

Accounting Alert

Analysis of the latest Accounting developments delivered to you via e-mail

The ED was publicly released on 1 October 2003

Changes to the accounting for government grants proposed to apply only to for-profit entities

Exposure Draft 124 Released

The Australian Accounting Standards Board (AASB) has released Exposure Draft (ED) 124 "Request for Comment on: The Definition of Reporting Entity; IASB Framework for the Preparation and Presentation of Financial Statements"; IAS 18 Revenue; and IAS 20 Accounting for Government Grants and Disclosure of Government Grants" as part of the convergence process with International Financial Reporting Standards (IFRS).

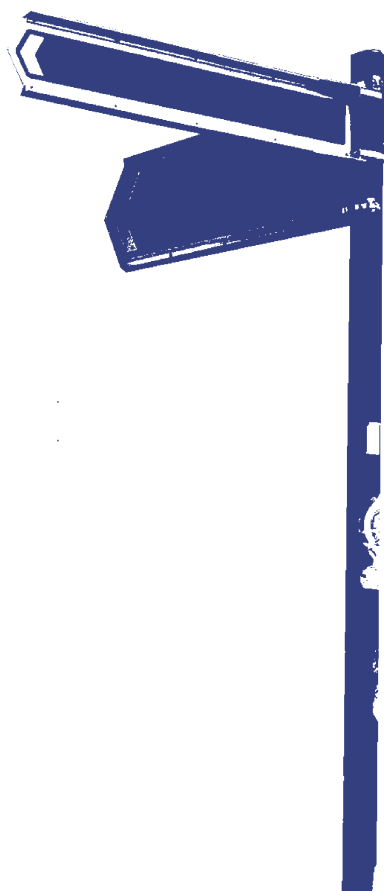
This *Accounting Alert* provides an outline of the proposals in the ED.

Overview

The AASB proposes to adopt the IASB Framework and IAS 18 without amendment for all entities. However, the AASB proposes that IAS 20 be adopted to apply only to for-profit entities, and that the revenue recognition rules prescribed by current Australian Accounting Standards in relation to government grants continue to apply to not-for-profit entities, as they are currently the subject of review by the AASB as part of the AASB's project on AAS 27 "Financial Reporting by Local Governments".

The AASB acknowledges that the present Australian requirements in respect of revenue recognition are superior to those of the current IASB Standards, especially in respect of the treatment of government grants; however, for the sake of convergence, Australia is expected to adopt requirements that will in the short term require Australian entities to take a regressive step. The IASB is considering accounting for government grants as part of their convergence project (post 2005) and is looking at the Australian requirements as part of this process, but this project is not expected to be completed in time for 2005. In addition, there is a larger revenue recognition project also in the early stages of discussion.

Copies of the EDs are available at www.aasb.com.au, with the comment period closing on 30 November 2003.



Proposed amendment of the definition of a 'reporting entity'

The Reporting Entity Concept

The IASB recognises that mandating the application of Standards is the domain of individual jurisdictions. Under the reporting entity concept in Australia, 'reporting entities' are required to prepare a general purpose financial report in accordance with Accounting Standards and UIG Consensus Views. As part of the ED the AASB proposes to amend the definition of 'reporting entity' to:

"An entity in respect of which it is reasonable to expect the existence of users who rely on the entity's general purpose financial report for information that will be useful to them for making and evaluating decisions about the allocation of resources. A reporting entity can be a single entity or a group comprising a parent and all of its subsidiaries."

As such subsidiaries of overseas listed entities are no longer specifically identified as reporting entities and may no longer need to prepare general purpose financial reports.

In this respect, SAC 1 "Definition of the Reporting Entity" and SAC 2 "Objective of General Purpose Financial Reports" are to be retained, however the form in which these statements are to be retained has yet to be decided.

The IASB is currently developing accounting and reporting Standards for small and medium-sized entities. These Standards will be based on other IFRS but are expected to include less guidance and disclosure. It is unclear how these requirements will interact, or replace, the reporting entity concept in Australia.

IASB Framework for the Preparation and Presentation of Financial Statements

Australian Pronouncements Affected

- SAC 3 "Qualitative Characteristics of Financial Information".
- SAC 4 "Definition and Recognition of the Elements of Financial Statements".

Major Changes to Existing Practice

- Income includes revenue (operating income) and gains (for example, those arising on the disposal of non-current assets). Similarly, a loss is a component of expenses. As a result, the current requirement to disclose proceeds on the sale of assets will no longer form part of revenue, rather the gain or loss will be appropriately classified.
- Additional guidance will be provided for not-for-profit entities regarding future economic benefits.
- Other differences exist between the IASB Framework and SAC 3 and SAC 4 but these are not expected to lead to major changes in practice.

Net profit rather than proceeds on sale of non-current asset reported as revenue

IAS 18 Revenue

Australian Standard Affected

- AASB 1004 "Revenue".

Major Changes to Existing Practices

- Revenue is recognised based on transfer of significant risks and rewards of ownership rather than control. Also, additional criteria required to be met before revenue is recognised is that related costs can be measured reliably. Together these changes may lead to the later recognition of revenue.
- When recognising revenue by reference to stage of completion, the condition that the entity controls the right to be compensated will no longer exist.
- Revenue recognised on the exchange or swap of goods or services will not be recognised as frequently. Where goods or services of similar nature and value (but not necessarily homogenous) are swapped (some cash consideration can be involved), the transaction is recognised at carrying values.

Although the impact of these changes may appear to be relatively minor, Deloitte believes that a lot of past Australian practice will need to be re-evaluated in light of the requirements of IAS 18, and that many of the differences between AASB 1004 and IAS 18 will only be determined after widespread implementation in Australia.

Revenue on exchange or swap of goods or services will not be recognised as frequently

IAS 20 Accounting for Government Grants and Disclosure of Government Grants

Australian Pronouncements Affected

- AASB 1004 "Revenue".
- UIG 11 "Accounting for Contributions of, or Contributions for the Acquisition of, Non-Current Assets".

Major Changes to Existing Practices

- Government grants should not be recognised until there is reasonable assurance that the enterprise will comply with the conditions attaching to the grant and that the grant will be received, potentially resulting in later recognition of grants.
- Non-monetary grants may be recognised at either fair value or nominal value.
- Grant income should be recognised over the period necessary to match with the related costs, for which they are intended to compensate, on a systematic basis. Grants received for the acquisition or construction of an asset and not yet recognised should be either presented as deferred income or deducted from the carrying amount of the related asset. (Except in relation to grants related to biological assets – refer IAS 41 "Agriculture".)
- Repayments of grants should be treated as a revision of an accounting estimate and first offset against any deferred credit/asset to which it relates, with the balance and any additional depreciation recognised as an expense.
- Introduction of new disclosures, including the nature and extent of government grants recognised, an indication of other forms of government assistance from which the entity has directly benefited, and any unfulfilled conditions and other contingencies attached to the recognised amounts.

Government grant revenue recognition to be matched to related expense

No changes for not-for-profit entities

Proposed Departures from IFRS

- Not-for-profit entities to continue to apply current Australian requirements, including where received in relation to biological assets.

Feedback and Assistance

We welcome your feedback on the matters covered in this *Accounting Alert* – please email your comments to accounting_alerts@deloitte.com.au.

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