree with the principles of reporting entity as contained in Section 2 of the ED as well as the process for identifying branches contained in the Application Guidance of Section 2.

Question 4: Principles to enable comparability of financial statements

a) Do you agree with the proposed changes to terminology from the *IFRS for SMEs* Accounting Standard? If not, what would you propose and why?

b) Do you agree that comparatives should be shown on the face of the primary statements? In particular, do you agree with the proposed comparatives for the Statement of Income and Expenses? If not, what do you propose and why?

c) Do the proposals for expressing compliance with INPAG create unintended consequences? If so, what are your key concerns?

Response: a) We agree with the proposed changes to terminology from the *IFRS for SMEs* Accounting Standard except for the usage of the term ‘beneficial interest’. While the term includes both financial and non-financial interest, in case of NPOs, a return from an interest in another entity is not necessarily a matter of obtaining funds or a financial return from the entity. Rather, the return can be a non-financial benefit that the controlling NPO derives from the activities of the entity. These non-financial benefits would exist where they lead to the direct or partial fulfilment of one or more of the purposes of the controlling NPO. Since in case of

NPOs, the focus is on the non-financial benefits, we may suggest that the term ‘interest in other entities’ may be used in place of ‘beneficial interest’.

b) We agree that comparatives should be shown on the face of the primary statements. We are of the view that for the Statement of Income and Expenses also, comparatives with bifurcation of income and expenses with and without restrictions should be shown on the face of the Statement which will enable users’ understanding of financial performance for the preceding reporting period.

c) As stated in our response to question a) above, the use of the term ‘beneficial interest’ would cause an unintended consequence as the term beneficial interest may have a different connotation and may not be used in case of NPOs.

Question 5: Scope and presentation of the Statement of Financial Position

a) Do you agree that all asset and liability balances should be split between current and non-current amounts (except where a liquidity-based presentation has been adopted)? If not, why not?

b) Do you agree with the proposal that not all categories of asset and liability balances should be split between those with and those without restrictions? If not, which categories of asset and/or liability should be split?

Response: While we agree with the presentation of the asset and liability balances as split between current and non-current amounts and the guidance given in Section 5 on the scope and presentation of the Statement of Financial Position, we have following concerns:

1. Considering the nature of NPOs and its resources, unnecessary complexities may be avoided and criteria for classification of an asset or liability as current/non-current should be made simple. In this regard, it was felt that determination of normal operating cycle may be challenging for NPOs and criteria of realisation of an asset or settlement of a liability within 12 months after the reporting date is easier for the NPOs to apply. Therefore, it is suggested that the first criteria for classification of an asset or liability as current given in paragraph G4.5(a) and G4.7(a) respectively, viz., it expects to realise the asset (or settle the liability), or intends to sell or consume it in the NPOs normal operating cycle, may be deleted.

   As a result, paragraph and G4.9 may be deleted and paragraph G4.6 may be amended as follows:

   G4.6 An NPO shall classify all other assets as non-current. ~~When the NPO’s normal operating cycle is not clearly identifiable, its duration is assumed to be twelve months.~~

2. The second criteria for classification of an asset or liability as current given in paragraph G4.5(b) and G4.7(b) respectively, is that an NPO holds the asset (or liability) primarily for the purpose of its operating activities, may also be deleted. Assets/liabilities other than current assets/liabilities may also get covered under this criterion since they may also be held for the purpose of operating activities, such as, property, plant and equipment. Therefore, this criterion is not specific to current asset or liability and may be deleted.

Question 6: Scope and presentation of the Statement of Income and Expenses

a) Do you agree with the name of the primary statement being 'Statement of Income and Expenses'? If not, why not?

b) Do you agree that the terms surplus and deficit should be used instead of profit or loss? If not, why not?

c) Do you agree that amounts on each line of revenue and expenses should be split between those with and those without restrictions on the face of the primary statement? If not, what alternative approach would you propose and why?

d) Do you agree that NPOs should be able to choose whether to present either income items or expense items first to get to a surplus or deficit? If not, what alternative approach would you propose and why?

Response: (a), (b) and (c)- We agree with the proposals.

d) We are of the view that income items should be presented first in the Statement of Income and Expenses to get a surplus or deficit because this will give a better readability of the Statement of Income and Expenses and it is quite important to ensure uniformity of presentation.

<u>Other Comments on Presentation of the Statement of Income and Expenses:</u>

1. Paragraph G5.7 is the main paragraph prescribing the line items to be included in the Statement of Income and Expenses for the period. Therefore, this paragraph should be given first as an opening paragraph.

   Further, paragraph G5.5 of Section 5 states that an NPO shall present its unrealised gains or losses from fair value adjustments as part of the surplus or deficit, except where these gains or losses are recognised in the Statement of Changes in Net Assets. The paragraph prescribes three items of unrealised gains and losses from fair value adjustment to be presented after surplus or deficit from operating activities in arriving at the total surplus or deficit of the NPO. However, the unrealized gains and losses apart from fair value adjustments are not prescribed in the paragraph, for example unrealized gains and losses from foreign exchange differences. Further, items other than unrealised gains and losses which are to be presented after surplus and deficit from operating activities, such as, share of surplus of associates, are also not covered in this paragraph. Therefore, it is suggested that the list should be exhaustive that needs to be shown after surplus and deficit from operating activities.

   Paragraph G5.6 prescribing four types of unrealised gains or losses to be recognised as part of Statement of Changes in Net Assets outside of surplus or deficit when prescribed by the ED may be given as an exception to the paragraph in the form of an exhaustive list.

2. In the illustrative format of the Statement of Income and Expenses also, items presented after the surplus or deficit from operating activities, are different from those prescribed in paragraph G5.5 and G5.7. For example,
   a) unrealised gains or losses on foreign exchange differences are covered in the format and not in the main guidance
   b) share of surplus of joint ventures are not given in the format but given in the main guidance

Therefore, it is suggested that consistency should be there in the illustrative formats and guidance given in the main section.
We also suggest that the final guidance that may be issued should be reviewed to ensure consistency in other aspects as well throughout the document.

3. Difference between paragraph G5.7(c) and G5.7(h) may be clarified.

Question 7: Scope and presentation of the Statement of Changes in Net Assets

a) Do you agree with the proposal that there is no Other Comprehensive Income (OCI), and that an expanded Statement of Changes in Net Assets would allow an equivalent to the OCI being produced. If not, why not?

b) Do you agree that funds are split between those with and those without restrictions on the face of the primary statement? If not, what alternative approach would you propose and why?

Response: a) We agree with the proposal that other comprehensive income is not required for NPOs and that the expansion of Statement of Changes in Net Assets may replace and would allow an equivalent to the OCI being produced.

However, it is suggested that there should be consistency within the document in this regard. For example, ED defines the term ‘Income Statement’ in the glossary as a financial statement that presents all items of income and expense recognised in a reporting period, excluding the items of other comprehensive income. As inclusion of concept of other comprehensive income is not proposed in case of NPOs, the definition may be suitably amended.

b) We agree that the funds should be split between those with and those without restrictions on the face of the Statement of Changes in Net assets.

Question 8: Scope and presentation of the Statement of Cash Flows

a) Do you agree with the separate presentation of cash donations and grants on the face of the statement? If not, what alternative approach would you propose and why?

b) Do you agree that donations or grants received for the purchase or creation of property, plant and equipment should be treated as investing activities? If not, what alternative would you propose and why?

c) Do you agree that both the direct method and indirect methods for the cash flow statement should be permitted? If not, why not?

Response: a), b) and c)- We agree with the proposals.

Question 9: Principles underpinning the notes to the financial statements

a) Do you agree that there are no NPO specific considerations for this Section? If not, what changes would you propose and why?

Response: We agree with the proposals.

Question 10: Approach to consolidated and separate financial statements

a) Is the Application Guidance to apply the control principles sufficient? If not, what changes or additions would you propose and why?

b) Do you agree that a rebuttable presumption relating to control should be retained? Is the current drafting sufficient? If not, what would you propose and why?

c) Is the Application Guidance sufficient to apply the fundamental characteristics of faithful representation and relevance to consolidation? If not, what additions would you propose and why?

d) Do you agree with the use of the terms 'controlling NPO', 'controlled entity' and 'beneficial interest' instead of 'parent', 'subsidiary' and 'investment'? If not, what would you propose and why?

Response: While we agree that consolidation by an NPO is relevant and required because NPOs may have SPVs operating in several jurisdictions for accomplishment of NPO's objectives, we have broader concerns on the consolidation of for-profit entities by NPOs. The objectives, users and financial reporting framework of for-profit entity are completely different from the objectives, users and financial reporting framework of an NPO. Therefore, significant amount of presentation differences will be there when the financial statements with two different financial reporting frameworks will be consolidated. Consolidated financial statements prepared by an NPO involving group entities with different objectives and financial reporting framework may not provide useful and faithful information to the users. For example, when the financial statements of the controlling NPO and its controlled for-profit entities are combined line by line by adding together like items of assets, liabilities, equity, income and expenses, majority of the funds of the for-profit entity will be recognized in the funds without restrictions of an NPO. Therefore, the funds without restrictions of the consolidated financial statements of NPOs will include the funds arising on consolidation of a for-profit entity which may not reflect a true and fair picture to the users. Therefore, we suggest that more research may be done on the relevance of consolidation of for-profit entities (following IFRS/IFRS for SME) by an NPO.

The questions raised are on the mechanics of consolidation, the responses to which may be given once the overall purpose of consolidated financial statements comprising the entities applying two different financial reporting frameworks is clarified.

Question 11: Approach to accounting policies, construction of estimates and accounting for errors

a) Do you agree with the updates to Section 10 and that there are no additional NPO specific considerations that need to be addressed in this Section? If not, what changes or additions would you propose and why?

Response: a) We agree with the updates to Section 10 and that there are no additional NPO specific considerations that need to be addressed in this Section. However, with respect to the alternative authoritative sources given in paragraph G10.6, we suggest that guidance may be provided with regard to exchange and non-exchange transactions in line with IPSAS 9, *Revenue from Exchange Transactions* and IPSAS 23, *Revenue from Non-Exchange Transactions (Taxes and Transfers)* respectively. Providing guidance will bring more clarity in transactions of mixed nature, such as, concessionary leases.

Question 12: Scope and content of narrative reporting

a) Do you agree with the principles proposed to underpin narrative reporting? If not, what would you propose to change and why?

b) Do you agree with the scope of the minimum mandatory requirement, with additional information, such as sustainability reporting to be optional? If not, what changes should be made and why?

c) Do you agree with the proposals that sensitive information can be excluded from narrative reports? If not, what alternative would you propose and why?

d) Should a two-year transition period for narrative reporting be permitted to assist in overcoming any implementation challenges? If not, what alternative would you propose and why?

Response: a), b), c) & d)- We agree with the proposals on narrative reporting.