International Non-Profit Accounting Guidance Part 2

Basis for Conclusions

INPAG

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Contents

The Preface, Sections 1 to 10 and Section 35 were published as drafts in Exposure Draft 1 and was accompanied by a **Basis for Conclusions**. A Basis for Conclusions will be published for the remaining sections in Exposure Draft 3.

[1] Status refers to whether the *IFRS for SMEs* Standard has been updated to reflect NPO specific requirements. Further explanation can be found in the Invitation to comment.

Preface

As part of the development of the content of Exposure Draft 2, an additional paragraph is proposed to the Preface.

BCP.2a The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. A list of 10 topics was prioritised for inclusion, with the remaining to be updated only for terminology changes, alignment with other sections or consequential changes arising from amendments to the other sections. The Basis for Conclusions identifies which sections have not been fully reviewed and the extent to which they have been updated.

Section 11 – Financial instruments

BC11.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Financial instruments was not included as a prioritised topic.

BC11.2 There were no significant issues arising from the review of this Section. Other than terminology, changes made reflect alignment with other INPAG Sections.

BC11.3 Changes are proposed to the scope of the financial statements in INPAG compared to the *IFRS for SMEs* Accounting Standard, particularly regarding the location of fair value adjustments. Accordingly, Section 11 has been updated to provide guidance on where these should appear. The proposed changes reflect the intent on how the Statement of Income and Expenses and the Statement of Changes in Net Assets are used.

BC11.4 It is proposed to retain the general requirements of the *IFRS for SMEs* Accounting Standard until such time as this Section is fully reviewed. INPAG therefore proposes that in subsequently measuring a financial instrument, changes in the fair value should generally continue to be required to be recognised through surplus or deficit.

BC11.5 With regard to hedging instruments in Part 2 of Section 11, in line with BC11.3, the Section has been updated to require that changes in the fair value of hedging instruments are recognised in the Statement of Changes in Net Assets until the instrument is discontinued. At this point any gains or losses are reclassified to surplus or deficit. This proposal reflects discussions by the TAG on which items appear in which financial statement.

BC11.6 Consideration was given to whether additional guidance on grant prepayment assets and grant payment liabilities as defined in Section 24 Part I *Expenses on grants and donations* was needed in this Section. The TAG was of the view that the guidance in Section 11 was sufficient and that there was no need for additional guidance in Section 11. Its advice was to keep any necessary guidance within Section 24 Part I.

Section 13 – Inventories

Consultation Paper – issues identified and approaches

BC13.1 The recognition and initial measurement of purchased or self-produced inventories does not give rise to any NPO-specific issues, and no changes to the *IFRS for SMEs* Accounting Standard requirements were proposed in the Consultation Paper.

BC13.2 The Consultation Paper did identify specific issues in respect of:

- the recognition and initial measurement of donated inventories, particularly those donated for resale or for distribution to service recipients;
- the recognition and initial measurement of work-in-progress of services to be provided for no or nominal consideration to service recipients; and
- the subsequent measurement of inventories held for distribution to service recipients or for use by the NPO in meeting its objectives.

BC13.3 The Consultation Paper also identified issues regarding the recognition of revenue in respect of donated inventories, and proposed exceptions permitting NPOs not to recognise revenue and inventories on receipt of the donated items, but to recognise revenue and either an asset or an expense when the items are sold, transferred to another party in the course of fundraising activities, distributed to service recipients or used by the NPO.

BC13.4 Respondents to the Consultation Paper supported the proposed permitted exceptions to the recognition and measurement of revenue from donated items, including donated inventories.

BC13.5 Respondents were supportive of the description of the issue. They provided some additional considerations that needed to be considered in developing the guidance. These included:

- specific issues regarding donated inventory (which have mainly been addressed by Section 23 *Revenue)*; and
- the subsequent measurement of perishable inventories, particularly where these are donated.

BC13.6 Section 13 reflects the adjustments to the requirements of the *IFRS for SMEs* Accounting Standard required to ensure the accounting for inventories is consistent with the proposals in Section 23 *Revenue*. Further changes to Section 13 may be required if the proposals in Section 23 are modified as a result of stakeholder comments.

Recognition and initial measurement

BC13.7 The proposals in Section 23 permit NPOs to not recognise many donated items as inventories. This will address most of the concerns raised about the initial recognition and measurement of donated items. Section 13 states that an NPO that uses the permitted exceptions in Section 23 should not recognise inventories in respect of those items.

BC13.8 Some Technical Advisory Group (TAG) members noted that while these exceptions are expected to meet the needs of NPOs, they may not meet the needs of the users of the financial statements. The Secretariat agreed to review the proposals once responses to ED2 have been received.

BC13.9 Respondents to the Consultation Paper also supported permitting NPOs to expense work-in-progress on services, such as legal casework, that will be provided to service recipients at no or nominal cost. Respondents were concerned that some NPOs would not have the systems in place to reliably measure such work-in-progress. Section 13 provides a permitted exception that allows NPOs to expense this work-in-progress as the costs are incurred, rather than to recognise it within inventories. The TAG discussed whether a requirement for all NPOs to expense work-in-progress on such services would support greater comparability. However, a permitted exception rather than a requirement to expense the work-in-progress is proposed as such work-in-progress may be material to some NPOs and it may provide more meaningful information if included as inventory.

BC13.10 Some respondents emphasised the importance of disclosure if items of inventory were not to be recognised. The Secretariat agreed with these comments, and NPOs that elect to apply any of the permitted exceptions are required to disclose the exceptions being utilised and provide further information about the inventory to which it relates. This will provide users with useful information that will help them understand the NPO's financial statements.

BC13.11 Some respondents noted that additional guidance on determining fair value where an NPO recognises donated items of inventory would be needed. The draft Third edition of the *IFRS for SMEs* Accounting Standard includes a new section (Section 12 *Fair value measurement)* covering this topic. Section 12 of INPAG, based on the *IFRS for SMEs* Accounting Standard, will be included in ED3. As this is not a prioritised topic it is anticipated that the focus will be on terminology and similar changes.

BC13.12 Section 12 of the draft Third edition of the *IFRS for SMEs* Standard includes a fair value hierarchy. NPOs will be required to follow this hierarchy in determining the fair value of donated inventories. Additional Application Guidance has been provided in Section 13 that where an NPO needs to refer to level 3 inputs (that is, unobservable inputs) to determine the fair value of the donated inventories, the NPO may use the cost to the donor (where this is known) as deemed fair value.

BC13.13 In developing Section 12, the Secretariat will consider whether any further guidance or modifications to either Section 12 or Section 13 are required.

Reliable measurement

BC13.14 Some respondents to the Consultation Paper commented that NPOs may face practical issues in measuring inventories in some circumstances. An example provided was a small NPO responding to an emergency that receives large volumes of donated inventories and distributes them almost immediately. A small NPO may not have the systems or resources to keep accurate records without delaying the response to the emergency. In discussion with the Advisory Groups it was considered that such circumstances would be rare, as many NPOs would be established for those purposes and have the systems and resources to keep accurate records. However, the Secretariat recognised that some smaller NPOs such as local first responders might not have such systems.

BC13.15 The possibility of electing to apply the permitted exception to not recognise inventories was discussed. However, this exception would require that a revenue and an expense is recognised when the inventory is distributed and the Secretariat agreed that in this scenario the inability to reliably measure the donations would mean that as well as not recognising inventories, a revenue and expense would also not be recognised.

BC13.16 Consequently, the Secretariat agreed that a narrative description of inventories could be provided in the exceptional circumstances that inventories cannot be measured reliably. The inclusion of a narrative description is intended to provide transparency of such circumstances. The guidance makes clear that the expectation is that donated inventories can be reliably measured.

Subsequent measurement of inventories held for distribution to beneficiaries or for use by the NPO in delivering its objectives

BC13.17 The *IFRS for SMEs* Accounting Standard requires inventories to be subsequently measured at the lower of cost and estimated selling price less costs to complete and sell.

BC13.18 Measuring inventories by reference to their selling price may not be appropriate for inventories that will not generate future cash flows. The Consultation Paper proposed two alternatives to this treatment in the *IFRS for SMEs* Accounting Standard:

- such inventory would be measured at the lower of cost or current replacement cost; or
- such inventory would be measured at cost, adjusted for any loss of service potential.

BC13.19 There was support for both approaches, although a number of respondents expressed concern that it may not always be possible to identify a replacement cost, particularly for some donated items. Other respondents noted that assessing any loss of service potential could be subjective.

BC13.20 Section 13 requires an NPO to measure inventories held for use or distribution to be measured at the lower of cost adjusted for any loss of service potential and replacement cost. This will allow NPOs to reliably measure inventories that may be impaired even if a replacement cost is not available.

Cost Formulas

BC13.21 The *IFRS for SMEs* Accounting Standard permits the use of two cost formulas: the first in, first out (FIFO) formula or the weighted average cost formula. A third formula, first expired, first out (FEFO) was suggested as being more appropriate for NPOs who received donations of perishable items such as food or medical supplies.

BC13.22 The Secretariat agreed that for practical purposes, inventories would need to be managed in this manner to maximise the benefits obtained from the donations. However, following discussion with the TAG, the Secretariat did not consider that the introduction of an additional cost formula was appropriate as it was not clear that it was necessary and would unlikely be NPO specific.

BC13.23 The Secretariat consider that the proposed formula, which is intended to address circumstances where donated items may have a significantly shorter expiry period than the equivalent purchased items, can be accommodated using the cost methods permitted by the *IFRS for SMEs* Accounting Standard. Where expiry periods for donated items are significantly less than for purchased items, and this affects the value of the items, the economic nature of the items will be different. This difference means that different classes of inventories could be maintained for items donated close to their expiry date and other (usually purchased) items. Either the FIFO or weighted average cost formula would then be used for each class. Identifying items by class of inventories is expected to be no more complex to implement in stock control systems than the use of a FEFO cost model.

Impairment

BC13.24 Section 27 *Impairment of assets* requires inventories to be impaired when the carrying amount will not be fully recoverable. The *IFRS for SMEs* Accounting Standard requires a comparison between the carrying amount and the selling price less costs to complete and sell when determining whether inventories are impaired.

BC13.25 As discussed in paragraphs BC13.17–BC13.20, Section 13 has introduced an alternative measurement for inventories that will not be sold. Consequently, the impairment requirement in Section 13 has been amended so that impairment of inventories held for distribution or use by the NPO in delivering its objectives are assessed by reference to the cost adjusted for any loss of service potential or replacement cost. Section 27 will be updated in ED3.

Section 21 – Provisions and contingencies

BC21.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Provisions and contingencies was not included as a prioritised topic. No major editorial changes are proposed for provisions and contingencies, with only minor changes to terminology.

BC21.2 Consideration has been given to whether changes are required as a consequence of the development of additional guidance on grants and donations. To date no consequential amendments have been identified.

BC21.3 Whilst no changes are proposed to the core text, the illustrative examples have been amended to be more relevant to NPOs.

Section 23 – Revenue

Consultation Paper – issues identified and approaches

BC23.1 The recognition and measurement of revenue, and in particular non-exchange revenue, was identified as a specific issue for non-profit organisations in the IFR4NPO Consultation Paper, with a number of financial reporting challenges highlighted. These included:

- the need to identify overarching principles for the recognition and measurement of incoming resources from 'non-exchange' transactions;
- the recognition and measurement process associated with the receipt of donations that are used to fulfil requirements in subsequent periods;
- when donations to purchase a capital asset should be recognised; and
- the circumstances when services and gifts in-kind should be recognised and how they should be measured.

BC23.2 The Consultation Paper also noted that accounting for bequests and endowments would not be covered in the initial INPAG and would be considered in a later phase.

BC23.3 Respondents were supportive of the description of the issue, and provided additional points for consideration in developing the guidance. These included:

- the need to place greater emphasis on how to distinguish between exchange and non-exchange revenue;
- the inclusion of greater detail in cases where goods and services are provided by an NPO at subsidised prices;
- the importance of capital grants; and
- grants that are only received once the activities funded by the grant have been carried out.

BC23.4 The Consultation Paper proposed four alternative financial reporting treatments for developing guidance. The first was to require all non-exchange revenue to be recognised in accordance with the *IFRS for SMEs* Accounting Standard with additional NPO-specific guidance. The second was to use the principles in IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* to extend the treatment of government grants to all non-exchange revenue. The third was to require non-exchange revenue to be accounted for using the principles in IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*. The final alternative would require non-exchange revenue to be accounted for using the principles in IPSAS, with exceptions drawn from various national standards to be considered for inclusion as part of NPO-specific guidance. Using these exceptions would simplify the accounting for gifts in-kind and services in-kind.

BC23.5 A significant majority of respondents favoured alternatives that used a performance approach where revenue is recognised as performance conditions are satisfied rather than deferring revenue to match expenditure. A performance approach is used in the draft Third edition of the *IFRS for SMEs* Accounting Standard for government grants and commercial revenue and is the approach used by the IPSASB when it updated its revenue standards.

BC23.6 The need for additional guidance was also raised. Respondents proposed that this guidance should cover:

- non-performance conditions (ie, terms that relate to other factors such as time);
- the distinction between ‘conditions’ and ‘restrictions’ (that is, the distinction between terms of the agreement that require an NPO to undertake something specific and terms of the agreement that do not require a specific activity to be carried out, but limit the use of the funds); and
- the need to ensure consistency of treatment between a grantor of resources and the recipient of those resources.

BC23.7 Respondents also supported the inclusion of exceptions where NPOs would face practical difficulties in applying the alternatives. This was particularly relevant for gifts in-kind and services in-kind, due to the difficulties some NPOs would experience in measurement.

BC23.8 Distinguishing between revenue with performance conditions and other revenue, rather than between exchange and non-exchange revenue was also proposed. It was argued this would be useful for those transactions that had both an exchange and non-exchange element.

Changes to the *IFRS for SMEs* Accounting Standard and IPSAS Standards and proposal for a two section approach

BC23.9 Following the publication of the Consultation Paper there have been significant developments in the *IFRS for SMEs* Accounting Standard and IPSAS approach to revenue.

BC23.10 The IASB issued the Third edition of the *IFRS for SMEs* Accounting Standard, which proposes that Section 23 *Revenue from contracts with customers* is based on the principles in IFRS 15 *Revenue from contracts* *with customers*. The revised section is longer and more detailed than most other sections of the *IFRS for SMEs* Accounting Standard. There was only minor redrafting to Section 24 *Government grants,* which deals with the accounting for some non-exchange transactions.

BC23.11 The IPSASB continued to develop its approach to revenue, and in May 2023 it issued IPSAS 47 *Revenue*, which replaced its previous revenue standards and covers all revenue transactions. The Guidance in IPSAS 47 for contractual arrangements is based on IFRS 15.

BC23.12 The accounting model for revenue adopted in IPSAS 47 considers whether revenue arises from a transaction with a binding arrangement or without a binding arrangement. For revenue from transactions with a binding arrangement, the 5 step revenue recognition model in IFRS 15 is adapted to apply to a wider range of obligations than the performance obligations in IFRS 15. The approach is also consistent with Section 24 of the *IFRS for SMEs* Accounting Standard.

BC23.13 The proposed amendments to the *IFRS for SMEs* Accounting Standard and the issuing of IPSAS 47 result in a similar underlying set of principles in accounting for revenue across all three international frameworks. As a result, the Secretariat proposed that INPAG should also adopt these principles in accounting for revenue.

BC23.14 The *IFRS for SMEs* Accounting Standard provides revenue accounting guidance across two sections whereas the IPSAS 47 includes all revenue guidance in one IPSAS Standard, removing the need to distinguish between exchange revenue and non-exchange revenue.

BC23.15 Extensive discussions were held with the Technical Advisory Group (TAG) and Practitioner Advisory Group (PAG) on a single INPAG Section for revenue or whether having separate INPAG Sections for revenue from contracts with customers and revenue from grants and donations would be more appropriate in the NPO context. A single INPAG Section was proposed to be based on IPSAS 47, adjusted and simplified as necessary to suit the NPO context. Separate INPAG Sections would require the development of a new section for non-exchange revenue while retaining the content of Section 23 *Revenue from contracts with customers* with minor changes for terminology.

BC23.16 A single section covering all revenue would provide a shorter, more simple set of guidance with the avoidance of duplication and without the requirement for NPOs to first determine whether a transaction is from a contract with a customer or a grant or donation. By contrast, separate sections for revenue from customers and revenue from grants and donations would be easier for NPOs that only receive grants and donations to apply, would potentially mean shorter individual sections that would be easier to use and maintain the link with the *IFRS for SMEs* Accounting Standard as the basis of INPAG.

BC23.17 Both the TAG and the PAG had mixed views, with some members stressing that covering all types of revenue in one section would be preferable while others felt a distinction between 'self-generated' revenue and 'grants and donations' would align itself better to how the sector thinks and talks about revenue.

BC23.18 In the light of these views, the Secretariat developed a third approach, with all revenue covered in a single section with two Parts, one covering grants and donations and one covering revenue from contracts with customers. Section 23 of INPAG therefore covers all revenue transactions, including those covered by Section 24 of the *IFRS for SMEs* Accounting Standard. Both the TAG and the PAG agreed with this approach.

Section 23 Revenue - Preface

BC23.19 As revenue from grants and donations and revenue from contracts with customers are covered in separate parts of Section 23, guidance is required to help NPOs determine whether a transaction should be accounted for as revenue from grants and donations or revenue from contracts with customers. Section 23 begins with a preface that provides this guidance.

BC23.20 The preface notes that the substance of a revenue transaction depends on whether an NPO receives consideration in exchange for the direct transfer of services, goods or other assets to another entity or individual (a customer). If the transaction involves the NPO directly providing a service, good or other to a customer in exchange for consideration then it should apply the model for accounting for revenue from contracts with customers. If the transaction involves the NPO receiving cash, a service, good or other asset from an entity without it directly providing cash, a service, good or other asset in return then it should apply the model for accounting for revenue from grants, donations and similar income. Guidance is also provided to assist NPOs determine the appropriate accounting for transactions where the amount of the grant received and the value of services or goods provided are not of approximately equivalent value.

BC23.21 To reduce duplication content common to both Parts is included in the preface. The preface covers the scope and structure of Section 23, the principles of revenue recognition and measurement (including the initial recognition of grants with enforceable grant agreements and contracts with customers and the 5 step revenue recognition model) and revenue in foreign currencies.

Principal versus agent considerations

BC23.22 Distinguishing between transactions where an NPO acts as an agent for other entities or is acting in its own right (as a principal) is important to understand the accountability of an NPO, to provide transparency over its operating income and its expenses. An NPO that is an agent will account for a revenue transaction differently than an NPO that is a principal. NPOs acting on behalf of other entities, was a topic that was included in the IFR4NPO Consultation Paper and respondents supported its inclusion in INPAG.

BC23.23 The draft Third edition of the *IFRS for SMEs* Accounting Standard introduces a control-based approach to the principal-agent distinction, rather than a risks and rewards approach. IPSAS 47 adopts a similar approach. It was agreed with the TAG that a control-based approach to principal-agent issues would be proposed in INPAG.

BC23.24 This control-based approach focuses on the extent to which an NPO has control over an economic resource. This requires the NPO to have the present ability to direct the use of the economic resource and obtain the economic benefits or service potential that may flow from it.

BC23.25 To be a principal therefore requires the NPO to obtain economic benefits or service potential from an economic resource in order to further its own purpose and achieve its own objectives, and to be able to do so without requiring authorisation from another entity. An NPO that is a principal will account for the economic benefits or service potential it receives (which may be revenue from a grant or donation or revenue from a contract with a customer).

BC23.26 An NPO is acting as an agent when it does not control the economic resources in an arrangement. This is the case when the NPO is acting for another entity's purpose and objectives, acts in accordance with the instructions or directions of the other entity, and has no discretion about the use to which the resources received are put. An NPO acting as an agent would only account for any management or administration charge, fee or commission it received.

BC23.27 It was agreed with the TAG that guidance would be integrated into those sections where guidance on principal-agent relationships is required. Section 23 Revenue is one such section.

Part I – Revenue from grants and donations

BC23.28 Given the strong support for the use of a performance approach from respondents to the Consultation Paper (see paragraph BC23.5) the Secretariat considered those international standards that had adopted (or were adopting) a performance approach to grants and donations.

BC23.29 The Secretariat and the TAG agreed to base Part I of Section 23 of INPAG on IPSAS 47. The Secretariat considered adapting Section 24 of the *IFRS for SMEs* Accounting Standard, but concluded that while the principles were appropriate for INPAG, there was insufficient detail to provide the required level of guidance for NPOs. IPSAS 47 has principles consistent with those in Section 24 of the *IFRS for SMEs* Accounting Standard, and includes sufficient detail to assist NPOs.

BC23.30 As IPSAS 47 covers both grants and donations and contracts with customers in a single section, changes were made to the terminology, to focus only on grants and donations. As a consequence, terms such as binding arrangement in IPSAS 47 have been adapted to enforceable grant arrangement (EGA) in Section 23 Part 1. Binding grant arrangements can include contracts with customers, whereas as an EGA cannot. The text of the IPSAS 47 was also simplified, with some paragraphs that are unlikely to apply to grants and donations (for example, warranties) being omitted.

BC23.31 The same 5 step revenue recognition model underpins both the IPSAS 47 contractual arrangements and Section 23 of the draft Third edition *IFRS for SMEs* Accounting Standard. Consequently, the Secretariat and the TAG agreed that aspects of the model that would only rarely be relevant to grants and donations need not be covered in Part I. Instead, it was agreed that INPAG would include guidance on how the guidance in Part II of INPAG could be applied to grants and donations, where the guidance in Part I is insufficient. This approach was adopted to enable Part I to be further simplified and reduce duplication, making it more usable for the majority of NPOs.

Identifying whether an enforceable grant arrangement exists

BC23.32 An essential element of the model for recognising revenue from grants and donations is the use of EGAs. An EGA is defined as ’a grant arrangement where both a donor and grant recipient have both rights and obligations, enforceable through legal or equivalent means. An EGA has a least one enforceable grant obligation (EGO)’.

BC23.33 The word ‘undertaking’ has been used to describe the actions or promises that an NPO takes in meeting its obligations. This word was viewed by outreach participants and some PAG members as better describing how NPOs practically operate, sometimes using best endeavours to meet its obligations in an EGA. The use of the word ‘undertaking’ was discussed by the TAG as there were concerns that it does not align with the requirement to satisfy specific deliverables in an EGA. The TAG agreed with the concern and also noted that it can have specific and different meanings in some jurisdictions. It was agreed that an undertaking without a deliverable is not likely to be enforceable by a grant provider.

BC23.34 This definition of an EGA allows the rights and obligations to be used as the basis of recognition for both revenue from grants and donations and for expenses on grants and donations (for those NPOs that provide grants to other entities or individuals).

BC23.35 Feedback from some PAG members and attendees at focus groups discussing the proposals for Section 23 raised concerns about whether in practice legally constructed grant agreements are legally enforceable. Concerns about the imbalance of power between grant-providers and grant recipients were cited along with the likelihood of legal action being taken. Section 23 Part I states that it is the ability to legally enforce a grant arrangement that is important to the existence of an EGA, and not the likelihood of those rights being exercised. In some jurisdictions, agreements may be enforceable because of possible intervention by the regulator in the event of non-compliance.

BC23.36 A grant agreement that gives an NPO the right to receive a grant without having any obligations would not meet the definition of an EGA. Such agreements are referred to as other funding arrangements (OFAs). The INPAG Secretariat considered that this was appropriate, as OFAs would not give rise to liabilities or assets that could affect the timing of revenue recognition. Consequently, Part I provides guidance separately for grants and donations without EGAs and those with EGAs.

BC23.37 In some jurisdictions oral agreements have the same force in law as written agreements subject to certain factors being in place. Therefore the potential for an EGA to exist as a result of oral agreements and customary practices has been retained from the IPSAS definition of a binding arrangement.

Recognition and measurement principles where there are no enforceable grant arrangements

BC23.38 Where there are no EGAs, revenue is usually recognised immediately. This approach is consistent with both IPSAS 47 and Section 24 of the *IFRS for SMEs* Accounting Standard. The TAG and the PAG agreed with the Secretariat that an announcement by a potential grant provider of an intention to transfer resources to an NPO is not of itself sufficient to give the NPO control of those resources.

BC23.39 The use of fund accounting in the financial statements (see Sections 3–7) will affect the presentation of grants and donations. The Secretariat considered whether to include guidance on such presentation in Section 23, but concluded that a separate, new, section covering fund accounting would better meet NPOs' needs. This new section will be included in ED3.

BC23.40 The Secretariat, TAG and PAG agreed that the general recognition principles applicable to revenue from grants and donations should apply to gifts in-kind and services in-kind, with initial measurement at fair value. However, given the practical difficulties that had been identified in the responses to the Consultation Paper, NPOs would be permitted to apply permitted exceptions to certain categories of gifts in-kind because the costs of reliably measuring the value of the items on receipt may exceed the value of the information to users of the financial statements. The exceptions relate to:

(a) low value items for resale – NPOs are permitted to recognise an asset and revenue when the item is sold, measured at the amount of consideration received, instead of on receipt.

(b) items for distribution to beneficiaries or for its own use – NPOs are permitted to recognise revenue when the items are distributed or used instead or receipt.

BC23.41 For services in-kind, the practical difficulties with measurement were the primary reason for providing an exception. Given these practical difficulties, some advisory group members thought it would be appropriate to allow an exception to apply to all services in-kind. However, some advisory group members were of the view that services in-kind should be recognised, particularly where an NPO is dependent on these services as part of its operating model. Having considered these views the TAG were of the view that services in-kind that are critical to an NPO's mission should be recognised where they can be reliably measured. Additional disclosures were proposed for mission critical services in-kind that cannot be reliably measured. The exceptions proposed therefore relate to services in-kind other than those that are critical to the NPO's mission – NPOs are not required to recognise revenue, an expense or an assets from such services provided in-kind.

Revenue from transactions with enforceable grant arrangements

BC23.42 The requirements for accounting for revenue from transactions with EGAs are based on those in IPSAS 47 for the reasons set out in paragraphs BC23.9-BC23.18. Revenue is recognised as or when EGOs are satisfied. This is consistent with stakeholder's preference for a performance approach to revenue recognition as seen in the responses to the Consultation Paper (see paragraph BC23.5).

BC23.43 As noted in paragraph BC23.31, Part I adopts a slightly simplified version of the 5 step revenue recognition model that is expected to cover most EGAs. Guidance for more complex EGAs (which are expected to be less common) has been provided by applying the requirements in Part II. This is appropriate because the revenue recognition model for these types of transactions and revenue from contracts with customers is essentially the same. The additional guidance describes how Part II is to be interpreted for more complex EGAs. Examples of where additional guidance may be required include modification of agreements and the treatment of variable grant amounts.

BC23.44 The TAG also considered simplifications where there is a single EGO. Consequently, summarised guidance has been included, which will allow NPOs to apply the requirements without the need to reference the whole of the guidance.

Multi-year grants

BC23.45 A key question for NPOs is the recognition of revenue when grants are intended to be used over a number of reporting periods. The Secretariat has included Application Guidance and an example to address this issue. The recognition point will depend on a number of factors. These include:

- the terms of the agreement and the nature of the EGOs; and
- whether the agreement is capable of being separated into parts, with some parts executory and therefore not recognised until one party performs.

BC23.46 The Application Guidance and example cover these issues, allowing NPOs to determine the appropriate accounting treatment for their circumstances. The TAG was of the view that time on its own is not a performance condition that would create an EGO.

Capital grants

BC23.47 Capital grants arise where an NPO is given a grant to purchase or construct a non-current asset. The general recognition and measurement principles apply to capital grants. However, NPOs will need to carefully identify the EGOs in the EGA as these will affect the timing of revenue recognition. Application Guidance and an example are provided to assist NPOs in this matter.

Enforceable grant arrangement assets and enforceable grant arrangement liabilities

BC23.48 An EGA confers enforceable rights and obligations on the parties to the arrangement. This means that if the NPO fulfils its EGOs to the grant-provider it has a right to receive the amount of grant that is due to it from the grant provider. Likewise, the grant-provider has rights that require the NPO to meet the EGOs.

BC23.49 Revenue is recognised by an NPO when it has met its EGOs. Timing differences related to the transfer of resources may mean that the transfer of resources occurs either before or after the revenue has been recognised.

BC23.50 If consideration is received from a grant provider prior to the NPO meeting the related EGOs, a liability will be recognised by the NPO. The term 'EGA liability' is used to distinguish these liabilities from other liabilities.

BC23.51 Similarly, if the EGOs are met prior to the transfer of resources by the grant provider, an EGA asset will be recognised. Again, the term 'EGA asset' is used to distinguish these assets from other assets.

Disclosures

BC23.52 IPSAS 47 (on which Part I is based) has extensive disclosures (consistent with IFRS 15), which the Secretariat does not consider to be appropriate for INPAG. Instead the disclosure requirements included in Part I of Section 23 are based on those in Section 23 of the draft Third edition of the *IFRS for SMEs* Accounting Standard. These have been adapted for the NPO context and the focus of Part I on grants and donations. Additional disclosures have been included where there is no equivalent requirement in the *IFRS for SMEs* Accounting Standard, for example OFAs.

Part II – Revenue from contracts with customers

BC23.53 No NPO-specific issues have been identified in respect of exchange revenue and exchange revenue was not discussed in detail in the Consultation Paper. INPAG amendments to the new *IFRS for SMEs* Accounting Standard Section 23 *Revenue from contracts with customers* are therefore related primarily to changes to terminology for the NPO-context and the inclusion of a small amount of material in the preface to Section 23 as this has helped reduce duplication.

BC23.54 Otherwise, the only significant change is the inclusion of additional guidance for simpler transactions that are more likely for NPOs. This highlights which requirements of the model are not relevant for simpler transactions with the intent of improving the ease of use this Section.

Section 24 Part 1 – Expenses on grants and donations

Consultation Paper – issues identified and approaches

BC24. 1 The recognition and measurement of grant expenses was identified as a specific issue for non-profit organisations in the IFR4NPO Consultation Paper with a number of financial reporting challenges highlighted. These included:

- that grant expenses are not currently explicitly covered in international accounting standards;
- that significant judgement may be required to determine what has been promised to a grant recipient, what commitments have been created, the identification of obligating events, and when a grant expense should be recognised; and
- how and when to recognise accruals, assets and/or provisions.

BC24. 2 Respondents were supportive of the description of the issue, and also provided some additional considerations including the need to ensure that any guidance covered in-kind transfers and that grant arrangements were properly distinguished from procurement.

BC24. 3 The Consultation Paper proposed two alternative financial reporting treatments for developing guidance. The first was to base the guidance on the *IFRS for SMEs* Accounting Standard but to provide additional guidance on NPO-specific issues, and the second was to build on the first alternative but to also include additional guidance based on the principles proposed in IPSAS ED 72 Transfer Expenses.

BC24.4 Respondents again provided some additional considerations that they did not believe were adequately covered by the alternatives. These included issues related to:

- constraints not based on performance such as time in multi-year grants; and
- detail on when a donor would have an obligation to make a payment to a recipient and recognise an expense in jurisdictions where grant arrangements included 'termination for convenience' clauses that allowed the donor to terminate an agreement at any time without there being a breach of the agreement.

BC24.5 The majority of respondents supported the alternative that incorporated the principles contained in IPSAS ED 72. While more complex, they noted that it would provide better and clearer guidance on key issues such as performance obligations and multi-year grants and may also bring broader financial management improvements.

BC24.6 Following the publication of the Consultation Paper and analysis of responses, the IPSASB further developed the proposals of IPSAS ED 72 and has published IPSAS 48 *Transfer Expenses*. Following discussion with the Technical Advisory Group (TAG), the draft INPAG guidance has been based on the IPSAS Standard, mindful of the cost/benefit of the proposals for NPOs, especially with respect to any additional monitoring or reporting requirements that may be required. The TAG also noted that it would be necessary to ensure that there was a common approach taken to terms used in guidance for both expenses and revenues.

Adaptation of the IPSAS Standard

BC24.7 The first essential concept requiring adaptation of the IPSAS Standard relates to the definition of grant expenses. The IPSAS Standard establishes principles for transfer expenses. INPAG Section 24 Part I *Expenses on grants and donations* takes a similar conceptual approach but transfer expenses are redefined as grant expenses, grant recipient is defined, and an explicit reference is made to cash transfers. In response to feedback from the Practitioner Advisory Group (PAG), the definition of a grant expense was clarified such that an expense can arise from an obligation to transfer resources and not just when resources are transferred.

BC24.8 Under the definition of grant expense, it was agreed with the TAG and the PAG that the term 'grant' encompasses any cash, service, good or other asset that is transferred by the grant-providing NPO to a grant recipient without the grant-providing NPO directly receiving any cash, service, good or other asset in return. This therefore incorporates items that may otherwise be described as donations, gifts, and similar transfers of resources as well as grants. The authoritative guidance was updated to include the common terminology by which such types of transaction may be known ie, non-exchange, non-reciprocal, or non-requited transfers and expenses.

BC24.9 By making explicit reference to the fact that the grant-providing NPO will not directly receive any cash, service, good or other asset in return for the transfer, this also makes a clear distinction between an NPO's grant providing activities and those that relate to procurement.

BC24.10 The second essential concept is the use of binding arrangements from the IPSAS Standard, redefined in Section 24 as enforceable grant arrangements (EGAs). EGAs are important conceptually because the enforceable rights and obligations they contain enables the NPO to assess whether it has the right to require a grant recipient to meet an obligation in exchange for an agreed transfer of resources.

BC24.11 The Secretariat initially considered an adaptation of the IPSAS Standard, to make a distinction between general and specific grant fulfilment rights and general obligations and specific compliance obligations.

BC24.12 It was considered that a general grant fulfilment right and general obligation would relate to the overall purpose of the grant recipient. In terms of overall purpose, the grant recipient's activities supported by the transfer of resources would comprise a collective set of services, goods or other assets for internal use or external transfer, which may not individually be distinct. Collectively, however, these services, goods or other assets would usually be incremental to the services, goods or other assets that would have been available to the grant recipient without the resource transfer. It was considered that this was insufficient for an enforceable grant obligation (EGO) and therefore an EGA to exist.

BC24.13 Conversely, specific grant fulfilment rights and specific EGOs would go beyond the overall purpose of the grant recipient and focus more specifically on individual programmes, projects and activities. They would involve an undertaking by the grant recipient to use resources internally for distinct services, goods or other assets or to transfer distinct services, goods, cash or other assets to a purchaser or third-party beneficiary.

BC24.14 Following extensive debate, and mindful of the need to ensure consistency with the proposals for Section 23 *Revenue* that also draws on the concept of an EGA, the distinction between general obligations and specific EGOs was removed. EGOs are defined as a grant recipient's undertaking in an EGA to achieve a specified outcome, carry out a specified activity, to use distinct services, goods or other assets internally for a specified purpose, or to transfer distinct services, goods, cash or other assets externally.

BC24.15 General obligations instead were deemed to fall under the recognition and measurement principles for grant expenses arising from an other funding arrangement (OFA). This is because while these obligations do place constraints on the use of transferred resources by the grant recipient, they do not give rise to a present obligation for the grant recipient when the resources are transferred.

Identifying whether an enforceable grant arrangement exists

BC24.16 An essential element of the model for recognising expenses on grants and donations is the use of EGAs. An EGA is defined as 'a grant arrangement where both a donor and grant recipient have both rights and obligations, enforceable through legal or equivalent means. An EGA includes at least one EGO'.

BC24.17 This definition of an EGA allows the rights and obligations to be used as the basis of recognition for both expenses on grants and donations and for revenue from grants and (for those NPOs that receive grants from other entities or individuals).

BC24.18 A grant agreement that gives an NPO the right to receive a grant without having any obligations would not meet the definition of an EGA. Such agreements are referred to an OFA.

BC24.19 The potential for an EGA to exist as a result of oral agreements and customary practices has been retained from the IPSAS definition of a binding arrangement. In some jurisdictions oral agreements have the same force in law as written agreements subject to certain factors being in place so it was deemed appropriate by the Secretariat for these to have the same standing. The inclusion of customary practices as being sufficient for an EGA to exist is more open to debate as this is primarily based on the law of legitimate expectations that is applicable in some jurisdictions but which is usually more associated with public bodies. It has been retained but such legitimate expectations would need to be capable of being upheld by either a legal or equivalent mechanism.

Recognition and measurement principles where there are other funding arrangements

BC24.20 Recognition and measurement principles for an OFA follow the same conceptual basis as IPSAS 48 *Transfer expenses*. As well as written and oral agreements, OFAs also encompass those implied by customary practices and those situations where a grant-providing NPO transfers resources to a grant recipient without there being any agreed or implied arrangement in place. The TAG and the PAG were both supportive of the requirement put forward by the Secretariat that a constructive obligation to transfer resources that results in the recognition of a provision would require the recognition of a grant expense by the grant-providing NPO, but that additional guidance was necessary around general statements of intent to provide resources and how this interacted with EGAs. This has been provided in Application Guidance and Implementation Guidance and illustrative examples.

BC24.21 The TAG discussed whether it would be more appropriate for a grant-providing NPO to measure a grant expense at the fair value of the previously controlled resources rather than at their carrying amount. The TAG concluded that it was appropriate to follow the same measurement principle as the IPSAS Standard and measure at their carrying amount. Also, measuring at fair value would not be expected to impact on surplus or deficit for the period and any benefits would likely be outweighed by additional costs.

Recognition and measurement where there are enforceable grant arrangements

BC24.22 EGAs may vary significantly in complexity, but there are common principles that will be applicable to all. The Secretariat has made clear that an EGA will be wholly unsatisfied if the grant-providing NPO has not yet transferred and is not yet obligated to transfer and amount of resources to the grant recipient, and the grant recipient has not yet met any of its stated EGOs in the EGA. Where this is the case, nothing will be recognised, although the disclosure requirements will still apply.

BC24.23 A key requirement will be for the grant-providing NPO, at the inception of the EGA, to determine its distinct grant fulfilment right(s) to have the grant recipient meet an EGO(s), and the amount of resources that it is required to transfer (in cash, services, goods or another asset) to the grant recipient for meeting each right. It is the nature of these grant fulfilment rights that dictates subsequent recognition and measurement.

BC24.24 The Secretariat recognises that NPOs may face difficulties in:

- determining if a grant agreement includes one or more EGOs and hence is an EGA;
- deciding on suitable methods for estimating stand-alone amounts; and
- understanding when the grant recipient has met its obligations meaning that grant fulfilment rights have been met.

While these will vary depending on the substance of each transaction, additional guidance has been provided in the Implementation Guidance and illustrative examples.

BC24.25 Authoritative guidance has also been provided for the following circumstances:

- payments of grant over more than one financial year;
- variable consideration;
- capital grants; and
- rights and obligations that are outside of the control of the grant-providing NPO.

Payments of grant over more than one financial year

BC24.26 The impact on the timing of the recognition of grant expenses was a significant issue raised through the Consultation Paper, particularly where the donor makes a grant payment in advance that covers multiple time periods.

BC24.27 Section 24 Part I requires that a grant expense be recognised by the grant-providing NPO for the total amount of the resources that must be transferred under the EGA to the grant recipient for the obligations it has met. This is regardless of the timing of the transfer of the resources from the grant-providing NPO.

BC24.28 As noted in BC24.22, where neither party has met any obligations under the EGA, the grant-providing NPO will not recognise any transactions associated with the EGA.

BC24.29 Where an obligation has been met by the grant recipient prior to the transfer of resources by the grant-providing NPO, the grant-providing NPO must recognise a liability for the grant expense. Where resources have been transferred by the grant-providing NPO to the grant recipient prior to the grant recipient meeting its obligation a prepayment asset will have previously been recognised. This will be derecognised when or as the grant expense is recognised.

BC24.30 This reflects the view of the Secretariat that a grant expense will not be recognised where grant payments for later years are subject to the grant recipient satisfying obligations that have not yet been met. This is because under the terms of the EGA the grant-providing NPO may be able to avoid the transfer of resources.

Capital grants

BC24.31 Capital grants was another area of concern raised by consultation respondents. A capital grant arises from an EGA in which a grant-providing NPO transfers cash or another asset to a grant recipient with a requirement that the grant recipient acquires or constructs a non-current asset that the grant recipient will then control.

BC24.32 Although there is a requirement for the grant recipient to acquire or construct an asset, from the perspective of the grant-providing NPO, the recognition of a grant expense for an EGA involving a capital grant is the same as for any other grant expense.

BC24.33 Complications may arise in recognising the grant expense where the grant fulfilment rights will be met as the asset is being built. The grant expense will need to recognised by the grant-providing NPO based on an agreed methodology for the measurement of progress made by the grant recipient. While no methodologies are included in the authoritative guidance, the implementation examples include one possibility that was discussed with the PAG.

BC24.34 Constraints in an EGA may prevent the grant recipient from disposing of an acquired or constructed asset or using it for purposes other than those specified by the grant-providing NPO. Such constraints may mean that the grant recipient does not control the capital asset. This is a complex area that will depend on the individual circumstances of each EGA and the application of professional judgement.

Variable consideration

BC24.35 Variable consideration can arise where the amount that the grant-providing NPO is obliged to transfer to the grant recipient varies for items such as incentives, penalties or other similar items. It can also arise if the grant-providing NPO's obligation to provide the resources is contingent on the occurrence or non-occurrence of a future event.

BC24.36 If the grant-providing NPO determines that it is more likely than not that a present obligation exists for the payment of variable consideration, then a liability of uncertain timing or amount will need to be recognised. The Secretariat is of the view that paragraphs G21.8-G21.12 of Section 21 *Provisions and Contingencies* are appropriate for the grant-providing NPO to estimate an amount of variable consideration.

Rights and obligations that are outside of the control of the grant-providing NPO

BC24.37 The same conceptual recognition principles as variable consideration apply where EGAs contain rights and obligations that are outside of the control of the grant-providing NPO. As discussed with the TAG, this can include factors such as a requirement for a grant recipient to find match funding.

BC24.38 In such circumstances the Secretariat's view is that if a present obligation exists and the transfer of resources is probable, the grant-providing NPO should follow the requirements of Section 21 *Provisions and Contingencies*. The probable existence of an obligation may depart from existing practice in some jurisdictions where, for example, in an arrangement that requires matched funding, a liability would not be recognised until it was certain that the match funding had been secured.

Prepayment assets and liabilities

BC24.39 A grant expense is recognised when the grant recipient has met its EGOs. Timing differences related to the transfer of resources may mean that the transfer of resources occurs either before or after the grant expense has been recognised.

BC24.40 The concept of a liability when the grant expense is recognised before the transfer of resources occurs is uncontroversial. However, the nature of a prepayment asset that is recognised when the transfer of resources is made to the grant recipient before a grant expense is recognised requires consideration.

BC24.41 The prepayment asset reflects the grant-providing NPO's right to require the grant recipient to meet its EGOs given that the grant-providing NPO has already met its own obligation to transfer resources. As such, it is not a financial asset. It may subsequently be reclassified to a financial asset if the grant recipient is unable or unwilling to meet its obligations and the grant-providing NPO has the right to receive cash back from the grant recipient.

Principal agent considerations

BC24.42 The importance of principal and agent considerations and the approach taken in INPAG are discussed in BC23.22 to BC23.27.

BC24.43 As noted in BC23.25, to be a principal an NPO is required to obtain economic benefits or service potential from an economic resource in order to further its own purpose and achieve its own objectives, and to be able to do so without requiring authorisation from another entity. Where a grant-providing NPO controls the economic resources that are transferred to the grant recipient, it is proposed that the grant-providing NPO will be a principal in the transaction and the recognition, measurement, presentation and disclosure requirements of INPAG Section 24 Part I relating to grant expenses will apply.

BC24.44 Where a grant-providing NPO does not control the economic resources, it is likely to be acting as an agent for another entity. In this situation it is proposed that the grant-providing NPO will follow the requirements in Section 24 Part I for NPOs acting as an agent and will only recognise in expenses the costs incurred in the administration of the agency arrangement.

BC24.45 In accordance with the agreement with the TAG that guidance would be integrated into those sections where guidance on principal-agent relationships is required, Section 24 Part I *Expenses on grants and donations* includes relevant guidance.

Disclosures

BC24.46 Disclosure requirements are driven by user needs and their ability to understand the nature, amount, timing and any uncertainty arising from grant expenses. Quantitative disclosures for grant expenses and associated assets and liabilities are proposed as well as narrative-based disclosures. These are focused on describing the purpose of material arrangements and the features of these material arrangements that are useful to users for accountability and decision-making purposes. This includes variable consideration, payment terms or resources to be transferred. Additional disclosures are also required where there are grant transactions arising from principal agent arrangements.

BC24.47 Following review of the first draft of the authoritative guidance, a TAG member noted that the proposals in Section 35 *Narrative Reporting* for 'sensitive information' may also be required in relation to aspects of grant expenses disclosures. The Secretariat agrees with this position and a sensitive information disclosure exemption has been included in the authoritative guidance. An NPO may not make disclosures when to do so would compromise the safety or wellbeing of individuals working/volunteering for and with the grant-providing NPO, or those to whom it provides cash, goods, services and other assets, because the information is sensitive and/or could prejudice the ability of the grant-providing NPO to deliver its mission.

BC24.48 A grant-providing NPO is required to disclose information related to grant expenses that does not result in sensitive information. This includes disclosures that might identify failures in organisational governance, performance or financial management that could for example have a negative impact on its ability to fundraise its operations.

Section 25 – Borrowing costs

BC25.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Borrowing costs was not included as a prioritised topic. No major editorial changes are proposed for borrowing costs, with only minor changes to terminology.

Section 26 – Share-based payments

BC26.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Share-based payments was not included as a prioritised topic.

BC26.2 In reviewing the *IFRS for SMEs* Accounting Standard Section on this topic, there were a number of additional considerations in relation to share-based payments. Section 26 on share-based payments specifies the accounting for all share-based payment transactions. This includes arrangements with employees where the provision of shares in the entity is part of their remuneration package. It also provides for scenarios where shares are used to pay other external parties including vendors. The Secretariat's considerations in relation to this topic stemmed from the expected characteristics of NPOs and as a result, the likely types of share-based payments that might exist.

BC26.3 As described in the basis for conclusions to Section 2, it has been considered possible but unlikely that an NPO will have equity claims and even more unlikely that it has traded shares with commercial value. Where such equity does exist then some guidance on share-based payments could in theory be beneficial. Also, given the characteristics of an NPO it would not be expected that share-based payments form a part of employee remuneration. It was originally proposed instead that this Section be amended to remove references to employees, including share appreciation rights and share options.

BC26.4 An approach that removes references to employees would also require some further consequential adjustments to reflect the role of equity for NPOs. This would in particular affect paragraphs relating to vesting and 'vesting conditions'.

BC26.5 Given the low level of likelihood that an NPO has shares and the even lower likelihood that these shares are used to make share-based payments, there is a key question as to whether this Section is needed.

BC26.5 The TAG considered whether INPAG should include a section on share-based payments and debated whether in the incredibly rare circumstances where an NPO has share-based payments that INPAG should default to alternative guidance in accordance with paragraph GP26. The TAG was of the view that including a section on share-based payments could cause confusion given the stated characteristics of NPOs and the expected role of equity and add unnecessary complexity to INPAG. Therefore, on balance, the TAG was of the view that the Section should be removed, as it is not likely to be needed.

Section 28 – Employee benefits

BC28.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Employee benefits was not included as a prioritised topic.

BC28.2 While a full review of the *IFRS for SMEs* Accounting Standard Section on this topic was not carried out, a high level review identified that there were a number of additional considerations in relation to employment benefits. These considerations mostly stemmed from the expected characteristics of NPOs and as a result, the likely types of remuneration arrangements that might exist with employees.

Scope of the Section

BC28.3 In the Basis for Conclusions for Section 26 *Share-based payments,* it is proposed that Section 26 is removed particularly as the nature of NPOs is such that employees are unlikely to participate in remuneration arrangements that involve shares. Consequently, references to share-based payments have been removed from Section 28 of INPAG.

Short term employee benefits

BC28.4 The characteristics of an NPO require that any surpluses (profits) are used to further the objectives of the NPO and for the benefit of service beneficiaries. For this reason, all references to profit-sharing arrangements are also proposed to be removed from Section 28 of INPAG. References to bonuses have been retained as this might be part of a remuneration structure, but not based on a profit-sharing arrangement.

Post-employment benefits

BC28.5 Section 28 includes guidance on post-employment benefits and the accounting for defined benefit pension schemes. The *IFRS for SMEs* Accounting Standard allows a policy choice for in-year changes to the amounts to be recognised for defined benefit pension schemes. Specifically, these changes can be included in either the profit or loss or in other comprehensive income.

BC28.6 Earlier discussions with the TAG highlighted the desire for simplicity by some users of NPO financial statements. The TAG discussed the possibility of removing an accounting policy choice and requiring actuarial changes from the revaluation of defined benefit pension schemes to be presented in the Statement of Changes in Net Assets, to achieve this desire for simplicity.

BC28.7 The TAG were, however, of the view that removing a policy choice was effectively introducing a rebuttable presumption. With the expectation that few NPOs will have defined benefit pension schemes and those that do may have more complex stakeholders requirements, the TAG were of the view that it was appropriate to maintain the policy choice.

BC28.8 As a consequence, the draft INPAG allows a choice between changes being recognised in the Statement of Income and Expenses or Statement of Changes in Net Assets.

BC28.9 Paragraph G28.37 refers to group arrangements and the possibility that other entities are following other GAAP. This paragraph has been amended to require that the allocation of employee benefit expense can only be made if the controlling NPO is following INPAG.

Section 29 – Income tax

BC29.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Income tax was not included as a prioritised topic. The updates to Section 29 *Income Tax* are largely to make them NPO specific with consequential changes to terminology.

BC29.2 In the *IFRS for SMEs* Accounting Standard Section 29 *Income tax* refers to taxable profits and losses. The term 'taxable profits and losses' is the term that is commonly used by tax offices that cover all organisations in the economy. Elsewhere in INPAG references to profit and losses have been amended to surplus and deficit. As this is a tax regulation term rather than an accounting term it was proposed to retain the term unchanged. This was discussed with the TAG and fully supported.

BC29.3 Paragraph 29.3 of the *IFRS for SMEs* Accounting Standard scopes out Section 24 *Government Grants*. With the proposal that Section 24 is repurposed and that the accounting for government grants is dealt with as part of a comprehensive section on revenue, this reference has been removed from Section 29 of INPAG.

BC29.4 The purpose of paragraph 29.3 is to specifically address timing differences. Additional guidance on timing differences arising from revenue may be appropriate, as well as additional guidance on gifts in-kind and services in-kind. It was therefore proposed that, as needed, additional text is developed (either core guidance or application guidance) as a consequential change as the drafting of the guidance on revenue is developed. However, no specific issues relating to government grants and income tax have as yet been identified.

BC29.5 As INPAG allows for some items of income and expense arising from fair value adjustments to go through the Statement of Changes in Net Assets, INPAG has been amended to allow for a tax expense to be recognised in the Statement of Changes in Net Assets, consistent with the text requiring that the tax expense appears alongside the related transaction. If it becomes clear that a tax expense is unlikely to arise in relation to these transactions, this amendment will be removed.

Section 30 – Foreign currency translation

BC30.1 A number of respondents to the Consultation Paper issued in January 2021 provided feedback that foreign currency translation should be treated as a priority topic for inclusion in INPAG. The PAG strongly supported the inclusion of this topic in INPAG, given the significant practical difficulties experienced by NPOs.

BC30.2 The TAG in its consideration of this feedback sought to understand the nature of the concerns raised. Through these discussions it concluded that the issues being raised were about the application of the accounting principles for foreign currency translation in the NPO context, rather than the principles themselves. This was particularly focused on the presentation and disclosure of foreign currency gains and losses associated with grant funding.

BC30.3 As a consequence it was decided to prioritise this topic for inclusion in INPAG, but to focus on presentation and disclosure. It was agreed not to review the principles for accounting for foreign currency translation in the *IFRS for SMEs* Accounting Standard but instead develop application guidance and implementation guidance.

BC30.4 Reflecting this decision, the draft Third edition of Section 30 of the *IFRS for SMEs* Accounting Standard has been modified to reflect NPO related terminology and the scope of the financial statements proposed for INPAG. It has also been updated to reflect the likely sources of NPO income and expense such as grants and donations. It has not been the subject of a full update.

BC30.5 The main amendments to this Section are to allow for the impact of fund accounting, which is proposed to be addressed in a separate section of INPAG. Exchange gains or losses arising on monetary items relating to enforceable grant arrangements (EGAs) and those other funding arrangements (OFAs) (grant arrangements) shall be presented consistent with the presentation of the transaction when this is prescribed by Section 36 *Fund accounting*.

BC30.6 Consideration was given to showing an exchange gain or loss on grant arrangements that are required to be presented as funds with restrictions as funds without restrictions. This was to show that an NPO may have to fund a loss on from its unrestricted resources. Whilst this had some benefits, it had the potential to create complexity and ultimately not provide the transparency over such gains and losses that was being sought. As a consequence, it is proposed that the presentation of any exchange gains or losses follow the presentation of the grant arrangement to which it relates.

BC30.7 There is a new requirement to disclose separately the impact of changes in exchange rates where there is a deficit or surplus on a grant arrangement that is required to be presented within funds with restrictions. The requirement to disclose these changes in exchange rates gains or losses separately, is intended to provide transparency of exchange rate exposures relating to grant arrangements. This transparency will improve the understanding of the source and use of an NPO's funds, which reflects the concerns raised by respondents to the Consultation Paper. The Secretariat recognise that the benefit of this requirement needs to be proportionate to the effort required, particularly for smaller NPOs.

BC30.8 Application Guidance has been developed to provide additional guidance on these key changes to the *IFRS for SMEs* Accounting Standard. This guidance explains that grant arrangement liabilities from EGAs are non-monetary items. This is because they reflect the revenue received or receivable or enforceable grant obligations (EGOs) in an EGA that need to be met by the grant recipient. The Secretariat initially considered whether EGA liabilities were monetary items, but the INPAG Glossary defines monetary items as units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency. Since no future cash flow is expected to settle these particular liabilities, they are considered a non-monetary item.

BC30.9 As a consequence, grant arrangement liabilities relating to EGAs measured in a foreign currency are to be recorded at historical cost using the exchange rate at the date of the transaction as set out in G30.10(b). This means that they do not need to be retranslated at each balance sheet date.

BC30.10 The Secretariat examined the treatment of the increased expenses required to meet the requirements of an EGA when exchange rates change. The Secretariat initially considered whether the additional obligation from the increased expenses should be classified as an EGA liability. However, as the additional liability does not change the initial revenue recognised and related EGOs, this was not considered appropriate.

BC30.11 The Secretariat considered instead whether the additional expenses created an onerous requirement under an EGA. It considered whether the recognition criteria for a provision, as set out in G21.4, would be met. As it is likely that criteria relating to the existence of the obligation and its probable occurrence would be met and the amount of additional expense can be reliably measured at the balance sheet date, the Secretariat concluded there would most likely be a present obligation under the grant arrangement. As a consequence, a provision for an onerous contract is an appropriate classification. The Secretariat were of the view that the corresponding expense is presented consistent with the presentation of the original grant arrangement.

BC30.12 The Secretariat considered the situation where a change in exchange rate changes means that a lower level of spend in the local currency is required to deliver the obligations in the grant arrangement. Where the grant arrangement requires that the grant recipient must spend all the grant received in the local currency, the NPO will need to incur additional expenses in that local currency to satisfy the grant arrangement, even though the original obligations have been met. The Secretariat considered that the additional expenses should follow the presentation of the original grant arrangement to show the complete impact of the grant arrangement.

BC30.13 Where there is an exchange gain and no additional expenses are required, if there are no other offsetting transactions, an individual grant arrangement will show a surplus. When the grant arrangement comes to an end, if the grant arrangement has been presented as funds with restrictions any surplus on the specific grant arrangement will be transferred to funds without restrictions. In this way the surplus will become available for any activity undertaken by the NPO.

BC30.14 A scenario of repaying an exchange gain to the grant-provider was considered. The Secretariat is of the view that a refund is a monetary item and should be distinct from other liabilities under a grant arrangement. It concluded that the repayment should first reduce the amount of any revenue recognised under that grant arrangement and presented consistent with the revenue initially recognised.

BC30.15 As it is possible that an exchange gain is greater than the original revenue or greater than the revenue recognised to date (where there are unfulfilled EGOs), the Secretariat proposed that where there are EGOs to be satisfied, the excess amount should be recognised as a change to the EGA liability. The Secretariat were of the view that under an OFA, a repayment to a grant-provider because of an exchange gain would be unlikely. If, however, it is required, the shortfall would be treated as a liability and expense. Any impact on revenue or expense is proposed to be presented on the in line with the presentation of the original grant arrangement. This presentation will provide transparency about the adequacy of funding.

BC30.16 Implementation guidance is provided to: explain how to account for transactions with a different denomination and settlement currencies; provide guidance where changes in exchange rates result in differences between revenue received and the obligation to incur costs; to provide guidance on disclosure of exchange rate gains and losses as they relate to grant arrangements; to provide guidance on re-translation of foreign currency monetary assets and liabilities relating to grant arrangements; for the judgements applied in identifying an NPO's functional currency; and to clarify the scope and limitations of the use of a presentation currency other than the function currency. To illustrate the conclusions reached about the presentation and disclosure of foreign exchange gains and losses, examples have also been created.

Section 31 – Hyperinflation

BC31.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Hyperinflation was not included as a prioritised topic.

BC31.2 No major editorial changes are proposed for hyperinflation, with minor changes to terminology and to align with other Sections. The main changes are to reflect the structure of the balance sheet proposed for NPOs in INPAG and the names and scope of the financial statements as they relate to income and expenses.

Section 32 – Events after the end of the reporting period

BC32.1 The IFR4NPO Consultation Paper proposed that only prioritised topics would be fully reviewed for the first issue of INPAG. Events after the balance sheet date was not included as a prioritised topic.

BC32.2 There were no significant issues arising from the high-level review of this Section. Other than terminology, changes reflect alignment with other INPAG Sections. Key changes to note are:

(a) the sources of bankruptcy have been expanded to include 'grant provider'. This reflects the importance of grant providers to an NPO and that the bankruptcy of a grant provider could have flow- on effects for an NPO;
(b) 'trade' has been deleted against 'trade receivable' consistent with Section 4;
(c) references to profit sharing have been removed consistent with the amendments made to Section 28;

(d) references to dividends have been removed as this is not expected to be a feature of NPOs who do not operate for returns. Amendments to the draft text allow for the possibility of an NPO making a distribution to holders of equity claims. This is expected to be extremely rare and will be reviewed to take account of feedback on equity as requested as part of Exposure Draft 1 (ED1); and

(e) an amendment has been made to reflect that it is not an entity's owners that has the power to amend the financial statements after issue, but there may be 'others' who have this type of power. This is to reflect that ownership is not a key driver of how an NPO operates.

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