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ACCOUNTING NEWS

AUSTRALIA HAS EXPANDED ITS WHISTLEBLOWING PROVISIONS

As a sport loving society, we are so accustomed to seeing the umpire or referee blow their whistle to rectify the transgression of one player against another or a breach of the rules of a game of sport. Yet in our professional lives the concept of 'blowing the whistle' doesn't seem to hold the same allure and for some compelling reasons.

Whistleblowing is defined by Transparency International as "*the disclosure of information related to corrupt, illegal, fraudulent or hazardous activities (including perceived or potential wrongdoing) being committed in or by public or private sector organisations – which are of concern to or threaten the public interest – to individuals or entities believed to be able to effect action*."

One fact remains, effective whistleblowing is essential in *"fostering integrity and accountability while deterring and exposing misconduct, fraud and corruption"*.

There are remarkable whistleblower stories such as the story of Toni Hoffman, an Australian nurse who exposed, through a whistleblower program, the medical malpractice of surgeon Jayant Patel. As a result, Hoffman received the 2006 Australian of the Year Local Hero Award and an Order of Australia Medal for her role as a whistleblower. While there are several positive examples of whistleblowers in Australia, such as the story of Toni Hoffman, Australia's whistleblower protection laws have long been criticised for leaving whistleblowers feeling vulnerable rather than protected.

Having been involved in a large number of investigations where whistleblower information has led to the discovery of significant fraud, corruption and in one case abuse, it has always concerned us that whistleblower protections are often inadequate and expose the whistleblower to potential fallout resulting from the investigation. In one case, the whisteblower, a Government executive, had their employment terminated on the spot because of their disclosure.

This is especially so in the private sector where protections are limited. In one case, we had to recommend a private sector whistleblower be placed under protective surveillance for a period of time, costing the client significantly. However, change is on the horizon.

Following the passage of the *Treasury Laws Amendment (Enhancing Whistleblowers Protections) Bill 2018* (**Whistleblower Bill**) through Parliament on 19 February 2019, new Federal whistleblower legislation was enacted on 19 March 2019. After modification on 4 April 2019, the new legislation took effect on 1 July 2019.

IN THIS EDITION

In this edition, we update you on recent regulatory activity with regard to expanded whistleblowing legislation. With respect to Australian developments, we draw your attention to the new Conceptual Framework and how it will apply to Australian entities.

We continue to explore further aspects of the 'triple threat' accounting standards. This month we illustrate Step Four and how variable consideration is allocated to performance obligations. We also remind you that the new expected credit loss model must be applied to intercompany loans receivable from subsidiaries, investments in associates/joint ventures and other related parties (including key management personnel).

Our not-for-profit section reviews recent proposals to amend the definition of 'not-for-profit entities' in Australian Accounting Standards (ED 291), and we continue our focus on whether AASB 15 or AASB 1058 applies to income received. This month we focus on grant contracts to conduct research which do not include 'sufficiently specific' performance obligations.

Lastly, in international developments, we summarise some recent agenda decisions of the IFRS Interpretations Committee.

AMENDMENTS TO OTHER LEGISLATION

The new whistleblower legislation amends and enhances the:

- *Corporations Act 2001* to consolidate and broaden the existing protections and remedies for corporate and financial sector whistleblowers
- *Taxation Administration Act 1953* to create a whistleblower protection regime for disclosures of information by individuals regarding breaches of the tax law or misconduct relating to an entity's tax affairs, and
- *Banking Act 1959*, *Insurance Act 1973*, *Life Insurance Act 1995* and *Superannuation Industry (Supervision) Act 1993* to make consequential amendments.[1]

[1] *The whistleblowing provisions in the Banking Act 1959, the Insurance Act 1973, the Life Insurance Act 1995 and the Superannuation Industry (Supervision) Act 1993 have been repealed, and replaced by the new provisions in the Corporations Act.*

KEY FEATURES OF THE NEW WHISTLEBLOWER REGIME

Key features of the new whistleblower regime include, but are not limited to:

- The new legislation expands whistleblower protections regarding all Australian companies and gives public and large proprietary Australian companies until 1 January 2020 to introduce a whistleblower policy that is compliant with the new legislation, or else companies may face fines of up to $12,600
- The new legislation has increased penalties for breaches of whistleblower protections, reaching up to $10.5 million
- It includes a requirement that the whistleblower has objectively reasonable grounds to suspect wrongdoing
- Victimisation and compensation provisions apply to protected disclosures made at any time
- Disclosures may now be made anonymously
- It extends the criteria of wrongdoing that qualifies for protection and sets out who is eligible for whistleblower protection. This expands to employees (current and former), officers, suppliers and their employees, an individual who is an associate of the entity, and family members of any of these eligible people, and
- It excludes disclosures of personal work-related grievances from the protected disclosures.

THE IMPORTANCE OF WHISTLEBLOWING IN THE WORKPLACE

Whistleblowers are an important source to detect cases of fraud and misconduct in the workplace and they often provide pivotal evidence for a successful prosecution. By promoting a whistleblowing culture, the company encourages transparency and integrity in the workplace.

However, in practice, there are limitations to having anonymous disclosures given that the information can be dismissed by virtue of perceived unreliability. In some cases, the information provided is too broad or ambiguous such that investigating the disclosure would require following up the whistleblower. This can be challenging or even impossible in some cases if the company has no means of contacting the person directly to provide additional information regarding the disclosure. This is why having a sound whistleblower program in place is extremely important to ensure that all disclosures can be properly investigated whilst protecting the anonymity of the person.

WHAT DOES IT MEAN FOR YOUR BUSINESS?

Companies should update their respective policies to reflect the significant changes made to Australia's whistleblower legislation prior to the 1 January 2020 deadline. Under the new legislation, all public companies and large proprietary companies must have a policy containing:

1. Information about the protections available to whistleblowers
2. How the company will ensure fair treatment of employees who are mentioned in whistleblower disclosures, and
3. Any matters prescribed by regulation.

This policy must be made available to all people who may be eligible whistleblowers in relation to the company. This requirement applies to all public companies and all proprietary companies that have become large proprietary companies for any financial year on any day in any later financial year that is at least six months after the last day of the first financial year. For example, companies with 30 June year-ends would need to have policies in place by 1 January 2020 and those with 31 December year-ends by 1 July 2020.

In addition, whistleblowers must know where, how, when to report; and that their identity as a whistleblower will be kept confidential. Raising awareness of the importance of whistleblowers can promote a 'speak up' culture and de-stigmatise the disclosure of wrongdoing. Therefore, businesses will need to implement comprehensive training across the organisation to ensure that whistleblower protections are recognised and dealt with upmost confidentially.

MORE INFORMATION AND ASSISTANCE

For information about how BDO can assist you with implementing these changes, please contact Adam Simms, Partner - Forensic Services.

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NEW CONCEPTUAL FRAMEWORK – WHO WILL IT APPLY TO AND WHEN?

In May 2019, the Australian Accounting Standards Board (AASB) issued *Conceptual Framework for Financial Reporting* (the new Conceptual Framework).

WHEN IS IT EFFECTIVE?

The new Conceptual Framework applies to periods beginning on or after 1 January 2020.

HOW WILL THE NEW CONCEPTUAL FRAMEWORK IMPACT FINANCIAL STATEMENTS IN FUTURE?

Australian Accounting Standards and Interpretations govern the accounting for many types of transactions and balances. Where there are 'gaps', AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*, paragraph 10 requires management to apply judgement in developing an appropriate accounting policy. In making this judgement, where Australian Accounting Standards do not deal with similar and related issues, paragraph 11(b) requires management to then refer to the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses laid out in the new Conceptual Framework.

As the new Conceptual Framework is different to its predecessor, entities looking to the new Conceptual Framework to develop accounting policies under AASB 108, paragraph 11(b) will need to take note of the:

- Updated definitions of an 'asset' and 'liability'
- Updated recognition criteria for including assets and liabilities in financial statements
- New concepts on measurement, including factors to consider when selecting a measurement basis (e.g. cost vs fair value)
- New concepts on presentation and disclosure, including classifying items as income vs other comprehensive income, and
- New guidance on derecognition of assets and liabilities.

CHANGES RELATING TO 'REPORTING ENTITIES'

The new Conceptual Framework applies to 'reporting entities', which paragraph 3.10 describes as effectively being all entities that are required, or choose, to prepare financial statements.

> A reporting entity is an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity.
>
> **Conceptual Framework for Financial Reporting, paragraph 3.10**

This is different to the concept of a 'reporting entity' in SAC 1 *Definition of a Reporting Entity*, which currently permits the preparation of special purpose financial statements if users are not dependent on general purpose financial statements for information to make and evaluate resource allocation decisions.

WHO WILL IT APPLY TO?

Without any Australian-specific amendment, all entities that are required, or choose to prepare, financial statements in Australia would be required to apply the new Conceptual Framework because they would be considered 'reporting entities'.

> This means that special purpose financial statements would no longer be permitted for entities:
>
> - Required to prepare financial statements applying Australian Accounting Standards (for example, as required by Part 2M of the *Corporations Act 2001* or a trust deed/agreement), and
> - That voluntarily prepare financial statements applying Australian Accounting Standards.

As part of its phased approach in scrapping special purpose financial statements, the AASB has therefore limited application of the new Conceptual Framework to only the following types of **for-profit entities**:

- Private sector entities that have public accountability and are required by legislation to comply with Australian Accounting Standards, and
- Other entities that voluntarily elect to apply the new Conceptual Framework.

This scope limitation is effective for periods beginning on or after 1 January 2020 by:

- Adding scope paragraph Aus 1.1 in the Australian version of the new Conceptual Framework to limit application to the types of for-profit entities noted above, and
- AASB 2019-1 *Amendments to Australian Accounting Standards – References to the Conceptual Framework* adding 'Aus' paragraphs to the *Framework for the Preparation and Presentation of Financial Statements* (old Framework) and SAC 1 *Definition of a Reporting Entity* such that the for-profit entities noted above cannot apply these documents from 1 January 2020.

WHAT ARE PUBLICLY ACCOUNTABLE ENTITIES?

In addition to entities whose debt or equity instruments are traded in a public market (or are in the process of issuing such instruments for trading in a public market), AASB 1053 *Application of Tiers of Australian Accounting Standards* (as amended by AASB 2019-1) clarifies that publicly accountable entities are those that hold assets in a fiduciary capacity for a broad range of outsiders as one of its primary businesses. These are likely to include banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.

The following types of entities that hold assets in a fiduciary capacity, but are doing so for reasons **incidental to the primary business,** are not automatically publicly accountable:

- Real estate agents
- Travel agents
- Schools
- Charitable organisations
- Co-operatives requiring a nominal membership deposit
- Sellers receiving an advance payment for goods or services such as utility companies.

WHAT OTHER AMENDMENTS DOES AASB 2019-1 ADDRESS?

AASB 2019-1 also makes consequential amendments to various Australian Accounting Standards and Interpretations to update references and quotations so that they refer to the new Conceptual Framework rather than the old.

STEP FOUR – ALLOCATING THE TRANSACTION PRICE (VARIABLE CONSIDERATION) TO PERFORMANCE OBLIGATIONS WHEN RECOGNISING REVENUE

In the April 2018 edition of Accounting News, we discussed the five-step model for revenue recognition introduced by IFRS 15 *Revenue from Contracts with Customers*:

Step 1	Identify the contract(s) with the customer
Step 2	Identify the performance obligations in the contract
Step 3	Determine the transaction price
Step 4	Allocate the transaction price to the performance obligations
Step 5	Recognise revenue when a performance obligation is satisfied

Since then we have included a number of articles on IFRS 15 in Accounting News that cover various issues from the five-step process in greater depth:

Step		Accounting News edition…
1	Identify the contract(s) with the customer	May and June 2018
2	Identify the performance obligations in the contract	July and September 2018
3	Determine the transaction price	November 2018, February 2019, March 2019 and May 2019
4	Allocate the transaction price to the performance obligations	June 2019
5	Recognise revenue when a performance obligation is satisfied	

In our June 2019 Accounting News article we demonstrated how the transaction price, including discounts, is allocated to separate performance obligations. In this article, we continue our examination of Step four and show how variable consideration is allocated to performance obligations.

WHAT IS 'VARIABLE CONSIDERATION'?

Variable consideration is consideration that is not fixed. It is estimated in Step three and includes items such as discounts, rebates, refunds, credits, price concessions, etc., as well as amounts that are contingent.

> An amount of consideration can vary because of discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties or other similar items. The promised consideration can also vary if an entity's entitlement to the consideration is contingent on the occurrence or non-occurrence of a future event. For example, an amount of consideration would be variable if either a product was sold with a right of return or a fixed amount is promised as a performance bonus on achievement of a specified milestone.
>
> **IFRS 15, paragraph 51**

HOW IS VARIABLE CONSIDERATION ALLOCATED TO PERFORMANCE OBLIGATIONS?

Variable consideration may be attributable either to:

- The entire contract, or
- Specific part(s) of the contract.

If allocating to specific part(s) of a contract, variable consideration may be attributed to:

- **One or more, but not all, performance obligations**. For example, a bonus may be contingent on the vendor transferring a good or service within a specified period of time
- **One or more, but not all, distinct goods or services promised in a series of distinct goods or services that forms part of a single performance obligation**. This would apply if, for example, the consideration promised for the second year of a two-year maintenance service contract will increase based on movements in CPI.

WHEN IS VARIABLE CONSIDERATION ALLOCATED TO A SINGLE PERFORMANCE OBLIGATION?

A variable amount of consideration (and subsequent changes to that amount) is allocated entirely to a single performance obligation (or a distinct good or service that forms part of a single performance obligation to transfer a series of distinct goods or services that are substantially the same) if both:

- The terms of a variable payment relate specifically to the vendor's efforts to satisfy the performance obligation or transfer the distinct good or service (or to a specific outcome from satisfying the performance obligation or transferring the distinct good or service), and
- The allocation of the variable amount in its entirety to a performance obligation or distinct good or service is consistent with the objective that the selling price is allocated to each performance obligation in order to reflect the consideration to which the vendor expects to be entitled in exchange for the good or service.

EXAMPLE ONE (BASED ON IFRS 15 ILLUSTRATIVE EXAMPLE 35 – CASE A)

ABC Limited enters into a contract with a customer for two licences of intellectual property (Licences X and Y).

Assume each licence represents a separate performance obligation, which is satisfied at a point in time (the transfer of each licence to the customer). Licence Y is transferred to the customer at inception and Licence X three months later.

The **stand-alone selling prices** of the licences are:

- Licence X $800
- Licence Y $1,000

The prices **specified in the contract** are as follows:

- Licence X $800 (fixed amount)
- Licence Y Royalty payment of 3% of the selling price of the customer's future sales of products that use the intellectual property to which Licence Y relates.

ABC Limited estimates that the amount of sales-based royalties that it will be entitled to in respect of Licence Y (variable consideration) will be approximately $1,000.

ALLOCATION OF TRANSACTION PRICE TO LICENCE X AND Y

ABC Limited then determines the allocation of the transaction price to each of the two licences and concludes that it should be as follows:

- Licence X - $800
- Licence Y - The variable royalty payment.

The transaction price is allocated as noted above because both of the following conditions apply (IFRS 15, paragraph 85):

- The variable payment relates solely to the transfer of Licence Y (the subsequent royalty payments), and
- The fixed amount of consideration for Licence X, and the estimated amount of sales-based royalties for Licence Y, are equivalent to their stand-alone selling prices (i.e. consistent with the allocation objective in IFRS 15, paragraph 73).

In contrast, the allocation of variable consideration will be different if the prices included in a contract do not reflect stand-alone selling prices.

TIMING OF REVENUE RECOGNITION

ABC Limited recognises revenue for Licences X and Y as follows:

Licence	When revenue recognised?
X	On transfer to customer (three months after contract inception)
Y	When subsequent sales of the customer's products that use Licence Y take place (IFRS 15, paragraph B63).

EXAMPLE TWO (BASED ON IFRS 15 ILLUSTRATIVE EXAMPLE 35 – CASE B)

Assume the same facts as for Example one above, except that the prices included in the contract are:

- Licence X $300 (fixed amount)
- Licence Y Royalty payment of 5% of the selling price of the customer's future sales of products that use the intellectual property to which Licence Y relates.

ABC Limited estimates that the amount of sales-based royalties that it will be entitled to in respect of Licence Y will be approximately $1,500.

Licence Y is transferred to the customer at inception and Licence X is transferred three months later.

ALLOCATION OF TRANSACTION PRICE TO LICENCE X AND Y

In this case, although the variable payments relate solely to the transfer of Licence Y (the subsequent royalty payments), allocating the variable consideration only to Licence Y would be inappropriate. This is because allocating $300 to Licence X and $1,500 to Licence Y would not reflect a reasonable allocation based on the stand-alone selling prices of those two licences (i.e. $800 for Licence X and $1,000 for Licence Y).

Fixed consideration

Instead, the fixed amount receivable in respect of Licence X is allocated to the two licences on the basis of their stand-alone selling prices. This allocation is calculated as:

Licence	Allocation of fixed revenue ($300)	
X	$133	(800 / 1800) x $300
Y	$167	(1,000 / 1,800) x $300
	$300	

ABC Limited then recognises fixed revenue for Licences X and Y as follows:

Licence	When revenue recognised?	How much?
X	On transfer to customer (three months after inception of contract)	$133
Y	On transfer to customer (at inception of contract)	$167
		$300

Sales-based royalties

Recognition of the royalty income allocated to each of the two licences will be deferred to future periods because IFRS 15 requires that royalty income is only recognised when the related product sales take place (IFRS 15, paragraph B63).

In contrast to Example one above, **ABC Limited allocates royalty income from Licence Y to Licences X and Y on a relative stand-alone selling price basis**.

Although the royalty income relates solely to the transfer of Licence Y, the allocation of the fixed selling price of Licence X, and the estimate of sales-based royalties to be generated by Licence Y, is disproportionate in comparison with the stand-alone selling prices of the two licences, i.e. there was pricing interdependency. This means that some of the royalty income to be generated by Licence Y in fact relates to the sale of Licence X, and some of the licence fee specified in the legal contract as relating solely to Licence X relates in part to the sale of Licence Y.

Assume that in the first month, royalties due from the customer's first month of sales is $200.

Licence	Allocation of royalties – Month 1 ($200)	
X	$89	*(800 / 1800) x $200*
Y	$111	*(1,000 / 1,800) x $200*
	$200	

ABC Limited then recognises royalty revenue for Licence Y as follows:

Licence	When revenue recognised?	How much?
X	On transfer to customer (three months after inception of contract)	$89
Y	At the end of Month 1	$111
		$200

The journal entry to record the royalties in Month 1 is:

	Dr ($)	Cr ($)
Receivable	200	
Revenue - Licence Y[1]		111
Contract liability – Licence X[2]		189

Notes:

1. *Performance obligation satisfied at inception of contract*
2. *Performance obligation satisfied three months after inception of contract*

NEW EXPECTED CREDIT LOSS MODEL APPLIES TO INTERCOMPANY LOANS

Most preparers of financial statements for 30 June 2019 are aware of the change in the way provisioning (impairment allowances) are calculated for financial assets such as loans receivable, trade debtors and contract assets under IFRS 15 *Revenue from Contracts with Customers*.

IFRS 9 *Financial Instruments,* effective for periods beginning on or after 1 January 2018 (30 June 2019 year-ends), requires impairment allowances to be recognised on the basis of expected, rather than incurred credit losses.

However, many are not aware that this new 'expected credit loss model' (ECL) also applies to intercompany loans and loans to key management personnel.

WHAT TYPES OF INTERCOMPANY LOANS ARE IMPACTED?

Intercompany loans impacted by the new ECL model include those made to:

- Subsidiaries
- Joint ventures and associates
- Other related parties, and
- Key management personnel.

Applying IFRS 9 to related company loans can present a number of application challenges as they are often advanced on terms that are not arms-length or sometimes advanced on an informal basis without any terms at all. In addition, they can contain features that expose the lender to risks that are not consistent with a basic lending arrangement. Preparers need to be aware of these issues when applying IFRS 9.

WHY LOANS TO SUBSIDIARIES IF THESE ELIMINATE ON CONSOLIDATION?

While loans to subsidiaries eliminate on consolidation, and are therefore excluded from consolidated financial statements, preparers need to remember that financial statements prepared under Part 2M.3 of the *Corporations Act 2001* must disclose additional parent summarised balance sheet information as required by Regulation 2M.3.01 *Disclosures required by notes to consolidated financial statements-annual financial reports*.

In making these additional parent entity disclosures, the ECL model must be applied when determining appropriate amounts of total current assets, and total assets, of the parent entity.

LOANS TO JOINT VENTURES AND ASSOCIATES

Many groups fund the operations of associates and joint ventures using long-term loan funding rather than injecting equity, particularly in the exploration industry. Such loans do not eliminate on consolidation and must be tested for impairment using the ECL model in the group financial statements.

Amendments to IAS 28 *Investments in Associates and Joint Ventures* (AASB 2017-7 *Amendments to Australian Accounting Standards – Long-term interests in Associates and Joint Ventures*, which have not yet been fully compiled into the latest version of AASB 128 on www.aasb.gov.au), also need to be noted. The process for determining impairment on long-term interests that in substance form part of the entity's net investment in an associate or joint venture (and the equity method is not applied) is as follows:

STEP 1: Determine if the interest is in the scope of IAS 28 or IFRS 9

STEP 2: Apply IFRS 9 ECL model to the long-term interest

STEP 3: Apply the equity method to equity interests

STEP 4: Allocate remaining losses to the long-term interest

STEP 5: Apply IAS 28 impairment indicators to the net investment and, if there is objective evidence of impairment, apply IAS 36

The amendments clarify that the ECL is applied to long-term interests before allocating any remaining equity accounted losses, and the final IAS 28 impairment test (based on the incurred loss model) is a 'catch all' test which is conducted last.

These changes could have a significant impact on the carrying amount of long-term loans to associates and joint ventures because currently impairment testing is typically 'left until last' and determined using the incurred loss rather than the ECL model.

While the AASB 2017-7 amendments only apply for periods beginning on or after 1 January 2019 (and therefore do not technically apply to 30 June 2019 year-ends), we recommend that these are considered because they serve to clarify the process, rather than being a new requirement. Financial statements for the half-year ending 30 June 2019 must apply these amendments.

OTHER RELATED PARTIES

Loans to other related parties also do not eliminate on consolidation and the ECL model must be applied to such balances in the consolidated financial statements.

KEY MANAGEMENT PERSONNEL – DON'T FORGET DISCLOSURES

It is important to remember that the ECL model also applies to loans granted to key management personnel (KMPs).

While expected credit losses on these loans may not be material in quantitative terms, they are likely to be considered qualitatively material. Additional disclosures are therefore required by IAS 24 *Related Party Disclosures* and in remuneration reports for listed entities.

For each type of related party loan receivable, including loans to KMPs, IAS 24, paragraph 18 requires entities to disclose information such as:

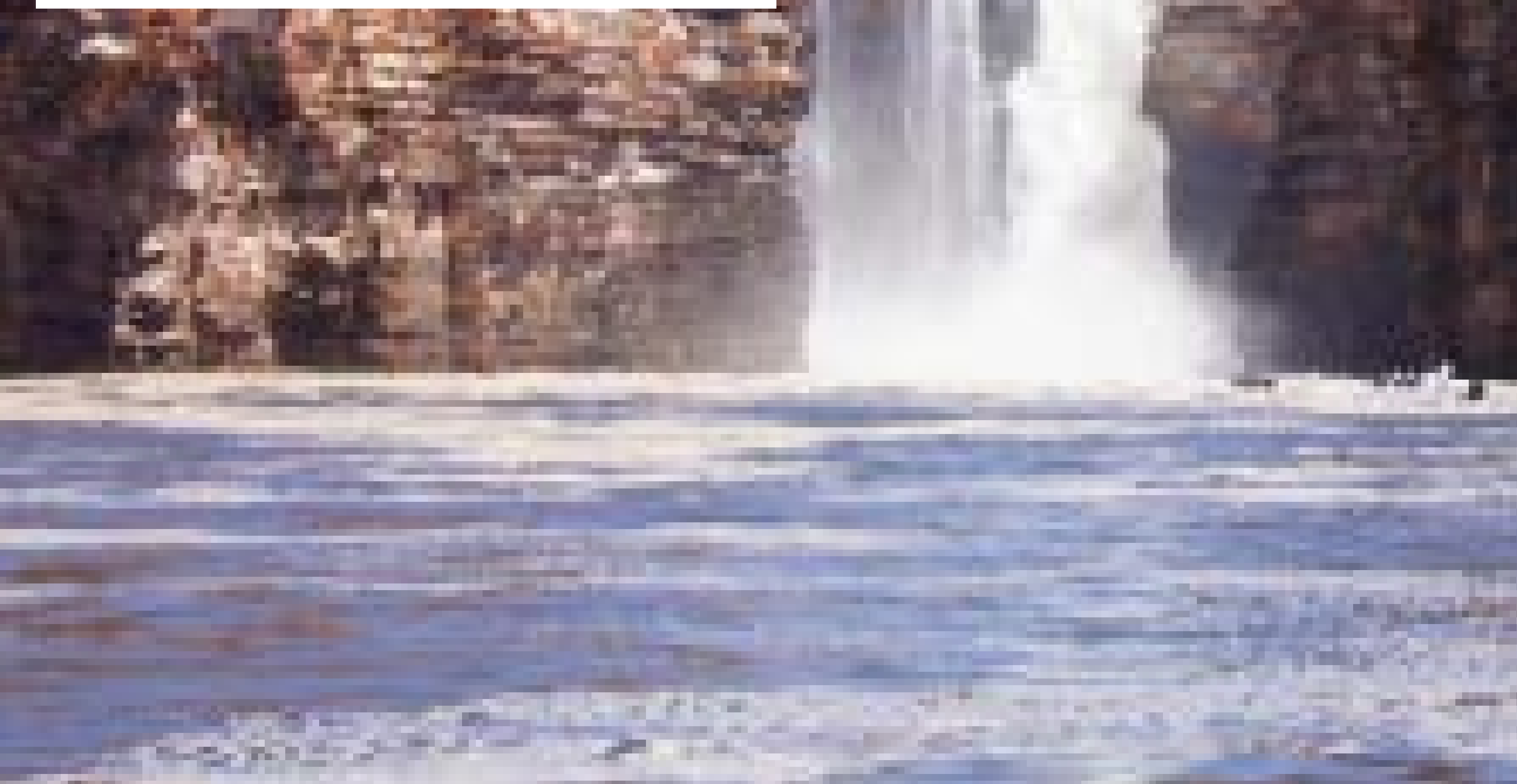
- The amount of outstanding balances, and
- Provisions for doubtful debts related to the amount of outstanding balances.

Listed entities will additionally be required to disclose information about the amount of impairment allowances for loans to KMPs:

- In aggregate for all loans to KMPs – refer *Corporations Regulation 2M.3.03(1) item 20(d)*
- For each KMP - where the loan is greater than $100,000 during the reporting period - refer *Corporations Regulation 2M.3.03(1) item 21(d)*.

MORE INFORMATION

BDO's IFRS in Practice - Applying IFRS 9 to Related Company Loans sets out a summary of the key requirements of IFRS 9 (focusing on those that are likely to be most relevant to related company loans) and uses examples to illustrate how these requirements could be applied in practice.



PROPOSED CHANGES TO NOT-FOR-PROFIT ENTITY DEFINITION

Australian Accounting Standards currently follow a 'transaction neutral' approach, whereby similar transactions and events are generally accounted for in a similar manner by all types of entities (i.e. both for-profit and not-for-profit entities). However, not-for-profit entities (NFPs) are required to account for some items differently. For example, revaluation increments and decrements relating to an item of property, plant and equipment of NFPs are offset between assets in a particular class, whereas revaluations by for-profit entities are determined on an individual asset basis, and there is no offsetting.

WHY THE NEED TO CHANGE THE NFP DEFINITION?

Because of the differences outlined above, it is critical that preparers of financial statements appropriately classify an entity as being 'for-profit' or 'not-for-profit' so that the appropriate recognition, measurement and disclosure requirements are applied.

As part of the Australian Accounting Standards Board's (AASB's) consultation on its standard-setting framework in 2017, respondents supported keeping the term 'not-for-profit entity' but requested additional guidance on how to distinguish for-profit and NFPs in practice.

Respondents also supported using the New Zealand Accounting Standards Board's (NZASB's) updated definition of 'public benefit entity' (PBE) because it gives greater focus on what a NFP is, rather than what it is not. That is, the term 'not-for-profit entity' is currently defined in Australian Accounting Standards as:

"…an entity whose principal objective is not the generation of profit…"

PROPOSED NEW DEFINITION OF A NFP ENTITY

In June 2019, the Australian Accounting Standards Board issued Exposure Draft ED 291 *Not-for-Profit Entity Definition and Guidance* which proposes to amend the definition of 'not-for-profit entity' in Australian Accounting Standards.

The ED proposes to keep the term 'not-for-profit entity' but replace the definition with the updated New Zealand definition of 'public benefit entity' as follows:

"…an entity whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders…"

HOW WILL THE NEW DEFINITION BE IMPLEMENTED?

ED 291 proposes removing the definition of NFP from AASB 102 *Inventories*, AASB 116 *Property, Plant and Equipment* and AASB 136 *Impairment of Assets*, and including the revised definition and guidance in a separate standard, AASB 1057 *Application of Australian Accounting Standards*.

IMPLEMENTATION GUIDANCE

The Implementation guidance to be included as part of AASB 1057 will help entities to determine whether they are NFPs. The ED proposes extensive discussion on:

- The definition of a NFP
- Indicators (including stated objectives, nature of the benefits and quantum, primary beneficiaries of the benefits, nature of equity interests, purpose and use of assets and nature of funding)
- Conflicting indicators, and
- Changing classification.

ILLUSTRATIVE EXAMPLES

These are also be included as part of AASB 1057 and include examples for the following types of entities:

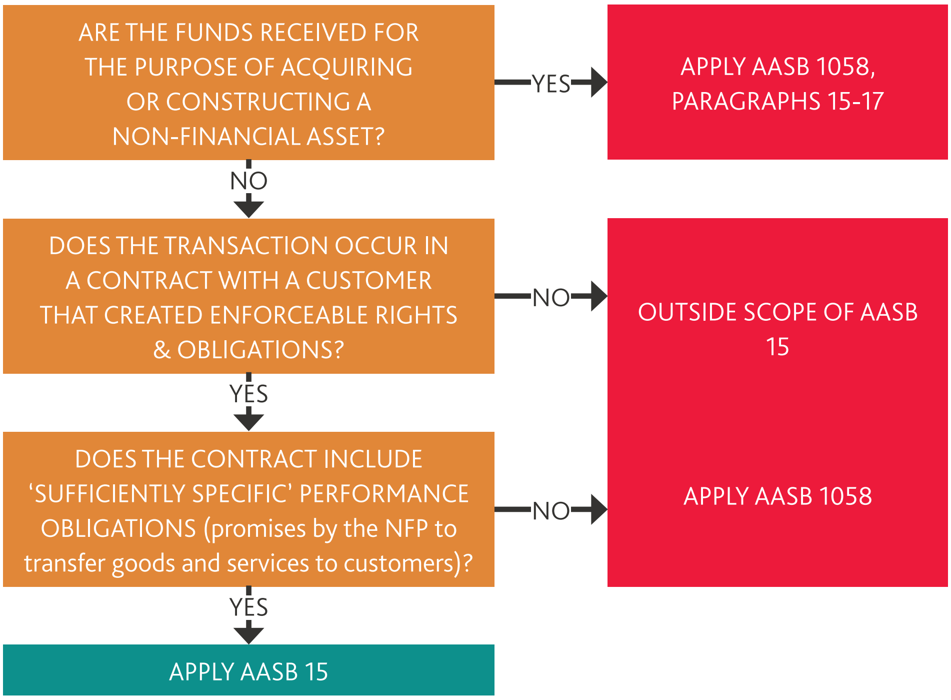
- Wholly-owned state entity
- Bicycle shop
- Private education organisation
- Sports club
- Social enterprise.

COMMENTS CLOSE

The AASB is requesting comments by 9 September 2019. We encourage interested parties to make submissions on this ED.

GRANTS TO NFPS TO TRANSFER RESEARCH FINDINGS TO A CUSTOMER – DOES AASB 15 OR AASB 1058 APPLY?

Grants and other donations received by not-for-profit entities (NFPs) can only be recognised as revenue under AASB 15 *Revenue from Contracts with Customers* if there is an enforceable contract with a customer, and that contract contains 'sufficiently specific' performance obligations. Otherwise, income is recognised under paragraph 9 of AASB 1058 *Income of Not-for-Profit Entities*.



Please refer to previous Accounting News articles for more background information on how to assess whether:

- The transaction occurs in a contract with a customer that creates enforceable rights and obligations (November 2018), and
- The contract includes 'sufficiently specific' performance obligations (February 2019).

GRANTS TO PERFORM RESEARCH ACTIVITIES

One of the areas where we encounter practical difficulties in applying the above requirements is where grants are received by NFPs to conduct research activities. The assessment of whether the contract includes 'sufficiently specific' performance obligations very much depends on what is being transferred to the customer (grantor).

If my entity performs research activities, which Standard do I apply when accounting for grants received and when do I recognise revenue?

AASB FAQ NO. 5

The flow chart below is extracted from FAQs issued by the Australian Accounting Standards Board (AASB) in August 2018. Chart 1 of FAQ No. 5 summarises the required thought process for determining the appropriate recognition of income from grant contracts for different types of research activities, based upon what is being transferred to the customer (sufficiently specific performance obligations), i.e.:

- Intellectual property (IP)
- Licence to use the NFPs' IP, or
- Research findings.

In April, May and June 2019 Accounting News, we considered these above three aspects. This month, we look at examples from AASB 15, Appendix 15, where it is determined that there are no 'sufficiently specific' performance obligations.

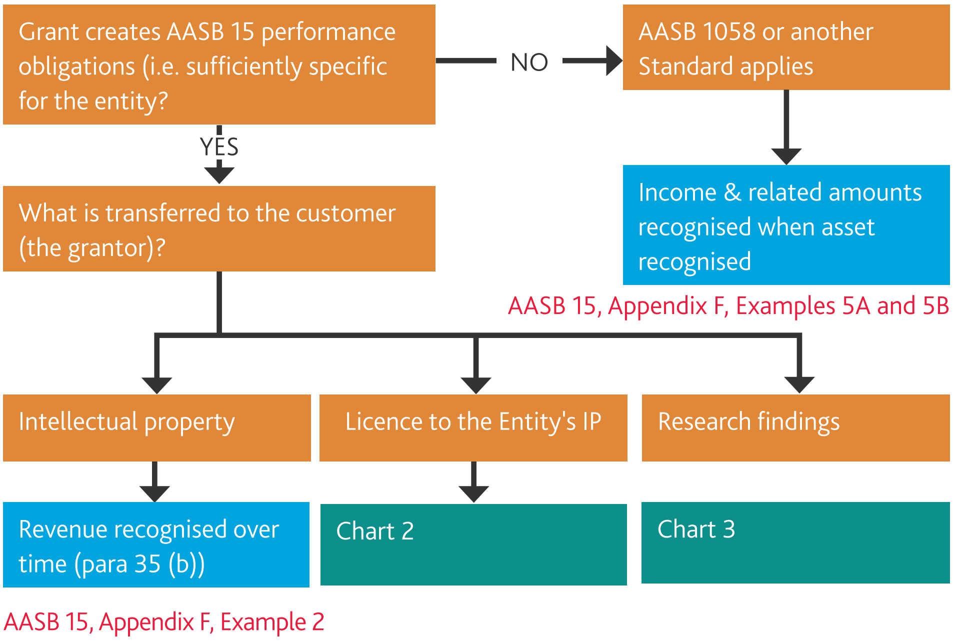


Chart 1 extracted from AASB FAQ No. 5

AASB 15 – EXAMPLES 5A AND 5B

Below is an extract of the relevant Fact Pattern from Example 5A contained in AASB 15, Appendix F.

Facts common to both examples

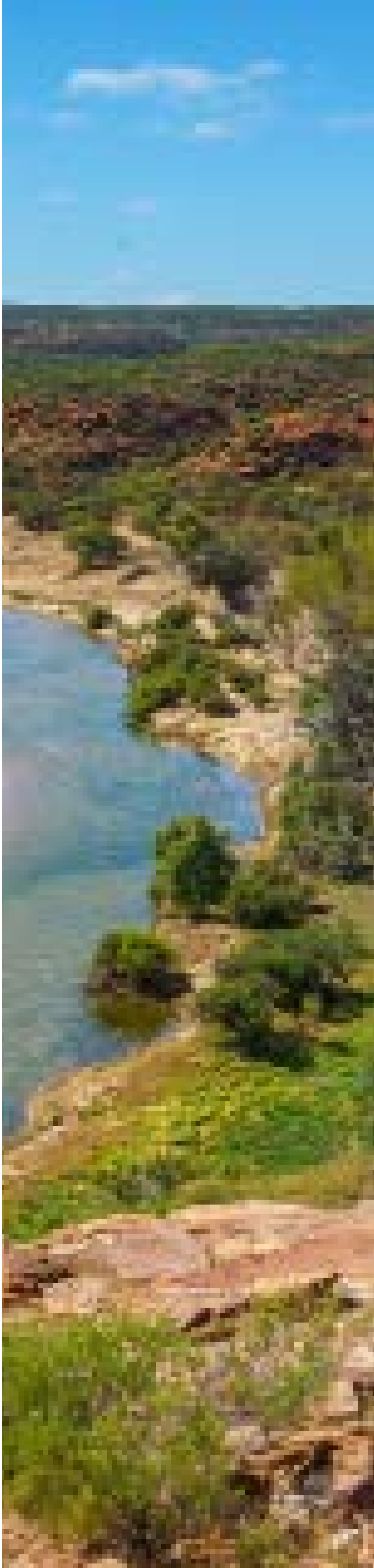
University G receives a cash grant from a donor, Medical Research Trust Z, of $2 million to undertake research that aims to identify and validate biomarkers to distinguish malignant cancers from benign tumours.

Terms of the grant that are common to both examples are as follows:

- A period of two years
- Return of funds that are either unspent or not spent in accordance with the agreement
- Semi-annual budget reports that detail how the funds have been spent to date, and
- The research results are publicised, when appropriate, in conference presentations and/or published in scholarly journals.

Additional Facts – Example 5B

- University G receives the grant funds to merely administer on behalf of a researcher named in the grant
- The named researcher may direct the use of the funds in accordance with the grant agreement, and
- The funding arrangement is tied to the researcher. If the researcher moves from University G to another research institution, any unspent grant funds held by the university will be transferred to the other research institution.



IS THERE AN ENFORCEABLE CONTRACT/AGREEMENT WITH A CUSTOMER?

In both of the above fact patterns, the arrangement is enforceable because the grant is refundable if the research is not undertaken.

DOES THE CONTRACT/AGREEMENT CONTAIN 'SUFFICIENTLY SPECIFIC' PERFORMANCE OBLIGATIONS?

University G concludes in both fact patterns that there are **no 'sufficiently specific' performance obligations** because:

- Publicising the research results when appropriate is not sufficiently specific to enable University G to identify when it satisfies its obligations because there is no requirement to produce a specified number of publications or deliver a specified number of presentations, and
- The budget reports merely provide the grantor an indication of University G's spending of funds and do not represent a transfer of a benefit to the grantor.

WHICH STANDARD DOES THE CONTRACT/ ARRANGEMENT FALL UNDER?

It should be noted that while both examples result in an enforceable agreement but no sufficiently specific performance obligations, each is accounted for under different Accounting Standards because of the additional facts provided in Example 5B.

Example 5A

The arrangement described in Example 5A falls outside the scope of AASB 15 and is accounted for as income under AASB 1058 because University G acquired cash (grant funds) for consideration that is significantly less than fair value (i.e. there are no performance obligations to recognise) principally to enable it to further its objectives (research).

Example 5B

On the other hand, in Example 5B, University G merely administers the grant funds on behalf of the researcher, and therefore considers the arrangement under the requirements of AASB 9 *Financial Instruments* because:

- It receives cash that it administers in accordance with the grant agreement (to which it is a party)
- It may invest the funds it holds as it considers appropriate, benefiting from any interest received and obliged to reimburse any losses incurred, and
- Agrees to expend the funds at the direction of the researcher.

ACCOUNTING TREATMENT – INITIAL RECOGNITION

Example 5A

As AASB 1058 applies, University G recognises the $2 million grant on initial recognition (receipt of cash) as income because it has no further sufficiently specific performance obligations.

	Dr ($)	Cr ($)
Cash	2,000,000	
Income		2,000,000

Example 5B

As AASB 9 applies, University G recognises a financial asset of $2 million for the funds received. It then considers whether it has transferred the financial asset to the researcher, but notes that because it may invest the funds as it considers appropriate, it retains substantially all the risks and rewards of ownership of the funds.

University G therefore recognises a financial asset for the $2 million grant funds on initial recognition, as well as an equal amount for a financial liability to expend the grant funds at the researcher's direction (AASB 9, paragraph 3.2.15).

	Dr ($)	Cr ($)
Cash	2,000,000	
Financial liability		2,000,000

ACCOUNTING TREATMENT – AFTER INITIAL RECOGNITION

In **Example 5A**, as all income is recognised on receipt of the grant, there are no further journal entries subsequent to initial recognition.

However, for **Example 5B**, because grant funds are spent by the researcher on the research project, the following journal entry (cumulative over the life of the project) will be processed by University G:

	Dr ($)	Cr ($)
Financial liability	2,000,000	
Cash		2,000,000

CONCLUDING THOUGHTS

Many NFPs defer recognition of a variety of income streams because there is a lack of clarity in the current accounting requirements for income of NFPs. However, from 1 January 2019, this situation is about to change. NFPs will need to undergo a **formal assessment of all income streams** to assess whether recognition under AASB 1058 or AASB 15 is appropriate. Importantly, revenue can only be recognised if there is an enforceable contract with a customer, and 'sufficiently specific' performance obligations. Disclosure will be required in the financial statements about key judgements made in arriving at the conclusion that performance obligations are/are not 'sufficiently specific'. Management should therefore already be undertaking a detailed review of all contracts and agreements to determine the appropriate accounting standard for accounting for grant income.

RECENT AGENDA DECISIONS OF THE IFRS INTERPRETATIONS COMMITTEE

IFRS Interpretations Committee (Committee) agenda decisions are those issues that the Committee decided not to take onto its agenda. Although not authoritative guidance, in practice they are regarded as being highly persuasive, and all entities reporting under IFRS should be aware of these decisions because they could impact the way particular transactions and balances are accounted for.

At its June 2019 meeting, the IFRS Interpretations Committee (Committee) issued four final agenda decisions dealing with questions on the appropriate accounting for:

- Holdings of cryptocurrencies
- Costs to fulfil a contract under IFRS 15 *Revenue from Contracts with Customers*
- Subsurface rights under IFRS 16 *Leases*, and
- The effect of a potential discount on plan classification under IAS 19 *Employee Benefits*.

A summary of the first three more commonly encountered issues is included below. Please refer to the June 2019 IFRIC update for more information on the other issue mentioned above.

ISSUE 1: HOLDING OF CRYPTOCURRENCIES

FACT PATTERN

Cryptocurrencies have all the following characteristics:

- They comprise a digital or virtual currency recorded in a distributed ledger that uses cryptography for security
- They are not issued by a jurisdictional authority or other party, and
- They do not give rise to a contract between the holder and another party.

Question:

Which standard applies to the holding of cryptocurrencies?

Rationale for agenda decision:	▶ IAS 38 *Intangible Assets* defines an intangible asset as 'an identifiable non-monetary asset without physical substance' ▶ In order for an asset to be identifiable, it must be separable or arise from contractual or other legal rights (IAS 38, paragraph 12) ▶ The essential feature of a non-monetary asset is the absence of a right to receive a fixed or determinable number of units of currency (IAS 21, paragraph 16) ▶ Holdings of cryptocurrencies meet the definition of intangible assets because: – They can be separated from the holder and sold or transferred individually, and – They do not give the holder a right to receive a fixed or determinable number of units of currency ▶ IAS 38 applies to the accounting for all intangible assets except for: those within the scope of another standard; financial assets as defined in IAS 32 *Financial Instruments: Presentation*; exploration and evaluation assets; and expenditure for the development and extraction of minerals, oil, natural gas and similar non-regenerative resources ▶ In reaching its conclusion (refer below), the Committee laid out its rationale as to why it considered cryptocurrencies to be none of the items scoped out of IAS 38. Refer to the agenda decision for more information ▶ Entities holding cryptocurrencies also need to include the following disclosures where relevant: – IAS 2, paragraphs 36-39 if these are held for sale in the ordinary course of business (inventories) – IAS 38, paragraphs 118-128 if IAS 38 is applied – If cryptocurrencies are measured at fair value, IFRS 13 *Fair Value Measurement*, paragraphs 91-99, and – IAS 10 *Events after the Reporting Period*, paragraph 21 if there are any material non-adjusting events (e.g. significant fair value changes).

Conclusion:

IAS 38 applies unless cryptocurrencies are held for sale in the ordinary course of business, in which case, IAS 2 applies.

ISSUE 2: COSTS TO FULFIL A CONTRACT UNDER IFRS 15 *REVENUE FROM CONTRACTS WITH CUSTOMERS*

FACT PATTERN

Local Building Co has identified a single performance obligation, being the construction of a house, that will be satisfied over time (i.e. one or more of the criteria for 'over time' revenue recognition in IFRS 15, paragraph 35, are met).

Local Building Co uses the 'output method' to measure its progress in satisfying the performance obligation.

Local Building Co incurs costs to complete the foundations and slab.

Question:

Is Local Building Co able to capitalise the costs incurred to lay the foundations and slab as a 'fulfilment cost' asset under IFRS 15, paragraph 95, i.e. the costs:

a. Relate directly to the contract
b. Generate or enhance resources of the entity that will be used in satisfying performance obligations in the future, and
c. The costs are expected to be recovered?

Rationale for agenda decision:	▶ The objective when measuring progress towards complete satisfaction of a performance obligation is to depict an entity's performance in transferring control of goods or services promised to a customer (IFRS 15, paragraph 39) ▶ When evaluating whether to use an 'output method', entities must consider whether the output selected would faithfully depict the entity's performance towards complete satisfaction of the performance obligation ▶ IFRS 15, paragraph 98(c) requires costs relating to past performance to be recognised as an expense when incurred, i.e. 'costs that relate to a satisfied performance obligation (or partially satisfied performance obligations) in the contract' ▶ Costs of the foundation and slab relate to the partially satisfied performance obligation in the contract, i.e. they relate to past performance of Local Building Co. These costs do not generate or enhance resources of Local Building Co that will be used in continuing to satisfy the performance obligation (delivery of a fully constructed house).

Conclusion:

Local Building Co cannot capitalise costs incurred to lay the foundation and slab as 'costs to fulfil a contract' because they relate to past performance and not for the satisfaction of a future performance obligation.

ISSUE 3: SUBSURFACE RIGHTS UNDER IFRS 16 *LEASES*

FACT PATTERN

Pipeline Operator obtains the right to place an oil pipeline in underground space for 20 years in exchange for consideration.

The contract specifies the exact location and dimensions (path, width and depth) of the underground space within which the pipeline will be placed.

The landowner retains the right to use the surface of the land above the pipeline, but it has no right of access to the pipeline. Nor can it change the use of the specified underground space throughout the 20-year period of use.

Pipeline Operator has the right to perform inspections and repairs and maintenance work (including replacing damaged sections of the pipeline when necessary).

Question:

Should Pipeline Operator apply IFRS 16 *Leases*, IAS 38 *Intangible Assets* or another IFRS standard when accounting for this contract?

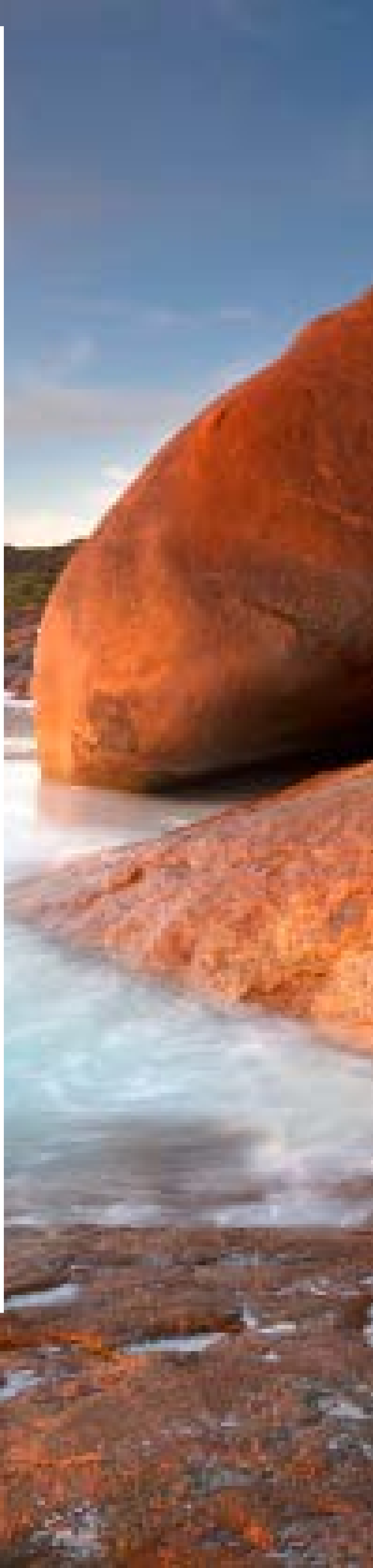
Rationale for agenda decision:

- IFRS 16, paragraph 3 requires an entity to apply IFRS 16 to all leases, except for the following:
  - Exploration for or use of minerals, oil, natural gas and similar non-regenerative resources
  - Biological assets (IAS 41 *Agriculture*) held by a lessee
  - Service concession arrangements (Interpretation 12 *Service Concession Arrangements*)
  - Licences of intellectual property granted by a lessor (IFRS 15 *Revenue from Contracts with Customers)*, and
  - Rights held by a lessee under licensing agreements (IAS 38 *Intangible Assets*) for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights
- For leases of intangible assets not scoped out above, IFRS 16, paragraph 4 gives lessees a choice to account for them under IFRS 16, but they are not required to do so. This means that lessees can effectively bypass capitalising all leases of <u>intangible assets</u> under IFRS 16
- The Committee noted that in this fact pattern, none of the scope exceptions applied, nor was this a lease of an intangible asset because the underground space was <u>tangible</u>
- Pipeline Operator would therefore first need to consider whether the contract contains a lease as defined in IFRS 16 (refer to Conclusion below).

Conclusion:

The contract contains a lease for a tangible asset which Pipeline Operator will need to capitalise under IFRS 16 because:

- There is an identified asset – the specified underground space is physically distinct from the remainder of the land, and the owner does not have substitution rights
- Pipeline Operator has the right to obtain substantially all the economic benefits from using the underground space throughout the period of use (20-year period)
- Pipeline Operator also has the right to direct the use throughout the 20-year contract.



BDO MONTHLY WEBINARS – PLEASE REGISTER FOR 2019 WEBINARS NOW

Are you interested in an easy way to stay up to date with financial reporting and accounting standards which impact your business?

We invite you to register for our 2019 BDO Financial Reporting and Accounting standards live webinar series (11am to 12pm Sydney AEDT or AEST).
Remaining 2019 webinars are as follows:

Date	Topic
July 2019	Disclosing the impact of implementing IFRS 15
August 2019	Disclosing the impact of implementing IFRS 9
September 2019	Disclosing the impact of implementing AASB 1058
October 2019	Lessons learned from implementing IFRS 15
November 2019	Accounting standards update: Getting ready for 31 December 2019
December 2019	Lessons learned from implementing IFRS 16

NEW BDO RESOURCES AND PUBLICATIONS

The IFRS Advisory section of our website contains a number of training resources and publications to help clients keep up to date on the latest developments in financial reporting.

TRAINING MATERIALS

The Accounting Standards Training page includes training materials on the 'triple threat' accounting standards, IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers and* IFRS 16 *Leases*, including:

- Interactive eLearning, and
- Webinars (one-hour video recorded presentations presented live on a monthly basis).

AUSTRALIAN DEVELOPMENTS

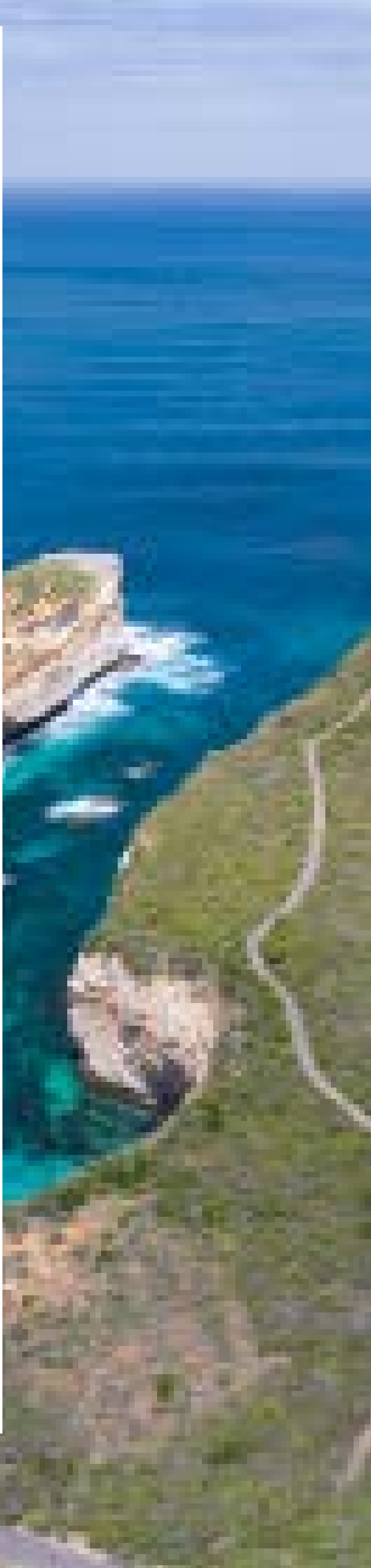
Our Australian Developments page collates resources on a variety of topics specific to Australian financial reporting, including:

- General purpose financial statements for significant global entities (SGEs)
- ASIC issues
- Corporate governance
- Not-for-profit entities, and
- Special purpose financial statements.

IFRS PUBLICATIONS

Our IFRS Publications page includes a range of publications on IFRS issues:

- Financial reporting standards updates (a summary of changes to accounting standards and other legislative changes impacting each June and December reporting season)
- Accounting news (monthly newsletters)
- Global IFRS resources, and
- Industry IFRS information.



COMMENTS SOUGHT ON EXPOSURE DRAFTS

At BDO, we provide comments locally to the Australian Accounting Standards Board (AASB) and internationally to the International Accounting Standards Board (IASB). We welcome any client comments on exposure drafts that are currently available for comment. If you would like to provide any comments please contact Aletta Boshoff at aletta.boshoff@bdo.com.au.

Document	Proposals	Comments due to AASB by	Comments due to IASB by
ED 289 *Annual Improvements to Australian Accounting Standards 2018-2020*	Proposes amendments to the following standards: ▶ IFRS 1 *First-time Adoption of International Financial Reporting Standards* – to permit transition exemptions for measuring cumulative exchange differences when a subsidiary becomes a first-time adopter later than its parent ▶ IFRS 9 *Financial Instruments* – When determining whether a modified financial liability is to be derecognised, 'fees' to be included in the 10% test are only those fees paid or received between the borrower and the lender (including on their behalf) ▶ IFRS 16 *Leases* Illustrative Example 13 – Removes the illustration of payments from the lessor relating to leasehold improvements ▶ IAS 41 *Agriculture* – To remove the requirement in paragraph 22 to exclude cash flows from taxation when measuring fair value so that cash flows used can align if a post-tax discount rate is used.	31 July 2019	20 August 2019
ED 290 *Reference to the Conceptual Framework* Proposed amendments to AASB 3	Proposes to: ▶ Update the old conceptual framework reference to the new *Conceptual Framework for Financial Reporting* (issued March 2018) ▶ Add an exception to the recognition principle for liabilities and contingent liabilities within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and IFRIC 21 *Levies* ▶ Make the IFRS 3 requirements for contingent assets more explicit.	20 August 2019	27 September 2019

Document	Proposals	Comments due to AASB by	Comments due to IASB by
ED 291 *Not-for-Profit Entity Definition and Guidance*	Proposes to: ▶ Retain the term 'not-for-profit entity' (NFP) but replace the definition currently included in AASB 102 *Inventories*, AASB 116 *Property, Plant and Equipment* and AASB 136 *Impairment of Assets* with the definition of 'public benefit entity' as included in XRB A1 Appendix A (with some amendments) ▶ Develop implementation guidance, and ▶ Remove the definition of NFP from AASB 102, AASB 116 and AASB 136 and include the revised definition and guidance in a separate standard, AASB 1057 *Application of Australian Accounting Standards*.	9 September 2019	N/A
ED 292 *Amendments to AASB 17*	Proposes targeted amendments to AASB 17 *Insurance Contracts* relating to the following topics: ▶ Scope exclusions - credit card contracts and loan contracts that meet the definition of an insurance contract ▶ Expected recovery of insurance acquisition cash flows ▶ Contractual service margin attributable to investment-return service and investment-related service ▶ Reinsurance contracts held - recovery of losses on underlying insurance contracts ▶ Presentation in the statement of financial position ▶ Applicability of the risk mitigation option ▶ Transition modifications and reliefs, and ▶ Minor amendments. Also proposes to defer the effective date of AASB 17 by one year to annual reporting periods beginning on or after 1 January 2022, and to extend the AASB 9 *Financial Instruments* temporary exemption in AASB 4 *Insurance Contracts* by one year.	30 August 2019	25 September 2019
ED 293 *Amendments to Australian Accounting Standards – Disclosure in Special Purpose Financial Statements of Compliance with Recognition and Measurement Requirements*	Proposes requiring entities preparing special purpose financial statements, and complying with AASB 1054, to disclose: ▶ The basis on which the decision to prepare special purpose financial statements was made ▶ Whether the entity has consolidated and equity accounted, if appropriate, investments in subsidiaries, joint ventures and associates, and ▶ An explicit statement whether or not the accounting policies applied comply with all recognition and measurement requirements in Australian Accounting Standards.	19 August 2019	N/A

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