14.3 Non-Monetary Related Party Transactions

Policy Statement

It is the policy of the Province of Nova Scotia to account for non-monetary related party transactions in accordance with Canadian public sector accounting standards (PSAS).

Definitions

CARRYING AMOUNT

Carrying amount is the value of an item as recorded in the accounts of the Province, after adjustments, if any, for amortization or impairment in value. For a tangible capital asset, the carrying amount is the net book value (cost less accumulated amortization).

EXCHANGE AMOUNT

Exchange amount is the amount of consideration paid or received as established and agreed to by related parties. The exchange amount reflects the actual amount of the consideration given for the item transferred.

FAIR VALUE

Fair value is the amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. It is essentially market price.

MONETARY ASSETS AND LIABILITIES

Monetary assets and liabilities are money or claims to future cash flows that are fixed or determinable in amounts and timing by contract or other arrangement. Examples include cash, accounts and notes receivable in cash and accounts and notes payable in cash.

NON-MONETARY ASSETS AND LIABILITIES

Non-monetary assets and liabilities are assets and liabilities that are not monetary. Inventories, investments in common stock, tangible capital assets and liabilities for rent collected in advance are examples of non-monetary assets and liabilities.

Non-monetary transactions are either:

(i) Non-monetary Exchanges
When non-monetary assets and liabilities are exchanged for other non-monetary assets and liabilities with little or no monetary consideration involved; or

(ii) Non-monetary Non-reciprocal Transfers
When non-monetary assets and liabilities are transferred without any consideration given in return. Donations of tangible capital assets are an example of non-monetary non-reciprocal transfers.

RELATED PARTIES

Related parties exist when one party has the ability to exercise, directly or indirectly, control or shared control over the other. Two or more parties are related when they are subject to common control or shared control. The Province and the entities within the Government Reporting Entity (GRE) are related parties as the Province has the ability to exercise control over the other entities within the GRE. As well, the entities within the GRE are related parties (e.g., a health authority and a regional centre for education) as they are subject to common control of the Province.

RELATED PARTY TRANSACTION

A related party transaction is a transfer of economic resources or obligations between related parties, or the provision of services by one party to a related party, regardless of whether any consideration is exchanged. The parties to the transaction are related prior to the transaction.

TANGIBLE CAPITAL ASSET

A tangible capital asset (TCA) is a non-financial asset that is purchased, constructed, or developed and:

i. is held for use in the production or supply of goods and services, for rental to others, for administrative purposes or for development, construction, maintenance, or repair of other capital assets;
ii. requires operating and maintenance expenditures and may need to be replaced in the future;
iii. has a useful life extending beyond an accounting period and is intended to be used on a continuing basis; and,
iv. is not intended for sale in the ordinary course of operations.

Policy Objectives

The objective of this policy is to ensure non-monetary related party transactions are accounted for appropriately and accurately.

Application

This policy applies to the Province's departments and public service units contained in the General Revenue Fund (hereinafter referred to as "departments").

Organizations outside of the General Revenue Fund but within the Government Reporting Entity[1] are encouraged to adopt a policy that allows for the accurate and consistent reporting of non-monetary transaction. This policy should comply with the entity's generally accepted accounting framework. It is recognized that many entities may already have an appropriate policy in place.

Policy Directives

MEASUREMENT

Generally, a non-monetary related party transaction is measured at the carrying amount (i.e., book value).

However, a non-monetary related party transaction is measured at the exchange amount in the following two situations:

1. if the transaction has commercial substance and is in the normal course of operations (unless the transaction is in the normal course of operations and the transaction will facilitate sales to other customers, other than the parties to the exchange); or
2. if the transaction has commercial substance and is not in the normal course of operations, and:
    i) the change in the ownership interests in the item transferred is substantive; and
    ii) the exchange amount is supported by independent evidence.

A change in the ownership interests in an item transferred is presumed to be substantive when a transaction results in unrelated parties having acquired or given up at least 20 percent of the ownership interests in the item.

1 For definition, see Corporate Administrative Policy Manual #200, Chapter 4.1 Government Reporting Entity.

COMMERCIAL SUBSTANCE

An entity determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows or service potential is expected to change as a result of the transaction. A non-monetary exchange transaction has commercial substance if:

- the risk, timing, or amount of the future cash flows or service potential of the asset received differs from that of the asset given up (e.g., from the asset received may be better suited for school construction than the asset given up); or
- the entity-specific value of the portion of the entity's operations affected by the transaction changes as a result of the exchange, and the difference is significant relative to the fair value of the assets exchanged (e.g., realization of cost savings; realization of additional revenues, ability to launch a new program).

The term "entity-specific value" is a measure of the value of an asset in the context of the entity owning the asset. It includes all of the cash flow effects of a transaction on the entire entity. The entity uses its expectations about its use of the asset rather than the use assumed by marketplace participants. More precisely, entity-specific value is the present value of the cash flows an entity expects to arise from the continuing use of an asset and from its disposal at the end of its useful life, or expects to incur when settling a liability.

NORMAL COURSE OF OPERATIONS

When determining whether the operations are normal, the following matters should be taken into account: type and scope of operations, characteristics of the industry, operating policies of the enterprise, nature of products and services, and the environment in which the enterprise operates.

Examples of transactions in the normal course of operations are: the sale or purchase of an inventory item, the provision or receipt of a recurring service including management and administrative services commonly shared by related parties, a lending activity undertaken by a financial institution, a sale or purchase of real estate by an enterprise that is in the business of selling real estate as part of its ongoing activities, and recurring investing activities by an investment company.

A related party transaction is presumed not to be in the normal course of operations when it is not of a type that is usually, frequently or regularly undertaken by the enterprise for the purpose of generating revenue. The sale or purchase of capital assets is an example of transactions not in the normal course of operations. A transaction involving the sale or purchase of assets that were not acquired for resale is also not in the normal course of operations.

DONATIONS – DEPARTMENTAL GRANT EXPENSE

In order to properly reflect the decrease in resources, donations of tangible capital assets by the Province are recorded by departments of the General Revenue Fund as departmental grant expenses (i.e., a donation in lieu of a grant). The amount of departmental grant expense to be recorded is measured as per the above Measurement section. Disposal costs such as legal fees and selling commissions for donated tangible capital assets are recorded as an operating expense, and are not netted against the gain or loss from disposal.

WRITE-DOWNS – DEPARTMENTAL OPERATING EXPENSE

Policy 14.1 Tangible Capital Assets states:

> "The net book value of a tangible capital asset is to be written down when conditions indicate the tangible capital asset no longer contributes to the government's ability to provide services or the future economic benefits are less than the net book value. Write-downs are not to be reversed. The amount of the write-down represents a charge against the department's budget appropriation."

Policy Guidelines

Each non-monetary related party transaction should be evaluated on an independent basis and the determination of the appropriate accounting treatment for each transaction requires the use of professional judgement. See examples described in Appendix 14-G.

Accountability

The process of accounting for and reporting non-monetary transactions is shared among and requires the collaboration of the following divisions within Finance and Treasury Board:

Financial Advisory Services (FAS) working with departmental representatives

- responsible for identifying, assessing, and tracking non-monetary transactions as well as ensuring that these non-monetary transactions are accounted for appropriately and completely, supported by sufficient audit evidence

- responding to Government Accounting inquiries regarding non-monetary transactions
- providing the Auditor General with the evidence requested for the audit of non-monetary transactions

Government Accounting

- responsible for providing guidance and advice relating to the appropriate accounting treatment for non-monetary transactions
- liaising with departments and the Auditor General, as needed
- updating this policy, periodically, in consultation with departments

Monitoring

Government Accounting will monitor the policy's implementation, performance, and effectiveness.

References

- Public Sector Accounting Standards, PS 2200 Related Party Disclosures
- International Public Sector Accounting Standards, IPSAS-17 Property, Plant, and Equipment
- Accounting Standards for Private Enterprises (ASPE), CPA Canada Handbook, Section 3840 Related Party Transactions
- Policy 14.1 Tangible Capital Assets Policy

Appendices

Appendix 14-F	Non-monetary Related Party Transactions Decision Tree
Appendix 14-G	Examples

Enquiries

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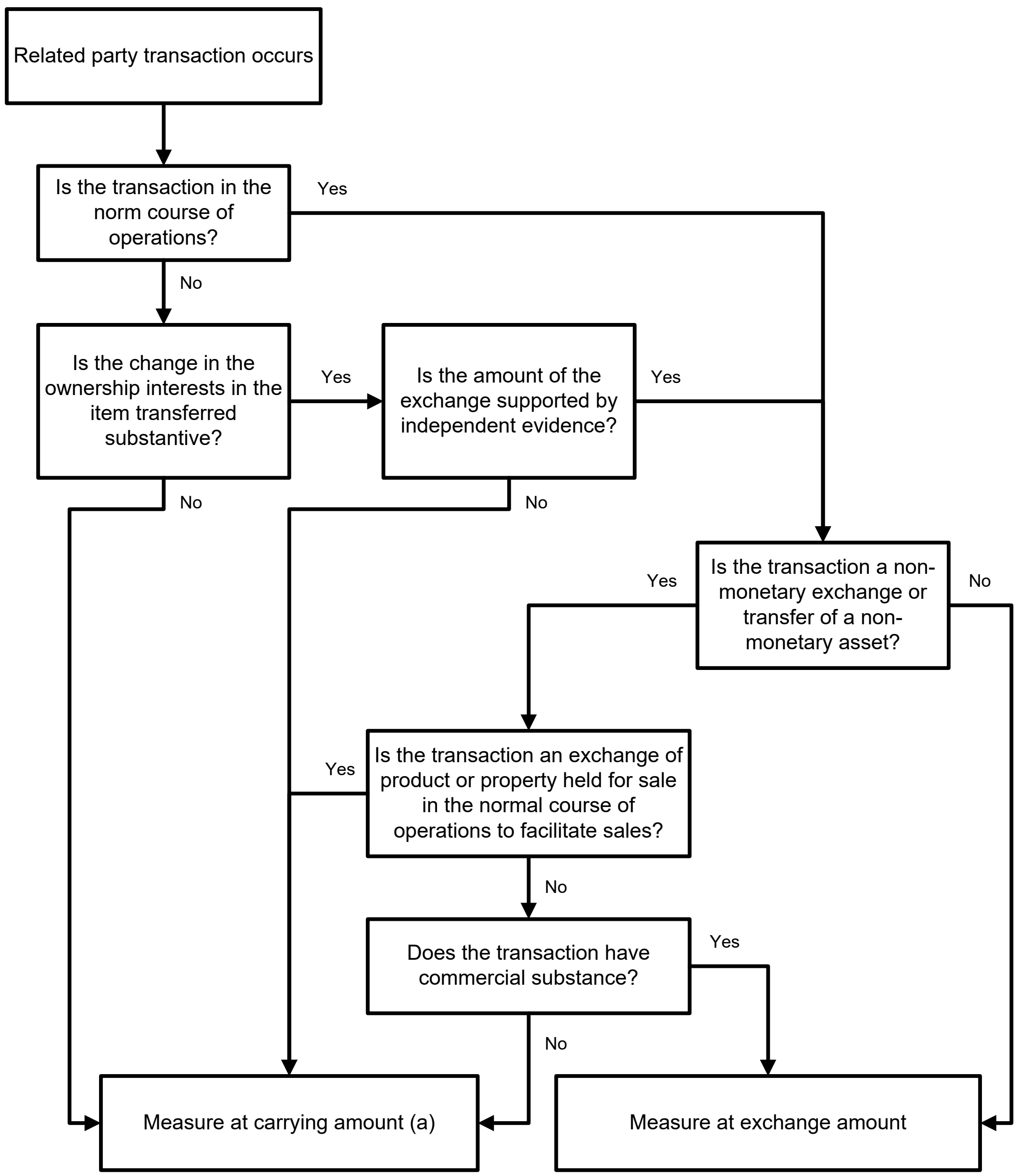
Appendix 14-F

Decision tree

The following decision tree is provided for illustrative purposes.



(a) In rare circumstances, when the carrying amount of the item received is not available, a reasonable estimate of the carrying amount, based on the transferor's original cost, may be used to measure the exchange.

Appendix 14-G

Examples

The following examples demonstrate the appropriate accounting treatment for non-monetary related party transactions in a variety of circumstances.

Example 1

EXCHANGE OF TCA

A department of the General Revenue Fund exchanges a vehicle with a carrying value of $20,000 with an entity within the GRE for a piece of major equipment with a carrying value of $25,000. The department determines the transaction is <u>not</u> within the normal course of operations. In addition, the change in the ownership interests in the property transferred is not substantive. As a result, the transaction should be measured at the carrying amount. The department would record the exchange as follows:

Debit:	TCA-Major Equipment	$25,000
Credit:	TCA-Motor Vehicles	($20,000)
Credit:	Gain on Disposal of Assets	($5,000)

The other related party entity would record the transfer as follows:

Debit:	TCA-Motor Vehicles	$20,000
Debit:	Loss on Disposal of Assets	$5,000
Credit:	TCA-Major Equipment	($25,000)

In preparation of the consolidated financial statements, the following elimination entry would be processed:

Debit:	Gain on Disposal of Assets	$5,000
Credit:	Loss on Disposal of Assets	($5,000)

Example 2

DONATION OF TCA - DEPARTMENTAL GRANT EXPENSE

A department of the General Revenue Fund donates property including land and buildings to an entity within the GRE for a nominal value of $1. The carrying amount of the land is $351,000 and the carrying amount of the buildings is $1,400,000. The department determines the transaction is <u>not</u> within the normal course of operations. In addition, the change in the ownership interests in the property transferred is not substantive. As a result, the transaction should be measured at the carrying amount. The department would record the transfer as follows:

Debit:	Cash	$1
Debit:	Departmental Grant Expense	$1,750,999
Credit:	TCA-Land	($351,000)
Credit:	TCA-Buildings	($1,400,000)

The other related party entity would record the transfer as follows:

Debit:	TCA-Land	$351,000
Debit:	TCA-Buildings	$1,400,000
Credit:	Grant Revenue	($1,750,999)
Credit:	Cash	($1)

In preparation of the consolidated financial statements, the following elimination entry would be processed:

Debit:	Grant Revenue	$1,750,999
Credit:	Departmental Grant Expense	($1,750,999)