New Public Sector Accounting Standards in Effect for 2018

A Guide for Municipalities

saskatchewan.ca

Government of Saskatchewan

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Note: This guide has been prepared by Ministry of Government Relations staff for guidance purposes only. It is always advisable to consult with your appointed auditor where necessary.

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Introduction

The Public Sector Accounting Standard Board (PSAB) issued the following Public Sector Accounting Standards (PSAS) that took effect for fiscal years beginning on or after April 1, 2017:

- PS 2200 Related Party Disclosures
- PS 3210 Assets
- PS 3320 Contingent Assets
- PS 3380 Contractual Rights
- PS 3420 Inter-Entity Transactions

For municipalities in Saskatchewan, these standards would apply beginning on January 1, 2018 or the 2018 Financial Statements.

This guide is prepared by Government Relations staff as a high-level summary of the new public sector accounting standards to provide municipal administrators/clerks guidance in preparing their annual financial statements. Sample disclosures have been added within the 2018 financial statement template. The template can be found in the Government of Saskatchewan's website linked **here**.

This guide is not intended to substitute the full extent of the requirements of the new public sector accounting standards contained in the CPA Canada Public Sector Accounting Handbook. Therefore, municipalities are advised to consult with their appointed auditors to assess and determine the applicability of the new sections to their annual financial statements.

Public Sector Accounting Standards Effective 2018

PS 2200 Related Party Disclosure

This Section defines a related party and establishes disclosures required for related party transactions.

What is a related party?

A related party exists when:

- The municipality has the ability to exercise control or shared control over the other party;
- Two or more parties are subject to common control or shared control; or
- Two or more parties share a key management personnel and/or a close family member of key management personnel.

For examples of the most common related parties of a reporting entity refer to PS 2200.07.

What is a related party transaction?

Related party transactions are defined as a transfer of economic resources or obligations between related parties, or the provision of services by one party to a related party. These transfers are related party transactions whether or not there is an exchange of considerations or transactions have been given accounting recognition.

The parties to the transaction are related prior to the transaction. When the relationship arises as a result of the transaction, the transaction is not one between related parties.

When is disclosure of a related party transaction required?

Not all related party relationships or transactions occurring between related parties are required to be disclosed. **Disclosure is generally required when related party transactions have occurred at a value different from that which would have been arrived at if the parties were unrelated (i.e. other than fair value)**.

Some other factors to consider in determining whether information about transactions occurring between related parties would need to be disclosed in the financial statements include, but are not limited to:

- The materiality of the effect the transactions, individually or taken as a whole, have or could have on the municipality's financial position and changes in financial position reported in financial statements; and
- The contribution the information would have to users' understanding of the operating environment and the financial statements of the municipality and comparability with other municipality’s financial statements.

Refer to the decision tree at **Appendix A.**

When does PS 2200 not apply?

PS 2200 does not apply to:

- Restructuring transactions;
- For consolidated financial statements, transactions that are eliminated on consolidation and those with entities accounted for under the modified equity method; and,
- Disclosure of key management personnel compensation arrangements, expense allowances and other similar payments routinely paid in exchange for services rendered.

What information is required to be disclosed?

When it is determined that information about related party transactions needs to be disclosed in the financial statements, this section prescribes the disclosure would include the following:

- Adequate information about the nature of the relationship with the related parties involved in related party transactions;
- The type and amount of related party transactions that have been recognized by financial statement category;
- The basis of measurement used;
- The amount of outstanding balances and the terms and conditions attached to them;
- Contractual obligations and/or contingent liabilities with related parties, separate from other contractual obligations and contingent liabilities; and
- The types of related party transactions that have occurred for which no amount has been recognized.

Items of a similar nature should be disclosed in aggregate.

Sample Disclosure:

Note [#] Related Parties

The consolidated financial statements include transactions with related parties. The municipality is related to [*list related parties*] under the common control of the Council.

[*Select one of the following as applicable*:]

Transactions with these related parties are in the normal course of operations and are settled on normal trade terms.

OR

[*If there are non-arm's length transactions recognized by the municipality at an amount other than normal trade terms during the year use the disclosure below.*]

Certain transactions with the following related parties were settled at an amount other than normal trade terms.

[*For each related party transaction describe:*

- *Adequate information about the nature of the relationship with the related parties involved in related party transactions;*
- *The type and amount of related party transaction that have been recognized by financial statement category;*
- *The basis of measurement used;*
- *The amount of outstanding balances and the terms and conditions attached to them;*
- *Contractual obligations and/or contingent liabilities with related parties separate from other contractual obligations and contingent liabilities;*
- *The types of related party transactions that have occurred for which no amount has been recognized.*

Items of a similar nature should be disclosed in aggregate.]

PS 3210 Assets

This Section establishes general disclosure standards for assets. It does not include standards for recognition and disclosure of specific types of assets, which are dealt with in other public sector accounting standards sections.

What is an asset?

Assets are economic resources controlled by a municipality as a result of past transactions or events and from which future economic benefits are expected to be obtained. An asset has three essential characteristics:

- They represent future economic benefits that involve a capacity, singly or in combination with other assets, to provide goods and services, to provide future cash inflows, or to reduce cash outflows;
- The municipality can control the economic resource and access to the future economic benefits; and
- The transaction or event giving rise to the municipality's control has already occurred.

What is an economic resource?

Economic resources represent value because they enable a municipality to meet its objectives. To embody value as an economic resource there must be some restriction on an economic resource's availability.

- Economic resources can arise from, but are not limited to:
- Contracts or agreements;
- Another government's legislation;
- A government's own legislation;
- Voluntary contributions; or
- Construction and development.

When would an asset not be recognized in the financial statements?

There are two possible reasons why an economic resource that meets the definition of an asset would not be recognized:

- An appropriate basis of measurement and a reasonable estimate of the amount involved cannot be made; or
- Other Public Sector Accounting Board Handbook sections prohibit recognition (example: intangible assets, inherited Crown land, historical treasures, etc.)

What information should be disclosed when an asset is not recognized?

Information about the major categories of unrecognized assets should be disclosed in the notes to the financial statements. When an asset is not recognized because a reasonable estimate of the amount involved cannot be made, the reason(s) for this must be disclosed.

Appendix B includes a decision tree on economic resources and the relationship and differences between Assets (PS 3210), Contingent Assets (PS 3320), and Contractual Rights (PS 3380).

PS 3320 Contingent Assets

This Section defines a contingent asset and establishes disclosures required of likely contingent assets

What is a contingent asset?

Contingent assets are possible assets arising from existing conditions or situations involving uncertainty. That uncertainty will ultimately be resolved when one or more future events not wholly within the municipality's control occurs or fails to occur. Resolution of the uncertainty will confirm the existence or non-existence of an asset.

Contingent assets are distinct from assets since there is a degree of uncertainty as to whether an asset exists at the financial statement date.

The most common form of a contingent asset is possible litigation proceeds.

What are the characteristics of a contingent asset?

Contingent assets have two basic characteristics:

- There is an existing **condition or situation that is unresolved** at the financial statement date that indicates there may be an asset; and
- There is an **expected future event that will resolve the uncertainty** as to whether an asset exists at year end (the future event proves or disproves the existence of the asset).

When is disclosure of a contingent asset required?

A contingent asset is allowed to be disclosed only if it reduces the amount accrued for a related contingent liability and the probability of recovery is likely. Otherwise, a contingent asset is not recognized.

Information on the existence, nature, and extent of a contingent asset is disclosed in the notes to the financial statements when the confirming event is likely and material.

The following range of probabilities express the uncertainty relating to the occurrence or non-occurrence of the future event confirming that an asset existed at the financial statement date:

- **Likely** – the probability of the occurrence/non-occurrence of the future event is high;
- **Unlikely** – the probability of the occurrence/non-occurrence of the future event is slight; and,
- **Not determinable** – the probability of the occurrence/non-occurrence of the future event cannot be determined.

Assessing the likelihood of the future confirming event occurring, and estimating its financial effects are matters for judgment by those responsible for preparing the financial statements. In identifying contingent assets and determining their amount, consideration would be given to all information available prior to completion of the financial statements, supplemented by experience in similar transactions and, in some cases, reports from independent experts.

What information is required to be disclosed?

The disclosure of the contingent asset should include:

- The nature;
- The extent, except where the extent cannot be measured or disclosure of the extent would have an adverse effect on the outcome;
- The reason(s) for any non-disclosure of the extent; and,
- When an estimate of the amount has been made, the basis for the estimate.

Sample Disclosure:

Note [#] Contingent Assets

The municipality has the following contingent asset(s) for which the probability of [*future event that would result in the asset(s)*] occurring is likely, resulting in [*describe the nature of the contingent asset*] where the estimated or known assets are, or exceed [*$*] at December 31 [*current year*] ([*prior year: $*]). The future receipt of these assets is dependent on [*describe nature of future event that will confirm existence of asset*]. [*When the disclosed amount is based on an estimate, explain basis of estimation*].

Contingent assets are not recorded in the financial statements.

(OR, in cases where the extent cannot be measured or when disclosure of the extent would have an adverse effect on the outcome, consider the following)

The municipality has the following contingent asset(s) for which the probability of [*future event that would result in the asset(s)*] occurring is likely, resulting *in* [*describe the nature of the contingent asset*]. The future receipt of these assets is dependent on [*describe nature of future event that will confirm existence of asset*]. [*Describe the reason for non-disclosure of the extent of the contingent asset*].

Contingent assets are not recorded in the financial statements.

PS 3380 Contractual Rights

This section defines and establishes financial statement disclosure standards on how to report contractual rights a municipality may have.

What are contractual rights?

Contractual rights are rights to economic resources arising from a legally binding contract or agreement between the municipality and another party(ies) that has been signed and that will result in both an asset and revenue in the future, when the terms of the contract or agreement are met. They may include, but are not limited to, rights to receive payments under a shared cost agreement or rights to receive lease payments.

How are contractual rights different from assets?

Contractual rights are distinct from assets because there has been no past transaction or event giving rise to an asset at the financial statement date. Until a transaction or event occurs under a contract or agreement, an entity only has a contractual right to an economic resource. Once the entity has received an asset, it no longer has a contractual right.

How are contractual rights different from contingent assets?

Contractual rights are distinct from contingent assets as there is no uncertainty related to the existence of the contractual right. Once the terms of the contract or agreement are met, the contractual right will give rise to an asset and a revenue.

Appendix B includes a decision tree on economic resources and the relationship and differences between Assets (PS 3210), Contingent Assets (PS 3320), and Contractual Rights (PS 3380).

When are contractual rights required to be disclosed?

Factors to consider when determining which contractual rights should be disclosed are:

- Contractual rights to revenue that are abnormal in relation to the financial position or usual business operations; and
- Contractual rights that will govern the level of certain types of revenue for a considerable period into the future.

PSAB limited the definition of contractual rights to those rights that will become assets and will result in revenue in the future when the terms of the contracts or agreements are met. Thus, disclosure of contractual rights is required only when the contract/agreement results in additional resources becoming available for the organization.

For an illustrative example refer to **Appendix D**.

When are contractual rights not required to be disclosed?

Disclosure is not required when:

- There is simply an exchange of one resource for another. For example, Town A has an agreement to sell a truck at its' carrying value in the future to Town B. This would not meet the definition of a contractual right because the sale would not result in additional resources to Town A. It is just an exchange of one economic resource (i.e. cash) for another economic resource (i.e. the truck).
- The right arises from legislation, such as the right to license or to tax, and does not arise from a contract. For example, a municipality has the right to collect taxes from individuals in the future. In the future, there will be both an asset (i.e. cash) and revenue (i.e. tax revenue). However, since the right to collect taxes arises from legislation and does not arise from contracts with each individual owing tax, future tax revenue would not be considered a contractual right for the municipality.

The limited definition of contractual rights provides a practical limit on the types of contractual rights that will have to be disclosed.

What information is required to be disclosed?

PS 3380 is a disclosure standard only, meaning that information about material contractual rights is to be disclosed in the notes or schedule to the financial statements and it should include descriptions about their nature and extent and the timing.

Sample Disclosure:

Note # Contractual Rights

Contractual rights are rights to economic resources arising from contracts or agreements that will result in an asset and revenue in the future. Significant contractual rights of the municipality are as follows:

Contractual Rights Type	Describe Nature Time and Extent	2018	2019	2020	2021	2022	Thereafter	No Fixed Maturity Date	Current Year Total	Prior Year Total
[*i.e. future lease Revenue]*		[$]	[$]	[$]	[$]	[$]	[$]	[$]	[$]	[$]
Contractual Rights 1										
Contractual Rights 2										
Contractual Rights 3										
[Other Specify]										
Total										

PS 3420 Inter-entity Transactions

This section establishes standards on how to account for and report transactions between public sector entities that comprise a government's reporting entity from both a provider and recipient perspective.

What are inter-entity transactions?

Inter-entity transactions are those transactions occurring between commonly controlled entities.

What is a commonly controlled entity?

Commonly controlled entities are all public sector entities that comprise a government's reporting entity as outlined in PS 1300 Government Reporting Entity.

When should an inter-entity transaction be recognized and by whom?

- Transfer of assets or liabilities -
  Inter-entity transactions involving the transfer of assets or liabilities should be recognized by both the provider and the recipient.
    - Provider: removes the assets or liabilities from its financial statements and any difference between the net proceeds received and the carrying amounts transferred is accounted for as a revenue or expense in the statement of operations.
    - Recipient: recognizes assets or liabilities in its financial statements when the items satisfy the definition and recognition criteria for an asset and liability in PS 1000 Financial Statement Concepts.
- Cost allocation and recovery-
  When there is a policy of cost allocation and recovery for the provision of goods and services:
    - Provider: reports all revenues and expenses on a gross basis.
    - Recipient: reports expenses on a gross basis.
- Unallocated costs-
  When there is no policy for allocating costs for the provision of goods and services:
    - Recipient: may choose to recognize these costs when they would otherwise have been purchased and a reasonable estimate of the amount involved can be made. These items are reported as revenues and expenses.

Refer to the decision tree at **Appendix C.**

At what value should an inter-entity transaction be recorded?

Inter-entity transactions should be recorded at the carrying amount as determined at the transaction date.

Exceptions:

- Transactions are undertaken on similar terms and conditions to those adopted if the entities were dealing at arm's length;
    - In which case inter-entity transactions should be recorded at the exchange amount when they are undertaken on similar terms and conditions to those adopted if the entities were dealing at arm's length.
    - Examples of transactions on similar terms and conditions to those adopted if the entities were dealing at arm's length may include the sale and purchase of utilities and the sale or purchase of an inventory item.
- Assets or liabilities are transferred for nominal or no consideration;
    - In which case inter-entity transactions should be measured at the carrying amount by the provider and at the carrying amount or fair value by the recipient. This does not require symmetrical accounting by the provider and recipient.
- Transactions are allocated costs and recoveries;
    - In which case inter-entity transactions should be measured at the exchange amount.

  OR

- Transactions are unallocated costs.
    - In which case, when recognized by the recipient, unallocated costs should be measured at the carrying amount or fair value unless policy, budget practices or accountability structures dictate otherwise.

When there is a difference between the exchange amount and the carrying amount of a transferred or exchanged asset or liability, a gain or loss should be reported in the statement of operations.

Related Definitions:

Carrying amount – the amount of an item transferred, or cost of services provided, as recorded in the accounts of the provider, after adjustments, if any, such as for amortization, impairment or changes in the fair value.

- For a tangible capital asset, the carrying amount is the net of cost and accumulated amortization.
- For other assets, the carrying amount may be the net of cost and valuation allowances or fair value, as appropriate.

Cost allocation and recovery – the allocation of costs of activities associated with providing goods or services to another entity and the recovery of the costs incurred from the other entities. Recoveries between entities may be a direct exchange of consideration or an accounting entry.

Exchange amount – the amount of the consideration given for the item transferred or service provided as established and agreed to by the related parties.

Fair value – the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable and willing parties who are under no compulsion to act.

Unallocated costs – the cost of resources recorded by the providing entity in its operating activities that are incurred on behalf of a recipient entity.

What information is required to be disclosed?

Inter-entity transactions are related party transactions. As such, an entity discloses information about inter-entity transactions, whether or not those transactions were given accounting recognitions, in accordance with the requirements of PS 2200, Related Party Disclosures.

Disclosures should include:

- the nature of the relationship with the related party involved;
- the type of inter-entity transactions that have been recognized;
- the amounts recognized classified by financial statement category;
- the basis of measurement used;
- the amounts outstanding attached to them; and
- the types of inter-entity transactions for which no amount has been recognized.

When does PS 3420 <u>not</u> apply?

PS 3420 does not apply to:

- Restructuring transactions;
- Transactions between a partner and a government partnership (PS 3060).

Sample Disclosure:

Note [#] Inter-entity Transactions

This standard has no impact on the consolidated financial statements.

OR

Inter-entity disclosures are included with Note # Related Party Transactions.

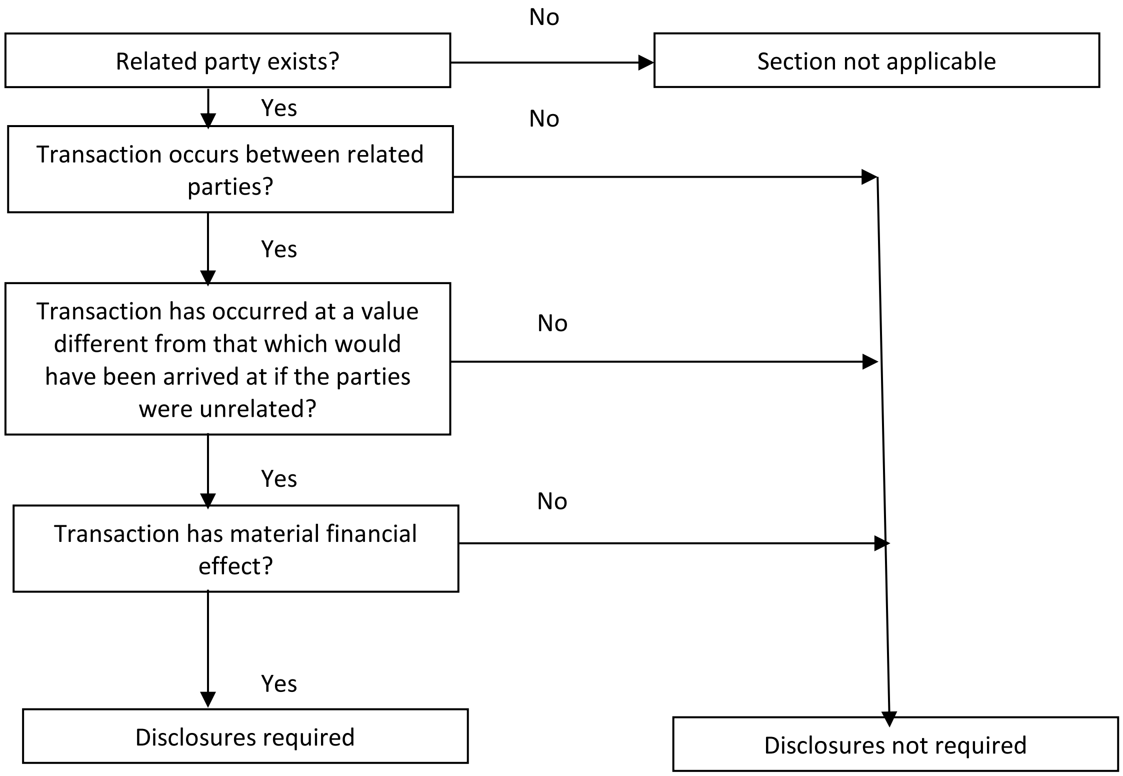
Resources

- CPA Canada Public Sector Accounting Handbook
- CPA Canada Public Sector Accounting Handbook Basis for Conclusion for each section
- "PSAB at a Glance", BDO Canada
- "2017-18 Financial Reporting Manual for School Divisions", Ministry of Education, Saskatchewan
- "User Guide PS 3380 Contractual Rights", Ministry of Education, Saskatchewan
- "Province of Saskatchewan General Revenue Fund 2017-18 Year-end Reporting Requirements and Procedures"

Appendices

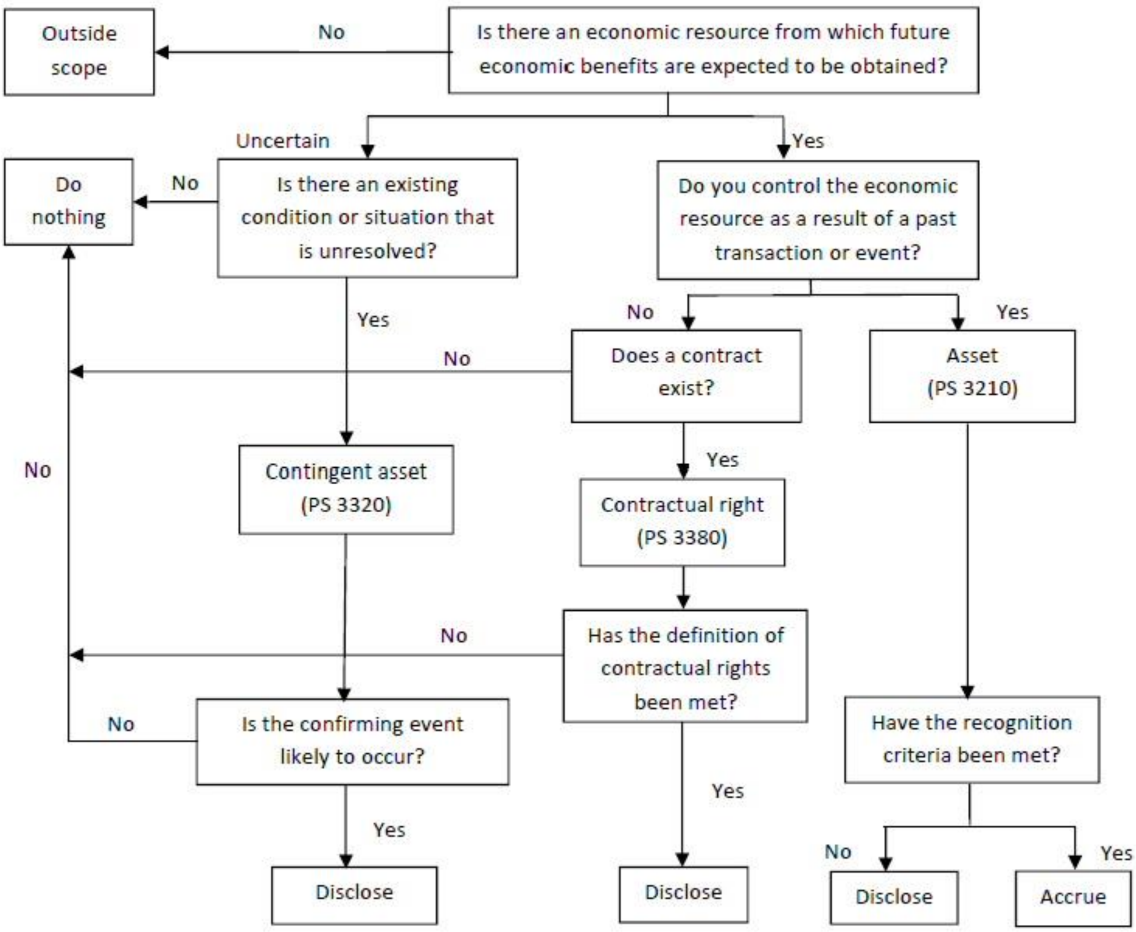
Appendix A: Decision Tree - Related Party Disclosures

The following decision tree has been prepared to illustrate the accounting treatment specified in PS 2200 Related Party Disclosures. The decision tree is illustrative only and matters of principle relating to particular situations should be decided in the context of the section.



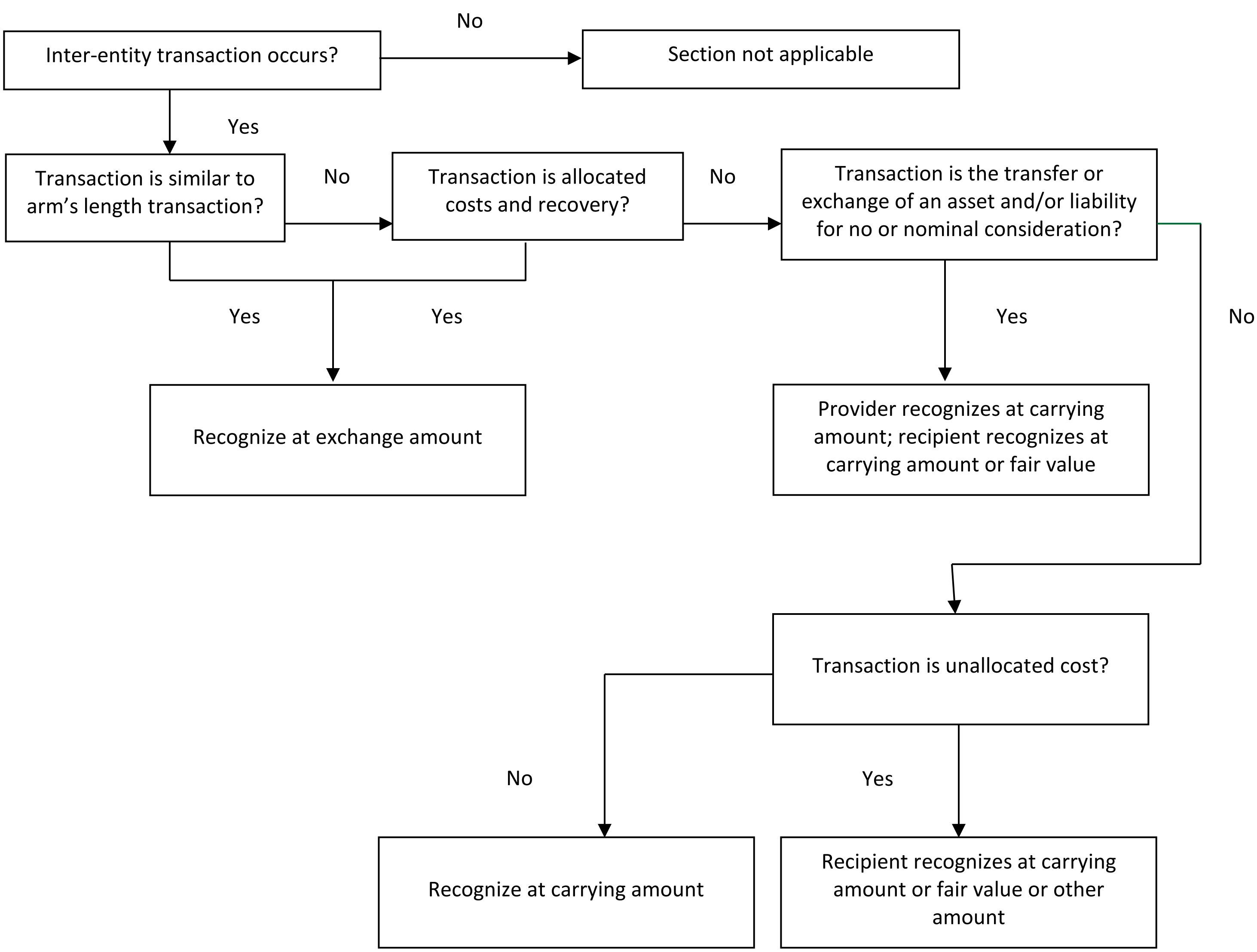
Appendix B: Decision Tree - Economic Resources

The following decision tree has been prepared to illustrate the accounting treatment specified in PS 3210 Assets and the relationship between Assets, Contingent Assets and Contractual Rights. The decision tree is illustrative only and matters of principle relating to particular situations should be decided in the context of the applicable sections.



Appendix C: Decision Tree - Accounting for Inter-entity Transactions

The following decision tree has been prepared to illustrate the accounting treatment specified in PS 3420 Inter-entity Transactions. The decision tree is illustrative only and matters of principle relating to particular situations should be decided in the context of the section.



Appendix D: Illustrative Example - Contractual Rights

Facts:

- The Federal Government of Canada and the Provincial Government of Saskatchewan have signed a cost-sharing agreement with Municipality A. Terms of the agreement are as follows:
- Municipality A will construct a new water treatment plant, with total eligible costs of the project expected to be $6 million.
- The Federal and Provincial Governments each agree to pay for 33% of the costs ($2 million for each party to the agreement).
- Municipality A must incur eligible costs to qualify for the reimbursement from the Federal and Provincial Governments.
- An agreement is signed September 1, 2018 with work expected to begin January 1, 2019 and to be completed by the end of December 31, 2019.
- Municipality A's normal business operations do not include building water treatment plants.

Questions to answer to determine if a contractual right exists:

Question	In this case – response
1. Is there a contract/agreement?	Yes *(If the answer was 'no', no need to proceed further as no contractual right)*
2. Will the contract/agreement give rise to economic resources to the municipality in the future?	Yes (*Economic resources are resources that embody value and are capable of being used to achieve objectives, generate cash inflows or reduce cash outflows. Economic resources can be financial in nature (i.e. cash) or non-financial in nature (i.e. tangible capital assets). The municipality expects to receive cash (i.e. economic resource) in the future when it begins and ultimately completes the construction of the water treatment plant, at which point the Federal and Provincial Governments will reimburse the municipality $4 million.*
3. Does the municipality control the economic resource as a result of a past transaction or event (t/e)?	*It is December 31, 2018 – the agreement is signed and is dated September 1, 2018. This means the transfers from the two governments have been authorized; however as of December 31, 2018 there has been no past t/e giving rise to an asset. This past t/e doesn't occur until the municipality begins construction of the water treatment plant (i.e. incurs eligible costs). As of December 31, 2018, a contract exists and the definition of a contractual right has been met since the municipality has a right to the $4 million in the future when it incurs eligible costs and this right arises from an agreement. Also, the right will result in both an asset (i.e. cash) and revenue (i.e. transfer revenue) in the future when the municipality builds the water treatment plant.*
4. Is this transfer revenue abnormal in relation to the municipality's usual business operations?	*Yes, the transfer revenue would be considered abnormal since the municipality's normal business operations do not include building water treatment plants.*
5. Do the agreements with the Federal and Provincial Government govern the level of specific revenue for a considerable period into the future for the municipality?	*No, the water treatment plant construction is expected to begin on January 1, 2019 and the work is expected to be completed within one year.* Note: It only takes one of these factors to support a decision to provide disclosure.

Conclusion:

The Public Sector Accounting Standard provides factors that should be considered when determining what contractual rights should be disclosed. The municipality went through the factors. Although the agreement does not govern the level of specific revenue for a considerable period into the future, the municipality uses professional judgment and concludes that the contractual right should be disclosed as it is for a significant amount of $4 million.