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ASSURANCE AND ACCOUNTING

ACCOUNTING STANDARDS FOR NOT-FOR-PROFIT ORGANIZATIONS (ASNPO) UPDATE 2018

Introduction

It was a busy year for the Accounting Standards Board (AcSB) and for Part III of the CPA Canada Handbook – Accounting: Accounting Standards for Not-for-Profit Organizations (ASNPO). During 2018, the Board issued three new Standards as well as advanced the progress of other not-for-profit organization (NPO) specific projects.

Private sector NPOs applying ASNPO also apply the relevant standards in Part II of the CPA Canada Handbook – Accounting: Accounting Standards for Private Enterprises (ASPE) to the extent that the standards in Part II address topics applicable for NPOs that are not addressed in Part III. As a result, some changes made to ASPE also affect NPOs. This publication will discuss amendments resulting from the 2017 ASPE Annual Improvements Process and their impact on NPOs as well as provide an update on other projects the AcSB is working on that will impact NPOs.

Standards Effective in 2018

2017 Annual Improvements Process

As a result of the 2017 ASPE Annual Improvements Process, amendments were made to the following ASPE Sections, which would also affect NPOs. These changes are effective for years beginning on or after January 1, 2018, with earlier application permitted.

Disclosure of Accounting Policies

Paragraph .08 in Section 1505, *Disclosure of Accounting Policies*, requires that an entity's accounting policies be disclosed "as the first note" to the financial statements. However, some stakeholders noted that this requirement is too prescriptive. As a result, the Board has amended this paragraph to require that this disclosure be provided "in one of the first notes," rather than as the first note, to the financial statements.

Accounting Changes

Paragraphs .34-.35 of Section 1506, *Accounting Changes*, set out the disclosure requirements related to changes in accounting policy. Paragraphs 1506.34(e) and .35(c) required an entity to disclose the amount of an adjustment related to an accounting policy change "for the current period," but not for each of the prior period(s) presented. However, stakeholders noted that disclosing the adjustment related to the prior period(s), instead of the current period, is what actually meets user needs. As a result, the Board removed the requirement to disclose the amount of an adjustment related to an accounting policy change for the current period and disclosure "for each of the prior period(s) presented" is required instead.

Balance Sheet

Section 1521, *Balance Sheet*, distinguishes between the items that must be presented separately on the face of the balance sheet and those items that can either be presented separately on the balance sheet or in the notes. Some stakeholders have noted that Section 1521 was not consistent with the presentation and disclosure requirements set out in other standards in ASPE. As a result, the Board revised paragraphs 1521.04 and .05 to clarify the line items that are required to be separately presented on the balance sheet, and added paragraphs 1520.04A and .05A to clarify the line items that may either be presented separately on the balance sheet or in the notes to the financial statements.

Foreign Currency Translation

Paragraph .53 of Section 1651, *Foreign Currency Translation*, does not allow an entity to reverse previously recorded write-downs of inventory in the translated financial statements of an integrated foreign operation. However, this contradicts Section 3031, *Inventories*, which requires that previous write-downs of inventory be reversed when the circumstances that caused the write-down no longer exist or there is clear evidence of an increase in the net realizable value reflecting changes in economic circumstances. Consequently, the Board removed paragraph 1651.53 and provided further clarification of this situation in the example included in paragraph 1651.51.

Leases

Paragraph .81 in Section 3065, Leases, requires disclosure of the carrying amount of impaired operating lease receivables and the amount of any related allowance for impairment. However, Section 3856, *Financial Instruments*, was amended during the 2014 Annual Improvements to ASPE to only require disclosure of any allowance for impairment for current trade receivables and not the carrying amount of impaired current trade receivables. Stakeholders believe the impairment disclosure for operating lease receivables should be similar. Therefore, the Board amended paragraph 3065.81 to clarify that disclosure is only required for the amount of the allowance for impairment.

Standards Effective in 2019

Tangible Capital Assets, Intangible Assets, & Collections

In March 2018, the Board issued the three new ASNPO Handbook standards listed in the table below. These three new Sections replace existing Sections 4431, 4432, and 4440.

New Section	Replace Existing Section
Section 4433, *Tangible Capital Assets Held by Not-for-Profit Organizations*	Section 4431 of same name
Section 4434, *Intangible Assets Held by Not-for-Profit Organizations*	Section 4432 of same name
Section 4441, *Collections*	Section 4440 of same name

The three new Sections are based on the existing Sections with certain revisions as outlined below.

Tangible Capital Assets & Intangible Assets

When accounting for and disclosing tangible capital assets and intangible assets, new Sections 4433 & 4434 prescribe that an NPO follow the guidance in ASPE Sections 3061, *Property, Plant and Equipment*, 3064, *Goodwill and Intangible Assets*, and 3310, *Asset Retirement Obligations*, except for NPO-specific guidance included in the new Sections on contributed assets and write-downs of assets. Applying Section 3061 would include considering the guidance on asset componentization.

A tangible capital asset or intangible asset is written down to its fair value or replacement cost (an NPO is given the choice of which of these bases to use on an asset-by-asset basis) to reflect a partial impairment of the asset when conditions indicate that the asset:

- No longer contributes to an NPO's ability to provide goods or services; or
- The value of future economic benefits or service potential associated with the asset is less than its net carrying amount.

Sections 4433 and 4434 provide examples of conditions that may indicate impairment and any impairment would be disclosed in accordance with the requirements in ASPE Section 3063, *Impairment of Long-lived Assets*.

Collections

Collections are works of art, historical treasures, or similar assets that are:

- Held for public exhibition, education, or research;
- Protected, cared for, and preserved; and
- Subject to an organization policy that requires any proceeds from their sale be used to acquire other items to be added to the collection or for the direct care of the existing collection.

New Section 4441 requires collections to be presented as a separate line item on the face of the Statement of Financial Position and an NPO make an accounting policy choice to record all of its collections at either:

- Cost; or
- Nominal value.

To reflect partial impairment of a collection recorded at cost whenever events or changes in circumstances indicate that its net carrying value may exceed fair value, it is written down to either fair value or replacement cost. Section 4441 provides examples of conditions that may be present to indicate impairment. When there is impairment, disclosure is required of whether the write-down is measured at the collection's fair value or replacement cost.

When items in a collection are disposed of during the year, Section 4441 requires:

- For items contributed to a collection that are subject to external restrictions, the gain or loss on disposal is accounted for in accordance with Section 4410, *Contributions – Revenue Recognition*.
- For items in a collection that do not have external restrictions, or when the net proceeds on disposal are less than the carrying amount of an item (i.e., loss on disposal), the difference is recognized in the Statement of Operations.

More extensive disclosures on collections are required under the new Section than in the past.

Works of Art and Historical Treasures Not Part of a Collection

For works of art, historical treasures and similar items that are not part of a collection, depending on their intended use, they continue to be accounted for as either:

- Tangible capital assets, in accordance with new Section 4433;
- Intangible assets, in accordance with new Section 4434;
- Investments in accordance with ASPE Section 3051; or
- Inventory-type items in accordance with Section 3032, Inventories held by Not-for-Profit Organizations.

Transition

All three new sections are effective for fiscal years beginning on or after January 1, 2019.

New Sections 4433 and 4434 are applied prospectively in accordance with Section 1506, *Accounting Changes*, except as permitted by the transitional provisions. The transitional provisions provide relief for an NPO to:

- Allocate the costs and related amortization of tangible capital assets to their component parts based on their relative cost or fair value at the date the assets were acquired, or at fair value or replacement cost at the date the Section is first applied; and
- Recognize an adjustment to opening net assets for partial impairments of tangible capital assets and intangible assets existing at the date the Section is first applied.

New Section 4441 requires retrospective application in accordance with Section 1506 except as permitted by the transitional provisions. The transitional provisions provide relief for an NPO that chooses to record its collection at cost to:

- Capitalize items in a collection acquired in previous periods at their cost or fair value at the date of acquisition, or at fair value or replacement cost at the date the Section is first applied;
- Record one or more items in a collection or an entire collection at nominal value when the cost cannot be reasonably determined; and
- Recognize an adjustment to opening net assets for partial impairments of collections existing at the date the Section is first applied.

The Board believes recording collections at cost provides information that is more useful to financial statement users. Therefore, they believe these transitional provisions would encourage more NPOs to record their collections at cost, as it would be easier to do so.

Projects on the Go

Over the past few years, the AcSB has been working on improvements to NPO standards. In 2015, the AcSB approved the creation of a "Not-for-profit Organizations Advisory Committee" to assist the Board with its standards improvements initiatives, as well as to provide input on other standard-setting matters of interest to private sector NPOs. In March 2018, the first three new standards to be developed from this improvements process were issued in the Handbook. Other projects the Board is currently working on that will affect NPOs are as follows.

Project — Contributions — Revenue Recognition and Related Matters

This project involves conducting further research on how NPOs should recognize revenue from contributions. It will also consider the implications to NPOs of eliminating the $500,000 size exemption for capital assets, as well as examine whether NPOs should be directed to follow the financial statement presentation guidance in ASPE except for presentation issues unique to NPOs for which guidance will be retained in Part III of the Handbook. The AcSB is currently carrying out research on recognition of revenue from contributions including:

- Seeking a better understanding of current practices, such as what types of NPOs use the deferral method vs. the restricted fund method and why they use each method;
- The types of contributions NPOs receive and their terms and conditions; and
- The significance of different types of revenue to those organizations.

The Board is also consulting with a range of users of NPO financial statements to understand what information they need to make decisions.

Based on feedback received from the Not-for-Profit Advisory Committee, the Board will also consider whether to undertake a future project on related party transactions.

As this project could have a significant impact on accounting for private sector NPOs, we would encourage NPOs and the users of their financial statements to watch it closely. The latest information on this project can be found on the ASNPO section of the Financial Reporting & Assurance Standards Canada website or by clicking here.

Project — Reporting Controlled and Related Entities by NPOs

This project will address whether and how to amend Section 4450, *Reporting Controlled and Related Entities by Not-for-Profit Organizations*, regarding how to account for controlled not-for-profit organizations and profit-oriented enterprises. This project is currently on hold as the Board focuses its attention on the contributions project discussed above.

Project — Combinations

During the Board's research on the above project, it heard from stakeholders that guidance on accounting for combinations between NPOs and the acquisition of a profit-oriented enterprise by an NPO is needed. Combinations between NPOs are becoming more frequent and currently no guidance on accounting for these types of transactions is included in either ASNPO or ASPE, which has led to diversity in practice. As a result, the Board has approved a project to provide guidance on the initial measurement of a combination and the relevant disclosures. The Board is currently determining the scope of this project and plans to issue an Exposure Draft in 2019.

Exposure Draft — Financial Instruments

In 2014, the AcSB issued its Post-implementation Review: Section 3856, *Financial Instruments*. Based on the feedback provided, the Board understood that the current guidance on the scope of accounting for related party financial instruments after initial recognition and the measurement of related party compound financial instruments is not clear and is resulting in diversity in practice. Additionally, financial instrument risk disclosures are not entity-specific and therefore are not providing useful information. As a result, the Board issued an Exposure Draft in October 2017. Some of the proposed main changes are as follows:

Scope

- The scope of Section 3856 would be amended to make it clear that the Section applies to the initial and subsequent measurement, derecognition, presentation, and disclosure of related party financial instruments.
- Guidance on how not-for-profit organizations initially measure related party financial instruments would be added.

Initial Measurement

- Section 3856 would explain that related party financial instruments would be initially measured at cost, unless the instrument is equity that is quoted in an active market or a derivative contract. Such instruments would be measured at fair value without any adjustment.
- The cost of a financial instrument in a related party transaction would depend on whether the instrument has repayment terms.
- The election to initially measure financial assets or financial liabilities at fair value would be prohibited for related party financial instruments.
- The equity component of a related party compound financial instrument would be permitted to be initially measured as zero.

Subsequent Measurement

Section 3856 would explain that subsequently related party financial instruments would be measured at cost, less any reduction for impairment. Except for equity instruments quoted in an active market and derivative contracts, which would be measured at fair value.

Presentation of Impairment and Forgiveness

- An enterprise would be required to first assess for, and recognize in net income, any impairment of a related party financial asset before the forgiveness of the related party financial asset is recognized.
- Except for not-for-profit organizations, the forgiveness of a related party financial asset would be recognized in:
    - Equity when the original transaction that resulted in acquiring the financial asset was not in the normal course of operations; or
    - Net income when the original transaction that resulted in acquiring the financial asset was in the normal course of operations or when it is impracticable to determine whether the amount forgiven originated outside the normal course of operations.
- For not-for-profit organizations, the Board sought stakeholder feedback on whether guidance on forgiveness of related party financial assets was needed.

Modifications and Extinguishment

- All modifications of a related party financial liability would be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.
- Not-for-profit organizations would recognize an extinguishment of a financial liability in accordance with Section 4410, Contributions – Revenue Recognition.

Disclosure

- Requirements would be added to Section 3856 for an enterprise to disclose when it recognizes the forgiveness of a related party financial asset or extinguishment of a related party financial liability in net income because it is impracticable to determine whether the amount forgiven or extinguished originated in the normal course of operations.
- The requirement to permit disclosures about significant risks arising from derivatives would be included with risks arising from other financial instruments, instead of disclosed separately.

The proposals would be applied retrospectively, with simplified transitional provisions, for fiscal years beginning on or after January 1, 2020.

Based on feedback received on the Exposure Draft, the Board is planning to amend some of the proposed changes to make the guidance clearer and to address several issues raised by respondents. The Board plans to issue the final amendments to the Handbook during the fourth quarter of 2018.

Conclusion

As we head closer to the end of the year, now is the time to check with your BDO advisor about how the changes made and the upcoming changes to the standards will affect your organization.