2 Carlton Street, Suite 600, Toronto Ontario M5B 1J3
Phone: (416) 597-2293, Fax: (416) 597-2294
1 800 263 1178

2, rue Carlton, bureau 600, Toronto (Ontario) M5B 1J3
Téléphone : 416 597-2293, Télécopieur : 416 597-2294
1 800 263 1178

November 5, 2013

Mr. Peter Martin, Director
Accounting Standards
277 Wellington Street West
Toronto, Ontario M5V 3H2
ed.accounting@cpacanada.ca

Mr. Tim Beauchamp, Director
Public Sector Accounting
277 Wellington Street West
Toronto, Ontario M5V 3H2
ed.psector@cpacanada.ca

Dear Mr. Martin and Mr. Beauchamp,

We are writing to you regarding "*Improvements to Not-for-Profit Accounting Standards*", the Statement of Principles prepared by the Accounting Standards Board and Public Sector Accounting Board (the Boards).

Imagine Canada is the national umbrella for Canadian registered charities and public-benefit nonprofits. There are approximately 165,000 registered charities and nonprofits (NPOs) in Canada, located in every community and ranging in size from small community-based organizations to large universities, hospitals, and national organizations. Charities and public-benefit nonprofits partner with communities, governments, and the private sector to help address many of the most intractable challenges we face as a society. The charitable and nonprofit sector is also an engine of economic activity, providing jobs for some two million Canadians and representing more than seven percent of GDP.

In our capacity as an umbrella, Imagine Canada engages directly with a large number of organizations representing the full breadth and diversity of the sector; our reach is extended by our close working relationships with organizations representing specific parts of the sector including community and private foundations, United Ways, arts organizations, and health charities, among others.

Imagine Canada is a strong supporter of enhanced transparency and accountability within the not-for-profit sector. For example, our CharityFocus.ca resource presents comprehensive CRA T3010 information for Canada's 85,000 Registered Charities in a clear and useful format, and provides charities with the ability to tell their full story by uploading additional information, including financial statements and annual reports. We support the Boards' continuing efforts to improve standards for financial reporting by NPOs.

Preamble

We are in general agreement with the underlying objectives of the proposals set out in the Statement of Principles (SOP):

- We concur that it is appropriate to eliminate guidance that is already included in the respective reference standards.
- We believe it is generally appropriate to conform guidance to be consistent with the reference standards, including their conceptual frameworks. We are pleased that the Boards have acknowledged that some differences are necessary to recognize the unique circumstances of NPOs.
- We agree that it is important to provide guidance to supplement the requirements in the reference standards to address transactions and circumstances that are unique to NPOs and that new or amended guidance is appropriate, where necessary, to address the needs of NPO users.

However, if all the proposals in the SOP are adopted, there will be a very significant impact on the financial statements of NPOs. The SOP appears to be based on the conclusion that there are significant issues with the current rules. We are not aware of significant problems with these rules.

Before addressing the specific questions noted below with respect to private sector NPOs, we think it is important to express our concern that the proposals in the SOP are not based on a well-defined understanding of the diversity of NPOs, who uses the financial statements of these organizations, and what their needs are for information. NPOs differ in many ways from each other including size, complexity, and type of operations and sources of funding. The users of their statements are also very diverse, ranging from being very sophisticated and financially literate to having little understanding of financial reporting. NPO financial statements are often used for very different purposes than are the financial statements of for-profit entities, for example, to assess efficiency as opposed to making investment decisions.

We believe it is essential to have a good understanding of NPOs, the users of their financial statements, and the needs of these users to be able to develop principles that will allow the preparation of financial statements that are meaningful to these users.

One important question that must be answered is how people with an interest in NPOs get information they need. Are the financial statements the primary source of information or are interested parties able to get the information they need in other ways? The input we have from our consultations with NPOs is that general purpose financial statements are not the primary way they provide information to address their accountability and stewardship responsibilities. Contributors can always request any additional information they need to make an informed decision. If the information a contributor needs isn't provided, they have the choice of not contributing.

Contributions

1. Do you agree with the proposal in Principle 1 that a contribution would be recognized as an asset when the recipient has control of the contribution and would exercise that control if necessary?

1.1 We agree that the criteria proposed to determine when contributions should be recognized in the accounts of an organization are reasonable. This principle is consistent with the approach now taken by many NPOs.

1.2 Some organizations, including many United Ways, generally recognize pledges in order to record revenue related to the campaign carried out in a particular fiscal year. Because their campaigns are done annually, they have significant experience in estimating the collection rate for these pledges in order to record a reasonable estimate of the amount that will be collected. Given the importance of recognizing pledges for these organizations, we believe this principle needs to be examined further.

2. Do you agree with the proposals in Principles 2 and 3 that a contribution would be revenue, except when the contribution gives rise to an obligation that meets the definition of a liability?

2.1 As noted in the SOP, the current standards permit two different approaches to revenue recognition. Organizations have different types of operations and these two approaches accommodate the diverse needs of operating organizations and foundations to adopt an approach that meets the information needs of their users.

2.2 Our comments in this section are initially focused on the proposals as compared to the existing deferral approach.

2.3 Our opinion about Principles 2 and 3 is very dependent on what contributions are considered to meet the definition of a liability. At this point in time, we do not believe there is a common understanding of how the definition of a liability would be applied in practice. There appear to be a number of different interpretations of how the definition would be applied. Based on the comments in the SOP related to specific types of contributions, we have significant concerns about what would be eligible to be recorded as a liability. We understand that some people believe that a contribution cannot be recorded as a liability unless it has to be repaid. This interpretation fails to take into consideration a unique aspect of donations to charities – the Canada Revenue Agency does not permit agreements that provide for the repayment of a restricted donation if the purpose is not satisfied.

2.4 We understand that NPOs who use the deferral method generally believe that all contributions with restrictions that have not been met need to be recorded on the balance sheet as liabilities. The definition of a liability was likely developed based on reciprocal transactions since this is the type of transaction entered into by for-profit organizations. We believe consideration needs to be given to whether adjustments are required to properly address non-reciprocal transactions since this type of transaction is very common in NPOs.

2.5 Based on consultation with NPOs who use the deferral method, their users generally want a statement of operations that provides a meaningful representation of the amounts available at the discretion of the organization and the expenses incurred during the year. As the AcSB acknowledged in the Exposure Draft related to employee future benefits, the statement of operations is significant to donors and other funders. Since these users often focus on the "bottom line", looking for a "balanced budget", surpluses and deficits created by poorly understood accounting practices can create misunderstandings that could, for example, affect donors' willingness to provide financial support to an organization.

2.6 NPOs who use the deferral method generally believe that, when a funder provides funding with a restriction, that funding should not be recorded as revenue until the restriction has been satisfied. It is essential that contributors are confident that their restrictions on the use of funds are respected by the recipient organization. For the accounting profession to impose rules that could result in amounts being recorded as revenue before the restrictions have been satisfied is completely inconsistent with the obligation to comply with the restrictions imposed by contributors. Recording a restricted contribution as a liability until the restriction is met imposes a discipline on the organization receiving the restricted contribution. The contribution isn't recorded as revenue until the restriction has been met. If contributions with restrictions are recorded as revenue before the restriction has been met because the contribution doesn't meet the accountant's definition of a liability, there is no need to demonstrate that the restriction has been met before the amount is recorded as revenue. A separate accounting would need to be maintained outside the books of record to keep track of restricted amounts already recorded as revenue even though the restriction had not been met. We believe it is important for the accounting records to be the way of tracking these restricted contributions.

2.7 The SOP makes comments about specific types of contributions that raise significant concerns for many NPOs. As detailed below, the proposed accounting will result in significant volatility in the statement of operations. Given the significance of the amounts related to these types of contributions, the statement is likely to become meaningless and potentially misleading for many organizations.

2.8 The SOP indicates that the AcSB believes that endowment contributions should be recorded as revenue since the requirement to retain the principal amount of the contribution permanently is not a condition that creates a liability for the recipient organization. Further, the SOP comments that endowment contributions are inflows or enhancements of assets resulting from the ordinary activities of an entity and that they are the same as other contributions to an organization that it actively solicits, invests to produce a return and expends in accordance with its terms. We believe these comments demonstrate a lack of understanding of the nature of an endowment contribution and the legal restrictions associated with this type of contribution. An endowment contribution is completely different from other types of contributions solicited by an organization since the principal amount is not available to be spent. It should not be accounted for in the same way as a contribution that is available to be spent. This type of contribution is more similar to a capital contribution received by a for-profit organization, which does not get recorded as revenue.

2.9 The SOP also comments on the accounting for contributions restricted for the purchase of capital assets. The SOP indicates that a contribution of this type should be recorded as revenue when the asset has been acquired. The commentary in the SOP about the need to develop new principles related to accounting rules for NPOs refers to inconsistencies between the accounting for similar transactions entered into by not-for-profit and for-profit organizations. What is being proposed for NPOs is inconsistent with how contributions received by for-profit organizations are accounted for. Parts I and II provide that government contributions for capital assets should be netted against the cost of the asset or the amount should be set up as a liability. The contributions are not recorded as revenue. We do not understand why the proposed principle for NPOs is inconsistent with how other organizations are required to account for the identical transaction. Adopting the approach set out in the SOP would result in a significant surplus in the year that a capital asset is purchased and deficits over the period when the asset is being amortized. NPOs are different than for-profits in that significant assets are frequently funded by third parties and the assets would not be purchased if they weren't externally funded.

2.10 Some NPOs use the restricted fund method. For certain types of organizations, this approach allows them to provide information that is of most interest to their users – the total amount of donations received and the total amount of investment income earned. Given the importance of this method for these organizations, we believe this principle needs to be examined further.

2.11 In conclusion, we believe that the principles related to the recording of revenue need to be reconsidered. We do not believe that the current proposals will permit the preparation of financial statements that provide meaningful information for the users of the statements. We believe that more research needs to be done to better understand who the users are of NPO financial statements, what information they need, and how best to record contributions to respond to those needs.

3. Do you agree with the proposal in Principle 4 to retain the option of recognizing contributed materials and services?

3.1 We agree that a choice should be available to NPOs with respect to the recognition of contributed materials and services. We recognize that this principle is inconsistent with the guidance in the reference standards. We concur that this inconsistency is appropriate.

Tangible capital assets

4. Do you agree with the proposal in Principle 5 that PROPERTY, PLANT AND EQUIPMENT, Section 3061, and DISPOSAL OF LONG-LIVED ASSETS AND DISCONTINUED OPERATIONS, Section 3475, in Part II of the CICA Handbook – Accounting apply to reporting the capitalization, amortization and disposal of tangible capital assets?

4.1 We agree that it is appropriate to use the standards in Part II to deal with the accounting for capital assets to the extent that there are no unique considerations for NPOs.

5. Do you agree with the proposal in Principle 5 that TANGIBLE CAPITAL ASSETS HELD BY NPOs, Section 4431, should be amended to take into account partial write-downs of tangible capital assets?

5.1 We agree that it is appropriate to deal with partial write-downs of tangible capital assets.

Intangible assets

6. Do you agree with the proposal in Principle 6 to continue to apply INTANGIBLE ASSETS HELD BY NPOs, Section 4432, in accounting for intangible assets?

6.1 We agree with the proposal that NPOs continue to apply Section 4432.

7. Do you agree with the proposal in Principle 6 that Section 4432 should be amended to take into account partial write-downs of intangible assets?

7.1 We agree that it is appropriate to deal with partial write-downs of intangible capital assets.

Tangible and intangible capital assets (size exemption)

8. Do you agree with the proposal in Principle 7 to eliminate the size test that currently permits qualifying NPOs not to recognize their tangible and intangible capital assets?

8.1 We agree with the proposal in Principal 7.

Works of art, historical treasures and similar items

9. Do you agree with the proposal in Principle 8 that works of art, historical treasures and similar items that are part of a collection should be recognized at either acquisition cost or nominal value in the statement of financial position?

9.1 We agree with Principle 8 that proposes no changes to the current accounting rules.

10. Should the definition of a collection be improved and, if so, how?

10.1 We are not aware of any issues with the current definition of a collection and, therefore, have no suggestions for improvements.

11. Do you agree with the proposal in Principle 9 to continue to apply the existing standards for works of art and similar items not part of a collection?

11.1 We are in agreement with the proposal in Principle 9.

Controlled and related entities

12. Do you agree with the proposal in Principle 10 to consolidate controlled NPOs, subject to an exclusion from consolidation of a large number of individually immaterial organizations?

13. Do you agree with the proposal in Principle 10 to account for controlled profit-oriented enterprises by the equity method?

12/13.1 We believe that there are a number of issues with the proposals in Principle 10, and that the SOP does not make a convincing case for what is being proposed.

12/13.2 The principles appear to be based on the AcSB's conclusion that the reference standards in Part II that provide for choices are not appropriate for NPOs since users may not have access to information about the controlled entities. We are not clear how the AcSB reached this conclusion since the option in the current rules could be carried forward requiring that summary financial statements for a controlled entity must be provided in the notes to the financial statements. If this requirement is retained, the user then has all the information needed to understand the full nature and extent of the financial affairs and resources that a reporting entity controls.

12/13.3 We believe that there should be choices that allow an organization to choose the most appropriate approach to presenting information about controlled organizations, both for-profit and not-for-profit.

12/13.4 We are not convinced that there should be different rules to account for controlled not-for-profit and for-profit organizations. The SOP says that it is inappropriate to co-mingle the assets, liabilities, revenues and expenses of a for-profit and a not-for-profit and therefore proposes that the equity method be used to account for controlled for-profit organizations. There are many situations where a controlled NPO is very different from the NPO that controls it and the consolidation of the controlled organization would result in issues similar to what would be involved with consolidating a for-profit entity (for example, a not-for-profit housing corporation controlled by a social service agency).

12/13.5 We do not believe that an organization's tax status should dictate its accounting treatment. However, if that approach is to be taken, there is a further complication with respect to these principles since, whether an organization is a for-profit or a not-for-profit is not always clear. There are a number of situations where an organization uses the not-for-profit rules because they file as a not-for-profit with CRA. The nature of their activities may not be significantly different from another organization that does not classify itself as a not-for-profit.

12/13.6 In addition, we believe the concept of control is not as easily defined with respect to a NPO. We expect that there will be significant difficulty in agreeing to a definition of control.

12/13.7 In conclusion, we believe these proposals need to be reconsidered to better understand their implications, based on a stronger understanding of user needs in this area.

14. Should the exclusion from consolidation of a large number of individually immaterial organizations continue to be permitted?

14.1 As noted above, we believe that there should be choices that allow an organization to choose the most appropriate approach to presenting information about controlled organizations, including individually immaterial ones.

15. Are there any other circumstances in which exclusion from consolidation should be permitted?

15.1 As noted above, we believe that there should be choices that allow an organization to choose the most appropriate approach to presenting information about controlled organizations.

16. Are there circumstances in which controlled profit-oriented enterprises should be consolidated?

16.1 As noted above, we believe that there should be choices that allow an organization to choose the most appropriate approach to presenting information about controlled profit-oriented enterprises.

17. Do you agree with the proposals in Principle 11 to continue to disclose economic interests in accordance with REPORTING CONTROLLED AND RELATED ENTITIES BY NPOs, Section 4450?

17.1 We agree that the existing requirements to provide disclosures with respect to economic interests should be retained.

18. Do you agree with the proposal in Principle 12 to continue to disclose related party transactions in accordance with DISCLOSURE OF RELATED PARTY TRANSACTIONS BY NPOs, Section 4460, until the AcSB has determined whether a standard for measurement of a NPO's related party transactions should be developed?

18.1 We agree with the proposal in Principle 12.

Financial statement presentation

19. Do you agree with the proposal in Principle 13 to apply INCOME STATEMENT, Section 1520, BALANCE SHEET, Section 1521, CASH FLOW STATEMENT, Section 1540, and other appropriate Sections in Part II of the CICA Handbook – Accounting for financial statement presentation?

19.1 We agree that it is appropriate to use the reference standards in Part II related to financial statement presentation assuming that any unique characteristics of NPOs are addressed in Part III.

20. Do you agree that guidance should be retained in FINANCIAL STATEMENT PRESENTATION BY NPOs, Section 4400, on fund accounting (including inter-fund transfers), disclosure of restrictions on net assets, reporting of net assets and changes in net assets balances, and reporting of revenues and expenses at gross versus net amounts.

20.1 We agree that guidance on matters unique to NPOs should be retained in Part III.

21. Are there other financial statement presentation matters on which additional guidance should be provided?

21.1 We are not aware of any financial statement presentation matters that require additional guidance.

22. Do you agree with the proposals in Principle 14 that:

(a) information regarding expenses should be provided by function and by object (nature) in the financial statements; and

(b) total fundraising expenses and general support expenses should be presented as a separate function in the statement of operations or disclosed in the notes to the financial statements?

22.1 We do not agree with the proposals in Principle 14. We do not believe it will be possible to develop a generally accepted definition of functions. As well, consistent with the reference standards in Part II related to presentation in the statements of private companies, we so not believe that the accounting profession should impose standards related to the overall presentation of expenses. Organizations should be able to choose the approach that is most appropriate based on their particular circumstances.

22.2 The SOP suggests that this requirement will enhance the comparability of reporting amongst NPO. We believe this conclusion demonstrates a lack of understanding about the difficulties in achieving consistency among organizations in defining certain functions, particularly fundraising and general support expenses.

22.3 Over the years, charities have attempted in many forums to develop common definitions of functions. These efforts have generally been unsuccessful. The significance of these inconsistencies is particularly important with respect to the fundraising and general support functions based on the attention given to the amounts spent on these functions. We do not believe that the accounting profession would be successful in defining these functions in a way that will result in organizations presenting numbers prepared consistently or meaningfully. Without a very clear definition of what is included in each function, this requirement will likely contribute to inappropriate pressure on charities to minimize these expense categories and would result in inappropriate reporting.

22.4 We are also concerned about the conclusion that information about fundraising and general support expenses is critical information for users. We believe that the focus needs to move away from these measures to information about the outcomes achieved by organizations.

22.5 Further, the need to provide this detail will create costs for NPOs that will likely not be offset by benefits for their users. This is a particular problem for smaller organizations.

22.6 In conclusion, we believe that these proposals need to be reconsidered.

23. Do you agree with the proposal in Principle 15 to continue to make prescribed disclosures when fundraising and general support expenses have been allocated to other functions in accordance with DISCLOSURE OF ALLOCATED EXPENSES BY NPOs, Section 4470?

23.1 We agree with the proposal in Principle 15.

Other

24. Are there any other aspects of the current financial reporting by NPOs that require improvement?

24.1 We are not aware of any other aspects of current financial reporting by NPOs that require improvement.

25. Are there any other matters that should be considered by the AcSB as it proceeds to determine the manner in which it will address the implementation of the proposals in this Statement of Principles?

25.1 As noted in the introduction, we support the review of accounting standards used by NPOs. However, we believe that the AcSB needs to do significantly more research to better understand who the users are of NPO financial statements and the information needs of these users. We are not convinced that the conclusions throughout the SOP related to user needs are accurate. We believe this research should be done before any reconsideration of the proposed principles, since a good understanding of user needs is critical in developing principles that will result in meaningful financial statements. As well, additional consideration needs to be given to the potential for the principles creating significant negative consequences for NPOs.

*   *   *

Imagine Canada would be very willing to participate in any further work undertaken by the Boards to better understand who the users are of NPO statements and what their information needs are. We would also be pleased to assist in future initiatives to develop standards that result in the preparation of meaningful financial statements that meet the needs of users.

Thank you in advance for your kind consideration of our comments, and we look forward to continue to working with you.

Yours truly,

Marcel Lauzière
President & CEO