Accounting Standards for Private Enterprises (ASPE) Briefing

SECTION 3462, EMPLOYEE FUTURE BENEFITS: A FOCUS ON DEFINED BENEFIT PLANS

August 2021

FINANCIAL REPORTING

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This publication was originally published in November 2014 and was updated in August 2021. Readers are cautioned that certain aspects of ASPE may have changed since the revision date.

CPA Canada expresses its appreciation to the author, Jane M. Bowen, FCPA, FCA, for developing this Briefing and to the members of the Employee Future Benefits ASPE Briefing Task Force for their contribution to its preparation. Without the valued and dedicated efforts of the Task Force, this publication would not have been possible.

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Acknowledgement of Sources

CPA Canada is grateful to KPMG LLP for permission to use the example, included within Appendix D, which illustrates the roll-forward technique.

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PART A
Introduction

Does This Standard Apply to Small Businesses?

More often than might be expected, the answer is yes. Section 3462, *Employee Future Benefits* in Part II of the *CPA Canada Handbook – Accounting* (*Handbook*) applies to many benefits provided to small business employees. These benefits include, but are not limited to, pensions and other formal benefit plans. A key challenge, therefore, is to be able to identify those situations where Section 3462 applies. Appendix A provides some guidance on this issue and Appendix B provides a checklist to help you assess the applicability of Section 3462.

Purpose and Scope of This Briefing

This Briefing is primarily designed to assist in the application of Section 3462 for private Canadian companies applying ASPE. This Briefing will:

- help identify those situations where the standard applies
- focus on obtaining an understanding of the issues related to the application of Section 3462 specifically for defined benefit plans
- answer frequently asked questions (FAQs)
- provide illustrative examples

This Briefing will focus on private enterprises, but it should be noted that the guidance in Section 3462 applies to not-for-profit organizations (NFPOs) that choose to apply Part III, Accounting Standards for Not-for-Profit Organizations of the *Handbook*. Section 3463, *Reporting Employee Future Benefits By Not-For-Profit Organizations* in Part III of the *Handbook* indicates that an NFPO applies Section 3462 in Part II of the *Handbook* for those matters not addressed in Section 3463 (see paragraph 3463.01). The most significant difference for NFPOs is that “remeasurements and other items” (discussed later in this Briefing) are recorded through net assets for NFPOs but are recorded in the income statement under ASPE.

Effective Date

Section 3462 is effective for annual financial statements relating to fiscal years beginning on or after January 1, 2014. Since that date, there have been two sets of amendments which generally focus on the policy choice related to the method used to measure a defined benefit obligation (DBO).

The first set of amendments to Section 3462 were issued in October 2015 to clarify when an enterprise can use a funding valuation in the measurement of a DBO. These amendments apply to annual financial statements relating to fiscal years beginning on or after January 1, 2016.

The second set of amendments to Section 3462 were issued in November 2020 in order to:

- clarify the measurement of a DBO for plans with a legislative, regulatory or contractual requirement to prepare a funding valuation
- remove the accommodation to allow for the use of a funding valuation for defined benefit plans without a funding valuation requirement

These amendments apply to annual financial statements relating to fiscal years beginning on or after January 1, 2022. Earlier application is permitted, but only if applied to all of an enterprise's defined benefit plans at the same time.

Transitional provisions

Transitional rules and guidance are included in Appendix E of this document. Section 1500, *First Time Adoption*, provides guidance on the preparation of an entity's first set of financial statements presented in accordance with ASPE.

Frequently Asked Questions

Below are answers to some frequently asked questions about Section 3462:

1. Which items fall within the scope of Section 3462?

Section 3462 captures benefits (e.g., compensation) that are earned by employees during service with an enterprise but which are provided when the employees are no longer in "active service."

An employee is not in active service during a time period when they are not currently rendering services to the enterprise. This may arise for a temporary period of time after which the employee will return to employment with the enterprise or this may arise because the employee is retiring from, or has been terminated by, the enterprise or will be unable to return to work due to disability. Section 3462 applies to most benefits relating to both a temporary period of inactivity as well as when an employee permanently leaves the enterprise.

In principle, Section 3462 requires that all compensation that is "promised" to employees while they are active, but which is provided to them when no longer in active service, to be accrued. The term "promised" captures the principle of both contractual and other commitments made by an employer (see paragraph 3462.002).

This general principle is applied to many different types of benefits. The benefits covered by Section 3462 fall into four categories (described in paragraph 3462.002) as summarized in the following chart:

Pension and Other Retirement Benefits	**Post-Employment Benefits**	**Compensated Absences**	**Termination Benefits**
Pension and other retirement benefits can be set up in two types of plans: • defined benefit plans • defined contribution plans	Expected to be provided after employment but before retirement		
Examples: • pension plans including Individual Pension Plans (IPPs) • other retirement benefits including the following: — life insurance — health care benefits — lump sum payments on retirement (commonly referred to as a "golden handshake")	**Examples:** • long- and short-term disability income benefits (including workers' compensation) • severance benefits • salary continuation, supplemental unemployment benefits • job training and counseling • continuation of benefits such as health care benefits and life insurance	**Examples:** • parental leaves • accumulating sick days that vest or are paid without an illness-related absence • sabbaticals that provide compensated, unrestricted time off for past service	**Examples:** • lump sum payments • periodic future payments • enhancement of post-employment benefits, either under an existing employee benefit plan or special termination benefits

2. Which items fall outside the scope of Section 3462?

Generally, employee future benefits, as the name implies, are benefits to be paid to employees in the future. Current compensation and benefits provided during active employment, therefore, are not covered by Section 3462. Some examples of these benefits are:

- wages/salaries and employer's contributions under government withholdings (i.e., CPP)
- paid vacation and paid sick leave that does not vest or accumulate beyond 12 months following the reporting period
- profit-sharing and bonuses provided in the current period or within 12 months following the reporting period
- non-monetary benefits (i.e., medical care, housing, cars and free or subsidized, goods or services for current employees) (see paragraph 3462.005)

In addition, if an enterprise provides employees with any type of stock-based compensation – such as stock options, – Section 3462 is not applicable. Rather, the enterprise should refer to Section 3870, *Stock-Based Compensation and Other Stock-Based Payments.*

3. What are the different classifications of benefit plans?

There are two main types of benefit plans: **defined benefit plans** and **defined contribution plans**. The classification of a plan must be made based on an understanding of the substance of the plan. Paragraph 3462.011 clarifies this as follows (emphasis added):

> **A particular benefit plan is classified as either a defined benefit plan or a defined contribution plan depending on the economic substance of the plan established by its terms and conditions.** A benefit plan may contain characteristics of both defined benefit and defined contribution plans but is, in substance, one or the other. For example, a benefit plan may stipulate the basis of contributions on which future benefits are determined and, because of this, appear to be a defined contribution plan. However, the plan may make the enterprise responsible for specific employee future benefits or a specified level of future benefits. In such a case, the plan is, in substance, a defined benefit plan. Another example is a pension plan in which the benefits provided are the greater of the benefits under a defined benefit plan and the benefits under a defined contribution plan. Such a plan is accounted for as a defined benefit plan.

An assessment of who bears a plan's inherent risks can help when attempting to classify the plan. An employer who provides a defined benefit plan bears the risks related to the amount of the benefit that each employee will receive, because the amount is not known with certainty until all of the benefits have been paid or have ceased to be owed. The employer is also at risk with respect to the investment returns on any of the plan assets set aside to pay for the cost of the benefits, because any shortfall from expected returns must be funded. When an employer provides benefits under a defined contribution plan, however, the employer does not assume the same risks as one who has no responsibility to make any further contributions. The employee bears the risk because the amount of the benefit is entirely dependent upon the amount of funds accumulated and the investment earnings (see paragraphs 3462.009-.010).

The characteristics and descriptions of the two types of plans are summarized in the following chart:

Type of Benefit Plans	
Defined BENEFIT Plans	**Defined CONTRIBUTION Plans**
"Benefit" is defined by the terms of the plan, and the employer must fund the obligation.	Only the contribution to the plan is defined.
Employer bears the risks related to the benefits.	Employee bears the risks related to the benefits.
Actuarial calculations are required to determine the measurement of current service cost and the DBO.	The obligation is based on amounts to be contributed in respect of the reporting period. The contribution to the plan is agreed upon, so there is little uncertainty about either the cash flow or the accounting measurement.
Section 3462 states that a defined benefit plan is "any plan that does not meet the definition of a defined contribution plan" [see paragraph 3462.006(o)].	Section 3462 states that "a defined contribution plan is a benefit plan that specifies how an enterprise's contributions to the plan are determined, rather than the benefits to be received by an employee or the method of determining those benefits [see paragraph 3462.006(p)].

Reminder: Refer to Appendix A and Appendix B to help with the classification of benefit plans under Section 3462.

4. What is an Individual Pension Plan (IPP)?

An individual pension plan is a registered pension plan designed for a single participant, though family members may also participate if they work for the same or a related employer. It is a preferred alternative to an individual RRSP for some owners of private companies. The Income Tax Act permits and prescribes the rules on the deduction of contributions to the IPP by the employer. The investment income earned within the plan is not subject to income tax. The decision to create or participate in such plans is not within the scope of this Briefing; only the accounting for such plans will be addressed.

5. Are all IPPs defined benefit plans?

In most cases, IPPs meet the definition of a defined benefit plan since they are designed as such under federal taxation rules. However, it is important to consider and carefully assess the economic substance established by the terms and conditions of the particular underlying plan agreement.

This issue was addressed in the Background Information and Basis for Conclusions document issued in 2009 by the Accounting Standards Board (AcSB) in Part II of the *Handbook*:

> **Employee future benefits**
>
> 47 The AcSB noted that most private enterprises do not have traditional defined benefit pension plans for their employees. However, in recent years, private enterprises have increasingly used "individual pension plans." The AcSB was informed that virtually all individual pension plans are defined benefit plans and that the beneficiaries of such plans are frequently the owner-managers of an enterprise. However, beneficiaries can also include key employees, minority equity investors or others. Accordingly, the issue considered was accounting for defined benefit plans of this general type.

This observation does not preclude an IPP from being classified as a defined contribution plan. It does, however, provide some insight into the classification of IPPs such that they would normally be defined benefit plans.

Reminder: See Appendix C for an example of the application of Section 3462 for an IPP.

6. Does the liability for all post-employment benefits have to be recognized before payment?

It depends on the economic nature of the benefits. If the benefits are defined and accrue to the employees as they provide services, the benefits will have to be accrued over the vesting period.

If the benefits only become a promise at the time of termination, but are payable for many years, the benefits will have to be accrued at the time of termination.

Therefore, the liability with respect to certain post-employment benefits that are not funded must be recognized if there is an obligation, even though the employer is not currently contributing cash towards it.

7. In a nutshell, what is the accounting for defined *contribution* plans, such as pensions under ASPE?

The full guidance for defined contribution plans is found in paragraphs 3462.013-.020. These paragraphs also address situations where funding does not match the current service costs. The following is a brief summary of the guidance:

> The current service cost is the employer's required contribution for services rendered during the period, so generally the expense for the period is the amount of the required contribution and no actuarial calculations are involved. In other words, the current service cost is measured on an undiscounted basis when the contributions fall due within the period or within twelve months thereafter. **The expense includes any amounts for past service costs from plan initiation or amendment.**
>
> The amount is recorded as an expense unless capitalization is dictated by another standard, such as amounts capitalized to inventory or property, plant and equipment.
>
> In situations where payments of required contributions are delayed (i.e., when the contributions are due more than twelve months after the reporting period), the current service cost is equal to the amount of the required contribution in the current period plus the present value of future payments that relate to services rendered during the current period.

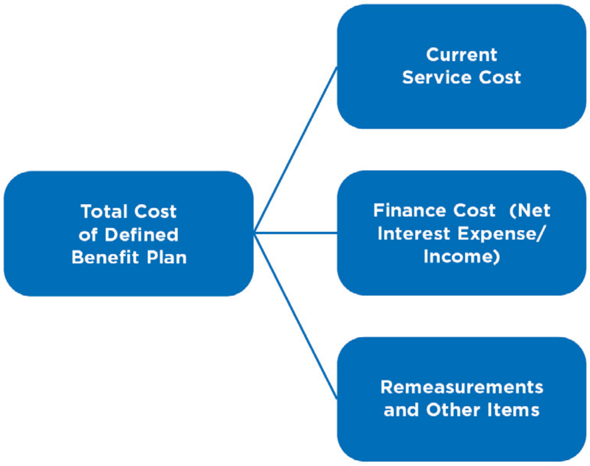
Therefore, in circumstances where contributions are due within the period (or within twelve months thereafter), all past service costs are funded and there is no capitalization of amounts to inventory or property, plant and equipment, the journal entry is simply:

General Ledger Account	Debit Amount	Credit Amount
Dr. Employee benefit expense	XX	
Cr. Cash		XX

8. In a nutshell, what is the accounting for defined *benefit* plans, such as pension plans under ASPE?

The principle for such plans is to record the cost of the benefits promised in the year in which the related service is provided. The obligation is the present value of the benefits (determined in accordance with an actuarial valuation), as defined by the plan. The guidance for an enterprise using ASPE to account for a defined benefit plan is as follows:

There are three components to the total cost of the defined benefit plan:



On the balance sheet, the net surplus or deficit is recognized as a defined asset or liability to show the funded status of the plan, with some restrictions, if a net asset results.

The accounting for defined benefit pension plans is discussed in more detail in Part B of this Briefing.

9. What is included in "remeasurements and other items"?

The term "remeasurements and other items" captures items such as actuarial gains and losses that arise when expected results do not match actual results or when assumptions change over time. These remeasurements and other items are included in the total defined benefit cost under Section 3462. The separate presentation or disclosure of remeasurements and other items permits users to better understand the income statement effects arising from defined benefit plan accounting.

As indicated in paragraph 3462.085, the amount included in remeasurements and other items is the aggregate of the following items:

- the difference between the actual return on plan assets and the return calculated using the discount rate used to determine the DBO (see paragraph 3462.077)
- actuarial gains and losses
- the effect of the valuation allowance in the case of a net defined benefit asset (see paragraph 3462.086)
- past service costs (see paragraph 3462.087)
- gains and losses arising from settlements and curtailments (see paragraphs 3462.006(z) and 3462.088-.089)

PART B
Overview of Defined Benefit Plans

Under a defined benefit plan, the benefit to which each employee will become entitled is defined (e.g., by reference to a formula based on years of service and salary over a specified period of time), and the risk of funding this benefit promise lies with the employer. A defined benefit plan can be for a pension or other benefits. A funded defined benefit pension plan consists of the pension fund assets, which are placed with a trustee or custodian, and the benefit obligation to the employees. The following discussion will focus on funded defined benefit pension plans; but it applies equally to all defined benefit plans. For those defined benefits that are not funded, there will be no fund assets and the focus will be on the accounting for the obligation.

Pension Plan Assets

For a funded plan, contributions made by the plan sponsor or plan members are made to a pension fund. Once made, the amounts are invested in line with the plan sponsor's investment policy. The value of the assets of a pension fund:

- increases when the employer or the employee makes contributions to the fund, and when the assets generate a positive return
- decreases on payment of benefits and expenses and when investment losses are incurred

Pension Plan Obligation

The obligation of a pension plan to its members is measured as the expected present value of all of the payments to be made to members when they retire, based on the service they have already rendered over their working lives under the plan. The amount of the obligation:

- increases each year as the employee works and earns additional pension benefits
- may increase or decrease as future benefits payable to employees change
- decreases when benefits are paid out
- may increase or decrease based on changes to the actuarial assumptions
- increases at the discount rate due to the passage of time

Neither the pension plan assets nor the pension plan obligations themselves appear on the employer's financial statements. The defined benefit liability, however, must be recognized under Section 3462. Any net benefit asset will only be recognized after consideration of whether the asset can be realized by the enterprise – in other words, the "ceiling test" or cap on the pension asset must be assessed (see paragraphs 3462.067-.075). The guidance in Section 3462 ensures that the appropriate measurement and disclosures are provided to "tell the full story" of the plan's funded position.

In a defined benefit pension plan, the future benefit can be estimated. Many factors must be taken into account in order to estimate the current cost of the future benefit, including, but not limited to, the following:

- discount rate
- future salary increases
- future inflation rates
- employee turnover
- mortality rates
- life expectancy after retirement
- timing of retirement
- incidence of disabilities
- assumed claim costs
- health care trend rates and aging factors
- level of expenses

Measurement

The objective of Section 3462 is to ensure that the best estimate of the current expense for employee future benefits is recorded in the employer's financial statements, and the net funded position of the plan at the year-end date, net of any "asset ceiling," is recorded on the balance sheet. As indicated, actuarial methods and assumptions are required to ensure this objective is met. The measurement of the current service cost and the obligation are to be completed by an actuary.

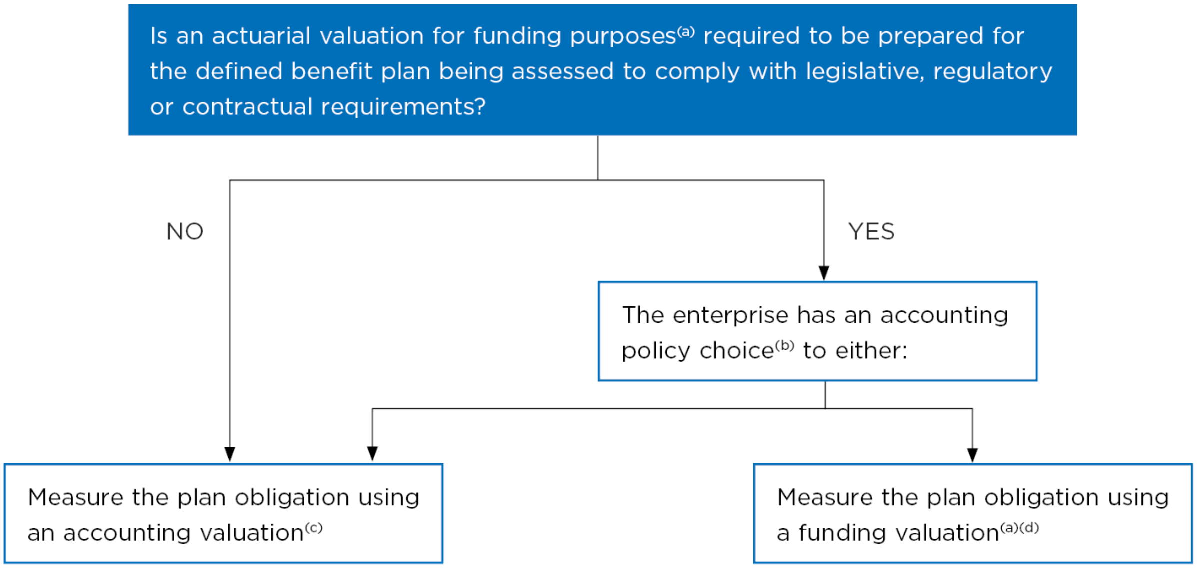
The obligation to fund a defined benefit plan differs from the accounting measurement of the expense for a specific period. Pension legislation requires funding valuations to establish an enterprise's range of funding requirements. The accounting valuation provides a measurement of the expense and obligation to meet the objectives of Section 3462.

For defined benefit plans for which there is no legislative, regulatory or contractual requirement to prepare an actuarial valuation for funding purposes, an enterprise measures the DBO as of the balance sheet date using an actuarial valuation for accounting purposes (see paragraph 3462.029AA).

An accounting policy choice to measure the DBO using a funding valuation can only be used for a defined benefit plan with a legislative, regulatory or contractual requirement to prepare a funding valuation. In such cases, the first step in the measurement process is to make an accounting policy choice as to whether measurement of the DBO will be based on the funding valuation or the accounting valuation.

The following decision tree illustrates the assessment an enterprise makes to determine when it is eligible to apply an accounting policy choice to measure the DBO for a defined benefit plan using a funding valuation:

Decision Tree – Determining Eligibility for Using a Funding Valuation to Measure the DBO for a Defined Benefit Plan[1]



(a) Excludes funding valuations prepared using a solvency, wind-up or similar valuation basis.

(b) The same accounting policy choice must be applied to each defined benefit plan for which a funding valuation is required to comply with legislative, regulatory or contractual requirements.

(c) Determined in accordance with paragraphs 3462.035-.061.

(d) Determined in accordance with paragraphs 3462.029(b), 3462.029AC and 3462.029D.

1 Source: Section 3462, *Employee Future Benefits*

Policy Choice: Funding Valuation or Accounting Valuation?

As previously indicated, Section 3462 provides an accounting policy choice on the valuation of a defined benefit plan (i.e., accounting valuation or funding valuation) if an actuarial valuation for funding purposes is required to comply with legislative, regulatory or contractual requirements (see paragraph 3462.029).

If an enterprise chooses to use an accounting valuation, then the actuarial assumptions will be based on management's best estimates and use of the appropriate method in accordance with Section 3462, depending on whether future salary levels affect the amount of the benefit. For example, if the benefit is based on an average of the last five years of salaries, then the projected benefit method would be used.

The following chart describes the funding valuation and accounting valuation policy choices:

<table>
<tr><th colspan="3">Policy Choice (see paragraph 3462.029)</th></tr>
<tr><th>FUNDING Valuation</th><th colspan="2">ACCOUNTING Valuation</th></tr>
<tr><td>The most recently completed valuation prepared by the actuary for funding purposes

The funding valuation can be used as long as the valuation is not prepared for solvency or similar situations, and the DBO is measured at the amount that is required to be funded by contributions in accordance with legislative, regulatory or contractual requirements, which could include cash contributions or a posted letter of credit (see paragraphs 3462.029D and .029AC)</td><td colspan="2">A separate valuation prepared by the actuary specifically for accounting purposes (as described in paragraphs 3462.035-.061)</td></tr>
<tr><th>Actuarial Valuation Method</th><th colspan="2">Prescribed Method</th></tr>
<tr><td>Actuarial method is selected by the actuary to comply with legislative requirements</td><td colspan="2">The valuation method is prescribed, (i.e., is not a choice) by the specific nature of the plan</td></tr>
<tr><td></td><td>Projected benefit method

When future salary levels or cost escalation affect the amount of the employee future benefits (see paragraph 3462.035)</td><td>Accumulated benefit method

When future salary levels and cost escalation do not affect the amount of the employee future benefits (see paragraph 3462.035)</td></tr>
</table>

Frequently Asked Questions

Below are answers to some frequently asked questions about the application of Section 3462 for defined benefit plans:

1. Can I use my actuarial valuation for funding purposes to determine my DBO?

Sometimes. As discussed above, there is an accounting policy choice available to use the most recently completed funding valuation, but only if an actuarial valuation for funding purposes is required to be prepared to comply with legislative, regulatory or contractual requirements. In addition, the funding valuation cannot be one that is prepared for solvency, wind-up or other similar purposes.

2. Since Section 3462 requires that the plan assets and DBO are measured at the balance sheet date, does that mean that a valuation must be completed each year and at the actual balance sheet date?

No. While the objective is to reflect the obligation/asset at the balance sheet date, there is guidance in Section 3462 as to how this can be accomplished without a full valuation being prepared each year. Paragraph 3462.062 requires that an actuarial valuation be performed every three years, or more frequently, in some cases.

For years in which a full actuarial valuation is not completed, or when the valuation is completed during the current year, but is measured at a date prior to the balance sheet date, a roll-forward technique is used. This technique is described in paragraph 3462.062.

3. What is the roll-forward technique and when is it used?

The roll-forward technique is a method of estimating an amount at a given date by using a previous estimate and rolling it forward to a later date. A roll-forward can be used, with some limitations, in the following circumstances to estimate in a practical way the:

- DBO at the end of a reporting period in the years between the actuarial valuations (i.e., within the three-year period, if applicable) (see paragraph 3462.062).
- DBO when the actuarial valuation is performed during the year and rolled forward to the year-end date (see paragraph 3462.062).
- Asset value of plan assets when market values are not readily available. For example, if the plan assets include real estate, an enterprise may obtain an independent appraisal during the year and update that valuation for known changes in conditions between the valuation date and the balance sheet date (see paragraph 3462.066).
- DBO at the date of a significant event (e.g., plan amendment) to calculate a gain or loss. When a significant event occurs, a new valuation is required, but an estimate of the DBO at the date of the significant event (or at the end of the year in which

the significant event occurs, or any date in between) can be made by using the roll-forward technique between the date of the last valuation of the DBO and the date the significant event is recognized. Professional judgment must be applied to determine whether an event is significant.

4. What guidance exists on the application of the roll-forward technique in the estimate of the DBO?

An enterprise can use the roll-forward technique in between valuations to estimate the DBO and the current service cost only if no significant events have occurred. An actuarial valuation must be completed at least every three years (see paragraph 3462.062). However, since the DBO must be measured at the balance sheet date each year (see paragraph 3462.009), a roll-forward technique is used to estimate the DBO for periods where a valuation has not been completed.

When performing a roll-forward, professional judgment must be exercised, and the following factors must be taken into account:

- the amount from the last actuarial determination of the DBO
- the increase in the obligation due to the passage of time
- the increase in the obligation due to the rendering of service in the current year
- any benefit payments (see paragraph 3462.062)

In the application of the roll-forward technique, the following guidance must be considered (see paragraph 3462.064):

- Since the DBO is the discounted value of expected benefit payments, the value of the DBO must be increased by the passage of time for one year, calculated as follows:

  DBO at end of previous period × discount rate used in the valuation

- The DBO will also increase due to the additional year of employees' service. The current service cost is estimated as follows:

  Current service cost for the prior year × (1 + discount rate used in the valuation)

An example of the application of the roll-forward technique is included in Appendix D.

5. What is a "significant event"? What does this mean for my actuarial valuation?

Section 3462 requires an actuarial valuation to be completed at least every three years, but also indicates that if a significant event takes place, a new valuation may be required. The enterprise must assess whether a significant event has taken place which requires a new valuation report. Professional judgment must be applied to determine whether an event is significant. Events that may be significant and require a remeasurement of the DBO include a settlement, curtailment or plan amendment such as a grant of benefits calculated by reference to past service. However, a significant change in the interest rate used in determining the discount rate to measure the DBO does not trigger a requirement for a new actuarial valuation (see paragraph 3462.063).

6. If my defined benefit plan is one in which an actuarial valuation for funding purposes is required to be prepared to comply with legislative, regulatory or contractual requirements and my accounting policy is to use a funding valuation, which one should I use? In other words, what does "most recently completed" mean?

Paragraph 3462.029(b) requires that if a funding valuation is used to measure a DBO, it should be "the most recently completed" one. The explanation for "the most recently completed" valuation was discussed in paragraphs 57-59 of the Background Information and Basis for Conclusion for Section 3462:

> **Paragraph 57 –** Former Section 3461 and the Exposure Draft referred to using "the most recent" actuarial valuation prepared for funding purposes. In finalizing Section 3462, some AcSB members questioned the meaning of these words. For example, should a valuation finalized shortly after the balance sheet date be used?
>
> **Paragraph 58 –** The AcSB noted that the following requirements provide users with information regarding the timing of the valuation used:
>
> - remeasurement of the defined benefit obligation at least every three years; and
> - disclosure of the effective date of the most recently completed actuarial valuation used in determining the defined benefit obligation.
>
> **Paragraph 59 –** The AcSB agreed that it did not intend that entities delay issuing financial statements by waiting for a valuation report. The AcSB also did not wish to require entities to accelerate their process of obtaining a funding valuation. The AcSB clarified that, when a funding valuation is used, the actuarial valuation of a defined benefit obligation is measured as of the balance sheet date using the most recently completed actuarial valuation.

Therefore, one must exercise judgment in determining which "the most recently completed" valuation is. "Completed" could mean completed and issued to management or it could mean that it has been filed with the regulator and tax authorities. As with all judgments, it is recommended that the policy for determining which valuation is "most recently completed" is provided in the notes to the financial statements, including the disclosure of the actual date of the valuation.

Examples

Enterprise A has a December 31 year-end and is preparing its financial statements as at December 31, 20X5. Enterprise A has a policy of measuring the DBO using the most recently completed actuarial valuation for funding purposes. Enterprise A last completed an actuarial valuation for funding purposes as at December 31, 20X2, and is in the process of obtaining one as at December 31, 20X5. The December 31, 20X5 report is:

- prepared to reflect conditions as at December 31, 20X5
- finalized by the actuary and delivered to management on May 1, 20X6
- filed with the regulator on May 15, 20X6

The following three scenarios illustrate various factors to consider when determining "the most recently completed actuarial valuation."

Scenario 1

Enterprise A authorizes the 20X5 annual financial statements for issuance on March 15, 20X6.

On the date that the financial statements are authorized for issuance, the most recently completed actuarial valuation is the funding valuation prepared as at December 31, 20X2. As stated in the Background Information and Basis for Conclusions to 3462, the requirements of the standard are not intended to accelerate the preparation of a funding valuation or hold up the release of the financial statements. Consequently, the fact that the 20X5 report is not completed should not delay the release of the financial statements. Rather, Enterprise A would use the "most recently completed" valuation, which in this case will be the December 31, 20X2 valuation, rolled forward to December 31, 20X5, using the techniques described in paragraph 3462.062.

Scenario 2

Enterprise A authorizes the 20X5 annual financial statements for issuance, on May 5, 20X6.

On the date that the financial statements are authorized for issuance, the 20X5 funding valuation has been finalized but has not yet been filed with the regulator. Enterprise A should use its judgment to determine whether "completed" for the purpose of applying paragraph 3462.029(b) is evidenced by the actuary's finalizing the valuation or the filing thereof with the regulator. Enterprise A should make this determination as part of its accounting policy related to DBOs and apply this policy consistently. Therefore:

- If Enterprise A determines that “completed” is evidenced by the finalization of the report by the actuary, then the December 31, 20X5 valuation should be used for the 20X5 financial statements.
- If Enterprise A determines that “completed” is evidenced by the filing of the report with the regulator, then the December 31, 20X2 valuation, rolled forward to December 31, 20X5, should be used for the 20X5 financial statements.

Scenario 3

Enterprise A authorizes the 20X5 annual financial statements for issuance on May 20, 20X6.

On the date that the financial statements are authorized for issuance, the most recently completed funding valuation is the December 31, 20X5 valuation. The funding valuation in this case will have been completed prior to the finalization of the financial statements.

7. Does Section 3462 prescribe which discount rate must be used for a separate accounting valuation?

No. Section 3462 does not prescribe which discount rate to be used when the plan is being valued using an accounting valuation, and some judgment is necessary. However, the selection should recognize the timing and amounts being measured, using a rate that would be suitable for similar high-quality debt instruments. Section 3462 provides the following guidance on which discount rate to use:

> 3462.047 The discount rate used to determine the defined benefit obligation shall be an interest rate determined at the date of the actuarial valuation by reference to:
>
> (a) market interest rates on high-quality debt instruments with cash flows that match the timing and amount of expected benefit payments; or
>
> (b) the interest rate inherent in the amount at which the defined benefit obligation could be settled.

Professional judgment is necessary to determine if a particular rate matches with the timing and amount of the expected payments of the benefits. The length of time expected until payment will be estimated, and the rate should be a long-term rate for high-quality debt that is for a similar length of time.

For some employee future benefits, the obligation is totally unfunded. Section 3462 does not offer any different guidance for funded or unfunded amounts, so the determination of an appropriate discount rate would also be addressed by professional judgment considering the above guidance. The discount rate and other assumptions must be disclosed to allow users of the financial statements to assess the assumptions used in measurement of the DBO.

8. What is the limit on the carrying amount of a defined benefit asset?

When there is a surplus in a defined benefit plan, this surplus may result in the recognition of an asset on the employer's financial statements. There is a requirement to limit the amount of the defined benefit asset (DBA) to be recognized in the financial statements to the amount of the expected future benefit that the employer can realize from the surplus. One benefit that can sometimes be realized is the reduction of future funding obligations. The recorded DBA cannot exceed the expected future benefit as defined in paragraph 3462.006(q).

The requirement to limit the DBA is often referred to as the "asset ceiling" or "cap." This is to ensure that the surplus of a plan is recognized only to the extent that an expected future benefit can be realized by the enterprise. The DBA is reduced to the "asset ceiling" using a valuation allowance. Any change in the measurement of the valuation allowance is recognized in income in the period that the change in measurement occurs (see paragraph 3462.067).

Example

Company A has a defined benefit pension plan with the following details:

Description	Dollar Amount
FV of plan assets	$ 900,000
Defined benefit obligation	(500,000)
Surplus	$ 400,000

It has been determined by the actuary that the expected future benefit of the surplus to Company A is only $260,000. This means that the surplus is $140,000 in excess of the benefit Company A could expect to receive. This situation requires the recognition of a valuation allowance. The allowance is recorded as follows:

General Ledger Account	Debit Amount	Credit Amount
Dr. defined benefit cost (pension expense)	$140,000	
Cr. valuation allowance		$140,000

The objective is to limit an enterprise's DBA to the amount it can expect to realize in the future. Any surplus currently in the plan may be available to reduce an enterprise's future contributions. Therefore, the value of the DBA is limited to the present value of the future cash flow streams. The appropriate rate for discounting these future cash flow streams is the same rate used in the measurement of the obligation.

9. In calculating the limit on the carrying amount of any DBA, the “expected future benefit” refers to the amount of the plan surplus that can be withdrawn in accordance with the existing plan and any applicable laws and regulations. Does this amount relate only to surplus amounts that can be withdrawn while the plan continues to be in existence?

In calculating the limit on the carrying amount of a DBA, an enterprise should ensure that the basis on which a withdrawable surplus is determined be consistent with the basis for calculating other pension accounting amounts. Accordingly, in most cases, an enterprise will assume that a plan will continue to be in effect rather than being wound up.

10. What are curtailments and settlements?

The accounting for curtailments and settlements is beyond the scope of this Briefing. However, the following references are provided:

> 3462.006 (l) A **curtailment** is an event that, under a defined benefit plan, results in:
>
> (i) a significant reduction of the expected years of future service of active employees; or
>
> (ii) the elimination, for a significant number of active employees, of the right to earn defined benefits for some, or all, of their future services.

The gain or loss from a curtailment, determined as of the date of the curtailment, is the change in the DBO resulting from the curtailment (see paragraph 3462.089).

> 3462.006 (aa) A **settlement** is a transaction in which an enterprise substantially discharges or settles all, or part, of a defined benefit obligation. A settlement is a transaction that is irrevocable, relieves the enterprise of primary responsibility for the defined benefit obligation and eliminates the significant risks associated with the defined benefit obligation and the assets used to effect the settlement. Examples of transactions that constitute a settlement include:
>
> (i) making lump-sum cash payments to employees in exchange for their rights to receive specified benefits; and
>
> (ii) purchasing non-participating insurance contracts.

Considerable professional judgment is necessary to determine the nature of the curtailment and settlement and the subsequent measurement of any gains and losses. The point is that any gain or loss should be recognized when the curtailment or settlement occurs (see paragraph 3462.063). As indicated earlier, the gain or loss on curtailments and settlement is included in remeasurements and other items.

PART C

Disclosure and Presentation for Defined Benefit Plans

The collection of disclosure and presentation requirements for defined benefit plans is included in Section 3462 and other sections, as follows:

1. Section 1505, *Disclosure of Accounting Policies* (and paragraph 3462.116)
2. Section 1508, *Measurement Uncertainty*
3. Section 3475, *Disposal of Long-Lived Assets and Discontinued Operations*
4. Section 1520, *Income Statement*
5. Section 1521, *Balance Sheet*

1. Section 1505, *Disclosure of Accounting Policies* (and paragraph 3462.116)

For defined benefit plans where an actuarial valuation for funding purposes is required to be prepared to comply with legislative, regulatory or contractual requirements, a significant accounting policy would be whether the DBO is measured using a funding valuation or an accounting valuation (see paragraph 3462.029).

An Example:

Defined Benefit Plans

The company uses the funding valuation to measure the defined benefit obligation.

It is expected that the selected valuation method be applied consistently. If a company changes its method of valuation, that would constitute a change in accounting policy and would be applied retrospectively (see paragraph 3462.117, and Section 1506, *Accounting Changes*).

2. Section 1508, *Measurement Uncertainty*

The note on measurement uncertainty should include the identification of any uncertainties related to employee future benefits.

3. Section 3475, *Disposal of Long-Lived Assets and Discontinued Operations*

Since Section 3462 addresses matters such as plan settlements and termination benefits, it is important to consider whether these events may be indicative of, or related to, discontinued operations and any disclosure or presentation requirements under Section 3475.

4. Section 1520, *Income Statement*

The amount of remeasurements and other items from defined benefit plans, if material, must be disclosed on the face of the income statement, or in the notes to the financial statements [see Section 1520, paragraph .04(s)].

5. Section 1521, *Balance Sheet*

The following items, if material, must be disclosed separately on the face of the balance sheet or in the notes to the financial statements:

- Defined benefit asset [see paragraph 1521.04A(e)]
- Defined benefit liability [see paragraph 1521.05A(b)]

Specific Disclosure Requirements for Defined Benefit Plans Under Section 3462

The disclosure requirements for defined benefit plans are as follows:

- a **general description** of each type of plan
- the **fair value of plan assets** at the end of the period
- the **DBO** at the end of the period
- the **plan surplus or deficit at the end** of the period
- any difference between the plan surplus or deficit at the end of the period and the amount recognized in the balance sheet as a result of a **valuation allowance**
- if not separately presented on the face of the income statement, the amount of remeasurements and other items for the period

- the effective date of the most recently completed actuarial valuation used in determining the DBO
- the nature and effect of significant changes in the contractual elements of the plans during the period (see paragraph 3462.115)

PART D

Other Resources

CPA Canada, ASPE Alert: Amendments to Section 3462, *Employee Future Benefits* (February 2021)

APPENDIX A

Identification and Classification of Employee Benefit Plans: Defined Benefit or Defined Contribution?

A thorough understanding of all compensation arrangements or "promises" made to employees is necessary. Once understood, one must then address the classification of a "promise" – is it contractual or does it arise from a substantive commitment? Is the plan a defined benefit or defined contribution plan? Professional judgment is required in the application of the classification process, and this process should be documented to support the conclusions reached. The following guidance provides steps to support the classification process:

Step 1	• Become familiar with **ALL** compensation arrangements
Step 2	• Read the terms of all employment contracts and plans
Step 3	• Read Section 3462 and other relevant guidance
Step 4	• Exercise professional judgment and determine whether the plan is classified as a defined benefit or defined contribution plan
Step 5	• Document conclusion

Step 1 – Become familiar with ALL compensation arrangements. Through a process of inquiry and research, identify all compensation arrangements, both contractual and constructive, to ensure that all arrangements (within the scope of Section 3462) are identified.

Step 2 – Read the terms of all employment contracts and plans. The objective of this step is to identify all future obligations that are related to current service and assess if the plan is a defined benefit or defined contribution plan. To classify a plan, management would consider the economic substance of the plan, as established by its terms and conditions. Thus, it is important to review the specific documents in detail. It is not possible to generalize about a plan's classification, as it is the specific terms of the plan that will establish its classification.

Step 3 – Read Section 3462 and other relevant guidance. It is important to be familiar with all aspects of the standard, particularly the guidance with respect to classification of plans and scope of the standard, to ensure that all required arrangements are included.

It should be noted that the definition of a defined benefit plan is in the negative (i.e., it is one that is *not* a defined contribution plan), so the analysis of a defined contribution plan should focus on whether the plan specifies how contributions are determined (rather than the amount of benefits an employee is to receive or the method for determining those benefits).

In addition, paragraphs 3462.009-.010 help distinguish between defined contribution plans and defined benefit plans, as these paragraphs discuss and explain actuarial risk and investment risk.

Review other sources. Complete research of other publications and guidance material, such as the documents included in Part D of this Briefing, if needed.

Step 4 – Exercise professional judgment and determine whether the plan is classified as a defined benefit or defined contribution plan. In considering the classification of a benefit plan, it is important that management exercises its professional judgment.

Step 5 – Document conclusion. It is always important to document the analysis and reference sources to support the conclusion reached when exercising professional judgment.

APPENDIX B

Applicability of Section 3462 Checklist

Does Section 3462 apply to any of the enterprise's benefit program?	Yes	No	Applicable Paragraph
The objective of the accounting for the cost of employee future benefits is to recognize a liability and a cost in the period in which an employee has provided the service that gives rise to the benefits. Before looking at specific items, does the enterprise have any obligations for employee benefits that have the characteristics of a liability?			3462.007-.008
Does the enterprise provide for pension benefits after retirement?			3462.002 (a)
Does the enterprise provide for health care or dental benefits, life insurance or other miscellaneous benefits after retirement? Often these benefits are in the form of a reimbursement to employees (and their dependents or beneficiaries), either directly or through an administrator. The administrator may be an insurance company, however, the benefit is not insured if the promise for future payments to retired employees and their families is a risk assumed by the enterprise. Benefits may also include direct payment to providers for the cost of specified services as the need for those services arise, or lump sum payments, such as death benefits. **Point for consideration:** Review current disbursements for benefits for employees who are no longer in active service.			3462.002 (a)
Does the enterprise directly compensate employees who are injured on the job rather than contribute to an insurance plan for workers' compensation?			3462.002 (b)

Does Section 3462 apply to any of the enterprise's benefit program?	Yes	No	Applicable Paragraph
Does the enterprise provide for continuation of benefits (e.g., health care, dental benefits or life insurance coverage) to former or inactive employees after employment but before retirement?			3462.002 (b)
Does the enterprise provide for disability benefits – short- or long-term?			3462.002 (b)
Do any employment contracts provide for severance benefits?			3462.002 (b)
Does the enterprise provide retiring allowances to employees whose employment has been voluntarily or involuntarily terminated?			3462.002 (d)
Does the enterprise have a practice of providing benefits even though such benefits are not set out in employment contracts?			3462.004
Does the enterprise provide death benefits to be paid to beneficiaries, including dependents?			3462.002 (a)-(b)
Are employees permitted to "bank" vacation days? For example, can banked vacation days accumulate and be paid out when the employee retires? If so, such vacation days are a form of compensated absence that vests or accumulates.			3462.002 (c)
Are employees permitted to "bank" sick leave? For example, are employees entitled to sick leave banks that vest?			3462.002 (c)
Are employees entitled to personal days that accumulate based on tenure?			3462.002 (c)
Are employees entitled to parental or maternity leave, such as a top-up, over and above, any government funding?			3462.002 (c)
Does the enterprise provide employees with sabbaticals that provide compensated, unrestricted time off for past services?			3462.002 (c)
Has the enterprise offered benefits in special circumstances, such as a plant closing or restructuring? These special termination benefits can cover pension, other retirement, post-employment and cash benefits as described in paragraphs 3462.002 (a) and 3462.002 (b).			3462.002 (d)

Does Section 3462 apply to any of the enterprise's benefit program?	Yes	No	Applicable Paragraph
Are benefits granted when unique situations occur that are covered by a contract, such as a union contract? For example, a contract may stipulate that benefits are to be paid when a plant closing occurs.			3462.002 (d)
Does the enterprise provide any other employee future benefits (after employment or after retirement), either contractually or expected by employees to be received as a result of past practice?			3462.002 (a)-(b)
Does the enterprise provide future benefits that may be financed through an intermediary, such as a pension plan or an insurance enterprise? These benefits are within the scope of Section 3462.			3462.004

Note: This is not an exhaustive list for all enterprises and all types of plans, but it will assist in the identification of events or transactions to assess if Section 3462 is applicable.

APPENDIX C

Illustrative Example of the Accounting for a Defined Benefit Plan

The following example is designed to illustrate the procedures required by Section 3462 in determining the total defined benefit cost for a defined benefit pension plan. The example includes those items that are most likely to be important in the annual calculation. Although the example is for a defined benefit pension, the approach is similar for all defined benefit plans.

This example shows the determination of the following amounts in the accounting for employee future benefits (with the respective paragraphs provided for reference):

- the total defined benefit cost (paragraphs 3462.076 and 3462.079)
- current service cost (paragraphs 3462.080-.083)
- finance cost (paragraph 3462.084)
- remeasurements and other items (paragraphs 3462.085-.090)

Facts

ABC Co. has an IPP for its sole shareholder and manager, which is classified as a defined benefit plan. This is not a year of transition. The following information and assumptions provided by ABC Co. and the actuary are as at the balance sheet date of December 31, 20X4:

Elements of Calculation	January 1, 20X4	December 31, 20X4
Fair value of plan assets (A)	$ 370,000	$ 426,000
Defined benefit obligation (from actuary) (B)	$ 413,000	$ 480,000
Funded status (deficit) [(C) = (A) – (B)]	$ (43,000)	$ (54,000)
Valuation allowance	$ 0	$ 0

Elements of Calculation	January 1, 20X4	December 31, 20X4
Current service cost (from actuary)[2]		$ 30,000
Discount rate		5.0%
Employer contributions during the year		$ 30,000
Benefit payments paid to employees during the year		$ 0

Calculations of Defined Benefit Cost for 20X4

Defined benefit cost for 20X4 = (1) Current service cost + (2) Interest (finance) cost + (3) Remeasurements and other items

1. Current service cost with interest for the year = $30,000 × (1+5%) = $31,500
2. Interest (Finance) cost = funded status at the beginning of the year × discount rate = $43,000 × 5% = $2,150
3. Remeasurements and other items = loss (gain) on obligations + difference between actual returns and returns using the discount rate + change in valuation allowance during the year = $14,850 – $7,500 + $0 = $7,350[3]

Defined benefit cost = (1) + (2) + (3)

= $31,500 + $2,150 + $7,350 = **$41,000**

Alternative Approach to Computing Defined Benefit Cost for 20X4

Defined benefit cost = Funded status at beginning of year + Employer contributions – Funded status at end of year

Defined benefit cost = $(43,000) + $30,000 – $(54,000) = **$41,000**

The supporting calculations for remeasurements and other items is provided below:

2 Assume current service cost provided from actuary excludes interest.

3 Refer to worksheet showing supporting calculations for remeasurements and other items (below).

Elements of Calculation	FV Plan Assets	Defined Benefit Obligation (DBO)	Defined Benefit (Liability)/ Asset [(DBL)/ DBA]	Defined Benefit Cost
Beginning of year	$370,000	$ 413,000	$ (43,000)	
Current service cost (including interest)		31,500		31,500
Benefits paid				
Employer contribution	30,000		30,000	
Expected interest on opening balance @ 5%	18,500	20,650		2,150
Expected closing value	418,500	465,150		
Actual closing	426,000	480,000		
Remeasurement / actuarial (gain) loss	**$ (7,500)**	**$ 14,850**		7,350
Expense / cost for year			(41,000)	$ 41,000
Closing balance			**$(54,000)**	

Proof of closing defined benefit liability balance	
Plan assets	426,000
DBO	480,000
Defined benefit liability	**$(54,000)**

Sample Presentation and Disclosure		
Elements of Calculation	**20X4**	**20X3**
[Paragraph 3462.115(c)] Defined benefit obligation, end of period	$(480,000)	$(413,000)
[Paragraph 3462.115(b)] Fair value of plan assets, end of period	426,000	370,000
[Paragraph 3462.115(d)] Plan deficit (Defined benefit liability)	$ (54,000)	$ (43,000)

[Paragraph 3462.115(g)] The most recent actuarial valuation was performed as of December 31, 20X4.

Cost recognized on the income statement (as part of administrative salaries and benefits)

Elements of Calulation	Dollar Amount
Current service cost	$ 31,500
Net interest cost	2,150
Remeasurements and other items	7,350
	$41,000

The general description of the plan will most likely be included in the significant accounting policies note. If it does not appear there, it will be disclosed elsewhere in the notes to the financial statements [see paragraph 3462.115(a)].

This sample disclosure is based on the assumption that ABC Co. has made a policy choice to measure the defined obligation using the most recently completed (December 20X4) actuarial valuation prepared for funding purposes (see paragraph 3462.029) and the following conditions are met:

- The funding valuation does not include a valuation prepared using a solvency, wind-up or similar valuation basis (see paragraph 3462.029D).
- The defined benefit obligation is measured at the amount that is required to be funded by contributions in accordance with legislative, regulatory or contractual requirements, which could include cash contributions or a posted letter of credit (see paragraph 3462.029AC).

The plan has a deficit, so no disclosure related a valuation allowance is required [see paragraph 3462.115(e)].

Paragraph 3462.115(f) requires the amount of remeasurements and other items be disclosed only if it is not separately presented on the face of the income statement. Therefore, there is no requirement to disclose the three components as shown above. It is shown to illustrate the different components based on the calculations in this example.

There are no significant changes in the contractual elements of the plan during 20X4 [see paragraph 3462.115(h)].

APPENDIX D

An Example of the Roll-Forward Technique

The following example illustrates the use of the roll-forward technique for the purposes of both the annual financial statements and the calculation of a settlement loss during the year. This example reflects the following assumptions:

- There were no significant changes in employee composition and salaries.
- No significant events occurred other than a settlement. The enterprise does not prepare interim financial statements and the settlement transaction is accounted for in the annual financial statements.
- In determining the amount of the DBO, the actuary reached the conclusion that the effects of the settlement, although large in terms of percentage of total assets and the DBO, resulted in a small loss that does not warrant obtaining a new actuarial valuation.
- The appropriate discount rate is 5%.

The following calculations are completed:

- The DBO increases by the discount rate to reflect the time value of money [see paragraph 3462.064(a)].
- The current service cost for the year is based on the amount of the current service cost in the prior year multiplied by 1.05 to reflect the impact of the 5% discount rate [see paragraph 3462.064(b)].
- The DBO decreases by any benefits paid [see paragraph 3462.062(d)].

When determining the current service cost, it must be remembered that, like the DBO, current service cost is a discounted value. Under Section 3462, calculation of the finance cost for the year is based on the DBO at the beginning of the year (see paragraph 3462.084). By default, the time value of money element related to the current service cost gets embedded in the measurement of the amount of the current service cost under Section 3462. It is important to assess whether the current service cost amount in the last actuarial valuation is calculated as at the end of the year. If it is not, it should be adjusted to an end-of-year amount to avoid failing to account for the time value of money element.

This example illustrates the following:

- Except for the effect of the settlement, no actuarial gain or loss results from the use of the roll-forward technique.
- The settlement transaction highlights the likely need for actuarial assistance to measure a change in the DBO attributable to a settlement transaction (the same holds true for changes in the DBO due to a curtailment or plan amendment). A settlement is identified as a possible significant event in paragraph 3462.063.
- A new actuarial valuation may not necessarily be required when no other significant events or changes affecting the measurement of the DBO have occurred.

ILLUSTRATION OF THE ROLL-FORWARD TECHNIQUE TO ESTIMATE THE DBO AT DECEMBER 31, 20X2

			Statement of Income			Balance Sheet
Elements of Calculation	**Plan Assets**	**Defined Benefit Obligation**	**Current Service Cost**	**Finance Cost**	**Remeasurements**	**Defined Benefit Liability**
Balance at December 31, 20X1	$10,000	$ (11,000)				$ (1,000)
Actual return on plan assets (Finance cost = $10,000 × 5% = $500)	600			(500)	(100)	600
Employer contributions	700					700
Employee contributions	300		(300)			300
Current service cost (Previous year current service cost = $857 × 1.05)		(900)	900			(900)
Finance cost ($11,000 × 5% = $550)		(550)		550		(550)
Benefits paid	(650)	650				
Actuarial gains and losses						
Settlement (see below)*	(1,500)	1,450			50	(50)
Balance at December 31, 20X2	**$ 9,450**	**$ (10,350)**	**$ 600**	**$ 50**	**$ (50)**	**$ (900)**

Description	Dollar Amount
Defined benefit liability, December 31, 20X1	$ (1,000)
Employer contributions	700
Current service cost	(600)
Finance cost	(50)
Remeasurements	50
Defined benefit liability, December 31, 20X2	**$ (900)**

***Settlement in 20X2**
On June 30, 20X2, the enterprise transferred $1.5 million to the locked-in retirement accounts of certain employees. Because no other significant events occurred during the period, the settlement loss at June 30, 20X2 is determined as follows:

Description	Dollar Amount
Defined benefit obligation, December 31, 20X1	$ (11,000)
Service cost to June 30, 20X2	(450)
Interest on the obligation	(275)
Benefits paid	300
Balance at June 30, 20X2 before settlement	$ (11,425)
Balance after giving effect to the settlement	(9,975)
Decrease in defined benefit obligation	$ 1,450
Decrease in plan assets	(1,500)
Settlement loss	**$ (50)**

Note: The portion of the DBO at June 30, 20X2 pertaining to the retiring employees was determined with the assistance of the plan actuaries.

Paragraph 3462.063 states that "A new actuarial valuation of the defined benefit obligation is performed in the year in which a significant event takes place. This valuation may be as of the date of the significant event, **the end of the year in which the significant event occurs, or any date in between**." Therefore, a remeasurement for a special event would not necessarily be required at the date of the settlement.

ILLUSTRATION OF THE ROLL-FORWARD TECHNIQUE TO ESTIMATE THE DBO AT DECEMBER 31, 20X3

			Statement of Income			Balance Sheet
Elements of calculation	**Plan Assets**	**Defined Benefit Obligation**	**Current Service Cost**	**Finance Cost**	**Remeasurements**	**Defined Benefit Liability**
Balance at December 31, 20X2	$ 9,450	$ (10,350)				$ (900)
Actual return on plan assets (Finance cost = $9,450 × 5% = $473)	400			(473)	73	400
Employer contributions	700					700
Employee contributions	300		(300)			300
Current service cost ($900 × 1.05 = $945)		(945)	945			(945)
Finance cost ($10,350 × 5% = $518)		(518)		518		(518)
Benefits paid	(650)	650				
Actuarial gains and losses						
Balance at December 31, 20X3	**$10,200**	**$ (11,163)**	**$ 645**	**$ 45**	**$ 73**	**$ (963)**

Elements of Calculation	Dollar Amount
Defined benefit liability, December 31, 20X2	$ (900)
Employer contributions	700
Current service cost	(645)
Finance cost	(45)
Remeasurements	(73)
Defined benefit liability, December 31, 20X3	**$ (963)**

APPENDIX E

Transition Guidance

Section 3462 has extensive transition guidance in paragraphs 3463.119 to .127. The following chart provides a summary:

Section 3462 (Paragraph Reference)	Nature of Guidance	Effective Date	Transition Guidance
.119	Effective date for Section 3462	Applies to annual financial statements relating to fiscal years beginning on or after January 1, 2014	
.119A	Effective date for October 2015 amendments	Applies to annual financial statements relating to fiscal years beginning on or after January 1, 2016	
.119B	Effective date for November 2020 amendments	Applies to annual financial statements relating to fiscal years beginning on or after January 1, 2022	Transition guidance for November 2020 amendments included in paragraphs 3462.125 to .127 (see table below)
.119C	General transition guidance	Indicates transition guidance in paragraphs 3462.120-.124 only applies when preparing annual financial statements relating to the first fiscal year in which Section 3462 is effective	The transition guidance in 3462.120 to .124 may be relevant to the first-time adoption of ASPE under Section 1500

The transition guidance in Section 3462, along with the relevant guidance in Section 1506 can be relevant in various situations, including when applying the amendments, when there is a change in accounting policy and/or upon first-time adoption of ASPE.

November 2020 Amendments

The November 2020 amendments included transitional relief, such that an enterprise is not required to:

- Obtain a new funding valuation on transition, and can wait until one is required; or
- Retroactively restate its financial statements for the effects of the amendments. The cumulative effects of applying the amendments are recorded in opening retained earnings at the date the amendments are first applied.

A summary of the November 2020 transition guidance is included in the table below:

	Enterprise Has Completed a Funding Valuation	Enterprise Has NOT Completed a Funding Valuation
Defined Benefit Plans With Funding Valuation Required Under Legislative, Regulatory or Contractual Requirements *The new measurement is at the beginning of the first fiscal year in which the amendments are first applied*	• Use that most recently completed **funding valuation** • Apply the roll-forward technique as required by paragraph 3462.062 • The cumulative effect of applying the amendments is recorded in **opening retained earnings at the date the amendments are first applied** • The financial statements of prior periods presented for comparative purposes are **not restated** [See paragraph 3462.125(a)]	• Apply the amendments **prospectively** • The effect of applying the amendments is recorded in net income in the year that such a funding valuation is completed • No adjustment to opening retained earnings [See paragraph 3462.125(b)]
Defined Benefit Plans With NO Funding Valuation Required Under Legislative, Regulatory or Contractual Requirements (or enterprise chooses to use accounting valuation)	• Apply at the beginning of the first fiscal year in which the amendments are first applied • Measure the DBO as of the balance sheet date using an **accounting valuation** (see paragraph 3462.029AA) • The cumulative effect of applying the amendments is recorded in opening retained earnings at the date the amendments are first applied • The financial statements of prior periods presented for comparative purposes are **not restated**	

Change in Accounting Policy

As discussed in this Briefing, when an actuarial valuation for funding purposes is required to be prepared for the defined benefit plan to comply with legislative, regulatory or contractual requirements, there is a policy choice to measure the DBO using an accounting valuation or a funding valuation. If an enterprise changes its policy, then the guidance in Section 1506 would be applicable, which would include retrospective application.

First-Time Adoption of ASPE

Section 1500 provides guidance on the preparation of an entity's first set of financial statements presented in accordance with ASPE.

Enterprises may face significant difficulties in retrospectively applying Section 3462 when first applying ASPE. Therefore, Section 1500 includes exemptions when preparing the opening balance sheet at the date of transition.

It is possible that upon adoption of ASPE, an enterprise may have an unamortized transitional asset or unamortized transitional obligation on the financial statements from previous accounting policies. Such balances are not carried forward into the ASPE financial statements, as indicated in paragraph 1500.16. Opening retained earnings at the date of transition are adjusted to offset this.

A first-time adopter may either adopt Section 3462 retrospectively in accordance with Section 1506, or elect under 1500.16A to apply the transitional provisions in Section 3462.

General Transition Guidance

An enterprise must apply Section 3462 retrospectively in accordance with Section 1506, with a few exceptions as specified in 3462.121 to .124. The exceptions are discussed below.

Possible changes that may be involved upon the adoption of ASPE may include:

1. Change in Measurement Date	**2. Change in Valuation Method**		**3. Change in Policy (i.e., deferral and amortization of certain amounts if applied in previous finance statements)**	
Possible Measurement Date Used	**Possible Valuation Methods**		**Possible Polices**	
From a date up to three months prior to the balance sheet date for the measurement of plan assets and the DBO	From funding valuation to accounting valuation	From accounting valuation to funding valuation	Deferred / amortized items including actuarial gains / losses and past service cost	Expensed as paid
General exception – No requirement to restate property, plant and equipment and inventory if employee future benefits costs have been capitalized (see paragraph 3462.121)				
Specific guidance and exceptions provided (see paragraphs 3462.122–.124)	No specific exceptions provided; retrospective application is required.(see paragraph 3462.120)			

The general guidance on retrospective application, with restatement, means that any measurement changes can be seen as falling into three components for financial statement presentation purposes:

1. **“Opening Adjustment”** The cumulative adjustments, if any, of the remeasurement on the first day of the comparative financial statements (the “transition date”). This cumulative adjustment is presented as an adjustment to retained earnings at the beginning of the period for the earliest comparative financial statement presented.
2. **“Comparative Adjustment”** The adjustments, if any, to the comparative amounts presented in the financial statements.
3. **“Current Adjustment, if needed”** The adjustments, if any, to the amounts presented in the current year. If the enterprise adopts Section 3462 at the beginning of the current period, no adjustments will be needed.

The adjustment for retrospective application of Section 3462 is recorded in the accounting records in the year of adoption. For presentation purposes, there must be a restatement of the financial statements, except in rare circumstances when it is impracticable to do so (see paragraphs 1506.14-.18).

For example, for an enterprise with a December year-end, the summary of the three parts are as follows:

	20X1	20X0
Component #1: "**Opening Adjustment**" Adjustment to opening retained earnings at beginning of 20X0		XX
Component #2: "**Comparative Adjustment**" Restatement of 20X0 financial statement amounts		XX
Component #3: "**Current Adjustment**" Recording of amounts in accordance with Section 3462, if not done within the 20X0 year	XX	

Transition Exceptions

Exception #1 – No need to restate asset for previously capitalized employee future benefits

When an enterprise includes costs of employee benefits in the carrying amount of its assets, such as inventories or property, plant and equipment, it is not required to restate the carrying amount of those assets at the date of application of Section 3462. The cost to change the measurement of assets retrospectively would generally outweigh the benefit, so this exception was provided as relief for companies. Employee benefits costs are capitalized if the costs for the employees that earned the benefits were relevant under Section 3031, *Inventories* (paragraphs 3031.13-.15) and Section 3061, *Property, Plant and Equipment* (paragraphs 3061.08-.12). See paragraph 3462.121.

Exception #2 – Change in measurement date

Under Section 3462, plan assets are measured at the fair value as of the balance sheet date (see paragraph 3462.065).

For DBOs for which there is **no** legislative, regulatory or contractual requirement to prepare an actuarial valuation for funding purposes, an enterprise shall measure the DBO as of the balance sheet date using an accounting valuation (see paragraph 3462.029AA).

For DBOs for which an actuarial valuation is **required** to be prepared to comply with legislative, regulatory or contractual requirements, there is a policy choice to use the most recently completed actuarial valuation prepared for funding purposes (see paragraph 3462.029).

When an enterprise previously used a measurement date prior to the balance sheet date for plan assets and the DBO rather than measuring them as of the balance sheet date, it applies the following transitional approach as per paragraph 3462.122(a)-(f):

(a) Use the measurement of plan assets and defined benefit obligations that the enterprise applied for year-end reporting for the year immediately preceding the year to which the Section is first applied, which may have been determined using a measurement date of up to three months prior to the balance sheet date. The enterprise does not remeasure plan assets and defined benefit obligations as of the beginning of the year in which this Section is first applied.

(b) Restate those measurements retrospectively to reflect any changes in accounting policies in accordance with ACCOUNTING CHANGES, Section 1506, other than the change in the measurement date. For example, an enterprise might previously have deferred and amortized actuarial gains and losses, and past service costs, for its defined benefit plans, or an enterprise may have decided to change from using an accounting valuation to a funding valuation to measure its defined benefit obligation.

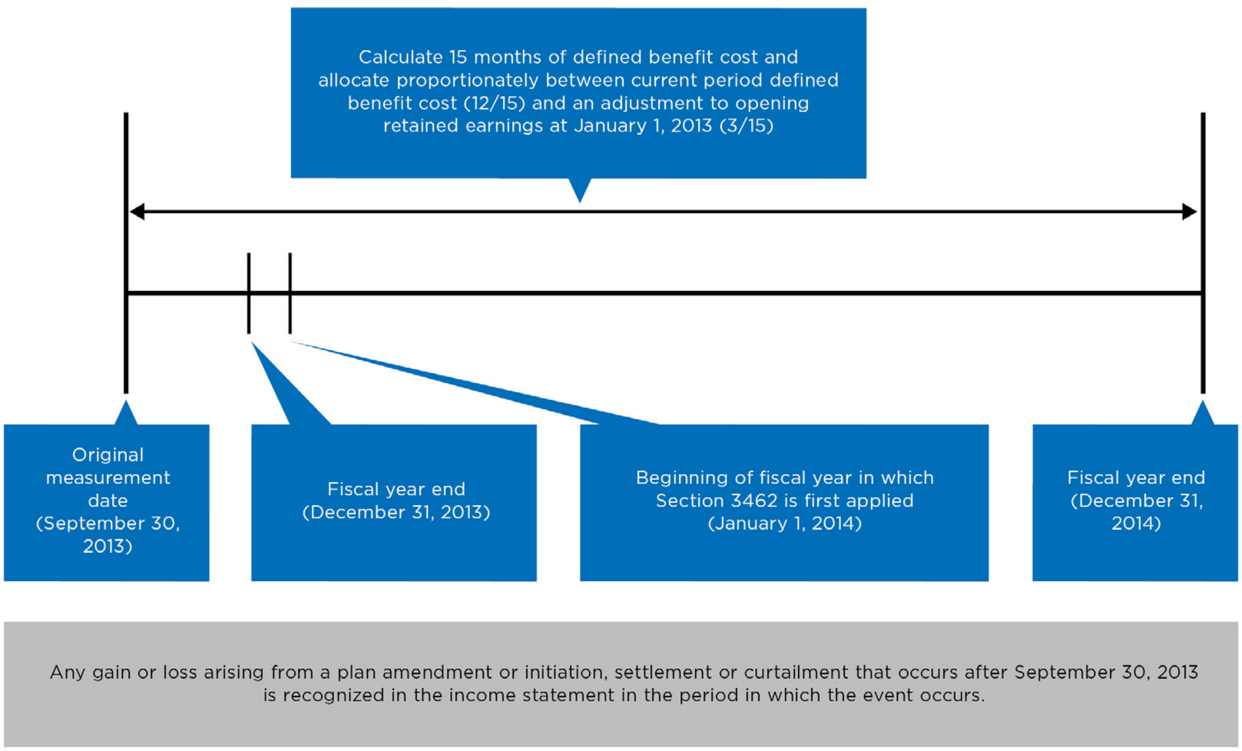
(c) Determine the defined benefit obligation as of the balance sheet date for the year in which this Section is first applied, either by an actuarial valuation as of that date or by a roll-forward of an earlier actuarial valuation prepared within the last three years in accordance with paragraph 3462.062. Determine the fair value of plan assets as of the balance sheet date for the year in which this Section is first applied in accordance with paragraphs 3462.065-.066.

(d) Using the amounts determined in (c), calculate defined benefit cost for the period between the measurement date for the year immediately preceding the year in which this Section is first applied and the balance sheet date for the year in which this Section is first applied, exclusive of any gain or loss arising from a plan amendment or initiation, settlement or curtailment.

(e) Allocate the defined benefit cost determined in (d) proportionately such that twelve months of costs are allocated to the current year, and adjust opening retained earnings for the earliest prior year presented by any remainder. For example, a calendar-year enterprise may have previously used a September 30, 2013 measurement date for the year ended December 31, 2013 and have no plan amendment or initiation, settlement or curtailment during the 15-month period between October 1, 2013 and December 31, 2014. The enterprise would allocate twelve-fifteenths of the defined benefit cost to the current period defined benefit cost for 2014 and the remainder as an adjustment to opening retained earnings at January 1, 2013.

(f) Any gain or loss arising from a plan amendment or initiation, settlement or curtailment between the measurement date that is used for the immediately preceding year and the beginning of the year in which this Section is first applied is recognized as a component of defined benefit cost in the period in which the event occurs and not as an adjustment of retained earnings.

The transitional approach for the measurement date provisions is illustrated in the following diagram using the dates from the example in paragraph 3462.122(e)[4] (above):



4 Source: Section 3462 of the *Handbook*.

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