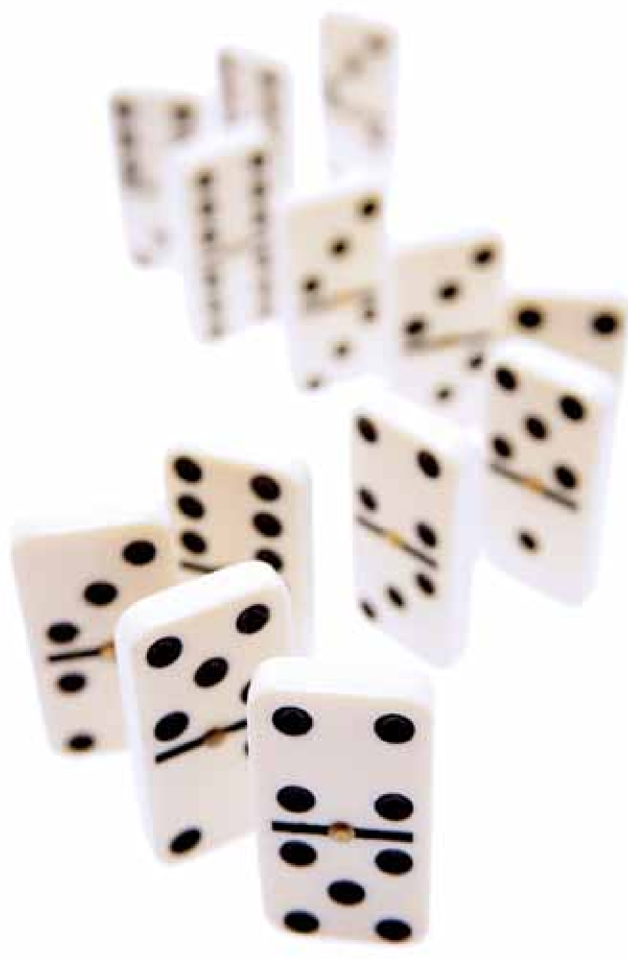


Managing the transition

A new accounting framework for Not-for-Profit Organizations in the private sector

Contents

Introduction

The accounting framework followed by Not-for-Profit Organizations (NPOs) in the private sector is in transition.

In September 2010, the Accounting Standards Board (AcSB) approved the following accounting framework **choices** for NPOs in the private sector:

1. The current accounting standards for Not-for-Profit Organizations – the "4400 series of standards" (with minor modifications) **with** Accounting Standards for Private Enterprises (ASPE) as the underlying accounting framework (ASPE + NPO), **or**
2. International Financial Reporting Standards (IFRSs).

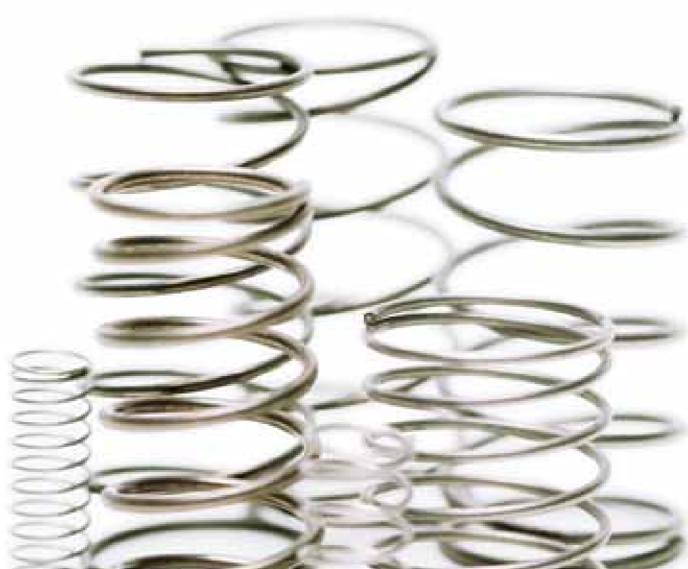
NPOs in the private sector will be required to adopt these standards for fiscal periods beginning on or after January 1, 2012, although earlier adoption is permitted.

The 4400 series of standards will be available in Part III of the CICA Handbook. To the extent that accounting topics are not covered by Part III, an NPO following ASPE + NPO will look to the guidance for ASPEs in Part II of the CICA Handbook.

Adopting a new underlying accounting framework will involve making more than just accounting standard changes. Most organizations will also need to make information system changes, provide training for staff, communicate with stakeholders, coordinate their activities with donors and review contractual and other agreements. Organizations need to design and implement a transition plan that addresses all of the financial, operational, legal and other considerations associated with the change in their underlying accounting framework.

This publication describes some of the issues for an NPO to address when planning its transition, including:

- Confirmation that the organization is an NPO in the private sector, as opposed to a government Not-for-Profit Organization (GNFPO)
- Evaluation of the accounting framework decision to select ASPE + NPO or IFRSs
- Reporting and operational considerations associated with adopting a new accounting framework
- The new Part III of the CICA Handbook
- An overview of the differences between current Canadian GAAP for NPOs and ASPE + NPO
- A road map for converting to ASPE + NPO or IFRSs
- Conversion issues for audit committees to consider



NPOs in the private sector versus GNFPOs

The first step in transitioning to the appropriate accounting framework is to ensure that your organization is in the correct NPO category. Government Not-for-Profit Organizations (GNFPOs) do not fall within the scope of the AcSB and are transitioning to Public Sector Accounting (PSA) Standards. If your NPO is controlled by government, or it is unclear whether your organization is controlled by government, please refer to Deloitte's publication entitled "Managing the transition- A new accounting framework for government Not-for-Profit Organizations" which can be obtained from your local Deloitte contact.

NPOs are defined in the CICA Handbook – Accounting as entities, "normally without transferable ownership interests, organized and operated exclusively for social, educational, professional, religious, health, charitable or any other Not-for-Profit purpose. A Not-for-Profit Organization's members, contributors and other resource providers do not, in such capacity, receive any financial return directly from the organization."

The differences in the accounting framework choices for GNFPOs as compared to NPOs in the private sector are as follows:

Accounting Framework Alternatives	NPOs in the private sector	GNFPOs
Adopt Accounting Standards for Private Enterprises, including guidance from current 4400 series of standards for Not-for-Profit Organizations (ASPE + NPO)	✓	✗
Adopt International Financial Reporting Standards (IFRSs) (not supplemented by the 4400 series of standards)	✓	✗
Adopt PSA Standards, including guidance from current 4400 series of standards for Not-for-Profit Organizations	✗	✓
Adopt PSA Standards, excluding guidance from current 4400 series of standards for Not-for-Profit Organizations	✗	✓

Given the potentially significant differences that could result from application of a different accounting framework, organizations who currently classify themselves as non-government controlled NPOs, or NPOs in the private sector, are advised to confirm that they do not meet the criteria of a GNFPO.

Understanding the accounting framework decision of ASPE + NPO or IFRSs

The choice between ASPE supplemented with the 4400 series of standards and IFRSs could seem like an easy decision at first. The choice seems easy for most organizations because IFRSs do not, and are not expected to add an equivalent to the 4400 series of standards for NPOs. However, before a decision is made, organizations should ask themselves the following questions:

	Questions	Further Discussion Points
Users of financial statements	Who are the users of the financial statements? Are they used to one accounting framework, or do they prefer a certain set of standards?	Foreign stakeholders of NPOs based in Canada may be more familiar with IFRSs.
Comparability in the global market	Does your NPO currently receive, or expect to receive, significant contributions from outside of Canada?	For some organizations, contributions from foreign donors (or through programs that are run in foreign countries) are significant. Some NPOs may find it easier to compete with other not-profit- organizations which provide financial information to foreign stakeholders under IFRSs.
Financing	Does your NPO currently receive (or plan to receive) financing from a lending institution that would expect financial statements prepared in accordance with IFRSs?	Foreign lending agreements are not typical for NPOs in Canada. However, an NPO whose head office is in Canada may have subsidiaries or chapters throughout the world where financing is obtained locally. If those financing agreements rely on consolidated financial statements, consolidated financial statements in accordance with IFRSs may be necessary.
Composition of organization	Is your NPO consolidated with foreign subsidiaries or chapters?	If all foreign subsidiaries or chapters are familiar with IFRSs and can easily report under those standards, it may be more efficient for the Canadian NPO to implement IFRSs, rather than requiring the other organizations to adopt standards that they may be unfamiliar with.
Significant related parties	Does your NPO have a significant relationship with (or is it managed by) an entity that is required to adopt IFRSs?	Many commercial companies have NPOs to coordinate their efforts to give back to the community. If the related commercial organization provides significant management and accounting support to the NPO, it may be more efficient to adopt the same set of standards that the commercial company uses. This may reduce training costs, information system costs, and provide more support to the NPO.

If you would like more information on IFRSs, please refer speak to your local Deloitte contact.

Reporting and operational considerations

Moving to a new accounting framework involves more than just identifying and quantifying the required accounting standard changes. Adopting a new accounting framework may also create a variety of reporting and operational issues that will need to be addressed. A summary of some of these challenges, and suggested strategies to mitigate them, is presented below.

	Challenge	Mitigating strategy
Relationships with stakeholders	Financial statements prepared under different accounting frameworks may present a challenge to stakeholders such as donors in assessing and comparing the performance of various NPOs in making a donation decision.	Timely consultations with all relevant stakeholders will help ensure that all of the potential impacts associated with the choice of accounting framework are identified and addressed appropriately.
Financial indicators	Changing accounting frameworks may affect the organization's key financial indicators and donor agreements.	The impacts on financial indicators and donor agreements should be assessed regularly throughout the conversion process. In some instances, exemptions may be appropriate in transitioning to new accounting standards.
Legal	A change in the organization's accounting framework may affect certain donation agreements and, therefore, contracts will need to be examined to fully understand any accounting implications.	Organizations should review and analyze the contractual underpinnings to their relationships to determine the appropriate accounting treatment for them.
Human resources	Activities required to plan and carry out the conversion to the new accounting framework will place increased demands on finance and other personnel.	The additional demands placed on key personnel may be reduced when personnel are provided with appropriate training programs and a rigorous project management and a comprehensive scoping exercise are utilized to manage the transition activities.

Part III of the CICA Handbook – Accounting

As previously noted, the existing 4400 series of standards for Not-for-Profit Organizations will be moved to a new section of the Handbook – Part III, entitled Accounting Standards for Not-for-Profit Organizations.

Part III will include the existing 4400 series of standards as well as:

- An Introduction to Part III that describes the accounting framework choices
- The following new sections, which are based on the equivalent sections from Part II of the Handbook – Accounting Standards for Private Enterprises, and have been tailored for NPOs:
  - Section 1001, Financial Statement Concepts for Not-for-Profit Organizations;
  - Section 1101, Generally Accepted Accounting Principles for Not-for-Profit Organizations;
  - Section 1401, General Standards of Financial Statement Presentation for Not-for-Profit Organizations; and
  - Section 1501, First-time Adoption by Not-for-Profit Organizations;

- Section 3032, inventories held by Not-for-Profit Organizations, which provides additional guidance on recognition and measurement issues specific to NPOs. Section 3032 of Part III supplements Section 3031 of Part II.

The AcSB concluded that having all sections that relate specifically to NPOs in one place will assist preparers, auditors and users of financial statements.

As previously noted, the existing 4400 series of standards for Not-for-Profit Organizations will be moved to a new section of the Handbook – Part III, entitled Accounting Standards for Not-for-Profit Organizations.

Differences between current Canadian GAAP for NPOs and ASPE + NPO

As previously noted, the AcSB has provided a choice of accounting frameworks for NPOs in the private sector. If your NPO has decided to adopt IFRSs, please speak to your local Deloitte contact to obtain additional information on IFRSs.

For the other NPOs who decide to continue to apply the 4400 series of standards, using ASPE as the underlying accounting framework, this section highlights some of the potentially significant differences between current Canadian GAAP (Part V of the CICA Handbook) and ASPE for those areas not covered by the 4400 series of standards.

Topic	Current Canadian GAAP – Part V	Accounting Standards for Private Enterprises (ASPE) – Part II
Financial instruments	Organizations are required to classify financial instruments into one of four categories, and this classification determines the subsequent measurement. Investments are typically carried at fair value, with immediate recognition of any changes in fair value, either in the Statement of Operations or in the Statement of Net Assets.	Financial assets and liabilities are measured at amortized cost, with the exception of derivatives, equities quoted in active markets, and indexed liabilities, which would be measured at fair value. A fair value option would be available for any instrument, upon an irrevocable designation made on initial recognition. An impairment loss is measured as the difference between the current carrying amount of the asset and the highest of the amount the entity expects to collect through the present value of future cash flows, the sale of the financial asset on the balance sheet date and collection of collateral.
Employee future benefits	Organizations use an actuarial report prepared specifically for accounting purposes to determine the accrued benefit obligation. Actuarial gains and losses are recognized in net income either on a deferred basis, with the minimum amount recognized computed using the “corridor” approach, or immediately. Past service costs are recognized on a deferred basis.	ASPE allows for a simplified accounting policy choice that would allow actuarial valuations used for funding purposes to be used to measure obligations. If the simplified approach is followed, all actuarial gains and losses and past service costs would be recognized into income as they are incurred. If the simplified accounting policy option is not selected, then the standards under current Canadian GAAP would be followed.

Differences between current Canadian GAAP for NPOs and ASPE + NPO (Cont'd)

Topic	Current Canadian GAAP – Part V	Accounting Standards for Private Enterprises (ASPE) – Part II
Intangible assets (including items sometimes referred to as deferred costs)	Currently, Section 3064, Goodwill and Intangible Assets, in Part V (current Canadian GAAP) provides a scope exclusion for NPOs. Given the minimal guidance in CICA 4430 on intangibles, some NPOs may currently consider this guidance when assessing whether certain items should be capitalized. Following Section 3064 would tend to limit an NPO's ability to capitalize items such as advertising and fund raising costs.	NPOs will follow Section 3064 in Part II (ASPE Standards) which does not exclude NPOs from its scope. Development costs, selling, advertising, administration and other overhead expenditures related to series of live performances, exhibitions or fund raising efforts will be subject to the guidance in Section 3064.
Disclosure of government remittances	Not required.	Organizations are required to disclose the amount payable at the end of the period in respect of government remittances such payroll taxes, health taxes, and sales taxes.
Asset retirement obligations (AROs)	AROs are currently measured at fair value.	AROs will be measured at the best estimate of the amount required to settle the obligation at each balance sheet date, where best estimate would be based on management's experience and judgment, considering probabilities of possible outcomes and the time value of money.

The AcSB has provided a choice of accounting frameworks for NPOs in the private sector. If your NPO has decided to adopt IFRSs, please speak to your local Deloitte contact to obtain additional information on IFRSs.

Transition to ASPE + NPO

First-time Adoption by Not-for-Profit Organizations, Section 1501, applies to the first financial statements prepared in accordance with the new accounting framework of the 4400 series of standards with ASPE as the underlying accounting framework. Some of the key provisions of that standard are:

Issue	Guidance
Transition	Retroactive application with restatement of prior periods, subject to the exemptions provided.
Exemptions	The guidance provides specific optional exemptions to retroactively restating prior periods in the following areas: a. Business combinations b. Fair value for capital assets c. Employee future benefits (The AcSB has recently published an ED to provide an additional alternative to further simplify the transition regarding employee future benefits) d. Cumulative translation differences e. Financial instruments f. Asset retirement obligations
Exceptions	The guidance prohibits retroactive application on: a. Derecognition of financial assets and financial liabilities b. Some aspects of hedge accounting c. Accounting estimates d. Non-controlling interests
Disclosure	The guidance requires additional disclosure in the year of transition to enable the reader to understand the material adjustments made to the financial statements as a result of the transition to the new accounting framework.

First-time Adoption by Not-for-Profit Organizations, Section 1501, applies to the first financial statements prepared in accordance with the new accounting framework of the 4400 series of standards with ASPE as the underlying accounting framework.

Timeline – First time adoption by NPOs with a March year-end

April 1, 2011 – Date of transition to ASPE + NPO or IFRSs

Opening statement of financial position date.

Beginning of first year of full comparative financial statements in accordance with ASPE + NPO or IFRSs.

April 1, 2012 – Date of conversion

External reporting commences under ASPE + NPO or IFRSs with restated comparative financial statements.

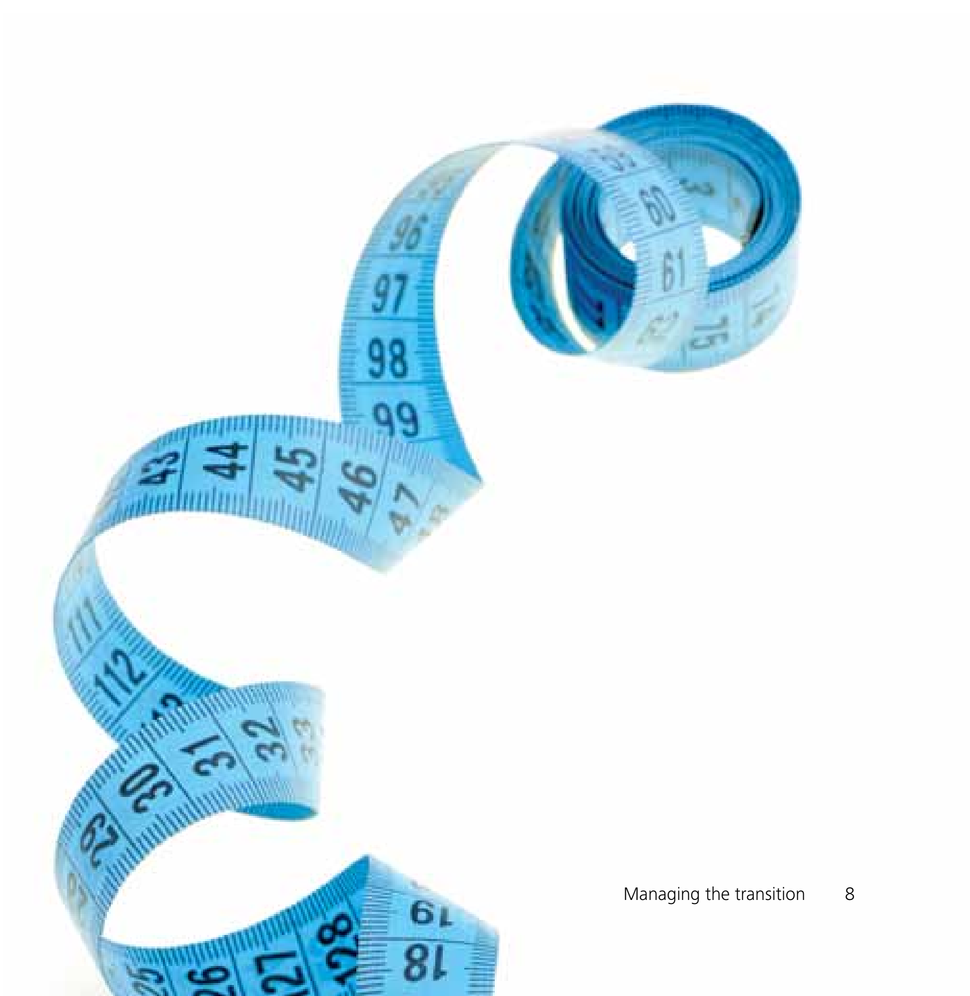
April 1, 2011 — March 31, 2012 — April 1, 2012 — March 31, 2013

March 31, 2012

Last audited financial statements prepared in accordance with current Canadian GAAP.

March 31, 2013

First audited financial statements under ASPE + NPO or IFRSs with restated comparative balances.



Approach to transition

The transition to a new accounting framework is a complex process that must be managed efficiently. NPOs may wish to utilize the following three-phase approach to manage their conversion to a new accounting framework.

	Phase 1 – Planning	Phase 2 – Detailed diagnostic	Phase 3 – Implement
Objective	• Identify the high-level differences between IFRSs, 4400 series of standards plus ASPE and Canadian GAAP. • Develop a project plan and identify the required resourcing.	• Evaluate the financial impacts of various options and methodologies provided under the new accounting framework. • Evaluate the financial impacts of various options under alternative methodologies.	• Build, implement and communicate the changes required to report information which is compatible with the new accounting framework.
Activities	• Identify the accounting standards that are most significant to the NPO. • Identify the major differences between IFRSs, 4400 series of standards plus ASPE and Canadian GAAP. • Determine the impacts on financial reporting.	• Identify and design operational and financial processes. • Develop required solutions to address identified issues. • Perform a detailed analysis on the work streams identified in the project plan.	• Implement changes to operational and financial processes. • Develop internal communications to promote consistent understanding, education and resolution of critical issues. • Develop external communications to ensure that stakeholders and governments understand changes in financial reporting.
Outcomes and deliverables	• Develop a "heat map" that highlights, by standard and by financial statement line item, the financial impact and complexity of transitioning to IFRSs or 4400 series of standards plus ASPE.	• Develop position papers for each significant area that analyze the current accounting and conclude on the appropriate future accounting treatment.	• Facilitate a knowledge transfer within the organization. • Prepare financial statements in accordance with the new accounting framework. • Implement ancillary changes (e.g. processes and controls) to meet the new accounting requirements.

Issue for audit committees to consider

NPO audit committees are actively involved in the oversight of their organization's accounting frameworks and financial reporting, and they should play an integral role in their organization's consideration of and transition to a new accounting framework. Some questions that audit committees may ask as part of their oversight of this process are presented below.

1. Has the organization decided on whether it will transition to IFRSs or the 4400 series of standards plus ASPE?

2. What are the most significant impacts on the financial statements?

3. What are the costs of the transition?

4. What are the ancillary impacts of the transition (i.e. reporting to funders or controls and processes)?

5. Have we vetted our positions externally?

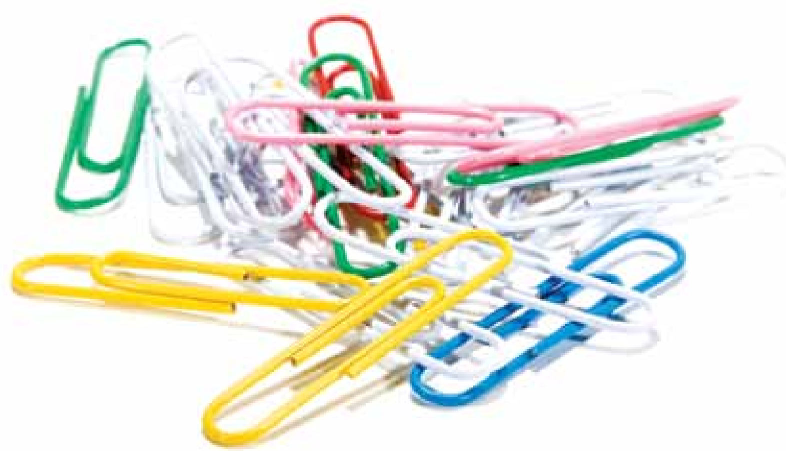
6. Has management prepared a work plan for the transition?

7. Do we require training on IFRSs or ASPE?

8. What are our opportunities and risks in this project?

9. What is the impact on our reporting to our donors?

10. Do we have the internal expertise to carry out this work?



Conclusion

Deloitte serves numerous NPOs across Canada. As a multidisciplinary organization, our comprehensive range of services related to NPO accounting goes beyond just addressing the financial issues associated with adopting new accounting standards. Deloitte also provides assistance with project management, human resources and training, information systems development, stakeholder communications and more.

To discuss your organization's needs, the potential impacts on your financial reporting, and develop a transition strategy, please contact one of our leaders.

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