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PUBLIC SECTOR  
ACCOUNTING BOARD



CONSEIL SUR  
LA COMPTABILITÉ  
DANS LE SECTEUR  
PUBLIC

# Withdrawal of Disclosure of Related Party Transactions by Not-for-Profit Organizations, Section PS 4260

## **Basis for Conclusions**

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**Section PS 4260**

**CPA Canada Public Sector Accounting Handbook**

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*Prepared by the staff of the Public Sector Accounting Board*

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## Foreword

CPA Canada Public Sector Accounting Handbook Revisions Release No. 45, issued in December 2016, covered the withdrawal of DISCLOSURE OF RELATED PARTY TRANSACTIONS BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4260.

The primary objective of a Basis for Conclusions document is to set out how the Public Sector Accounting Board (PSAB) reached its conclusions. As well, it sets out significant matters arising from comments received in response to the proposals exposed and indicates how PSAB has dealt with the issues raised.

These documents are intended to assist financial statement users, preparers, auditors and other parties interested in public sector financial reporting in understanding the rationale followed by PSAB when developing standards.

This document has been prepared by staff of PSAB. It does not form part of the CPA Canada Public Sector Accounting (PSA) Handbook nor is it part of public sector generally accepted accounting principles (GAAP). Basis for Conclusions documents also do not include any guidance on the application of the relevant Section or Guideline.

December 2016

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## BACKGROUND

- 1 In March 2015, Public Sector Accounting Board (PSAB) issued a new standard, RELATED PARTY DISCLOSURES, Section PS 2200. These new disclosure requirements were very similar to those set out in DISCLOSURE OF RELATED PARTY TRANSACTIONS BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4260. However, the major difference between the two Sections was that Section PS 2200 does not include the notion of significant influence or economic interest.
- 2 Principle 12 of the Accounting Standards Board (AcSB) and PSAB jointly prepared Statement of Principles, “Improvements to Not-for-Profit Standards,” issued in April 2013, stated that a not-for-profit organization applying the CPA Canada Public Sector (PSA) Handbook including Sections PS 4200 to PS 4270 (the PS 4200 series) should continue to apply Section PS 4260, pending completion of PSAB’s Related Party Transactions project. Respondents were generally supportive of the proposed principle, noting that related party transactions should be accounted for consistently by public sector entities. Some respondents did express concern regarding the applicability of significant influence and economic interest in the public sector. It was noted that these concepts might be too broad to apply.
- 3 In January 2016, PSAB issued an Exposure Draft proposing the withdrawal of Section PS 4260. PSAB thought that the disclosure requirements set out in RELATED PARTY DISCLOSURES, Section PS 2200, together with the disclosure requirements related to significant influence and economic interest set out in REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250, would be sufficient for those entities that apply the PS 4200 series. The withdrawal of Section PS 4260 would not significantly impact current reporting practices.

## SIGNIFICANT INFLUENCE

- 4 Section PS 4260 defined the term “significant influence” as the ability to affect the strategic operating, investing and financing policies of the entity. The Basis for Conclusions issued for RELATED PARTY DISCLOSURES, Section PS 2200, notes that PSAB determined that a related party does not include entities that have significant influence over, or are subject to the significant influence of, another entity because public sector entities have wide-ranging powers that would typically allow them to exert significant influence over the operating and financial policies of a broad range of parties in all sectors of the economy.
- 5 For those not-for-profit organizations that adopted the PSA Handbook with the PS 4200 series, guidance regarding significant influence is available in REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250.

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- 6 Some respondents to the Exposure Draft raised concerns regarding the title of Section PS 4250. In particular, it was noted that Section PS 4250 pertained to related entities. The concern was that under RELATED PARTY DISCLOSURES, Section PS 2200, the definition of a related party does not include those entities in which a significant influence or economic interest exists. Some confusion may result as those entities following the PS 4200 series may be uncertain as to whether Section PS 4250 is applicable.
  - 7 Acknowledging the concerns of respondents, a footnote was added to the definition of a related party in RELATED PARTY DISCLOSURES, Section PS 2200. The footnote states that for those not-for-profit organizations that apply the PSA Handbook with the PS 4200 series, a related party would also include when one party has significant influence over the other, when two or more parties are subject to common significant influence, or when a not-for-profit organization has an economic interest in another not-for-profit organization. A reference to REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250, is also provided for additional information.

## **ECONOMIC INTEREST**

- 8 Section PS 4260 stated that an economic interest in another not-for-profit organization exists if the other organization holds resources that must be used to produce revenue or provide services for the reporting organization or the reporting organization is responsible for the liabilities of the other organization. In the public sector, particularly for governments, this is a difficult concept to apply given that governments, through their transfer programs and legislative requirements, will direct the use of certain funds or guarantee the liabilities of non-controlled entities. Consequently, for reasons similar to why the concept of significant influence was not included for related party disclosures, the notion of economic interest was also not included.
- 9 As a few of the respondents to the Statement of Principles noted, the concept of economic interest might be too broad for governments but useful for government organizations. For example, hospital foundations provide significant funding to hospitals but are often considered to be outside the control of the hospital itself. Currently, hospitals do provide disclosures about the nature of the relationship with their foundations because they represent an economic interest.
- 10 For those not-for-profit organizations that adopted the PSA Handbook with the PS 4200 series, guidance regarding economic interest is available in REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250.
- 11 The same issue as noted above regarding significant influence would pertain to economic interest. To address the concerns and try to alleviate any confusion, the footnote added to the definition of a related party in RELATED PARTY

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DISCLOSURES, Section PS 2200, would also include reference to when a not-for-profit organization has an economic interest in another not-for-profit organization.

- 12 The intent of the proposals, for those not-for-profit organizations that apply the PS 4200 series, was to retain the disclosures currently reported by not-for-profit organizations when there is significant influence or an economic interest in another entity. This was to be achieved by applying the guidance found in REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250, by those not-for-profit organizations that apply the PS 4200 series.

## **MATERIALITY**

- 13 Section PS 2200 requires that only those transactions that have or could have a material financial effect on the financial statements be disclosed. This differs from the requirements in Section PS 4260 that is generally understood to require disclosure of all related party transactions unless clearly immaterial.
- 14 PSAB believes there no compelling reason to require government not-for-profit organizations to make more extensive disclosures than other government organizations.

## **TERMINOLOGY DIFFERENCES**

- 15 The Issues Analysis that accompanied the Exposure Draft recognized that while some minor terminology differences exist between RELATED PARTY DISCLOSURES, Section PS 2200, and Section PS 4260, the basic intent of each Section is the same.
- 16 Agreeing that the basic intent was the same, some respondents still thought the differences may cause confusion. This may be evident when an entity following the PS 4200 series tries to apply REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250. Section PS 4250 contains the same terms used in Section PS 4260.
- 17 Acknowledging respondents concerns, the definitions in REPORTING CONTROLLED AND RELATED ENTITIES BY NOT-FOR-PROFIT ORGANIZATIONS, Section PS 4250, were amended to be consistent with those in RELATED PARTY DISCLOSURES, Section PS 2200.

## **TRANSITIONAL PROVISIONS**

- 18 The Exposure Draft proposed an amendment to the transitional provisions of RELATED PARTY DISCLOSURES, Section PS 2200, that would grant not-for-profit organizations that apply the PS 4200 series an extension of one year to the effective date. Those respondents that commented noted that these not-for-profit organizations are already disclosing related party information and additional time would not be required. Therefore, PSAB decided that no amendment to the transitional provisions is needed.

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