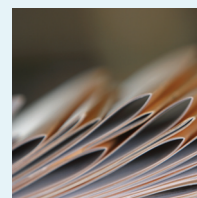




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Filling the GAAP – New Standards for Private Companies – April 2009

Background

In 2006, the Accounting Standards Board (AcSB) decided to pursue separate strategies for publicly accountable enterprises and non-publicly accountable enterprises. They have already announced that publicly accountable enterprises will move to International Financial Reporting Standards (IFRS) for interim and annual periods beginning on or after January 1, 2011. For not-for-profit enterprises (NPOs), the AcSB and the Public Sector Accounting Standards Board (PSAB) jointly issued an Invitation to Comment requesting feedback from stakeholders on the future direction of standards for NPOs. See BDO's publication "[Not-for-Profit Organizations Update – February 2009](#)" for further details on the Invitation to Comment.

In 2007, the AcSB spent time researching the needs of users of private enterprise financial statements to determine the direction of private enterprise standards; they issued an Invitation to Comment and held various roundtables around the country. Based on the feedback they received, the AcSB decided to develop a stand-alone set of accounting standards that would be available to all private enterprises using the following approach:

- They would maintain a common conceptual framework for both publicly accountable enterprises and private enterprises. The AcSB wants to keep the same basic financial statement concepts and definitions for the elements of financial statements (assets, liabilities, equity, revenue and expenses);
- The February 2008 Canadian Institute of Chartered Accountants' (CICA) Handbook would be the starting point for the new private enterprise generally accepted accounting principles (GAAP);
- Standards that do not apply to private enterprises would be eliminated from the Handbook. A list of the Sections and Guidelines the AcSB proposes to remove appears in Appendix A;
- All EIC Abstracts would be eliminated. Abstracts that contain key principles addressing issues of importance to private enterprises would be incorporated into the relevant Handbook Sections in the new GAAP for private enterprises. A list of the Abstracts that contain some principles or concepts that the AcSB proposes to incorporate into certain Handbook Sections in the proposed GAAP for private enterprises is located in Appendix B;
- The issues that were considered significant problem areas for private enterprises would be reconsidered by the AcSB from a cost / benefit standpoint to determine if simplifications could be made for private enterprises;
- Disclosures would be revisited for all Sections and Accounting Guidelines with a focus on what disclosures were needed for private enterprise users; and
- The recognition, measurement, and presentation requirements in the remainder of the standards in the existing Handbook would remain as is.

In the fall of 2008, the AcSB held round tables across the country to obtain feedback from stakeholders in the sector on the approach being taken to develop the new Handbook for private enterprises. As a result of the feedback, the AcSB added some topics to its list of problem areas for private enterprises.

The Result: Canadian GAAP for Private Enterprises

Applicability

The Exposure Draft for the new GAAP was issued on April 30, 2009, with the Basis of Conclusions for the Exposure Draft to be issued imminently. The new GAAP for Private Enterprises will be stand-alone standards and all private enterprises will be given the choice of applying full IFRS or the new Canadian GAAP for Private Enterprises. All the accounting policy choices allowed will be a free choice for all private enterprises; as a result, there will no longer be any requirement for unanimous consent by shareholders or other users for different accounting policy choices, as is currently required under Section 1300, *Differential Reporting*.

Significant Changes

Disclosures

The proposed GAAP for Private Enterprises retains the overall disclosure requirement in Section 1400, *General Standards of Financial Statement Presentation* that requires an entity to provide clear and sufficient information about transactions or events that are of a size, nature or incidence that their disclosure is a necessity to understand their effect on the financial statements. With the reduction of disclosures in the proposed Handbook, there will be more judgment required to determine what disclosure is necessary for users to understand the financial statements, but ultimately Section 1400 still requires sufficient disclosure about transactions or events to explain their effect.

Overall, the AcSB believes the reduction in the number of disclosures is significant; for example, the required disclosures for pensions have decreased approximately 60%, inventory disclosures have decreased by approximately 80% and Section 1535, *Capital Disclosures* and the requirement to disclose upcoming accounting changes (new or amended GAAP) were deleted entirely. Total required disclosures for financial instruments appear to have been reduced by approximately 25% from the level of disclosure currently required for private enterprises; compared to their public company counterparts, who are required to follow Sections 3862, *Financial Instruments – Disclosure* and 3865 – *Hedges*, private enterprises seem to have approximately 60% less required disclosure.

The current Handbook disclosures were developed to meet the financial statement needs of users of publicly accountable, private and not-for-profit entities' financial statements. The users in these three different groups have a very diverse range of needs when it comes to disclosures, so some disclosures that may be necessary for publicly accountable entities' and NPOs' users may not be as relevant to private enterprise users. Ultimately, the AcSB determined that the disclosures in the current handbook can be broken down into six different categories:

- **Accounting Policies** adopted and any changes in them;
- **Risks and Uncertainties** (for example, going concern);
- **Assumptions** used in any estimates;
- **Reconciliations** of any amount on the financial statements to another amount;
- **Detailed Breakdowns** of figures in the financial statements; and
- **Unusual Events** (for example, subsequent events).

In determining the level of disclosure for private enterprises, the AcSB heard the users in this sector say they were most concerned with accounting policies, risks and uncertainties and unusual events and would not be willing to accept reductions in disclosures in these areas. Users believe those types of disclosures are necessary to understand and analyze an entity's financial statements and assess the ability of the entity to meet its future obligations. The AcSB believes users of private enterprise financial statements may be more amenable to reductions in disclosures in the other areas, as long as, the financial statements meet the general disclosure requirement in Section 1400.

Financial Instruments

The new proposed Section 3856, *Financial Instruments* will replace, combine or eliminate a number of Sections from the former Handbook. See Appendix A for a list of the Sections.

The highlights of the proposed new standard are as follows:

- Most accounting choices for financial instruments have been eliminated (e.g. no option to capitalize some transaction costs, no classification choices like Available-for-Sale or Held-for-Trading, no settlement-date recognition option for financial assets);
- All financial assets and liabilities, with two exceptions, are measured at cost less impairment (e.g. portfolio investment in a private company) or amortized cost less impairment (e.g. accounts receivable, accounts payable, loans). The following are recorded at their fair values:
 - All free standing derivatives that are not part of a hedging relationship for which hedge accounting is used; and
 - Investments in equity securities that are quoted in an active market (e.g. Royal Bank of Canada Shares).
- The Section ignores all embedded derivatives except those embedded in long-term debt;
- Entities will be given the option of assigning a zero value to the conversion option in convertible debt; thus, convertible debt can be entirely presented as a liability;
- Redeemable preferred shares issued in certain tax planning arrangements are now always shown as a part of equity;
- There is now one impairment model for all financial assets. Previously there were different models for different items (accounts receivable, impaired loans, investments in significantly influenced entities etc.). Impairment must now be assessed for all significant assets individually. All other items may be grouped for assessing impairment based on credit risk characteristics (e.g. number of days past due, geography, industry). If there are events or circumstances that demonstrate the financial asset (or group of assets) may be impaired, it is written down to the highest of:
 - The present value of the estimated future cash flows from holding the asset(s) (discounting is not necessary for short-term items);
 - The net amount that could be realized by selling the asset at the balance sheet date; and
 - The amount the entity would receive by exercising its right to collateral to secure repayment.If the value increases in a future period, the item(s) may be written back up as far as its (their) original carrying value.
- For hedge accounting:
 - Hedge accounting will only be allowed when the critical terms of the hedging item and hedged item are the same; in other words, the changes in fair value or cash flows attributable to the risk being hedged are expected to offset completely;
 - There will no longer be any requirement to document the risk management strategy and relate the relationship to a risk management objective but some documentation requirements at the inception of the hedge transaction will remain;
 - Assessments of effectiveness will not be required, but an ongoing assessment that any designated relationship continues to meet the “critical terms match” conditions will be required; and
 - The derivatives in a qualifying hedge relationship will not be accounted for at fair value; this treatment of the derivative is similar to the treatment that had been used in former Accounting Guideline 13 – “Hedge Accounting.”

Future Income Taxes

In the proposed income taxes standard, private entities will have a free choice between the taxes payable method and the future income taxes method in accounting for income taxes. Additional illustrative guidance has been provided for entities that adopt the taxes payable method to demonstrate what is required for the reconciliation of the income tax rate or expense to the statutory income tax rate or expense due to confusion in the private enterprise sector of what is required in the disclosure. An example illustration has been provided in Appendix C.

Business Combinations

The new Handbook for private enterprises will replace Sections 1581, *Business Combinations* and Section 1600, *Consolidated Financial Statements* with the new standards Section 1582, *Business Combinations*, 1601, *Consolidated Financial Statements* and 1602, *Non-controlling Interests*. Any entity choosing to apply the new Handbook will have to apply the new Sections. The new business combinations model is substantially different than the previous model, but it will be the same one public companies will adopt on their conversion to IFRS. See BDO Publication [Canadian GAAP - IFRS Comparison Series - Issue 11 - Business Combinations](#) for a description of the differences between current Canadian GAAP for Business Combinations and the IFRS model.

Stock-Based Compensation

The current CICA Handbook includes an exception for private companies that allows them to use the minimum value method when calculating the fair value of a stock option (or its equivalent) using an option pricing model. The minimum value method ignores the volatility of the private entity's equity in the option pricing model. The proposed Section 3870, *Stock-based Compensation and Other Stock-based Payments* removes the minimum value method as an option, requiring all private enterprises to incorporate volatility into their calculations when measuring stock-based compensation. Entities will be allowed to use the calculated value method to estimate their volatility. This method requires management to consider the size and industry of the entity and then use an appropriate sector index such as the Dow Jones Industrial Average to estimate volatility.

Goodwill and Intangible Assets

The proposed Section makes the current differential reporting option for impairment testing available to all private enterprises. Private enterprises will only test for impairment if there are indicators that suggest impairment.

In addition, the proposed Section tests for impairment of goodwill at the reporting unit level rather than mandating the additional step of allocating the fair value of the reporting unit to individual assets and liabilities, which was required previously.

Internally-Developed Intangible Assets

Under proposed Section 3064, *Goodwill and Intangible Assets*, private enterprises will be given a choice between capitalizing and expensing development costs on internally generated intangible assets that meet certain criteria (the same criteria that are in the current Section 3064, *Goodwill and Intangible Assets*). Previously, entities were required to capitalize all development costs incurred on internally developed intangible assets that met the criteria.

Employee Future Benefits

During its various round tables, the AcSB heard concerns that the accounting for "Individual Pension Plans" was too onerous for private enterprises. As a result, a simplified approach has been proposed in Section 3461, *Employee Future Benefits* for defined benefit plans for which the only members are the controlling owner, his or her spouse or both. A significant number of individual pension plans should qualify for the simplified approach. Entities with plans that qualify will be allowed to:

- Use the actuarial valuation that is prepared for funding purposes to measure the obligation. This will eliminate the need for and cost of the actuarial valuation for accounting purposes that many entities had to obtain to account for these types of plans under GAAP; and

- Recognize all actuarial gains and losses and past service costs in net income when they occur rather than amortizing them.

All other defined benefit plans will continue to use the recognition and measurement requirements in Section 3461 that are used currently in practice.

Asset Retirement Obligations (ARO)

The proposed Section attempts to provide a more simplified approach (based on International Accounting Standard 37, *Provisions, Contingent Liabilities and Contingent Assets*) to measure the ARO. The amount that is recognized as an ARO is the best estimate of the expenditure that will be required to settle the present obligation at the end of the reporting period. The Section is less prescriptive than its predecessor and bases the estimate on management’s experience and judgment.

Investments in Subsidiaries, Interests in Joint Ventures and Investments in Significantly Influenced Investees

Private enterprises are now given the free choice to account for these investments as follows:

	Investments in Subsidiaries (Section 1590)	Interests in Joint Ventures (Section 3055)	Investments in Significantly Influenced Investees (Section 3051)
Measurement Choice	1. Consolidation 2. Cost Method 3. Equity Method	1. Proportionate Consolidation 2. Cost Method 3. Equity Method	1. Cost Method 2. Equity Method
	Note: If the investment is quoted in an active market, then fair value must be used in place of the cost method. This results in the same treatment as other equity investments that are quoted in an active market and are recorded at fair value under Section 3856, <i>Financial Instruments</i> . The consolidation and equity method options will still remain as alternative policy choices for the entity.		

As previously discussed under financial instruments, the AcSB is proposing one impairment model for all financial assets. Investments in subsidiaries and interests in joint ventures that are not consolidated and investments in significantly influenced investees will also be assessed for impairment using the impairment model in Section 3856, *Financial Instruments*. The old concept of assessing if an impairment is “other than temporary” will no longer exist.

Current Liabilities

The current Handbook requires all demand or callable debt to be shown as a current liability. The proposed Handbook provides illustrative guidance to demonstrate an alternative way of presenting debt that has stated repayment terms but also is callable at the option of the holder. Entities must still show the debt as current, but they may show the debt after a subtotal for all other current liabilities. See Appendix D for an example of the proposed balance sheet presentation and note disclosure.

Proposed New Section 1521 – Balance Sheet

Similar to Section 1520, *Income Statement*, this Section was drafted as a useful guide for preparers of financial statements; it is intended as a “one-stop-shop” for preparers to see what needs to be presented separately in the balance sheet, rather than having to go through various Handbook Sections. It will not add any additional presentation requirements; it only summarizes the presentation requirements of assets, liabilities and equity in one Section.

Effective date

The proposed effective date for the new GAAP for Private Enterprises is for interim and annual periods beginning on or after January 1, 2011. At that point, the current CICA Accounting “blue book” will disappear. Early adoption will be allowed. The AcSB hopes to have the final Handbook out by the end of the year and if this happens, private enterprises could early adopt the Handbook for December 31, 2009 year ends.

Transitional Guidance

The adoption of the new Handbook will generally require retrospective treatment; in other words, prior years figures will have to be restated as if the Handbook had always been applied. The good news is the Exposure Draft contains a new Handbook Section 1500, *First-time Adoption* that provides relief to entities that elect specific exemptions on initial adoption of GAAP for Private Enterprises. Without the Section, adopting this new GAAP for the first time could result in significant costs for entities when they apply certain sections. For example, an entity that may have never used GAAP accounting would have had to look for accounting information for business combinations from many years ago in order to comply with the Handbook; the business combination exemption will provide relief in this case. The areas for which there are possible exemptions / exceptions on first-time adoption are listed in Appendix E.

The Future for Canadian GAAP for Private Enterprises

The AcSB plans to leave the Accounting Handbook for Private Enterprises in place for at least five years, upon which, they will reassess their strategy for the sector. They intend to add new standards or make amendments to the Handbook only once every year or two to allow the sector time to adjust to changes. The AcSB continues to reiterate its plans to transition private enterprise standards so they align with IFRS.

Conclusion

Changes are coming for private enterprises. The AcSB is looking for comments on its Exposure Draft. We would strongly encourage stakeholders in this sector to thoroughly review and respond to the Exposure Draft to make sure their opinions are heard. The deadline to provide comments to the AcSB is July 31, 2009.

Appendix A

Standards Removed from the Proposed GAAP for Private Enterprises

Items Not a Part of GAAP for Private Enterprises	Explanation
Section 1300 – <i>Differential Reporting</i>	Differential reporting was created to provide relief to private enterprises. Since the Handbook is now entirely for private enterprises, the options are either hard-coded into the sections themselves as policy choices or removed, eliminating the need for the section.
Section 1530 – <i>Comprehensive Income</i> Section 3855 – <i>Financial Instruments – Recognition and Measurement</i> Section 3861 – <i>Financial Instruments – Disclosure and Presentation</i> Section 3862 – <i>Financial Instruments – Disclosures</i> Section 3863 – <i>Financial Instruments – Presentation</i> Section 3865 – <i>Hedges</i> Section 3020 – <i>Accounts and Notes Receivable</i> Section 3025 – <i>Impaired Loans</i> Section 3210 – <i>Long-term Debt</i> Accounting Guideline 4 – <i>Fees and Costs Associated with Lending Activities</i> Accounting Guideline 12 – <i>Transfers of Receivables</i> Accounting Guideline, AcG-13 – <i>Hedging Relationships</i>	The entire financial instruments suite along with Sections and Guidelines that pertained to some specific financial instruments (accounts receivable, impaired loans, long-term debt etc.) were removed and have been replaced with a new Section 3856 – <i>Financial Instruments</i> , which covers Recognition, Measurement, Presentation and Disclosure for Financial Instruments. There is now one impairment model for all financial assets.
Section 1535 – <i>Capital Disclosures</i>	The section related entirely to disclosure. Removed as part of overall review of disclosures.
Section 1581 – <i>Business Combinations</i> Section 1600 – <i>Consolidated Financial Statements</i>	Replaced with Section 1582 – <i>Business Combinations</i> , Section 1601 – <i>Consolidated Financial Statements</i> and Section 1602 – <i>Non-controlling Interests</i> . These sections were added into the current CICA Handbook in January 2009. The new sections converge with the IFRS business combinations standards.
Section 1701 – <i>Segment Disclosures</i> Section 3500 – <i>Earnings Per Share</i> Accounting Guideline 7 – <i>“The Management Report”</i>	These Sections and Guidelines are only applicable to public companies.
Section 1751 – <i>Interim Financial Statements</i>	This section appears to be rarely used by / applicable to private enterprises. Private enterprises can look to International / US standards if they need guidance.
Section 3040 – <i>Prepaid Expenses</i>	This section was only one line which is now incorporated into Section 1510 – <i>Current Assets and Current Liabilities</i> .

Items Not a Part of GAAP for Private Enterprises	Explanation
Section 3480 – <i>Extraordinary Items</i>	There is no such Section under IFRS. It did not make sense for private enterprises to have more stringent requirements than their public counterparts. Section 1400 – <i>General Standards of Financial Statement Presentation</i> still contains the general requirement to disclose transactions and events in sufficient detail for users to understand their effect.
Section 4100 – <i>Pension Plans</i>	Pension plans are not private enterprises.
Section 4211 – <i>Life Insurance Enterprises</i> Accounting Guideline 3 – “ <i>Financial Reporting by Property and Casualty Insurance Companies</i> ” Accounting Guideline 8 – “ <i>Actuarial Liabilities of Life Insurance Enterprises – Disclosure</i> ” Accounting Guideline 9 – “ <i>Financial Reporting by Life Insurance Enterprises</i> ”	Life insurance enterprises are not private enterprises.
Section 4250 – <i>Future-Oriented Financial Information</i>	Guidance for future-oriented financial information will be sent to the Canadian Performance Reporting Board as it is not seen as a GAAP reporting issue.
Sections 4400 to 4470 – <i>Not-for-Profit Organizations (NPOs)</i>	Currently, the private enterprise Handbook is only intended for private enterprises and not NPOs; however, the AcSB and Public Sector Accounting Board have issued a joint Invitation to Comment (ITC) “ Financial Reporting by Not-for-Profit Organizations ” that could result in some form of these Sections remaining. See the BDO Publication “ Not-for-Profit Organizations Update – February 2009 ” for discussion of the ITC.
Accounting Guideline 11 – “ <i>Enterprises in the Development Stage</i> ”	Once changes were made to Section 3064, <i>Goodwill and Intangible Assets</i> , this Guideline no longer provided any significant additional guidance that could not be interpreted from Section 3064.
All EIC Abstracts	Public enterprises will not be required to follow EIC Abstracts once they move to IFRS so the AcSB felt that the private enterprise Handbook should not include them. Also, quite a few of the Abstracts are very prescriptive and the AcSB wants Canadian enterprises to move to a more principle-based framework similar to IFRS. Some principles from the Abstracts were incorporated into the private enterprise Handbook itself (e.g. leases, revenue). See Appendix B for a list.

Appendix B

List of EIC Abstracts for which Components are included in the Proposed Standards

All the EIC Abstracts were removed from the new GAAP for Private Enterprises. Below is a list of those abstracts which had portions included in the related Sections in the Handbook:

EIC-8, – “Recognition of an Equity Accounted Investee’s Losses in Excess of the Investment”	A summary of the consensus on the first issue in this Abstract is incorporated into Section 3051, <i>Investments</i> .
EIC-19, – “Minimum Lease Payments and Contingent Rentals” EIC-21, – “Accounting for Lease Inducements by the Lessee” EIC-25, – “Accounting for Sales with Leasebacks” EIC-97, – “Accounting for a Guarantee by the Lessee In Connection with (1) an Operating Lease and (2) a Sales-Leaseback Transaction”	Summaries of the consensuses in these Abstracts are included in Section 3065, <i>Leases</i> .
EIC-52, – “Lessee’s Accounting on Re-negotiation of an Operating Lease”	A summary of the consensus on the first issue in this Abstract is included in Section 3065, <i>Leases</i> .
EIC-59, – “Long-Term Debt with Covenant Violations” EIC-122, – “Balance Sheet Classifications of Callable Debt Obligations and Debt Obligations Expected to be Refinanced”	Summaries of the consensuses in these Abstracts are included in Section 1510, <i>Current Assets and Current Liabilities</i> along with a new Illustrative Example for the Presentation of Callable Debt Obligations (See Appendix D).
EIC-77, – “Application of Section 3840 to a Transaction Involving the Issuance of Non-Voting Participating Shares to an Unrelated Party” EIC-103, – “Related Party Transactions — Meaning of a Substantive Change and Measurement of a Change in a Transfer of Ownership Interests”	Summaries of the consensuses in these Abstracts are included in Section 3840, <i>Related Party Transactions</i> .
EIC-78, – “Construction Contractors — Revenue Recognition When the Percentage of Completion Method is Applicable” EIC-141, – “Revenue Recognition”	Summaries of the consensuses in these Abstracts are included in Section 3400, <i>Revenue</i> .
EIC-132, – “Share Purchase Financing”	A summary of the consensus in this Abstract is included in Section 3251, <i>Equity</i> .
EIC-133, – “Unit of Accounting for Testing Impairment of Indefinite-Lived Intangible Assets”	A summary of the consensus in this Abstract is included in Section 3064, <i>Goodwill and Intangible Assets</i> .

<p>EIC-142, – “Revenue Recognition with Multiple Deliverables”</p>	<p>The basic principle in the Abstract is incorporated by including paragraph 13 of International Accounting Standard (IAS) 18, <i>Revenue</i> in Section 3400, <i>Revenue</i>.</p> <p>Essentially the principle is as follows:</p> <p>“...in certain circumstances, it is necessary to apply the recognition criteria to the separately identifiable components of a single transaction in order to reflect the substance of the transaction...Conversely, the recognition criteria are applied to two or more transactions together when they are linked in such a way that the commercial effect cannot be understood without reference to the series of transactions as a whole.”¹</p>
<p>EIC-149, – “Accounting for Retractable or Mandatorily Redeemable Shares”</p>	<p>A summary of the consensus on the first issue in this Abstract is included in new Section 3856, <i>Financial Instruments</i>.</p>
<p>Former EIC-158, – “Accounting for Convertible Debt Instruments”</p>	<p>Summaries of the consensuses on the first four issues are incorporated in new Section 3856, <i>Financial Instruments</i>.</p>

¹ International Financial Reporting Standards, International Accounting Standard 18, 2008.

Appendix C

Illustrative Examples of Rate Reconciliation Disclosure - Taxes Payable Method

Private enterprises can provide the rate reconciliation disclosure using the income tax rates or the income tax expense. One example of each has been provided.

Example 1 – Using the income tax expense

Note X: Income taxes

The Company accounts for income taxes using the taxes payable method. As a result, the company's income tax expense varies from the amount that would otherwise result from the application of the statutory income tax rates as set out below:

	<u>2011</u>	<u>2010</u>
Net income before income taxes	<u>\$110,000</u>	<u>\$ 95,000</u>
Expected income tax expense at the combined basic Federal and Provincial tax rate of 44% (2010 - 46%)	<u>\$ 48,400</u>	<u>\$ 43,700</u>
Increase (decrease) in income tax expense due to:		
Non-taxable income and non-deductible expenses	<u>3,000</u>	1,800
Income or expenses claimed in different periods for income tax purposes:		
Capital cost allowance in excess of amortization	<u>(3,400)</u>	(4,500)
Interest in net earnings of affiliate	<u>(10,000)</u>	<u>(10,000)</u>
	<u>38,000</u>	31,000
Rate adjustments:		
Small business deduction	<u>(18,000)</u>	(14,200)
Manufacturing and processing deduction	<u>(3,500)</u>	<u>(2,700)</u>
Income tax expense per financial statements	<u>\$ 16,500</u>	<u>\$14,100</u>

Example 2 – Using the income tax rates

The note is the same as the previous note except for the reconciliation which is below:

	<u>2011</u>	<u>2010</u>
Net income before income taxes	<u>\$110,000</u>	<u>\$ 95,000</u>
Combined basic federal and provincial tax rates	<u>44%</u>	46%
Increase (decrease) in income tax expense due to:		
Non-taxable income or non-deductible expense	<u>2%</u>	2%
Income or expenses claimed in different periods for income tax purposes:		
Capital cost allowance in excess of amortization	<u>(3%)</u>	(5%)
Interest in net earnings of affiliate	<u>(9%)</u>	<u>(11%)</u>
	<u>34%</u>	32%
Rate adjustments:		
Small business deduction	<u>(16%)</u>	(15%)
Manufacturing rate deduction	<u>(3%)</u>	(3%)
Effective income tax rate (Income tax expense \$16,500 (2010 — \$14,100).	<u>15%</u>	<u>14%</u>

Appendix D

Illustrative Example of the Presentation of Callable Debt

	<u>2011</u>	2010
Current		
Accounts payable and accrued liabilities	\$10,000	\$15,000
Income taxes payable	2,000	1,500
Deferred revenue	1,000	500
Scheduled cash repayments for long-term debt (Note X)	<u>18,000</u>	<u>18,000</u>
Current liabilities before callable debt	31,000	35,000
Callable debt (Note X)	<u>26,000</u>	<u>38,000</u>
Total current liabilities	57,000	73,000
Long-term debt (Note X)	<u>6,000</u>	12,000
Total liabilities	<u>63,000</u>	<u>85,000</u>

Note X – Long-term Debt

	<u>2011</u>	2010
Prime plus 2%, repayable \$500 monthly plus interest, secured by equipment, due December 2013	\$12,000	\$18,000
Prime plus 3%, repayable \$1,000 monthly plus interest, secured by general security agreement, callable on demand (i)	<u>38,000</u>	<u>50,000</u>
Total debt	<u>50,000</u>	<u>68,000</u>
Less: Scheduled cash repayments due within one year	(18,000)	(18,000)
Callable debt (i)	<u>(26,000)</u>	<u>(38,000)</u>
Current debt	<u>(44,000)</u>	<u>(56,000)</u>
Long-term debt	\$ 6,000	\$12,000

- (i) Canadian generally accepted accounting principles require that loans that the lender can require to be repaid on demand be classified as current liabilities.

Management does not believe that the demand features of the callable debt will be exercised in the current period. Assuming payment of the callable debt is not demanded, regular principal repayments required on all long-term debt for the next five years are due as follows:

2012	\$18,000
2013	18,000
2014	12,000
2015	2,000
2016	—
	<u>\$ 50,000</u>

Appendix E

Proposed Transitional Guidance on First Time Adoption of Canadian GAAP for Private Enterprises

An entity may elect to use exemptions provided in the proposed Section 1500, *First Time Adoption* related to one or more of the following on first time adoption of the new GAAP for Private Enterprises:

- Business Combinations
- Fair Value
- Employee Future Benefits
- Cumulative Translation Adjustments
- Financial Instruments
- Stock-Based Compensation and Other Stock-based Payments
- Asset Retirement Obligations
- Related Party Transactions