

IFRS accounting standards

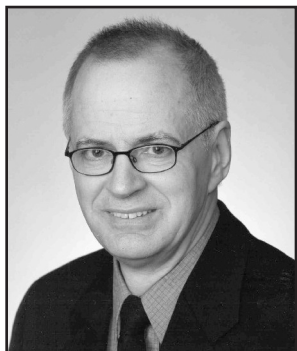
ACTIVITIES OF THE CANADIAN ACCOUNTING STANDARDS BOARD AND STAFF

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MESSAGE FROM THE CHAIR



PRIVATE ENTERPRISES: TIME FOR A NEW DIRECTION?

Differential reporting was introduced in 2001. It remains controversial but most people now seem to agree that the financial reporting needs of private enterprises differ from those of publicly accountable enterprises in important respects. We have tried to develop appropriate eligibility criteria. The current requirement for unanimous consent for differential reporting can be onerous and focuses on shareholders, whereas creditors are the major users. Size tests are arbitrary, easily abused and not a good indicator of financial reporting needs. We considered a distinction

based on “significant” external users but the prospect of judging any external user to be insignificant was unappealing. Then we stepped back. Why do we need eligibility criteria? The vast majority of private enterprises have very straightforward financial reporting needs. Let’s concentrate on them. Entities with more sophisticated needs will “self select” to use full IFRSs.

The challenge is to strike the right balance in terms of the extent of change. The definitions of assets, liabilities, revenue and expenses and the recognition/derecognition criteria must be the same as in IFRSs. This is necessary to maintain the integrity of the standards and avoid confusing users who often receive both private and publicly accountable enterprise financial reports. Disclosure requirements can be greatly reduced. Some standards could be greatly simplified by emphasizing principles, eliminating detailed rules and other implementation guidance, such as EIC Abstracts, and placing more reliance on professional judgment. There may be scope to revert to cost-based measurements rather than fair value in a number of cases. The greater the changes, the greater the effort required of preparers, auditors and users to learn, implement and maintain the system, and the greater the difficulty of migrating to full IFRSs.

Why stop with private enterprises? The vast majority of not-for-profit organizations have very straightforward financial reporting needs, similar to those of private enterprises. We encourage all entities that are not “publicly accountable enterprises” (as identified in the AcSB’s April 2008 Exposure Draft, “Adopting IFRSs in Canada”) to participate in the current project to develop a simpler GAAP.

Paul Cherry

See our website at www.acsbcanada.org for the most recent information on activities in progress.

FINANCIAL REPORTING STANDARDS FOR PRIVATE ENTERPRISES

The AcSB is seeking to finalize its strategy for private enterprises. It is developing a “made in Canada” financial reporting system for private enterprises and, possibly, for not-for-profit organizations. The standards being developed will produce general purpose financial statements, on which assurance can be provided.

The following provides a summary of the primary elements of the standards for private enterprises, together with an overview of the approach and timetable for completing the project.

PRIMARY ELEMENTS

The standards will be:

- *Available for use by all private enterprises*
An entity will not be subject to a size test or other qualifiers such as unanimous consent as a condition of applying the standards for private enterprises. Private enterprises will be given a free choice to adopt this model; an entity could elect to follow IFRS, the standards being developed, or as is the case with many private enterprises, follow no financial reporting standards at all.
- *Developed using the same conceptual framework as standards for publicly accountable enterprises*
The definitions of assets, liabilities, revenue and expenses and the recognition/derecognition criteria must be the same as in IFRSs and existing Canadian GAAP. This is necessary to maintain the integrity of the standards and avoid confusing users. This does not rule out differences from standards applicable to publicly accountable enterprises — the cost/benefit constraint will serve as a basis for creating differences. The standards will be developed based on user needs, recognizing that creditors are the most frequent user of private enterprise financial statements. It will also be recognized that users in this sector often have the ability to obtain additional financial reporting information beyond the financial statements.
- *Based on the existing CICA Handbook – Accounting (Handbook)*
The financial reporting standards contained in the existing Handbook are of high quality; they have been developed over a number of years following established “due process” procedures. The financial reporting community in Canada is familiar with the standards, having used them (through application of the standards or use of financial statements) for many years. Many users have stated that radical change from

the existing Handbook is not needed; however, there are a limited number of issues that should be revisited. Finally, using the existing Handbook as a starting point will allow timely production of the standards. There has been a strong demand from stakeholders to produce the standards for private enterprises as soon as possible.

Earlier strategic consultations noted that the standards for private enterprises could be based on IFRSs (full IFRSs or the proposed IFRS for SMEs). These platforms are not being used as a starting point, as a system based on full IFRSs would be asking too much from this sector at this time, and there is some degree of uncertainty with respect to the timing of the IFRS for SMEs. Additionally, many stakeholders have expressed concern regarding the approach and content of the proposed IFRS for SMEs.

- *Linked to standards for publicly accountable enterprises*
Financial reporting standards must evolve over time so that they do not become stale. A connection between standards for publicly accountable enterprises and private enterprises promotes understandability and eases the burden on education and training. Accordingly, the standards for private enterprises will evolve based on relevant changes in standards applicable to publicly accountable enterprises.

APPROACH

An Advisory Committee has been formed to assist the AcSB in developing the standards. The Advisory Committee consists of knowledgeable individuals from within the sector representing public practitioners, preparers, and financial statement users.

The Advisory Committee will consider input received from the AcSB’s widespread consultations on its Invitation to Comment, “Financial Reporting by Private Enterprises,” and the CICA’s proposed financial reporting “Framework for Owner-managed Enterprises.”

Key areas of change, from the existing Handbook, will be as follows:

- *Contentious issues*
There are a limited number of areas in the existing Handbook that are problematic for private enterprises. These areas will be redeliberated, primarily based on cost/benefit considerations. Problematic areas include: financial instruments, consolidation and accounting for affiliates, future income taxes, asset retirement obligations, employee future benefits, leases, current/non-current classification, goodwill and intangible assets, and stock-based compensation.

- *Disclosures*

A complete reconsideration will be given to the existing disclosure requirements. Most users of private enterprise financial statements have the ability to make direct enquiries regarding specific areas of interest, and private enterprises are much less constrained than publicly accountable enterprises in responding. On this basis, the AcSB expects the disclosure requirements in the standards for private enterprises to be significantly fewer than in the existing Handbook.

- *Irrelevant material*

Sections, Guidelines and Abstracts that are relevant only to publicly accountable enterprises will be excluded. Examples of such material include Section 1701, *Segment Disclosures*, Section 1751, *Interim Financial Statements*, and Section 3500, *Earnings Per Share*.

Other aspects of the existing Handbook will be relatively unchanged.

NOT-FOR-PROFIT ORGANIZATIONS

On the recommendation of the Not-for-Profit Organizations Advisory Committee, the AcSB will consider permitting not-for-profit organizations to apply the standards for private enterprises. Accordingly, the needs of these organizations will be considered in developing the standards. It will remain the responsibility of the Not-for-Profit Organizations Advisory Committee, as well as other stakeholders, to make recommendations to the AcSB on the suitability of the standards for the not-for-profit sector.

TIMETABLE

The Advisory Committee will discuss aspects of the proposed standards over the summer. Its recommendations will be communicated to the AcSB on a fast-track basis.

Working drafts of individual standards will be posted to the AcSB website, for general information and comment by constituents, on an ongoing basis. The current expectation is that this process will be completed by the fall of 2008. This project is of top priority to the AcSB, and it has arranged additional meeting time to ensure that this project can proceed in a timely fashion.

The AcSB will conduct consultations with interested parties across the country on the approach to developing the new standards this summer and fall. The purpose of these meetings is to inform stakeholders of the activities regarding this project, and seek input with respect to the overall approach to developing standards for private enterprises.

Meeting dates and locations will be posted to the AcSB website, as they are organized. If you are interested in attending any of these sessions, please consult the AcSB website (www.acsbcanada.org) in the coming months.

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GAAP FOR NOT-FOR-PROFIT ORGANIZATIONS

The AcSB is in the process of implementing its Strategic Plan pursuant to which it has adopted IFRSs for publicly accountable profit-oriented enterprises, is developing standards for private enterprises, and is evaluating what future standards should be for not-for-profit organizations (NFPOs).

In evaluating future standards for NFPOs, the AcSB will only be considering standards that would constitute GAAP. The AcSB understands that there are many occasions when NFPOs prepare non-GAAP financial statements that presumably meet their users' needs (for example, statements of receipts and disbursements prepared by some church congregations and small sports organizations). The AcSB is not intending to propose any changes to such non-GAAP approaches.

NFPOs that currently prepare GAAP financial statements do so in accordance with the standards contained in the CICA Handbook – Accounting (Handbook), thus sharing a common conceptual framework with, and generally applying standards that are developed for, profit-oriented enterprises. The Handbook also contains a series of standards, the 4400 series, that are applicable only to NFPOs.

As noted, the AcSB has decided to replace existing standards with IFRSs for certain profit-oriented enterprises (for example, companies whose shares trade on a stock exchange). The AcSB is also developing a comprehensive set of standards that could be applied by other profit-oriented enterprises such as private enterprises. The AcSB is considering the implications for financial reporting by NFPOs of adopting IFRSs as the basis for GAAP reporting by publicly accountable enterprises and developing a separate set of GAAP standards for private enterprises.

Many stakeholders believe the current credibility of the financial statements of NFPOs financial statements relates directly to their association with standards of general applicability. There is significant benefit to the financial statements of NFPOs being prepared on a basis of accounting that is generally understood by users, is supported by a common conceptual framework, and appropriately reports all transaction and circumstances of NFPOs, particularly those that are unique to NFPOs.

FYI

Accounting Standards

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Based on that information, the AcSB has determined that one viable option is to continue to require NFPOs to follow standards developed for profit-oriented enterprises with guidance appended to those standards that addresses the unique transactions and circumstances of NFPOs in a manner similar to the 4400 series of pronouncements. It should be noted that those future standards would have to be compatible with the standards to which they are appended and, consequently, will differ in some respects from those in the existing 4400 series.

In that context, the AcSB has agreed to consider permitting NFPOs to apply the standards developed for private enterprises, together with the additional standards addressing unique circumstances of NFPOs. Accordingly, the needs of NFPOs will be considered in the development of the private enterprise standards.

Therefore, preparers, users and auditors of the financial statements of NFPOs should monitor the development of the new standards for private enterprises and consider the utility of the proposals in their own particular circumstances. Developments may be followed on the AcSB's website at www.acsbcanada.org/index.cfm/ci_id/29407/la_id/1.htm.

Any tentative decisions by the AcSB will be exposed for stakeholder comment in an Invitation to Comment on the future direction of NFPO accounting standards in Canada. It is expected that the Invitation to Comment will be issued later this year.

The AcSB would like to receive input from preparers, users and auditors of the financial statements of NFPOs financial statements as the process evolves. Comments should be addressed to the Not-for-Profit Organizations Advisory Committee's staff contact (see below).

In a related matter, the AcSB approved the amendments proposed in the 2007 Not-for-Profit Organizations Exposure Draft, with the exception of the proposals to amend Section 4450, *Reporting Controlled and Related Entities by Not-for-Profit Organizations*, pending the outcome of its deliberations on future standards for NFPOs.

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