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Assurance and Accounting

Accounting Standards for Not-For-Profit Organizations (ASNPO) Update 2021

Introduction

It was a busy year for the Accounting Standards Board (AcSB or the Board) and for Part III of the CPA Canada Handbook – Accounting: Accounting Standards for Not-for-Profit Organizations (ASNPO). As was the case with many, the Board has been hard at work dealing with the ever-evolving situation of the COVID-19 pandemic. The Board has continued to adjust and make quick decisions to ensure they are continuing to address stakeholder needs while also furthering the progress of various projects, including its project on the recognition of contributions.

In addition, a new standard was issued around the accounting for the combinations of NPOs. Although this standard is not applicable until 2022, it is highly recommended that entities consider early adoption if entering into a combination. Given the pressures of COVID-19, there has been an increase in combinations, which is why issuing this new standard was a priority for the Board.

This publication will discuss this change as well as, provide a highlight on the evolving COVID-19 accounting impacts, an outline of other amendments and standards effective over the next few years and an overview of the projects the Board has on the go that will affect not-for-profit organizations.

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 highlight the significant ASPE changes and provide a list of other ASPE changes relevant to NPOs. To see more details on the ASPE changes refer to our 2021 ASPE Update publication by clicking here.

COVID-19 Impacts

Global, national, and local responses to COVID-19 are continuing to evolve and change. The implications of this virus are far reaching. It is impacting operations across multiple sectors and continues to lead to economic uncertainty. As vaccination efforts continue to improve there has been improvement across most industries but, the threat of variants and further lockdowns still remain. Some of the ways in which the pandemic is still affecting entities include:

- Reduced consumer demand for goods and services due to lost income and/or restrictions on consumers' ability to move freely;
- Reduction in ability to provide goods and services and lost revenues due to government imposed shutdowns and product shortages;
- Difficulties in collecting from customers and other counterparties facing financial difficulties;
- Receipt of government grants and discounted loans for economic stimulus;
- Reduction in donations received as individuals and businesses face financial difficulties; and
- Disruption of global supply chains.

The financial reporting implications for entities may be similarly broad, and the precise effects will depend on the facts and circumstances of each entity. The following are some financial reporting considerations NPOs should keep in mind for December 31, 2021 and subsequent year ends.

- As restrictions begin to loosen and businesses begin to open up and return to some form of normal, there is still the need to consider the lingering effects of COVID around going concern and impairment. This has been an unprecedented situation and the lasting effects are still not known.
- To help many business weather these difficult times the government has increased and made government assistance available to more entities. As time passes these programs are being extended or evolving as the virus evolves as well. This funding, especially those which cover multiple periods and years should be reviewed to ensure the accounting is appropriate under ASPE.

- Revenue recognition continues to be an area where additional care must be taken, as entities are still struggling with operations it is important to ensure the revenue criteria for recognition are reviewed and assessed to ensure the timing of revenue recognition is appropriate.
- In addition to the above accounting considerations, an entity should ensure that the financial statements provide sufficient information about the extent and nature of the effect COVID-19 has had on its financial position, operations, and cash flows. This is to ensure readers have a clear understanding of the impact and any potential future impacts as this situation continues to evolve.

Many landlords over the pandemic have provided concessions to tenants. The Board recognized that under the previous guidance in Section 3065, *Leases,* accounting for these concessions from a lessor and lessee perspective was onerous. Therefore, in 2020 the Board amended the guidance in Section 3065 to provide relief to lessors and lessees when accounting for rent concessions related directly to COVID-19. The relief was broken down into two scenarios, a deferral of lease payments and a reduction or waiver of lease payments.

- For a deferral of lease payments with no changes to the total payments required by the original lease contract, a lessee and a lessor would continue to account for the lease according to the terms of the original lease contract. To account for the rent concession, a lessee would recognize a lease payable and a lessor would recognize a lease receivable for the amount representing the deferred lease payments.
- For a reduction in the total payments required, a lessee and a lessor would continue to account for the lease according to the terms of the original lease contract. To account for the rent concession, a lessee and a lessor would recognize the reduction in total lease payments in net income in the period to which the lease payments relate.

This relief became effective for fiscal years ending on or after December 31, 2020 and was originally only covering reductions in payments due on or before December 31, 2021. As the pandemic continues to impact businesses across multiple sectors, the Board extended this relief to cover reductions in payments due on or before December 31, 2022.

Standards Effective in Coming Years

We have only included summaries for ASNPO specific standards and ASPE standards which are expected to have a significant impact on not for profit organizations in this publication. To see summaries of the other ASPE standards that are applicable for not-for-profit organizations click here to access the 2021 ASPE Update Publication. The table at the end of each section will include a list of ASNPO and ASPE topics relevant to not-for-profit organizations to make searching the ASPE Update publication easier. The table will also include resources for each applicable standard.

Standards Effective in 2021

The Board issued no ASNPO specific guidance or amendments that relate to 2021 fiscal years. The Board issued amendments to section 3856, *Financial* Instruments in ASPE. We have included a brief summary here as we believe this will have a direct impact on not-for-profit organizations applying Part III of the CPA Canada Handbook – Accounting. See the table below for resources for this amendment.

Significant Amendments to Section 3856, *Financial Instruments*, and Section 3840, *Related Party Transactions*, on accounting for related party financial instruments

The Board understood that the guidance on accounting for related party financial instruments after initial recognition, and the measurement of related party compound financial instruments was not clear and resulted in diversity in practice. Additionally, financial instrument risk disclosures were not entity-specific which resulted in the entity not providing useful information to financial statement users. The board amended Section 3856 to address these concerns. The amendments focused around the scope, initial measurement, subsequent measurement, presentation of impairment and forgiveness, and the accounting for modifications and extinguishments of related party financial instruments.

The scope of Section 3856 was amended to move all the guidance on related party financial instruments to Section 3856. Section 4460, *Disclosure of Related Party Transactions by not-for-profit organizations* was amended to clarify that a not-for-profit organization applies Section 3856 for the accounting and disclosure of financial instruments in a related party transaction.

Initial and subsequent measurement guidance for related party financial instruments has been added to Section 3856. This requires related party financial instruments to be measured at cost unless, the instrument is quoted in an active market, it is a debt instrument that has inputs that are significant to fair value that are observable, or is a derivative contract, then it is measured at fair value. The cost of a related party financial instrument will depend on if the instrument has repayment terms or not. The equity component of a related party compound financial instrument may be initially measured at zero. The subsequent measurement of a related party financial instrument has been aligned with initial measurement.

An entity must assess and recognize any impairment loss on a related party financial instrument prior to recognizing any forgiveness. The forgiveness of a not-for-profit organization's related party financial assets shall be recognized in operations. All modifications of a related party financial liability are accounted for as an extinguishment.

Lastly, guidance was added to Section 3856 to require all financial instrument risk disclosures to be prepared using enterprise specific information so that the disclosures provide useful information to users.

Amendment/ New Standard	Resources
Significant amendments to Section 3856, *Financial Instruments*, and Section 3840, *Related Party Transactions,* on accounting for related party financial instruments	• ASPE at a Glance: Section 3856, Financial Instruments • ASPE at a Glance: Section 3840, Related Party Transactions

Standards Effective in 2022

The Board issued one new standard in the current year that impacts not-for-profit organizations for their 2022 fiscal years. The remaining changes related to ASPE standards that impact not-for-profit organizations. We have highlighted the amendments made to Section 3400, *Revenue* for upfront fees as we feel this will be an area of change for many not-for-profit organizations. For a more detailed look at the changes to Section 3400 and other ASPE standards please refer to the 2021 ASPE Update Publication by clicking here. The table below list the ASPE changes that will impact not-for-profit organization's and includes applicable resources.

Section 4449, Combinations by not-for-profit organizations

Combinations between not-for-profit organizations ("NPOs") are becoming more frequent. As no guidance on accounting for these types of transactions was previously included in either ASNPO or ASPE, there was diversity in practice. As a result, in March 2021, the Board issued new Section 4449, *Combinations by not-for-profit organization.* The main points of the standard include:

Scope

- This section applies to a combination involving two or more NPOs that are unrelated parties or related parties.
- This section does not apply to the acquisition of a for-profit enterprise by an NPO, a contribution of a for-profit enterprise to an NPO, a contribution of cash or other assets which do not constitute an NPO to an NPO and the formation of a joint venture.

Distinguishing between a merger and an acquisition

- The accounting treatment for a combination depends on the substance of the transaction. Determining the proper accounting treatment depends on certain characteristics and criteria being met.
- Except for a combination of NPO's under common control which is always accounted for as a merger, a combination is accounted for as a merger when all the following are met:
  - Neither party to the combination is considered the acquirer or acquiree.
  - Those charged with governance of the previous organizations participate in determining terms of the combined organization.
  - No significant consideration flows to a third party, other than transaction costs.
  - The combined organization must encompass the purposes of the combining NPOs.
  - At the combination date there is no decline or planned decline in the client communities serviced
- If any of the above criteria are not met the combination would be accounted for as an acquisition

Accounting for a Combination as a Merger

- The carrying values of the assets, liabilities and net assets of the combining entities become the combined carrying values of the assets, liabilities, and net assets of the combined organization.
- Where the combining organizations have been applying different accounting policies in their separate financial statements, the combined organization shall make adjustments to ensure the accounting policies are uniform in both the current and comparative period.
- Comparative information shall also be presented showing the combined results as though the organizations had always been combined. The figure shall be marked as combined figures.
- Subsequently, the organization shall account for the combined assets, liabilities, and net assets in accordance with other applicable Sections for those items.
- The organization shall disclose information that enables users to evaluate the nature and financial effect of the combination that occurred during the current reporting period.

Accounting for a Combination as an Acquisition

- An acquirer and acquiree must be determined in the transaction using guidance in Section 4450, *Reporting Controlled or Related Entities by Not-for-Profit Organizations*.
- The transaction is accounted for using the acquisition method. The organization can either disclose or consolidate its controlled not-for-profit organizations.
- Where the organization decides to consolidate, at the combination date the acquirer shall recognize the identifiable assets and liabilities of the acquiree at their acquisition date fair values.
- Where there is excess consideration, or a bargain purchase, this amount is recognized and presented separately in the statement of net assets.
- Subsequently, the organization shall account for the acquired assets and assumed liabilities in accordance with other applicable Sections for those items.
- Where the organization chooses to disclose the controlled NPO, it should identify the acquirer, determine the combination date, and include disclosures required by both Section 4449 and 4450.

Significant amendments to Section 3400, Revenue on accounting for multiple-element arrangements, bill-and-hold arrangements, the percentage of completion method, gross vs. net revenue recognition and upfront non-refundable fees

In 2017, the AcSB issued a survey asking stakeholders for feedback on issues they encountered when applying the guidance in Section 3400, *Revenue*. Based on the feedback provided, the Board understood that a lack of guidance in certain areas was causing issues when applying the standard. As a result, in December 2019 the Board issued an amendment to Section 3400.

For not-for-profit organizations, the biggest change is the guidance issued around the accounting for upfront non-refundable fees. Under this guidance an entity will need to assess if the fee paid is received in exchange for a good or service provided to a customer that would meet the revenue recognition criteria or the fee has stand alone value to the customer. If this is not the case, then the upfront non-refundable fee and the remaining fees to be paid upon the delivery of the service or good are considered an integrated package. The revenue from the upfront non-refundable fee must be deferred and recognized over the period or periods where the related product or service is delivered or performed. This guidance will likely be very different to what is currently being performed in practice around these fees. For more information on all the amendments made to Section 3400, refer to the 2021 ASPE Update Publication by clicking here.

Amendment/ New Standard	Resources
New standard Section 4449, *Combinations by not-for-profit organizations*	• ASNPO at a Glance: Section 4449, Combinations by not-for-profit organizations – *Coming soon!*
Significant amendments to Section 3400, *Revenue*, on accounting for multiple-element arrangements; bill-and-hold arrangements; the percentage of completion method; gross vs. net revenue recognition; and upfront non-refundable fees	• ASPE at a Glance: Section 3400, Revenue
Amendments to Section 3462, Employee Future Benefits for the use of a funding valuation.	• ASPE at a Glance: Section 3462, Employee Future Benefits

Projects on the Go

The AcSB currently has a number of projects in progress that propose future changes to standards that will impact NPOs. The following provides a brief discussion of these projects. We have only included summaries here for ASNPO specific projects and the AcSB Strategic Plan. Please refer to the 2021 ASPE Update Publication by clicking here to see summaries for the following ASPE projects that will impact not-for-profit entities.

- **Exposure Draft – Effect of IBOR Reform on Financial Reporting**
- **Project – Cloud Computing Arrangements**
- **Project – Financial Statement Concepts**

Consultation Paper – AcSB Strategic Plan

The Board sets out strategic plans to provide broad objectives that will guide them in achieving their public interest mandate. The current strategic plan remains in effect until March 31, 2022, and the Board is undertaking this project to develop the next Strategic Plan. In May 2021 the Board issued a Consultation Paper seeking comments on the Draft Strategic Plan which will cover the years 2022 to 2027. The Strategic Plan is broken down into three major areas where work will be completed;

- Deliver relevant and high-quality accounting standards
  - Review and potentially update the Preface of the Handbook to evaluate whether to continue or change the framework required to be used by certain entities.
  - Explore how the frameworks work together and consider scaling the standards to better meet the range of needs of Canadian entities, and their financial statement users. This may include allowing additional accounting policy choices and/or addressing the extent of disclosures required for certain frameworks.
  - Continue to establish high-quality accounting standards for publicly accountable enterprises, private enterprises, not-for-profit organizations, and pensions.
- Demonstrate leadership in reporting beyond traditional financial statements
  - Ensure the voice of Canadian stakeholders are heard.
  - Consider the connection between financial and non-financial reporting
  - Continue to respond to stakeholder needs by developing guidance as needed.
- Raise the AcSB's International Influence
  - Continue to share the views of Canadian stakeholders on a global scale.
  - Continue to engage with other standard setters in Canada and globally to help further develop Canadian domestic standards.
  - Continue to influence and participate in the development of IFRS standards.

The Board is currently seeking feedback on this Consultation Paper and stakeholders are encouraged to respond, the Consultation Paper can be accessed here, all comments must be received by October 15, 2021.

Consultation Paper - Contributions – Revenue Recognition and Related Matters

The AcSB wants to ensure that the guidance on accounting for contributions in Part III of the Handbook is still appropriate. The existing contributions standard has remained largely unchanged since it was established almost 25 years ago. However, research suggests that the landscape for many NPOs has changed over the years and that contribution agreements are becoming more complex. Additionally, the AcSB has heard from users of NPO financial statements that the current accounting policy choice for recognizing contributions (deferral method or restricted fund method) adds complexity to NPO financial statements and creates a lack of comparability among the financial statements of similar NPOs. On the other hand, preparers of NPO financial statements have informed the AcSB that the accounting policy choice accommodates the diverse needs of NPOs and their users and allows individual NPO's to clearly communicate their operations and results.

The Board has undertaken extensive research over the past few years to gain a preliminary understanding of the benefits of, and issues with, the existing contributions guidance. Then in May of 2020, the Board issued a Consultation Paper seeking input from NPO stakeholders, including financial statement users, preparers, and practitioners on:

- The definition of restricted and unrestricted contributions;
- The timing for recognition of revenue from contributions;
- Specific types of contributions and transactions, including:
  - Contributed materials and services;
  - Endowment contributions;
  - Capital asset contributions;
  - Bequests;
  - Pledges;
- Presentation and disclosure:
  - The use of fund accounting presentation;
  - Presentation of net assets including restricted and unrestricted net assets;
  - Disclosure of restricted cash and other restricted assets;
- The exemption from recognizing tangible and intangible capital assets when an NPO's average consolidated revenues for the current and preceding fiscal years are less than $500,000; and
- The interaction between the financial statement concepts in Section 1001, *Financial Statement Concepts for Not-for-Profit Organizations*, and the accounting for contributions.

The information gathered from this Consultation Paper is helping the Board decide on the direction this project on accounting for contributions should go. Any guidance developed through this project would aim to balance the diverse needs and operations of NPOs, while addressing financial statement users concerns.

The Consultation Paper closed for comment on December 31, 2020 and the Board is currently deliberating feedback and deciding on next steps.

Conclusion

As we head closer to the end of the year, now is the time to check in with your BDO advisor about how the impacts of COVID-19, the changes made to the ASNPO Handbook and the projects on the go will affect your organization. Reach out to us today.