

30 September 2022

Carolyn Cordery
Chair, New Zealand Accounting Standards Board
External Reporting Board
PO Box 11250
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Wellington 6142

Via email: accounting@xrb.govt.nz

Dear Carolyn

Tier 3 and 4 Not-for-Profit and Public Sector Reporting Consultation

ED 2022-5, Reporting Requirements for Tier 3 Not-for-Profit Entities
ED 2022-6, Reporting Requirements for Tier 4 Not-for-Profit Entities
ED 2022-7, Reporting Requirements for Tier 3 Public Sector Entities
ED 2022-8, Reporting Requirements for Tier 4 Public Sector Entities

As the representatives of over 300,000 professional accountants in Australia, New Zealand and around the world, CPA Australia and Chartered Accountants Australia and New Zealand (CA ANZ) welcome the opportunity to provide feedback on the above Exposure Drafts (EDs).

We are strong supporters of the not-for-profit (NFP) and public sectors (PS) as many of our members are involved in these sectors as advisors, auditors, employees and volunteers. We advocate in the public interest for requirements that promote the transparency of these sectors and their activities, to stakeholders and the public, in a way that minimises the complexity and cost for these entities. For these reasons, we are largely supportive of the amendments proposed to the reporting requirements for Tier 3 and Tier 4 NFP and PS entities.

Reporting requirements for Tier 4 entities

Compliance with reporting requirements is critical to enhancing and promoting public trust and to the integrity of the system. Therefore, the evidence gathered that identifies a relatively low level of compliance with the Tier 4 reporting requirements by charities is a concern. While professional accountants, including our members, have little difficulty in applying the Tier 4 reporting requirements, the same may not be the case for non-accountants with limited accounting or financial experience, who are often tasked with the preparation of Performance Reports.

We commend the External Reporting Board (XRB) for its efforts in significantly reducing the length and complexity of the Tier 4 Standards. However, we note that although reducing and/or simplifying reporting requirements can lead to improved compliance rates, there is no consensus that this is the best approach. Capability building is essential, and it is critical that those charged with governance of entities of all types and sizes possess the appropriate skillset, including financial literacy, to ensure these entities can fulfil their statutory obligations.

Reduced reporting requirements for “small” Tier 4 entities

We do not support the proposals to introduce reduced reporting requirements for “small” Tier 4 entities (total annual payments of less than \$10,000 for the current and previous financial years). We believe that the other proposed amendments, including the simplifications to the Tier 4 Standards, would be sufficient to result in an uplift in charity compliance rates, without the need for reduced reporting requirements for small Tier 4 entities. We are not aware of any similar demand or drivers for such concessions in the public sector.

Incorporating what is essentially two sets of reporting requirements, including a “reduced reporting requirements” approach for small Tier 4 entities, within a single standard appears contrary to the XRB’s financial reporting strategy of a multi-tiered approach that uses different tiers of accounting standards to match costs and benefits. Including reduced reporting requirements within the Tier 4 Standards is likely to add complexity, a potential outcome contrary to the fundamental objective of this project.

Recording transactions directly in accumulated funds

We do not support the proposals to recognise the effect of any transactions (other than transactions with owners) directly in accumulated funds. These proposals appear contrary to paragraph A138.1 (NFP) / A140.1 (PS) which states, “most transactions are recorded through the statement of financial performance rather than directly through the accumulated funds balance”.

In our view, only capital contributed by owners (which is uncommon for NFP and PS entities) should be recorded directly in accumulated funds. Instead, and ideally, such transactions should be presented below “operating surplus/(deficit)” in the statement of financial performance. This would enable an entity to separate these transactions from other revenue and expenses. We agree with the proposal to separately recognise within accumulated funds, any gain/loss movements relating to particular asset classes (a revaluation reserve for gains/losses on revalued property, plant and equipment).

The **Attachment** to this letter sets out our responses to the specific questions posed in the consultation papers. Unless otherwise specified, our comments relate to both the NFP and PS proposals within each Tier. If you have any questions about our submission, please contact either Ram Subramanian (CPA Australia) at ram.subramanian@cpaaustralia.com.au or Amir Ghandar (CA ANZ) at amir.ghandar@charteredaccountantsanz.com.

Yours sincerely

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Attachment

Specific matters for comment

Reporting Requirements for Tier 3 Not-for-Profit and Public Sector Entities (ED 2022-5 and ED 2022-7)

1. Do you agree with the proposed amendments relating to service performance reporting?

We support the proposed amendments relating to service performance reporting as they bring the requirements in the Tier 3 Standards more into line with those in the applicable Tier 2 Public Benefit Entities (PBE) Standard (i.e., PBE FRS 48 *Service Performance Reporting*). In particular, we support removing the requirements to report on “outcomes” and “outputs”, as the terms are not well understood, in favour of plain English requirements to disclose objectives and significant activities undertaken to achieve those objectives.

We note that there is reference to both “objectives” and “broader aims and objectives” in relation to service performance reporting. We recommend consistent terminology is used. Our preference is to use the former as it is simpler and shorter.

2. Do you agree with the proposal to include requirements for the revaluation of property, plant and equipment within the Tier 3 Standards, rather than require an entity to opt-up to Tier 2?

We support the proposal to include requirements for the revaluation of property, plant and equipment within the Tier 3 Standards rather than require an entity to opt up to the applicable Tier 2 PBE Standard (i.e., PBE IPSAS 17 *Property, Plant and Equipment*). When an entity elects to apply a Tier 2 PBE Standard, it is required to apply the whole Standard to all transactions of that type. Therefore, complying with the full requirements of the Tier 2 PBE Standard can be both complex and time consuming for a Tier 3 entity.

3. Do you agree with the proposal to require revaluation movements on property, plant and equipment to be recognised directly in accumulated funds through a revaluation reserve?

We do not agree with the proposal to recognise the revaluation movements on property, plant and equipment directly in accumulated funds. It is unclear why the proposed treatment is different to that proposed for changes in the market value of publicly traded financial investments when they have the same economic characteristics (i.e., unrealised gains/losses on assets).

We recommend that the accounting treatment of revaluation movements on property, plant and equipment be the same as the proposed treatment for changes in the market value of publicly traded financial investments, i.e., recognised as revenue or expenses in the statement of financial performance.

In addition, as noted in our cover letter, ideally such transactions should be presented below “operating surplus/(deficit)” in the statement of financial performance. We recommend that the presentation of revaluation movements on property, plant and equipment below “operating surplus/(deficit)” is incorporated into the alternative format of

the statement of financial performance in paragraph A48 (NFP) / A51.1 (PS). This would enable an entity to present these movements separately from other revenue and expenses on the basis that they are unrealised.

In our view the proposed treatment for revaluation gains and losses described below is overly complex:

- Require revaluation gains to be recognised directly in accumulated funds through a revaluation reserve, unless they reverse an impairment charge recognised in a prior financial year.
- Require revaluation losses to be recognised as an expense unless these losses offset any previous revaluation gains, in which case they would be recognised directly in accumulated funds.

The proposed treatment is likely to require increased record keeping to track the revaluation gains and losses, and therefore, in our view does not meet the objective of this project to “introduce simple requirements”.

For clarity, we agree with having a separate revaluation reserve within accumulated funds for revaluation movements on property, plant and equipment.

4. Do you agree with the proposal that investment property should be accounted for in the same manner as property, plant and equipment?

Subject to our comments in response to question 3 above regarding the treatment of revaluation gains/losses, we agree with the proposal to account for investment property in the same manner as property, plant and equipment because it meets the objective to “introduce simple requirements”.

5. Do you agree with the proposal to allow publicly traded financial investments to be measured at market value?

We agree with the proposal to allow publicly traded financial investments to be measured at market value because there are quoted prices in active markets and the value is easily and freely obtainable.

6. Do you agree with the proposal to require changes in the market value of investments to be recognised as revenue or expenses in the statement of financial performance?

We agree with the proposed treatment to require changes in the market value of publicly traded financial investments to be recognised as revenue or expenses in the statement of financial performance. Consistent with our response to question 3, we recommend that changes in the market value of public traded financial investments be presented as transactions below “operating surplus/(deficit)” in the statement of financial performance, and that this presentation is incorporated into the alternative format of the statement of financial performance in paragraph A48 (NFP) / A51.1 (PS). This would enable an entity to present these changes separately from other revenue and expenses on the basis they are unrealised.

7. Do you agree with the proposals to amend the required revenue and expense categories?

We support the proposed revenue and expense categories. We believe they will capture most transactions without the need for excessive use of the “other” categories line item.

Feedback from our members indicated a need for clarity around the differentiation between “government” and “non-government” sources in the Tier 3 Standards. We suggest providing additional guidance to provide clarity.

We also highlight some inconsistencies between the Tier 3 PS and NFP Standards. Paragraph A55.3 of the Tier 3 NFP Standard refers to “grants received from the government or other agencies”. The Tier 3 PS Standard uses the distinction “central or local government” and “non-government”. We question whether it is conceivable for revenue to be received from a government organisation that is not central or local government, and if so, how it would be categorised. We recommend using consistent terminology (e.g., “government organisations”) across and throughout the Tier 3 (and Tier 4) Standards and defining such terminology for consistency and clarity.

With respect to the Tier 3 NFP Standard, we acknowledge that the XRB is working closely with Charities Services, and we understand that the intention is for the revenue and expense categories in the standard to align with the Charities Services annual return. We support this outcome and emphasise the importance of this alignment to the charitable sector.

8. Do you agree with the proposals to amend the revenue recognition requirements for grant, donation, bequest and pledge funding?

We agree with the proposals to amend the revenue recognition requirements. We support taking a practical approach to the deferral of revenue recognition over a pure conceptual approach. Having to recognise revenue without a ‘use or return’ condition upon receipt can be problematic, where the associated costs related to the revenue are recognised in a different reporting period. Despite the disclosure of such unexpended funds, many users do not understand the substance of the transaction, and this can have unintended consequences for the entity concerned, such as potential reductions in future funding.

However, we recommend making it clear (e.g., in paragraph A65 (NFP) / A67 (PS)) that capital grants are included as part of these proposed changes and can be deferred, and that revenue is recognised as and when the asset is acquired or constructed, instead of upon receipt. Furthermore, we note there is no mention of capital grants in Table 1 in paragraph A64 of the Tier 3 PS Standard. We recommend that capital grants also be specifically referenced in paragraph A64 for the avoidance of doubt.

Finally, during our outreach with members we heard concerns from some preparers over the judgement involved in applying the definition of “significant”. We recommend that the XRB considers developing and providing additional guidance to assist with application.

9. Do you agree with the proposals to require an entity to provide enhanced note disclosure that explains the purpose for which accumulated funds are held?

We support the proposal to require disclosure of the purpose for which accumulated funds are held. Our view is that there is scope to improve the narrative description of an entity's accumulation strategy, purposes and restrictions, on the grounds of increased transparency and enhanced confidence in both the NFP and public sectors.

Funders are increasingly looking to fund fewer entities but do so more deeply and over longer periods. Assessing the activities undertaken by an entity to fulfil its stated objectives and its commitment to financial stability and longevity are core considerations for funders. Accumulating funds can enable entities to achieve better results over a longer period, by investing in people, assets, innovation, and growth. Being transparent about the purpose of accumulations can assist an entity in demonstrating its financial stability, sustainability and effectiveness to funders, other key stakeholders, and the public.

In particular, disclosures around any restrictions placed by external funders in respect of portions of accumulated funds can signal to funders and other stakeholders, the availability of free cashflows and other unrestricted resources for the funding of day-to-day activities and working capital requirements. Such disclosures can also fulfil an important accountability function in bringing about transparency with respect to the stewardship and management of funds that are earmarked by external providers of such funding for specific purposes. Accordingly, we suggest including an option for entities to include disclosures around portions of accumulated funds that are subject to restrictions imposed by external funders.

10. Do you agree with the proposals to remove the requirements related to restricted reserves?

As stated in our response to the previous question, we suggest including an option to disclose information around restricted reserves, but support the proposals to remove the requirement related to restricted reserves on the basis that revenue is allowed to be deferred in a wider set of circumstances, as proposed.

11. Do you agree with the proposed accounting for items of other comprehensive revenue and expense?

We do not agree with the proposal to recognise the effects of specific transactions directly in accumulated funds if, for a specific type of transaction, an entity elects to apply the requirements of a Tier 2 PBE Standard, and that Standard requires the effect of that transaction to be recognised in the statement of other comprehensive revenue and expense. Instead, we recommend that the effect of such transactions be recognised as revenue or expenses in the statement of financial performance, albeit below "operating surplus/deficit". In addition, we recommend that such transactions also be incorporated in the alternative format of the statement of financial performance in paragraph A48 (NFP) / A51.1 (PS), included below "operating surplus/(deficit)". This would enable an entity to present these transactions separately from other revenue and expenses.

For clarity, we agree that the effect of such transactions should be presented in "other reserves" within accumulated funds.

12. Do you have any comments on the new Appendix C?

We support moving all of the “opting up” requirements to the new Appendix C.

13. Do you agree with the proposed amendments to Section 3 Entity Information?

We support removing duplication and allowing cross-reference to other documents if, and only if, such documents containing entity information are publicly and freely available at the same time as the performance report.

14. Do you agree with the proposed amendments to the statement of cash flows?

We support aligning the categories within the statement of cash flows with the categories of revenue and expense in the statement of financial performance. It would be helpful if the categories within the statement of cash flows were presented in the same order in the Tier 3 Standards as the categories of revenue and expense in the statement of financial performance.

15. Do you agree with the proposed amendments to the definition of cash?

We support including short-term deposits in the definition of cash, as it aligns with the definition of “cash and cash equivalents” in the applicable Tier 2 PBE Standard (i.e., PBE IPSAS 2 *Cash Flow Statements*). There is currently confusion over whether term deposits are “bank accounts and cash” or “investments” so clarifying that short-term means “deposits with a maturity of three months or less from the date purchased” is helpful.

16. Do you agree with the proposed effective date of 1 April 2024, with early adoption permitted?

We agree with the proposed effective date and permitting early adoption.

17. Do you have any other comments on the proposals to amend the reporting requirements for Tier 3 entities?

The term “pledge” is introduced in paragraph A62 of the Tier 3 NFP Standard, and is used repeatedly, but inconsistently, and does not form part of the minimum revenue categories in paragraph A54. In contrast, the term “pledge” is only mentioned once in the Tier 3 PS Standard (at paragraph A67.4). For these reasons, and because such pre-commitments (pledges) may not be legally enforceable, we recommend removing the term from the Tier 3 Standards entirely.

It would be useful if the types of revenues in Table 1 in paragraph A64 of the Tier 3 PS Standard followed the same order as the minimum categories presented in paragraph A56 of the Tier 3 PS Standard. Likewise, we suggest a similar approach for the expenses in both the NFP and PS Standards.

The requirements introduced in paragraphs A37(c) and (d) of *Appendix A - Specific requirements - Entity Information* (Appendix A) both require a description of the entity’s governance arrangements. To avoid unnecessary duplication, we suggest removing the requirement in paragraph A37(c).

Paragraph A138 of Appendix A states that “Accumulated funds represents the owners’ financial interest in the entity and/or the net assets available to the entity to fulfil its objectives in the future.” This reference to “financial interest” is inconsistent with the definition of a PBE, i.e., “no financial return to equity holders”. It would be more appropriate if the explanation given in paragraph A138 does not refer to a “financial interest”.

Reporting Requirements for Tier 4 Not-for-Profit and Public Sector Entities (ED 2022-6 and ED 2022-8)

1. Do you agree with the proposed simplifications to the Tier 4 Standards (NFP and PS)?

We agree with the proposed simplifications to the Tier 4 Standards and are pleased to see that the length of the Tier 4 Standards has been reduced significantly as a direct consequence. In particular, we support the use of plain English, and the removal of the optional disclosures from the main body of the standards by including them as separate guidance material, so that the standards just contain the minimum reporting requirements.

2. Do you agree with the proposal to reduce reporting requirements for small Tier 4 entities?

As noted in our cover letter, we do not support the proposals to introduce reduced reporting requirements for “small” Tier 4 entities. We believe that the other amendments proposed to the Tier 4 Standards, especially the removal of the statement of resources and commitments, sufficiently reduces and simplifies the reporting requirements for all Tier 4 entities.

Incorporating what is essentially two sets of reporting requirements, including a “reduced reporting requirements” approach for small Tier 4 entities, within a single standard appears contrary to the XRB’s financial reporting strategy of a multi-tiered approach that uses different tiers of accounting standards to match costs and benefits. Including reduced reporting requirements within the Tier 4 Standards is likely to add complexity, a potential outcome contrary to the fundamental objective of this project.

We note, from the recently published [policy decisions](#) to modernise the *Charities Act 2005* (policy decisions), the desire of the Minister for the Community and Voluntary Sector to reduce the reporting requirements for small charities. We also note from the [Charities Amendment Bill](#) that the Department of Internal Affairs (DIA) Chief Executive will have the power to exempt “very small” charities from preparing general purpose financial reports (i.e., using the XRB standards). The threshold will be developed in regulations but is suggested to be annual payments under \$10,000 and total assets under \$30,000. Such charities will still be required to file an annual return with Charities Services containing specified financial information, an approach which we support as it achieves conceptual alignment with “small” (as defined) Australian registered charities.

3. Are there any proposed reporting concessions for small Tier 4 entities you do not support?

See our response to question 2.

4. Are there any other reporting concessions for small Tier 4 entities that should be considered?

See our response to question 2.

5. Do you agree with the proposed amendments to the service performance reporting requirements?

We support the proposed amendments relating to service performance reporting as they bring the requirements in the Tier 4 Standards more into line with those in the applicable Tier 2 PBE Standard (i.e., PBE FRS 48 *Service Performance Reporting*). In particular, we support removing the requirement to report on “outcomes” and “outputs”, as the terms are not well understood, in favour of plain English requirements including the description and quantification of significant activities undertaken during the year.

We note there is reference to both “objectives” and “broader aims and objectives” in relation to service performance reporting. We recommend that consistent terminology be used. Our preference is the former as it is simpler and shorter.

6. Do you agree with the proposals to amend the required cash received and cash paid categories?

We support the proposed cash received and cash paid categories. We believe they will capture most transactions without the need for excessive use of the “other” categories line item.

However, we are unsure whether the following categories of cash received in the Tier 4 PS Standard are appropriately named:

- General funding received from central or local government
- Donations, koha, and bequests from the public
- Grants from non-government organisations
- Funding from service delivery grants/contracts

Feedback received from our members indicates a need for clarity around the differentiation between “central and local government” and “non-government” sources of cash received in the Tier 4 PS Standard, especially when the source of “funding from service delivery grants/contracts” is not specified. We question whether it is conceivable for cash to be received from a government organisation that is not central or local government, and if so, how it would be categorised. On the contrary, the Tier 4 NFP Standard categories of cash received are solely based on the type of funding as opposed to the source. Therefore, we recommend taking the same approach in the Tier 4 PS Standard for consistency.

Also, we note that the Tier 4 NFP Standard has “Interest or dividends received”, whereas the Tier 4 PS Standard has “Interest or dividend income received”. We recommend that these terms be aligned as we see no reason for them to differ.

With respect to the Tier 4 NFP Standard, we acknowledge that the XRB is working closely with Charities Services in the development of the proposals. We understand that the intention is for the categories of cash received, and cash paid, in the Standard to align with the Charities Services annual return. We support this intention and emphasise the importance of this alignment to the charitable sector.

7. Do you agree with the proposal to remove the Statement of Resources and Commitments from the Tier 4 (NFP) Standards and instead require note disclosure about any significant assets or liabilities?

We support the proposal to remove the statement of resources and commitments from the Tier 4 NFP Standard. For clarity, although this question is not raised in the consultation on the Tier 4 PS Standard our view is that the statement should also be removed from that Standard. We believe this proposed removal alone will improve compliance rates considerably. Feedback received from our members suggests that this requirement causes confusion, with entities trying to make the statement balance by bringing in accrual concepts. The resulting performance report then becomes a hybrid of cash and accrual, which is not aligned with the objectives of the Tier 4 Standard.

We support the proposal to require disclosure of any significant assets and liabilities in the notes to the performance report. However, during our outreach with members we heard concerns from some preparers over the judgement involved in applying the definition of "significant". Additional guidance may be needed on what constitutes "significant".

8. Do you agree with the proposed effective date of 1 April 2024, with early adoption permitted?

We agree with the proposed effective date and permitting early adoption.

9. Do you have any other comments on the proposed improvements to the Tier 4 Standards?

We recommend further consideration be given to the current requirement for consolidation within the Tier 4 Standards. For cost/benefit reasons, we do not believe this should be a requirement for Tier 4 entities. At the time of writing this submission, we note that the Australian Accounting Standards Board is considering including consolidation as an option only in its proposed Tier 3 simplified accounting requirements for smaller NFP entities in Australia. We question the rationale for a higher financial reporting requirement for New Zealand NFPs compared to their Australian equivalents. For clarity, we agree that for the purpose of applying the legislative size threshold, where an entity has controlled entities, total operating payments means the combined operating payments of the entity and all its controlled entities.¹

In the Tier 4 NFP Standard, Table 2 is in the middle of paragraph 73. We believe it should be positioned at the end of paragraph 72.

The Tier 4 NFP Standard has a 'Summary of Required Information' on page 6 which provides a useful summary of minimum information required to comply with the Standard. However, there does not appear to be the same summary in the Tier 4 PS Standard. We recommend an equivalent summary be added to the Tier 4 PS Standard.

¹ XRB A1 *Application of the Accounting Standards Framework*, Par. 42A