Special Notice

December 1, 2020

AcSB finalizes changes to CPA Section 3462 regarding use of funding valuation for Employee Future Benefits

On November 2, 2020, Canada's Accounting Standards Board (AcSB) *announced* final amendments to Section 3462, Employee Future Benefits, of Part II of the CPA Canada Handbook - Accounting Standards for Private Enterprises. Because Section 3463 of Part III of the CPA Canada Handbook - Accounting Standards for Not-for-Profit Organizations follows Section 3462, the amendments apply to both private enterprises and not-for-profit organizations.

The amendments clarify the measurement of the defined benefit obligation (DBO) for retirement and post-employment benefit plans with a legislative, regulatory or contractual requirement to prepare a funding valuation. The amendments also remove the accommodation to allow the use of a funding valuation for defined benefit (DB) plans without a funding valuation requirement. While the amendments are effective for annual financial statements beginning on or after January 1, 2022, the AcSB is encouraging early adoption. Details of the changes and the impact for plan sponsors are summarized below.

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Background

In 2019, the AcSB initiated plans to amend Section 3462 based on comments from stakeholders regarding diversity in practice related to the use of a funding valuation in the measurement of the DBO for employee future benefits. In particular, regulatory changes in Ontario and Quebec had left uncertainty regarding the measurement of the DBO when the funding valuation option was chosen in Section 3462. It was unclear whether the Stabilization Provision (SP) introduced in Quebec and the Provision for Adverse Deviation (PfAD) in Ontario should be included in the DBO for DB plans funded under these rules, which resulted in diversity in practice.

In addition, it was not clear whether the SP and PfAD requirements should also be applied to DB plans without a funding valuation requirement, but which were being valued using a funding valuation for the purposes of Section 3462. This led the AcSB to reconsider allowing DB plans without a funding valuation requirement, to choose between measuring the DBO using an accounting valuation or a funding valuation.

Amendments

In response to stakeholder feedback and with the objective of eliminating the diversity in practice, the AcSB made the following amendments to Section 3462 to clarify the measurement of the DBO of employee future benefit plans:

- When determining the DBO *for plans with a legislative, regulatory or contractual requirement to prepare a funding valuation*, all components of a funding valuation required to be funded by contributions, in cash or by letter of credit, would be included in the measurement of the DBO. As a result, the measurement of the DBO would include the PfAD and SP from Ontario and Quebec, respectively. The wording is general enough that it would apply to similar requirements that may be mandated in other jurisdictions in the future.
- When determining the DBO *for plans with no legislative, regulatory or contractual requirement to prepare a funding valuation*, the DBO must be measured using an accounting valuation. As a result, the DBO for these plans is no longer able to be measured using a funding valuation even if the entity has at least one DB plan that has a funding valuation requirement. This change applies to all unfunded plans, including those that have a direct connection to a funded plan, such as a supplemental pension plan that pays benefits that cannot be paid from an underlying registered pension plan due to *Income Tax Act* limitations.

Transitional relief

To provide plans with transitional relief as a result of the amendments, the AcSB will not require plans to obtain a new funding valuation on transition but will allow plans to wait until they are required to obtain an updated valuation. Plans will not be required to make retroactive adjustments to comply with the amendments. The cumulative effect of applying the amendments will be recorded in opening retained earnings at the date the amendments are first applied.

Impact

The amendments offer increased clarity around the components of funding valuations to be included in a funded plan's DBO after several years of legislative amendments in Canadian jurisdictions. For entities that were not including the SP and PfAD in the valuation of their funded plans for their financial statements, the amendments will increase the plan's DBO recorded in the entity's financial statements and its annual cost.

A potentially greater impact to entities is the amendment to remove the ability to use a funding valuation for plans with no requirement to prepare a funding valuation. The difference in current accounting discount rates and typical discount rates used for funding valuations could result in a substantial increase in the DBO and annual cost for these plans.

Plan sponsors should consult with their actuaries to estimate the impact of these amendments on their plans and to ensure they are in compliance for their fiscal years beginning on or after January 1, 2022.

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