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Dear Karen and team

Submission on INPAG Part 2 Exposure Draft

International Non-Profit Accounting Guidance (INPAG)

Thank you for the opportunity to make a submission on the above Exposure Draft (ED). As a member of the IFR4NPO's Practitioner Advisory Group (PAG), and of the research team that undertook in the CCAB Commissioned research in 2013/14 (Crawford et al., 2014) referred to in the ED, I am very supportive of the IFR4NPO project.

The INPAG work will importantly introduce a set of internationally-acceptable and legitimate standards for a broad range of non-profit organisations (NPOs) including those that some define as social enterprises, and other social-purpose entities that do not fit a for-profit or public sector reporting model. I appreciate the work that has gone into this Part 2 ED on INPAG as the suite begins to take shape. This ED deals with significant issues, in particular the rights and obligations involved in grant arrangements and the revenue and expenditure issues arising from this resourcing.

Although as a member of the PAG I have provided input at various stages of this project, my responses below are made in my personal capacity. They cannot be seen to reflect the views of the New Zealand Accounting Standards Board of which I am Chair, nor of Victoria University of Wellington. I trust the answers to the questions in the ED provided in the following pages are helpful in moving INPAG forward to completion.

Yours sincerely,

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Question 1: Financial instruments

- a) Do you agree that there are no significant alignment changes required to Section 11, other than those that have already been made? If not, set out the alignment changes you believe are required.

- a) The alignment changes appear to be suitable. Notwithstanding the difficulty in determining interest rates (especially when recognising financial liabilities) the use of the effective interest rate appears to be a pragmatic solution in the absence of a specified interest rate.

However, this section raises two questions:

- a. Issued financial guarantee contracts (G11.7(e)) are dealt with in subsequent measurement (at G11.17(d)) but G11.7(e) is not specifically referred to in the main paragraphs. I would have expected it to be included in the discussions in G11.9-16.
- b. It would be helpful if G11.4(d) noted that such loans could be concessionary. Such concessionary loans are not uncommon in the NPO sector. Therefore, NPOs should be encouraged to reflect on whether they have these items or not, as is apparent from the text in G11.6. However, a NPO must read to the detail in G11.16 before being alerted to that fact.

Question 2: Inventories

- a) Do you agree with the expansion of Section 13 Inventories to specifically include inventory held for use internally, for fundraising or distribution? If not, why not?
- b) Do you agree with the permitted exceptions that allow for certain donated inventories and work in-progress that comprises services to be provided for no or nominal consideration to not be recognised as inventory? If not, what would you propose instead?
- c) Do you agree that fair value should be used to value donated inventory? If not, what would you propose instead?
- d) Do you agree that inventories that are held for distribution at no or nominal consideration or for use by the NPO in meeting its objectives shall be measured at the lower of cost adjusted for any loss of service potential, and replacement cost? If not, what would you propose instead?
- e) Do you agree with the proposed disclosure requirements, particularly regarding the use of permitted exceptions and where donated inventories are not recognised because they cannot be reliably measured? If not, what would you propose instead?

- a) Yes.
- b) Without the fair value hierarchy in Section 12, any comments are conditional on INPAG ED 3 and the shape of the eventual guidance. Nevertheless, the proposals in G13.5(a)-(d) combined with the proposal to describe inventories not recognised in G13.26(e) provides for inventory disclosures even when the costs of valuing short-term/low value assets outweigh the benefits to users of that valuation.
- c) This is difficult to answer without the guidance on fair value, nevertheless it is a good place to start.
- d) Yes.

- e) Yes (see also my response to (b)).

Question 3: Provisions and contingencies

a) Do you agree that an illustrative example on warranties is removed from the Implementation Guidance, and a new example on onerous contracts is added? If not, why not?

- a) Yes. The provision of numerous illustrative examples can be overwhelming. Therefore, it is sensible to provide examples that illustrate difficult areas and onerous contracts is one.

Question 4: Revenue

- a) Section 23 Part I and Section 24 Part 1 introduce new terminology relating to grant arrangements. Do you agree with the terms enforceable grant arrangement and enforceable grant obligations and their definitions? If not, what alternative terms would you propose to achieve the same meaning? What are the practical or other considerations arising from these definitions, if any
- b) Do you agree with the structure of Section 23, with Part I focused on grants and donations, Part II focused on contracts with customers and a preface that brings together the key principles and information about how to navigate the guidance? If not, what changes would you make and why?
- c) Do you agree that revenue is only deferred where the grant recipient has a present obligation in relation to the revenue received? If not, in what other circumstances could revenue be deferred and what is the conceptual basis for this proposal?
- d) The revenue recognition model for enforceable grant arrangements requires that revenue is allocated where there is more than one enforceable grant obligation. Do you agree with the allocation methods identified? If not, what methods would you propose? What are the practical considerations?
- e) Do you agree with the permitted exceptions that allow the recognition of some gifts in-kind, either when sold, used or distributed, and that these permitted exceptions cannot be used where donations are received as part of an enforceable grant arrangement? If not, what would you propose instead and what is the rationale?
- f) Do you agree that services in-kind are not required to be recognised unless they are mission critical? If not, on what basis should services in-kind be recognised and what is the rationale?
- g) Do you agree that donations in-kind (both gifts in-kind and services in-kind) should be measured at fair value? If not, what would you propose instead?
- h) Do you agree that administrative tasks are generally not separate individually enforceable obligations, but a means to identify or report on resources in an enforceable grant arrangement? If not, provide examples of where administrative tasks are an enforceable obligation.
- i) Do the proposals for disclosure of grant revenue provide an appropriate level of transparency? If not, what would you propose and what is the rationale for your proposal?
- j) Part I is written for simpler grant arrangements and Part II includes a paragraph for simpler contracts with customers. For more complex grant arrangements, additional guidance is provided about how to apply Part II in the NPO context. Do these proposals successfully remove duplication, help understandability and the ability to implement? If not, what would you change and why?
- k) Do you have any other comments on the proposals in Section 23, including whether the full content of the IFRS for SMEs section on revenue from contracts with customers in Part II is necessary for NPOs? If so, provide the rationale for the comment and cross reference to the relevant paragraphs.

- a) Yes. The notions of EGAs (with EGOs) and OGAs are useful to analyse the difference between revenue from contracts with customers and longer-term EGOs. These types of transactions have been a source of contention, especially where NPOs seek to use grant funding over more than one financial year (and that is the grantor's intention), but have been unable to show this longer-term use in their accounting.
- b) Yes. There is clear guidance at the beginning of the section (and Figure 23.1) to enable users of INPAG to navigate the different arrangements discussed.
- c) Yes. Identifying the presence of promises (or not) in a contract enable the grantor and grantee to operate under a common understanding which supports more effective grant-making and service provision.
- d) Yes. This proposal may also encourage an NPO to utilise appropriate accounting systems and controls to ensure that the resources allocated to satisfying a grant are align with the expectations and value of the grant received.
- e) Yes. This is a practical expedient.
- f) Yes. This is useful for comparability purposes. Nevertheless, such a requirement would not stop an NPO from voluntarily reporting donated services-in-kind either in its primary financial statements (following G23.40) or in other communications.
- g) Without the fair value hierarchy in Section 12, any comment on this must be conditional on INPAG ED 3 and the eventual guidance. Nevertheless, the proposals on in-kind donations appear sensible.
- h) No. Para G23.49 may not be required as the practice to provide reporting or not during a EGA is likely to be context-specific. Therefore it may be related to satisfying an EGO and trigger sanctions – or it may be merely a report with no following actions. The proposals may proscribe practice unnecessarily.
- i) It would be important for materiality to guide an NPO's disclosures of revenue received from grants, as with all disclosures.
- j) Part II manages to take NPOs through various different scenarios and should provide guidance to a preparer to successfully navigate how to disclose revenue arising from different arrangements.
- k) I note that many preparers using the equivalent of IFRS 15 Revenue with Customers struggle with identifying whether they are principal or agent in complex arrangements. The BCs provide notes of the attempt to ensure sufficient advice was given to preparers to assess control and whether the NPO is a principal or agent in a transaction. It is important to ensure G23.16-G23.17 is sufficient.
Further the guidance at G23.35-40 on donations-in-kind are likely to increase transparency and comparability.

Question 5: Expenses on grants and donations

- a) Section 24 Part I and Section 23 Part 1 introduce new terminology relating to grant arrangements. Do you agree with the terms enforceable grant arrangement and enforceable grant obligations and their definitions? If not, what alternative terms would you propose to achieve the same meaning? What are the practical or other considerations arising from these definitions, if any?
- b) Do you agree that all expenses on grants and donations can be classified as an enforceable grant arrangement or as an other funding arrangement? If not, provide examples of which expenses on grants or donations would not fit in either of these classes, and why not?
- c) Enforceable grant arrangements are required to be enforceable through legal or equivalent means. Do you agree that regulatory oversight and customary practices can be sufficient to create an enforceable grant arrangement? If not, why not? What weight should be applied to these mechanisms?
- d) Do you agree that the full amount of the grant (including where it covers multiple years) should be recognised as an expense if the grant-provider has no realistic means to avoid the expense? If not, under what circumstances should a grant-provider not recognise the full expense and what is the rationale?
- e) Do you agree that grants for capital purposes are expensed by the grantor using the same principles as other grants? If not, why not? What would you propose instead?
- f) Do the proposals for disclosure of grant expenses, which include a sensitive information exemption, provide an appropriate level of transparency? If not, what would you propose and what is the rationale for your proposal?
- g) Do you agree that a grant-providing NPO with an OFA can only recognise an asset at the point that a grant recipient has not complied with a constraint on the use of funds provided? If not, what would you propose instead?
- h) Do you have any other comments on the proposals in Section 24, including that administrative tasks in an enforceable grant arrangement are generally not an enforceable grant obligation but a means to identify or report on resources? If so, provide the rationale for any comments and cross reference to the relevant paragraph.

- a) Yes. As noted above, the notions of EGAs/OGAs for longer-term grants as opposed to expenses on short-term grants/procurement is a useful way to analyse the differences. This delineation is likely to lead to more transparent reporting of longer-term grants, rather than variable practice that has also included some entities deducting grants from equity.
- b) Yes. I am not aware of other transactions that would not fit these definitions.
- c) Yes. One benefit of requiring legal or equivalent means is that all parties should come to the same conclusion. This is also likely to assist assurance providers in determining the efficacy of the reporting of such expenditure (or for the grantee, the revenue).
- d) Yes. I am unaware of a situation where this would not be appropriate.
- e) Yes.
- f) The overriding proposals in G24.32 combined with the constraints regarding sensitive information should enable sufficient disclosure. Paras G24.33-G24.35 are sensible not only in light of the need to protect individuals, but also to comply with privacy legislation in many jurisdictions.

- g) Yes.
- h) No.

Question 6: Borrowing costs

a) Do you agree that there are no significant alignment changes required to Section 25, other than the terminology changes that have been made? If not, set out the alignment changes you believe are required.

- a) Yes.

Question 7: Share-based payments

a) Given the characteristics of NPOs, do you agree that guidance on share-based payments is not required? If not, provide examples of share-based payments and explain how they are used.

- a) Yes. Even when there are shares (for example in some social enterprises), I am unaware of instances where NPOs make share-based payments to staff or suppliers.

Question 8: Employee benefits

a) Do you agree that profit sharing and share-based payments are removed from Section 28 Employee benefits to reflect that employees of NPOs are very unlikely to be incentivised by sharing in the surpluses made by an NPO? If not, provide examples of such arrangements used by NPOs.

b) Do you agree that in-year changes to the value of post-employment benefits can be shown on either the Statement of Income and Expenses or Statement of Changes in Net Assets? If not, why not?

- a) It is important to have guidance on accounting for employee benefits, beyond merely cash-in-hand regular payments. I agree with the removal of profit-sharing and share-based payments from Section 28. I have not seen such arrangements in NPOs.
- b) Yes.

Question 9: Income tax

a) Are there any elements of Section 29 Income taxes that are not required by NPOs? If so, explain which elements are not needed and why.

- a) NPOs seldom pay income tax, but guidance for taxation reporting is necessary, including taxes withheld. I cannot comment on which elements might be superfluous, but this section appears to be sympathetically amended for NPOs.

Question 10: Foreign currency translation

- a) Do you agree that grants and donations should be considered when setting the functional currency? If not, why not?
- b) Do you agree with the principle that exchange gains and losses are shown as part of funds without restrictions unless they relate to a transaction that is to be shown as restricted? If not, why not?
- c) Do you agree with the proposal to require exchange gains and losses that contribute to a surplus or deficit on grant arrangements presented as funds with restrictions to be disclosed? If not, why not? What would you propose instead?
- d) Do you have any other comments on Section 30, including whether there are any NPO-specific recognition and measurement issues associated with foreign currency translation? If so, explain your comments and the NPO-specific recognition and measurement issues?

- a) Yes. The proposal guiding G30.3(c) is particularly useful as it notes that the functional currency will typically be the currency in which income and costs are settled/denominated. Therefore while a donor may use a different currency, a recipient NPO would be able to consider its functional currency in terms of its total operations (as well as by referring to G23.14).
- b) Yes.
- c) Yes.
- d) I am unaware of any NPO-specific recognition and measurement issues in this area.

Question 11: Hyperinflation

- a) Do you agree that there are no significant alignment changes required to Section 31, other than the terminology changes that have already been made? If not, describe any further alignment changes required?

- a) I have no experience in accounting in a hyperinflationary context.

Question 12: Events after the end of the reporting period

- a) Do you agree that there are no significant changes required to Section 32, other than those that have already been made for alignment purposes? If not, describe any further alignment changes required.

- a) Yes.