



Not-for-profit financial reporting for June 2020

The June 2020 reporting season is a challenging period for many not-for-profit entities as they navigate through the first-time adoption of the new income and leases accounting requirements and the uncertainties arising from COVID-19

The key matters that not-for-profit (NFP) entities should consider when adopting the new Standards are:

- New income recognition requirements – Whether an arrangement is enforceable and the performance obligations relating to the transfer of goods or services are sufficiently specific is important as this determines whether the transaction is recognised under AASB 15 *Revenue from Contracts with Customers* (the possibility of income deferral) or AASB 1058 *Income of Not-for-Profit Entities* (generally upfront recognition of income). For entities with research grants, some contentious issues arise around the identification of the performance obligations and the timing of revenue and cost recognition
- New leases accounting requirements – Determination of the lease term for leases in holdover (renewable/cancellable) can be challenging as international discussions have indicated that the enforceable period of the lease term considers the economics of the arrangement rather than just the legal form. In addition, entities with below-market or peppercorn rentals may choose, as an accounting policy choice, whether to recognise such leases under a cost or fair value model. Additional disclosures are required where the cost model is selected
- Special purpose financial statement disclosure requirements – Additional disclosures are required in respect of the extent of compliance with recognition and measurement of Australian Accounting Standards.

The NFP-specific accounting considerations arising from COVID-19 are:

- Financial reporting – Cashflow forecasting, asset impairment, subsequent events and going concern, charity operations and charity reserves
- Accounting for the government relief packages (e.g. Job keeper) – Timing of income recognition is impacted by when the eligibility criteria for the relief are met. Presentation of grant income may be different to for-profit entities because NFP entities cannot present grant income 'net' of the related expense.

Looking ahead, some key developments are:

- Regulatory – Upcoming Australian Charities and Not-for-profits Commission (ACNC) legislative review proposing changes to revenue thresholds and additional disclosures (related party transactions and key management personnel compensation)
- Standard-setting – Simplified disclosures for entities currently preparing Tier 2 'Reduced Disclosure' financial statements.

Adoption of new accounting standards for June 2020

Overview

The June 2020 reporting season is a challenging period for many not-for-profit entities ('NFP') as they navigate through the first-time adoption of new income and leases accounting requirements. The new accounting standards that are mandatorily effective for NFP entities for the 30 June 2020 reporting period are:

- AASB 1058 *Income of Not-for-Profit Entities* (AASB 1058)
- AASB 15 *Revenue from Contracts with Customers* (AASB 15)
- AASB 16 *Leases* (AASB 16)
- AASB 2019-4 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Not-for-Profit Private Sector Entities on Compliance with Recognition and Measurement Requirements* (AASB 2019-4).

These new accounting standards can add complexity and require the use of significant judgement in their application at a time when many NFP entities are having to navigate the adoption of these standards whilst dealing with the impacts of COVID-19.

This publication discusses the various accounting issues for NFP entities to consider for the June 2020 reporting season covering the implementation challenges from the adoption of the above standards as well as the NFP-specific matters arising from the impacts of COVID-19. Looking past June 2020, this publication also covers some upcoming NFP-specific developments in the standard-setting and regulatory space with the Australian Accounting Standards Board (AASB) and ACNC.

This is a challenging period for many NFP entities as they not only have to apply the new income and lease accounting requirements for the first time but do so during a global pandemic

New income recognition requirements (AASB 15 and AASB 1058)

Overview

Since the AASB issued the new income recognition requirements for NFP entities in December 2016, this has resulted in a significant change for many NFP entities in the way they recognise income. The new requirements shift the focus from a reciprocal/non-reciprocal basis to a basis of assessment that considers the enforceability of a contract and the specificity of performance obligations. In cases where there is an 'enforceable' contract with a customer with 'sufficiently specific' performance obligations, income is recognised when (or as) the performance obligations are satisfied under AASB 15, as opposed to immediate income recognition under AASB 1058. This assessment can be very challenging to apply in practice and requires significant judgement by NFP entities in analysing the various contract terms to ensure that income is recognised correctly.

This section discusses the following various implementation issues that entities should consider when adopting the new income requirements:

- Assessment of sufficiently specific
- Other implementation issues
- Research grants
- Capital grants.

Assessment of sufficiently specific

The assessment of sufficiently specific is a key area for entities to focus on when applying the new income recognition requirements. This is an important and fundamental concept as the specificity of performance obligations (together with enforceability) will determine whether the transaction is accounted for under AASB 1058 (which may result in upfront income recognition) or under AASB 15 (which may require overtime and/or point in time revenue recognition).

Under AASB 15, a promise needs to be sufficiently specific to be able to determine when the obligation is satisfied and AASB 15 provides some factors to consider when assessing if the promise is sufficiently specific. These factors are split into four conditions, or indicators, (nature/type, cost/value, quantity and time period). However, AASB 15 states that no specific number or combination of the conditions need to be specified in an agreement for the promise to be sufficiently specific. Accordingly, this has resulted in implementation challenges as entities need to apply judgement when determining whether a promise is sufficiently specific.

Below are some examples that highlight the difficulties in applying the requirements in practice.



Example 1: Specified usage of funds

Base fact pattern: Charity A has received \$500,000 from the government. The non-cancellable contract states that the contract period is from 1 January 2020 to 31 December 2021 and requires the charity to use the funds to provide practical assistance and support to families affected by domestic violence in a specific region in Australia with the aim of improving their lives so they can move on to a life free from violence. In the event that there are unspent funds at the end of the contract, Charity A has to refund any unspent funds to the government.

Accounting considerations: Based solely on the facts provided, the contract is enforceable, but it is not considered sufficiently specific as the required use of the funds is not outlined in sufficient detail for the charity to determine when the obligation is satisfied (e.g. how much assistance and support is required to be provided in order for the charity to meet the obligation).



Example 1B: Detailed activity plan

Additional fact: Based on the fact pattern in Example 1 and adding an additional fact – the contract contains a specific annual activity plan to be submitted to the grantor for approval which must contain a timeline and schedule of required activities to be completed prior to the granting of the funds i.e. the grant is made on the basis of the submitted activities and timeline which forms part of the contract.

Accounting considerations: The arrangement could be sufficiently specific based on the level of detail in the activity plan regarding the specific activities in order to achieve the outcomes (e.g. provide crisis counselling services for a given number of hours per week for the period of January to December 2020 and 2021)



Example 1C: Milestones (Acquittal process)

Additional fact: Based on the fact pattern in Example 1 (excluding Example 1B) and adding an additional fact – the contract contains a payment schedule of \$125,000 every six months with an acquittal process for the achievement of milestones (e.g. submission of a progress report on the activities undertaken and the progress to date).

Accounting considerations: It is important to consider the nature of the milestones – some questions to ask in this scenario are as follows: Are the milestones administrative in nature? Do the milestones provide any details on the specified performance obligations (e.g. the nature/type of services and the quantity)? Do the milestones correspond with the value transferred i.e. is the allocation of revenue to each milestone commensurate with the satisfaction of the performance obligation?

Furthermore, if it is determined that the performance obligations are sufficiently specific and the contract is therefore accounted for under AASB 15, the entity should consider whether the progress report is subject to an approval process by the grantor in their sole discretion – if so, the entity needs to consider if the approval is perfunctory in assessing whether the approval process results in the application of a constraint on revenue recognition. In some cases, the assessment can be qualitative and/or quantitative in nature. If it is qualitative, it might mean that a constraint should be applied as the grantor will evaluate whether the qualitative targets have been met. If it is quantitative (that is, measurable targets that need to be achieved), it may be possible to recognise revenue provided achievement of the targets can be reliably proven.



Example 1D: Key performance indicators (Benchmarks)

Additional fact: Based on the fact pattern in Example 1 (excluding Examples 1B and 1C) and adding an additional fact – the contract contains certain specific performance measures (KPIs) that demonstrate achievement of the applicable four conditions that must be achieved for each period (for example every six months). Failure to meet targets will result in the clawback of the payment.

Accounting considerations: The entity should consider if meeting the KPI demonstrates the transfer of sufficiently specific services and outcomes (KPIs) – that is, the performance requirements underpinning the KPIs are sufficiently identifiable, measurable and linked to the required outcome (the service). In cases where the measurable targets would make the services within the contract sufficiently specific, it is important to also note that revenue can only be recognised for the amount that the entity expects to be entitled to by meeting those targets for the period as it may be necessary to apply a constraint on revenue recognition.

**Example 2: Stand-ready obligations**

In some cases, the contract might not contain measurable and specified quantities of the required services. Instead, the nature of an entity's promise under the contract is to stand ready to provide goods or services rather than to provide a defined amount of discrete goods or services.

A stand-ready performance obligation arises when the nature of the entity's promise in a contract is to stand ready to provide goods or services for a period of time rather than to provide the goods or services underlying the obligation. The customer consumes and receives benefits from a stand-ready obligation from the assurance that a service or resource is available to it when and if needed or called upon.

In the NFP sector, tripartite arrangements are very common where the customer might direct that goods or services are to be provided to third-party beneficiaries (including individuals or the community at large) on the customer's behalf. In such cases, the customer is identified as the party that has contracted with the entity for those goods or services and promises consideration in exchange for those goods or services. The provision of goods or services to third-party beneficiaries is a characteristic of the promised transfer of goods or services to the customer.

Fact pattern: Charity B has received \$500,000 from the government. The contract is non-cancellable and states that the contract period is from 1 January 2020 to 31 December 2021 and requires the charity to use the funds to provide crisis counselling services to families affected by domestic violence in a specific region in Australia. In the event that there are unspent funds at the end of the contract, Charity B has to refund any unspent funds to the government.

The contract requires that Charity B has to establish, promote and operate a hotline to provide crisis counselling services as needed to the victims of domestic violence. This hotline will operate 24 hours and 7 days a week for the period of 1 January 2020 to 31 December 2021. The hotline is required to be manned by a specified number of specifically qualified counsellors based on a roster of available lines at designated times and Charity B has to provide evidence of opening times, call log and staff who were on call at the centre over the period.

Accounting considerations: In this case, it is necessary to determine whether the nature of an entity's promise under the contract is (1) to stand ready to provide goods or services or (2) to provide a defined amount of discrete goods or services.

For this example, it could be seen as a stand-ready obligation as the nature of the entity's promise in the contract is to stand ready to provide an unspecified quantity of counselling services for a defined period of time (e.g. an unspecified number of calls which is measurable as it relates to the hotline being open 24/7 during the period) rather than to provide the specified services (e.g. provide 1,000 calls relating to counselling services for the period).

The timing is clear and measurable, the nature of the services is specified, the arrangement also requires qualified counsellors (defined level) and a defined roster of counsellors to provide the services and a de-identified log of calls as a record of calls. A key point is that the transfer of the service is not measured by the number of calls but rather by having the call centre operating at the required level all day and every day to provide the counselling services whether or not the centre receives any calls. While this is a stand-ready obligation to provide an unspecified quantity of service over a period of time, it is important to note that it is still necessary to determine whether the performance obligation is sufficiently specific based on the four conditions referred to above.

Under AASB 15:

- Over-time revenue recognition – A promise to stand ready to provide goods or services over a period of time results in the transfer of services being satisfied over time as the customer benefits from being able to call upon a resource if and when needed throughout the stand-ready obligation period
- Straight-line measure of progress (e.g. one that is based on the passage of time) may be appropriate in many cases for stand-ready obligations. The substance of the stand-ready obligation must be considered in order to select a measure of progress that reflects the nature of the entity's promise underlying that obligation.

Practical implementation issues

In addition to the assessment of sufficiently specific, there are other areas that we have seen entities grapple with when applying these new requirements. These include:

- Upfront fees – For upfront fees (e.g. mobilisation payments relating to infrastructure projects received – where AASB 15 applies), the entity needs to assess whether the fee relates to the transfer of a promised good or service and if it constitutes a separate performance obligation. Otherwise, the upfront fee represents an advance payment for future goods or services and would be recognised as revenue when those future goods or services are provided
- In-kind contributions – When an entity receives an in-kind contribution which is in the scope of AASB 1058, it should recognise the asset (e.g. the fair value for a motor vehicle under AASB 116 *Property, Plant and Equipment*) and assess if there are any related amounts to be recognised under other Standards. For example AASB 15 may apply where the transfer of the asset has attached conditions on specified utilisation in connection with the transfer of measurable services). Where there are no related amounts (e.g. no contractual conditions), income is recognised upfront, akin to a donation, in accordance with AASB 1058)
- Cash scholarships – When an entity receives cash to be distributed to recipients as cash scholarships, it should determine whether the nature of its promise is a financial liability under AASB 9 as a ‘related amount’ (no transfer of specific goods or services is required, just the payment of cash to settle the prescribed obligation) or a transfer of goods or services (e.g. provision of education services itself) under AASB 15 or AASB 1058
- Principal vs. Agent – When another party is also involved in providing goods or services to a customer, the entity should determine whether the nature of its promise in the arrangement is a performance obligation e.g.:
 - To provide the specified goods or services itself where it is a principal (e.g. entity engages the use of sub-contractors but remains the party responsible to grantor for delivering the promised services)
 - To arrange for those goods or services to be provided by the other party – Agent (e.g. entity takes on the role of a grant administrator for grantor with no decision-making power).

Research grants

Another area of complexity is accounting for research grants in the research sector. The challenges for the research sector resulted in the AASB deferring the application of AASB 15 and AASB 1058 in respect of research grants for six months, from 1 January 2019 to 1 July 2019. In addition, the AASB updated the [AASB Staff FAQs](#) to include further guidance related to the accounting for research grants which includes flowcharts, indicators of what might lead to a sufficiently specific performance obligation and accompanying examples.

One of the key areas of complexity for research grants is the assessment of specificity of the performance obligations. The identification of what it is that is being transferred through the research process requires detailed analysis. The AASB Staff FAQs have guidance indicating that transfers of intellectual property (IP) to the donor, licenses to IP given to the donor and publication of research findings could be indicators of a sufficiently specific performance obligation but that this will generally be an area of significant judgement.

If the enforceable agreement contains sufficiently specific performance obligations, the contract falls in the scope of AASB 15. Under AASB 15, an entity shall recognise revenue when (or as) the performance obligation is satisfied which can be recognised at a point in time or over time depending on the facts and circumstances.

To be over time, one of the following three conditions must be satisfied and the application and assessment of these conditions is proving difficult for a research grant:

- The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs (i.e. an asset is transferred to the customer which is immediately consumed) (AASB 15.35(a)). As an example, this can be satisfied where the transfer of the research findings is contemporaneous because the research grant contract requires the entity to share the research findings as the research is performed. The entity's contemporaneous transfer of research findings (rather than accumulated with periodic publication) meets the paragraph 35(a) requirements (see Example 4A¹ of AASB 15).

¹ Example 4A can be found in the *Australian illustrative examples for not-for-profit entities* (Appendices section) of AASB 15 (available at www.aasb.gov.au)

Clarity in financial reporting

Not-for-profit financial reporting for June 2020

Another example is where the research data is made public as it is collected (resulting from a promise to undertake the research and contemporaneously publish the research data). The undertaking of the research and contemporaneous publication of the data will represent transfer of services provided to the donor, as it is a beneficiary of the research even though the research data is publicly available (see Example 4A² of AASB 15).

In some circumstances, the application of paragraph 35(a) may be unclear. AASB 15 paragraph B4 refers to an entity assessing whether another entity would have to substantially re-perform the work that the entity has completed to date, if that other entity were to fulfil the remaining performance obligations to the customer. Paragraph B4 should be applied in the context of AASB 15 paragraph 35(a) (BC128). That is, the reperformance test specified under paragraph B4 only applies in conjunction with AASB 15 paragraph 35(a) (BC128). Accordingly, in cases where the control of the goods or services have not been transferred to the customer, the customer does not simultaneously receive and consume the benefits and the paragraph 35(a) requirement is not met and the reperformance test under paragraph B4 is therefore not relevant. This would be the case where a research grant contract requires only the periodic transfer or transfers of research findings, therefore the benefits of the research activities are accumulated as the research is performed, and hence not immediately consumed by the customer.

- The entity's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced (AASB 15.35(b)) – e.g. in cases where the IP rights arising from the research are transferred to the donor the entity's performance creates or enhances an asset (knowledge – the IP) that the donor controls as the asset is created or enhanced (see Example 2³ of AASB 15);
- The entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date (AASB 15.35(c)) – e.g. in cases where the research performance does not create an asset with an alternative use to the entity due to the agreement restricting the ability of the customer to use research for its own purpose or any other use. This criterion will also only be met if the entity also has an explicit, enforceable right to payment for performance completed to date (see Example 4B⁴ of AASB 15).

If revenue cannot be recognised over time, it must be recognised at a point in time when the performance obligation is satisfied (which could be at the conclusion of the research project when the research paper is published).

If the contract falls out of scope of AASB 15, income would be recognised upfront under AASB 1058 but specific consideration needs to be given to the timing of legal right to receive the cash and any claw back/refund mechanisms under the grant.

Capital grants

In cases where the transaction includes a transfer to enable an entity to acquire or construct a recognisable non-financial asset to be controlled by the entity (commonly known as capital grants), AASB 1058 requires the entity to recognise a liability for the excess of the fair value of the transfer over any related amounts recognised (for example, other performance obligations including under AASB 15, which involve the transfer of goods or services to other parties) and recognise any excess as income as the entity satisfies its obligations under the transfer.

In some cases, when a NFP entity receives a capital grant with an attached service requirement (e.g. grant to construct a building and the building must be used for a designated purpose for a defined period post completion), it is important for the entity to consider if there are any related amounts, specifically if the service requirements constitute a sufficiently specific performance obligation under AASB 15.

In other cases, NFP entities may have capital grants that only partially fund the total construction cost. The example below illustrates the accounting for such scenarios.

² Example 4A can be found in the *Australian illustrative examples for not-for-profit entities* (Appendices section) of AASB 15 (available at www.aasb.gov.au)

³ Example 2 can be found in the *Australian illustrative examples for not-for-profit entities* (Appendices section) of AASB 15 (available at www.aasb.gov.au)

⁴ Example 4B can be found in the *Australian illustrative examples for not-for-profit entities* (Appendices section) of AASB 15 (available at www.aasb.gov.au)



Example: Capital grant that partially funds the construction costs

Fact pattern: Charity C plans to construct a building expected to cost \$1 million. The project is funded 60% by the charity and 40% by the government via a capital grant. Under the capital grant, the building will remain a property of the charity. There is a clause for a refund obligation which requires the charity to return any misspent funds back to the grantor. The construction of the building will take place over two years with a detailed work plan with specified milestones.

Charity C receives \$400,000 cash on 1 July 20X0. At the end of year one (30 June 20X1), the building construction is 50% complete.

Accounting considerations: Firstly, Charity C needs to assess if this grant falls under the specific capital grant accounting requirements in paragraphs 15-17 of AASB 1058.

This capital grant meets all three criteria in AASB 1058.15 and will be accounted for under the specific capital grant accounting requirements in paragraphs 15-17 of AASB 1058 (note: there are no related amounts to be recognised per AASB 1058.9) e.g.:

- The agreement is enforceable due to the existence of the refund obligation
- The agreement requires the entity to use the financial asset received (cash of \$400,000) to construct a recognisable non-financial asset (building under AASB 116 *Property, Plant and Equipment*) to identified specifications
- The agreement does not require the entity to transfer the non-financial asset to the transferor or other parties which is true in this case as the charity retains the building post completion.

Accordingly, AASB 1058.15-17 requires the charity to recognise a liability of \$400,000 on initial receipt of the cash which represents the obligation to construct the building and income will be recognised as the performance obligation is satisfied (which will be over time as the building is constructed). At the end of year one, the charity would recognise \$200,000 (50% of \$400,000) as income in that year.

New lease requirements (AASB 16)

Overview

We've been talking about the implementation of AASB 16 for a number of years. Below we highlight some of the common implementation issues we've been seeing.

Lease term: holdover leases

Determining the lease term is critical when applying AASB 16. It is important to get this step right as it is probably the input that most materially impacts the present value of cash flows calculation and, as a result, the lease liability (and asset) that is carried recognised on the balance sheet. In order to determine the lease term, it is necessary to understand the interaction between the non-cancellable period (being the minimum period for which the contract is enforceable), the lease term (which includes options to extend that are reasonably certain to be exercised and options to terminate that are reasonably certain not to be exercised) and any enforceable period beyond this.

It can be challenging to determine the lease term for a complex contract with multiple optional periods for extension and leases that are in holdover. The IFRS Interpretations Committee (IFRIC) discussed this topic recently and issued an agenda decision. Where the entity has leases in holdover (e.g. renewable leases⁵ and/or cancellable leases⁶), it is important to understand the impact of this agenda decision.

⁵ A lease that specifies an initial period and renews indefinitely at the end of the initial period unless terminated by either of the parties to the contract is often referred to as a renewable lease.

⁶ A lease that does not specify a particular contractual term but continues indefinitely until either party to the contract gives notice to terminate, is often referred to as a cancellable lease.

Clarity in financial reporting

Not-for-profit financial reporting for June 2020

AASB 16 requires entities to consider the lease term to be the period over which the lease is 'enforceable'. The IFRIC was asked whether a lease contract could be 'enforceable' beyond the notice period of a cancellable lease or the initial period of an indefinitely renewable lease. Paragraph B34 of AASB 16 specifies that 'a lease is no longer enforceable when the lessee and the lessor **each** has the right to terminate the lease without permission from the other party with no more than an insignificant penalty'. (**emphasis** added)

The discussion in the agenda decision indicates that the IFRIC intends for this assessment to be based on the economics of the arrangement rather than just the legal form of the contract, meaning that it is possible for the contract to be enforceable beyond the notice period of a cancellable lease (or the initial period of a renewable lease). This is primarily based on the principle that the term 'penalty' is broader than amounts that are contractually built into the agreement and could include scenarios, for example, where the costs associated with finding or obtaining an alternative asset would exceed the benefits of moving or in the case of a property where the lessee had spent a lot of money on a fit out in respect of which it would lose the future economic benefits if it decided to relocate. Both of these situations indicate that the lessee has an economic disincentive to exercise its termination option (if it exists) or not to continue to occupy the property and therefore the lease remains enforceable. To demonstrate this, consider the example below:



Example: Holdover leases

Fact pattern: Charity D has a lease which is in holdover on a month-to-month basis with the following characteristics:

- Charity D has made significant investment in non-removable leasehold improvements with a significant remaining useful life
- Due to the nature of the facility the lessor would have difficulty finding a new lessee without incurring considerable refurbishment costs.

Due to the above factors Charity D is reasonably certain that it will remain in the facility for a further 10 years.

Accounting considerations: The above are examples that suggest the contract would be economically enforceable beyond the month-to-month period of the holdover arrangement.

An entity should consider the broader economics of the contract when determining the enforceable period of the lease such as the costs of abandoning the non-removable leasehold improvements. If an entity expects to use the leasehold improvements beyond the date on which the contract can be terminated, the existence of those leasehold improvements indicates that the entity might incur a more than insignificant penalty if it terminates the lease. Consequently, applying paragraph B34 of AASB 16, an entity considers whether the contract is enforceable for at least the period of expected utility of the leasehold improvements.

Once the enforceable period of the lease has been determined, it is necessary to determine the lease term as this impacts the measurement of the lease liability and the right of use asset. The lease term should reflect the non-cancellable period of a lease, together with periods covered by options to extend if the lessee is reasonably certain to exercise the options and periods covered by options to terminate if the lessee is reasonably certain not to exercise the termination option. Only options during the period for which the contract is enforceable are considered.

In assessing whether a lessee is reasonably certain to extend (or not to terminate) a lease, paragraph B37 of AASB 16 requires an entity to consider all relevant facts and circumstances that create an economic incentive for the lessee. This includes significant leasehold improvements undertaken (or expected to be undertaken) over the term of the contract that are expected to have significant economic benefit for the lessee when an option to extend or terminate the lease becomes exercisable (paragraph B37(b)). Therefore, in this example, if the reasonably certain period based on the economics is 10 years, even though the contract is in holdover, the lease term would be assessed as being 10 years. In some cases, where there are other economic reasons that act as a disincentive for either the lessee or lessor to terminate the lease determining the lease term of a holdover lease may be a matter of significant judgement.

This is a complex area that requires significant judgement. Entities need to ensure they have clear accounting policies and documentation to support conclusions and we encourage consultation to assist in working through these issues.

Common implementation issues

Key area	Considerations
1. Identifying a lease	<p>Identifying a lease will sometimes require a significant amount of judgement. A common issue we are seeing is the need to consider service agreements that involve the use of an asset for potential embedded leases.</p> <p>For example, entities should consider arrangements relating to leased IT platforms, cloud services, etc as some arrangements could include embedded leases, where an operator is providing exclusive use of an asset (e.g. hardware). All service arrangements where there is the right to access or use an asset should be considered.</p>
2. Variable lease payments	<p>AASB 16 requires the build-up of the lease liability based on a number of inputs including lease payments and accordingly requires the identification of fixed lease payments, which can include payments that are deemed 'in-substance' fixed payments. In-substance fixed payments are those that while structured as variable, are unavoidable.</p> <p>Consider the example of leases where the lease charge is based on the number of students enrolled in a school for a given academic year. Consideration needs to be given to whether there is genuine variability in the clause or whether the agreement requires the school to enrol a minimum number of students. It should be noted as well, that where the lease payment varies based on an index or rate such as CPI this will impact the measurement of the lease liability. When measuring a lessee's lease liability, such payments should initially be measured using the index or rate as at the commencement date.</p>
3. Concessionary leases	<p>AASB 16 and AASB 1058 give accounting guidance for leases that are below market value, or concessionary. Commonly these are referred to as 'peppercorn leases'. AASB 2019-8 <i>Amendments to Australian Accounting Standards – Class of Right-of-Use Assets arising under Concessionary Leases</i> clarifies that entities that have concessionary leases have an option to apply temporary relief from the requirement to fair value concessionary leases by applying a deemed cost approach. This relief must be applied on a class by class basis.</p> <p>For entities with peppercorn leases who take advantage of the temporary cost option, it is important to note that there are additional disclosures to be made that provide an explanation of the entity's dependence on such leases to enable the entity to further its objectives. These disclosures will need to be made for each 'material lease'. Accordingly, judgement will be required in determining which concessionary leases are material. In disclosing concessionary leases more generally, AASB 2019-8 clarifies that right of use assets arising out of concessionary leases can be treated as a separate class of right of use assets.</p> <p>For government not-for-profit entities AASB 2018-8 <i>Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities</i> and AASB 2019-8 also clarified that these entities are equally able to adopt the temporary cost exemption for concessionary leases.</p>

All of these areas can be highly judgemental. Entities need to ensure they have clear accounting policies and documentation to support conclusions and we encourage consultation to assist in working through these issues.

Additional disclosures in special purpose financial statements on compliance with recognition and measurement requirements in Australian Accounting Standards (AASB 2019-4)

Overview

For certain NFP private sector entities preparing special purpose financial statements (SPFS), there are some new disclosure requirements to take note of for 30 June 2020. The AASB has issued an amending standard, AASB 2019-4 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Not-for-Profit Private Sector Entities on Compliance with Recognition and Measurement Requirements* which introduces new disclosure requirements in AASB 1054 and is effective for periods ending on or after 30 June 2020.

The AASB has introduced these new disclosures to provide greater transparency for SPFS as its previous research indicated that, for 44% of medium and large charities lodging SPFS with the ACNC, it was unclear whether or not they complied with the recognition and measurement requirements in Australian Accounting Standards (AAS).

The new disclosure requirements affect the following entities:

- Medium and large charities registered with the ACNC preparing SPFS
- NFP entities that are lodging SPFS with ASIC (e.g. companies limited by guarantee).

There are three key areas of disclosures:

Key area	Disclosure requirements
1. Disclosure of basis	Disclose the basis on which the decision to prepare SPFS was made.
2. Application of the consolidation and equity accounting requirements (this is only applicable where the entity has interests in other entities)	Should the entity's interests in other entities give rise to subsidiaries, associates or joint ventures, the entity shall disclose whether it has accounted for those interests in accordance with AASB 10 <i>Consolidated Financial Statements</i> and AASB 128 <i>Investments in Associates and Joint Ventures</i> . If the entity has not accounted for those interests in accordance with AASB 10 and/or AASB 128, it shall disclose that fact and the reasons why. Alternatively, if the entity is not required by legislation to make such an assessment for the purpose of assessing its financial reporting requirements and it has not done so, it shall instead disclose that fact.
3. Compliance with the recognition and measurement requirements in AAS (except for consolidation and equity accounting)	For each material accounting policy that does not comply, the entity shall either disclose where it does not comply or disclose that an assessment has not been made. The entity will also need to disclose the overall compliance of the financial statements with the recognition and measurement requirements of AAS.

There is informative implementation guidance and illustrative examples included in the standard for you to refer to when drafting your new disclosures.

NFP-specific accounting considerations arising from COVID-19

COVID-19 is having an unprecedented impact on the economic outlook for the Australian and global economy. For the first time, many entities will be required to consider the impact of COVID-19 on their financial reports arising from this global pandemic.

This pandemic is affecting economic and financial markets, and virtually all industries are facing challenges associated with the economic conditions resulting from efforts to address it. The NFP sector is no different in that it doesn't escape the challenges, but it does have some unique NFP-specific issues to consider which are covered in this section.

Financial reporting considerations, charity operations and charity reserves

For many entities, there are several financial reporting considerations to consider, such as preparation of forecast cash flow estimates, recoverability and impairment of assets, accounting for financial assets, contract modifications, events after the end of the reporting period and the ability to continue operating as a going concern. These are covered in more detail in the below Deloitte publication which is periodically updated as new developments arise.



Publication: [IFRS in Focus — Accounting considerations related to the Coronavirus 2019 Disease](#)

In addition to those issues outlined in the above publication, some other NFP-specific matters to consider are:

- Grants management – Doing a stocktake of obligated or committed grants and understanding the relevant cancellation clauses to understand the impact on grant funding e.g. speaking to funders about the effects of cancelling or delaying activities that are part of funding agreements
- Charity fundraisers – For a charity that has decided to cancel or postpone a fundraising event due to concerns over COVID-19, there may be questions raised over what to do with any money already committed (e.g. through ticket sales or other purchases). In these situations, it is important that a charity is transparent about what it is going to do (e.g. refund or reschedule the fundraiser) and considers the impacts of this on its cash flow forecasts and related expenditure commitments (e.g. consider the existence of onerous contracts if suppliers are already engaged for these events)
- Charity reserves – A charity may want to draw on its reserves to stay afloat at this time, but it is vital that a charity assesses whether drawing on reserves is the best option and considers any restrictions on the use of reserves
- Charity operations – A charity's operations may be affected by COVID-19 in that some or all of its activities may need to be modified or even temporarily halted. In such cases, it is vital to have regular communication about the charity's changed activities and most importantly that it remains consistent with its charitable purpose if the charity's operations do change.

Accounting for the government relief packages received (e.g. JobKeeper)

To stimulate the economy and to support those entities that have been significantly affected by the economic impacts of the COVID-19, governments are providing a range of financial support to them. The Federal Government support for eligible NFP entities includes the Federal Government's Boosting Cash Flow for Employers measure which includes support for eligible charities to manage cash flow and retain employees and the Federal Government's JobKeeper measure which aims to provide wage subsidies to eligible businesses and not-for-profit entities, including charities, that are significantly affected by COVID-19.

For many entities, accounting for government support of this nature will not be something encountered previously.

The AASB has released a new [Staff FAQs – Accounting for Government Support](#) which illustrates the decision-making process of the applicable Standards (e.g. AASB 1058 for NFP entities and AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* for for-profit entities) when accounting for government support.

Specifically, the illustrative example in section three of the AASB Staff FAQ's discusses how a NFP entity would account for a wage subsidy reimbursement (e.g. JobKeeper), which is as follows:

- The NFP entity recognises an asset on the receipt of cash from the government or when the eligibility criteria for the subsidy are met
- The entity also recognises any related amounts arising under other Australian Accounting Standards in accordance with AASB 1058. In cases where the entity did not identify any related amounts, the entire amount of the subsidy for the latest fortnightly period is recognised as income upon the recognition of the asset.

Clarity in financial reporting

Not-for-profit financial reporting for June 2020

Another key difference between NFP entities and for-profit entities in the accounting for such government support is the presentation of grant income. AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance* (which is applicable only to for-profit entities) allows grant income to be presented net against the related expense. AASB 101 *Presentation of Financial Statements* paragraph 32 prohibits an entity from offsetting income and expenses, unless required or permitted by an Australian Accounting Standard. Unlike AASB 120, which explicitly permits net presentation of grants, neither AASB 15 nor AASB 1058 requires or permits the offsetting of revenue or income against the associated expenses. Accordingly, for NFP entities, grant income cannot be presented net against the related expense.

Available ACNC reporting relief

The ACNC recognises that a charity's usual operations may be affected by the outbreak and spread of COVID-19, as well as measures being established to try and control its spread. To aid charities in navigating this crisis, the ACNC has developed a [webpage](#) dedicated to addressing all issues regarding charity operations and COVID-19.

Some key matters to note on the webpage are:

- ACNC compliance during COVID-19 – In recognition of the unique challenges brought about by COVID-19, the ACNC Commissioner has decided that the ACNC will not investigate certain breaches of the Governance Standards and the External Conduct Standards that occur from 25 March until 25 September 2020
- Charity meetings and AGMs – The ACNC's Governance Standard 2 requires a charity to be 'accountable to members'. One common way in which a charity can do this is through AGMs and other meetings. The ACNC acknowledges that there may be difficulties for charities in holding its meetings at this time due to government requirements on physical distancing. The ACNC has provided some options to consider at this time such as holding meetings remotely via video or phone conference.

Looking ahead

Looking ahead past June 2020, there are upcoming NFP-specific developments in the standard-setting and regulatory space in AASB and ACNC that NFP entities should take note of.

Regulatory developments – ACNC legislative review

The Government is required to undertake a review of the *Australian Charities and Not for profits Commission Act 2012* and the *Australian Charities and Not-for-profits Commission (Consequential and Transitional) Act 2012* after their first five years of operation. This review presents an opportunity to evaluate the performance of the legislative framework, the regulation of the sector and to identify any improvements that can be made.

A review panel was established to conduct the review. The final report was tabled on 22 August 2018 and contained 30 recommendations. The [Government response](#) was released on 6 March 2020. The table below covers the three key financial reporting changes (among the 30 recommendations put forward by the panel) and the respective Government responses.

Key changes	Government responses	Next steps
1. New revenue thresholds Revenue thresholds should be determined on a rolling three-year basis rather than on an annual basis (which is currently required): <ul style="list-style-type: none">• Small charities: Less than A\$1 million (currently A\$250,000)• Medium charities: Less than A\$5 million (currently A\$1 million)• Large charities: More than A\$5 million (currently A\$1 million).	Supportive	The Government is consulting with States and Territories on the appropriate level of revenue thresholds for minimum reporting requirements, before proceeding with legislative change
2. Registered entities should be required to disclose related party transactions Small registered entities to provide a simplified disclosure involving a brief description of a related party transaction	Supportive	The Government will implement this recommendation by changes to regulations. The start date for this measure will align with any change to the revenue thresholds for financial reporting requirements

Key changes	Government responses	Next steps
<p>3. Large registered entities should be required to disclose the remuneration paid to responsible persons and senior executives on an aggregated basis</p> <p>Only required for entities with two or more key management personnel to accommodate privacy concerns</p>	Supportive	The start date will align with any change to the revenue thresholds for minimum reporting requirements

There is no expected timeline as to when the Government will pass the new legislation to make the above changes effective. However, due to resources being diverted for addressing the COVID-19 pandemic, we understand that there may be delays in this regard.

Standard-setting developments – AASB 1060 and other NFP developments

In the standard-setting space, a key development for NFP entities using the current Tier 2 reporting requirements for preparing general purpose financial statements is the issuance of AASB 1060 *General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* (AASB 1060) which is a new 'Tier 2' 'Simplified Disclosure' Standard which replaces the existing 'Reduced Disclosure Requirements' (RDR). AASB 1060 generally provides disclosure relief compared to the existing RDR and is effective for annual periods beginning on or after 1 July 2021, with earlier application permitted.

Another key development to monitor is the amendment to the not-for-profit entity definition. The AASB issued AASB ED 291 *Not-for-Profit Entity Definition and Guidance* in June 2019 which proposes to amend the current NFP entity definition to a new definition that is based on the public benefit entity definition in New Zealand. Since the issue of ED 291, the AASB has decided to proceed with the NFP entity definition proposed in ED 291 with revised implementation guidance and illustrative examples. The matter was last discussed at the March 2020 AASB Board meeting and the final amending standard is expected to be issued in quarter four of 2020.

Some other NFP projects to be aware of are:

- NFP Private Sector Financial Reporting Framework – This project aims to develop a simple, proportionate, consistent and transparent financial reporting framework for all NFP private sector entities in Australia and establish reporting tiers and specify financial reporting requirements for each tier proportionate to the resources and user needs of entities. It is expected that this project will consider reporting in relation to service performance reporting, remuneration of key management personnel and fundraising, among other information that is integral to financial reporting in the NFP sector. On this front, the AASB issued [AASB Research Report 14 – Literature Review: Service Performance Reporting for Not-for-Profits](#) in February 2020. Based on the AASB Work Program (dated June 2020), the AASB is planning to issue an exposure draft in the second half of 2020/first half of 2021
- NFP Conceptual Framework project – The initial phase of this project is to update the AASB's *Conceptual Framework for Financial Reporting* to make it relevant to NFP entities.

Conclusion

This June 2020 reporting season is a challenging period for many NFP entities. They not only have to apply the new income and lease accounting requirements for the first time which are complex, requiring significant analysis and judgement, but do so during the effects of a global pandemic which increases many other reporting considerations that may be new to these entities.

In addition to the work required to implement the new requirements including contract assessment and system modifications, another key aspect for this June 2020 reporting season is the importance of disclosures on the impacts from the adoption of the new Standards and the impacts of COVID-19. In today's environment with high levels of uncertainty due to the pandemic, it is a matter of importance that the financial reports include relevant disclosures that are transparent and entity-specific regarding significant judgements and estimates. The disclosures in the financial report should explain the effects of adoption of the new Standards and explain the effects of the impacts of COVID-19 on the entity's financial statements.

For NFP-specific illustrative disclosures for the adoption of the new standards for June 2020, the below publication is an addition to Note 2 in Section 10: Illustrative disclosures of the [Deloitte Australian financial reporting guide](#) (for financial reporting periods ending on or after 30 June 2020) which includes NFP specific considerations. It covers the adoption of AASB 15 and AASB 1058 for the various illustrative revenue streams and the illustrative disclosures for a concessionary lease measured under the cost option.



Publication: [Not-for-Profit \(NFP\) Illustrative Disclosures for the year ended 30 June 2020](#)

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