



THE PRACTITIONER'S VIEW

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BREAKING BREAD WITH BILL BAKER

Nova Scotia practitioners were well represented at a breakfast session held on January 15 at the Ramada Hotel in Dartmouth. Over 50 members attended to hear Mr. Bill Baker, Assistance Commissioner of CCRA, speak on the new civil penalties legislation. Mr. Baker presented a forthright summary of the reasons why such legislation came into being, as well as insights and his personal views on the enforcement of such penalties. He provided assurance that the forthcoming Information Circular would provide better clarification of when penalties may be assessed, and Elaine Sibson FCA got him to assure that all proposed penalties would be reviewed personally by him!

The draft Information Circular was released shortly after the meeting, and members in attendance received a request to provide comments to the Institute to serve as a basis for its submission to the CICA, who will be coordinating a response on behalf of the CA profession. The Practitioners Committee was pleased with the attendance, and would like to offer additional such sessions when a timely matter of particular interest to the practitioners arises.

GAAP - TO FREEZE OR NOT TO FREEZE

Many covenants and agreements refer to "in accordance with GAAP". As you know, GAAP changes over time, and projects currently being studied by the Accounting Standards Board have a potential to result in significant unanticipated changes to financial results and ratios.

If you're advising a client or lawyer in creating such agreements, consider the benefit of freezing the planned outcome by referring to "GAAP in effect at the date of the agreement". This way, there are no unpleasant surprises or the need for re-negotiation if the goal posts change. In the absence of any specified date, GAAP will be interpreted at the time the calculation must be done.

LITTLE GAAP MAY BE ON THE WAY

The view of the Small Business Enterprise Advisory Committee is that enterprises other than public enterprises, cooperative business enterprises and regulated financial

institutions would be eligible for simplified reporting after obtaining annual unanimous consent of all owners. "Little GAAP" will likely cover disclosure exemptions and presentation differences but measurement differences are not ruled out. The advisory committee will report at the end of December 2000 and the Accounting Standards Board will then release an exposure draft.

COMPILATION ENGAGEMENTS

(The following is reprinted from ICABC News 'N Views – Dec/00)

"What is needed for a compilation engagement – both for financial statements and working papers?"

The answer to this commonly asked question is one where personal preference and judgment play a significant role. The standards for compilation engagements are minimal, including due care and the belief that the statements are not false or misleading. "What is needed" is at least enough to meet the minimum requirements, and enough to satisfy the practitioner and/or client's needs.

• Financial Statements

There are a wide variety of acceptable "compiled" statements:

- single year balance sheet and income statement with no notes.
- comparative balance sheet and income statement, with some selective notes.
- financial statements in full compliance with GAAP.

Any of these are acceptable as long as they are not false and misleading.

A caution to practitioners – the barest presentation may be misleading. If significant assets or liabilities are not recorded or disclosed because the statements are on a cash basis or a capital lease is recorded as an operating lease, a reader might be misled. This could lead to professional or civil liability.

On the other hand, inclusion of additional information provides more information, which the practitioner has to check to ensure it is not false or misleading. Therefore, additional work may be required, both to ensure the information provided is not false or misleading, and to ensure that the reader is not misled to think that this is all the relevant information. For instance, if a note on capital assets is included but there is no disclosure that the debt is secured by these assets, the statements may be misleading.

Full GAAP statements may well similarly require additional work. If the client is prepared to pay the additional costs in compiling these statements, and the practitioner is prepared to do the work to ensure the additional disclosure is not false or misleading, this is acceptable.

- **False or Misleading**

It is worth remembering that it is not only what we know, but what we **should know**. As CAs, we cannot “turn a blind eye”.

In some cases, the policies used in compiling statements could be considered misleading if a reader assumed that the statements were based on GAAP. By providing note disclosure of the policies under which the statements were prepared, the information is not misleading.

- **Supporting Working Papers**

Previously, the Professional Advisory Services department advised that the minimum working papers for a compilation engagement depends on the specific circumstances, but basically in every file, you should have:

- an engagement letter;
- copy of the financial statement;
- adjustments to the client’s records;
- a worksheet, or the like, summarizing the source of accounting information to the f/s groupings;
- general file support for significant assets and liability accounts and other working papers.

Some firms get a letter of representation, while others do not.

Y2K – NOTE REQUIREMENTS WITHDRAWN

Note disclosure on the Y2K issue is no longer required and the CICA has withdrawn the related accounting and auditing guidelines as of November 2000 (AcG#10, AuG#22, 23, 24, 27).

RISK ALERT

The CICA just released its latest Risk Alert in December, which covers, amongst other topics, economic environment, earnings management and interim financial statements. We encourage members to read this bulletin, which is available on the CICA Web site at www.cica.ca under “What’s New.”

PLAGUED BY VIRUSES?

Remember when your worst fear was you or your staff coming down with the flu during busy season? Today, an even worse fear may be when your computers phone in sick.

The average practitioner deals with dozens of e-mail messages every day. Messages from clients, colleagues, friends and even family are commonplace. Unfortunately, so too are computer viruses which replicate and spread via e-mail.

While many of these viruses are not destructive, others can be. Most are of the “worm” or “trojan horse” variety, in that they may only activate when a particular function of the infected program is used, and they generally burrow deep into certain systems on your computer. They may corrupt certain types of files stored on your hard drive, such as JPEG image files, or in the most serious cases, they can erase files and programs from your system. You may lose data, and you will most certainly lose work time.

Many viruses are designed to replicate themselves once they are opened by unsuspecting victims. They immediately spread into your computer’s hard drive, and they re-transmit themselves using Microsoft Outlook by attaching themselves to e-mail messages that are sent to everyone in your Outlook contact list. Depending on the number of contacts you happen to have on file, there could be a lot of people out there receiving a most unwelcome e-mail – from you! Talk about client and business goodwill!

What can you do?

Consider the following:

- ICANS, like most associations, has anti-virus software in place designed to identify and quarantine these electronic viruses when they are received. We trust that all of you have installed similar software and are diligent in downloading updates on a regular basis. However, each week new viruses are created and spread (as one of the ICANS staff stated “Don’t these people have a life?”) and relying on this protection alone is not prudent.
- Keep your staff informed about viruses and the need to be on the lookout for them all the time.
- Do not open any attachments that appear suspicious. Beware of files ending in “.exe” (executable programs) or with an extra extension on the end of an otherwise normal-looking file (e.g. picture.jpg.vbs). Remind them that they cannot rely on the “trusted” source of the e-mail (their friend may just have become a virus victim!).
- If you have anti-virus software installed, but are in the habit of disabling it to improve efficiency, don’t set your Outlook view to Auto-preview.
- When in doubt, DON’T. If you receive an e-mail you even think may be the result of a virus, phone or e-

mail the source and do not open the attachment until you have received positive confirmation that it is safe.

You may wish to check out the Symantec AntiVirus Research Center at <http://www.sarc.com> for up-to-date virus information.

REDUCING PSR COSTS

The easiest way to reduce PSR costs is to limit the number of findings and points for discussion since these add to the reviewer's "write-up" time. Although there are no "perfect files" (and it would be cost-prohibitive to try to attain this), ensuring that the most common items arising from practice review are not applicable to your financial statements and files will save you money. Consideration should be given to addressing the following:

Financial Statement Presentation

- Financial statements of a not-for-profit organization should include a description of the organization's:
 - a) purpose. (CICA 4400.04)
 - b) intended community of service. (CICA 4400.04)
 - c) status under income tax legislation (CICA 4400.04)
 - d) legal form (CICA 4400.04)
 - Financial statements of a not-for-profit organization using fund accounting should include a description of each fund reported. (CICA 4400.06)
 - The statement of financial position of a not-for-profit organization should disclose, for each financial item, a total that includes all funds reported. (CICA 4400.18)
 - The significant accounting policy with respect to recognition of contributions should be disclosed. The organization should use either the deferral or restricted fund method, (CICA 4410.10) See sample disclosure – Schedule A.
 - A not-for-profit organization should disclose the policy followed in accounting for:
 - a) endowment contributions. (CICA 4410.21)
 - b) restricted contributions. (CICA 4410.21)
 - c) contributed materials and services. (CICA 4410.23)
 - A small not-for-profit organization meeting the criteria of CICA 4430.03 should disclose the amount of capital assets expensed in the current period (CICA 4430.40), as well as the policy followed. (CICA 4430.40)
 - Restricted cash should be excluded from current assets. (CICA 3000.01)
- The basis of valuation of inventories and short-term marketable securities should be disclosed. (CICA 3030.10, 3010.04)
 - The quoted market value of both short and long-term marketable securities should be disclosed.(CICA 3010.04, 3050.33)
 - Disclosure of capital lease obligations should include:
 - a) interest rate implicit in the lease. (CICA 3065.22)
 - b) the expiry date. (CICA 3065.22)
 - Related party transactions would normally include disclosures of:
 - a) rent received/paid
 - b) interest received/paid
 - c) management fees received/paid
 - d) measurement basis used (CICA 3840.43)(See sample financial statements in the Professional Engagement Manual for examples of note disclosure.)
 - Disclosure of authorized capital should include the redemption terms of redeemable shares. (CICA 3240.02)
 - Common disclosures for financial instruments include:
 - a) For term deposits, interest rates and maturity dates. (CICA 3860.52, 3860.57)
 - b) For short-term borrowings, interest rates. (CICA 3860.52, 3860.57)
 - c) For authorized lines of credit, the amount authorized, the interest rate, and the renegotiation date. This information should be provided for all clients who have an authorized line of credit, whether they use it or not. It should also be noted that instead of indicating the exact renegotiation date, an entity may simply indicated that the line of credit is renegotiated annually. (CICA 3860.52, 3860.57)
 - d) For long-term debts, the renegotiation date when such date precedes the maturity date. (CICA 3860.52, 3860.57)
 - The reason for not presenting a cash flow statement should be disclosed. A cash flow statement is required unless the reporting enterprise is not a public enterprise and the required cash flow information is readily apparent from other financial statements or adequately disclosed in the notes. (CICA 1540.03)

Documentation of Review Engagements

- Although the review engagement checklist and/or supporting schedules are generally signed off indicating that enquiries have been made of the client, documentation should include notes indicating the results of these discussions with respect to:
 - a) Cut-off
 - b) Allowance for doubtful accounts
 - c) Client's inventory count procedures & valuation

- d) Contingencies, commitments & subsequent events
- e) Comparison of gross profit margin
- f) Comparison of revenues & expenses
- g) Comparison of balance sheet items
- h) Comparison of operating ratios
(CICA 5025.56, 5026.62, 8100.15, 8100.24)

When questions on the review engagement checklist require documentation of the client's procedures, as it usually does for the first three items above, it is not appropriate to sign off these steps as having been completed without documenting the procedures and assessing their adequacy.

Gross profit is usually reviewed but the last three comparisons are often not documented. Comments should be noted on file for significant variances in all areas and where possible the comments should be reasonably specific (i.e. less general than "better economy")

Analytical review is a key component of a well-documented review engagement file, i.e. its relative importance to a review engagement is much greater than to an audit. **The absence of analytical review, which includes proper explanation of differences in ratios and financial statement items, would figure prominently in the Committee's decision to reinspect review documentation.**

Documentation of Audit Engagements

- Regardless of the size of an audit engagement, the file should include some documentation of the planning process, including the auditor's assessment of materiality/significance and audit risk, intended audit approach, understanding of internal control and knowledge of the entity's business. **In particular, for audits, which are purely substantive, and most, or all, transactions are subject to audit, this fact should be clearly set out in the planning notes.** (CICA 5025.31, 5025.46, 5025.51, 5100.02, 5130.30, 5140.03, 5140.076, 5205.11, 5205.13, 5205.22)
- In general, inherent and control risk are assessed **but documentation is weak or contradictory regarding the link between overall assessment and the nature, extent and timing of substantive procedures.**
- On substantial completion of the audit, the auditor should use analytical procedures to assist in evaluating the overall financial statement presentation and document the results in the file. (CICA 5301.23)
- Where a legal enquiry letter has not been sent, the reason should be documented in the working papers.

2001 CHANGES TO SUMMER JOBS FOR STUDENTS INITIATIVE

Many practitioners assist their clients in applying for Summer Career Placements (SCP) each year. SCP is a wage subsidy program that has been in effect for more than 20 years and enables private, public and not-for-profit employers to create career related summer jobs for students.

Some changes to the program guidelines have been implemented this year.

- Changes in the rate of wage subsidy for public sector employers. For summer 2001, public sector employers are now eligible to receive a contribution of up to 50% of the prevailing provincial/territorial minimum wage rate for adults (same as private sector rate). Not-for-profit employers are eligible to receive a contribution of up to 100% of the prevailing provincial/territorial minimum wage for adults.
- Size of employers in the private sector - increased focus on small- and medium-sized businesses. CAs wishing to assist clients in attaining benefits under this program are reminded that the deadline for Nova Scotia employers to submit an application for SCP funding is March 30, 2001. For more information, contact your nearest Human Resources Development Canada office, call 1 800 935-5555, or visit the website at <http://youth.hrdc-drhc.gc.ca>.

CONDOMINIUM CORPORATIONS

Practitioners are reminded of a new regulation under the Condominium Act that was approved on February 16, 2000.

Section 72B(c)(ii) of the regulations requires an auditor to express an opinion:

"on the viability of the plan adopted by the corporation to achieve the required fund amount within the period prescribed in the reserve-fund study"

in a statement to be included in the annual financial statement referred to in Section 24A of the Act.

The Office of Business and Consumer Services advises "it is our expectation that the accountant will, as part of the review process for preparation of the audited financial statement, determine from the corporation the details of the accumulation plan for the reserve fund adopted by the corporation and comment on whether this accumulation plan will meet the *financial targets set out in the study in the time frame set out in the study*. It is in no way expected that the accountant will comment on the viability of the recommendations of the study to meet repair/replacement needs of the corporation or the likelihood of the final projections to meet the costs of these repairs."

SUGGESTIONS FOR THE NEXT ISSUE?

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