Deloitte Private

ASPE: where are we now?
Where are we going?
Welcome to Deloitte’s annual round-up of news and activities relating to Canadian Accounting Standards for Private Enterprises (ASPE), in which we look at what has been happening this year and what we can expect in the year to come.

One of the objectives of the Canadian Accounting Standards Board (AcSB) is to ensure that significant changes to ASPE do not occur more often than every two years, with minor changes occurring in the interim. In 2014, we saw significant changes to the ASPE standards dealing with employee future benefits and discontinued operations. In 2016, we are set to see the introduction of new standards dealing with the accounting for subsidiaries and joint arrangements.

There was some activity under ASPE in 2015, despite there being no new accounting standards either issued or brought into effect. This included: (1) deliberations and continued outreach on responses to an Exposure Draft dealing with the accounting for preferred shares issued under a tax planning arrangement, which attracted a lot of attention; (2) the ASPE annual improvements process; (3) some other projects, which we will touch in this publication.

I hope you find this publication helpful in providing you with a snapshot of where ASPE is now and what we can expect to see down the road. Remember also that to stay on top of developments in ASPE on a regular basis, you can visit Deloitte’s Centre for Financial Reporting, which includes news and resources dedicated to meeting your ASPE financial reporting needs.

In addition to this publication, we will also be hosting a webcast on December 9, 2015, focusing on some of the key changes that will impact you next year.

Regards,
Diana De Acetis
Partner and ASPE Technical Accounting Leader, Deloitte Canada
Activities in the year

Redeemable preferred shares issued in a tax planning arrangement

In 2013, the AcSB approved a project to re-examine the accounting for redeemable preferred shares issued in a tax planning arrangement. An estate freeze transaction is an example of a tax planning arrangement in which business owners wish to transfer the future growth of their business onto their children, and in so doing take back redeemable preferred shares fixed at the value of the business at the date of the estate freeze. In the fall of 2014, an Exposure Draft was issued, proposing to remove the ability of entities to classify these preferred shares as equity at what has historically been a nominal amount and replacing it with a requirement that the shares be presented as a liability at fair value, which could be the full redemption amount. The Exposure Draft proposed that an offsetting charge would be recorded as a separate component of equity. Slightly more than 70 comment letters were received in response to the Exposure Draft, many not supportive of the proposals and suggesting that users other than creditors be consulted — including regulators in certain industries, bonding agencies, suppliers, customers and landlords. The concern was that other users may not understand the results of reporting redeemable preferred shares issued in a tax planning arrangement as liabilities. Other concerns included potential difficulty in renegotiating loan agreements, potential unintended tax consequences in some provinces and increased complexity in accounting for such shares in certain circumstances.

The AcSB was responsive to the responses received and, after much deliberation, made a decision to delay finalizing any changes until further outreach is performed. No change will be proposed to the existing standard prior to January 1, 2016, and any change that may be proposed will not be effective before January 1, 2018. This is to provide entities with sufficient time to work with their financial statement users to understand the changes and address any resulting impacts.
Post-implementation review: Financial instruments

In October 2014, the AcSB issued a request for information seeking feedback on Section 3856, Financial Instruments. This review was the first of its kind to be undertaken by the AcSB. The purpose of the review was to assess whether Section 3856 provides information that is useful to financial statement users; whether there are unexpected costs or challenges in applying the standard; and whether there are any areas of the standard that present interpretation challenges such that the standard may not be applied consistently.

The post implementation review considered the following topics: measurement of financial instruments, both initially and subsequently; recognition and measurement of financial instruments in the context of a related party transaction; impairment of financial instruments; presentation of liabilities and equity; hedge accounting; and disclosures.

The AcSB held numerous roundtable discussions throughout the comment period, which were open to the public for participation. All feedback received through comment letters and through the roundtable discussions was considered and a Feedback Statement was issued in September 2015, summarizing the common responses to the questions posed. Overall, stakeholders supported the principles and most of the requirements in the standard. Some expressed concerns included:

• Challenges in determining the initial measurement of certain financial instruments
• Confusion regarding the scope and both initial and subsequent measurement of financial instruments issued between related parties
• That certain disclosures, particularly risk and uncertainty, were not necessarily helpful to users.

The AcSB plans to further analyze the feedback. Should a decision be made to implement changes to the standard as a result of the feedback, these changes will go through the AcSB’s due process. The form of any amendments to the standard as a result of the post-implementation review will depend on the level of change, with small amendments being considered through the ASPE annual improvements project and more significant changes going through a more thorough vetting process.
2015 ASPE annual improvements project

In October 2015, the AcSB issued minor changes to ASPE arising from the 2015 Annual Improvements project. Of the four changes made, three are amendments to disclosures around business combinations, investments and leases. The fourth change looks at employee future benefits and the option to use a funding valuation when accounting for defined benefit obligations. The final amendments are effective for fiscal years beginning on or after January 1, 2016, with early application permitted.

**Business combinations**
This change is limited to providing disclosure of each major class of assets acquired and liabilities assumed when a business combination is achieved through the acquisition of an asset or group of assets. The previous requirement to disclose each major class of assets acquired and liabilities assumed was only required when a business combination was achieved through the acquisition of a subsidiary that was consolidated.

**Investments and leases**
This change is limited to a requirement for disclosure of the amount of an impairment loss or reversal of a previously recognized impairment loss included in net income that is related to investments accounted for using the cost or equity method under Section 3051. A similar amendment was made to Section 3065, Leases, requiring lessors to disclose the amount of any impairment loss or reversal of a previously recognized impairment loss.

**Employee future benefits**
This amendment clarifies the circumstances in which a funding valuation may be used to measure the defined benefit obligation of certain defined benefit plans. The amendment provides that an entity with a defined benefit plan for which there is no legislative, regulatory or contractual requirement to prepare a funding valuation can only elect to use a funding valuation to measure its defined benefit obligation when the entity has at least one defined benefit plan for which a funding valuation is required to be prepared in order to comply with legislative, regulatory or contractual requirements and for which the defined benefit obligation has been measured using a funding valuation.

For example, an enterprise that has a defined benefit plan to provide post-retirement medical and dental benefits that does not require a funding valuation, and has no other defined benefit plans that require a funding valuation, would no longer have the option to measure the defined benefit obligation for such plan using a funding valuation.

The change may have a significant impact to entities with defined benefit plans that have elected to measure their plan obligations using a funding valuation and they do not have a least one plan for which a funding valuation is required. Enterprises are encouraged to monitor their defined benefit plans for changes down the road, such as when a plan requiring a funding valuation is wound-up or otherwise ceases to exist. This amendment is required to be applied retrospectively.
Upcoming changes

Section 1591 - Subsidiaries

In the fall of 2014, a new standard on subsidiaries (Section 1591, Subsidiaries) was issued, replacing Section 1590, Subsidiaries, and AcG-15, Consolidation of variable interest entities. Section 1591 is mandatorily effective for fiscal years beginning on or after January 1, 2016. Section 1591 introduces a new model for determining whether one enterprise controls another when voting equity may not be the dominant factor in determining control, such as when contractual rights provide the power to determine the strategic policies of the other enterprise.

Companies that elect to prepare consolidated financial statements will need to evaluate whether they control entities through contractual rights alone or in combination with voting rights and/or potential voting rights. This will involve reviewing contractual arrangements that may confer control, such as supply arrangements, management contracts, lease agreements and license agreements. In evaluating whether contractual rights are sufficient to confer control, the enterprise is required to consider all facts and circumstances, including the following:

- The degree of involvement in and decisions made in determining the purpose and design of the other enterprise
- How decisions are made about the strategic policies of the other enterprise
- The risks to which the other enterprise was designed to be exposed, the risks it was designed to pass onto those involved with it, and whether the enterprise is exposed to some or all of these risks
- Whether the enterprise has the continuing ability in a contractual arrangement to direct the strategic policies of the other enterprise without the co-operation of others.

Entities that account for their subsidiaries using the cost or equity method will be not be impacted.

Companies that prepare consolidated financial statements will need to evaluate whether variable interest entities that are consolidated under AcG-15 are controlled based on the new guidance in Section 1591 such that consolidation remains appropriate. Additionally, companies preparing consolidated financial statements will also need to evaluate whether entities not currently consolidated under AcG-15 are controlled under Section 1591 such that they are now required to be consolidated.

Entities previously struggling with the application of the rules-based approach in AcG-15 will welcome its replacement with the more conceptual guidance provided in Section 1591. It is expected that such guidance may be subject to interpretation and will likely require a greater degree of professional judgment to apply.
Section 3056 - Joint arrangements

In the fall of 2014, a new standard was issued on joint arrangements, replacing the former standard on joint ventures. Previously, entities had the option to account for their interests in joint ventures using the cost method, the equity method or the proportionate consolidation method. This “free choice” has been eliminated on the grounds that it did not result in the faithful representation of an investor’s interests in certain circumstances. Under the new standard, an investor with joint control in a joint arrangement is required to account for its interests according to its rights and obligations in the joint arrangement, subject to the simplification provided for interests in jointly controlled enterprises.

As a result, it will be important for an investor with joint control to determine the type of joint arrangement in which it has an interest as this will drive the accounting. Specifically for:

• **Jointly controlled assets** – An investor with joint control would account for its share of the jointly controlled assets, its share of the liabilities incurred jointly and any revenue from the sale or use of its share of the output of the arrangement and its share of any expenses incurred by the arrangement.

• **Jointly controlled operations** – An investor with joint control would account for the assets it controls, the liabilities it incurs and its share of the revenue generated and expenses incurred by the arrangement.

• **Jointly controlled enterprises** – An investor with joint control would have an accounting policy choice to apply:
  1. Cost method – to all such interests
  2. Equity method – to all such interests
  3. Perform an analysis of all such interests.

The analysis to be performed on an enterprise considers relevant facts and circumstances and can be complex and highly judgmental.

In the event that the analysis concludes that the entity holds an interest in the net assets of the investee, it would apply the cost or equity method. In the event that the analysis concludes that the entity holds an interest representing rights to the individual assets and obligations for the liabilities of the investee, it would account for the interest consistent with the accounting for either jointly controlled assets or jointly controlled operations.

Section 3056 is mandatorily effective for fiscal years beginning on or after January 1, 2016, with early application permitted. If the standard is adopted before January 1, 2016, the enterprise must apply the amendments to Section 3051, Investments, at the same time.
In September 2015, the AcSB issued an Exposure Draft to clarify the accounting for a subsidiary and for an investment subject to significant influence when the cost method is applied. The Exposure Draft was issued in response to comments from stakeholders that diversity had merged in practice in the application of the cost method.

The Exposure Draft addresses the following key areas of uncertainty:

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<tr>
<th>Areas of uncertainty</th>
<th>Clarification proposed in Exposure Draft</th>
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<tr>
<td>Cost of an interest in a subsidiary and an investment subject to significant influence</td>
<td>The cost is measured at the acquisition-date fair value of the consideration transferred to the other party in exchange for the interest.</td>
</tr>
<tr>
<td>Treatment of acquisition costs</td>
<td>Acquisition-related costs are recognized as expenses in the period incurred.</td>
</tr>
<tr>
<td>Acquisitions of additional interests</td>
<td>The carrying amount of the resulting interest would be the carrying amount of the investor’s interest in the investee immediately before the increase in the investor’s interest plus the cost of the additional interest acquired.</td>
</tr>
<tr>
<td>Initial measurement of an interest in a subsidiary</td>
<td>Provisional amounts may be used. The provisional amounts would be adjusted in a subsequent period when amounts are finalized (not exceeding a one-year period from date of acquisition) with no retrospective adjustment.</td>
</tr>
<tr>
<td>Bargain purchases</td>
<td>Bargain purchase gains are not recognized when the cost method is applied.</td>
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The proposed changes resulting from the Exposure Draft would be effective for fiscal years beginning on or after January 1, 2018 and would be applied on a prospective basis. Comments to the AcSB on this Exposure Draft are due January 6, 2016.

**Agriculture discussion paper**

Currently, there is no comprehensive standard in ASPE dealing directly with the accounting for biological assets (i.e., living animals and plants). This has led to significant diversity in practice. The AcSB is expected to release a discussion paper on agriculture in late 2015. Issues to be addressed by this project include:

- When a biological asset should be recognized
- How the asset should be measured on initial recognition and in subsequent periods
- How agricultural produce at the point of harvest should be accounted for
- What disclosures should be required.
# Preparing for year-end

## Questions to consider for the current year end

| Interests in other entities | • Is there any benefit to early adopting Section 1591, Subsidiaries, or Section 3056, Interests in joint arrangements?  
  • Have there been any changes to ownership interests held in other entities during the year? |
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<td>Revenue</td>
<td>• Has the company entered into new types of revenue arrangements such as bill-and-hold, non-refundable fee arrangement, multiple element arrangements?</td>
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| Bank debt                  | • Has there been a violation of bank covenants?  
  • Is debt appropriately classified on the balance sheet?                                                                                                                                                                                                 |
| Impairment                 | • Has management performed an assessment of whether indicators of impairment are present for long-lived assets, intangible assets, goodwill, cost or equity investments, financial assets, deferred tax assets?  
  • Have circumstances improved such that a past impairment should be reversed?                                                                                           |
### Estimates
- Have estimates that require management judgement been updated?
- Estimates include, but are not limited to: recoverability of accounts receivable; net realizable values of inventory; recoverability of property, plant and equipment; useful lives of property, plant and equipment; provision for sales returns; warranty provisions; provision for taxes.

### Significant and/or unusual transactions
- Has the company entered into any significant and/or unusual transactions in the year including: transactions with related parties that are not in the normal course of business, new leasing arrangements, factoring arrangements, preferred share financing, tax reorganizations, business acquisitions or divestitures, restructuring, employee terminations, exiting business lines, amending benefit plans?

### 2014 annual improvements
- Is the company impacted by the 2014 annual improvements (effective January 1, 2015) that deal with hedge accounting and disclosure of impaired financial assets?
Please tune in to our annual ASPE webcast on December 9, 2015 where our ASPE specialists will discuss some of the key changes to standards impacting private enterprises, areas of judgment and interpretation, and where ASPE is going.

To register for the webcast, click on the link below.

Click here to register
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