

ASSURANCE AND ACCOUNTING

NOT-FOR-PROFIT ORGANIZATIONS: NEW DIRECTIONS

In December 2010, the Accounting Standards Board (AcSB) and the Public Sector Accounting Board (PSAB) each issued the accounting and financial reporting requirements for Not-for-Profit Organizations (NPOs). Which options are available to your NPO will depend on whether or not it meets the definition of a government not-for-profit organization.

Are You a Government Not-for-Profit (GNPO)?

A GNPO is defined in the Public Sector Accounting Standards as an organization that has all of the following characteristics:

- It has counterparts outside the public sector;
- It is an entity normally without transferable ownership interests;
- It is an entity organized and operated exclusively for social, educational, professional, religious, health, charitable or any other not-for-profit purpose; and
- Its members, contributors and other resource providers do not, in such capacity, receive any financial return directly from the organization.

The NPO would also have to be controlled by a government to be considered a GNPO¹. Determining if your organization is a GNPO will determine which standards they will be required to use in the future.

Which Standards Will You Use?

Type of Not-for Profit Organization	Which Accounting Board	Generally Accepted Accounting Principles (GAAP) Options
All NPOs other than Government NPOs	Accounting Standards Board	Choice of: <ol style="list-style-type: none"> 1. Part 1 of CICA Handbook – Accounting: International Financial Reporting Standards (IFRS); OR 2. Part III of CICA Handbook – Accounting: Accounting Standards for Not-for-Profit Organizations (ASNPO). <ul style="list-style-type: none"> • These standards are essentially the relevant standards from Part II of the Handbook: Accounting Standards for Private Enterprises (ASPE) plus NPO-only standards in Part III including the current Section 4400 series of standards with minor modifications.
Government NPOs	Public Sector Accounting Board	Choice of: <ol style="list-style-type: none"> 1. Public Sector Accounting Standards plus the Section 4400 series of NPO-specific standards (with some modifications). This series will be renumbered to become the public sector 4200 series; OR 2. Public Sector Accounting Standards EXCLUDING the new 4200 series of Standards (i.e. choosing not to apply the NPO-specific standards).

¹This requirement is from Public Sector Standard Section 1300.

The Section 4400 to 4470 series of standards that NPOs currently follow contain guidance that is only relevant and applicable to NPOs (such as accounting for contributions). These standards are listed in Appendix A.

All Not-for-Profit Organizations Other than Government Not-for-Profit Organizations

Your NPO may be considering which set of standards you should adopt (IFRS or NPO (i.e. ASPE with addition of NPO-specific standards)). Below summarizes some of the pros and cons of adopting either set of standards.

	Pros	Cons
International Financial Reporting Standards (IFRS)	<p>The financial statements are more useful to the users of your financial statements if:</p> <ul style="list-style-type: none"> Your NPO is compared to other international NPOs who use IFRS; Your NPO is part of a larger NPO that wants to use IFRS; and Your donors are outside of Canada and may better understand financial statements prepared using IFRS. 	<ul style="list-style-type: none"> The disclosures required under IFRS are extensive (the total required disclosures in IFRS are approximately 3000 while the current standards NPOs follow require less than 700). IFRS would require additional resources to gather this information and perhaps a change in information systems to track this information; The Preface to IFRS specifically states that IFRS is designed for financial reporting of <u>all profit-oriented entities</u> and although it is not designed to apply to NPOs, entities with similar activities may find them appropriate. As a result, there will be no guidance for NPOs in a number of areas specific to them (e.g. contribution revenue or impairment from a NPO perspective). The standards will have a profit-oriented user in mind at all times; and NPOs will not be able to use the same fund accounting presentation they use now.
Accounting standards for NPOs (i.e. Accounting Standards for Private Enterprises (ASPE) plus NPO-specific standards)	<ul style="list-style-type: none"> The standards are fairly similar to those which NPOs are following currently, thus less change; More accounting policy choices are provided (e.g. simplified method of accounting for defined benefit employee future benefit plans); NPOs can continue to use their current financial statement presentation format (e.g. fund accounting); Disclosures required are significantly less than IFRS (approximately 700 versus 3000); and Contains standards dealing specifically with NPO issues (e.g. contributions, inventory). 	<ul style="list-style-type: none"> Less disclosure required under ASPE may result in insufficient disclosure for NPO financial statement users (although NPOs have the option of disclosing more).

What are the Differences between Current Canadian Accounting Standards and IFRS / Accounting Standards for NPOs (ASNPO)?

BDO Canada has prepared a number of Publications in our IFRS Comparison Series² that explains the differences between current Canadian Accounting standards and IFRS. If you are interested in more information on the differences, please look [here](#)³.

BDO Canada has also issued a publication describing the differences between current Canadian GAAP and the Accounting Standards for Private Enterprises. NPOs that choose ASNPO will be following ASPE. If you are interested in what has changed, look [here](#)⁴.

² As of December 8, 2010, there are 18 publications in this series. Not all publications will be relevant for NPOs (e.g. Oil and Gas) but quite a few are relevant (e.g. Employee Future Benefits, Hedging etc.).

³ <http://www.bdo.ca/library/publications/ifrs/ifrs-CanadianGAAP.cfm>

⁴ <http://www.bdo.ca/library/publications/assuranceandaccounting/documents/filling-the-GAAP-new-standards-for-private-companies.pdf>

Government Not-for-Profit Organizations

Government Not-for-Profit Organizations (GNPOs) will be required to transition to the Public Sector Accounting Handbook. Their reason for this move is that PSAB believes GNPOs are better served by using public sector reporting standards because the focus of operations for these government organizations is on the provision of public services. They are accountable to a broad group of users including legislators, investors and the general public and, in many provinces, these government organizations disburse a majority of the service delivery expenditures.

GNPOs, will have a choice as to whether or not they want to adopt the Public Sector 4200 Series of NPO-Specific Standards. These Standards are the former 4400 series of NPO-specific standards with a few minor changes.

What are the Differences between Current Canadian Accounting Standards and PSAB?

The Canadian Institute of Chartered Accountants recently released a publication comparing Public Sector Accounting Standards to current Canadian accounting standards; for the publication please look [here](#)⁵. There are fewer standards in the Public Sector Accounting Handbook; for example, there is no asset retirement obligation standard. Some of the changes for GNPOs that move to the Public Sector Handbook, regardless of whether your NPO chooses to apply the 4200 series or not, are as follows:

- A model for accounting for financial instruments is expected to be introduced into the Public Sector Handbook in early 2011. Fair value accounting would be required for equities quoted in an active market and derivatives; under certain conditions, NPOs would be allowed to designate certain financial instruments to be accounted for at fair value. Also, the standards would remove any hedging accounting rules and change the requirements for foreign exchange gains and losses. There would also be a new statement called the statement of remeasurement gains and losses. The statement of remeasurement gains and losses would report:
 - a. Unrealized gains and losses associated with financial instruments in the fair value category;
 - b. Amounts reclassified to the statement of operations upon derecognition or settlement; and
 - c. Other comprehensive income reported when a government includes the results of government business enterprises and partnerships in the government's summary financial statements⁶.
- NPO would have to make adjustments to their employee future benefits accounting policies. Public Sector standards require the use of a different discount rate, a different method of accounting for actuarial gains and losses, past service costs and curtailments, and recording of a liability for benefits that accumulate but do not vest; and
- GNPOs will have to move to the modified equity method from the equity method, if they previously used the equity method to account for any of their controlled / related entities. Under the modified equity method, the investee's accounting principles are not adjusted to conform to those of the investor. Application of the modified equity method will avoid the need to restate the figures of the investee when its basis of GAAP is other than the Public Sector Handbook.

If My GNPO Chooses NOT to Apply the 4200 Series of NPO Standards, What Else Will Be Different?

In addition to the changes listed in the previous section, your GNPO should also note the following differences from current Canadian accounting standards if they choose to adopt PSAB without the 4200 series:

- NPOs can no longer use the fund method of presenting their financial statements. PSAB financial statements look quite different from what NPO financial statement users are used to seeing. For an example financial statement, see Appendix B.
- One of the biggest changes occurs in accounting for capital contributions. Under current NPO standards, capital contributions are deferred and amortized to revenue on the same basis as the related capital asset (or in the case of land, put directly to retained earnings). Under the most recent PSAB Exposure Draft, capital contributions would be recognized as revenue once the contribution is authorized and the NPO meets all eligibility criteria. In most cases, this would mean that once the capital asset was purchased or built, all criteria would be met and the GNPO would have to recognize the revenue. This change in accounting could mean huge swings in surpluses from year to year that would have to be explained to users of the financial statements because in the year a large capital contribution was received and the item was purchased or built, the entire amount would most likely be recognized as revenue.

⁵ <http://www.psab-ccsp.ca/documents/item36400.pdf>

⁶ As at November 15, 2010, PSAB is reviewing responses to its Exposure Drafts on Financial Instruments and Foreign Currency Translation which, if approved, would be effective for fiscal years beginning on or after April 1, 2012 (early adoption would be allowed).

- All intangible assets, including those that have been purchased, developed, constructed or inherited, are not recognized as assets. For example, if a research NPO developed a patent, it would not recognize the asset.
- Previously, NPOs had the choice of whether they wanted to recognize their collections⁷ as assets on their books. Under PSAB, works of art and historical treasures⁸ are not recognized as tangible capital assets.

Effective Date

All NPOs would transition to their new standards for year ends beginning on or after January 1, 2012. Early adoption is allowed.

Transitional Guidance

No matter what GAAP your NPO will generally follow, the adoption of any of these new standards will require retrospective / retroactive treatment; in other words, prior years' figures will have to be restated as if the Handbook had always been applied. The good news is IFRS, ASNPO and Public Sector Accounting Standards have first-time adoption standards that provide relief to entities that elect specific exemptions on the initial adoption of their new GAAP⁹.

Conclusion

Changes are coming for all NPOs. Whether you are an NPO or a GNPO you will have decisions to make. If you are interested in further information on how these changes may affect your organization, contact your BDO advisor.

⁷ Under the 4200 series, collections are defined as works of art, historical treasures or similar assets held for public exhibition, education or research that are held for public exhibition, education or research, protected and are preserved and subject to an organizational policy that requires any proceeds from their sale to be used to acquire other items to be added to the collection or for the direct care of the existing collection.

⁸ Works of art, historical treasures are defined under PSAB as items that have cultural, aesthetic or historical value that is worth preserving perpetually

⁹ For IFRS, it is Standards IFRS 1 – First-time Adoption of International Financial Reporting Standards; for ASNPOs, it is Section 1501 – First-time Adoption; for PSAB, it is Section 2125 - First-time Adoption by Government Organizations.

The information in this publication is current as of December 3, 2010.

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Appendix A

List of Current 4400 Series of Standards Specifically for Not-For-Profit Organizations

Section 4400 - Financial Statement Presentation by Not-for-Profit Organizations

Section 4410 – Contributions — Revenue Recognition

Section 4420 - Contributions Receivable

Section 4430 - Capital Assets Held by Not-for-Profit Organizations

Section 4440 - Collections Held by Not-for-Profit Organizations

Section 4450 - Reporting Controlled and Related Entities by Not-for-Profit Organizations

Section 4460 - Disclosure of Related Party Transactions by Not-for-Profit Organizations

Section 4470 - Disclosure of Allocated Expenses by Not-for-Profit Organizations

Appendix BSample Not-for-Profit Public Sector Accounting Financial Statements (electing not to follow 4200 series of NPO-specific standards)¹

December 31	Government NPO	
	Consolidated Statement of Financial Position	
	20X9	20X8
	('000's)	('000's)
Financial assets		
Cash and cash equivalents	\$ 1,577	\$ 1,366
Grants receivable	1,864	1,708
Portfolio investments (Note 1)	7,031	6,932
Business enterprise equity (Note 2)	331	207
Inventories for resale	109	135
	10,912	10,348
Liabilities		
Accounts payable and accrued liabilities	2,383	2,644
Debt (Note 3)	9,363	9,796
Pensions and other employee benefits (Note 4)	4,813	4,890
Other accrued liabilities	1,703	1,841
	18,262	19,171
Net financial assets (debt)	(7,350)	(8,823)
Non-financial assets (Note 5)		
Tangible capital assets (Note 6)	87,218	97,215
Inventories of supplies	112	222
Prepaid expenses	30	20
	87,360	97,457
Accumulated surplus (Note 7)	\$ 80,010	\$ 88,634

¹These financial statements are based on the Illustrative Financial Statements in Appendix B, Section 1200 Financial Statement Presentation

Appendix B

Sample Not-for-Profit Public Sector Accounting Financial Statements (electing not to follow 4200 series of NPO-specific standards)

Government NPO			
Consolidated Statement of Operations			
For the year ended December 31	20X9	20X9	20X8
	Budget	Actual	
	('000s)	('000s)	('000s)
Revenues			
Donations	\$ 9,756	\$ 10,448	\$ 11,151
Government grants	3,962	4,397	4,457
Investment income	409	610	747
Income from business enterprises	50	525	97
Miscellaneous	100	342	402
	14,277	16,322	16,854
Expenses			
Education	4,329	4,061	3,938
Fundraising	8,541	8,626	8,457
Research	7,360	7,557	7,449
General support	4,019	4,702	4,459
	24,249	24,946	24,303
Annual deficit	(9,972)	(8,624)	(7,449)
Accumulated surplus, beginning of year	88,634	88,634	96,083
Accumulated surplus, end of year	\$ 78,662	\$ 80,010	\$ 88,634

Appendix B

Sample Not-for-Profit Public Sector Accounting Financial Statements (electing not to follow 4200 series of NPO-specific standards)

Government NPO			
Consolidated Statement of Change in Net Debt			
For the year ended December 31	20X9	20X9	20X8
	Budget	Actual	
	('000s)	('000s)	('000s)
Revenues			
Annual deficit	\$ (9,972)	\$ (8,624)	\$ (7,449)
Acquisition of tangible capital assets	(294)	(294)	(250)
Amortization of tangible capital assets	10,000	10,226	10,230
(Gain) / loss on sale of tangible capital assets	-	(5)	(19)
Proceeds on sale of tangible capital assets	-	46	72
Write-downs of tangible capital assets	-	24	44
	(266)	1,373	2,628
Acquisition of supplies inventories	-	-	(324)
Acquisition of prepaid expense	-	(30)	(20)
Consumption of supplies inventories	-	110	102
Use of prepaid expense	-	20	
	-	100	(242)
Change in net financial assets / net debt	(266)	1,473	2,386
Net financial assets (net debt), beginning of year	(8,823)	(8,823)	(11,209)
Net financial assets (net debt), end of year	\$ (9,089)	\$ (7,350)	\$ (8,823)

Appendix B

Sample Not-for-Profit Public Sector Accounting Financial Statements (electing not to follow 4200 series of NPO-specific standards)

Government NPO		
Consolidated Statement of Cash Flow		
For the year ended December 31	20X9	20X8
	Actual	
	('000s)	('000s)
Cash provided by (used in) operating transactions		
Annual deficit	\$ (8,624)	\$ (7,449)
Non-cash items including amortization	10,504	10,522
Prepaid expenses	(30)	(20)
Other	(842)	93
	<u>1,008</u>	<u>3,146</u>
Cash provided by (used in) capital transactions		
Proceeds on sale of tangible capital assets	46	72
Cash used to acquire tangible capital assets	(294)	(250)
	<u>(248)</u>	<u>(178)</u>
Cash provided by (used in) investing transactions		
Proceeds from portfolio investments	1,030	4,126
Portfolio investments	(1,129)	(4,369)
Other	(17)	(15)
	<u>(116)</u>	<u>(258)</u>
Financing transactions		
Proceeds from debt issues	13,970	3,694
Debt repayment	(14,403)	(6,175)
	<u>(433)</u>	<u>(2,481)</u>
Increase in cash and cash equivalents	211	229
Cash and cash equivalents, beginning of year	<u>1,366</u>	<u>1,137</u>
Cash and cash equivalents, end of year	<u>\$ 1,577</u>	<u>\$ 1,366</u>