# Ottawa-Carleton District School Board

Audit Planning Report for the year ended August 31, 2019

KPMG LLP

Prepared on August 8, 2019 for the Audit Committee Meeting on September 25, 2019

KPMG

Appendix B
to Report 19-075

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**The contacts at KPMG in connection with this report are:**


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# Executive summary

## Audit and business risks

Our audit is risk-focused. In planning our audit of the consolidated financial statements of the Ottawa-Carleton District School Board (the "Board") we have taken into account key areas of focus for financial reporting. These include:

- Cash, investments, and investment income
- Government grants, related accounts receivable, and deferred revenues
- Capital assets and deferred capital contributions
- Accounts payable and accrued liabilities, including non-payroll expenses
- Long-term debt
- Salaries and benefits, including the employee future benefit liability
- Other fees and revenues
- School-funded activities including the school generated funds and school council funds
- Accumulated surplus
- Contingencies
- Financial reporting

## Audit materiality

Materiality has been determined based on total prior year expenses. We have determined materiality to be $12,000,000.

## Additional audit-related work

KPMG will perform the following services in addition to the audit of the Board's consolidated financial statements:

- Audit of the School Generated Funds and School Council Funds
- Audit of the Ontario Youth Apprenticeship Program

# Executive summary (continued)

## Independence and Quality Control

We are independent and have extensive quality control and conflict checking processes in place. We provide complete transparency on all services and follow Audit Committee approved protocols.

## Proposed Fess

Proposed fees for the consolidated financial statement audit are $79,000.

Proposed fees for additional work related to School Generated Funds and School Council Funds for the year-ended August 31, 2019, which is required in support of our audit opinion over the financial statements, are $17,000.

## Current Developments and Audit Trends

Please refer to Appendix 6 for upcoming accounting and auditing changes relevant to the OCDSB and relevant audit trends.

There are no significant new relevant accounting or auditing changes to be brought to your attention at this time, other than the New Independent Auditor's Report.

This Audit Planning Report should not be used for any other purpose or by anyone other than the Audit Committee. KPMG shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this Audit Planning Report has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

# Highly talented and experienced team

| Team member | | Background / experience | Discussion of role |
|---|---|---|---|
|  | **Rob Clayton, CPA, CA**<br>Lead Audit Engagement Partner<br>Tel: (613) 212-3601<br>rclayton@kpmg.ca | – Rob has over 15 years of experience serving not-for-profit organizations. Rob co-leads Ottawa's Public Sector practice. | – Rob will be responsible for the quality and timeliness of our work and the conclusions reached by the engagement team.<br>– He will provide the overall direction for audit and related services, and will have frequent and direct contact with the Board.<br>– Rob will help ensure the entity receives the full benefit of our audit and specialist resources on a timely and effective basis. |
|  | **Rebecca Prophet, CPA, CA**<br>Audit Senior Manager<br>Tel: (613) 212-3748<br>rprophet@kpmg.ca | – Rebecca has over ten years of experience serving public sector and not-for-profit organizations. Rebecca is a key member of KPMG's public sector audit practice group in Ottawa. | – Rebecca will work closely with Rob in developing and executing the audit strategy. She will be responsible for the direct supervision and management of the audit, the development of the detailed audit approach in consultation with Rob, the identification of financial reporting and operational efficiency issues, as well as review of the audit.<br>– Rebecca will be on site regularly during the audit period and will be your main point of contact throughout the year. |
|  | **Andrew C. Newman, FCPA, FCA**<br>Engagement Quality Review Partner<br>Tel: (613) 212-2877<br>andrewnewman@kpmg.ca | – Andrew has over 25 years of experience serving not-for-profit organizations.  Andrew is KPMG Canada's National Leader, Education, and co-leads Ottawa's Public Sector practice.<br>– Andrew is also Vice-Chair of the Public Sector Accounting Board of Canada. | – Andrew will be responsible for ensuring the overall quality of our work and to review the conclusions reached by the engagement team.<br>– Through his role on the Public Sector Accounting Board, Andrew will support the Board through any accounting standard changes and continue to provide updates and insights to the Board regarding the future of accounting standards. |

# Key Board team members

KPMG has identified the following management and other team members who will play a vital role in the Board's audit execution. The availability and participation of these individuals in the audit process is key to the successful completion of the audit in the timelines provided. During the post-audit Audit Committee meeting, we will debrief the Audit Committee on the readiness and performance of the Board's team during the audit.

| Key Team Member | Key Responsibilities in Support of the Audit |
|---|---|
| **Michael Carson,** Chief Financial Officer | – Michael Carson provides general oversight of the financial close process and will attend debrief meetings with the KPMG Partner and Senior Manager. |
| **Kevin Gardner**, Manager of Finance | – Kevin Gardner provides general oversight of the financial close process and will attend debrief meetings with the KPMG Partner and Senior Manager. |
| **Teri Adamthwaite**, Financial Reporting Coordinator | – Teri Adamthwaite provides general oversight of consolidation, expenses, cash, and accounts payable of the Board. |
| **Kim Lebrun**, Finance Officer | – Kim Lebrun provides general oversight of the revenue, accounts receivable, and capital assets of the Board. |
| **Richard Sinclair**, Manager of Legal Services | – Richard Sinclair provides general oversight of legal matters of the Board. |
| **Amanda Wright,** Supervisor Payroll Services | – Amanda Wright provides general oversight of the salaries of the Board. |
| **Andrea Henry,** Assistant to Kevin Gardner | – Andrea Henry provides general oversight of minutes, Internal Audit, School Generated Funds, School Council Funds, scheduling meetings with Kevin Gardner (Manager of Finance) with the Board and will attend debrief meetings with the KPMG Partner and Senior Manager. |

# Audit risks

| Significant financial reporting risks | Why is it significant? |
| --- | --- |
| Professional standards presume a fraud risk from revenue recognition. | Audit standards require us to assume there are generally pressures & incentives on management to commit fraudulent financial reporting through inappropriate revenue recognition. This can be perpetrated through revenue cut-off or manual journal entries and other adjustments related to revenue recognition. |

## Our audit approach

Although there is a presumption that there are risks of fraud in revenue recognition, this presumption may be rebutted. We have exercised professional judgment and have rebutted this presumed risk. We have done this primarily because no risk factors have been identified. Revenues are not complex and they do not involve elements of significant judgment and there are no external expectations specifically on the Board's revenue which will be used for significant financial decisions of third parties.

# Audit risks (continued)

| Significant financial reporting risks | Why is it significant? |
|---|---|
| Professional standards presume the risk of management override of controls exists in all organizations. | The risk of fraudulent revenue recognition can be rebutted but the risk of management override of controls cannot, since management is typically in a unique position to perpetrate fraud because of the ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. |

**Our audit approach**

As this risk is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk. These procedures include testing of journal entries and other adjustments, performing a retrospective review of estimates and evaluating the business rationale of significant unusual transactions.

We also make enquiries of upper management and the Audit Committee related to their awareness of fraud risk factors of the Board and whether the Board is currently dealing with any suspected, alleged or known fraudulent activity.

# Materiality

Materiality represents the level at which we think misstatements will reasonably influence users of the financial statements. It considers both quantitative and qualitative factors. To respond to aggregation risk, we design our procedures to detect misstatements at a lower level of materiality.

The first step is the determination of the amounts used for planning purposes as follows:

| Materiality determination | Comments | Amount |
|---|---|---|
| **Metrics** | Relevant metrics including net assets/equity, total revenue, total expenses, and other program costs. | |
| **Benchmark** | Based on total prior year expenses. The benchmark and materiality will be re-assessed during the audit period to adjust for any new normalization or adjustment in activities. The prior year amount was $888,048,201. | $952,262,168 |
| **Materiality** | Determined to plan and perform the audit and to evaluate the effects of identified misstatements on the audit and of any uncorrected misstatements on the consolidated financial statements. The prior year amount was $11,500,000. | $12,000,000 |
| **% of Benchmark** | The corresponding percentage in the prior year was 1.30%. | 1.26% |
| **Performance Materiality** | Used 75% of materiality, and used primarily to determine the nature, timing and extent of audit procedures. The prior year amount was $8,625,000. | $9,000,000 |
| **Audit Misstatement Posting Threshold (AMPT)** | Threshold used to accumulate misstatements identified during the audit. The related prior year amounts were $575,000 and $1,150,000 respectively. | $600,000<br>$1,200,000 for reclassification |

Professional standards require us to re-assess materiality at the completion of our audit based on period-end results or new information in order to confirm whether the amount determined for planning purposes remains appropriate. Our assessment of misstatements, if any, in amounts or disclosures at the completion of our audit will include the consideration of both quantitative and qualitative factors.

# Audit approach

## Areas of Audit Focus

The following accounts have been identified in our risk based audit approach and our audit work will be focused on these items that represent the majority of assets, liabilities, revenues and expenses for the Board. These areas of audit focus may be revised because of new transactions or events at the Board, or changes in systems, people or structure, and/or the results of our audit procedures. We will communicate any changes to the Audit Committee in our Audit Findings Report.

| Significant account | Comments |
| --- | --- |
| Cash, investments, and investment income | - Confirmation with third parties for cash and bank indebtedness<br>- Review of bank reconciliations and vouch significant reconciling items to supporting documentation<br>- Review of restrictions and disclosures |
| Government grants, related accounts receivable, and deferred revenues | - Perform substantive analytical procedures over revenues and related accounts<br>- Evaluate revenue recognition, revenue restrictions, deferral and presentation considerations<br>- Vouch a selection of revenue transactions to supporting documentation to verify restrictions, if any<br>- Direct confirmation of amounts received and receivable from the Ministry<br>- For amounts receivable at year-end, we will inquire of management as to the collectability of the receivable balance |
| Capital assets and deferred capital contributions | - Significant additions / disposals vouched to supporting documentation<br>- Assessment of assets for write-down<br>- Amortization / interest on long-term debt, and amortization of deferred capital contributions recalculated<br>- Examination of supporting documentation related to restriction of funds intended for capital asset additions and treatment of proceeds from any disposed contributed assets |
| Accounts payable and accrued liabilities, including non-payroll expenses | - Perform substantive analytical procedures over payables and non-payroll expenses<br>- Significant accruals vouched to supporting documentation<br>- Search for unrecorded liabilities<br>- Evaluate completeness and valuation of the liability for contaminated sites, if any |
| Long-term debt | - Confirmation of debt balances with third parties |

# Audit approach (continued)

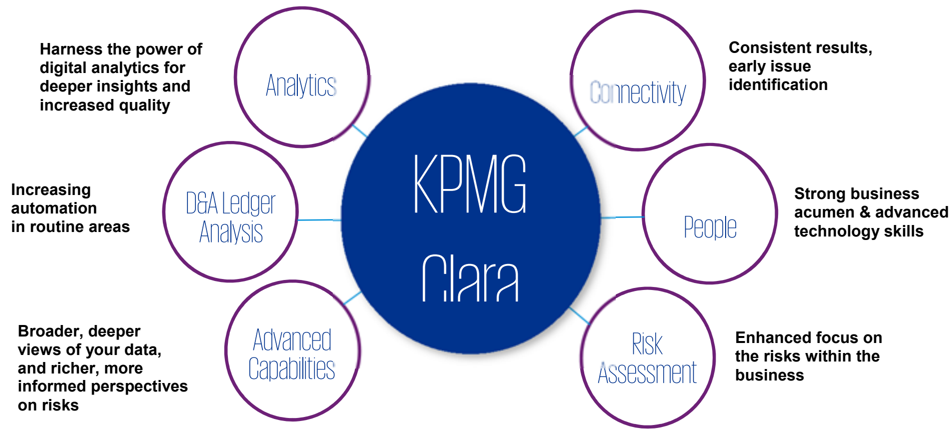
| Significant account | Comments |
| --- | --- |
| Salaries and benefits, including the employee future benefit liability | - Test and evaluate design and operating effectiveness over controls related to payroll monitoring controls<br>- Significant payroll-related accruals recalculated and vouched to supporting documentation<br>- Perform substantive analytical procedures over salaries and benefits, and related accounts<br>- Receipt and analysis of the actuarial report to independently verify employee future benefit accruals<br>- We will review the assumptions used in the valuations and perform audit procedures on the underlying employee data provided to the actuary in the year of full valuation |
| Other fees and revenues | - Significant additions and disbursements vouched to supporting documentation<br>- Ensure purpose-specific restrictions are recognized and accounted for appropriately |
| School-funded activities including the school generated funds and school council funds | - Substantive testing including selecting a sample of expense and revenue transactions, obtaining supporting documentation<br>- Performing analytic procedures over expenses and revenue followed by discussion with management |
| Accumulated surplus | - Significant additions and disbursements vouched to supporting documentation<br>- Ensure purpose-specific restrictions are recognized and accounted for appropriately |
| Contingencies | - Review of Board of Trustee and Audit Committee meeting minutes and legal correspondence<br>- Direct communication with external legal counsel to ensure that all significant contingent liabilities are appropriately disclosed and/or recorded<br>- Significant findings reviewed with management |
| Financial reporting | - Review by the engagement team of the consolidated financial statements prepared by the Board's management to ensure the disclosure is consistent with current public sector accounting, disclosure requirements, as well as industry practice |

KPMG has not identified any significant financial reporting risks as at the time of preparing this report that will require any additional audit procedures for the August 31, 2019 consolidated financial statement audit. KPMG will assess throughout the audit whether there are any activities that are outside the normal operations for the Board and will perform additional procedures if necessary. KPMG will address any new significant financial reporting issues with the Audit Committee in the Audit Findings Report.

# The audit of today, tomorrow & the future

As part of KPMG's technology leadership, our audit practice has developed technologies and alliances to continuously enhance our capabilities and deliver an exceptional audit experience.

Technology empowers us with the ability to perform deep analysis over your financial information, focusing our effort and interactions on the areas of greatest risk and minimizing disruption to your business.




## Technology we use today

| Tool | Benefit to audit |
|---|---|
| **KPMG Clara Client Collaboration** | KCCC is our secure audit platform and a one-stop shop through which we plan, execute and manage the audit, providing you with real-time access to the process at every step, including exchange of information and access to the real-time reporting you need in one central location. |
| **KPMG Clara Advanced Capabilities** | KPMG Clara Advanced Capabilities leverage our data and analytics capabilities, enabling us to analyze 100% of your general ledger data in the planning and account analysis stage and adjust our planned audit approach accordingly to target the areas of greatest risk. It allows us to use automation in performing our audit procedures over accounts such as (teams to edit for client-specific D&A routines; i.e., revenue and receivables, salaries, purchases and payables) and journal entries. |
| **Journal Entry Analysis** | Our journal entry tool assists in the performance of detailed journal entry testing based on engagement-specific risk identification and circumstances. Our tool provides auto-generated journal entry population statistics and focusses our audit effort on journal entries that are riskier in nature. |

# Data & analytics in the audit

We will be integrating Data & Analytics (D&A) procedures into our planned audit approach. Use of innovative D&A allows us to analyze greater quantities of data, dig deeper and deliver more value from our audit.

We believe that D&A will improve both the quality and effectiveness of our audit by allowing us to analyze large volumes of financial information quickly, enhancing our understanding of your business as well as enabling us to design procedures that better target risks.

| Areas of focus | Planned D&A routines |
|---|---|
| Journal Entry Testing | – Utilizing KPMG application software to evaluate the completeness of the journal entry population through a roll-forward of all accounts.<br>– Utilizing computer-assisted audit techniques (CAATs) to analyze journal entries and apply certain criteria to identify potential high-risk journal entries for further testing. |
| School Generated Funds and School Council Funds – funds raised directly in the school for activities and events within the schools | – KPMG will perform a substantive test of details over the revenue and expense transactions reported.<br>– KPMG will also perform a variance analysis using data and analytics techniques on the balances by school to identify any unusual activity during the year for further investigation and discussion with management.<br>– Utilizing computer-assisted audit techniques (CAATs) KPMG intends to analyse the reported School Generated Funds and School Council Funds of the top 10 schools in terms of revenue and expenses. KPMG also plans to perform a trend analysis over revenue and expenses by month and by type for the current year in comparison to the prior year in order to identify any significant anomalies. |

Detailed results and summary insights gained from D&A will be shared with management and presented in our Audit Findings Report.

# Additional audit-related work

KPMG will perform the following services in addition to the audit of the consolidated financial statements of the Board, either as a required deliverable per the Proposal dated April 24, 2012, the Engagement Letter dated September 25, 2019, or per request from the Audit Committee or consolidated entities.

## Additional audit work required to support our audit opinion on the financial statements

**N/A**

- KPMG will complete audit procedures over the School Generated Funds and School Council Funds for the year-ended August 31, 2019. These school-funded activities are incorporated into the consolidated financial statement of the Board. These activities are material to the Board's consolidated financial statements, and are reported on within the Board's Audit Findings Report.
- The Ottawa Student Transportation Authority (OSTA) is a consolidated entity to the Board. The OSTA's financial statements for the year ended August 31, 2019 will be audited by another auditor. KPMG will request a confirmation from that audit firm, a copy of the financial statements, and perform procedures over the consolidation into the Board's financial records.
- As at the date of this report, KPMG has not identified any additional, one-time audit procedures required to support our audit opinion of the consolidated financial statements.
- Any additional audit work identified during our audit will be discussed with Management and communicated to the Audit Committee in the Audit Findings Report.

## Other audits

**N/A**

- KPMG will complete the audit of the Ontario Youth Apprenticeship Program for the year-ended August 31, 2019.
- KPMG will complete the audit of the Ottawa-Carleton Education Network (OCENET) for the year-ended August 31, 2019. OCENET is a consolidated entity of the Board, but is not considered material in our audit approach.
- As at the date of this report, KPMG has not identified any other audits to be performed.
- Any additional audit engagements identified will be discussed with Management and communicated to the Audit Committee in the Audit Findings Report.

## Additional requested audit-related work

**N/A**

- Any additional audit work identified during our audit will be discussed with Management and communicated to the Audit Committee in the Audit Findings Report.

# Key deliverables and milestones

The following table details the detailed audit timetable for the year, outlining specific dates that KPMG will deliver on, as well as deadlines for audit requirements of management. The following planned dates have been agreed-upon by KPMG and management, and delays from this timeline may impact the achievement of this audit plan. KPMG will work with management to achieve this planned timeline and will communicate significant changes in our Audit Findings Report to the Audit Committee in November 2019.

| Audit Key Activities/Deliverables | Fiscal Year 2018 Date | Planned Milestone Date |
|---|---|---|
| Engagement Letter and Audit Planning Report sent to Management for review and approval | August 31, 2018 | August 13, 2019 |
| Presentation of the Audit Planning Report to the Audit Committee | September 26, 2018 | September 25, 2019 |
| Receipt of signed confirmation letters from management | August 21, 2018 | September 6, 2019 |
| Board to substantially complete the close of the August 31, 2019 year-end books and records | October 1 -November 7, 2018 | October 5, 2019 |
| Management to provide required working papers to KPMG | October 9, 2018 | October 7, 2019 |
| Audit fieldwork and wrap-up to be performed by KPMG | October 9 – November 9, 2018 | October 7 – November 7, 2019 |
| Draft financial reporting deliverables prepared by KPMG and provided to management | November 13, 2018 | November 15, 2019 |
| Deadline of receipt of legal letters, management to follow up with outstanding confirmations if applicable | November 10, 2018 | November 20, 2019 |
| Presentation of Audit Findings Report to the Audit Committee | November 19, 2018 | November 25, 2019 |
| Attendance at the Board of Trustees meeting for approval of the consolidated financial statements and KPMG's issuance of our independent auditor's report thereafter | November 20, 2018 | November 26, 2019 |

# Proposed fees

In determining the fees for our services, we have considered the nature, extent and timing of our planned audit procedures as described above.

Our fee analysis has been reviewed with and agreed upon by management as outlined in our proposal submission.

**Our fees are as follows:**

| | Current period (budget) |
|---|---|
| Audit of the consolidated financial statements for the Ottawa-Carleton District School Board for the year-ended August 31, 2019 | $79,000 |
| Additional audit work related to School Generated Funds and School Council Funds for the year-ended August 31, 2019 that is required in support of our audit opinion on the financial statements | $17,000 |

## Matters that could impact our fee

The proposed fees outlined above are based on the assumptions described in the Engagement Letter.

The critical assumptions, and factors that could cause a change in our fees, include:

- Audit readiness, including delays in the receipt of requested working papers, audit samples, inquiries and financial statements information from the agreed upon timelines, and the books and records being properly closed at the start of our year-end audit work;
- The availability, participation and responsiveness of key Board team members during the audit;
- Identification of control deficiencies during our audit, resulting in additional audit effort;
- Significant changes in the nature or size of the operations of Board beyond those contemplated in our planning processes;
- Changes in professional standards or requirements arising as a result of changes in professional standards or the interpretation thereof;
- Changes in the timing of our work, including the deadlines for deliverables;
- Significant one-time transactions entered into by the Board;
- Attendance at more than two meetings of the Audit Committee annually;

– Attendance at more than one meeting of the Board of Trustees annually.

# New auditor reporting

The new auditors' report will come in to effect for the 2019 fiscal year of the Ottawa-Carleton District School Board. The impact on the Board will be fairly minimal as a **non-listed** entity:

| Change | Applicability |
|---|---|
| **Re-ordering of the auditors' report including moving opinion to the first section** | Listed and non-listed entities |
| **Expanded descriptions of the responsibilities of management, those charged with governance and auditor** | Listed and non-listed entities |
| **Separate section on "Material Uncertainty Related to Going Concern", if applicable** | Listed and non-listed entities |
| **Separate section on "Other Information" (e.g. MD&A)** | Listed and non-listed entities |
| **Disclosure of name of the engagement partner** | Listed entities |

Please refer to the Engagement Letter in Appendix 1 for a draft auditors' report using the new auditor reporting model.

## Key audit matter reporting today

There has been much discussion in the financial reporting community about the inclusion of Key Audit Matters (KAMs) in the auditors' report. KAMs are those matters that, in the auditors' professional judgment, were of most significance in the audit, such as areas of higher assessed risk of material misstatement, significant auditor judgments and the impact on the audit of significant events or transactions.

Currently, in Canada, the reporting of KAMs in the auditors' report is only applicable when required by law or regulation or when the auditor is engaged to do so. There is no law or regulation requiring the reporting of KAMs for national not-for-profit organizations, and we have not been engaged to do so by the Board.

## Key audit matter reporting in the future

The Auditing and Assurance Standards Board in Canada is deliberating how and when the disclosure of KAMs will be required for **listed** entities in Canada. It is anticipated KAM reporting for certain listed entities in Canada will be required starting in 2020.

# Appendices

# Appendix 1: Required communications

In accordance with professional standards, there are a number of communications that are required during the course of and upon completion of our audit. These include:

### Engagement letter

The objectives of the audit, our responsibilities in carrying out our audit, as well as management's responsibilities, are set out in the Engagement Letter as attached.

### Management representation letter

We will obtain from management certain representations at the completion of the annual audit. In accordance with professional standards, copies of the representation letter will be provided to the Audit Committee.

### Audit planning report

This report. The purpose of this report is to provide Audit Committee members with an understanding of the audit approach and to provide the opportunity to provide input into the audit approach.

### Audit findings report

At the completion of our audit, we will provide our audit findings report to the Audit Committee.

### Required inquiries

Professional standards require that during the planning of our audit we obtain your views on risk of fraud and other matters. We make similar inquiries of management as part of our planning process; responses to these will assist us in planning our overall audit strategy and audit approach accordingly.

### Annual independence letter

At the completion of our audit, we will provide our Independence Letter to the Audit Committee.

# Appendix 2: Audit quality and risk management

KPMG maintains a system of quality control designed to reflect our drive and determination to deliver independent, unbiased advice and opinions, and also meet the requirements of Canadian professional standards. Quality control is fundamental to our business and is the responsibility of every partner and employee. The following diagram summarises the six key elements of our quality control systems. Visit our Audit Quality Resources webpage for more information including access to our audit quality report, *Audit quality: Our hands-on process.*

We conduct regular reviews of engagements and partners. Review teams are independent and the work of every audit partner is reviewed at least once every three years.

We have policies and guidance to ensure that work performed by engagement personnel meets applicable professional standards, regulatory requirements and the firm's standards of quality. We do not offer services that would impair our independence.

All KPMG partners and staff are required to act with integrity and objectivity and comply with applicable laws, regulations and professional standards at all times.

The processes we employ to help retain and develop people include:

- Assignment based on skills and experience
- Rotation of partners
- Performance evaluation
- Development and training
- Appropriate supervision and coaching


We have policies and procedures for deciding whether to accept or continue a client relationship or to perform a specific engagement for that client.

Existing audit relationships are reviewed annually and evaluated to identify instances where we should discontinue our professional association with the client.

Technical department and specialist resources provide real-time support to audit teams during the audit.

Our professionals receive industry-specific training on the trends, environment, regulations, common transactions, relevant accounting standards and audit risks, to provide our team members with an understanding of our client's operating environment.

# Appendix 3: KPMG's audit approach and methodology

This year we will expand our use of technology in our audit through our new smart audit platform, KPMG Clara.


### Collaboration in the audit

A dedicated KPMG Audit home page gives you real-time access to information, insights and alerts from your engagement team

### Issue identification

Continuous updates on audit progress, risks and findings before issues become events

### Data-driven risk assessment

Automated identification of transactions with unexpected or unusual account combinations – helping focus on higher risk transactions and outliers

### Deep industry insights

Bringing intelligence and clarity to complex issues, regulations and standards

### Analysis of complete populations

Powerful analysis to quickly screen, sort and filter 100% of your journal entries based on high-risk attributes

### Reporting

Interactive reporting of unusual patterns and trends with the ability to drill down to individual transactions

# Appendix 4: Lean in Audit™

## An innovative approach leading to enhanced value and quality

Our innovative audit approach, Lean in Audit, further improves audit value and productivity to help deliver real insight to you. Lean in Audit is process oriented, directly engaging organizational stakeholders and employing hands-on tools, such as walkthroughs and flowcharts of actual financial processes.

By embedding Lean techniques into our core audit delivery process, our teams are able to enhance their understanding of the business processes and control environment within your organization – allowing us to provide actionable quality and productivity improvement observations.

Any insights gathered through the course of the audit will be available to both engagement teams and management. For example, we may identify control gaps and potential process improvement areas, while management has the opportunity to apply such insights to streamline processes, inform business decisions, improve compliance, lower costs, increase productivity, strengthen customer service and satisfaction and drive overall performance.

## How it works

Lean in Audit employs three key Lean techniques:

### 1. **Lean training**

Provide basic Lean training and equip our teams with a new Lean mindset to improve quality, value and productivity.

### 2. **Interactive workshops**

Perform interactive workshops to conduct walkthroughs of selected financial processes providing end-to-end transparency and understanding of process and control quality and effectiveness.

### 3. **Insight reporting**

Quick and pragmatic insight report including immediate quick win actions and prioritized opportunities to realize benefit.

# Appendix 5: Background and professional standards

## Internal control over financial reporting

As your auditors, we are required to obtain an understanding of internal control over financial reporting (ICFR) relevant to the preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on internal control. Accordingly, we do not express an opinion on the effectiveness of internal control.

Our understanding of ICFR was for the limited purpose described above and was not designed to identify all control deficiencies that might be significant deficiencies and therefore, there can be no assurance that all significant deficiencies and other control deficiencies have been identified. Our awareness of control deficiencies varies with each audit and is influenced by the nature, timing, and extent of audit procedures performed, as well as other factors.

The control deficiencies communicated to you are limited to those control deficiencies that we identified during the audit.

## Documents containing or referring to the audited financial statements

We are required by our professional standards to read only documents containing or referring to audited financial statements and our related auditors' report that are available through to the date of our auditors' report. The objective of reading these documents through to the date of our auditors' report is to identify material inconsistencies, if any, between the audited financial statements and the other information. We also have certain responsibilities, if on reading the other information for the purpose of identifying material inconsistencies, we become aware of an apparent material misstatement of fact.

Management has represented to us that the Board does produce an annual report containing or referring to audited consolidated financial statements.  We will ensure our audit requirements are completed prior to the issuance of our auditors' report.

We are also required by our professional standards when the financial statements are translated into another language to consider whether each version, available through to the date of our auditors' report, contains the same information and carries the same meaning.

# Appendix 6: Current developments

*Current Developments*, created by the KPMG Public Sector and Not-for-Profit Practice, summarizes some of the regulatory, operational and governance developments impacting public sector, charitable and not-for-profit organizations. We provide this summary to inform our clients of changes that may impact their organization, and the trends we see in the industry based on our discussions with management and Audit Committee members of our public sector, not-for-profit and charity clients. Some of these developments may not impact your organization directly but we believe it is important for management and Committee members of charities and not-for-profit organizations to understand what is happening in the broader public, not-for-profit and charity sector.

## Annual Accounting, Tax and Risk Update for Not-for-Profit Organizations

KPMG held its Annual Accounting, Tax & Risk Update for Not-for-Profit Organizations on April 4, 2019 at the KPMG office in downtown Ottawa. The seminar covered current accounting, tax, technology and risk issues, including some of those discussed below, in greater detail providing not-for-profit organizations and charities with guidance on new standards, regulations and best practices. This event consistently attracts over 100 executives, financial officers and Board members from the Ottawa and area not-for-profit and charity community.

Audit Committee members are also invited to attend our future sessions, and be invited to other relevant webinars and thought leadership events. If you wish to have your name included on the invite list going forward, please e-mail Marcella Mannrich at mmannrich@kpmg.ca.

## Registered Charities

Below we provide a summary of activities and announcements that could have an impact on Canadian registered charities:

### Official Donation Receipts:

All official donation receipts need to include the CRA's name and website address. CRA's website recently merged with the Canada.ca domain website. Therefore, official donation receipts will need to be updated to include the new website address: Canada.ca/charities-giving. Receipts issued after March 31, 2019 must include the new website address.

### Social Innovation and Social Financing:

The federal government's Social Innovation and Social Finance Strategy Co-Creation Steering Group released its report: *Inclusive Innovation: New Ideas and New Partnerships for Stronger Communities*. The report provides a number of recommendations to the Government to promote social innovation and social financing in Canada, and is of significant interest to the Canadian charity and not-for-profit industry. The full report can be found at the following website:

https://www.canada.ca/en/employment-social-development/programs/social-innovation-social-finance/reports/recommendations-what-we-heard.html.

### Senate Committee on the Charitable Sector

In January 2018, The Senate of Canada established a new special committee to examine the impact of federal, provincial and territorial laws and policies governing charities and study the role that the charitable sector plays in Canadian society. The Committee will issue a report of the Committee's findings and make recommendations on revisions to government policies at all levels to support charities to fulfil their important missions. The Committee continues to hold meetings and hear from expert witnesses from the charity and other sectors. More information on the Committee can be found on the website of the Senate of Canada.

# Appendix 6: Current developments (continued)

### CRA's Charity Education Project

In the fall of 2017, Canada Revenue Agency announced the implementation of its Charity Education Project (CEP) initiative, as a complement to its traditional audit program. Per the CRA announcement the CEP program is "*designed to conduct in-person visits with registered charities, providing them with information and assistance in understanding these obligations*". A CEP visit by a CRA Charity Education Officer will include information sharing on the charity's purpose and activities, a review of the charity's books and records and T3010 information return, and a summary of findings and recommendations prepared by the Charity Education Officer. The registered charity will be requested to sign the summary of findings and recommendations to indicate their agreement with it.

CRA plans to perform 500 CEP visits per year. We are aware of registered charities receiving notification that they have been selected for a CEP visit in January 2018. At KPMG, we will be tracking these initial visits at our clients to identify patterns in CRA's approach and in their findings and recommendations, to assist our clients in preparing for future CRA visits.

To paraphrase Shakespeare's "A rose by any other name would smell as sweet"; a CRA visit by any other name smells like an audit. We encourage our registered charity clients who receive a CEP request letter to contact us to discuss how to prepare for CRA's visit and to prepare a response to the summary of findings and recommendations.

As a matter of good governance, we also encourage all registered charities to do the following on a regular basis:

1) Review the charity's operations to verify that activities directly support their charitable objectives. Consider the level of time and resources invested in fundraising or political activities, as these are two activities that CRA monitors.
2) Verify that the charity's T3010 Charity Information Return is accurate and that it strategically and faithfully represents the activities and operations of the charity. Verify that the T3010 published on the CRA's website agrees with the submitted return.
3) Assess the charity's accumulated reserves, surpluses and net assets, including the purpose for having them and support for the amounts. Consider developing a Board-approved "net asset reserve policy" documenting the purpose and amount of reserves in the context of organization risks and strategic plan.

KPMG will continue to monitor this situation and will provide updates to you.

## Tax-Exempt Status of Not-for-Profit Organizations

Over the past few years, the income tax-exempt status of not-for-profit organizations and the activities that should be eligible for this exemption have been the subject of significant political and public debate.

This debate intensified with the CRA's Non-Profit Organization Risk Identification Project (the "NPORIP") looking at entities claiming the exemption from income tax under Paragraph 149(1)(l) of the Income Tax Act of Canada, and the release of their report in 2014. The report emphasized three main risk areas which in the eyes of CRA would disqualify a not-for-profit organization from claiming the income tax exemption:

- having individual activities not related to their not-for-profit objectives; or earning non-incidental profits from individual activities
- using income to provide personal benefits to members
- maintaining excessive accumulated reserves, surpluses or net assets

# Appendix 6: Current developments (continued)

In 2014, the Department of Finance announced its intention to hold public consultations with not-for-profit organizations on these issues. Since then, the Department of Finance has provided no further indication as to when, or if, it expects to begin public consultations with the not-for-profit community on the issues surrounding the tax-exempt status of not-for-profit organizations, or when legislation is anticipated.

In the interim, CRA has not performed specific audits of the income tax-exemption status of not-for-profit organizations to our knowledge. However, CRA continues to perform regular HST and payroll compliance audits of not-for-profit organizations and charities. As part of these audits, CRA has included questions relating to the accumulated surplus/net assets/reserves of the audited organization, and is seeking documented evidence of purpose, future plans and governance oversight related to these balances.

KPMG encourages the Boards and management of not-for-profit organizations, and of charities, to continue to prepare their organizations for the anticipated changes to tax legislation and regulations. Not-for-profit organizations should review and consider their not-for-profit or charitable objectives, strategic plans, risk assessments, financial results and operational practices in the context of the aforementioned risk areas identified by CRA. In particular, not-for-profit organizations should develop or update a written, approved Board policy relating to their net assets, accumulated surpluses and/or reserves explicitly documenting the reasons for maintaining these balances, how the amounts were calculated and quantified, and how the amounts will ultimately be used. Boards should also demonstrate and document their oversight of this policy on an annual basis.

KPMG continues to monitor this situation closely and will continue to update you and all of our NPO audit clients.

## Decriminalization of Cannabis

On October 17, 2018, the use of cannabis for recreational purposes became legal in Canada. Most organizations are reviewing their policies with respect to the use of cannabis from a human resources perspective, such as impairment in the workplace. However, from a governance and management perspective there are also a number of policies that will also need to be considered and revised. A couple of examples:

1) What is the organization’s policy with respect to serving cannabis-infused drinks or products at official events and functions?
2) What is the organization’s policy with respect to reimbursing for cannabis-infused drinks and products on expense reports of employees, volunteers and Board members? What are the policies of your funders relating to whether these will be considered eligible costs under their contribution agreements?

Fortunately, most organizations have these policies relating to alcohol which will serve as a good starting point. We encourage our clients to review all of their policies to identify ones potentially in need of revisions to reflect this new law.

## Charities, Not-for-Profit Organizations and the # MeToo Movement

In the last five years, the bar has been raised steadily for employers by a series of class-action and individual law-suits, legislative, regulatory and public policy changes, all in relation to sexual harassment in the workplace. There is a need and desire to stamp out sexual harassment in the workplace, and Boards and Management must understand their role in addressing this very real and significant workplace risk. Apart from the obvious impact to individuals involved in a harassment situation, there are significant reputational risks for charities, not-for profit organizations and individuals.

Managing the risk of sexual harassment in the workplace is similar to managing other risks in the organization and must be included as a very important element of an organization's overall governance and risk management strategy. To protect against the risk of sexual harassment in the workplace, Boards and Management need to maintain a robust risk management program designed to address the core objectives of prevention, detection and response.

# Appendix 6: Current developments (continued)

**Prevention** starts with the "tone from the top", where a culture of honest and ethical behaviour is promoted throughout the organization, starting with the Board and Senior Management. This tone can be reflected in the Code of Conduct or Ethics policy, outlining core values and specifics regarding what constitutes sexual harassment. In addition to setting an appropriate tone for the organization, periodic risk assessments should be conducted, which identify the areas/business units and activities most susceptible to incidents of sexual misconduct.

**Detection** of sexual harassment in the workplace can be difficult, and as such, it is critical for organizations to provide a mechanism for employees, volunteers and the public at large to report incidents of sexual harassment to Senior Management or the Board, if they suspect an issue. The keys to a successful incident reporting mechanism include sufficient training and awareness for all employees and volunteers, ongoing communication including periodic reminders of the program (and annual signoff by employees regarding their awareness of the program and their duty to report), and transparency of reporting the status of complaints (in an anonymous fashion) to employees.

An organization's **response** to sexual harassment in the workplace is critical in mitigating potential damage, including personal and organizational reputational harm. As such, it is important to have a response plan in place before a sexual harassment complaint occurs, including investigation and communication protocols.

Boards and Management of charities and not-for-profit organizations are beginning to incorporate sexual harassment awareness in their training programs to increase awareness, and to develop a greater understanding of the key organizational elements of a robust sexual harassment risk management strategy. Such a risk management strategy is not a "nice to have" - it is a business imperative.

## Cyber Security – Prevention and Response

Organizations are subject to increasing amounts of legislative and public pressures to show they are managing and protecting their information appropriately. Simultaneously, the threats from cyber criminals and hacktivists are growing in scale and sophistication. Organizations are also increasingly vulnerable as a result of technological advances and changing working practices including remote access, cloud computing, mobile technology and services on demand. The financial and reputational costs of not being prepared against a cyber-breach could be significant. Not-for-profit organizations are at particular risk due to the information they maintain, including research data, personal data, and health and financial information. The reputational risk of this information not being adequately protected can often outweigh the financial consequences of a breach.

Cyber Security is not solely about information technology; it is fundamentally an operational and governance issue. Not-for-profit organizations should document their assessment of operational threats, implement preventative safeguards against a cyber-attack, and create a comprehensive response plan to a cyber-breach. Every organization should have a Computer Security Incident Response Team (CSIRT) consisting of individuals from many areas of the organization, including those involved in finance, human resources, procurement, customer/member relations, upper management and Board members. Key elements to consider in developing your cyber plans include:

- Assessing the likelihood and intensity of a cyber-attack, based on the value of your information and your public profile
- Assessing your organization's vulnerabilities to a cyber-attack
- Preparing your people, processes, infrastructure and technology to prevent a cyber-attack from being successful
- Detecting, responding and reporting a cyber-breach within your organization
- Initiating your cyber response plan, including containing and investigating the cyber breach
- Recovering from a cyber-breach and resuming business operations
- Reporting on the cyber breach, including informing authorities and affected individuals, as required by legislation and industry common practices.
- Doing a "lessons learned" process to identify improvements

# Appendix 6: Current developments (continued)

Not-for-profit organizations need to review their operations from the perspective of cyber risks, preventative measures against an attack and response plans for breaches. Of particular importance is the cyber response plan as most experts believe that it is now a matter of when, not if, a cyber-breach occurs. A proper cyber response plan should include at least the following elements:

1) Define sensitive data and information -- what is important to your organization and of value to hackers
2) Identify cyber breach scenarios – perform a Threat Risk Assessment of threats, vulnerabilities and likelihood of exploitation
3) Assess detection and response capabilities – what is your organization's capability to manage an incident (CSIRT structure and effectiveness, required performance metrics, business resumption, internal/external communication protocols)
4) Develop and refresh your organization's response plan – Identify a target state and address gaps, including time to discover, time to manage, severity of post-mortem reviews
5) Test and improve response plan – develop a testing strategy that includes key internal and external CSIRT responders (event simulations, live testing)

We encourage all not-for-profit organizations and charities to develop their cyber response plans and discuss them at the Board level.

Members of Audit Committees should be asking management fundamental questions such as: How effective is our organization's cyber strategy at identifying and addressing cyber risks? Is the organization relying on the correct and accurate information to oversee and understand those risks? Is the organization addressing its data privacy and security obligations? Does the organization have a response plan in place to manage a cyber-crisis when an incident occurs?

## Indirect Tax Considerations

The GST/HST is constantly evolving. The kinds and pace of the changes affecting your organization will depend on your status and activities, and may result from new legislative and regulatory rules, court cases, and changes in the CRA's administrative policies. In addition, major organization changes, such as reorganizations, cessation of activities, major capital projects, new relationships (e.g., shared service arrangements), and new revenue generating activities may have significant GST/HST implications.

The Canada Revenue Agency (CRA) continues to increase its focus on public service bodies (e.g., municipalities, universities, colleges, hospitals, schools, associations, charities, non-profits etc.) for purposes of conducting GST/HST audits. These audits may be undertaken by GST/HST audit teams dedicated to the public sector or by auditors attached to the CRA's GST/HST Refund Integrity Unit. Many organizations have undergone audits over the past couple of years. Based on our work with audited organizations, we offer the following general observations on the impact of the CRA's ongoing focus on the public sector:

- The CRA has been focusing on documentation, cost sharing and buying group arrangements, grants and sponsorships, as well as the allocation of inputs between taxable and exempt activities for input tax credit purposes (e.g. the filing of a Section 211 election and claiming of input tax credits on the use of real property).
- The CRA has not consistently been applying audit offsets (e.g., allowing unclaimed input tax credits or rebates) that would help minimize the impact of any assessments.
- Proposed assessments based on sampling and alternative valuation or allocation methodologies conducted by CRA auditors should be reviewed as fair and reasonable alternatives may be available that could significantly reduce an GST/HST assessment.
- The CRA is required to communicate the amount and basis for a proposed assessment to the registrant, and should allow the registrant a reasonable amount of time to review and respond to the assessment (i.e., generally 30-days). It is entirely appropriate to carefully review and question a proposed assessment. Our experience is that proposed assessments can often be significantly reduced at the audit stage. If a Notice of Assessment is issued, you will have 90 days to file a Notice of Objection with the CRA.

# Appendix 6: Current developments (continued)

- It is important that you have a plan in place for a GST/HST audit, including having a fixed point of contact for the auditor. Planning and managing the audit is as important as having the appropriate policies and procedures.
- Organizations that have undergone significant changes in operations are more likely to be selected for an audit. Many of these organizations are completing compliance reviews by indirect tax professionals in advance of a potential GST/HST audit to verify that the GST/HST is being appropriately handled. A proactive approach can reduce compliance costs and the time needed to deal with CRA auditors.

Our experience with GST/HST auditors has varied from audit to audit. However, in each case, the taxpayer has the burden of proof. The best approach is to be prepared in advance of receiving that audit notification from CRA.

## Reporting Requirements in the United States

Over the past two years, the United States has implemented significant tax reforms impacting Canadian business and individuals with activities and investments in the United States. Given this current environment, it is prudent for Canadian charities and not-for-profit organizations to consider whether they have any reporting obligations in the United States, which is dependent on their U.S. sources of revenue and activities.

For example, Canadian registered charities may be required to file the Form 990: Return of Organizations Exempt From Income Tax, depending on whether the Canadian charity is recognized as a U.S. public charity or a U.S. private foundation and depending on the total gross receipts that the Canadian charity receives from U.S. sources (including individual and corporate donations). The Internal Revenue Service (IRS) assumes that a Canadian registered charity is the equivalent of a U.S. private foundation unless it applies to the IRS to be recognized as a public charity. Normally, a Canadian registered charity receiving more than $25,000 in gross receipts from sources within the United States will have a requirement to submit the Form 990 to the IRS.

The Form 990 reporting requirements are significantly more extensive than the Canadian reporting requirements. The Form 990 can easily be more than 50 pages long and includes an 8-page detailed questionnaire on the organization’s governance, operations and activities, and very detailed information on the organization’s donors, activities outside of the United States, grants provided to other entities inside/outside the United States, executive compensation, and related party transactions. The Form 990 is a Canadian registered charity’s only public document in the United States and is available on the IRS information website.

We encourage all of our charity and not-for-profit clients to review their activities and sources of revenue on a regular basis to determine whether they have U.S. reporting requirements.

## Fraud Risk in Charities and Not-for-Profit Organizations

You only have to read the local and national news to understand the significant, adverse impact that a fraudulent or illegal act can have on an entity’s financial position, on-going operations and public reputation. For charities and not-for-profit organizations, a fraudulent or illegal act can be absolutely devastating not only because of their reliance on public financial support but also their need to maintain public confidence and trust in their activities. With social media, and the 24-hour continuous news cycle, the financial, operational and reputational risk of a fraud on a charity or not-for-profit organization has never been higher.

Therefore, fraud risk management is now a very important element of an organization's overall governance and risk management. To protect against the risk of fraud, Boards and management need to maintain a robust fraud risk management program designed to address the core objectives of prevention, detection and response.

Prevention starts with having a heightened awareness of fraud including the key indicators that a fraud may have occurred, an understanding of the profile of a fraudster and what may drive otherwise good people to do bad things. In addition to a heightened awareness of fraud, conducting regular fraud risk assessments allows charities and not-for-profit organizations to identify the key fraud risks they are facing and what they need to do to mitigate these risks.

# Appendix 6: Current developments (continued)

Detecting fraud can be difficult, so in addition to implementing and monitoring detection controls, it is critical for organizations to provide a mechanism for employees, volunteers and the public at large to report incidents of alleged fraud or wrongdoing to the Board.

An organization's response to a fraud is critical in mitigating potential damage, including reputational harm. As such, it is important to have a response plan in place before a fraud occurs, including investigation and communication protocols.

Boards and management of charities and not-for-profit organizations are beginning to incorporate fraud awareness in their training programs to increase fraud awareness, and to develop a greater understanding of the key organizational elements of a robust fraud risk management program.

## The COSO Framework: Demonstrating Sound Management Practices and Internal Controls

Charities and not-for-profit organizations are facing increasing pressures and challenges from various internal and external stakeholders, who are demanding greater transparency and accountability. Chief among these is a heightened level of scrutiny and higher expectations on charities and NPOs to demonstrate sound stewardship, accountability, and achievement of results. This includes being able to demonstrate that resources are managed in a cost-effective manner and that funding received is used to maximize the achievement of the organization's mandate.

A charity's or not-for-profit organization's ability to clearly demonstrate sound management and use of funding and the achievement of objectives are of direct interest to donors, funders, partners, stakeholders and beneficiaries, and increasingly to the Canadian general public. This, combined with a general increase in competition for scarce resources, can compound the challenges experienced by charities and not-for-profit organizations.

In this environment, your organization will be asked to demonstrate that it is using and managing funds in an economical and efficient way and that maintains a solid control environment supporting management decisions made by the organization. National charities and not-for-profit organizations are beginning to formally adopt the "COSO Framework" of management practices and internal controls to respond to their stakeholder demands. The COSO Framework is an internationally recognized framework for the assessment of management practices and internal controls in all types of entities.

The main reason that the COSO Framework is gaining acceptance in the charity and not-for-profit sector is that it considers internal controls from the perspective of achieving organizational objectives categorized into three areas:

- Effectiveness and efficiency of operations, at the entity-wide and divisional/program levels
- Reliability of financial and non-financial reporting to internal and external stakeholders
- Compliance with applicable laws and regulations

In the current environment of transparency and accountability, charities and not-for-profit organizations must not only achieve, but also explicitly demonstrate, their performance in these three areas. COSO provides a methodology to develop and maintain an effective system of internal control that reduces, to an acceptable level, the risk of not achieving these objectives.

The COSO Framework identifies five core components (Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities) and seventeen key principles within these five components that are required for an effective system of internal control. The Framework is fully scalable to an organization's size, structure, funding sources, or mandate.

# Appendix 6: Current developments (continued)

The Framework provides a recognized baseline against which existing management practices can be documented and assessed to confirm existing sound practices and identify areas for improvement to strengthen an organization's internal control structure and prioritize efforts and resources to the areas of most significance. As a recognized management control framework, an assessment of internal controls against COSO will also serve to provide both internal and external stakeholders with additional confidence in the stewardship, accountability and overall control environment of the organization.

## Accounting Standards Board: Accounting Standards for Government Not-for-Profit Organizations

The Public Sector Accounting Board of Canada is responsible for setting the accounting standards that your organization is required to apply in preparing the general purpose financial statements. The following new or revised accounting standards approved by the Board may have an impact on your financial statements over the next couple of years, as described below. In addition, PSAB has various projects underway which may significantly impact your financial reporting for future fiscal years. We encourage Management to review these standards and projects to determine the impact, if any, on your organization's financial statements.

***<u>Summary of New and Revised Accounting Standards</u>***

PSAB previously issued the following sections that are effective in the Board's 2019 fiscal year or future years:

| Sections | Effective for fiscal years |
|---|---|
| *Restructuring Transactions,* Section 3430 | Beginning on or after April 1, 2018 |
| *Financial Instruments*, Section 3450 *<br>*Portfolio Investments,* Section 3041 *<br>*Foreign Currency Translation,* Section 2601 *<br>*Financial Statement Presentation*, Section 1201 *<br>*(* Must be adopted together)* | Beginning on or after April 1, 2021<br>*For entities who previously applied Part V of CICA Handbook, Accounting – April 1, 2012* |
| *Asset Retirement Obligations,* Section 3280 | April 1, 2021 |
| *Revenues,* Section 3400 | April 1, 2022 |

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The three standards with the most impact on government not-for-profit organizations are summarized on the following pages.

# Appendix 6: Current developments (continued)

**Restructuring Transactions**

This section relates to accounting for assets and liabilities transferred in a restructuring transaction. It also differentiates between an acquisition (where a payment or other consideration approximates the fair value of the net assets) and a restructuring transaction (with little or no consideration rendered, or consideration which is disproportional to the value of assets received). Restructuring transactions differ from a government transfer as restructuring transactions result in the recipient assuming the related program or operating responsibility as opposed to a government transfer, where only a contributed asset is received and accounted for as a contribution.

Assets and liabilities are to be measured at their carrying amount in a restructuring transaction.

The section is effective for years commencing on or after April 1, 2018. Earlier adoption is encouraged.

**Asset Retirement Obligations**

In August 2018, PSAB issued the new standard, Section PS 3280, Asset Retirement Obligations. The new accounting standard addresses the reporting of legal obligations associated with the retirement of certain tangible capital assets such as buildings with asbestos, and solid waste landfill sites by public sector entities. The new accounting standard has resulted in a withdrawal of the existing Section PS 3270, Solid Waste Landfill Closure and Post-Closure Liability.

The new accounting standard proposes similar accounting for asset retirement obligations as in private sector accounting. An asset retirement obligation would be recognized when, as at the financial reporting date, ALL of the following criteria are met:

- there is a legal obligation to incur retirement costs in relation to a tangible capital asset;
- the past transaction or event giving rise to the liability has occurred;
- it is expected that future economic benefits will be given up; and
- a reasonable estimate of the amount can be made.

Public sector entities would be required to capitalize asset retirement obligations associated with fully amortized tangible capital assets, except in the following instances:

- Asset retirement obligations associated with unrecognized tangible capital assets should be expensed;
- Asset retirement obligations associated with tangible capital assets no longer in productive use should be expensed.

The estimate of a liability should include costs directly attributable to asset retirement activities. Costs would include post-retirement operations, maintenance and monitoring that are an integral part of the retirement of the tangible capital asset. Includes costs of tangible capital assets acquired as part of asset retirement activities to the extent those assets have no alternative use.

The new Section is to apply to fiscal years beginning on or after April 1, 2021. Earlier adoption is permitted. This Section may be applied retroactively or prospectively. If retroactive application is selected, a public sector entity may choose to apply certain transitional provisions provided in the Section.

# Appendix 6: Current developments (continued)

**Revenue**

In June 2018, PSAB approved Section PS 3400, Revenue. The final standard is to be released by March 31, 2019.

The framework is focused on two categories of revenue – exchange and unilateral. Transactions which give rise to one or more performance obligations are considered to be exchange transactions. Performance obligations are defined as enforceable promises to provide goods or services to a payer as a result of exchange transactions. Revenue from an exchange transaction would be recognized when the public sector entity has satisfied the performance obligation(s), at a point in time or over a period of time. If no performance obligations are present, the transaction would represent unilateral revenue, and be recognized when the public sector entity has the authority to claim or retain an inflow of economic resources and a past event gives rise to a claim of economic resources.

Excluded from this standard are reporting of contributions and appropriations which continue to be accounted for as government transfers, and tax revenues, interest, dividends, gains and restricted assets.

The proposed new section is expected to apply to fiscal years beginning on or after April 1, 2022, and be accounted for as a change in accounting policy applied retroactively with restatement of prior periods.

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