2013 Improvements to Accounting Standards for Private Enterprises — Background Information and Basis for Conclusions

Foreword

In October 2013, the Accounting Standards Board (AcSB) released the 2013 annual improvements to accounting standards for private enterprises. The AcSB has approved for publication the contents of this document setting out its rationale for making these improvements.

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.

October 2013

INTRODUCTION

1 This document summarizes considerations that were deemed significant by members of the Accounting Standards Board (AcSB) in reaching their conclusions in approving the 2013 annual improvements to accounting standards for private enterprises. It sets out the reasons the AcSB undertook the project to improve the standards, 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 CICA Handbook – Accounting. However, the discussion may help readers to understand how the AcSB reached its conclusions in developing the standards and the AcSB's intent with respect to their interpretation and application.

BACKGROUND

3 Accounting standards for private enterprises are changed periodically through two processes: major improvements and annual improvements. Major improvements result in significant changes to accounting standards for private enterprises and are not included in the annual improvements process.

4 The purpose of the annual improvements process is to amend accounting standards for private enterprises to clarify guidance or wording and to correct for unintended consequences, conflicts or oversights. These changes are "bundled" together to reduce the number of individual changes to the standards.

5 The AcSB released an Exposure Draft, "2013 Improvements to Accounting Standards for Private Enterprises," in March 2013. The Exposure Draft proposed amendments to a number of Sections as discussed in this document. The proposed

amendments were largely in response to issues submitted to the AcSB by stakeholders. In deliberating the individual issues, the AcSB considered input from its Private Enterprise Advisory Committee.

6 Responses received were primarily from public accounting firms. Respondents generally expressed agreement with the proposals set out in the Exposure Draft.

7 The specific issues addressed in this improvements project, including substantive comments received on the Exposure Draft and any changes made in response to those comments, are in the paragraphs that follow.

BUSINESS COMBINATIONS — CONTINGENT CONSIDERATION

8 Prior to amendment, BUSINESS COMBINATIONS, Section 1582, required that contingent consideration be remeasured only on settlement. The AcSB was informed that in some cases, the contingency is resolved but payment is deferred. Several stakeholders noted that in those cases, it is unclear when the remeasurement should occur. The Exposure Draft proposed to address this issue by clarifying that remeasurement should occur when the contingency is resolved.

9 Respondents generally supported addressing this issue; however, a few respondents suggested improvements to the proposed amendments. Some respondents requested clarification in respect of when a contingency is resolved, specifically whether a contingency is resolved when the amount of the payment is known or when the condition is met. The AcSB discussed this suggestion and agreed to leave the interpretation of when a contingency is resolved to professional judgment.

10 Other respondents noted that the Exposure Draft proposals did not address situations in which the resulting asset or liability is a non-financial instrument. The AcSB discussed this issue with a number of stakeholders and concluded that such a transaction is very rare. The AcSB noted that to qualify as an annual improvement an issue must be encountered in practice with some frequency. Issues that are rare are generally not addressed as part of the annual improvements process. On this basis, the AcSB decided not to address this issue. Accordingly, the AcSB approved the amendments as exposed.

BUSINESS COMBINATIONS — DISCLOSURES

11 Prior to being amended, the disclosures in BUSINESS COMBINATIONS, Section 1582, were applicable to all business combinations, regardless of the subsequent accounting for the subsidiary. Some stakeholders noted, and the AcSB agreed, that certain of those disclosures are not of significant benefit when the subsidiary is subsequently accounted for under the cost or equity method. Accordingly, the Exposure Draft proposed that an entity disclose the following information when the subsidiary is consolidated:

(a) a condensed balance sheet showing amounts recognized as of the acquisition date for each major class of assets acquired and liabilities assumed;

(b) the amount of any gain recognized in a bargain purchase; and

(c) the amount of the non-controlling interest in the acquiree recognized at the balance sheet date and the measurement basis for that amount.

12 Several respondents addressed this proposal, raising questions of a broad nature regarding the accounting for the acquisition of a subsidiary when the acquirer will use the cost or equity method to subsequently account for the subsidiary. Those respondents were unclear whether the acquisition should be accounted for in accordance with Section 1582. The AcSB discussed those questions and agreed that the issues are broader than an annual improvement. The AcSB agreed to examine those issues further, separately from the annual improvements process.

13 Several respondents proposed that the disclosure in respect of the amount of gain recognized in a bargain purchase should be retained. The AcSB noted that bargain purchases are relatively rare and that financial statement users have expressed interest in understanding bargain purchases. On that basis, it withdrew the proposal to restrict disclosure of the amount of any gain recognized in a bargain purchase to situations in which the subsidiary is consolidated.

SUBSIDIARIES — CHANGE OF OWNERSHIP INTEREST

14 Prior to amendment, SUBSIDIARIES, Section 1590, did not address how a change of ownership should be accounted for when the cost or equity method is used to account for a subsidiary. Several stakeholders had requested clarification on this issue. The Exposure Draft proposed that the accounting for a change in ownership should be based on the method used to account for the subsidiary.

15 Several respondents provided comments on that proposal. One respondent requested that the AcSB provide an example illustrating a change in ownership interests. The AcSB noted that, in the creation of accounting standards for private enterprises, it was decided that detailed illustrative examples can impede professional judgment. Accordingly, the AcSB did not agree with the suggestion to add an illustrative example.

16 Other respondents raised issues relating to when an enterprise using the cost or equity method to account for a subsidiary applies Section 1582. The AcSB agreed that these issues, as well as other related issues, should be discussed along with those noted in paragraph 12. On this basis, the AcSB approved the amendments as exposed.

NON-CONTROLLING INTERESTS

17 The AcSB was informed that some stakeholders did not understand that non-controlling interests are not a deduction in determining net income. The Exposure Draft proposed amending NON-CONTROLLING INTERESTS, Section 1602, to address this issue. The AcSB also noted that Section 1602 may be unclear with respect to how exchange gains and

losses arising from translation of a self-sustaining foreign operation that are attributable to the non-controlling interest are to be allocated. Accordingly, the AcSB proposed to clarify that those exchange gains and losses should be included in the non-controlling interests component of equity.

18 Respondents agreed with the proposals. Accordingly, the AcSB approved the amendments as exposed.

FINANCIAL INSTRUMENTS — ECONOMIC COMPULSION

19 Some stakeholders noted that FINANCIAL INSTRUMENTS, Section 3856, is unclear as to whether economic compulsion should be considered in determining whether a financial instrument should be classified as a financial liability. The Exposure Draft proposed to clarify that a financial instrument that would only be redeemed as a result of economic compulsion, rather than by any contractual requirement, would not be classified as a financial liability.

20 Respondents agreed with the Exposure Draft proposals. Accordingly, the AcSB approved the amendments as exposed.

FINANCIAL INSTRUMENTS — CLARIFICATION OF HEDGE ACCOUNTING

21 The AcSB observed that the hedge accounting requirements in FINANCIAL INSTRUMENTS, Section 3856, were not achieving the intended result for a hedging relationship in which a foreign currency denominated anticipated purchase transaction is hedged by a foreign exchange forward contract and the forward contract settles by exchange of currencies before the hedged transaction is recognized. When the foreign currency received upon settlement of the hedging contract is held continuously between the date the forward contract is settled and the date the hedged purchase transaction is recognized, the foreign currency does not qualify as a hedge. Any gain or loss on translating the foreign currency is recorded directly in income. The Exposure Draft proposed that the foreign exchange gain or loss on the foreign currency held would be presented as a separate component of equity until the purchase is recognized, at which time it would be transferred to the carrying amount of the asset acquired or to net income in accordance with paragraph 3856.33(a).

22 Respondents agreed with the Exposure Draft proposals. The AcSB confirmed that the amendment cannot be applied to hedges of anticipated sales transactions. The amendments were finalized with a further clarification that the foreign currency received upon settlement of the foreign currency forward contract must be held continuously over the period from the date the forward contract is settled until the date the hedged transaction is recognized.

EFFECTIVE DATE AND TRANSITIONAL PROVISIONS

23 The Exposure Draft proposed that the amendments be effective for annual financial statements beginning on or after January 1, 2014. Respondents agreed with this proposal and, accordingly, the AcSB finalized the effective date as proposed.

24 The Exposure Draft proposed that the amendments be applied retrospectively, with the following exceptions:

(a) In respect of the amendment regarding contingent consideration, an entity would not adjust contingent consideration that has been extinguished in periods prior to the adoption of the amendment.

(b) The proposed amendment to the hedge accounting requirements would be effective for hedging relationships in effect at January 1, 2014, with earlier application permitted for hedging relationships in effect on or after January 1, 2013.

Respondents agreed with the proposals. Accordingly, the AcSB finalized the transitional provisions as proposed.
