

# Investments, Section 3051 — Background Information and Basis for Conclusions

## Foreword

In June 2019, the Accounting Standards Board (AcSB) amended INVESTMENTS, Section 3051 in Part II of the CPA Canada Handbook – Accounting. The AcSB has approved for publication the contents of this document setting out its rationale for the amendments.

Background Information and Basis for Conclusions documents are sources of generally accepted accounting principles, as described in GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100 in Part II of the Handbook. These documents are intended to help readers understand how the AcSB reached its conclusions, but they do not include explanations of requirements or guidance on the application of the relevant Section or Accounting Guideline.

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## INTRODUCTION

- 1 This document summarizes considerations that were deemed significant by members of the AcSB in reaching their conclusions to amend INVESTMENTS, Section 3051 in Part II of the CPA Canada Handbook – Accounting. This document sets out the reasons the AcSB undertook the project to develop the amendment, the process of research and deliberation, the key decisions made and the principal reasons for adopting the positions taken and rejecting others. Individual AcSB members gave greater weight to some factors than to others.
- 2 Nothing in this document is to be taken as overriding the requirements of the Handbook. However, the discussion may help readers understand how the AcSB reached its conclusions in developing the amendment and the Board's intent with respect to its interpretation and application.

## BACKGROUND AND EFFECTS ANALYSIS

- 3 Stakeholders informed the AcSB that the scope of paragraph 3051.07A is unclear. Specifically, stakeholders observed that it was not clear whether this paragraph, which relates to the application of the cost method, also applies to interests in jointly controlled enterprises accounted for using that method. Consequently, the Board decided to amend Section 3051 to clarify that paragraph 3051.07A also applies to investments in jointly controlled enterprises (JCEs) accounted for using the cost method.
- 4 In developing this amendment, the AcSB considered the consequences of adopting it relative to the objective of financial statements and the benefit versus cost constraint. As described in FINANCIAL STATEMENT CONCEPTS, paragraph 1000.12, the "objective of financial statements is to communicate information that is useful to investors, creditors and other users ('users') in making their resource allocation decisions and/or assessing management stewardship."
- 5 A primary effect of the amendment is to reduce the potential diversity in practice by clarifying that the guidance relating to the cost method in Section 3051 also applies to interests in JCEs accounted for using the cost method.
- 6 Having considered the effects of the change to Section 3051 discussed above, the AcSB thinks that the amendment will result in improvements to financial reporting.

## DEVELOPMENT OF THE AMENDMENT

- 7 Throughout the development of the amendment, the AcSB followed its due process. This process included:
- (a) ongoing input from its Private Enterprise Advisory Committee (Advisory Committee);
  - (b) issuance in September 2018 of the Exposure Draft, "Investments"; and
  - (c) analysis and consideration of feedback received through written responses to the Exposure Draft (eight comment letters).
- 8 The AcSB received written responses to the Exposure Draft from seven public accounting firms and a joint working group. The Board reminds stakeholders that as part of its due process related to Part II of the Handbook, unless confidentiality is requested, it makes available a public file of materials relating to completed projects, which includes response letters received.
- 9 Respondents supported the underlying principles in the Exposure Draft. However, some respondents provided additional comments suggesting changes to some of the proposals.
- 10 The specific issues addressed in this project, including the substantive comments received on the Exposure Draft and any changes made in response to those comments, are as follows.

#### **COST METHOD**

- 11 The issue arises because INTERESTS IN JOINT ARRANGEMENTS, Section 3056, refers to Section 3051 when the cost method is used to account for an interest in a JCE. In December, 2016, paragraph 3051.07A was added to Section 3051 to provide guidance on how to apply the cost method. However, paragraph 3051.07A specifies that it applies only to investments subject to significant influence. After it issued paragraph 3051.07A, the AcSB received feedback from the Advisory Committee. The Advisory Committee noted that since the guidance in paragraph 3051.07A only refers to investments subject to significant influence, it is unclear whether paragraph 3051.07A was intended to also apply to investments in JCEs accounted for using the cost method. The Advisory Committee also noted that there is no discussion in the Basis for Conclusions when paragraph 3051.07A was introduced as to whether the guidance also applies to investments in JCEs.
- 12 Consequently, the Advisory Committee advised, and the AcSB agreed, that the scope of paragraph 3051.07A be clarified to specify that it also applies to investments in JCEs accounted for using the cost method. All but one respondent agreed with this proposal. The respondent who did not agree thought that the scope of paragraph 3051.07A was sufficiently clear that it also applied to interests in JCEs. Based on feedback from other stakeholders and to reduce potential diversity in practice, the Board decided that paragraph 3051.07A be amended to include investments in JCEs.

#### **EFFECTIVE DATE**

- 13 The Exposure Draft noted that if no significant changes were required to the proposals after deliberating the comments received, the AcSB planned to issue the amendment in the second quarter of 2019. In that case, the Exposure Draft proposed that the effective date of the amendment would be for fiscal years beginning on or after January 1, 2020. Respondents did not raise any concerns on the timing of the effective date. Accordingly, the amendment is applicable for annual financial statements relating to fiscal years beginning on or after January 1, 2020, with earlier application permitted.
- 13A In August 2020 the AcSB deferred the effective date of this amendment by one year to alleviate pressure for stakeholders as they navigate challenges and uncertainty created by the COVID-19 pandemic. The amendment is now effective for annual financial statements beginning on or after January 1, 2021. Earlier application is permitted and therefore, the deferral of the effective date does not prohibit stakeholders from applying the amendment in an earlier fiscal year.

#### **TRANSITION**

- 14 In developing the Exposure Draft, the AcSB proposed that the amendment should be applied retrospectively in accordance with ACCOUNTING CHANGES, Section 1506. Most respondents agreed with the proposal. However, three respondents did not agree and suggested prospective application of the amendment. These respondents noted that the amendments to Section 3051 in 2016 when paragraph 3051.07A was introduced, required prospective application. They also noted that the Board indicated in the Basis for Conclusions document accompanying the 2016 amendments to Section 3051 that requiring investors to retrospectively apply the amendments regarding application of the cost method could be time consuming and costly for some enterprises and may not provide useful information to users of financial statements. Consequently, the respondents thought that the current amendment to paragraph 3051.07A should also require prospective application. The reason was investors in JCEs that account for their investments using the cost method should not be required to apply more onerous transitional provisions than were given in 2016 to investors that hold investments subject to significant influence.
- 15 The AcSB agreed that stakeholders should not be given more onerous transition requirements than were given in 2016 to investors that hold investments subject to significant influence. Therefore, the Board decided that the amendment to Section 3051 be applied prospectively to years beginning on or after January 1, 2020.

#### **CONSEQUENTIAL AMENDMENT**

##### **FIRST-TIME ADOPTION, Section 1500**

- 16 Without a consequential amendment made to FIRST-TIME ADOPTION, Section 1500, an enterprise that applies Part II of the Handbook for the first time would be required to retrospectively apply Section 3051. However, since the AcSB

decided prospective application of the amendment to Section 3051 as described above, requiring retrospective application would entail the same difficulties that led the Board to provide transition relief. Therefore, the Board decided that a consequential amendment be made to Section 1500 to permit first-time adopters of Part II of the Handbook to apply the transitional provisions from Section 3051. The Board notes that this would be consistent with the amendment to Section 1500 when paragraph 3051.07A was issued in 2016.

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