

ASNPO Alert

ACCOUNTING STANDARDS FOR NOT-FOR-PROFIT ORGANIZATIONS

AUGUST 2020

Assessing Potential COVID-19 Impacts on Financial Statements: Questions and Considerations under ASNPO

This *CPA Canada Alert (Alert)* provides questions to ask and other considerations for financial statement preparers and practitioners under various sections of Parts II and III of the *CPA Canada Handbook – Accounting (Handbook)*¹ to identify potential impacts on financial statements of not-for-profit organizations (NFPOs) resulting from the COVID-19 pandemic. The issues in this *Alert* will primarily relate to NFPOs with year-ends subsequent to January 2020, however, the timing, nature and extent of the issues will vary depending on the facts and circumstances specific to each NFPO.² Reference should be made to the applicable sections under Accounting Standards for Not-for-Profit Organizations (ASNPO) and Accounting Standards for Private Enterprises (ASPE) when assessing various COVID-19 accounting issues.

1 A not-for-profit organization applying Part III of the *Handbook* also applies the standards for private enterprises in Part II of the *Handbook* to the extent that the Part II standards address topics not addressed in Part III.

2 Although COVID-19 was reported in China before December 31, 2019, there were few reported impacts in Canada at that date, and the World Health Organization did not declare a public health emergency until January 2020.

GOING CONCERN

Section 1401, *General Standards of Financial Statement Presentation for Not-for-Profit Organizations*

COVID-19 may raise questions, such as:

- Does the NFPO continue to meet the criteria in Section 1401 for financial statements to be prepared on a going concern basis? This assessment includes careful analysis of the impact of events that occur between the year-end date and the date of completion of the financial statements.
- Are there material uncertainties related to events or conditions that may cast significant doubt upon the NFPO's ability to continue as a going concern? If so, such uncertainties should be disclosed.

A more detailed discussion about applying the going concern guidance in Section 1401 can be found in the CPA Canada [ASNPO Alert – Assessing COVID-19 Effects on Financial Statements: Subsequent events and other considerations](#).

SUBSEQUENT EVENTS

Section 3820, *Subsequent Events*

Section 3820 identifies two types of subsequent events:

- a. those that provide further evidence of conditions that existed at the financial statement date; and
- b. those that are indicative of conditions that arose subsequent to the financial statement date.

The first type of subsequent event requires adjustment to the financial statements. For example, if between the date of the financial statements and the date of completion of the financial statements it becomes evident that an asset was impaired at the date of the financial statements, that impairment should be recorded in the statement of operations and statement of financial position.

The second type of subsequent event is disclosed in the notes to the financial statements, but is not recorded in the statement of operations or statement of financial position.

A more detailed discussion on applying the subsequent events guidance in Section 3820, including considerations for financial statements with periods ending in 2019 and 2020, can be found in the CPA Canada [ASNPO Alert – Assessing COVID-19 Effects on Financial Statements: Subsequent events and other considerations](#).

IMPAIRMENT OF ASSETS OTHER THAN FINANCIAL INSTRUMENTS

The financial performance of NFPOs may be significantly affected by COVID-19 and related government measures. This may raise impairment concerns for various assets held by a NFPO including property, plant and equipment, intangible assets, interests in other entities, inventories and other assets.

Capital Assets

Section 4433, Tangible Capital Assets Held by Not-for-profit Organizations; Section 4434, Intangible Assets Held by Not-for-profit Organizations and Section 4441, Collections Held by Not-for-profit Organizations

Section 4433 states that a capital asset may be impaired when conditions indicate that it no longer contributes to an organization's ability to provide goods and services, or that the value of future economic benefits or service potential associated with the capital asset is less than its net carrying amount. Impaired capital assets are written down to either fair value or replacement cost (a choice can be made on an asset-by-asset basis). The same rules apply for intangible assets held by NPFOs, in accordance with Section 4434.

Section 4441 states that a collection or collection item that is recorded in the statement of financial position at cost is written down whenever events or changes in circumstances indicate that its net carrying amount may exceed its fair value. An impaired collection or collection item is written down to its fair value or replacement cost. A NFPO may choose fair value or replacement cost on an item-by-item basis.

COVID-19 may raise questions, such as:

- Are some capital assets no longer in use due to COVID-19? Have certain operations of the NFPO closed down, either temporarily or permanently?
- Has the provision of some or all of the NFPO's services dropped significantly (e.g., due to government regulations, employee availability, reduced demand, etc.)?
- Is the useful life of any asset likely to be shortened as a result of COVID-19? For example, a license for a limited period may be impaired if the NFPO's operations are shut down or reduced for a period of time.
- Has there been a significant decrease in the market price of a capital asset?
- Is it more likely than not that a capital asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life?

The above are examples of indicators of impairment and are not meant to be an exhaustive list. Judgment will need to be exercised when assessing the expected significance and duration of COVID-19 impacts and related government measures on the NFPO, and when evaluating how quickly the NFPO is expected to recover. A short-term reduction in cash flows followed by a rapid return might not be significant enough to be considered an indicator of impairment for some

NFPOs. For others, even a relatively short disruption due to COVID-19 may affect recoverability of carrying amounts of certain assets.

When a capital asset's carrying amount is written down, a corresponding amount of any unamortized deferred capital contributions related to the tangible capital asset is recognized as revenue, provided that all restrictions have been complied with. An impairment loss on a capital asset cannot be reversed in future periods.

Controlled Entities

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

A NFPO can make an accounting policy choice to account for joint ventures or controlled for-profit enterprises using the equity method. A NFPO is required to use the equity method to account for for-profit enterprises over which the NFPO can exercise significant influence³.

Entities accounted for using the equity method are required to be assessed for impairment by the NFPO at the end of each reporting period in accordance with Section 3051, *Investments*. COVID-19 may raise questions about equity accounted entities, such as:

- Has the sector or region that the entity or its customers operate in faced significant negative impacts due to COVID-19?
- Does the entity have (or is it expected to have) significant reductions in cash flows?
- Does the entity have sufficient financing available, including lines of credit?
- Has the entity breached debt covenants, or is it likely to do so in the future?
- Does the entity have any obligations that may be onerous, including guarantees, in respect of third parties?
- Has the market for the entity's products or services been significantly reduced?
- Does the entity face supply chain difficulties or other factors that are likely to reduce output below normal levels?

The above are examples of impairment considerations and are not meant to be an exhaustive list. As discussed above, judgment is required when evaluating how long COVID-19 and related government measures will affect the investee and how quickly the investee will recover.

³ Joint ventures may also be accounted for by proportionate consolidation and controlled for-profit enterprises may be accounted for by consolidation. Controlled NFPOs are either consolidated or reported by making the disclosures required by Section 4450. Significantly influenced NFPOs are reported by making the disclosures required by Section 4450. Where consolidation or proportionate consolidation is used, the assets of the controlled entity are tested for impairment in accordance with Sections 4433, 4434 and 4441.

Inventory

Section 3032, *Inventories Held by Not-for-profit Organizations* and Section 3031, *Inventories*

Inventories may be held by a NFPO for:

- a. distribution at no charge or for a nominal charge; or
- b. consumption in the production process of goods to be distributed at no charge or for a nominal charge.

Such inventory is measured at the lower of cost and current replacement cost in accordance with Section 3032 in Part III of the *Handbook*. Questions to ask may include:

- Has the price at which the inventory items can be purchased by the NFPO dropped because COVID-19 has resulted in lower demand?
- Will the items still be (i) distributed or (ii) consumed in the production of goods to be distributed at no charge?

Some NFPOs hold inventory for sale as part of their day-to-day activities. For example, a museum may have a gift shop, a religious institution may sell prayer books and other religious items or a golf club may sell golf balls and tees. Such inventory is measured at the lower of cost and net realizable value in accordance with Section 3031 in Part II of the *Handbook*. COVID-19 may cause the net realizable value of certain inventories to decrease below cost. Questions to ask may include:

- Has the market price or demand for the inventory decreased?
- Can inventory items with a limited life be sold in a timely manner? Will these inventories have to be discounted?
- Were some orders cancelled? Will it be feasible to sell these items to another customer?
- If demand has decreased and inventory will have to be held for an extensive period, are there significant holding costs (e.g., warehousing)?

Prepaid Expenses and Other Assets

Prepaid amounts or other assets may no longer meet the criteria for recognition as an asset under Section 1001, *Financial Statement Concepts for Not-for-profit Organizations*. Alternatively, the carrying amount of certain assets may need to be reduced. Questions to ask when reviewing prepaid amounts and other assets may include:

- Do prepaid rent amounts for new premises that are unlikely to be occupied as a result of COVID-19 need to be adjusted?
- Do prepaid travel amounts for employees or volunteers who will no longer be travelling as a result of COVID-19 need to be adjusted?
- Will prepaid services that are not currently needed or cannot be provided due to COVID-19 be needed and provided at a future date?

- Have deposits been paid for future events (e.g., the NFPO’s annual general meeting, fundraising events or conferences that the NFPO is sponsoring or which staff will be attending) that are unlikely to take place due to COVID-19?

In reviewing such items, NFPOs should take into account whether the vendor is likely to refund some or all of the prepaid amount(s).

OTHER ACCOUNTING ISSUES FOR NON-FINANCIAL ASSETS

Amortization of Capital Assets

Section 3061, *Property, Plant and Equipment* and Section 3064, *Goodwill and Intangible Assets*

Amortization of property, plant and equipment is charged to income based on the greater of:

- a. cost less salvage value over the life of the asset, or
- b. cost less residual value over the useful life of the asset.

Intangible assets (other than those with an indefinite life) are amortized over their useful life.

NFPOs may ask:

- Will the net realizable value of an item of property, plant and equipment, when it is no longer in use and is disposed of, have decreased because of changes in the marketplace for that asset resulting from COVID-19?
- Has COVID-19 affected the remaining useful life of an intangible asset?

If an asset has been written down, the amortization charge related to that asset will need to be recalculated to reflect its new carrying amount. Changes to an asset’s useful life, rate of amortization and/or residual value are considered a change in accounting estimate and accounted for prospectively.

Contingent Assets

Section 3290, *Contingencies*

Section 3290 does not permit the recording of contingent assets or gains. However, it does require disclosure when it is likely that a future event will confirm that an asset had been acquired or a liability reduced at the date of the financial statements.

Questions to ask may include:

- If a contingent gain or asset was disclosed in the prior period, is the “likely” criterion still met?
- Are amounts expected to be received as insurance proceeds (e.g., under business continuity insurance)? If so, they should only be recorded when there is no remaining uncertainty. For insurance proceeds, this is normally when the insurer has approved the claim. If these amounts are not recorded, consideration should be given as to whether they should be disclosed.

LIABILITIES (OTHER THAN FINANCIAL INSTRUMENTS)

COVID-19 and related government measures may affect a NFPO's obligations. Some obligations may not have been previously recorded because the organization considered it unlikely that an amount would have to be paid. Other obligations may have been recorded, but the amount at which the liability should be measured has changed. The following questions include some of the accounting issues related to liabilities that may be asked as a result of COVID-19:

- Have any contracts become onerous, requiring a provision to be recorded? For example:
 - On a revenue contract, has the price been reduced or have costs increased so that a loss is now expected? (e.g., a golf club may have a contract to host a golf tournament and will now incur increased costs or generate lower revenues.)
 - Is there a non-cancellable contract for the purchase of services that will not be required?
 - Is there a non-cancellable contract to purchase goods for use or resale and the retail price has fallen due to reduced demand?
 - Will cancellation fees be incurred in order to cancel onerous contracts?
- Will contract penalties be incurred because the NFPO can no longer meet its obligations under a contract, or does not intend to do so given changing circumstances?
- Are there obligations under guarantees that may have to be met because of defaults by other parties?
- Has the NFPO decided to restructure its operations? Are there liabilities that need to be recorded as a result?
- Do the NFPO's provisions for employee costs need to be adjusted? For example:
 - Does sick pay need to be adjusted to reflect expected time off for employees who have fallen ill?
 - Does vacation pay need to be adjusted to reflect reduced working hours or reduced employee head count?

This is not an exhaustive list. NFPOs should consider whether any additional liabilities have arisen, or if existing liabilities have changed in amount, as a result of COVID-19 or related government measures.

FINANCIAL INSTRUMENTS

Section 3856, *Financial Instruments*

Impairment of Financial Assets

Different types of financial instruments are measured at cost or fair value in accordance with Section 3856. NFPOs should consider whether COVID-19 has resulted in indicators of impairment for financial assets measured at cost or amortized cost. Relevant questions may include:

a. *Receivables*

- Has the debtor indicated it will have difficulty making payments or missed making payments?
- Has the NFPO granted concessions to the debtor?
- Is the debtor in financial difficulty?

b. *Debt and equity instruments of a third party held by the NFPO*

- Has there been a breach of contract, such as default or delinquency in interest or principal payments?
- Have terms of a debt instrument been renegotiated?
- Is the issuer in financial difficulty?
- Is there no longer an active market for the securities of the issuer?

Financial assets measured at fair value (for example, investments in equity instruments quoted in an active market) are remeasured to their fair value at the end of each reporting period.

Financial Liabilities

As a result of COVID-19 and related government measures, a NFPO may need to renegotiate the terms of its debt instruments or other financial liabilities. In accounting for such changes, it is necessary to determine if they are substantial. The terms of a renegotiated financial liability differ substantially from the original liability when:

- a. the present value of the cash flows under the new terms, including any fees paid net of any fees received, differs by at least 10 percent from the present value of the remaining cash flows of the original financial liability, both discounted at the original interest rate; or
- b. there is a change in the creditor and the original debt is legally discharged by the debtor through a cash payment or otherwise.

Relevant questions may include:

- Have debt instruments been replaced by another instrument with substantially different terms (e.g., interest rate or term)? Such changes are accounted for as an extinguishment of the original debt instrument and the recognition of a new debt.
- Have substantial modifications been made to the terms of an existing financial liability (e.g., interest rate or due date)? Such changes are accounted for as an extinguishment of the original financial liability and recognition of a new financial liability.
- Have debt or other covenants been breached (or are they expected to be)? Long-term debt with a measurable covenant violation is classified as a current liability unless:
 - a. the creditor has waived, in writing, or subsequently lost, the right, arising from violation of the covenant at the statement of financial position date, to demand repayment for a period of more than one year from the statement of financial position date; or

- b. the debt agreement contains a grace period during which the debtor may cure the violation and contractual arrangements have been made that ensure the violation will be cured within the grace period;

and a violation of the debt covenant giving the creditor the right to demand repayment at a future compliance date within one year of the statement of financial position date is not likely.

OTHER MATTERS AND ISSUES

Leases

Section 3065, Leases

Lessees and lessors may renegotiate the terms of a lease, for example, to defer or reduce rent payments for a period of time. Questions to ask may include:

- a. *Operating lease*
- Have lease payments been deferred? If so, the lessor records a receivable for the amount deferred each period and the lessee records a liability. The lessor should evaluate whether the amount deferred will be received or if it should be written down.
 - Have lease payments been reduced? Both the lessor and the lessee should record the reduced lease revenue / expense in the periods to which they apply.
- b. *Capital lease - Lessor*
- Has COVID-19 or related government measures impacted the lessee's ability to make lease payments, although the contractual lease terms have not been renegotiated? If so, consideration should be given as to whether there are indicators that the lease is impaired under Section 3065.
 - Has the lessor agreed to defer lease payments? If so, the lessor records a receivable for the amount deferred each period, however, the lessor should evaluate whether the amount deferred will be received or whether it should be written down.
 - Has the lessor agreed to reduce lease payments for a period of time? If so, the lease receivable should be written down to reflect the reduced lease payments.
- c. *Capital lease - Lessee*
- Are there indicators that an asset leased under a capital lease is impaired? The impairment test would be the same as that used for property, plant and equipment (see above).
 - Has the lessor agreed to reduce lease payments for a period of time? If so, the lease liability should be remeasured to reflect the reduced lease payments

Contributions From Donors

Section 4410, Contributions – Revenue Recognition and Section 4420, Contributions Receivable

Donor contributions may be restricted or unrestricted or take the form of endowments.

Questions to ask may include:

- Does the purpose for which restricted contributions were made still exist? For example, will a new program or construction of a new building proceed as planned?
- If an endowment fund exists to fund specific services, will those services continue to be provided?
- Has there been a change in the useful life of a capital asset that was purchased with money from a restricted contribution, resulting in a change in the periodic amortization of the capital asset? If so, the corresponding amount of restricted contribution revenue recognized each period will also need to be revised.
- Is the collection of contributions receivable reasonably assured and can the amounts be reasonably estimated? Consideration should be given to the financial situation of the donors and their ability to fulfill their commitment to the NFPO given the impact of COVID-19.

Government Assistance

Section 4410, Contributions – Revenue Recognition and Section 4420, Contributions Receivable

The Canadian Federal and Provincial governments have announced various forms of assistance to help businesses, NFPOs and individuals through the current pandemic. Government funding provided to a NFPO is considered a contribution (as per Section 4410) and is accounted for using either the deferral method or restricted fund method in accordance with the NFPO's accounting policy choice for contributions.

There may be uncertainty as to whether a NFPO will receive funds under a government program. For example, a NFPO may have applied for assistance but not yet know if its claim will be accepted or rejected. In other cases, a NFPO may intend to apply for assistance under a program that has been announced but has not gone through the required legislative steps to be implemented. In accordance with Section 4420, government assistance should only be recognized if the amount to be received can be reasonably estimated and ultimate collection is reasonably assured. If the available assistance under a government program does not meet this recognition criteria, the NFPO should consider whether note disclosure is appropriate.

A NFPO should ensure there is transparency around government assistance amounts recorded in its financial statements. Consideration should be given to disclosure of amounts received under different programs and any terms or conditions attached to these amounts.

Defined Benefit Plans

Section 3463, Reporting Employee Future Benefits by Not-for-profit Organizations and Section 3462, Employee Future Benefits

COVID-19 may have affected the amount at which a defined benefit asset or liability is measured or whether there is still a defined benefit asset. Questions to ask may include:

- Has the value of the plan assets decreased significantly due to COVID-19 market declines?
- Has there been a curtailment or settlement, or other significant event, requiring a new actuarial valuation of the defined benefit obligation?
- If a new actuarial valuation is not deemed necessary, have changes occurred as a result of COVID-19 that should be factored into the roll-forward estimate of the defined benefit obligation?
- Is a liability required for severance payments?

Disposal of Long-lived Assets and Discontinued Operations

Section 3475, Disposal of Long-lived Assets and Discontinued Operations

NFPOs may decide to dispose of long-lived assets or to discontinue certain operations as a result of COVID-19 and related government measures. The accounting in Section 3475 would apply. Provided the criteria for classification as held for sale are met, the assets or discontinued operations are measured at the lower of carrying amount and fair value less cost to sell. The results of discontinued operations, including any gain or loss, are reported as a separate line in the statement of operations.

Changes in Accounting Policies and Estimates

Section 1506, Accounting Changes

An accounting estimate may need revision if changes occur in the circumstances in which the estimate was based or as a result of new information. Paragraph 1506.19 provides the following examples of estimates:

- a. bad debts;
- b. inventory obsolescence;
- c. the fair value of financial assets or financial liabilities;
- d. the useful lives of, or expected pattern of consumption of the future economic benefits embodied in, depreciable assets; and
- e. warranty obligations.

NFPOs should consider whether any changes in accounting estimates are required as a result of COVID-19.

Fair Presentation and Disclosure

Section 1401, *General Standards of Financial Statement Presentation for Not-for-profit Organizations*

In accordance with Section 1401, fair presentation requires the following:

- a. applying GENERALLY ACCEPTED ACCOUNTING PRINCIPLES FOR NOT-FOR-PROFIT ORGANIZATIONS, Section 1101;
- b. providing sufficient information about transactions or events having an effect on the NFPO's financial position, results of operations and cash flows for the periods presented that are of such size, nature and incidence that their disclosure is necessary to understand that effect; and
- c. providing information in a manner that is clear and understandable.

NFPOs should make a general assessment of fair presentation after the financial statements have been substantially completed. Questions to ask may include:

- Do the financial statements fully reflect the impacts of COVID-19 as at the date of the statements?
- Do the note disclosures provide sufficient information in a clear manner so that the reader can understand the impacts of COVID-19 on the NFPO's financial statements?
- Is there appropriate disclosure of material uncertainties in accordance with Section 1508, *Measurement Uncertainty*?
- Is disclosure of subsequent events complete and clear?

RESOURCES

CPA Canada

[ASNPO Alert – Assessing COVID-19 Effects on Financial Statements: Subsequent events and other considerations](#)

[COVID-19: Resources related to reporting and audit](#)

[COVID-19 Information Resources](#)

[Operating in the Post-Pandemic World: Resources for NFPs](#)

Accounting Standards Board

[COVID-19 News and Resources](#)

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