PAGFG05

Thursday 16 January 2025

Summary

The IFR4NPO Project Practitioner Advisory Group met to discuss two topics: 1. Fund accounting and 2. Classification of expenses. The agenda, issue papers and recording are available here. Present at the meeting were the Chair, 4 staff from Humentum and CIPFA, and 9 members.

Acronyms

- IFR4NPO – International Financial Reporting for Non-Profit Organisations (Project)
- PAG – Practitioner Advisory Group
- TAG – Technical Advisory Group
- CIPFA – Chartered Institute of Public Finance and Accountancy
- ED – Exposure Draft
- INPAG – International Non-Profit Accounting Guidance
- NPO – Non-Profit Organisation
- NGO – Non Governmental Organisation

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1. Fund accounting

1.1 Framing comments by INPAG Secretariat

Fund accounting is a new section in INPAG (International Non-Profit Accounting Guidance), developed in response to extensive stakeholder feedback. Detailed responses to the questions about fund accounting in ED3 (Exposure Draft 3) were presented at the TAG meeting on 3 December 2024. Key concerns highlighted the need for additional guidance, particularly on the relationship between funds and grants, materiality, and the criteria for distinguishing between restricted and unrestricted funds. Respondents broadly supported the proposed framework but sought further clarification and practical examples.

In response to feedback, the secretariat has proposed new text emphasizing that revenue from contracts with customers should generally not be included in restricted funds, with any inclusion being incidental. Respondents requested clarification about the creation of ‘reasonable expectations’ about the use of funds, and additional guidance about equivalent arrangements such as religious funds (e.g., Zakat). The methods by which NPOs may make a public commitment also sparked comments, particularly the need to address modern communication methods (eg social media) and the role of judgment in determining adequacy.

ED3 respondents recommended that implementation guidance include practical examples to help classify funds and address potential challenges, such as distinguishing contracts for services from grants. The secretariat is keen to keep illustrative examples to a minimum to avoid the risk that preparers look for the example that most closely matches their circumstances, rather than applying the principles to their own specific fact pattern.

1.2 Feedback sought from PAG members

- Do PAG members have any comments or advice on the additional guidance proposed to support the application of the criteria for a fund and/or a fund with restrictions?
- What are PAG members' views on the Secretariat's proposals for the tracking of assets and liabilities for each fund?
- Do PAG members have any comments on the proposed approach to materiality and immaterial funds? Do PAG members have advice on the need for materiality guidance specific to fund accounting?
- What advice to PAG members have on the terms used to describe activities including the use of funds, grants, projects and programmes and what would help assist the navigation of these terms?
- What are members' views on the separation of support costs as a mandated disclosure requirement in the movement of funds note?
- Which of the potential additional illustrative examples listed in Annex B would PAG members prioritise to illustrate a fundamental concept or principle?

1.3 Key comments from PAG members

- There was support for the new text explaining that revenue from contracts with customers would normally be unrestricted.
- An example was offered of an organisation communicating its intention that proceeds or profits from certain sales be directed towards specific activities, which could create a reasonable expectation and the inclusion of sales revenue in funds with restrictions
- There was strong support for the pragmatic approach of requiring that only non-current assets and liabilities be tracked by fund, even while retaining an encouragement to also track current assets and liabilities where systems allow.

- Grant accounting and Project accounting can only be conflated into a unidimensional concept of fund accounting if there is 1:1 relationship between funders and activities, which is frequently not the case.
- Consider developing a Practice Guide 2 for harmonised rules-based approach to defining support costs.
- There was no support for separate guidance about the application of materiality to the identification and aggregation of funds.
- Agree with the approach of avoiding providing too many examples, over and above those that are needed to demonstrate principles.
- Further guidance or examples are requested about how to account for grant funded assets and inter-fund borrowing, beyond educational materials.

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2. Classification of expenses

2.1 Framing comments by INPAG Secretariat

The classification of expenses is a complex issue, and two key areas require careful consideration. First, the rebuttable presumption to present expenses by nature has generated significant discussion, with concerns that it might lead to unintended consequences or fail to deliver meaningful benefits. Second, the categorization of fundraising costs—especially for commercial trading income and investment income—has been contentious. While traditional fundraising activities are well-understood, these other categories are less universally applicable to non-profits, and additional criteria like materiality may be needed to determine when disclosures should be triggered.

Section 24 introduces grant expenses and expense classification, allowing for classification by nature, function, or a mixed approach. While feedback on the rebuttable presumption was generally supportive, there were notable concerns about its alignment with international standards, the risk of defaulting to classification by nature, and potential challenges for comparability. A mixed or matrix approach was suggested as a flexible solution, but it may impose a resource burden, particularly for smaller non-profits.

To address these concerns, the secretariat proposes clarifying that the rebuttable presumption is not a prescription or default. This clarification aims to balance reducing the resource burden with providing relevant and reliable information. Providing functional analysis may depend on robust accounting systems to support the proposed approaches, particularly for smaller organisations.

2.2 Feedback sought from PAG members

- What are PAG members' views on the benefits or otherwise of including a rebuttable presumption that NPO should classify expenses by nature?
- What are PAG members' views on the optionality for an expense classification to be on the face of the Statement of Income and Expenses or in the notes to the financial statements?
- Do PAG members consider the feedback raises new issues about whether commercial and trading and investment management costs should be included in fundraising costs? Would exploring reference to materiality in relation to funds raised used be useful?
- Do PAG members consider that the description of investment management costs should refer specifically to treasury management activities or should NPOs be able to make a judgement based on its significance to funds raised?

2.3 Key comments from PAG members

- There was support for the rebuttable presumption to present expenses by nature, but emphasis on flexibility and the need for more complex organisations to consider relevant and reliable information, even matrix if useful.
- Even though the inclusion of commercial and investment activities as 'fundraising activities' was broadly supported by ED3 respondents, PAG members felt a return to a more traditional definition of fundraising costs was more in line with the needs of users of financial statements, such as public donors keen to know how much is spent on fundraising activities.
- Including more types of costs under the heading 'fundraising costs' could be confusing and counter-productive, and also have tax implications in some jurisdictions
- There was mention of examples of NGOs engaging in commercial activities (such as selling items made by service recipients) or requiring contributions from service recipients, which are motivated by building a sense of dignity and ownership / buy-in at least as much as generating money.
- Treasury management activities may be carried out with the view of protecting assets from risks associated with exchange rate losses, rather than generating income.
- There was support for disclosing the costs of other types of activities that could generate funds (such as commercial activities and treasury management) but without having them under the heading 'fundraising costs'.