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It’s that time of year again…

Accounting Standards for Private Enterprises (ASPE)

December 10, 2014

Agenda

- Subsidiaries and joint arrangements
- 2014 annual improvements
- Future changes headed our way
- Employee future benefits implementation
- Year-end reminders
- Questions and answers

Important caveats

This webcast does not provide official Deloitte interpretive accounting guidance.

Consult your Deloitte advisor for additional support.

Subsidiaries and joint arrangements

What’s new in 2014

Section 1591 Subsidiaries **new** → Replaces both Section 1590 Subsidiaries and AcG-15 Consolidation of Variable Interest Entities

Section 3056 Joint Arrangements **new** → Replaces Section 3055 Interests in Joint Ventures

Section 3051 Investments **amended**

It’s not too early to start thinking about the changes and the resulting implications!

Effective for January 1, 2016 with early adoption permitted

Section 3056 Joint Arrangements
What's changed

What is a joint venture?

- Contractual arrangement where 2 or more investors have joint control over an economic activity
- **No change, except now called "joint arrangements"**

Joint control

- Contractually agreed sharing of the continuing power to determine strategic operating, investing and financing policies of the economic activity
- **No change**

Types of joint ventures

- Jointly controlled assets + jointly controlled operations + jointly controlled enterprises
- **No change**

Accounting for interests in joint ventures

- **Old:** Single accounting policy choice for all interests in joint ventures: cost method, equity method or proportionate consolidation
- **New:** Accounting method depends on type of joint arrangement: jointly controlled assets, jointly controlled operations, JCEs

Changed

Contributions/sales to joint ventures

- Removed requirement to defer and amortize portion of the gain on contribution (or sale of assets) to a joint arrangement that does not relate to cash/fair value of other assets received. The gain is recognized in net income to the extent of the interest of non-related investors

Section 3056 Joint Arrangements (cont'd)

Joint arrangements

Jointly controlled assets

Investor recognizes:

- Its share of jointly controlled assets
- Its share of liabilities incurred jointly
- Revenue from the sale or use of its share of the output and its share of expenses incurred

Jointly controlled operations

Investor recognizes:

- Assets it controls
- Liabilities it incurs
- Its share of the revenues and expenses incurred

Jointly controlled enterprises

Accounting policy choice:

1. Cost method – for all
2. Equity method – for all, OR
3. Analyze each interest. If interest gives investor:
   - **Right to net assets –** account for all such interests using the cost or equity method
   - **Rights to individual assets and liabilities** – account for all such interests using the guidance for JCAs, JCOs

Key:

- For JCAs + JCOs – no longer have option to use the cost or equity method
- For JCEs – have option to account for share of assets and liabilities, provided certain conditions are met

Section 3056 Joint Arrangements (cont'd)

Analysis of interest in a jointly controlled enterprise

		Yes
Legal form	Does **legal form** of the JCE give the investors rights to the assets and obligations for the liabilities relating to the JCE?	Yes → Investor has: rights to the individual assets and obligations for the individual liabilities of the JCE
	No ↓	
Terms of the contractual arrangement	Do the **terms** of the contractual arrangement specify that the investors have rights to the assets and obligations for the liabilities, relating to the JCE?	Yes → Investor has: rights to the individual assets and obligations for the individual liabilities of the JCE
	No ↓	
Other facts and circumstances	Is the JCE **designed** so that: a) Its activities primarily aim to provide the investors with an output (i.e. they have substantially all the economic benefit of assets held in the JCE) AND b) It depends on the investors on a continuous basis for settling the liabilities relating to the JCE?	Yes → Investor has: rights to the individual assets and obligations for the individual liabilities of the JCE
	No ↓	
	Investor has **rights to the net assets** of the JCE	

Investor has:

- **Rights to the individual assets and**
- **Obligations for the individual liabilities** of the JCE

Section 1591 Subsidiaries

What's changed

What is a subsidiary

- An enterprise controlled by another enterprise that has the right and ability to obtain future economic benefits from the resources of the enterprise and is exposed to the related risks
- **No change**

What is control

- Continuing power to determine strategic operating, investing and financing policies without cooperation from others
- **No change**

Control other than through equity interests

- **More judgment** introduced when determining whether control exists through means other than equity interests
- **Additional guidance provided on**
  - The types of contractual arrangements that might give control
  - Other facts and circumstances to consider when assessing control

Changed

Policy choices for accounting for subsidiaries

- Accounting policy choices are:

1. Consolidate all subsidiaries OR
2. Account for subsidiaries that
   - Controlled by voting interest, potential voting interests or a combination thereof using the cost or equity method; AND
   - Controlled through contractual arrangements in accordance with the applicable Handbook section

- **Clarifies** accounting for subsidiaries not controlled through equity

Control through means other than equity interests

An enterprise has control through contractual rights when:

- It holds rights that are sufficient to direct the strategic operating, investing and financing policies of the other enterprise without the co-operation of others; AND
- It has the right and ability to obtain the future economic benefits and is exposed to the related risks of the other enterprise.

Analysis requires exercise of more judgment vs prescriptive approach to evaluate whether consolidation of VIE is required in AcG-15.

Control through means other than equity interests (cont'd)

Supply agreements

Lease agreements

Finance agreements

Management agreements

License agreements

Royalty contracts

An entity reviews its contractual arrangements and considers all facts and circumstances when determining whether it controls another enterprise.

Considerations when evaluating whether contractual arrangements are sufficient to give control

- Degree of involvement in determining **purpose and design** of the other enterprise?
- How are **decisions** made that could affect whether entity has the right and ability to obtain future economic benefits/exposed to the risks of the other enterprise?
- What **risks** was the other enterprise designed to be exposed? What risks was it designed to pass onto others? Is the enterprise exposed to some/all of those risks?
- Does the entity have the continuing ability in a contractual arrangement to direct the strategic policies of the other enterprise **without the co-operation of others?**

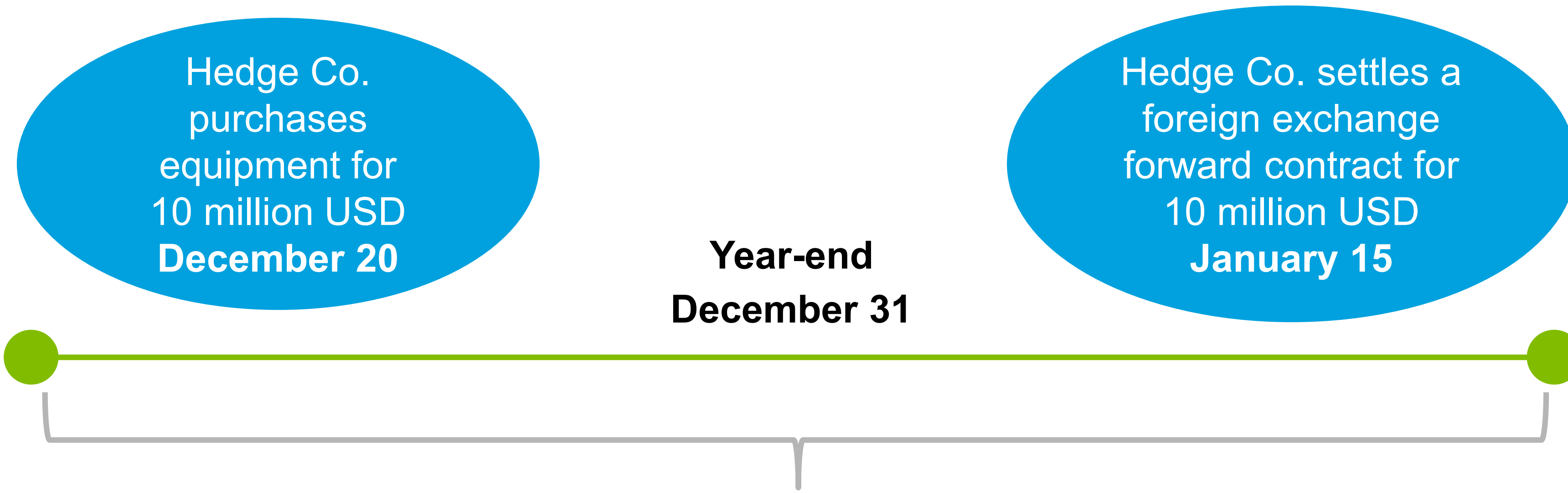
Consider all rights including call rights, put rights, liquidation rights, rights that are exercisable only when an event or circumstance occurs (for entities on auto-pilot)

2014 Annual improvements

ASPE 3856 financial instruments

Hedge of an anticipated transaction

A hedge of an anticipated transaction may mature after the anticipated transaction occurs.



Amendment

The hedging item is remeasured at the balance sheet date using the spot rate, with any gain or loss included in net income.

ASPE 3856 financial instruments (cont'd)

Asset impairment disclosure

Pre-change 3856 paragraph .42 read:

An entity shall disclose the carrying amount of impaired financial assets, by type of assets, and the amount of any related allowance for impairment.

Post change 3856 paragraph .42 reads:

For financial assets other than current trade receivables, an entity shall disclose the carrying amount of impaired financial assets, by type of asset, and the amount of any related allowance for impairment **For current trade receivables, an entity shall disclose the amount of any allowance for impairment.**

What does this change really mean?

ASPE 3856 financial instruments (cont'd)

Asset impairment disclosure

Current receivables	$XX
AFDA	$(XX)
Net Receivables	$XX

Irrespective of the composition of the current receivables balance – the AFDA balance can be disclosed as a single number

ASPE 3462 employee future benefits

- ASPE 3462.031 permits the use of a funding valuation to determine the obligation for an unfunded defined benefit plan.
- This allows an entity that uses a funding valuation for funded defined benefit plans to measure all defined benefit plans on a consistent basis.

Proposed amendment

Does the entity have at least one funded defined benefit plan?

Yes – Option to use a funding valuation for unfunded defined benefit plans **can** be applied

No – Option to use a funding valuation for unfunded defined benefit plans **cannot** be applied

Proposed amendment **NOT APPROVED** at this time – AcSB will consider the issue further

Future changes headed our way

Future changes

DP: Discussion Paper **ED**: Exposure Draft **HB**: Handbook Release

ITC: Invitation to Comment **RI**: Request for Information

Standards for private enterprises	2014	2015		
	Q4	Q1	Q2	Q4
AcSB Strategic Initiative			ITC	
Annual Improvements 2015		ED		HB
Major Improvements				
Agriculture		DP		
Redeemable Preferred Shares Issued in a Tax Planning Arrangement				
Subsidiaries			ED	
Post-implementation Reviews				
Section 3856, Financial Instruments	RI			

Redeemable preferred shares issued in a tax planning arrangement

Exposure Draft (ED)

Paragraph 23 in Section 3856

- ✓ Redeemable preferred shares issued in certain tax planning arrangements classified as EQUITY
- ✓ Re-classified to LIABILITIES when redeemable
- ✓ Measured at par, stated or assigned amount

Paragraph 23 in Section 3856 removed (as proposed in the ED)

- ✓ Redeemable preferred shares issued in certain tax planning arrangements classified as LIABILITIES
- ✓ Measured at fair value
- ✓ With the corresponding impact separately identified within SHAREHOLDERS' EQUITY

Redeemable preferred shares issued in a tax planning arrangement (cont'd)

Exposure Draft (ED)

Example

- Joe wants to pass his business onto his children on a tax deferred basis
- He uses a Section 85 income tax roll-over to transfer the business to his children and in exchange receives preferred shares at a nominal amount of $1 with fair value of $1M

Current accounting with paragraph 23

- On the entity's balance sheet, record the preferred shares in **equity at $1**

Proposed accounting if paragraph 23 is removed

- On the entity's balance sheet, record the preferred shares as a **liability at fair value of $1M** with a corresponding debit to a separate component of equity

Redeemable preferred shares issued in a tax planning arrangement (cont'd)

Exposure Draft (ED)

When drafting your response to the ED consider among other things:

- User needs and perceptions
- Tax implications, and the
- Conceptual framework

Comments on the ED due to the AcSB staff by January 15, 2015

Post implementation review on Section 3856

Post Implementation Review (PIR)

Significant changes were made to the financial instruments guidance with the introduction of Section 3856

PIR is intended to help the AcSB assess the effectiveness of the guidance in Section 3856:

- Is it useful?
- Are there unexpected costs or challenges when applying the guidance?
- Are there interpretative issues or concerns?
- Are preparer and user needs being met?

This is a great opportunity to have your say and impact the future of the accounting standards!

Comments on the PIR due to the AcSB staff by February 9, 2015

Post implementation review on Section 3856 (cont'd)

Post Implementation Review (PIR)

The specific questions in the "Request for Information" relate to the following areas:

- Initial measurement
- Subsequent measurement and fair value
- Related party transactions
- Impairment
- Presentation of liabilities and equity
- Derecognition
- Hedge accounting
- Disclosures
- Other matters

Employee future benefits implementation

Employee future benefits
Reminders on what changed

- Section 3462 Employee Future Benefits replaced Section 3461.
- Was effective for fiscal years beginning on or after January 1, 2014.
- Section 3462 resulted in:
  - Increased comparability between entities
  - A more meaningful balance sheet number, and
  - Increased income statement volatility

Employee future benefits (cont'd)

	What changed?
Elimination of the policy choice	• The deferral and amortization policy choice for defined benefit plans was eliminated. An approach similar to the immediate recognition approach remains as the only option
Presentation of the defined benefit (liability) asset	• The defined benefit (liability) asset is presented as a net number on the balance sheet

Defined benefit obligation	$XX
Fair value of pension assets	$XX
Less: valuation allowance (if any)	$XX
Defined benefit liability (asset)	$XX

Employee future benefits (cont'd)

	What has changed?
Elimination of the three month window	• The three month window to measure plan obligations and plan assets has been eliminated. The obligations and assets are measured as at the balance sheet date
Discount rate	• The discount rate is the date of the actuarial valuation
Funding or accounting valuation	• A policy choice is available with respect to using either an actuarial valuation prepared for funding purposes or an actuarial valuation prepared specifically for accounting purposes. Choice must be applied consistently to ALL plans with an appropriate funding valuation
Actual return on plan assets	• The costs of managing plan assets paid for by the sponsor are deducted from the actual return on plan assets

Employee future benefits (cont'd)

Components of cost and presentation

Current service cost
- Actuarial present value of benefits attributed to employee's services in the period

Less
- Contributions received from active or retired employees

P&L

Finance cost
- Net defined benefit liability (asset) at the start of period multiplied by the discount rate used to determine the defined benefit obligation

P&L

Remeasurements and other items
- Actuarial gains and losses
- Difference between the actual return on plan assets and the return calculated to determine the finance cost
- Changes in the effect of any valuation allowance
- Past service cost resulting from plan amendments
- Gains and losses on settlements or curtailments

Separate disclosure required – Either in P&L or in the notes

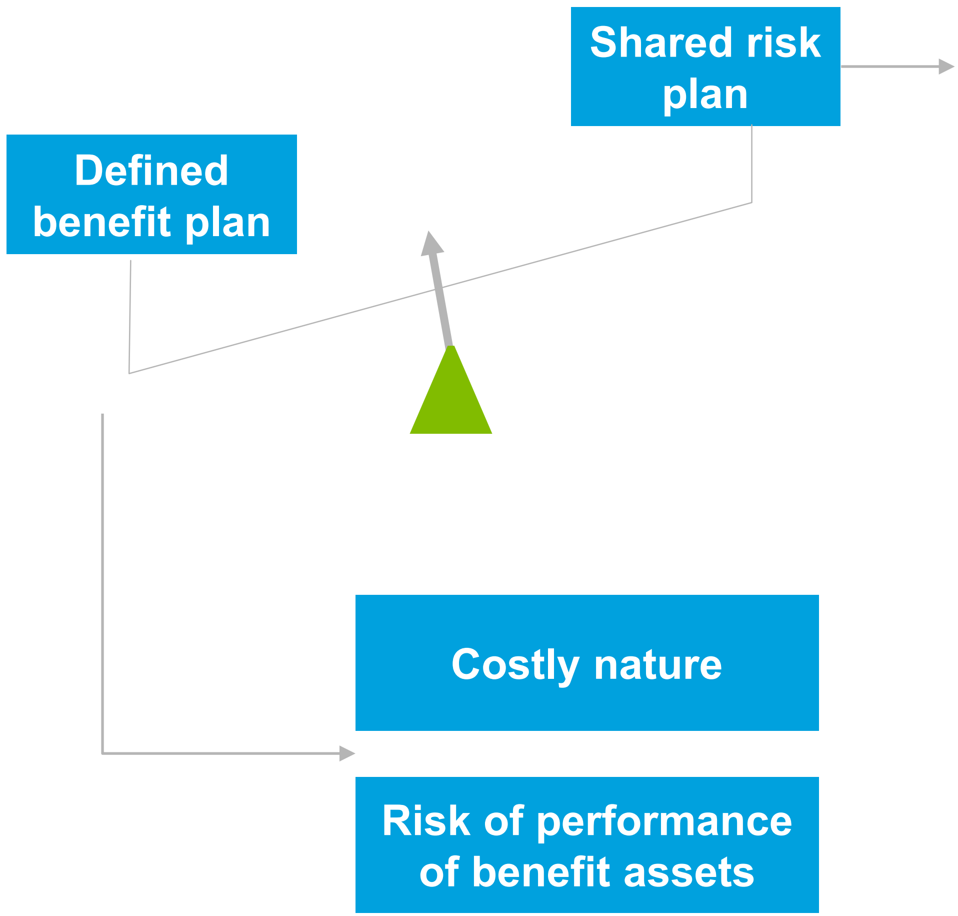
Employee future benefits transition questions

New guidance is generating questions as entities transition:

- When is the policy choice to use a funding or an accounting valuation available?
- What are the differences between a funding and an accounting valuation?
- What is considered to be the most recently completed actuarial valuation?

Work closely with your actuaries and auditors as you transition to the new guidance

Shared risk pension model



New model is generating a lot of attention and interest

- Province of New Brunswick (NB) enacted the concept of a ‘Shared Risk Pension Plan’ in legislation in July 2012
- Various entities within NB are moving or considering moving to the new model

Shared risk pension model (cont'd)

Classification?

Defined contribution | **Defined benefit**

Common characteristics of a shared-risk plan:

- Employee and employer contributions set at a base level
- Variability in employee and employer contributions within a certain range
- May be an initial period of temporary employer contributions
- Benefits are not generally guaranteed – Rather, a target benefit is set
- High probability of meeting benefit targets
- Often two classes of benefits – Base (i.e., regular pension) and ancillary (conditional indexation)

Year-end reminders

Classification of debt

Long-term debt with a measurable covenant violation is classified as a **current liability** unless

- ✓ the creditor has waived, in writing, or lost the right to demand repayment for more than one year from the B/S date **OR**
- ✓ debt agreement contains a grace period and contractual arrangements have been made to ensure violation will be cured during grace period.

AND

- ✓ Future violation of debt covenant giving creditor right to demand repayment within 1 year is “not likely”

Classification of debt (cont'd)

- Non-current classification is **based on facts existing at the balance sheet date rather than** expectations regarding future financing or refinancing.
- **What happens when a measureable covenant violation does not exist at year-end but occurs after year-end?**
  - Factually at year-end there is no covenant violation.
  - Subsequent event disclosure would be appropriate.
- **What happens when there is a covenant violation at the balance sheet date which has been waived?**
  - Section 1510.14 requires that the entity assess future compliance with the covenants for a period of one year from the balance sheet date.
  - If a violation of the covenants is likely within the year – appropriate classification is current. (despite the covenant being waived at year-end)

Impairment
Hierarchy

Step 1: Assets other than non-monetary long-lived assets (such as PPE, intangible assets with finite useful lives and goodwill) are considered first.
e.g. inventory, AR, indefinite life intangibles, financial instruments

Step 2: Assets which fall under the guidance of ASPE 3063
e.g. PPE, definite life intangibles

Step 3: Goodwill is tested for impairment only after all other assets have been assessed for impairment and any identified impairment loss has been recognized.

Impairment (cont'd)

	Long lived assets & intangible assets subject to amortization	Intangible assets not subject to amortization	Goodwill
Impairment loss is recognized when	The carrying amount is not recoverable (i.e. carrying amount exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposition) and exceeds its fair value	The carrying amount exceeds the fair value	The carrying amount of a reporting unit, including goodwill, exceeds its fair value
Impairment loss is measured	As the amount by which the carrying amount exceeds fair value		

Impairment (cont'd)
Indicators

Have any of the following events occurred (list is not exhaustive)?

- ✓ Decline in market value
- ✓ A major competitor enters the market
- ✓ A change in consumer demand that the entity is unable to respond to
- ✓ Increases in interest rates or cost of capital
- ✓ Changes in foreign exchange rates or commodity prices
- ✓ Evidence of obsolescence or physical damage
- ✓ Actual or projected profit or cash flows from the asset/reporting unit are declining
- ✓ Changes to the entity's business model and/or plans to restructure/discontinue operations

If so, you should consider whether the asset/reporting unit is impaired

A few year-end reminders

Area of focus	Did you…
Changing accounting policies	• Consider if you want to change any of the policies listed in Section 1506.09?
Review of estimates including amortization methods and useful life policies	• Revisit amortization methods and useful life policies to ensure they are reflective of an asset's actual and expected life? • Review and assess the appropriateness of other estimates (i.e., bad debts, inventory obsolescence, fair value of financial assets and liabilities, warranty obligations, or contingent liabilities)?
Tax considerations	• Review uncertain tax positions. • If entity follows the future income tax method, consider recoverability of future tax assets.
Financial statement considerations	• Consider whether there an appropriate process in place to do a comparison of the draft financial statements to the requirements in the handbook to identify presentation and disclosure deficiencies?
Significant/unusual transactions	• Consider whether the enterprise will be impacted by any significant or unusual transactions? If so, did management consider how the financial statements will be impacted and what information needs to be disclosed? • Consider how users will be impacted or perceive the financial statement impacts?

Q&A

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