



Not for Profit Sector

Issues in Financial Reporting in the Not-for-Profit Sector

Paul McDonald

AUDIT / ADVISORY /

AUDIT ■ TAX ■ ADVISORY

Not-for-profits in the spotlight ...

“Not for profit organisations are a big part of the economy, yet they are virtually unaccountable”

BRW March 2005

“Community trust in NFP’s ... is maintained and enhanced when the NFP’s activities are open transparent to the community”

ICAA Sept 2006

“The complexity of the legal forms of NFP organisations has important implications for accountability, governance and regulation”

University of Melbourne Feb 2004

“An increasing number of donor companies are establishing performance indicators (for NFP’s) and seeking increased transparency and accountability”

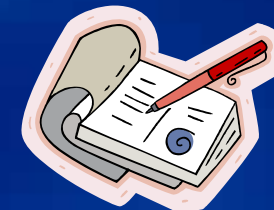
BCA July 2007

Three Imperatives for Finance Managers ...

- **The regulatory and accounting framework for NFP's is flawed**
- **There are sound commercial reasons to improve the transparency and utility of financial reporting**
- **There are some immediate accounting and reporting issues to consider**

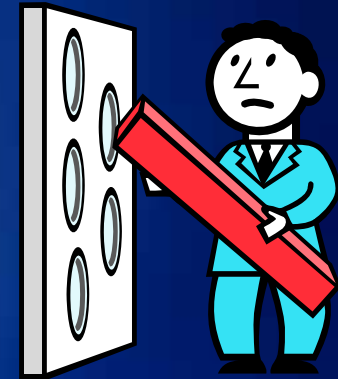
A significant sector of the economy ...

- **NFP's play a significant role in our society**
 - economic
 - social
 - political
- **Legal and regulatory framework complicated and unclear**
 - State-based regulation
 - Corporations Act
 - specific Acts of Parliament



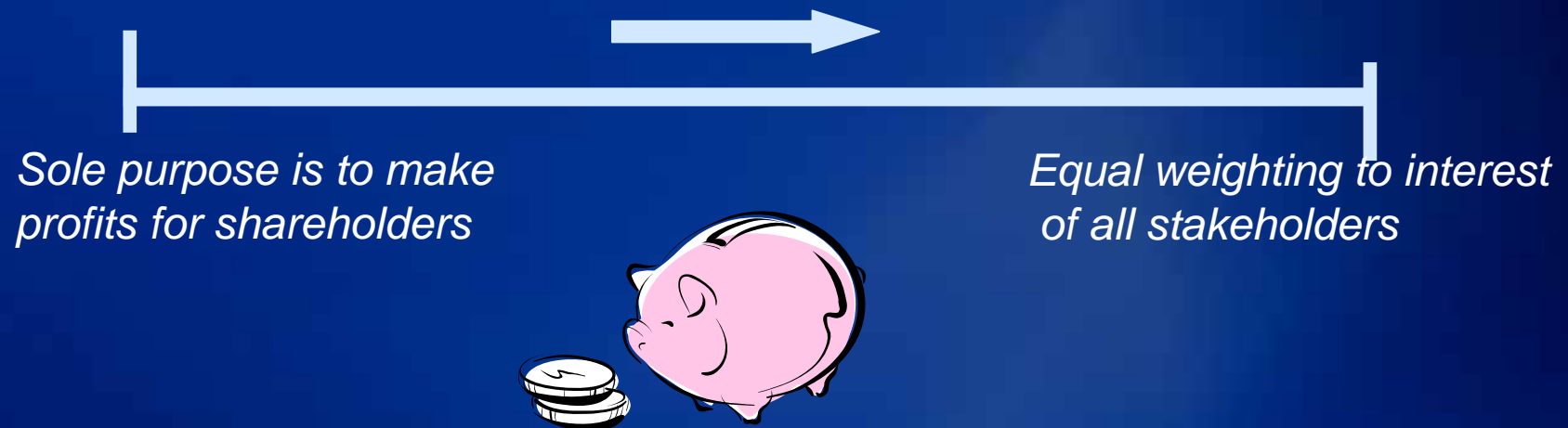
Not for Profit's – square peg in a round hole

- **NFP's are fundamentally different:**
 - no residual ownership interest
 - broader definition of 'entity'
- **Complicated legal framework**
 - incorporated association
 - company limited by shares
 - company limited by guarantee
- **Application of IFRS to NFP's**
- **Financial reporting for based solely on 'compliance' will always be sub-optimal**



Winds of change ... the rise of Corporate Social Responsibility

- The role of companies in the community



- Corporate community investment as a sub-set of CSR

- shift from ad hoc grant making
- corporate community investment as part of core business strategy
- more rigorous identification and selection of NFP partners

Winds of change ... the rise of Corporate Social Responsibility



“Companies will increasingly address the issue of accountability and stewardship ... and seek better ways to measure returns for the business and the community”

“An increasing number of companies are seeking increased transparency and accountability”

Improving the quality of financial reporting

- **More meaningful disclosures ... abandoning the “compliance” mindset**
 - **performance**
 - **financial position**
 - **governance**

More meaningful disclosures ... abandoning the 'compliance' mindset

Performance Reporting

- Focus on stewardship and measuring outputs

More meaningful disclosures ... abandoning the 'compliance' mindset

The Research Institute into the Mental Health of of Retired Auditors Inc

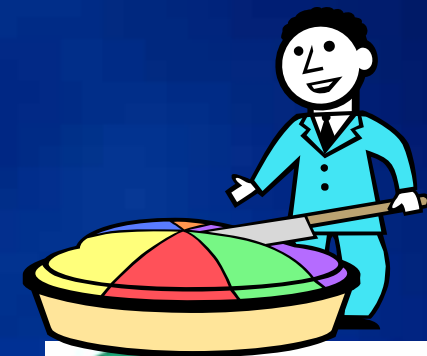
Statement of Operating Activities

Trading revenue				375,210
Trading expenses				(227,123)
Net trading surplus / (deficiency)				<u>148,087</u>
Non trading revenues				
Government grants				2,000,000
Corporate donations				150,600
Investment income				25,000
Other				13,650
Total non trading revenue				<u>2,189,250</u>
Total revenue available for programmes				<u>2,337,337</u>
<i>Programme 1 Programme 2 Programme 3</i>				
Revenue allocated to programmes	950,000	900,000	400,000	2,250,000
Expenses				
Direct programme expenses	(750,000)	(562,000)	(390,000)	
Administration	(25,000)	(30,000)	(10,000)	
Other	(10,000)	(12,000)	(8,000)	
Net programme surplus / (deficiency)				<u>165,000 296,000 (8,000) 453,000</u>
Unallocated expenses				
Administration				67,000
Fundraising				500,000
Other				215,000
Net profit / (loss)				<u>1,555,337</u>

More meaningful disclosures ... abandoning the 'compliance' mindset

Performance Reporting

- Focus on stewardship and measuring outputs
- Reporting KPI's to evaluate efficiency (eg ratio of expenditure on fundraising the total funds raised, administration)



More meaningful disclosures ... abandoning the 'compliance' mindset

The Salvation Army Australia
Southern Territory Social Fund
Notes to the Financial Statements
for the year ended 30 June 2006

	2006 \$'000	2005 \$'000
4. Auditors' Remuneration		
Audit services:		
Audit of the Social Fund	497	552
Audit of the Aged Care Completion Statement	50	30
	<u>547</u>	<u>582</u>
Other services:		
Audit	9	-
5. Red Shield Appeal Donations		
Donations		
Victoria	16,054	13,981
South Australia (includes Eyre Peninsula Bushfire Appeal)	3,487	4,627
Western Australia	5,167	4,400
Tasmania	1,519	1,535
Northern Territory	356	361
	<u>26,583</u>	<u>24,904</u>
Less: Expenses	<u>(5,799)</u>	<u>(5,279)</u>
Net Revenue Available For Distribution	<u>20,785</u>	<u>19,625</u>
Distribution		
Social programme deficits:		
Employment, education and training	168	134
Children and young people at risk	1,415	1,340
Addictions and substance abuse	2,324	3,058
Aged care and disability support	351	751
Individual and family support	7,145	4,142
Homelessness and domestic violence	3,472	3,928
Chaplaincy	2,329	2,153
Social services and community programmes total	<u>17,204</u>	<u>15,506</u>
Capital Appeal – St Kilda Crisis Centre	257	-
Donor designated gifts for social services and community programmes (includes Eyre Peninsula Bushfire Appeal)	<u>3,324</u>	<u>4,119</u>
Total Distribution	<u>20,785</u>	<u>19,625</u>

The Salvation Army provides substantial additional funding to cover social programme deficits allocated to individual and family support, from non Red Shield Appeal sources.

More meaningful disclosures ... abandoning the 'compliance' mindset

Performance Reporting

- Focus on stewardship and measuring outputs
- Reporting KPI's to evaluate efficiency (eg ratio of expenditure on fundraising the total funds raised, administration)
- Reporting KPI's to evaluate efficacy (eg actual outputs vs planned outputs)



More meaningful disclosures ... abandoning the 'compliance' mindset

Financial Position

- Liquidity and restrictions on assets
- Recognition of the importance of fund accounting

More meaningful disclosures ... abandoning the 'compliance' mindset

Governance

- Board process
- Internal controls
- Management remuneration



Some existing reporting challenges ...

IFRS Issues

- Revenue recognition
 - 'exchange' transaction or non-reciprocal transfer;
 - choosing the policy that best reflects economic reality
- Fair value accounting
 - non-current assets
 - financial assets – AFS or Trading ?
- Contributions
 - 'in kind' contributions
 - volunteer hours



Some existing reporting challenges ...

Recent Developments

- **AASB invitation to comment**
 - abolish existing 'reporting entity' concept
 - focus on general purpose financial reports
- **New IFRS Standard for SME's**
- **Corporations Act amendment to large / small proprietary company test**
- **Treasury Discussion Paper on Unlisted Public Companies**



To wrap up ...

- **Regulatory and accounting framework is flawed**
- **There are sound commercial reasons to improve transparency and utility of your financial report**
- **There are some significant existing reporting challenges to consider**



Discussion / Question time





Presenter's contact details

Paul McDonald

Partner

9288 5795

pjmcdonald@kpmg.com.au

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.