



**International  
Non-Profit  
Accounting  
Guidance  
Part 1  
Basis for  
Conclusions**

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## INPAG

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## Preface

### Introduction

- BC P.1 This Basis for Conclusions summarises the factors considered during the development of the Exposure Draft.
- BC P.2 It includes details of any changes made to the approach that were set out in the IFR4NPO Consultation Paper Part 1 and the development of financial reporting options that were included in Part 2 as a result of feedback from respondents. The discussion has been provided to enable respondents to this Exposure Draft to understand the evolution of the proposals from the Consultation Paper to Exposure Draft stage.
- BC P.3 This Basis for Conclusions will be updated following the Exposure Draft stage, in the light of comments received and subsequent deliberations.

### Governance framework

- BC P.4 The IFR4NPO project, which is being funded by donations and grants, is being delivered jointly by a Project Secretariat formed of two non-profit organisations (NPOs), the Chartered Institute of Public Finance and Accountancy (CIPFA) and Humentum.
- BC P.5 A Steering Group comprising executive and non-executive members governs the project. The Steering Group provides oversight to the delivery of the project, ensuring that the project partners remain focused on the project objectives and that these are delivered cost effectively. The project is also being supported by a Technical Advisory Group, a Practitioner Advisory Group, a Donor Reference Group and Country Champions.
- BC P.6 As the IFR4NPO project has moved to the Exposure Draft stage, the INPAG Secretariat has been formed by CIPFA to undertake its development.
- BC P.7 The INPAG Secretariat uses professional judgment in reaching its conclusions. As part of due process, it consults with the Technical Advisory Group on technical financial reporting considerations. The aim of these consultations is to achieve consensus on the changes proposed. The INPAG Secretariat also consults with the Practitioner Advisory Group on practical financial and operational implications for NPOs. The Steering Group is informed of any risks arising to the project from significant disagreements or issues that impact project delivery. Ultimately, CIPFA is responsible for the approval of INPAG and related documents.

### Accrual-based guidance

- BC P.8 INPAG is accrual-based guidance. The additional information accrual accounting can provide improves the quality and transparency of financial reports and information. Accrual accounting is also best able to address NPO-specific issues and improve comparability.
- BC P.9 Respondents to the IFR4NPO Consultation Paper were asked to highlight practical challenges that NPOs might face in implementing accrual-based guidance.
- BC P.10 Respondents noted that some NPOs and their staff would potentially not have the capacity and capability to move to and maintain an accruals-based accounting system. This was deemed a particular issue for those NPOs reliant on volunteer and/or non-specialist staff who may not have the skills and technical expertise required to operate finance systems on an accrual basis, or understand the accrual based financial reports that they produced.
- BC P.11 Respondents also commented that access to, and the affordability of, the education and training needed to apply accrual accounting would be challenging in many jurisdictions, and that the resources needed to introduce the computer software and hardware that would be required for accrual accounting would be scarce for many NPOs. The additional costs associated with compliance and audit of accrual-based financial reports was also noted as posing additional burdens.

- BC P.12 In addition to practical challenges, some respondents to the IFR4NPO Consultation Paper also raised conceptual challenges to the use of accruals. The most common was that NPOs with less complex financial reporting needs were unlikely to gain any significant benefit from accrual-based guidance. Respondents noted that this was because the stakeholders of these NPOs would have little understanding of accrual-based financial information and their transactions were simple and adequately accounted for on a cash-basis.
- BC P.13 It was also noted by respondents that for many NPOs, donors and regulators would continue to require cash or modified cash basis reports to understand the utilisation of funding or for tax or other purposes.
- BC P.14 These practical and conceptual issues, and the need to ensure that the guidance provides for proportionate financial reporting requirements that can be applied by a wide range of NPOs in many jurisdictions, have been key considerations when developing INPAG.
- BC P.15 For some NPOs, cash-based or modified cash-based accounting will continue to be appropriate given the level of the financial reporting needs of their users. Decisions on which entities are required or permitted to use INPAG rests with legislative and regulatory authorities and standard setters in individual jurisdictions. It will be for these authorities to determine whether the accrual-based guidance within INPAG in whole, or part, should apply and to which entities. An NPO will, however, only be able to state that its general purpose financial reports are compliant with INPAG if it complies with all of the requirements of INPAG.
- BC P.16 As noted by respondents, there will continue to be a requirement for other forms of reporting by NPOs, including potentially reporting using a different accounting basis. INPAG can, however, support a reduction in the reporting burden on NPOs, as greater consistency in requirements at the level of general purpose financial reports will enable a range of stakeholders to make greater use of these financial reports.
- BC P.17 The introduction of common financial reporting standards also has the potential to reduce diversity in different reporting requirements if utilised by donors for any continued special purpose financial reports requested from NPOs.
- BC P.18 While there is a cost to producing accrual-based financial information, for many NPOs these will be significantly outweighed by the benefits to them and the users of this information or accountability and decision-making purposes.

## **General purpose financial reports**

- BC P.19 INPAG provides financial reporting guidance for the production of general purpose financial reports. General purpose financial reports present management commentary and other narrative reporting alongside the financial information contained in the general purpose financial statements.
- BC P.20 General purpose financial reports will provide users with information to allow a meaningful understanding of an NPO's nature, objectives, strategy, risks, and performance. When used effectively, management commentary and other narrative reporting provides a range of performance measures and indicators consistent with underlying financial information. This can give users a clearer view of the impact of the NPO's projects, programmes, and wider activities.
- BC P.21 Respondents to the IFR4NPO Consultation Paper recognised that it was important to include non-financial information reporting within INPAG as its inclusion would be beneficial in enabling NPO financial reports to meet the broader needs and expectations of users.
- BC P.22 Guidance on the requirements for non-financial information reporting is included in Section 35 *Narrative Reporting*

## The use of existing international frameworks

- BC P.23 The IFR4NPO project does not currently have sufficient resources to develop, from first principles, a conceptual framework and complete suite of NPO financial reporting standards. The use of existing international frameworks is a pragmatic approach given the time and resource constraints on the IFR4NPO project. There are several examples from across the globe of jurisdictions that have adapted existing international frameworks to develop NPO financial reporting frameworks that demonstrate that an adaptive approach can succeed.
- BC P.24 There are significant advantages in being able to utilise the work that has been undertaken to develop and maintain these international frameworks, including the extensive consultation and best practice development processes associated with these frameworks, the potential for familiarity amongst preparers and users, and the existence of extensive educational and support material.
- BC P.25 While jurisdictional-level frameworks are also used to develop INPAG in specific areas, international frameworks are considered the best start point because they are developed with international rather than jurisdictional-level application in mind and are subject to international rather than jurisdictional-level due process.
- BC P.26 It is recognised that existing international frameworks have been developed to provide financial reporting standards for for-profit organisations and government entities based on their respective sector contexts and the needs of their primary users of financial statements. In developing INPAG, the primary users of NPO general purpose financial reports have been identified and their financial and non-financial information needs articulated. The primary users of NPO general purpose financial reports are covered in Section 2 *Concepts and pervasive principles*.

## The use of the *IFRS for SMEs Accounting Standard*<sup>1</sup> as the foundational framework

- BC P.27 INPAG is a single set of standalone financial reporting guidance, that can be applied to preparing general purpose financial reports of NPOs without access to or knowledge of other financial reporting frameworks. Assessment of the existing international frameworks showed that the use of the *IFRS for SMEs Accounting Standard* as the foundational framework for INPAG had the most benefits, as it provides a shorter, simplified standalone Standard with less onerous disclosure requirements.
- BC P.28 Where INPAG does not yet directly address a topic, the relevant Sections in the *IFRS for SMEs Accounting Standard* have been retained for now. For the topics within the IFR4NPO project scope, other international and jurisdictional-level frameworks are used to develop financial reporting guidance where NPO-specific financial reporting issues have not been comprehensively or appropriately dealt with in the existing *IFRS for SMEs Accounting Standard*, or where there is no related Section in the *IFRS for SMEs Accounting Standard*.
- BC P.29 Several respondents to the IFR4NPO Consultation Paper questioned whether IPSAS would be more appropriate as the foundational framework. Had an “IPSAS for SMEs” standard been available, that could have potentially provided a better solution than the *IFRS for SMEs Accounting Standard*. Such a framework does not currently exist. Whilst recognising that IPSAS addresses some NPO specific accounting issues, it was considered that the benefits of utilising the shorter, simpler, standalone *IFRS for SMEs Accounting Standard* outweighed this potential benefit. IPSAS is a key source of financial reporting guidance on public benefit related financial reporting issues.
- BC P.30 The process for using the *IFRS for SMEs Accounting Standard* as a starting point, with terminology changes and modification made where necessary for the NPO context is similar to the IPSASB’s well-established process for using relevant IASB documents as a start point for its guidance. The process used by the INPAG Secretariat can be found in **Process for developing the International Non-Profit Accounting Guidance through changes to the IFRS for SMEs Accounting Standard**.

<sup>1</sup> All references to the *IFRS for SMEs Accounting Standard* in this document are to the Third edition of the *IFRS for SMEs Accounting Standard* exposed in September 2022 unless otherwise stated.

## Section 1 – Non-profit organisations

### Intended scope of the INPAG

BC 1.1 INPAG application can be beneficial for all non-profit organisations no matter their size or jurisdiction. For those organisations that are small, have simple stakeholder needs, and where there is no fiduciary obligation, INPAG and its accrual requirement may be more than is needed to meet accountability requirements. For these organisations INPAG provides useful guidance that NPOs may draw on and move to over time. More complex organisations that meet the public accountability definition in IFRS need to follow full IFRS Accounting Standards, or equivalent national Generally Accepted Accounting Practice (GAAP). However, INPAG may provide useful guidance for NPO specific transactions that can be adopted. The decision about which entities apply INPAG rests with legislative and regulatory authorities and standard setters in individual jurisdictions.

### Description of non-profit organisations

BC 1.2 A broad characteristics approach was developed for INPAG to identify the entities that INPAG is expected to primarily benefit. This has enabled a focus on how to best meet the needs of the users of the general purpose financial reports of entities with these characteristics.

BC 1.3 Respondents to the IFR4NPO Consultation Paper were overwhelmingly supportive of this approach. It was recognised that a narrower focus on entities with, for example, a specific legal status as an NPO could exclude many entities that could benefit from INPAG and that not all jurisdictions have a relevant legal framework that would permit a narrow legal status approach. In addition, entities that are deemed to be NPOs in one jurisdiction's legal code may not be deemed to be an NPO in another jurisdiction, despite them being structured in the same way and carrying out the same activities.

BC 1.4 Based on the feedback to the Consultation Paper, changes have been made to the broad characteristics that were included in the IFR4NPO Consultation Paper. Respondents noted that the broad characteristics included in the Consultation Paper could have unintentionally included or excluded entities. This was partly due to the presentation of the characteristics as "and/or" statements, concern about how each individual characteristic might be applied and uncertainty as to what was meant by key terms included in the characteristics.

BC 1.5 Some respondents, for example, noted that the characteristics might call for the inclusion of a wide range of entities that they did not expect to be an appropriate focus for the Guidance. These included:

- government entities that should follow public sector accounting standards;
- private sector entities like hospitals that provide services for the public benefit or use assets to fulfil a social purpose, but which would be expected to follow private sector accounting standards; and
- certain types of organisations providing benefit only to a small and privileged membership that could be deemed too exclusive to be viewed as a non-profit organisation.

BC 1.6 As well as scoping in entities that they did not believe were an appropriate focus for INPAG, some respondents also noted that the broad characteristics currently proposed might exclude entities that they believed should be within scope. Examples included:

- entities providing goods for the benefit of the public and not services;
- grant-giving bodies providing funding to other NPOs; and
- entities that work to preserve and enhance the environment, heritage assets, or other areas that might not immediately be deemed to be for a "social" purpose.

BC 1.7 In addition to raising the possibility of unintended consequences with respect to scope, some respondents also questioned whether all of the broad characteristics were characteristics in their own right or should more appropriately be seen as indicators of other characteristics or consequential to activities driven by them.

## Broad characteristics

- BC 1.8 The broad characteristics were amended so that they are no longer presented as “and/or” statements. Rather, an entity is expected to display all the broad characteristics if it is to be described as an NPO for the purpose of INPAG.
- BC 1.9 The broad characteristics of NPOs were revised as follows:
- they have the primary objective of providing a benefit to the public;
  - they direct surpluses for the benefit of the public; and
  - they are not government or public sector entities that should prepare general purpose financial reports under public sector financial reporting standards.

## Primary objective of providing a benefit to the public

- BC 1.10 Having a primary objective of providing a benefit to the public is an essential characteristic of an NPO, and in many cases this will be specified in the founding documents of the entity. Through the services and goods it delivers in pursuit of its primary objective, the NPO will provide a benefit to the general public, community or wider society, and it is the general public, community or a particular section of the community who will be the primary beneficiaries of the entity’s activities. The primary objective of an NPO will not be for financial or other economic returns, though some incidental private benefits may be provided in the pursuit of its purpose.
- BC 1.11 This contrasts with for-profit entities, which have the primary objective of generating a financial surplus in order to provide a financial return to equity holders or others for private benefit. It is these equity holders, or other providers of resources to the entity such as holders of debt or suppliers, who will be the primary beneficiaries of the activities of the entity.
- BC 1.12 In response to the feedback received on the IFR4NPO Consultation Paper, this characteristic explicitly notes that an entity may provide goods for public benefit as well as services. The characteristic also makes clear that depending on the services and goods provided by the entity, the section of the public that benefit from the NPOs activities could be quite limited and even restricted to a defined membership of the entity. Where the ‘public’ is limited in this way it is likely to be necessary to carefully examine the other characteristics and indicators to ensure the entity is an NPO.

## Direct surpluses for public benefit

- BC 1.13 NPOs will need to be financially viable to meet their objectives. This may include undertaking activities which generate a profit or financial surplus such as selling goods and services or holding and trading financial assets. These should be used to support the primary objective of providing a benefit to the public) Generating profits or a financial surplus should not be the primary objective of the NPO.
- BC 1.14 This contrasts with for-profit entities, where generating profits is a primary objective and financial returns are generally distributed to providers of economic resources such as contributors of equity.

## Not government or public sector entities that should prepare general purpose financial reports under public sector accounting standards

- BC 1.15 Responses to the IFR4NPO Consultation Paper noted that it was unclear whether government entities were expected to be within scope of INPAG.
- BC 1.16 In some jurisdictions, financial reporting guidance for NPOs is included as part of a broader framework of standards for all ‘public benefit entities’ which includes government and public sector entities as well as non-profit organisations. Where this is the case, however, there is usually a clear distinction made between those standards that are applicable to entities that are controlled by government and other public benefit entities which are not.



BC 1.17 The IFR4NPO project does not have an objective of providing financial reporting guidance to government entities, nor to examine those transactions and economic events that are only relevant in the public sector context. For most government and public sector entities, the accountability and decision-making needs of the users of their general purpose financial reports are likely to be best met by preparing them under public sector accounting standards.

## Indicators

BC 1.18 Some of the broad characteristics included in the IFR4NPO Consultation could more appropriately be seen as indicators of other characteristics or consequential to activities driven by them. Implementation Guidance may assist in cases where there may be uncertainty as to whether the broad characteristics have been met.

BC 1.19 “Indicators” were therefore developed to assist entities in determining whether they are within the intended scope of applicability of the INPAG. These are intended to assist in decision making where it is not clear if an entity fully displays the broad characteristics of an NPO.

BC 1.20 Two of these, namely ‘voluntary funding’ and ‘holding and using assets for the benefit of the public’ were previously included as broad characteristics in the IFR4NPO Consultation Paper. ‘Voluntary funding’ was expanded to cover grant-giving bodies that provide funding to other NPOs. The Consultation Paper was only focussed on the receipt of voluntary funding and not its provision. ‘Holding and using assets for the benefit of the public’ was also expanded to provide clarity that it covers entities that have a responsibility for the preservation and enhancement of assets such as artistic works, heritage assets, and natural assets.

BC 1.21 Two additional indicators were introduced for the Exposure Draft. These are ‘an absence of individuals with rights to financial returns from surpluses’ and ‘a requirement that the NPO transfer residual net upon dissolution to an entity with a similar purpose’. These indicators were included as the consultation responses identified them as being useful in a number of jurisdictional-level frameworks that provide guidance on determining whether an entity exists to provide a benefit to the public) These additional indicators focus on the nature of defined rights to financial benefits during an entity’s existence and upon its dissolution.

## Public accountability and societal accountability

BC 1.22 The IFR4NPO Consultation Paper proposed that NPOs have a wider societal accountability. This is an expansive view of accountability that recognises a general accountability to society at large due to the importance of NPO goods and services, the funding environment, the preferential treatment that NPOs can receive compared to other organisations, and the need to ensure the effective operation of the wider sector.

BC 1.23 While all NPOs can be said to have societal accountability, some may also meet the IFRS definition of public accountability. The *IFRS for SMEs* Accounting Standard notes that an entity has public accountability if:

- a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or
- b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (for example most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks often meet this second criterion)

BC 1.24 INPAG uses the *IFRS for SMEs* Accounting Standard as its foundational framework. As a standard that is specifically designed for entities that do not have public accountability:



- there are topics that may be relevant to entities that have public accountability that have been omitted;
- accounting policy options that may be useful to entities that have public accountability are unavailable; and
- there are simplified recognition and measurement principles and reduced disclosures that may not be appropriate for entities with public accountability to meet the needs of users.

BC 1.25 Entities that have public accountability are expected to use IFRS Accounting Standards or follow an appropriate jurisdictional GAAP. If an entity has public accountability, it is likely that INPAG will not meet the requirements of either the preparers or the users of their general purpose financial reports, although entities should follow any direction provided by their jurisdictional standard setter or regulator.

BC1.26 INPAG is being developed to provide accounting guidance specifically for NPOs. Those NPOs that have public accountability may find the guidance in INPAG useful. Such organisations are not prohibited from using INPAG. In the event that an entity with public accountability chooses or is required to use INPAG, the Exposure Draft requires an explanation of how INPAG is being used to provide transparency, including an explanation as to why the use of INPAG meets the needs of users of its financial statements.

## Section 2 – Concepts and pervasive principles

### The use of the IFRS Conceptual Framework and the IPSASB's Public Sector Conceptual Framework

BC 2.1 INPAG utilises the *IFRS for SMEs* Accounting Standard as its foundational framework. Where NPO-specific financial reporting issues have not been comprehensively or appropriately dealt with in the existing *IFRS for SMEs* Standard, or where there is no related Section in the *IFRS for SMEs* Standard providing financial reporting guidance, INPAG may differ from the *IFRS for SMEs* Standard. In accordance with the **"Process for developing the International Non-Profit Accounting Guidance through changes to the IFRS for SMEs Standard"**, this allows for the use of:

- IFRS Accounting Standards and its conceptual framework (the IASB's revised *Conceptual Framework for Financial Reporting* March 2018); and
- International Public Sector Accounting Standards (IPSAS) and its conceptual framework (the IPSASB *Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities* October 2014)

where this can provide more appropriate financial reporting guidance in the NPO context.

BC 2.2 A number of responses to the IFR4NPO Consultation Paper indicated that the conceptual basis of the *IFRS for SMEs* Accounting Standard was inappropriate for NPOs as it is based on the needs of users of general purpose financial statements of for-profit entities. At the time that the Consultation Paper was released it was also the case that the *Concepts and pervasive principles* contained in the *IFRS for SMEs* Standard published in 2015 did not reflect changes made to the conceptual framework that underpins IFRS Accounting Standards. The Third edition of the *IFRS for SMEs* Accounting Standard, which is currently being exposed for comment has now, however, incorporated the changes made to the conceptual framework that underpins IFRS Accounting Standards.

BC 2.3 The Consultation Paper explained that there are insufficient resources available to the IFR4NPO project to develop an entirely new conceptual framework for NPO financial reporting. As such it was necessary to use those aspects of the IASB's Conceptual Framework that have been incorporated into the *IFRS for SMEs* Accounting Standard where these are suitable for use in the NPO context. The IPSASB's Conceptual Framework was also drawn upon to provide the concepts and principles needed to develop financial reporting guidance for NPOs where these are not comprehensively or appropriately dealt with in the existing *IFRS for SMEs* Standard.

BC 2.4 As such there are aspects of both the IASB and IPSASB's conceptual frameworks that were utilised in developing Section 2 *Concepts and pervasive principles* for INPAG.

## **Primary users of general purpose financial reports and their information needs**

- BC 2.5 The IFR4NPO Consultation Paper focused on the external stakeholders, to whom NPOs are accountable, and their information needs. These were service users, resource providers, regulators and broader society. Feedback from respondents indicated that recognition had not been given to internal stakeholders who are also important in the NPO context. Examples provided by these respondents of internal stakeholders included those charged with governance, staff, and members.
- BC 2.6 Stakeholders who may traditionally be seen as internal in nature are important for NPOs. With specific reference to general purpose financial reporting, however, the conceptual bases of international frameworks for general purpose financial reporting define primary users as those that do not possess the authority to require an entity to disclose the information they need. Many of the internal stakeholders raised by respondents to the Consultation Paper, including those charged with governance and staff, are likely to possess the authority to require an entity to disclose information to meet their own specific information needs.
- BC 2.7 The position of internal stakeholders was discussed with both the Practitioner Advisory Group and Technical Advisory Group. It was agreed that they would be likely to possess the authority to require an NPO to disclose the information they need for accountability and decision-making purposes. In this regard, they are akin to some external stakeholders, in particular regulatory bodies and major donors, who are also likely to possess this authority in certain circumstances.
- BC 2.8 International financial reporting frameworks indicate that those who possess the authority to require an entity to disclose the information they need are not the primary users of general purpose financial reports even if they may find the information contained within them useful. As such the primary users of NPO general purpose financial reports were deemed to be the public to whom the NPO provides services and goods and those resource providers who do not possess the authority to require an NPO to disclose the information they need for accountability and decision-making purposes.
- BC 2.9 Primary users also include those that fulfil oversight functions on behalf of the public and resource providers. This is likely to include elected representatives and public officials who have a duty to represent the interests of members of the public who are provided with services and goods by the NPO or who provide it with financial and other resources.
- BC 2.10 Respondents supported the view expressed in the Consultation Paper that the information needs of these primary users cannot be met only through the reporting of financial information contained in general purpose financial statements. As indicated in the Preface, general purpose financial reports are needed to provide users with a meaningful understanding of an NPO's nature, objectives, strategy, risks, and performance.

## **Qualitative characteristics**

- BC 2.11 The qualitative characteristics of financial information are set out in conceptual frameworks to identify the types of information that are likely to be most useful to users of financial reports for accountability and decision-making. The qualitative characteristics provide a coherent framework for determining the decision-usefulness of financial reporting information, guidance on what to do when qualitative characteristics may be in conflict, and overall cost-benefit constraints on financial reporting.
- BC 2.12 The *IFRS for SMEs* Accounting Standard provides explanations of the qualitative characteristics of information in financial statements. These qualitative characteristics match those of the revised IASB Conceptual Framework which underpins the development of IFRS Accounting Standards. They are also consistent with the broader scope of general purpose financial reporting that is recognised in the IPSASB's Conceptual Framework.

- BC 2.13 The qualitative characteristics in the IASB Conceptual Framework that are now reflected in the *IFRS for SMEs* Accounting Standard are appropriate in the NPO context. As such these qualitative characteristics were deemed to be appropriate for use in the concepts and pervasive principles of the INPAG.

## Undue cost or effort exemption

- BC 2.14 The revised *IFRS for SMEs* Accounting Standard retains an undue cost or effort exemption. As there are Sections of the *IFRS for SMEs* Accounting Standard that have not yet been examined except for terminology changes as part of the IFR4NPO project, the undue cost or effort exemption was retained.
- BC 2.15 In order to assist NPOs in the correct use of the undue cost or effort exemption, Implementation Guidance was developed. This Implementation Guidance notes that the exemptions relate to the cost or effort required to obtain or determine the information necessary to comply with a requirement which will depend on the NPOs specific circumstances, management's judgement on the costs and benefits from applying that requirement, and the information available at the time of the assessment.
- BC 2.16 It also makes clear that NPOs should not treat the undue cost or effort exemptions as accounting policy choices and that NPOs need to disclose when they have used the exemption and the reasons why applying the requirement would in management's judgement involve undue cost or effort.

## The reporting NPO

- BC 2.17 The Consultation Paper considered the definition of the reporting NPO in terms of the financial reporting definition and its links to both the definition of control and the sometimes complex operational structures of NPOs. This included the use of local offices or administrative units that operate as branches of the NPO, that can be established to reach local communities and the recipients of the goods and services provided by NPOs.
- BC 2.18 The Exposure Draft therefore provides additional guidance to assist in the identification of the reporting NPO which have been discussed with focus groups and included in Application Guidance. This can assist in identifying an NPO as a reporting entity where there is no legal entity nor a group/parent structure.
- BC 2.19 Implementation Guidance and illustrative examples were also developed. These examine different types of operating structure and provide suggestions for the questions and analysis may be undertaken to determine the reporting NPO.
- BC 2.20 The Consultation Paper also considered in its alternatives the use of the definition of control when looking at the reporting entity and the operational structures used, including branches. The Basis for Conclusions for Section 9 *Consolidated and Separate Financial Statements* provides a commentary on the conclusions on that issue.
- BC 2.21 As noted in the Preface, the decision on which entities are required or permitted to use the INPAG rests with legislative and regulatory authorities and standard setters in individual jurisdictions. As such, the reporting NPO for the purpose of applying the INPAG could also be any entity that relevant authorities deem to be an NPO and that is required or chooses to prepare general purpose financial reports.

## The elements of financial statements

- BC 2.22 The *IFRS for SMEs* Accounting Standard follows the IASB Conceptual Framework in including equity as an element of financial statements. Equity is defined in these standards as the residual interest in the assets of the entity after deducting all its liabilities, and it effectively encompasses all net assets. The term equity implies a formal ownership structure with holders of equity being entitled to financial returns and the residual of net assets based on that ownership. This is unlikely to reflect the reality of the majority of NPOs, where such considerations either will not exist or such ownership interests are likely to be inconsequential.

- BC 2.23 Although the term 'equity' and its association with ownership is unlikely to be relevant for most NPOs, there does need to be an element that reflects the possibility of a party external to the NPO having a financial interest in the net assets of the NPO.
- BC 2.24 The IPSASB faced a similar challenge in the development of its Conceptual Framework. It decided that reference to ownership was appropriate in the public sector context. The IPSASB Conceptual Framework defined ownership contributions as an element, which establish or increase an interest in the net assets of an entity, and ownership distributions, which return or reduce that interest. The approach taken by the IPSASB has been examined and the possibility of the development of an element defined as contributed capital was considered for INPAG to reflect that parties external to the NPO may have a financial interest in the net assets of the NPO.
- BC 2.25 Following discussion with the project's Technical Advisory Group, the retention of the element of equity was deemed preferable to the definition of a new element that ultimately reflected the same underlying concept. As such, equity was included as a financial statement element, with the Application Guidance providing additional detail on its use in the NPO context.
- BC 2.26 NPOs will often be provided with financial resources where the provider of those resources restricts the use to specific purposes or activities. INPAG includes these financial resources as funds with restrictions. Funds with restrictions are to be used by NPOs when there are externally imposed funding or other legal arrangements governing the use of financial resources. Other financial resources, including those that the NPO internally designates itself to specific purposes or activities, are included within funds without restrictions. Funds with restrictions and funds without restrictions will reflect accumulated surpluses. They are presented as a component of net assets but are not a separate financial statements element.
- BC2.27 Net assets comprise funds with and without restrictions, as well as equity where it exists. Exceptionally, an NPO may also need to recognise and present non-controlling interests. As this is expected to be rare, detail on such interests were not included specifically in Section 2. Where an NPO does recognise and present any non-controlling interest, this will also form part of net assets.
- BC2.28 Net assets are an arithmetical total and were not considered to be a financial statement element. Amounts may be set aside for future distribution to holders of equity claims. These amounts will be included within funds with restrictions only if there is an externally imposed basis for them being set aside. This could be for example a legal requirement that holders of equity claims are guaranteed a specific return on their contributions of equity. Otherwise they will be disclosed in funds without restrictions. Funds set aside for future distribution to holders of equity claims will need to be transferred to equity prior to distribution. This is to ensure that equity is not understated following distribution.
- BC2.29 Although the majority of the Technical Advisory Group agreed with this overall approach to the inclusion of equity as an element and the use of funds with restrictions and funds without restrictions to present accumulated surpluses, one member disagreed. They were concerned that there were transactions and economic events that might not be adequately captured by the elements, and in particular equity as defined in the NPO context. SMCs 2(d) and 2(e) seek stakeholder views on this position.
- BC 2.30 Service potential is not a concept explicitly recognised in the IASB Conceptual Framework, although it is included in the IPSASB's Public Sector Conceptual Framework. It was included, where appropriate, in the definition of elements for INPAG. This is because it is relevant for assets that are held by an NPO not to generate cash flows, but rather for the services that can be provided by the asset. As part of measurement, value in use as a potential measurement basis was amended to incorporate the concept of service potential.
- BC 2.31 Details of how service potential will apply in the NPO context are not part of Exposure Draft 1. The topic will be covered Exposure Draft 2 as it relates to revenue and in Exposure Draft 3 as it relates to inventory. As a result of feedback from respondents to the Consultation Paper Section 17 *Property, Plant and Equipment* is not currently proposed to be updated. This will, however, be a priority area should resources allow.

## Recognition and derecognition

- BC 2.32 Feedback from the Consultation Paper was that users of general purpose financial reports do not associate the financial performance of NPOs with profit and loss, but many accept the concept of a surplus or deficit. There was also feedback to request simplicity in the presentation of information. On this basis the INPAG Statement of Income and Expenses is focused on surplus and deficit and not comprehensive income as permitted in the *IFRS for SMEs Accounting Standard*. Further explanation is provided in the Basis for Conclusions to Sections 3, 5 and 6.
- BC 2.33 As a consequence, amendments were made to the recognition process of the *IFRS for SMEs Accounting Standard* and specifically in which primary financial statements transactions are recognised. These amendments ensure that income and expenses that contribute to surplus and deficit are recognised in the Statement of Income and Expenses, and income and expenses that do not contribute to surplus and deficit are instead recognised in the Statement of Changes in Net Assets.

## Presentation in GPFs

- BC 2.34 Presentation concepts and principles in both the *IFRS for SMEs Accounting Standard* and the IASB's Conceptual Framework are focussed primarily on the primary financial statements, whereas presentation in the IPSASB Conceptual Framework has a wider scope encompassing financial reports outside the core financial statements. This IPSASB Conceptual Framework was utilised in developing additional presentation concepts and principles for INPAG.

# Section 3 – Financial statement presentation

## Presentation

- BC 3.1 The format and content of financial statements is fundamental to how the information is presented to stakeholders. This presentation is particularly important when revenue can only be used for particular purposes. A detailed description of the issue was included as Issue 7: Financial statement presentation in Part 2 of the IFR4NPO Consultation Paper.
- BC 3.2 Feedback was sought on how financial statements should be presented to help the user's understanding of an NPO's activities and whether there should be disclosure of material categories of income and expenses and/or transactions. The Consultation Paper also sought views on how unrestricted and restricted funds should be presented in the main financial statements and notes (including reserves), the role of fund accounting and how any requirements might align with donor reporting requirements.
- BC 3.3 The Consultation Paper proposed three alternatives for developing guidance for the presentation of NPO financial statements. The first was to retain the requirements in the international standards (IFRS Accounting Standards, the *IFRS for SMEs Accounting Standard* and IPSAS) unchanged and provide supplementary guidance. The second was to build on the *IFRS for SMEs Accounting Standard* and to add the use of fund accounting which would require, as a minimum, that income is split between restricted and unrestricted income on the face of the income statement. The third alternative included a new requirement to provide supplementary donor or project statements for material funds or projects in addition to proposals for fund accounting in alternative two.
- BC 3.4 There was no consensus as to the preferred alternative, with roughly a third supporting each alternative, but accountability and meeting users' needs were highlighted as important issues. Approximately two thirds of respondents supported alternatives that included the use of fund accounting. Some responses suggested that fund accounting is essential to ensure the stewardship of funds with restrictions and provide clarity regarding the NPO's free reserves position at year-end. Other responses suggested that fund accounting often results in more complex financial statements that readers find difficult to understand, and that it may not be suitable for all NPOs. It is acknowledged that adopting fund accounting could result in more complex financial statements, but on balance consider this risk is

justified by the need to provide information that supports the proper stewardship of funds with restrictions. This information is also needed for a full understanding of NPOs' financial statements.

- BC 3.5 A slight amendment to terminology is proposed as the term 'restricted' can be used alongside other accounting terms (eg restricted cash) and potentially have a different meaning to 'restricted' in the context of NPOs, where the focus is on restrictions placed by fund providers and grantors. As a consequence, the financial statements include proposals for the separation of funds with and without restrictions in a number of places. A definition of funds with restrictions and funds without restrictions is provided in Section 2.
- BC 3.6 Respondents to the consultation raised concerns about the potential complexity and increased length of financial statements that could occur with the introduction of fund accounting. As a consequence it is proposed to require separate presentation of income and expenses, net assets (and changes in net assets) for the aggregates of funds with restrictions and funds without restrictions only. Any additional disclosures are to be driven by the usefulness of the information based on the nature of the NPO and the materiality of the information to the understanding of the users of General Purpose Financial Reports.
- BC 3.7 The separate presentation of funds with restrictions and funds without restrictions will provide useful information to users of the financial statements without imposing the costs associated with full fund accounting on NPOs. Respondents commented that requiring the presentation of funds with restrictions and funds without restrictions beyond the income and expenses statement and net assets could be challenging for some NPOs and would add little value for readers of the financial statements.
- BC 3.8 However, some NPOs may have the capacity to implement full fund accounting and may consider that this would improve the usefulness of their financial statements. Such NPOs are permitted to provide this additional information, in line with the additional disclosures permitted for all financial statements.
- BC 3.9 Issues were raised about capital grants and donated assets in responses from stakeholders. As a consequence, additional presentation requirements have been included in the Statement of Income and Expenses and Statement of Cash Flows to provide transparency over such items, where they are material to an NPO's financial statements.

## Deferred revenue

- BC 3.10 The Consultation Paper sought feedback on the approach to deferring revenue as part of considerations about the presentation of the financial statements. Proposals for revenue recognition and measurement will be included in Exposure Draft 2 (ED2) and are not considered further here. Consequently, the presentation of deferred revenue included in ED1 is subject to change, depending on the accounting for revenue that is adopted.

## Additional supplementary information

- BC 3.11 As discussed above, the third alternative for the presentation of financial statements proposed supplementary donor or project information on major funds. Some respondents acknowledged that if a donor statement could be developed that would meet the reporting and auditing requirements of major donors, this could lead to an overall reduction in the reporting burden.
- BC 3.12 The INPAG Secretariat will explore this further with the IFR4NPO Donor Reference Group. This process is expected to take some time, and consequently proposals will be developed for inclusion in Exposure Draft 3 (ED3) at the earliest. The INPAG Secretariat is of the view that supplementary donor or project statements would be permitted but not required.
- BC 3.13 Where a standardised reporting format cannot be developed in time, it is proposed, as part of ED3, to develop generic guidance setting out the issues NPOs will need to consider in preparing their own donor or project statements should they choose to do so.



## Statement names and terminology

- BC 3.14 The Consultation Paper proposed the use of the term 'Statement of Financial Performance' for the statement that contains the NPO's income and expenses and sought feedback on this proposal. Around two thirds of those that responded to this question supported the use of this term.
- BC 3.15 The main reason given by those that did not support the use of the term was that NPOs' performance is not judged on whether they make surpluses or deficits, but whether they meet their aims and objectives (social performance). Using the term 'financial performance' could imply that this is the main measure of NPOs' performance, which is not the case. It is therefore proposed that the term Statement of Income and Expenses is used as it may be better understood.
- BC 3.16 Based on feedback, surplus or deficit is preferred to profit or loss to show the difference between income and expenses. This is seen as more relevant for users of NPO financial statements.
- BC 3.17 The other key area of terminology where a proposal has been made to add NPO context to a term relates to the description of what is traditionally equity. Equity is a term that is used in for-profit standards. Equity is defined in the for-profit standards as the residual interest in the assets of the entity after deducting liabilities. This will include items that don't meet the definition of a liability such as share capital and will also include retained earnings and reserves, for example the revaluation reserve (sometimes called revaluation surplus).
- BC 3.18 In for-profit entities, all the residual interest in the assets of the entity after deducting liabilities are ultimately due to external parties who would be described as owners. This form of ownership with entitlement to all the residual interest of the entity does not exist for NPOs, but it is possible that some entities that meet the definition of an NPO have some form of equity claims on the organisation, either from historic set-up or because of jurisdiction specific legislation/regulation.
- BC 3.19 It is therefore proposed to retain the term equity but describe it in the NPO context and include it as an element that is a component of a Section in NPO financial statements named 'net assets'. Net assets will typically comprise equity, funds with restrictions, and funds without restrictions. Equity would include all forms of equity claims including any shares that have been issued.
- BC 3.20 This discussion of these responses to the Consultation Paper are also discussed as appropriate in Sections 4-10.

## Fair presentation

- BC 3.21 Along with responses from the consultation, the INPAG Secretariat has received input from various stakeholders and has reviewed a number of academic reports. Collectively, these point to concerns about the understandability of financial statements. As a consequence, the INPAG Secretariat has considered the number and scope of the financial statements.
- BC 3.22 Following this review, it is proposed that the Statement of Income and Expenses statement totals to surplus or deficit and that some of the items that under the *IFRS for SMEs* Accounting Standard are shown in the Statement of Comprehensive Income (Other Comprehensive Income), are presented in a Statement of Changes in Net Assets. Presenting these items outside the Statement of Income and Expenses is expected to deliver some simplification. As not all Sections of the *IFRS for SMEs* Accounting Standard are being reviewed as part of the first phase of INPAG, some items, predominantly changes arising from fair value adjustments will need to continue to be shown in the Statement of Income and Expenses. Many NPOs will not have these fair value adjustments.
- BC 3.23 The Statement of Changes in Net Assets is proposed to disclose information that will allow the information equivalent to that found in statements prepared under the *IFRS for SMEs* Accounting Standard, such as comprehensive income. It will also show the movement between restricted and unrestricted funds.
- BC 3.24 Not all members of the Technical Advisory Group supported the decision to depart from the presentation used in the *IFRS for SMEs* Accounting Standard. Instead, they supported the retention



of comprehensive income. They also had some concerns over the presentation of some items in the Statement of Changes in Net Assets. As some of these items will be dependent on the requirements of other Sections of INPAG that are scheduled for ED2 or ED3, these requirements will be reviewed once the remaining Sections of INPAG are complete.

## Comparability

BC 3.25 Some responses to the Consultation Paper proposed limiting the comparative information provided in respect of fund accounting (for example, the provision of comparative information for movements in fund balances). The Technical Advisory Group questioned the removal of comparatives given the beneficial information they provide. It was agreed that the matter of comparatives would be considered in later topics, and proposals finalised in Exposure Draft 3 (ED3). A specific matter for comment on comparatives (SMC 4 b)) is included to inform these later considerations.

## Section 4 – Statement of Financial Position

### Funds with and without restrictions

BC 4.1 The Consultation Paper asked whether unrestricted and restricted funds (that are to be used for specific NPO purposes) should be presented in the main financial statements and notes (including reserves). It asked for feedback on how this would align with donor reporting requirements and the role of fund accounting.

BC 4.2 The level of disclosure in the Statement of Financial Position is proposed to be limited to a split between funds with restrictions and funds without restrictions on the face of the statement. Taking this approach will provide users with important information about the level of funds available to the NPO, which is key to financial resilience. However, for some NPOs, users' needs may only be met by providing an analysis of funds with restrictions. Such information may be provided in the notes to the financial statements. It was also agreed that NPOs should not be prevented from presenting this information on the face of the statements where they considered this would be useful to the users of their financial statements.

BC 4.3 Detailed proposals regarding the accounting for income with restrictions, which will impact on funds will be developed as part of the topics on non-exchange revenue and grant expenses that will be included in Exposure Draft 2 (ED2). Income with restrictions may include income from endowments. Endowments are typically donations of cash or other assets to an NPO to be used as an investment, with the investment income being made available for the NPO to use, either for a specific purpose or more generally. Because of the complexity associated with endowments, and potentially differing treatments under different legal frameworks, detailed requirements for endowments will not, for the time being, be included in INPAG.

BC 4.4 In addition to the split between funds with restrictions and funds without restrictions, consultation respondents also supported the provision of information about the purposes for which reserves are being held as this would be useful to users of the financial statements. This requirement is being carried forward from the existing requirement in the *IFRS for SMEs* Accounting Standard.

### Equity

BC 4.5 In reviewing the content of the Statement of Financial Position, consideration has been given to whether to include the term equity and its use. Equity is a term that is used in for-profit standards and is also included in the standards to be used by public sector entities. Equity is defined in the for-profit standards as the residual interest in the assets of the entity after deducting liabilities. This includes items that don't meet the definition of a liability such as share capital and will also include retained earnings and reserves, for example the revaluation reserve (sometimes called revaluation surplus). Equity is defined as a financial statement element.

- BC 4.6 The standards for the public sector recognise that some entities may have share capital. The IPSAS Conceptual Framework does not define equity as a financial statement element but does discuss the terms 'net assets/equity' and 'net financial position' as equivalent terms to the 'equity' section of the balance sheet of for-profit financial statements. IPSAS 1 *Presentation of Financial Statements* also uses the term 'net assets/equity' which it defines as contributed capital (with ownership contributions and ownership distributions defined as financial statement elements), accumulated surplus or deficit, reserves and non-controlling interests.
- BC 4.7 Non-profit organisations have a variety of different legal structures, including incorporated entities, trusts, or various forms of unincorporated entity. It is possible that some entities that meet the definition of an NPO have some form of equity claims on the organisation, either from historic set-up or because of jurisdiction specific legislation/regulation.
- BC 4.8 The use of the term contributed capital was considered to describe these arrangements for NPOs, but the retention of the term equity was deemed preferable, with a description of equity in the NPO context included in AG 2.6-AG2.9. As with the *IFRS for SMEs* Accounting Standard, equity is defined as a financial statement element but because of the different concept of ownership, equity in the NPO context does not equate to a residual interest encompassing all the NPO's net assets.
- BC 4.9 Instead, to reflect the NPO context and to recognise the various arrangements that might exist, it is proposed that the net assets in an NPO financial statements comprise equity, funds with restrictions, funds without restrictions, and exceptionally, non-controlling interests. Equity would include all forms of equity claims including any shares that have been issued. Funds with restrictions and funds without restriction would together be the accumulated surplus or deficit of the NPO.
- BC 4.10 It is considered much less likely, although not impossible for an NPO to have share capital. As a consequence the information required to be presented in the financial statements places less emphasis on share capital, and it is not a mandatory heading in the Statement of Financial Position. However, disclosures must be made where it is relevant.
- BC 4.11 Similarly non-controlling interests are expected to be unlikely, but not impossible for NPOs. Given the nature of such interests, the requirement to disclose on the face of the financial statement has been maintained, but is expected to be used rarely in practice.
- BC 4.12 Further information on the definition of equity is available in Section 2 *Concepts and pervasive principles*.

## Section 5 – Statement of Income and Expenses

### Statement name

- BC 5.1 The Consultation Paper covered a number of aspects of financial statement presentation including the term that should be used for the primary statement that covers the income and expenses of an NPO. The Consultation Paper proposed the use of the term 'Statement of Financial Performance'.
- BC 5.2 Around two thirds of respondents supported the use of the term 'Statement of Financial Performance' although many of these respondents did not provide a rationale for supporting the term. However, there were a number of disagreements with the proposal. The main reason given by those that did not support the use of the term was that NPOs' performance is not judged on whether they make surpluses or deficits, but whether they meet their aims and objectives (social performance).
- BC 5.3 Respondents were concerned that using the term 'financial performance' could imply that this is the main measure of an NPOs' performance. Alternative terms proposed by respondents were considered. The most commonly suggested alternative terms were 'income and expenses statement' and 'statement of financial activities' as these terms were considered to be better understood by NPO stakeholders.
- BC 5.4 Alternatives were discussed with the project advisory groups and it was agreed that Statement of Income and Expenses was best understood by stakeholders and had the benefit of simplicity.

- BC 5.5 Nevertheless, NPOs will have the flexibility to use a different term in their financial statements if an alternative would best explain the financial statement or to comply with local regulations.

## Key financial information

### Surplus and deficit

- BC 5.6 The INPAG Secretariat received a substantial amount of feedback that profit or loss was not an appropriate term for non-profit organisations. In discussion with stakeholders and advisory groups, the term surplus or deficit was considered to be more appropriate. As a consequence this term has been adopted in the financial statements. This removes the implication that there is any profit or loss and is more focused on the arithmetic difference between income and expenses.

### Classification of expenses

- BC 5.7 The presentation of expense information is included in Section 5 of the *IFRS for SMEs* Standard. This topic was identified as a priority issue for NPOs and was included as topic 8 in the Consultation Paper. This topic will be considered as part of Exposure Draft 3 (ED3). As a consequence, the text from the *IFRS for SMEs* Standard has not yet been updated with the requirements yet to be determined. This text will be updated at part of ED3, and a new INPAG Section will be created to provide more guidance on expense analysis and disclosure.

## Statement format

- BC 5.8 The Consultation Paper sought views on how financial statements should be presented to help the user's understanding of an NPO's activities. This included feedback on the disclosure of material categories of income and expenses and/or transactions. The Consultation Paper also asked about the presentation of restricted and unrestricted funds.

### Income and expenses with restrictions

- BC 5.9 Most of the feedback received related to the use of fund accounting, which has implications for the presentation of income with, and without, restrictions and its related expenses rather than on the disclosure of material categories of income and expenses.
- BC 5.10 The majority of respondents to the Consultation Paper supported the separate presentation or disclosure of restricted and unrestricted funds. Respondents felt that this was an important aspect of accountability and meeting users' needs. As a consequence it is proposed that the Statement of Income and Expenses shows separately, through two columns, an aggregation of those incomes and expenses with restrictions and, separately, an aggregation of those incomes and expenses without restrictions.
- BC 5.11 There was some discussion in response to the Consultation about the need for comparatives, and concerns about the complexity of the financial statements if comparatives are mandated alongside fund accounting requirements. This was considered by the project advisory groups, and whilst acknowledging the potential for complexity, the advice was that comparative information is important for users to understand the financial statements. As a consequence, it is proposed that comparatives are required for aggregated income and expenses with restrictions; and aggregated income and expenses without restrictions only. It is proposed that comparatives will not be mandated for the disaggregation of these balances, but can be provided where this is helpful to the understanding of the NPO's financial statements.
- BC 5.12 As part of Exposure Draft 2 (ED2), guidance will be developed on revenue from grants and donations and grant expenses, which will include the accounting for income and expenses that might have restrictions. Possible impacts on this Section include additional items of revenue and expenses to

be presented, subtotals for transactions arising from exchange transactions and non-exchange transactions and/or possible requirements regarding offsetting revenue and fundraising expenses.

### Single statement

- BC 5.13 In response to issues raised about the understandability of financial statements, it is proposed that the Statement of Income and Expenses gives prominence to the income and expenses in the reporting period and focuses less on the impact of revaluations of items held in the Statement of Financial Position. This will mean that income and expenses and the effects of realised gains and losses (such as from the sale of an asset) are the focus of the Statement of Income and Expenses.
- BC 5.14 As not all Sections of the *IFRS for SMEs* Standard are being reviewed as part of this initial set of guidance, the Guidance may require that some unrealised gains or losses are shown in the Statement of Income and Expenses, particularly those losses or gains from adjustments to fair value. These will be shown in a separate Section in the Statement of Income and Expenses.
- BC 5.15 With this focus, it is proposed that all other items be presented in a Statement of Changes in Net Assets. This statement would provide a subtotal of transactions that form Other Comprehensive Income in IFRS based standards, so that equivalent information to the Statement of comprehensive income could be found. This would be a departure from the *IFRS for SMEs* Accounting Standard which provides a choice of whether Other Comprehensive Income is in a single statement that includes all types of income and expense.
- BC 5.16 As a consequence of these changes, it is proposed that the Statement of Income and Expenses should show 'surplus or deficit from operating activities', share of surplus or loss from associates, gains or losses on the disposal of assets, unrealised gains from foreign exchange differences, unrealised gains or loss through fair value adjustments (if any) and then a total surplus or deficit. The presentation of foreign exchange differences is being considered as part of Exposure Draft 2.

## Section 6 – Statement of Changes in Net Assets

### Statement structure

- BC 6.1 The Consultation Paper did not directly seek feedback on the Statement of Changes in Net Assets. Amendments to this statement arose as a result of feedback on other financial statements and from stakeholder feedback about the understandability of financial statements.
- BC 6.2 It is proposed that the Statement of Income and Expenses should be simplified by excluding items referred to in the *IFRS for SMEs* Accounting Standard as 'Other Comprehensive Income'. As a consequence, other Sections of INPAG would require some items of income and expenses to be presented in a Statement of Changes in Net Assets rather than in an 'Other Comprehensive Income' section of the Statement of Income and Expenses.
- BC 6.3 The INPAG Secretariat noted that this approach might mean that information that was previously available in the *IFRS for SMEs* Accounting Standard based statement formats would be harder to find. As a consequence it is proposed that the Statement of Changes in Net Assets:
- a) commences with the surplus or deficit from the Statement of Income and Expenses;
  - b) adds or subtracts the items that would be unrealised gains and losses found in 'Other Comprehensive Income' in the statements prescribed by the *IFRS for SMEs* Accounting Standard; and
  - c) produces a sub total of a) and b)
- BC 6.4 This approach will generate a subtotal that would provide equivalent information to the Statement of comprehensive income. This would be a departure from the *IFRS for SMEs* Accounting Standard, which provides a choice of whether Other Comprehensive Income is in a single statement that includes all

types of income and expense, but does not require its inclusion in the Statement of Changes in Net Assets.

- BC 6.5 To support understandability of this statement it is proposed to subdivide the Statement of Changes in Net Assets into the following sections:
- a) movements arising from unrealised gains and losses (other than those prescribed in the Guidance to be taken through the Statement of Income and Expenses);
  - b) movements between funds and reserves (including movements between funds with restrictions and funds without restrictions);
  - c) movements arising from contributions from holders of equity claims or distributions to holders of equity claims; and
  - d) other changes in net assets.

These sections would provide a reconciliation of the opening and closing carrying amount of components of net assets.

## Section 7 – Statement of Cash Flows

- BC 7.1 No major revisions have been made to the principles established in the *IFRS for SMEs* Accounting Standard for the Statement of Cash Flows. Any updates have been limited to terminology, use of language specific to NPOs or alignment with updates to Sections 1-10. This Section is marked as updated to show that it has not been fully reviewed as yet.
- BC 7.2 The Statement of Cash Flows was included in the scope of topic 7 *Presentation of financial statements* in part 2 of the Consultation Paper, primarily to consider whether the cash flow could be used as a basis for an additional statement for inclusion in general purpose financial reporting to meet the needs of donors and funders. This was based on feedback that donors and funders frequently require cash-based information to meet their reporting requirements.
- BC 7.3 The possibility of an additional donor/project statement was included in alternative 3 of this topic) Around one third of respondents supported the development of a donor/project statement. It was acknowledged that if donors are willing to rely on such statements, and not require special-purpose financial reports, this could reduce burdens, costs and complexity. However, other respondents felt that donors' requirements are best met by special-purpose financial reports, not general-purpose financial reports. There was also a concern that any proposals would only be helpful to some NPOs and that this could come at the cost of additional complexity.
- BC 7.4 The objective of producing supplementary project/programme information as part of the NPO's general purpose financial statements requires coordinated outreach with donors, which was supported by consultation respondents. As a result, the development of a supplementary information statement will be explored with the IFR4NPO Donor Reference Group.
- BC 7.5 Respondents to the consultation supported the availability of guidance on the form and content of supplementary information if it is required as it would assist consistency. A guidance-based approach would allow each organisation to balance the cost/benefit of preparing supplementary information in its own context. As a consequence, respondents were of the view that reporting on material projects should be optional and not a mandatory requirement. Given the likely varied circumstances of each non-profit organisation, the INPAG Secretariat supported this approach.
- BC 7.6 The process to develop a supplementary information schedule is expected to take time. A proposal for a new statement may be ready for inclusion in Exposure Draft 3 (ED3). However, if such a statement is not developed in time for inclusion in ED3, generic guidance setting out the issues that NPOs will need to consider in preparing their own donor or project statements, should they choose to do so, will be included in ED3 instead.

## Section 8 – Notes to the financial statements

- BC 8.1 Section 8 does not specify the notes to the financial statements required in respect of specific assets, liabilities, revenue, or expense. Such requirements are set out in the sections of INPAG dealing with those items, and the rationale for any revisions to those requirements is set out in the Basis for Conclusions to those sections.
- BC 8.2 No major revisions have been made to Section 8 (which covers the general requirements for the notes to the financial statements) in ED1. Any updates have been limited to terminology or use of language specific to NPOs, or to reflect revisions to the financial statement requirements in other sections of INPAG.
- BC 8.3 The Consultation Paper did not include specific proposals relating to the general requirements for the notes to the financial statements, and where respondents commented on the notes, these comments related to specific disclosures rather than the general principles set out in Section 8.
- BC 8.4 The approach to the notes to the financial statements set out in Section 8 of the *IFRS for SMEs Accounting Standard* is consistent with the approach to the notes in full IFRS Accounting Standards and in IPSAS. These requirements have been reviewed and it was concluded that there are no NPO-specific issues that require addressing. The requirements in the *IFRS for SMEs Accounting Standard* have therefore been retained in INPAG.

## Section 9 – Consolidated and separate financial statements

### Introduction

- BC 9.1 The consultation paper considered the definition of the reporting entity in terms of the financial reporting definition and its links to the definition of control, and the sometimes complex structures such as branches and other operational structures that can be established to reach local communities and the recipients of the goods and services provided by NPOs (see also comments in the basis of conclusions for Section 2 *Concepts and pervasive principles*).

### Requirement to present consolidated financial statements

#### Defining control

- BC 9.2 The Consultation Paper considered alternatives for the approach to the definition of control in relation to the reporting entity. Alternative 1 was based on the IFRS 10 *Consolidated financial statements* and IPSAS 35 *Consolidated financial statements* definition of control. Alternative 2 was based on the guidance in the *IFRS for SMEs Accounting Standard* 2015 edition that included a rebuttable presumption about control to simplify application.
- BC 9.3 The IFRS and IPSAS standards on consolidated financial statements require a judgement about control to be formed based the concepts of control in those standards.
- BC 9.4 On balance, respondents to the consultation favoured the approach in alternative 2, but there was also support for alternative 1. The reasons provided for favouring alternative 2 centred on the ease of application and respondents contrasted this with the resources that might be required in forming the judgements needed under alternative 1.
- BC 9.5 Alternative 1 was expressed as a preference by some respondents as this was consistent with the key international frameworks and because the control frameworks are based on the substance of the transaction and not the form. Comments included that NPOs can find it easier to understand the substance of the relationships in operation better than their legal forms. As the IASB and IPSASB



frameworks do not use 'bright-lines' judgements, they can be more easily adopted in different jurisdictions.

- BC 9.6 A Focus Group held to explore these views further was more evenly balanced in support for the two alternatives. Attendees supported consultees views on both approaches but placed additional emphasis on the resource benefits of alternative 2.
- BC 9.7 Since the Consultation Paper was issued, the IASB has issued an Exposure Draft proposing revisions to the *IFRS for SMEs* Accounting Standard. In this revision, the IASB has agreed with respondents to its consultation to align the definition of control with IFRS 10. The IASB's view was that using the control model as a single basis for consolidation is a simplification. The IASB acknowledged, based on its Post Implementation Review of IFRS 10 that assessing control requires judgement, and that depending on the complexity of transactions this can sometimes be significant.
- BC 9.8 The Technical Advisory Group were strongly of the view that alignment with IFRS 10 is important. On the basis of these views, the feedback from the consultation paper and the alignment proposed in the revised *IFRS for SMEs* Accounting Standard the control framework in IFRS and IPSAS have been adopted. In drafting the Guidance and Application Guidance, the Technical Advisory Group supported the use of IPSAS 35 and other internationally available guidance to explain how these concepts apply to NPOs. The Application Guidance specifically addresses how the concepts in IFRS 10 of:
- a) power over the investee;
  - b) exposure, or rights, to variable returns from its involvement with the investee; and
  - c) the ability to use its power over the investee to affect the amount of the investor's returns.
- should be used in an NPO context.

### Rebuttable presumption

- BC 9.9 Paragraph 9.5 of the 2015 *IFRS for SMEs* Accounting Standard says that 'control is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting power of an entity'. It also provides other examples of control relating to powers by virtue of voting rights, power to govern the financial or operating policies of an entity, powers to appoint members of the board, or to cast the majority of votes on the Board.
- BC 9.10 The *IFRS for SMEs* Accounting Standard includes a rebuttable presumption to simplify the application of the control concepts, which were considered by consultation respondents to be valuable for NPOs. Applying a rebuttable presumption would allow judgements to be formed in line with the benefits of alternative 1, but allows a simplified approach.
- BC 9.11 The ED for the Third edition of the *IFRS for SMEs* Accounting Standard continues to include a rebuttable presumption to ease application of the control model. However, the examples have changed to focus on contractual arrangements between the parent and other vote holders, rights arising from other contractual arrangements, the parent's actual and potential votes. These examples appear to be less relevant to NPOs, where control might be more likely to come from the ability to govern the financial or operating policies of an entity and from the power to appoint trustees or members of a board. For a rebuttable presumption to be effective for NPOs, it needs to be applicable to a wide range of NPOs. As a consequence, it is proposed to retain the examples from the current *IFRS for SMEs* Accounting Standard rather than those in the Exposure Draft for the Third edition of the *IFRS for SMEs* Accounting Standard.

### Basis of consolidation

- BC 9.12 In developing the Guidance, the Technical Advisory Group raised questions about the conceptual basis of consolidation of NPOs and whether there were any differences between for-profit and non-profit entities. It was noted, predominantly through review of academic studies, that some users find



it difficult to understand consolidated financial information, but value understanding the relationship between associated and controlled entities.

- BC 9.13 In some cases, the elimination of intra-group items may mean that information is less complete in a way which matters for some readers of the financial statements, perhaps because important 'internal' transactions become invisible when eliminated. This might be best addressed by additional disclosure rather than producing a full consolidation.
- BC 9.14 How the qualitative characteristics that form part of the concepts and pervasive principles for INPAG might apply to consolidation were considered. The two fundamental qualitative characteristics of 'faithful representation' and 'relevance' were identified as being important in considering whether controlled entities should be consolidated by a parent NPO.
- BC 9.15 Further guidance to explain how an NPO might consider each of these characteristics in forming a judgement about whether it should consolidate a controlled entity has been developed.
- BC 9.16 The INPAG Secretariat was strongly of the view that, where an NPO has not consolidated a controlled entity, it must explain the reasons why, and set out the relationship between the entities. This should include information about the nature of the relationship, governance arrangements and the nature and value of transactions between the entities, including related party transactions.

## **Consolidation procedures, disclosures in consolidated financial statements, separate financial statements and combined financial statements**

- BC 9.17 The topic of consolidation was not prioritised in responses to the Consultation. It is therefore outside of the scope of current developments and will not be included in the initial INPAG. However, the INPAG Secretariat is keen to understand views on this topic to further develop the Guidance in subsequent phases.
- BC 9.18 A number of the requirements in Section 9, particularly with regard to non-controlled entities, may be less likely to occur for NPOs. As a consequence, paragraphs G9.36 and G9.39 are intended to only be applied in the rare situations where they are needed by an NPO.
- BC 9.19 Changes to terminology have been made to be consistent with other Sections of INPAG and to reflect the nature of NPOs. As noted in BC9.17, this Section has not been reviewed for NPO specific issues related to consolidation. As a consequence, this Section is considered to only have been partially updated for the NPO context.

## **Section 10 – Accounting policies, estimates and errors**

- BC 10.1 The Consultation Paper did not include specific proposals relating to accounting policies, estimates and errors, and respondents did not raise any issues.
- BC 10.2 The approach to the accounting policies, estimates and errors set out in Section 10 of the *IFRS for SMEs* Accounting Standard is consistent with the approach to the issues in full IFRS Accounting Standards and in IPSAS. These requirements have been reviewed and it was concluded that there are no NPO-specific issues that need addressing. The requirements in the *IFRS for SMEs* Accounting Standard have therefore been retained in INPAG, with the exception of text relating to the use of accounting standards (see paragraph BC10.3 to BC 10.5). Any other updates have been limited to changes in terminology or use of language specific to NPOs.
- BC 10.3 The *IFRS for SMEs* Accounting Standard permits an entity to refer to full IFRS Accounting Standards in developing accounting policies for transactions, other events, or conditions not addressed in the *IFRS for SMEs* Accounting Standard. This approach has been retained in INPAG, but noted that NPOs

may encounter transactions, other events or conditions that are not addressed in full IFRS Accounting Standards.

- BC 10.4 Transactions, other events, or conditions not addressed in full IFRS Accounting Standards may involve transactions that are not commercial in nature (non-exchange transactions such as grants and donations), which may be addressed in IPSAS. The INPAG Secretariat therefore decided that where there are no specific requirements or guidance in either the *IFRS for SMEs* Accounting Standard or full IFRS Accounting Standards, NPOs may refer to IPSAS in developing an appropriate accounting policy. Permitting NPOs to refer to a relevant IPSAS only where there are no requirements or guidance in either the *IFRS for SMEs* Accounting Standard or full IFRS Accounting Standards, is intended to maximise consistency with the concepts and principles set out in Section 2.
- BC 10.5 The INPAG Secretariat noted that there may be transactions, other events or conditions that are not addressed in any international standard. In such cases, it was agreed that it would be appropriate for NPOs to refer to national standards that addressed such transactions, other events or conditions where the accounting treatment in those national standards are consistent with the concepts and principles set out in Section 2.

## Section 35 – Narrative reporting

### Consultation Paper feedback on narrative reporting

- BC 35.1 The IFR4NPO Consultation Paper proposed in Part 1 that one of the core premises of the INPAG, in order to meet Guidance objectives, would be the inclusion of non-financial reporting information also known as narrative reporting. This would lead to NPOs producing general purpose financial reports rather than just general purpose financial statements.
- BC 35.2 A detailed description of the issue was included as part of Issue 10: *Narrative Reporting* in Part 2 of the Consultation Paper. This highlighted the importance of non-financial information for NPOs to demonstrate accountability and stewardship to stakeholders, and the difficulty caused by varying disclosure requirements globally.
- BC 35.3 Respondents to Part 1 of the Consultation Paper provided feedback on what they deemed the challenges would be from guidance that included non-financial information reporting requirements for NPOs. At a conceptual level, respondents highlighted issues such as scope, timing of introduction, prescription and flexibility, the reliability and integrity of data, and integration with existing performance reporting. A number of practical challenges were also raised, including NPO capacity and capability, costs and expertise, and subjectivity in reporting.
- BC 35.4 For Part 2, respondents were asked to provide feedback on the description of the issue, the alternative treatments proposed, and whether the guidance should be set at the level of an overarching framework and high-level principles, or include more specific reporting requirements. Respondents to Part 2 were supportive of the description of the issue (96% agreed) and were mainly in agreement with the list of alternatives identified (77% agreed). Substantive comments received from respondents included a need for a fuller understanding of user's needs to determine how they can be met, which could require a solution not presented as an alternative. There was also support for narrative reporting to focus on an NPO's objectives, its impact, the effectiveness of the organisation's governance structures and processes, and broader sustainability issues, rather than being restricted to financial statement analysis.
- BC 35.5 With respect to the alternatives put forward in the Consultation Paper, there was little support for the do-nothing alternative, which was widely seen as a missed opportunity. There was relatively even support amongst those providing a preference for the other alternatives, with the approach based on the Integrated Reporting Framework (50%) being slightly more favoured than an approach based on IASB/IPSASB guidance (37%).

- BC 35.6 Those favouring the IASB/IPSASB guidance approach indicated that it would complement the information in the financial statements and would be less complicated for NPOs to apply. Those favouring the Integrated Reporting Framework approach felt that, although more ambitious, it offered an opportunity for NPOs to apply emerging best practice and to deliver standardised narrative reporting based on stakeholder needs.
- BC 35.7 With respect to whether guidance should be set at the level of an overarching framework and high-level principles, or if specific reporting requirements or recommendations should be required instead, the majority of respondents noted that the diversity of NPOs and jurisdictions pointed to the need for a framework and principles solution. Some of these respondents noted, however, that this would need to be backed by detailed guidance on how to apply the framework and principles.

## Compulsory requirement

- BC 35.8 Analysis of the Consultation Paper responses supported a framework and principles-based approach that provides a mandatory core of narrative reporting requirements that could be applied by all NPOs. The approach proposed is adaptable, so that NPOs wishing to go beyond this core could do so provided that the mandatory topics and elements important to users of all NPO general purpose financial reports were met. The proposed approach is designed to ensure a base level of consistency and comparability amongst all NPOs applying the INPAG, while providing NPOs the freedom to move beyond this to meet the needs of the users of their general purpose financial reports.
- BC 35.9 Concerns were raised by the IFR4NPO project's Technical Advisory Group, the Practitioner Advisory Group and by attendees at additional outreach events, that requiring all NPOs to comply with narrative reporting requirements could act as a barrier to the adoption of INPAG.
- BC35.10 While feedback from these groups was that the narrative reporting proposals could bring significant benefit to both the users of the NPOs general purpose financial reports and the NPOs themselves, it is the case that international guidance in this area is not mandatory and there are only a few jurisdictions that mandate NPOs to produce general purpose financial reports and undertake this type of reporting.
- BC35.11 As such, whilst the Exposure Draft contains proposals for a mandatory core of narrative reporting, a specific matter for comment has been included to gain additional feedback on whether this should be mandatory for all NPOs.

## Narrative reporting proposal

- BC35.12 The narrative reporting requirements were developed as a mandatory framework, using a principles approach based on the existing IASB Practice Statement and IPSASB Recommended Practice Guidelines (RPGs) and jurisdictional-level frameworks. The IASB Practice Statement and IPSASB RPGs and jurisdictional-level frameworks were used instead of the Integrated Reporting Framework as they are expected to be less complicated for NPOs to apply and will complement the information in the financial statements rather than require NPOs to also apply broader integrated reporting principles.
- BC35.13 In developing these proposals, the requirements of the IASB Practice Statement, IPSASB RPGs and jurisdictional-level frameworks were tailored to meet the needs of users of NPO general purpose financial reports and to reflect the capacity and capability of the NPOs that the INPAG is initially aimed at.
- BC35.14 Under the proposals for narrative reporting, NPOs would need to:
- present information to enable users to understand what the performance objectives of the NPO are and what it has done during the reporting period in working towards those performance objectives; and
  - present commentary to discuss and analyse the NPO's financial statements.

- BC35.15 Reporting on these two areas was integrated where possible to reduce repetition and reflect their integrated nature, with the proposals requiring that NPOs provide mandatory information on defined topics:
- **Overview of the NPO** – contextual information that enables users to understand the NPO such as legal form, structure, governance, purpose, mission, vision, main activities and significant relationships.
  - **Performance information** – information on performance objectives and plans and what has been achieved with measures and descriptions to demonstrate performance being a mix of quantitative measures, qualitative measures and qualitative descriptions.
  - **Financial objectives and strategies** – users with an understanding of the NPOs financial objectives and strategies in relation to its financial position, income and expenditure, net assets and cash flows and how these support the achievement of its performance objectives.
  - **Analysis of financial statements** – information on significant changes and trends and how these impact on the achievement of its performance objectives.
  - **Description of principal risks and uncertainties** – information on principal risks and uncertainties and how these relate to the NPO's performance objectives and financial objectives and strategies. Any significant changes and how the NPO manages risks and uncertainties should also be included.
- BC35.16 Sitting alongside this mandatory requirement is a proposal that this information be presented in accordance with certain principles including:
- the performance information and financial statement commentary being for the same reporting NPO and reporting period as the financial statements;
  - in selecting and presenting the performance information and financial statement commentary the NPO should apply the qualitative characteristics and pervasive constraints on information in Section 2 Concepts and pervasive principles;
  - the NPO should also ensure that the performance information and financial statement commentary presented is fair and balanced; and
  - non-disclosure of aspects of performance information and financial statement commentary would be permitted where an NPO engages in 'sensitive' activities. This would mean that where the activities of the NPO would be compromised by aspects of the narrative report, for example specific humanitarian aid programs, this can be omitted.
- BC35.17 Permission to not disclose information was introduced to the proposals following recommendations from the project's Practitioner Advisory Group and a specific focus group that was created to provide additional advice to the INPAG Secretariat on narrative reporting. These groups noted that the mandatory nature of the narrative reporting proposals would cause difficulties for some NPOs if they were required to disclose information that could jeopardise the safety and security of staff, volunteers, or the public that benefit from the goods and services provided by the NPO. They also noted that subsequently requiring NPOs to disclose that they had made use of the permission to not disclose information on 'sensitive' activities could also be problematic, especially if this were to highlight the nature of substance of the information that was not being disclosed.
- BC35.18 It is recognised that there is the possibility that exercising a permission to not disclose sensitive information could be misused by NPOs as a way of hiding poor performance or financial problems that may have arisen with aspects of its operations, particularly if there were no requirements to disclose that information relating to 'sensitive' activities has been withheld. The project's Technical Advisory Group shared these concerns. As such, agreement was reached that where an NPO does use the sensitive information exemption, users should be required to disclosure that the narrative report has been prepared in accordance with the requirements of the sensitive information exemption paragraph. NPOs are not, however, required to provide any information that would have the effect of highlighting the nature or substance of the sensitive information.

## Extended transition period

BC35.19 It is recognised that for some NPOs, the narrative reporting required by INPAG might represent a challenge, particularly if the NPO is also transitioning to accrual accounting at the same time. Extensive guidance was developed to assist in implementing these requirements through the implementation guide and implementation examples. The option for an extended transition period of two years was supported by a focus group on narrative reporting, and this is being considered alongside other feedback as evidence of support for an extended transition period.

## Additional specific reporting requirements

BC35.20 Consultation Paper responses, and outreach feedback, did see some support for the inclusion of certain specific reporting requirements, including governance, objectives and risks. These are included as areas that the NPO would be required to report on in the mandatory topics, so have effectively been integrated into these narrative reporting proposals.

BC35.21 Climate reporting and broader sustainability reporting were also highlighted by some respondents to the Consultation Paper as specific topics for inclusion in NPO narrative reporting. Inclusion of these areas as mandatory requirements was also supported by the narrative reporting focus group.

BC35.22 It is recognised that this is an important area for NPOs and their users. Developments in climate reporting and sustainability reporting frameworks are ongoing, and have, to date, been aimed at the needs of private sector entities and their users. Given the broader challenges to introducing mandatory narrative reporting for NPOs, the INPAG Secretariat and the project advisory groups felt that it was premature to require sustainability reporting as a mandatory component of narrative reporting at the current time.

BC35.23 The proposed approach to narrative reporting does, however, permit NPOs to apply existing climate reporting and sustainability reporting frameworks should they wish to do so. This could be either through a specific climate and/or sustainability report or by reporting on the impacts of climate related issues and sustainability through the financial statement commentary and performance information presented in areas such as governance, strategy, risk, and performance measures and descriptions.

BC35.24 Developments in this area, and their impact on broader reporting requirements, are being actively monitored as part of the IFR4NPO project's ongoing work. Any changes to the requirements of Section 35 *Narrative reporting* to reflect them would be undertaken in accordance with due process.



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