

MAY 2021

# RICHTER

## THE CFO SERIES

### NEW ACCOUNTING RULES FOR RETRACTABLE SHARES

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# OUR EXPERTS

NEW ACCOUNTING RULES FOR RETRACTABLE SHARES



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RETRACTABLE OR MANDATORILY REDEEMABLE SHARES  
ISSUED IN A TAX PLANNING ARRANGEMENT

*Are retractable preferred shares  
issued in a tax planning arrangement going back  
to the liabilities section of the balance sheet?*

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# REASON FOR CHANGE



**Goals of AcSB**

Greater transparency and understandability  
+  
User needs

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# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

## HIGHLIGHTS OF THE AMENDMENTS

- 

Instruments have been reclassified as to not limit the application to only those of preferred shares.
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Once a liability, always a liability.
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Shares are classified as liabilities and measured at redemption value, **UNLESS** three conditions for equity classification are met.
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Transitional relief provided.
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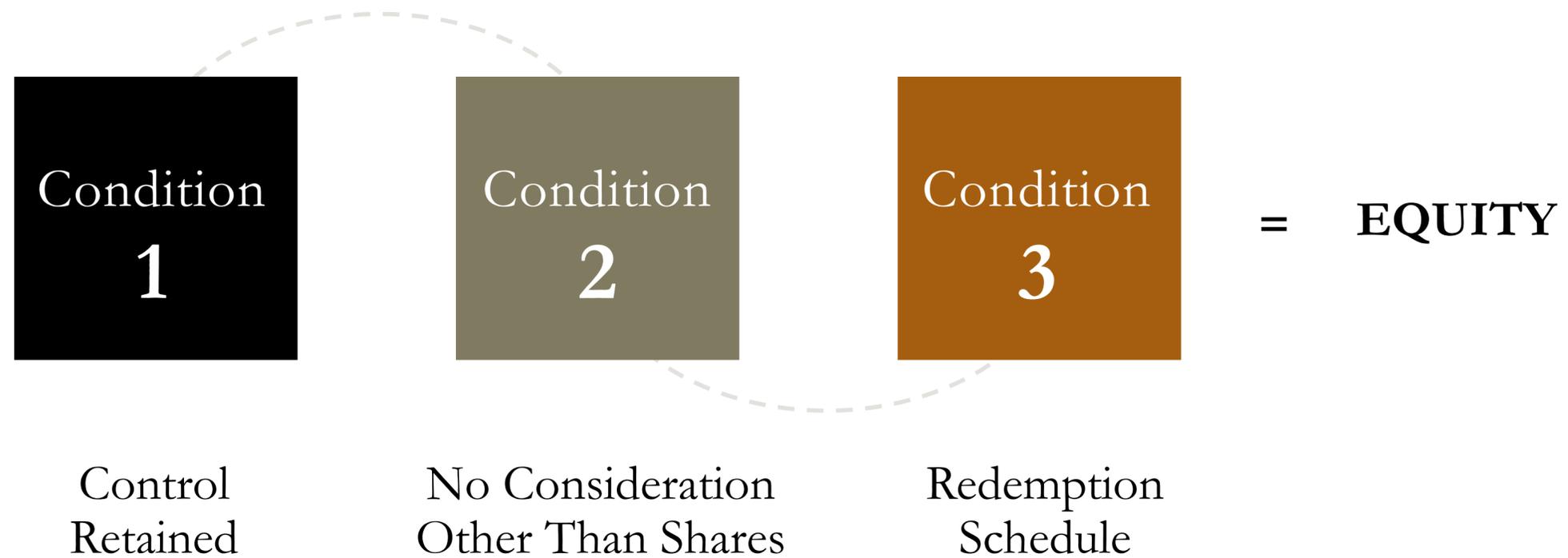
Option to classify the shares as a liability even if conditions for equity classification are met.
- 

Effective date January 1, 2021.

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

ALL **THREE** CONDITIONS MUST BE MET...

**ONLY** RE-ASSESS WHEN AN EVENT OR TRANSACTION OCCURS THAT MAY INDICATE THAT ALL THREE CONDITIONS ARE NO LONGER MET.



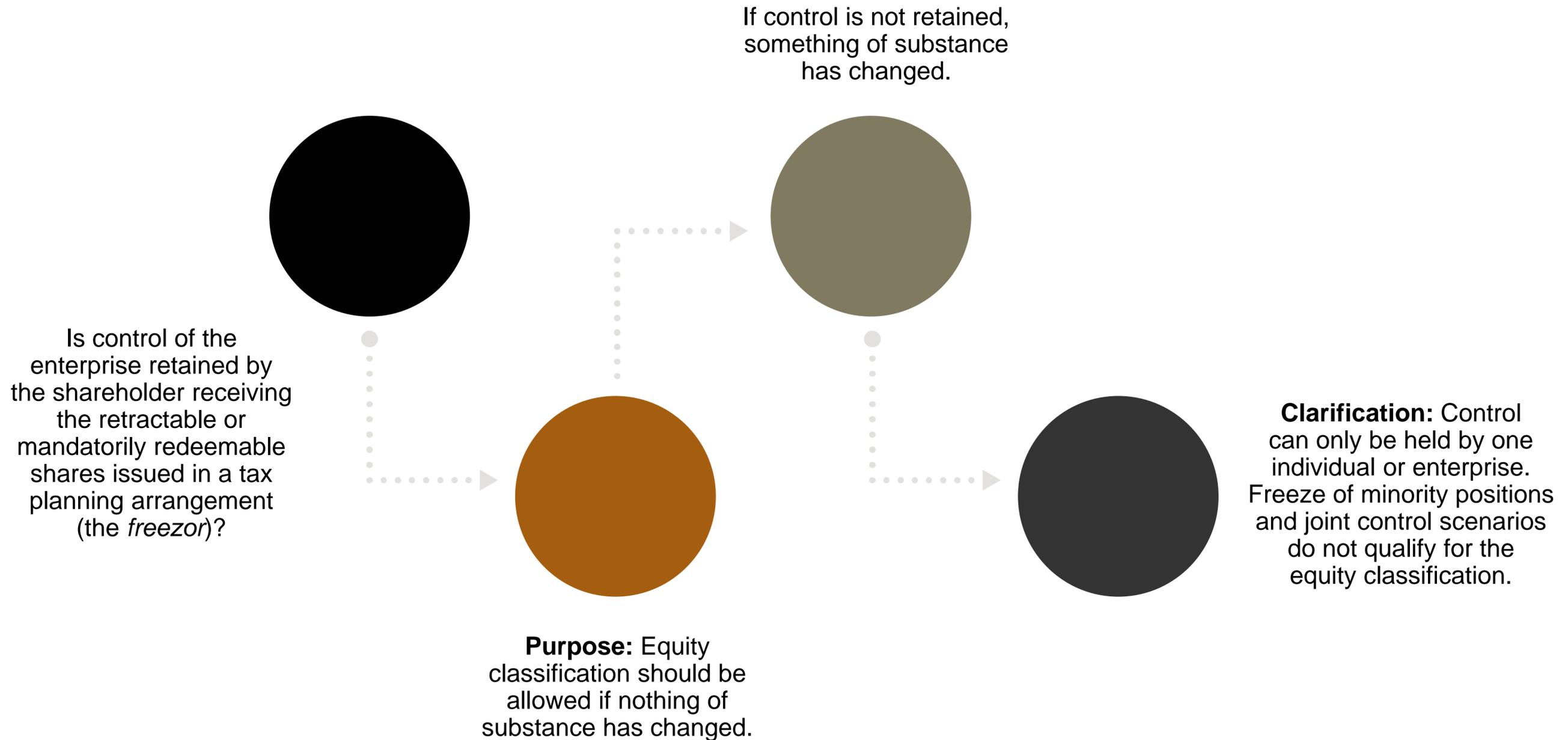
# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT NEW PARAGRAPH 23

- .23 An enterprise that issues retractable or mandatorily redeemable shares in a tax planning arrangement shall present the shares at par, stated or assigned value as a separate line item in the equity section of the balance sheet **only when all of the following conditions are met:**
- (a) control (see SUBSIDIARIES, Section 1591) of the enterprise issuing the retractable or mandatorily redeemable shares in a tax planning arrangement is retained by the shareholder receiving the shares in the arrangement;
  - (b) in the arrangement, either:
    - (i) no consideration is received by the enterprise issuing the retractable or mandatorily redeemable shares; or
    - (ii) only shares of the enterprise issuing the retractable or mandatorily redeemable shares are exchanged; and
  - (c) no other written or oral arrangement exists, such as a redemption schedule, that gives the holder of the shares the contractual right to require the enterprise to redeem the shares on a fixed or determinable date or within a fixed or determinable period.

If any of the above conditions are not met for any or all of the shares issued, the issuer shall classify those shares as a financial liability, present them separately on the balance sheet and measure them in accordance with paragraph 3856.09A. Any resulting adjustment shall be recognized in either retained earnings or a separate component of equity (see EQUITY, Section 3251).

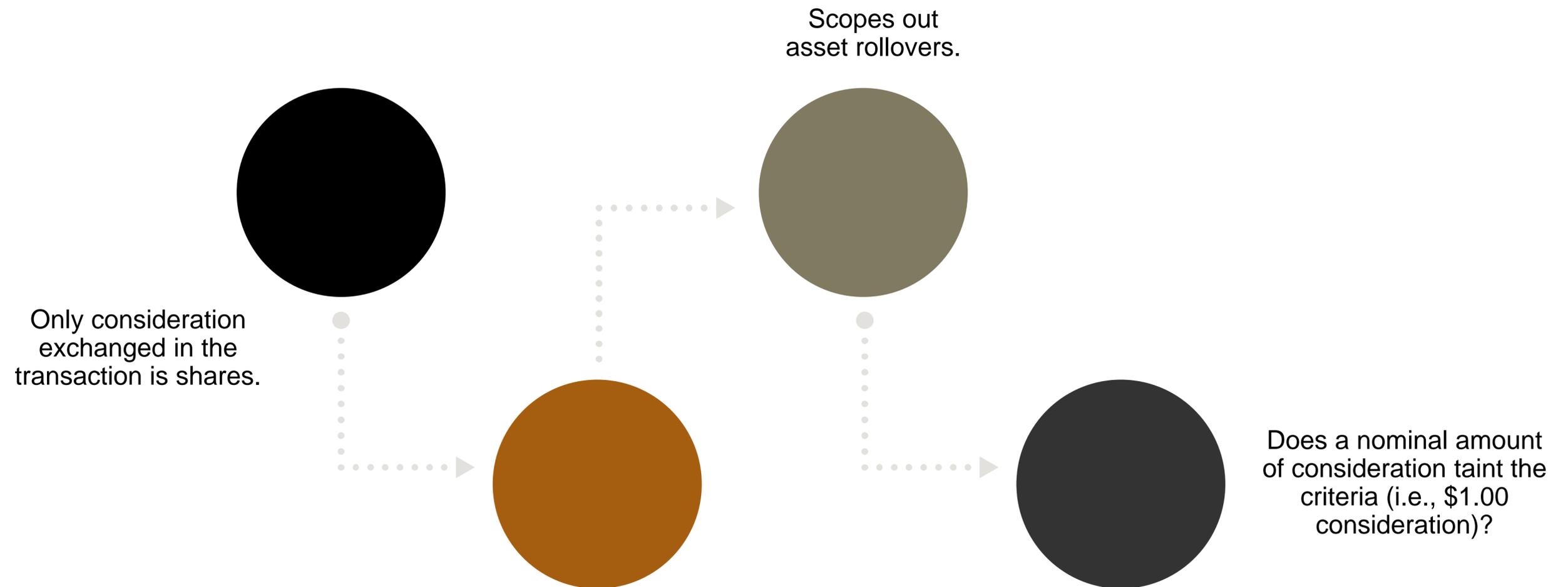
# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

**CONDITION 1 – CONTROL OF THE ENTERPRISE ISSUING THE SHARES IS RETAINED BY THE SHAREHOLDER RECEIVING THE SHARES**



# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

## CONDITION 2 – NO CONSIDERATION OTHER THAN SHARES

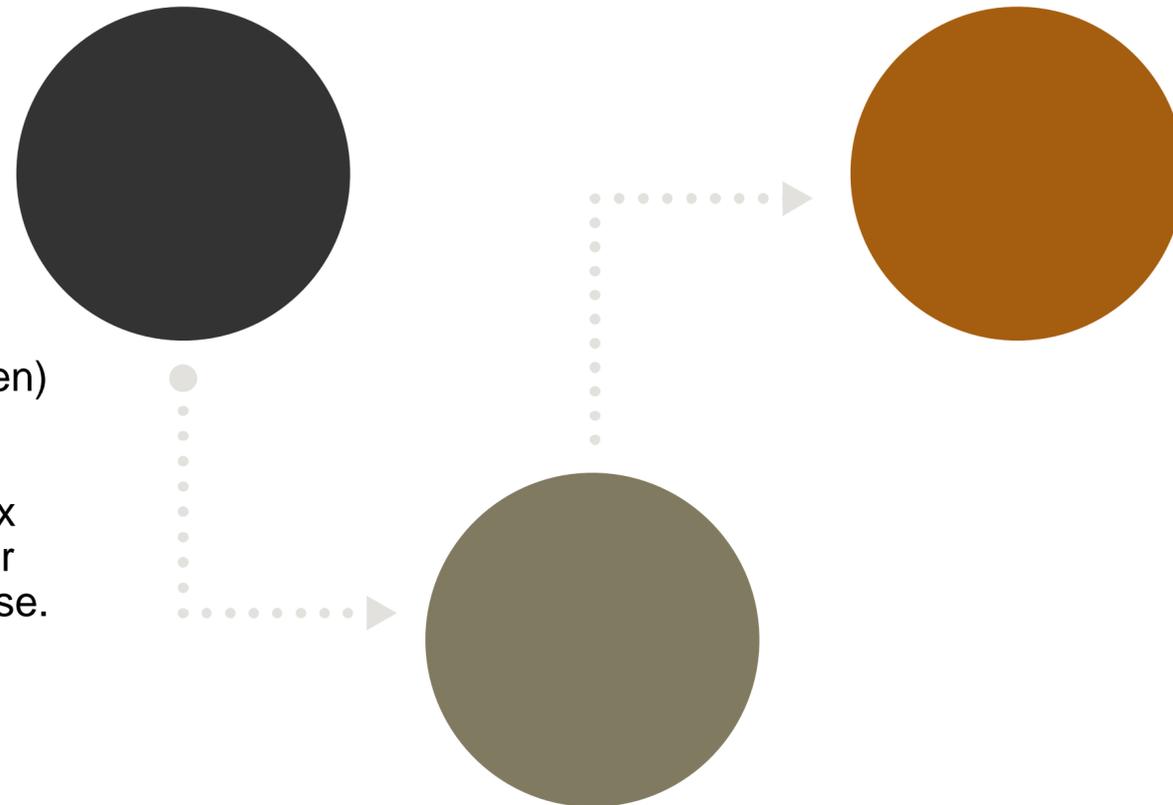


**Purpose:** Equity classification should be allowed if there is no change to the enterprise's future cash flows since nothing of substance has changed. Transactions in which other consideration is exchanged for shares are in effect financing transactions.

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

**CONDITION 3 – NO REPAYMENT ARRANGEMENT EXISTS SUCH AS A REDEMPTION SCHEDULE**

No other arrangement (oral or written) exists that requires redemption of the retractable or mandatorily redeemable shares issued in a tax planning arrangement in a fixed or determinable period by the enterprise.



The existence of a redemption schedule points to who ultimately controls the cash outflows relating to the shares.

**Purpose:** A redemption schedule would be indicative of a liability therefore in order to classify as equity, there should be no fixed or determinable period for redemption.

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

## PRACTICAL EXAMPLES

As part of a tax planning arrangement, a husband and wife who respectively hold 70% and 30% of the voting and participating shares of a corporation, exchange all but one of their shares for non-voting and non-participating retractable shares. There is no repayment arrangement. How should the retractable shares be presented?

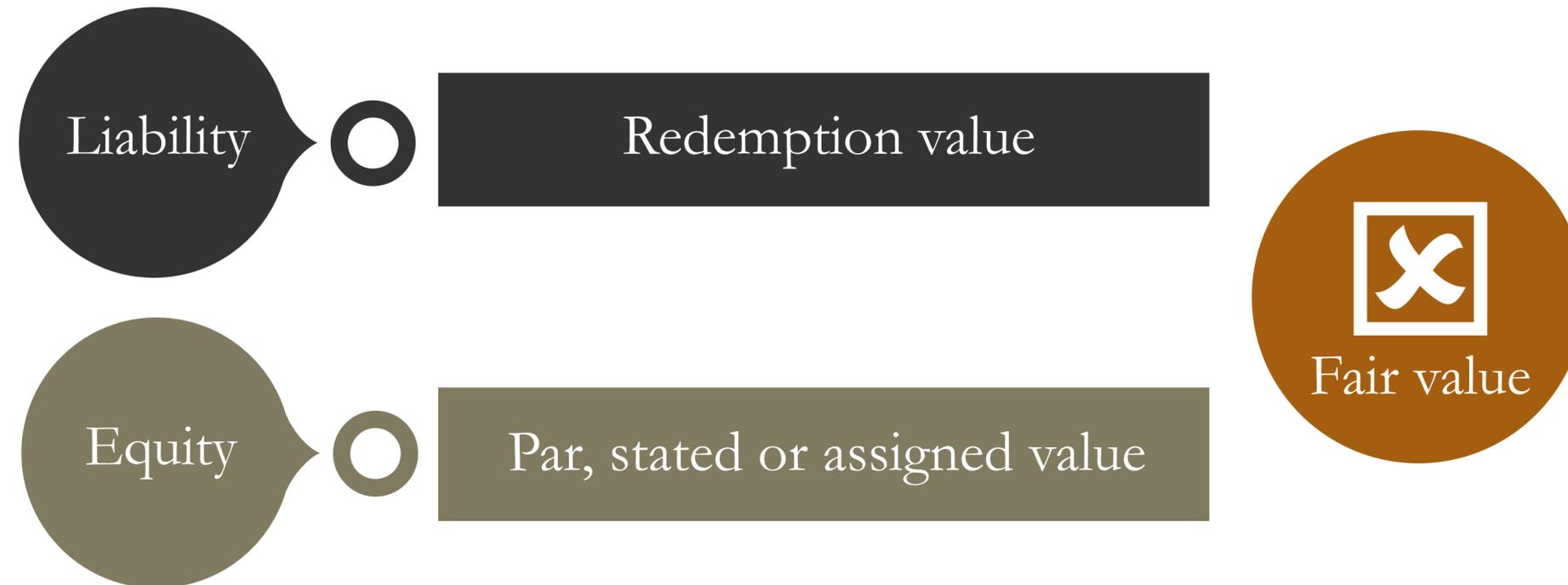
In the case of an estate freeze, four siblings who each hold 25% of the company's voting shares, exchange their shares for retractable shares. These shareholders are not related under Section 3840. New voting shares are issued in the same proportions. How should the retractable shares be presented?

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT PRACTICAL EXAMPLES

In the context of a tax freeze, a shareholder who owns 100% of the voting shares of a company exchanges its shares for retractable (non-voting) shares. New voting shares are issued, 50% to this shareholder and 50% to his spouse. How should the retractable shares be presented?

In the context of an estate freeze, a shareholder who owns 100% of the voting shares of a corporation exchanges its shares for retractable (non-voting) shares. There is no repayment arrangement. New voting shares are issued to his daughter. How should the retractable shares be presented?

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT MEASUREMENT



# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT DISCLOSURE

LIABILITY	EQUITY
<ul style="list-style-type: none"> <li>• The arrangement that gave rise to the shares;</li> <li>• Disclose on the face of the balance sheet the amount included in retained earnings; OR</li> <li>• The amount of the separate component of equity that will be reclassified to retained earnings as shares are called for redemption.</li> </ul>	<ul style="list-style-type: none"> <li>• Disclose the redemption amount of the redeemable on the face of the balance sheet.</li> <li>• The arrangement that gave rise to the shares.</li> </ul>

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT TRANSITION RELIEF PROVIDED

ONE	TWO	THREE
<ul style="list-style-type: none"> <li>• Only need to meet two conditions for equity classification of shares if they were issued <b>PRIOR</b> to January 1, 2018:               <ol style="list-style-type: none"> <li>1. Control; and</li> <li>2. No other redemption arrangement exists.</li> </ol> </li> </ul>	<ul style="list-style-type: none"> <li>• Option available to <b>NOT</b> restate comparable information.</li> </ul>	<ul style="list-style-type: none"> <li>• No need to reassess classification of shares redeemed <b>PRIOR</b> to the date the amendments are first applied.</li> </ul>

# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

## PRACTICAL EXAMPLES

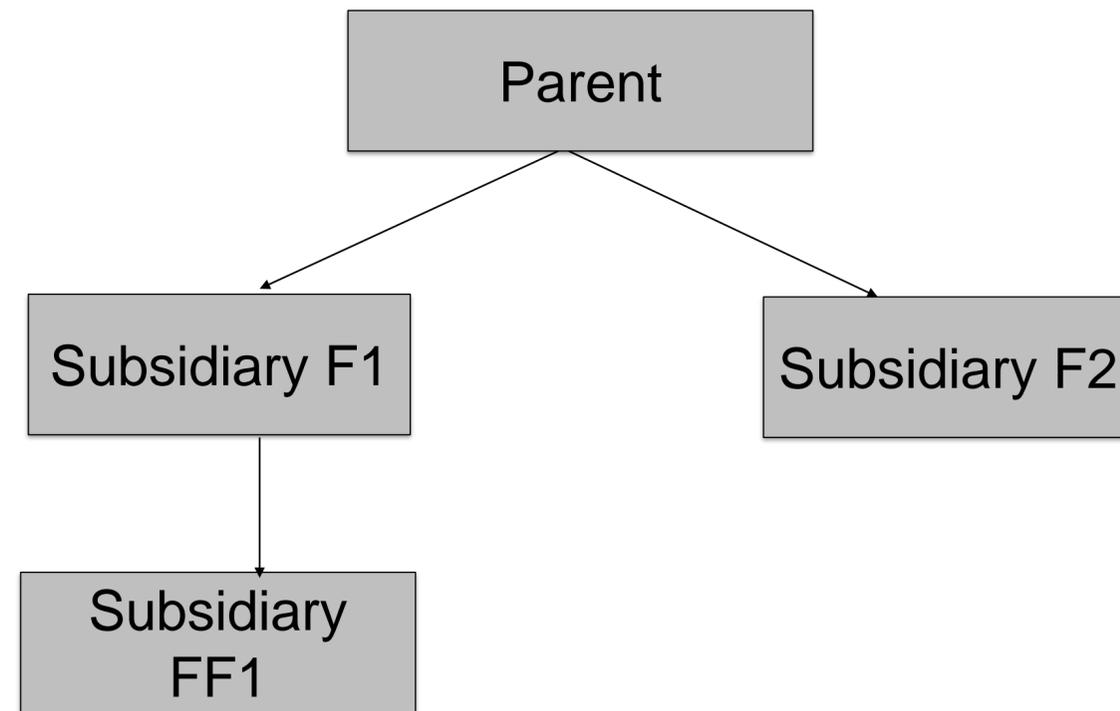
A management company is incorporated. Voting and participating shares of the Management Company are issued to Mr. X for \$ 10. Mr. X then transfers, on a tax-free basis, the voting and participating shares of an operating company that he personally holds to the management company, in exchange for retractable shares of the management company. There is no repayment arrangement. Mr. X holds 100% of the shares of the management company. The management company holds 100% of the shares of the operating company. How should the retractable shares be presented?

The parent company owns 100% of the shares of its subsidiaries; F1 and F2. The F1 subsidiary holds 100% of the shares of its own subsidiary FF1. As part of a tax rollover, F1 transfers the shares of its subsidiary FF1 to F2 under common control in exchange for retractable shares of F2. There is no repayment arrangement. How should the retractable shares be presented?

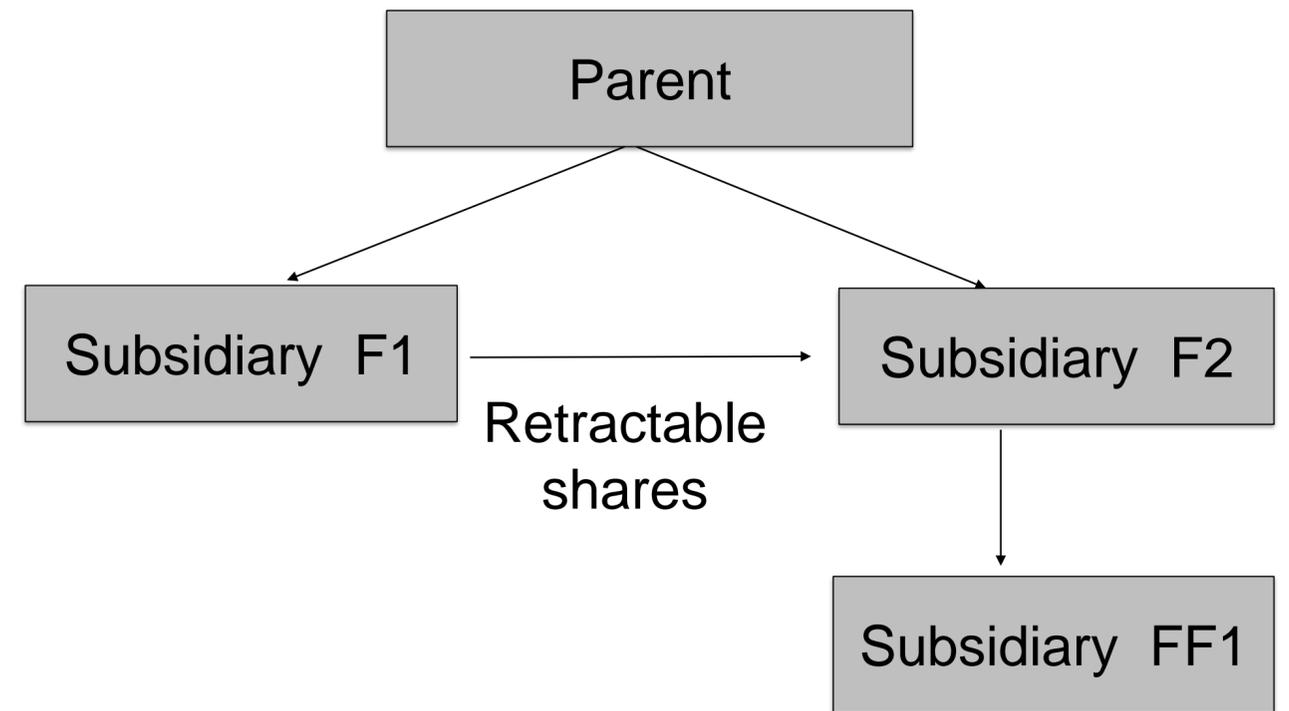
# RETRACTABLE OR MANDATORILY REDEEMABLE SHARES ISSUED IN A TAX PLANNING ARRANGEMENT

## PRACTICAL EXAMPLES

**BEFORE**



**AFTER**



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# EFFECTIVE DATE



1. The amendments will apply to annual financial statements relating to fiscal years beginning on or after **January 1, 2021**.



2. Earlier application will be permitted.

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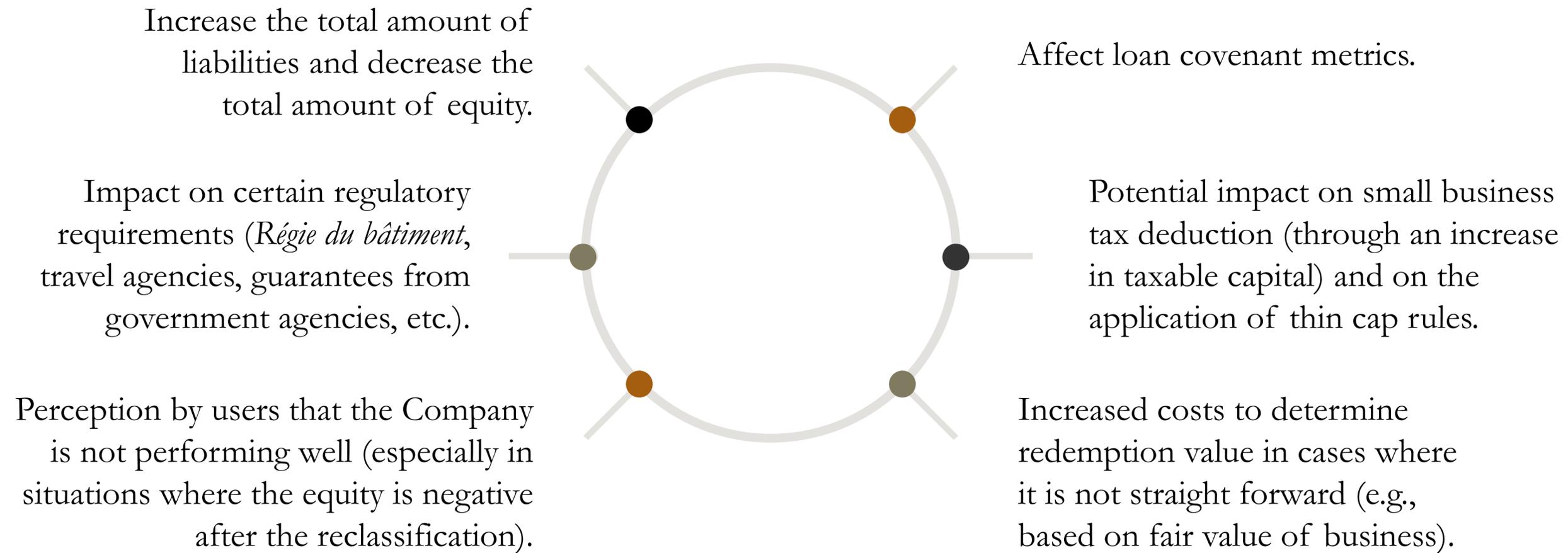
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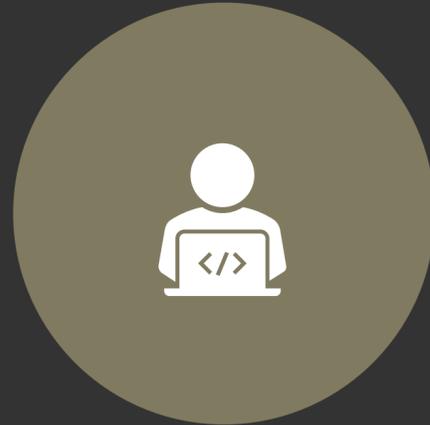
Potential Impacts

# POTENTIAL IMPACTS





CONCLUSION  
AND DISCUSSION  
QUESTIONS AND COMMENTS



NEXT WEBINAR

**New requirements for compilation engagements –**  
June 15, 2021 at 11:30 a.m.

**RICHTER**

THANK YOU!