Not-for-profit financial reporting and tax update

August 2019

Building a better working world

Not-for-profit update – financial reporting

Financial reporting for Not-for-Profits (NFP entities) continues to be an area of focus for the Australian Accounting Standards Board (AASB). We also continue to see developments in taxation law for NFP entities. We outline the latest developments in financial reporting and tax below. Please contact your EY advisor for further details.

	Detail	Status	Impact
Financial Instruments (new standard)	► This Standard was issued in 24 July 2014 and replaces most of the guidance in AASB 139 *Financial Instruments: Recognition and Measurement*. ► AASB 9 introduces a new classification model for financial assets that is more principle-based than the previous requirements under AASB 139. Financial assets are classified according to their contractual cash flow characteristics and the business models under which they are held. ► AASB 9 also introduces a significant change in impairment requirements, based on expected credit losses rather than incurred losses as under AASB 139. The Standard allows a simplified approach for trade receivables, lease receivables and contract assets.	► AASB 9 Financial Instruments ► The new standard is effective for annual periods beginning on or after 1 January 2018.	► Adopting the expected credit loss model requires changes in current system and processes and the use of judgement. For NFP entity, trade receivables and intra group loan provisioning may require new data analysis. ► Some managed investment portfolios may need to be held at fair value, introducing income volatility. ► Concessional loans and other receivables which may not reflect simply payments of principal and interest may no longer be able to be carried at amortised cost but rather be required to be carried at fair value through profit and loss.
Leases (new standard)	► This standard was issued in February 2016, and replaces the existing AASB 117 *Leases*. ► AASB 16 provides a single model for accounting for leases by lessees. Leases other than low value and short-term leases must be recognised on the balance sheet of lessees. The lessee will recognise an asset, reflecting its right to use the underlying asset, and a liability, in respect of its obligation to make lease payments. ► Expenses in respect of leases will include amortisation of the right-of-use asset and interest expense in respect of the lease liability. ► Lessors will continue to account for leases as either operating or finance leases, consistent with current practice.	► AASB 16 Leases ► The new Standard is effective for annual periods beginning on or after 1 January 2019.	► For all entities with current operating lease arrangements, lease liabilities and right-of-use assets will be brought onto the balance sheet (subject to limited exemptions). ► The timing and nature of expenses recognised in profit or loss will change. ► All service arrangements will need to be revisited to determine if they contain leases e.g. data management services, transport services.

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Not-for-profit update – financial reporting

	Detail	Status	Impact
Income of NFP entities (including temporary relief to not measure peppercorn leases at fair value)	▶ Income of NFP entities is currently governed by AASB 1004 *Contributions*. ▶ The new Standards will defer income recognition in some circumstances for NFP entities, particularly where there is a performance obligation or any other liability. In addition, certain components in an arrangement, such as donations, may need to be separated from other types of income and recognised immediately. ▶ AASB 1058 also expands the circumstances in which NFP entities are required to recognise income for goods and services received for consideration that is significantly less than its fair value principally to enable the entity to further its objectives (discounted goods and services) ▶ AASB 2018-8 postpones the requirement for NFP entities to recognise peppercorn leases at fair value. Applying the temporary relief, NFP entities can measure right of use assets associated with peppercorn leases at the present value of payments required. If they choose to apply the deferral option, specific disclosures need to be made to explain the effects of peppercorn leases. ▶ AASB 1004 will continue in force but with its scope restricted to specific issues for government entities and contributions by owners.	▶ AASB 1058 *Income of Not-for-Profit Entities* and AASB 2016-8 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Entities*, and revised AASB 1004 issued in December 2016. ▶ The new and revised Standards apply to accounting periods beginning on or after 1 January 2019, and may be early adopted. ▶ AASB released a AASB Staff FAQ which addresses questions specific to NFP entities. ▶ AASB 2018-8 *Amendments to Australian Accounting Standards – Right-of-Use Assets of Not-for-Profit Entities* is also effective beginning on or after 1 January 2019.	▶ Depends on how an NFP entity currently applies AASB 1004. ▶ Timing and amount of revenue/grants to be recognised by an NFP entity may be impacted. We expect this will result in more deferral of revenue. ▶ Clearer guidance for deferral of revenue from some transactions where sufficiently specific goods/services are promised (referencing the AASB 15 requirements). ▶ Peppercorn transition relief avoids the income statement reflecting a large income item in the year a new peppercorn lease is signed. ▶ Entities will need to make an accounting policy choice in relation to peppercorn leases, and monitor developments for an end date to transition relief.
Deferral of application date for Service Concession Standard (Grantors)	▶ AASB 1059 *Service Concessions Arrangements: Grantors* was originally applicable to annual reporting periods beginning on or after 1 January 2019. ▶ The AASB has issued an amending standard deferring the application date by one year to 1 January 2020	▶ AASB 2018-5 *Amendments to Australian Accounting Standards – Deferral of AASB 1059* has been released in November 2018.	▶ Government grantors will have an additional year to implement the new standard. ▶ Main impact will be on government entities granting rights to build and/or operate infrastructure assets involving a public service, such as hospitals, schools and roads.

Not-for-profit update – financial reporting

	Detail	Status	Impact

Licenses issued by NFP Public Sector Licensors	▶ AASB 2018-4 *Amendments to Australian Accounting Standards – Australian Implementation Guidance for Not-for-Profit Public Sector Licensors* provides guidance for NFP licensors in accounting for the issue of licenses (for example, gambling, driving, fishing licences).
	▶ The Standard amends AASB 15 to:
	  ▶ Expand its scope to cover non-contractual licences;
	  ▶ Provide guidance to distinguish licences from taxes, for example, a tax will:
	    ▶ Be compulsory rather than discretionary
	    ▶ Be intended to generate income rather than have a non financial purpose such as equitable allocation of resources
	    ▶ Not grant any specific rights to the payer or obligations for the recipient;
	  ▶ Clarify types of licences issued by NFP public sector licensors; and
	  ▶ Provide guidance to assist in clarifying performance obligations relevant to such licence arrangements.
	▶ The Standard also amends AASB 16 to clarify that licenses that are in substance leases or contain leases, except intellectual property, fall within the scope of AAAB 16.
		▶ The new Standard is applicable to annual periods beginning on or after 1 January 2019.
		▶ Early application is permitted.
			▶ Government departments and other NFP public sector entities issuing licences will be required to determine whether they will be impacted by these changes.
			▶ Where no separate performance obligations exist from the transfer of the licence, the licence fee will be required to be recognised as revenue at the time of issue. This may result in a change in accounting to the extent that such revenue is currently deferred and recognised over the licence period.
			▶ The Standard clarifies that performance obligations do not include activities that a licensor must undertake to fulfil a contract unless those activities transfer a good or service additional to the licence. For example: a promise that the right is restricted to the licensee; activities that a licensor is required to undertake to benefit the general public such as 'policing' activities; or activities that a licensor performs to check that a licensee continues to meet the eligibility criteria of the licence, are not performance obligations.
			▶ Certain non-IP licence arrangements that arise due to statutory requirements may involve granting a licensee rights over an identified asset/s. Arrangements that are in substance leases or contain leases will be required to be accounted for in accordance with AASB 16.
			▶ The Standards' classification of licences and taxes differs from the Government Financial Statistics (GFS) guidance. Entities need to be conscious of these differences when reporting on licences and taxes.
			▶ A practical expedient is provided over the recognition of short-term (less than 12 months) and low value licences, so accounting for those types of licences may not be effected.

Not-for-profit update – financial reporting

	Detail	Status	Impact
Exposure Draft ED 291 *Not-for-Profit Entity Definition and Guidance*	▶ Currently, several Australian Accounting Standards include the definition of a NFP entity as one whose "*principal objective is not the generation of profit*". Entities which meet this definition apply modified accounting requirements in certain areas, eg inventory and fixed assets. ▶ ED 291 proposes a revised definition of Not-for-Profit, based on the New Zealand definition of Public Benefit Entity. ▶ Under the ED, a NFP entity is one "*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…*". ▶ The ED provides several illustrative examples.	▶ The AASB requests comments by 9 September 2019	▶ All NFP entities will need to revisit their assessment of whether they meet the new definition of NFP entity which will allow them to continue to apply NFP accounting requirements. ▶ Certain member based organisations may find that if the benefits they provide are restricted to members, as opposed to providing benefits to the broader community, they may not fall within the revised definition. Going forward, such entities would need to apply the general for profit entity rules.
Other AASB reporting initiatives affecting NFP • *ED 293 amending AASB 1054 Australian Additional Disclosures* • *ED 295 **Simplified Disclosures for Tier 2 Entities***	ED 293 proposes additional disclosures for entities (both FP and NFP) preparing Special Purpose Financial Reports, including: ▶ information about how the decision to prepare special purpose reports was made ▶ whether all subsidiaries and associates have been consolidated ▶ whether any recognition and measurement requirements have not been complied with and, if not, an indication of where they do not comply. ED 295 proposes replacing the current RDR framework with a new tier 2 disclosure framework with all the disclosure requirements for Tier 2 entities combined in one (new) standard. The disclosures have been developed using *IFRS for SMEs* as a base however certain disclosures have been added, removed or amended compared to this.	▶ ED 293 - Comments closed 19 August 2019 ▶ ED 295 - Comments close 15 November 2019	▶ All NFP entities will need to: ▶ consider and plan for disclosure changes ▶ engage with stakeholders to communicate the possible changes ▶ update assessments of controlled entities and associates/joint venture relationships.

Not-for-profit update – tax

	Key impacts	Status
Deductible Gift Recipient (DGR) reform	On 22 August 2018, Treasury released a consultation paper on the Government's proposed DGR reforms. The consultation paper covers the following: ► The requirement for non-government organisations with DGR status to register as a charity with the ACNC from 1 July 2019 ► Transition arrangements to support existing organisations with DGR status to register as a charity with the ACNC ► The Commissioner's discretion to exempt organisations with DGR status from the requirement to register as a charity in specific circumstances ► The abolition of certain public fund requirements	► Consultation process now complete. ► Date of effect: 1 July 2019.
2018 Annual Information Statement due date extended	The due date for the 2018 Annual Information Statement has been extended for many charities. Charities with due dates between 31 December 2018 and 28 February 2019 now have until 31 March 2019 to submit their statement. This decision was made by the Commissioner of the ACNC due to the significant changes in the ACNC's IT system.	► Extension until 31 March 2019.
ACNC Annual report	The ACNC annual report for 2017-2018 was released in October 2018. The report highlights ACNC's dedication to ensure charities meet their obligations under the ACNC Act and Governance Standards, with a 65% increase in investigations and 22 revocations of charity registration throughout the year. These organisations will lose access to Commonwealth charity tax concessions (income tax exemption, FBT concessions and GST concessions).	► Ongoing.

Not-for-profit update – tax

	Key impacts	Status
Draft Taxation Ruling 2018/D1	The ATO has released draft taxation ruling *Income Tax: the 'in Australia' requirement for certain deductible gift recipients and income tax exempt entities* ("TR 2018/D1"). The draft ruling provides the Commissioner's views on the following conditions in ITAA97: ► The condition that certain DGRs be 'in Australia' before a gift or contribution to them is tax deductible ► The condition that certain entities have a 'physical presence in Australia' before their income is exempt from tax ► The condition that a registered charity or DGR have a 'physical presence in Australia' before they qualify for a refund of franking credits Under the ordinary meaning of the word, an entity is "in Australia" if it is established or legally recognised in Australia and it operates in Australia at that time. The Commissioner is of the view that an entity will not operate in Australia if the management and operational decisions occur outside of Australia. To have a physical presence in Australia, an entity must conduct physical operations in Australia. The mere ownership of property in Australia does not constitute having a 'physical presence' in Australia. The entity must also incur its expenditure and pursue its objectives principally in Australia and the location where this occurs is very fact dependent. The draft ruling provides a number of examples for organisations to consider.	► Released on 4 July 2018.
External conduct standards	Treasury released exposure draft regulations proposing external conduct standards (ECS) that charities registered with the ACNC will need to comply with when operating outside Australia. ► ECS will set minimum standards for conduct, governance and behaviour that ACNC registered charities must adhere to when operating overseas or when partnering with others to operate overseas. ► The ECS are intended to provide greater confidence to the public that funds sent outside Australia are being used for legitimate purposes. ► The ECS assist in meeting Australia's international obligations including under the Financial Action Task Force Recommendations.	► Consultation process now complete. ► Date of effect: 1 July 2019
ATO activity and enforcement powers	Increased ATO activity is expected and is happening due to the Government's increased funding to the ATO to target tax avoidance and ensure Justified Trust (particularly in relation to Significant Global Entities – "SGEs"). Two key areas of interest are: ► The ATO has been encouraging larger taxpayers to adopt the *Tax risk management and governance review guide* and embrace tax risk management as part of good corporate governance. We anticipate the ATO to extend its focus on tax risk management and governance practices (at least to some extent) to all taxpayers in future years. ► The ATO has begun issuing penalty notices to SGEs for failing to lodge any form type. We recommend you ensure all tax reporting obligations are up-to-date.	► Ongoing.

Not-for-profit update – tax

<table>
<tr><th></th><th>Key impacts</th><th>Status</th></tr>
<tr><td>Updated FBT Rates</td><td>
The FBT rates and thresholds remain consistent for the year ending 31 March 2020:
<table>
<tr><th></th><th>2019</th><th>2020</th></tr>
<tr><td>FBT Rate</td><td>47%</td><td>47%</td></tr>
<tr><td>Type 1 Gross Up Rate</td><td>2.0802</td><td>2.0802</td></tr>
<tr><td>Type 2 Gross Up Rate</td><td>1.8868</td><td>1.8868</td></tr>
<tr><td>Rebate Threshold</td><td>$30,000</td><td>$30,000</td></tr>
<tr><td>Rebate Percentage</td><td>47%</td><td>47%</td></tr>
<tr><td>Days in the FBT year</td><td>365</td><td>366</td></tr>
</table>
</td><td>Changes have been legislated with effect from 1 April 2017</td></tr>
<tr><td>Single Touch Payroll</td><td>From 1 July 2019, Single Touch Payroll ("STP") is also effective for employers with less than 20 employees. Legislation imposed STP requirements from 1 July 2018 for employers with more than 20 employees.
Under STP reporting, employers will be required to report specific payroll data directly to the ATO each time an employee payment is processed (whether this is weekly, fortnightly, monthly, off cycle etc.). More importantly, the real time information will need to be reported at an individual employee level (not at an aggregated level as was previously the case).</td><td>Changes have been legislated with effect from 1 July 2018</td></tr>
<tr><td>Superannuation in relation to annual leave loading payments</td><td>Historically, there has been confusion as to how annual leave loading payments should be treated from a superannuation guarantee ("SG") perspective. As per guidance provided by the ATO, annual leave loading payments are subject to superannuation unless demonstrably referable to overtime. The written evidence that refers to overtime can be in the form of amending the current Award or Enterprise Agreement, or other evidence such as a documented policy.
For those employers that have paid leave loading to employees with no entitlement to overtime, this new guidance will not provide any relief, either historically or on a go forward basis. In these cases, employers are likely to have an exposure and may need to make internal system changes to ensure they are compliant in the future as well as taking remedial action for historical shortfalls.</td><td>Employers are required to comply as soon as practicable where remediation only requires documentation updates.</td></tr>
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Not-for-profit update – ACNC and other guidance material

	Key impacts	Status
Fundraising reforms	The Australian Charities and Not-for-profits Commission (ACNC) has tabled its legislation review report. The report recommends fundraising reform and a single national scheme for the charity sector, requiring a referral of powers from the states to the Commonwealth. Australia currently has eight separate jurisdictions whose regulatory regimes affect charities and not-for-profits (NFPs). The Commonwealth government's regulatory requirements, through the ACNC Acts and the tax system, overlay each of these, resulting in inconsistency, complexity and inefficiency for charities. The review panel believes a national scheme is the best option for the sector going forward, especially in areas such as governance, fundraising and registration.	► The report was issued on 22 August 2018
Reducing the administrative burden for Incorporated Associations	Registered charities incorporated as associations in NSW will have their administrative burden cut, as a result of an agreement signed by NSW Fair Trading and the Australian Charities and Not-for-profits Commission (ACNC) in September 2018. Key elements of the agreement are: ► charities incorporated under the Associations Incorporation Act 2009, will only have to submit their annual financial reports to the ACNC which will then securely share the data with NSW Fair Trading. ► incorporated associations must still notify NSW Fair Trading of any changes to their name, details or rules As a result of these changes, ACNC-registered NSW incorporated associations that are medium or large will need to ensure that the financial reports meet all the ACNC reporting requirements.	► The changes apply to year ends on or after 30 June 2018. ► ACNC has established a two-year transitional reporting arrangement
AICD Good governance principles and guidance	The Australian Institute of Company Directors (AICD) has released new governance principles for the NFP sector. The document noted media reportage of misconduct and poor practice in the NFP sector has intensified in recent years, with a focus on governance failures in the sector that have caused harm to vulnerable people. AICD's principles consist of three components: 10 individual principles, accompanied by supporting practices and guidance, including: ► the board's roles and responsibilities, ► managing conflicts of interest, ► organisational culture, and ► risk management The revised principles have a greater level of guidance with supporting practices and case studies to assist NFPs to think about what appropriate governance is for their organisation. AICD encourages users to conduct regular assessments of their performance and to report outcomes to stakeholders, including why an organisation is not meeting any part of the principles.	► Guidance issued in January 2019

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