a state of change

Not-for-profit newsletter | June 2014

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Introduction

In this issue we bring you three articles that highlight three diverse issues impacting not-for-profit organizations. The first article relates to changes in the reporting of employee future benefits by not-for-profit organizations, and provides key questions for Management and Audit Committee members to consider. The second article is of most relevance to Hospitals and their affiliated foundations, and relates to new technical amendments to the Excise Tax Act that may provide exemption from GST/HST with respect to patients and visitors parking. Our final article addresses the Improvements to Not-for-Profit Standards – Statement of Principles ("SOP") issued for comments by the Canadian Accounting Standards Board and the Public Sector Accounting Board. The SOP outlines 15 key principles proposing some significant changes to the future of not-for-profit accounting for organizations in both the private and public sectors. The comment period has now closed. Our article summarizes the common themes of the comments received from respondents.

Reporting employee future benefits by not-for-profit organizations

Overview

The accounting for employee future benefits by not-for-profit organizations is changing with the recent introduction of *Section 3462 Employee Future Benefits* ("Section 3462") in Part II of the CPA Canada Handbook and *Section 3463 Reporting Employee Future Benefits by Not-for-Profit Organizations* ("Section 3463") in Part III of the CPA Canada Handbook.

Effective date and transition

A not-for-profit organization is required to apply both Section 3462 and Section 3463 for fiscal years beginning on or after January 1, 2014. Earlier application is permitted, but only for all of a not-for-profit organization's defined benefit plans. Retrospective application is required subject to the transitional provisions outlined in the Sections.

What are the significant changes introduced by Section 3462?

✓ The deferral and amortization policy choice for accounting for defined benefit plans that exists in Section 3461 will be eliminated. An approach similar to the immediate recognition approach will remain as the only option for accounting for defined benefit plans. As a result, the defined benefit asset or liability on the statement of financial position will reflect the defined benefit obligation, net of the fair value of any plan assets, adjusted for any valuation allowance as of the balance sheet date.

✓ The three month window that allowed plan obligations and plan assets to be measured within 3 months of the year-end date will be eliminated.

What are the significant changes introduced by Section 3463?

✓ Section 3463 is a supplement to Section 3462 and narrowly addresses the recognition of remeasurements and other items. All other aspects of Section 3462 are applicable to not-for-profit organizations following Part III of the CPA Canada Handbook. Remeasurements and other items include actuarial gains and losses, past service costs, gains and losses arising from settlements and curtailments and changes in the valuation allowance.

✓ Remeasurements and other items are to be recognized directly in net assets on the statement of financial position rather than in the statement of operations and not reclassified to the statement of operations in a subsequent period. Furthermore, remeasurements and other items are to be separately identified as a line item in the statement of changes in net assets.

Section 3462 and Section 3463 should be read in their entirety for a full understanding of all of the changes being introduced.

Some questions for management and the audit committee to start to consider

- What does the actuary need to do differently to meet the new requirements?
- How will line items in the financial statements be impacted?
- What process is in place to capture the new disclosure requirements and terminology changes that have been introduced?
- Will bank covenants, compensation or other agreements be impacted?

Section 3462 and Section 3463 should be read in their entirety for a full understanding of all of the changes being introduced.

GST/HST – New parking rules for public sector bodies

Be Patient and Please Review the New Rules

On January 24, 2014 the Federal Government announced new technical amendments to the / (ETA) that, in certain cases, provides an exemption from the GST/HST for patients and visitors parking provided by hospitals and their affiliated charitable foundations. This new policy announcement effectively reverses the previous Federal Budget announcement on March 22, 2013 that intended to tax parking supply made by charitable foundations.

Background

In general, the supply of parking is taxable when provided by a person engaged in commercial activities or a public sector body (PSB). However, the supply of parking was almost always exempt when provided by a registered charity. This created distortions in the marketplace wherein charities frequently compete with the private sector, and other non-for-profits, in providing commercial parking spaces. To address this perceived inequity, and to prevent specific tax planning opportunities, the 2013 Budget introduced the following two measures

1. A "clarification" that the exemption that applies to supplies by a public sector body of property or services where all or substantially all of the body's supplies of the property or service are made free would not apply to supplies of parking spaces. This change was applied retroactively to the introduction of the GST legislation in 1991.

2. An amendment to the exemption that applies to parking provided by charities that are not also a particular type of PSB (a municipality, university, public college, school or hospital.) so that the exemption will not apply in the case of parking that is supplied by way of lease, licence or similar arrangement in the course of a business carried on by a charity set up or used by such a PSB to operate a parking facility. This amendment was to apply to supplies of parking made after March 22, 2013.

There was significant backlash with respect to the second measure as several organizations refused to comply with the proposed changes. Adding to this policy confusion, Finance Canada did not release the supporting draft legislation, suggesting that it was reconsidering its position.

The new parking rules – Charities

A new provision is added to exclude from the general exemption for charities, other than public institutions, supplies of parking when the following three conditions are met:

1. The supply of a parking space is made for consideration, by way of lease, licence or similar arrangement **and in the course of a business** carried on by the charity that makes the supply.

2. It must **be reasonable to expect**, at the time when the supply of the parking space is made, that the **specified parking area** in relation to the supply of the parking space will be used, during the calendar year in which the supply is made, primarily (more than 50%) by individuals who are accessing property of, or facilities or establishments operated by a municipality, a school authority, a hospital authority, a university or a public college.

3. The third condition for exclusion from exemption is where
   - If the charity that makes the supply of a parking space is expected under its governing documents to use a significant part of its income or assets for the benefit of any particular municipality, school authority, hospital authority, university or public college, or several of them;
   - If the charity that makes the supply of a parking space and a particular entity that is a municipality, school authority, hospital authority, university or public college in relation to which the reasonable expectation for use of parking is met have entered into one or more agreements in respect of the use of the parking spaces by the individuals who are accessing a property of, or a facility or establishment operated by, the particular entity;or,
   - This third condition can also be met for a supply of a parking space by a charity if a particular municipality, school authority, hospital authority, university or public college in relation to which the reasonable expectation for use of parking spaces condition is met performs any function or activity in respect of supplies by the charity of parking spaces in the specified parking area in relation to the supply of the parking space (e.g., snow removal or deduction of fees for parking at the specified parking area from employee wages).

The new rules – All or substantially all free supplies of parking by a charity

The legislation exempts supplies by a charity that is not a public institution if all or substantially all of the charity's supplies of the property or service are made for no consideration. Such supplies are not considered to be made in the course of a commercial activity. This section is amended to also expressly exclude from exemption supplies of parking spaces if the supply of a parking space is made for consideration, by way of lease, licence or similar arrangement and in the course of a business carried on by the charity. The amendment ensures that the exemption does not apply to supplies of commercial paid parking by a charity even if the charity provides a significant amount of parking at no charge.

This amendment applies to any supply made after March 21, 2013.

New hospital parking rules

A new provision exempts the supply (other than by way or sale) made by a PSB of a parking space for hospital parking when the three conditions are met.

The first condition for exemption which can be met in either of the two ways described below:

1. Reserved test – This first condition can be met if **all of parking spaces** in the specified parking area in relation to the supply of the parking space are **reserved** for use by individuals who are accessing a public hospital. A supply of a parking space that allows use of any vacant parking space in a parking lot where all of the parking spaces in the parking lot are reserved for individuals accessing a public hospital is exempt; or,

2. Expected use test – The way the first condition can be met is based upon the **expected use** of the parking spaces in the specified parking area in relation to the supply of the parking space. In order for the first condition to be met it must be reasonable to expect, at the time when the supply of the parking space is made, that these parking spaces will be used, during the calendar year in which the supply is made, primarily by individuals who are accessing a public hospital.

Reserved parking – Not for patients or visitors – A supply of a parking space would not meet this second condition for exemption if all or substantially all of the parking spaces in the specified parking area in relation to the supply are reserved for use other than by individuals accessing a public hospital otherwise than in a professional capacity. For example, a supply of a parking space would not meet this condition for exemption if all or substantially all of the parking spaces in the specified parking area in relation to the supply were reserved for the use of students attending a university or staff of a public hospital.

Not accessing a public hospital – A supply of a parking space would not meet the second condition for if the supply of the parking space, or the consideration for the supply, is conditional on the parking space being used by a person other than an individual accessing a public hospital otherwise than in a professional capacity. For example, a supply of a parking space by way of sale of a parking pass that can be obtained only by university students, or that is available at a reduced consideration if for use of hospital employees but at full price if for use of hospital patients, would not meet the second condition for exemption.

Parking pass – Not for patients or visitors – A supply of a parking space would not meet the second condition if the agreement for the supply is entered into in advance, the period over which parking spaces can be accessed under the supply is more than twenty-four hours and the access to the specified parking area in relation to the supply is to be used by a person other than an individual accessing a public hospital otherwise than in a professional capacity. For example, a supply of a parking pass to allow a family member of a public hospital patient to access a parking lot over a period of one month while visiting the patient would meet the second condition for exemption whereas a supply of the same pass to allow a nurse to access the parking lot while working at the public hospital would not.

Real property elections – For the exemption to apply, then the supplier cannot have a section 211 election in place.

This amendment applies to any supply made after Announcement Date.

Transitional rules

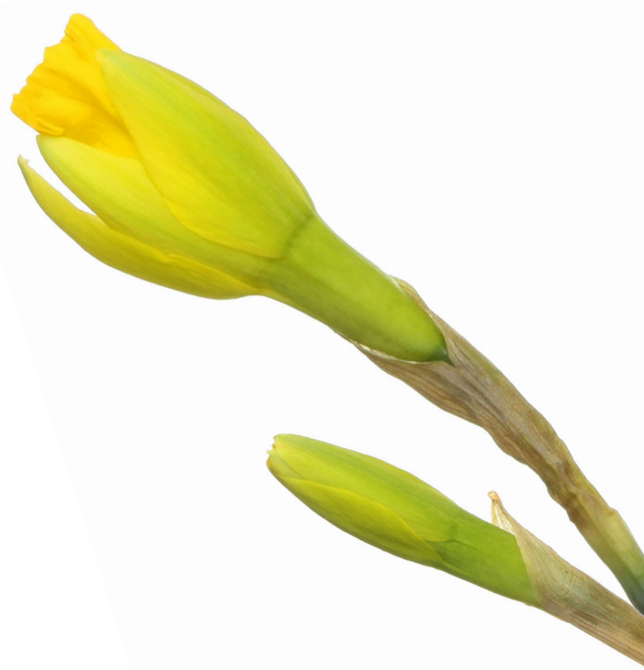
Relieving measures have been introduced for charities that have collected tax based on the Budget announcement on parking spaces made after March 21, 2013 and on or before February 24, 2014, where the supply would now be exempt. Under the relieving measure, the amount is deemed not to have been collected as or on account of tax for purposes of determining the net tax of the charity. This deeming rule has the effect of relieving the charity from the obligation to remit the amount or, if the amount has been remitted, allowing the charity to recover the amount as a tax paid in error rebate.

A further special rule applies if an amount is subject to the deeming rule discussed above and that amount has been taken into account in assessing the net tax of a charity. In these circumstances, the amount could not be rebated as a tax paid in error rebate. The special rule allows the charity to request in writing, within one year after the enactment of new parking rules that the Minister of National Revenue assesses, reassesses, or makes an additional assessment of, the net tax to take into account the effect of the deeming rule.

There are no further requirements for charities that did not collect tax based on the Budget announcement provided that the new exemption is applicable.

Conclusion

The new rules are very complex and require a detailed review for each charity's particular situation. We encourage you to reach out to your Deloitte representative or professional service providers to discuss the implications on your organization. Note, Finance Canada requested comments concerning the proposed changes which suggests that further changes may be released in the future.



Deliberation time

Improvements to Not-for-Profit Standards – Statement of Principles comments are in

The Canadian Accounting Standards Board ("AcSB") and the Public Sector Accounting Board ("PSAB") are deliberating the comments received on the Improvements to Not-for-Profit Standards – Statement of Principles ("SOP"). The SOP was issued in April of 2013 and outlines 15 key principles proposing some significant changes to not-for-profit accounting for organizations in both the private and public sectors.

Comments on the principles outlined in the SOP were due in December 2013. There were over 280 responses, an overwhelming number from a variety of interested parties. The comments vary depending on the perspective of the respondent. However, when all responses are looked at collectively, there seem to be common concerns mainly with a handful of the proposed principles.

Common concerns

Over
90%
of the respondents expressed concerns with Principles 2 & 3

Principles 2 & 3
Contributions
Private and public sector organizations
Principles 2 and 3 propose that a contribution would be recognized as revenue when the contribution is received or receivable in accordance with Principle 1, except when it gives rise to an obligation that meets the definition of an accounting liability.

Common concerns include:

- Lack of clarity in terms of the definition of a liability and how it would be applied in practice. As an example, consider deferred capital contributions – would the capital contribution be recognized on the date that the capital asset was purchased? If so, this would be a significant change from the current practice of recognizing the capital contribution over the asset's life and matching it with the amortization taken;
- If contributions, such as endowments, are no longer recorded as direct increases in net assets, this treatment will not be reflective of their nature as permanent capital;
- The volatility in the statement of operations resulting from these changes could impact the willingness of donors to provide financial support to an organization; and
- Consideration should be given to specifically defining non-reciprocal transactions which may not create a legal obligation but may result in a moral or ethical obligation. How should such transactions be accounted for?

Over
80%
of the respondents expressed concerns with Principle 10

Principle 10
Controlled and Related Entities
Private and public sector organizations
Principle 10 proposes to eliminate some of the current policy choices thereby requiring controlled not-for-profit organizations to be consolidated and controlled profit oriented organizations to be accounted for in accordance with the modified equity method.

Common concerns include:

- There is not a strong basis for justifying different accounting for controlled not-for-profit versus controlled profit oriented enterprises; and
- By eliminating policy choices, the result could be less meaningful financial statement presentation depending on individual circumstances.

The statistics and common concerns are based on approximately the first 170 responses to the SOP posted on *www.frascanada.ca* website.

Over
80%
of the respondents expressed concerns with Principle 13

Principle 13
Financial Statement Presentation
Public sector organizations only
Principle 13 proposes that public sector organizations should apply *PS 1201 Financial Statement Presentation* which could introduce some significant changes to financial statement presentation including a new statement of net debt.

Over
80%
of the respondents expressed concerns with Principle 14

Principle 14
Financial Statement Presentation
Private and public sector organizations
Principle 14 proposes that expenses should be presented by function and disclosed by object (nature) in the financial statements AND total fundraising expenses and general support expenses should be presented as separate functions in the statement of operations or disclosed in the notes to the financial statements.

Common concerns include:

- Some organizations and their users lack an understanding of the net debt model in *PS 1201 Financial Statement Presentation;*
- The proposal does not acknowledge the range of users whose needs must be met by the general purpose financial statements;
- The disclosure of a budget in the financial statements may not be useful as primary users may already have access to such information and likely at a more detailed level; and
- The proposal will result in differences between the financial statements of private sector and government not-for-profit organizations. This is problematic where similar organizations fall into different categories depending on which province they are located. As an example, universities are considered private sector in some provinces and government not-for-profit organizations in others.

Common concerns include:

- It is difficult to achieve consistency in defining functions, including, fundraising and general support expenses;
- Inappropriate focus may be placed on fundraising and general support expenses as an indicator of an organization’s success;
- Organizations should be able to choose the presentation of their expenses so that the approach is the most appropriate based on individual circumstances; and
- The requirement to provide this level of detail may create costs that outweigh the benefits.

Some organizations and their users lack an understanding of the net debt model in PS 1201 Financial Statement Presentation

There were also principles with which the majority of the respondents generally seemed to agree with or did not express concerns. The following 6 principles fall into that bucket for private sector organizations:

Principle 4

Contributions of Materials and Services

An NFPO may choose to recognize contributions of materials and services at fair value when a fair value can be reasonably estimated.

Principle 5

Tangible Capital Assets

An NFPO applying Part III should apply PROPERTY, PLANT AND EQUIPMENT, Section 3061 and DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475 in Part II, in reporting the capitalization, amortization and disposal of tangible capital assets. TANGIBLE CAPITAL ASSETS HELD BY NFPOs, Section 4431 in Part III, would be amended to include write-downs to reflect a partial loss of service potential of an asset that is still being used.

Principle 6

Intangible Assets

An NFPO applying Part III of the CPA Canada Handbook – Accounting should continue to apply INTANGIBLE ASSETS HELD BY NFPOs, Section 4432. This Section would be amended to include write-downs to reflect a partial loss of service potential of an asset that is still being used.

Principle 11

Controlled and Related Entities

An NFPO applying Part III of the CPA Canada Handbook – Accounting should continue to disclose an economic interest in another NFPO over which it does not have control in accordance with REPORTING CONTROLLED AND RELATED ENTITIES BY NFPOs, Section 4450.

Principle 12

Controlled and Related Entities

An NFPO applying Part III of the CPA Canada Handbook – Accounting should continue to apply DISCLOSURE OF RELATED PARTY TRANSACTIONS BY NFPOs, Section 4460.

Principle 13

Financial Statement Presentation

A private sector NFPO applying Part III of the CPA Canada Handbook – Accounting should apply INCOME STATEMENT, Section 1520, BALANCE SHEET, Section 1521, CASH FLOW STATEMENT, Section 1540, and other appropriate Sections in Part II in presenting their financial statements.

Interestingly, the 6 principles listed above are ones that mostly suggest that the current accounting treatment for private sector organizations be carried forward essentially unchanged. Apparently, many of the respondents are supportive of current practice in these areas. Such agreement was not as apparent when looking at the responses to the specific questions asked on the principles for public sector organizations.

At this point, it is uncertain what direction the standard setters will take with the comments received and the principles as originally proposed in the SOP. Stay tuned as the Boards work together to improve the future direction of not-for-profit accounting standards! If you are interested in reading any or all of the comments received on the SOP, visit the financial reporting and assurance standards website (*www.frascanada.ca*).

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