EFRAG

European Financial Reporting Advisory Group

The costs and benefits of implementing IFRS 10 *Consolidated Financial Statements* (IFRS 10), IFRS 11 *Joint Arrangements* (IFRS 11), IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12), IAS 27 *Separate Financial Statements* (IAS 27 (2011)) and IAS 28 *Investments in Associates and Joint Ventures* (IAS 28 (2011))

Introduction

1 Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28.

2 EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. In the case of IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28, EFRAG's view is that the cost and benefit implications could be assessed by carrying out a field-test. The results of the consultations that EFRAG has carried out seem to confirm this. Therefore, as explained more fully in the appendices of this report, the approach that EFRAG has adopted has been to carry out detailed initial assessments of the likely costs and benefits of implementing IFRS 10, IFRS 11, IFRS 12, IAS 27 and IAS 28 in the EU, to consult on the results of those initial assessments, and to finalise those assessments in the light of the comments received.

3 In order to get evidence to support its overall assessment of IFRS 10, IFRS 11 and IFRS 12, EFRAG considered the effect analysis published by the IASB, held meetings with the various groups of constituents and conducted field-testing activities. The details of EFRAG's initial consultations and field-testing activities undertaken by EFRAG are included from paragraph 4 to paragraph 16.

EFRAG's initial consultations

4 EFRAG sought feedback from different groups of constituents, including preparers, auditors and users to obtain a more comprehensive understanding of costs and benefits of implementing the new requirements.

5 EFRAG discussed IFRS 10, IFRS 11 and IFRS 12 with its Insurance Accounting Working Group (IAWG) to understand how the new standards affect insurers. IAWG members indicated that the main impact on insurers resulted from the requirements on de facto control, agent/principal relationships, structured entities and disclosures. They also noted that the investment entity consolidation exemption proposed by the IASB would affect insurers.

6 To gather feedback from banks and assets managers, EFRAG discussed the requirements of IFRS 10, IFRS 11 and IFRS 12 with its Financial Instruments Working Group (FIWG). The FIWG focused on the requirements set out in IFRS 10 and IFRS 12 in the context of investment structures that are common in the financial services industry.

7 EFRAG also discussed the new proposals with the representatives of users during the September 2011 meeting of its User Panel, in order to understand users' views on the new requirements.

8 To gather feedback from the audit profession, EFRAG held a workshop in July 2011 with audit firms to discuss IFRS 10, IFRS 11 and IFRS 12.

EFRAG's field-tests

9 The field-tests of the new requirements in IFRS 10, IFRS 11 and IFRS 12 were conducted by EFRAG staff from September to November 2011, in partnership with the staff from some European National Standard Setters.

10 EFRAG staff invited companies to participate in the field-tests via a news item on EFRAG's website. In addition, a separate email was sent to National Standard Setters asking them to help identify participants. All companies that requested to participate in the field-tests were included in the study.

11 The field-tests were conducted by way of two separate questionnaires; one for IFRS 10 and the related disclosures in IFRS 12 and another for IFRS 11 and the related disclosures for joint arrangements in IFRS 12.

12 Participants were asked to review the main changes introduced by IFRS 10, IFRS 11 and IFRS 12 and to apply the new requirements to a representative sample of their investees (i.e. a selection of investees that are reflective of the range of interests that the participant holds) and their joint arrangements (i.e. a selection of joint arrangements that are reflective of the various structures and types of joint arrangements they are involved with).

13 In both questionnaires participants were asked to report any implementation and operational issues that they experienced in applying the new requirements.

14 EFRAG staff received overall 53 questionnaires (27 on IFRS 10 and 26 on IFRS 11) from the companies operating in various industry classes and in different countries. After receiving the completed questionnaires, EFRAG staff analysed them and, where necessary, contacted participants by email or phone to obtain further clarifications. The feedback reports on the results of the field-tests were presented to EFRAG TEG members and representatives of European National Standard Setters on the joined meeting of EFRAG TEG and Consultative Forum of National Standard Setters (CFSS) in December 2011.

15 Participants in the field-tests provided information to EFRAG staff on the condition that the information was kept confidential. Therefore, the reports generated from the field-tests have been written in such a way that no individual company or person could be identified.

16 The results of the field-tests were considered by EFRAG in developing its draft endorsement advices and effect study reports on the Standards. EFRAG's draft endorsement advices and effect study reports do not refer directly to the results of

the field-tests, but rather incorporate the arguments and issues identified by participants. However, the feedback statements on the field-tests of IFRS 10, IFRS 11 and IFRS 12 were published on EFRAG's website.

EFRAG's endorsement advice

17 EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB against the endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

A SUMMARY OF IFRS 10, IFRS 11, IFRS 12, IAS 28 and IAS 27

18 A summary of IFRS 10, IFRS 11, IFRS 12, IAS 28 and IAS 27 are set out in the following appendices:

(a) IFRS 10 is set out in Appendix 1A.

(b) IFRS 11 is set out in Appendix 2A.

(c) IFRS 12 is set out in Appendix 3A.

(d) IAS 27 is set out in Appendix 4A.

(e) IAS 28 is set out in Appendix 5A.

EFRAG's INITIAL AND FINAL ANALYSIS OF THE COSTS AND BENEFITS OF IFRS 10, IFRS 11, IFRS 12, IAS 28 and IAS 27

19 EFRAG's initial and final analysis of the costs and benefits of IFRS 10, IFRS 11, IFRS 12, IAS 28 and IAS 27 are set out in the following appendices:

(a) IFRS 10 is set out in Appendix 1B.

(b) IFRS 11 is set out in Appendix 2B.

(c) IFRS 12 is set out in Appendix 3B.

(d) IAS 27 is set out in Appendix 4B.

(e) IAS 28 is set out in Appendix 5B.

APPENDIX 1A – SUMMARY OF IFRS 10

Background

1 Existing IFRSs provide two sets of guidance that an entity should apply to assess control of an entity – IAS 27 *Consolidated and Separate Financial Statements* (IAS 27) uses 'control' as the basis for consolidation, while SIC-12 *Consolidation – Special Purpose Entities* focuses on 'risks and rewards'. Some believe that there is a perceived conflict between the guidance in IAS 27 and SIC-12, which has resulted in diverge application of the control definition in IAS 27.

2 The IASB's effect analysis explains that the IASB's outreach work confirmed that there are several causes for the potential inconsistent application of IAS 27 and SIC-12. In some cases, entities found it difficult to determine which investees are within the scope of IAS 27 and which are within the scope of SIC-12. As stated by the IASB, entities also noted that because the requirements are different in IAS 27 and SIC-12, they could reach different consolidation conclusions depending on which guidance is applied.

3 In addition, the existing literature lacks specific guidance with regard to some situations involving less than the majority of voting rights in investees (such as de facto control situations) and agent/principal relationships.

4 The recent financial crisis has highlighted the importance of the information provided in the notes to the financial statements, including transparency about the risks to which an entity is exposed from its involvement with other entities. These risks are mainly related to 'off-balance sheet vehicles' which an entity has set up or sponsored.

Objective of IFRS 10

5 IFRS 10 *Consolidated Financial Statements* (IFRS 10) considers the concerns expressed by users on consolidation and aims to address the diversity in practice (of assessing which consolidation model applies), by introducing a model for consolidation based on an 'ability to control' approach and provides guidance for applying that model.

6 In its Effect analysis, the IASB explains that the reason it issued IFRS 10 and the related disclosure requirements in IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12) is to articulate more clearly the principle of control. IFRS 10 defines control as consisting of three elements: power, exposure to variable returns, and the investor's ability to use that power to affect its amount of variable returns. The IASB discusses these three elements in detail throughout the standard. Existing IAS 27 and SIC-12 do not contain a detailed discussion of the concept of control, nor do they provide application guidance.

7 IFRS 12 sets out the disclosure requirements for an entity's relationships with interests in other entities (including unconsolidated structured entities) which include assumptions and judgement applied to assess control and risks an entity is exposed to through its involvement in another entity. The objective is primarily to address the concerns raised by users about lack of transparency in information about interests in other entities.

8 Taken together, IFRS 10 and the more comprehensive disclosures in IFRS 12, aim to ensure consistent application of the control definition and improve transparency of information.

What has changed?

9 IFRS 10 builds on the requirements and concepts in IAS 27 and SIC-12 with regard to the concept of control and sets out a consolidation model that applies to all investees including entities that are accounted for under SIC-12. In doing so, IFRS 10 provides additional context, explanations and application guidance on how to assess control, without changing the fundamental concept of control in IAS 27, which is based on the ability the control.

10 IFRS 10 provides guidance and illustrative examples regarding situations in which control might exist without a majority of voting rights, including situations of de facto control, agent/principal relationships and relationships with entities that are designed so that voting rights are not the dominant factor in assessing control (structured entities).

11 Under IFRS 10, assessment of control may not be the same compared to IAS 27 and SIC-12; in some cases 'more' entities might be consolidated and in other cases 'fewer' entities might be consolidated. This is primarily because of the shift in focus from 'majority of risks and rewards', to 'ability to control', and introducing a control model that applies to all investees.

12 IFRS 10 explains that there are different ways in which an investor can have power (ability to control) over an investee. In the most straightforward cases, control arises by owning more than 50 per cent of the voting rights. However, the standard explains that it is also possible that an entity controls another entity even though it has less than a majority (or half) of voting rights over the investee. This possibility depends on the assessment of all facts and circumstances affecting the investor and investee relationship.

13 Based on its assessment of the new requirements, EFRAG has considered the following new elements in the way entities will be consolidated:

(a) Ability to direct the investee's relevant activities.

(b) Power without a majority of voting rights of an investee (de facto control).

(c) Circumstances when the existence of potential voting rights give an investor power.

(d) Agent/principal relationships.

(e) Consolidation of structured entities (previously called special purpose entities 'SPEs').

14 Each of these new elements is discussed in turn below.

Ability to direct the investee's relevant activities

15 For control to exist over an investee under IFRS 10, an entity must have the ability to direct the investee's relevant activities through its ability to use power to affect its amount of variable returns.

16 The concept of 'relevant activities' is generally broader than the reference to operating and financing activities in existing IAS 27, although IFRS 10 indicates that operating and financing activities can (in some cases) be relevant activities.

17 The standard explains that for an entity to be able to apply the control model to all investees, there was a need to broaden the focus on the activities that an investor can direct (or has the ability to do so), as looking only at the operating and financing activities might not always be helpful when assessing control of some investees (such as structured entities).

18 For example, IFRS 10 explains that relevant activities include: sale of goods or services, management of financial assets, selection and acquisition or disposal of assets, management of research and development activities, and determination of funding structures. Typically, such activities are common in more conventional types of entities governed by voting rights, but perhaps less common in structured entities, which might be created with a predetermined purpose. In those entities, it might be that more than one party has decision making authority over different activities of an investee and each activity may significantly affect the investee's returns. Examples of these activities include multiple seller conduits, multi seller securitisations, and investors for which the assets are managed by one party and the funding is managed by another.

19 Furthermore, the relevant activities of an entity can change over time; and investors will need to reconsider their assessment when facts and circumstances change.

De facto control

20 Existing IAS 27 does not include guidance on de facto control, and different interpretations exist in practice. IFRS 10 extends the 'ability' to control approach to include other situations that would result in controls without a majority of voting rights. Contractual rights must be included in the assessment of control, and all substantive rights are considered by the holder of those rights in relation to an investee. Factors to consider include:

(a) Whether there are any barriers that prevent the holder from exercising the rights or, when the rights are held by more than one party.

(b) Whether the party or parties that hold the rights would benefit from the exercise of those rights (e.g. synergies).

21 To assess the existence of de facto control, IFRS 10 requires a two-step approach; in the first step, an investor should consider:

(a) size of the investor's holding of voting rights relative to the size and dispersion of the holding of other vote holders;

(b) potential voting rights held by the investor, other vote holders or other parties; and

(c) other contractual arrangements.

22 In the second step, if the above factors alone are not conclusive to determine de facto control, the following additional facts and circumstances are considered:

(a) voting patterns at previous shareholder's meetings;

(b) evidence of power;

(c) any special relationships; and

(d) level of investor's exposure to variability in returns.

23 IFRS 10 explains that, the smaller the size of the investor's holding of voting rights and the less dispersion of the holding of other vote holders, the more reliance is placed on the additional facts and circumstances, for example agreements between shareholders other than the dominant shareholder.

24 In addition, when considering the voting patterns at previous shareholder's meetings, an entity should consider the usual quorum in shareholders' meetings, and how the other shareholders vote (e.g. whether they usually vote the same way).

Potential voting rights

25 An investor might own options, convertible instruments or other instruments that, if exercised, would give the investor voting rights. These are referred to as 'potential voting rights'.

26 Similar to IAS 27, the existence of potential voting rights must be considered in assessing control under IFRS 10. However, IFRS 10 focuses on rights that are s*ubstantive* in nature and does not refer to voting rights that are 'currently exercisable' at the reporting date.

27 Assessment of control is based on the purpose, design and terms of the potential voting rights and an entity's reasons for agreeing to those terms (e.g. whether the holder of such potential voting rights has the contractual right to 'step in' and exercise its voting power to direct the relevant activities).

(a) The intention of the writer or buyer of the instrument would be considered, while under IAS 27, the intent was irrelevant.

(b) Market conditions relating to the potential voting rights are taken into account (e.g. whether or not the option is in the money), while in IAS 27 this was not considered, unless, the options lacked economic substance.

Agent/principal relationships

28 Sometimes an investor is appointed as an agent and acts on behalf of a principal. Typical examples are investment managers, asset managers and fund managers that act on behalf of a fund (e.g. real estate funds, mutual funds, pension funds and other types of investment funds).

29 Neither existing IAS 27 nor SIC-12 provide specific guidance about situations in which power is delegated to an agent and about how to assess whether a decision maker is an agent or principal. On page 27 of its effect analysis the IASB explains that the lack of guidance has resulted in diversity in practice as investors with decision making rights arrived at different interpretations about whether or not they control an investee or the fund which they manage. The IASB explains that it was often difficult to determine whether such situations were within the scope of IAS 27 or SIC-12, and a different consolidation outcome could be reached depending on which guidance was applied.

30 IFRS 10 introduces the concept of *delegated power* and provides a range of factors to consider when determining whether a decision maker is using its power as a principal (to generate returns for itself) or an agent (and uses the delegated power for the benefit of others).

31 When a single party holds substantive removal rights and can remove the decision maker without cause, this is alone sufficient to conclude that the decision maker is an agent. In the absence of such unilateral removal rights, investors would have to consider the following factors:

(a) Scope of the decision-making authority.

(b) Rights held by other parties (does any single party holds substantial removal rights).

(c) Remuneration (whether it is at market rates).

(d) The decision maker's exposure to variability of returns from other interests that it holds in the investee.

Consolidation of structured entities

32 IFRS 10 reduces the use of 'bright-lines' and increases the degree of judgement by requiring an assessment of the relevant activities of an investee rather than which investor, if any, obtains a majority of the risks and rewards of the investee. This assessment applies to all investees, including structured entities. IFRS 12 defines a structured entity as an entity where voting rights are not necessarily dominant to the assessment of control.

33 Similar to the requirements described above in relation to agent/principal relationships, in order to control a structured entity, an investor would need to have the ability to direct its relevant activities, have exposure to significant risks and rewards or rights to variable returns and the ability to affect those returns. Therefore, control conclusions could be different from those of SIC-12, which focused on which investor, if any, obtained a majority of the rewards or was exposed to a majority of the risks of the investee.

When does IFRS 10 become effective?

34 IFRS 10 becomes effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies IFRS 10 earlier, it shall disclose that fact and apply IFRS 11 *Joint Arrangements*, IFRS 12, IAS 27 *Separate Financial Statements* (IAS 27 (2011)) and IAS 28 (2011) at the same time.

35 There are no specific transitional requirements. Therefore, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, retrospective application is required. Although relief is provided in situations where retrospective application is impracticable.

APPENDIX 1B – ANALYSIS OF THE COSTS AND BENEFITS OF IFRS 10

EFRAG's initial analysis of the costs and benefits of IFRS 10

1 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IFRS 10, both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – EFRAG's initial assessment was that all preparers would incur additional costs to implement the requirements in IFRS 10, and for some preparers (particularly companies in the banking industry and insurance industry), the initial costs of implementation and conducting the required analysis would be significant, with ongoing costs being less significant and decreasing over time. Furthermore, EFRAG's initial assessment was that IFRS 10 is unlikely to result in significant costs for users.

(b) *Benefits* – EFRAG's assessment was that preparers and users are likely to benefit from IFRS 10. In particular in areas where current IFRSs was silent or contained limited guidance, the new requirements should enhance consistency of application and increase comparability for users, in a significant way.

2 EFRAG published its initial assessment and supporting analysis on 9 February 2012. It invited comments on the material by 11 March 2012. In response, EFRAG received 24 comment letters. Nine respondents agreed with EFRAG's assessment of the benefits of implementing IFRS 10 and the associated costs involved for users and preparers. Eleven respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing IFRS 10 in the EU, but supported EFRAG's recommendation that IFRS 10 be adopted for use in Europe. Four respondents did not agree with EFRAG's assessment of the benefits of implementing IFRS 10 and/or the associated costs or did not comment on this specific assessment.

EFRAG's final analysis of the costs and benefits of IFRS 10

3 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IFRS 10 is presented below.

Cost for preparers

4 The significance of the costs to preparers of implementing IFRS 10 will depend on various factors such as the number of investees, the complexity of the ownership structures of the investees with which the preparer is involved, and the preparer's involvement in structured entities.

One-off costs

<u>Reading and understanding IFRS 10</u>

5 Preparers will incur one-off costs to familiarise themselves with the new requirements and to train their employees accordingly. Those costs could also include consultations with other parties (e.g. peers and auditors) in order to establish a common understanding and consistent application of the requirements,

especially in terms of new terminology used in the standard (e.g. ‘relevant activities’, ‘significant’, ‘protection rights’).

6 For certain types of transactions, the implications of implementing IFRS 10 are relatively easy to understand. However, for other types of transactions – that require assessing control in situations involving less than the majority of voting rights including agency/principal relationships and applying a principles-based model to complex structured entities – the changes resulting from IFRS 10 will have a significant effect on the assessment of control and result in more (or less) consolidation. In these cases preparers may need to use additional resources to read and understand the elements of IFRS 10.

7 Overall, EFRAG believes that there are not likely to be any significant costs involved for preparers or users in reading and understanding IFRS 10.

Ability to direct the investee’s relevant activities

8 EFRAG notes that the term ‘relevant activities’ is broader than ‘financial and operating policies’ in existing IAS 27. Preparers will need to identify the relevant activities of their investees that significantly affect the investee’s returns, and judgement will be required in doing so.

9 The initial identification of the relevant activities of entities will be straightforward in some cases. However, when entities are involved in complex ownership structures or structured entities, the assessment can be complex and involve certain costs. These cases include situations where the relevant activities of an investee are split between multiple investors. Other cases may include situations when an entity has an interest in a structured entity and the relevant activities are set out in agreements between other investors, but where the entity does not have access (or has limited access) to that information. These more difficult situations are likely to impact banks and insurers, and have little or no impact on other preparers.

10 Some banks and insurers that engage in complex ownership structures and hold interests in many structured entities will initially need to identify the relevant activities for each type of arrangement that they are involved in. For some of those preparers, the total initial costs might be significant.

11 The term ‘relevant activities’ indicates a broader range of activities that goes beyond the term ‘financial and operating policies’; however, IFRS 10 does not provide a clear dividing line between those two approaches and neither does it define some of the terms used in the standard. For example, ‘significant’ and ‘substantive’ are not defined. As a result, preparers will need to exercise judgement and their own definitions that are consistent with the underlying principles on control, which in some cases might be difficult and time consuming, and result in preparers incurring costs.

12 To the extent that preparers need to consolidate additional entities as a result of the broader focus on which activities need to be considered in the control assessment, they will incur additional costs to set up financial systems and procedures in order to consolidate those investees. Those costs will depend on the size, complexity and number of the investees; and involve costs of issuing internal guidelines and preparing reporting packages. The complexity will vary and will depend to what extent the challenges identified in paragraph 9 affect the underlying investees.

De facto control

13 EFRAG understands that the assessment of de facto control may require a detailed review of the relevant facts and circumstances that might give an entity ability to control an investee. In some cases, the assessment will be straightforward and consideration of facts and circumstances will not entail significant judgement.

14 However, in other cases, the assessment might be challenging particularly when other shareholders are widely dispersed and have entered into agreements without the involvement of the entity making the assessment. EFRAG has learned that the main challenge will arise from obtaining the information required to assess control in situations where an entity might not legally control an entity. This challenge will generally arise when determining whether the rights held by others are substantive for the purpose of assessing control.

15 In particular, those preparers that currently do not consolidate on the basis of de facto control will need to obtain new information the first time when they make the assessments. Therefore, in some cases they will and incur additional costs. The explicit requirement that entities need to consolidate based on an 'ability to control', even though an entity holds less than the majority of voting rights, will mean a change in the scope of consolidation for some entities.

16 To the extent that preparers need to consolidate additional interests in entities on the basis of de facto control, they will incur certain additional costs to set up systems and procedures to consolidate those interests. Those costs will depend on the size and complexity of the investee, and may in individual cases be significant. EFRAG believes that to some extent the costs of interpreting and consequently implementing the requirements will be alleviated by the application guidance and the examples provided in IFRS 10, which should help with developing a common interpretation of the analysis required.

Potential voting rights

17 Similar to existing IFRSs requirements, the existence of potential voting rights must be considered in assessing control which requires preparers to collect information about the existence, terms and potential impact of the 'ability to control' another entity based on potential voting rights. Therefore, EFRAG does not expect preparers to incur significant initial costs to collect the required information.

18 However, IFRS 10 includes new requirements on whether or not potential voting rights are considered to give rise to control, and specifically requires determining whether the rights are substantive or not. Existing guidance does not focus on 'substantive' rights. Therefore, preparers will incur certain costs in reassessing the impact of existing potential voting rights when they implement IFRS 10. Overall, EFRAG does not believe that the costs of this reassessment when first implementing IFRS 10 will be significant.

19 To the extent that preparers will no longer need to consolidate certain investees, the one-off costs of this change are not expected to be significant. In situations where additional investees need to be consolidated, the costs will depend on the size and complexity of the investee. These costs would include costs of issuing internal guidelines and preparing reporting packages.

20 Overall, EFRAG believes that these requirements will not have a significant impact on the work preparers undertake to assess the effect of potential voting rights.

Agent/principal relationships

21 IFRS 10 provides guidance in relation to areas involving less than the majority of voting rights and whether an entity acts as an agent or principal when exercising decision-making authority over an investee. Current IFRSs provide limited guidance in this area. If the requirements in a standard are not clear or there is no guidance, preparers will often turn to independent advice and engage with their auditors to resolve uncertainty on how to account for a particular type of transaction. These costs would decrease if the requirements on agent/principal relationships are clearer.

22 IFRS 10 requires an entity to consider various factors when assessing control when it has decision-making rights but holds less than the majority of the voting rights. The absence of guidance in existing IFRSs will mean that currently entities might apply different accounting practices, and will need to conduct a one-off assessment to implement the new requirements. This assessment might lead to consolidation of previously unconsolidated entities and vice versa. A preparer may incur costs to determine whether it is an agent or a principal as a result of:

(a) collecting and evaluating the information about the scope of its decision-making authority, rights held by other parties, remuneration to which it is entitled and its exposure to variability of returns;

(b) conducting the analysis; and

(c) if it acts as a principal, consolidating the investee.

23 EFRAG understands that for many preparers that are banks or insurers holding interests in mutual funds, investment funds and similar entities, it might not be obvious whether the link between the power granted in the decision-making process and the returns generated indicates that they act as an agent or as a principal. Preparers will need to collect the information required to make the assessment and conduct an analysis based on various factors set out in the standard. In some cases, this might be a challenging and costly exercise.

24 For some of those preparers, particularly those that hold interests in a large number of different types of investees and/or complex structures, the total initial costs are likely to be significant. The costs are higher if an entity needs to consolidate previously unconsolidated funds.

Consolidation of structured entities

25 Additional one-off costs may be incurred by preparers to the extent that the requirement to apply a uniform basis for consolidation in IFRS 10, results in consolidation of additional structured entities.

26 Similar to the assessment of one-off costs for agent/principal relationships, the level of costs incurred will depend on the complexity of the structure of the underlying entities and the number of investees that need to be analysed. Banks and insurers are likely to be the most affected by this new requirement.

27 The change introduced by IFRS 10 in respect to the accounting for structured entities will not always result in more consolidation. In some cases, structured entities will no longer be consolidated, and therefore reduce costs for these preparers.

Transition requirements

28 IFRS 10 is required to be applied retrospectively. EFRAG notes that in some cases it can be difficult for preparers to obtain all the information about facts and circumstances, including the related financial data for prior periods. Collation of information would be more challenging when mergers and acquisitions have taken place in the past, in which case applying acquisition accounting under IFRSs might be challenging as reliable information may not always be available. Due to these factors and because of others, information for full retrospective application might not be readily available.

29 EFRAG notes that the transition requirements in IFRS 10 contain various relief provisions that reduce the cost of initial application of IFRS 10. In particular, no restatements are required regarding entities that remain consolidated and regarding entities that remain unconsolidated. Furthermore, where restatement is impracticable (as defined in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*), IFRS 10 provides relief when an entity needs to consolidate an investee that was previously not consolidated. A similar relief is available in respect of investees that are no longer required to be consolidated under IFRS 10.

30 EFRAG believes that the reliefs mentioned above will reduce the initial costs for preparers of applying IFRS 10 although for some other preparers the costs to restate prior periods will be high.

Ongoing costs

31 As explained below, the magnitude of the ongoing costs will vary from preparer to preparer and is likely to affect preparer entities that have a large number of structured entities and investees with complex ownership structures. Similar to one-off costs, preparers operating in the insurance and banking industries are most likely to be affected by the new requirements.

Ability to direct the investee's relevant activities

32 On an ongoing basis, preparers will need to monitor any changes in relevant activities of the entities in which they hold an interest. However, the relevant activities of investees are generally not expected to change often and therefore unlikely to result in significant costs to preparers.

33 In addition, preparers will need to assess the relevant activities of new interests in investees. EFRAG notes that once preparers have applied the new requirements and analysed their investees, the costs of applying the notion of relevant activities subsequently will diminish over time.

Power without a majority of voting rights of an investee (de facto control)

34 The assessment of de facto control may require, on an ongoing basis, judgement and a detailed review of the relevant facts and circumstances. However, over time preparers will develop internal guidelines necessary to collect information that is necessary to assess de facto control. Such guidelines will help preparers to address challenging situations regarding de facto control that require a high degree of judgement.

35 While preparers would incur certain costs in making these assessments, it is unlikely that there will be many business combinations on the basis of de facto

control in any particular reporting period. Therefore, ongoing costs are unlikely to be significant to preparers.

Potential voting rights

36 Under current IAS 27, preparers are already required to collect information about, and assess the impact of, potential voting rights on an ongoing basis. In addition, EFRAG notes that the ongoing costs relate mainly to those arising from new potential voting rights and the reassessment of change in facts and circumstances regarding existing potential voting rights. Overall, the ongoing cost to implement this requirement is unlikely to be significant.

Agent/principal relationships

37 IFRS 10 provides new guidance on agent/principal relationships. The new guidance would mean that preparers need to incur costs to monitor their existing relationships with investees to determine whether their role as an agent or a principal remains unchanged. In EFRAG's view, these costs should decrease over time and are unlikely to be significant as entities will develop internal guidelines to apply the requirement in a consistent manner.

38 Preparers will also incur ongoing costs from new relationships with investees. However, even for preparers in the financial services industry and insurance industry, the number of new agent/principal relationships that arise each year, is likely to be relatively small compared to the total number of such investees that they are involved with. However, entities that engage in high volumes of agent/principal relationships will need to undertake additional work in assessing whether they control the underlying funds in each relationship and should consolidate those funds based on the outcome of their assessment.

Consolidation of structured entities

39 Additional ongoing costs may be incurred by preparers that are involved in many structured entities because a preparer would need to assess whether it acts as a principal or agent in a structured entity. There would be perceived costs if their assessment would result in the consolidation of additional structured entities. Similar to the assessment of ongoing costs for agent/principal relationships, the level of costs incurred will depend on the complexity of the underlying structures and the number of investees that need to be monitored each year.

Costs for users

40 EFRAG has carried out an assessment of the cost implications for users resulting from IFRS 10.

41 Users will need to understand why the numbers in the financial statements are different and what this means when performing their analysis. They will also need to amend their models. However, these costs are unlikely to be significant.

Conclusion on costs for preparers and users

42 Overall, EFRAG's assessment is that all preparers will incur additional costs to implement the requirements in IFRS 10, and for some preparers (particularly companies operating in the financial industry and insurance industry), the initial

costs of implementation and conducting the required analysis will be significant, with ongoing costs being less significant and decreasing over time.

Benefits for preparers and users

43 EFRAG has carried out an assessment of the benefits for users and preparers resulting from the IFRS 10.

Preparers

44 One of the reasons that the IASB developed IFRS 10, was to more clearly articulate the principle of control and establish a common control approach that can be applied to all investees. This would benefit preparers because they would be able to apply the requirements in a consistent manner across investees.

45 Overall, the main benefit from the new control model in IFRS 10 for preparers is expected to be the improvement in financial communication. This should result in increased credibility of the entity's financial statements and improve the accessibility to capital markets.

46 Having a uniform basis of consolidation (based on control) will allow preparers to apply the same requirements to all investees (including structured entities) and therefore enhance comparability of information for users, which will benefit preparers. If a uniform basis of consolidation proves to result in more appropriate consolidation decisions over time, preparers will benefit from enhanced user confidence in the information presented in the financial statements, and benefit from a decrease in the cost of capital.

47 The additional guidance on de facto control, potential voting rights and agent/principal relationships is expected to reduce the existing divergence in practice, and benefit preparers.

Users

48 The main objective of IFRS 10 is to address a number of concerns expressed by users. These concerns, in particular, include divergence in the scope of consolidation (IAS 27 versus SIC-12) and lack of explicit guidance on situations involving less than majority voting rights including agent/principal relationships.

49 EFRAG acknowledges that there will be one-off costs for users. These costs particularly include time and resources to be spent to modify existing financial models to incorporate the new requirements of IFRS 10.

50 Users would have an appropriate understanding of the basis to consolidate or not to consolidate an investee because preparers will use a uniform control basis for consolidation, together with the requirement to conduct a thorough analysis of facts and circumstances that might lead to control.

51 It is likely that, overall, the usefulness of consolidated information will improve, given that consolidation will be based on a uniform basis that applies to all investees and is complemented by comprehensive application guidance to assist entities with the assessment of control. In particular, this would be the case, when entities do not have the majority of voting rights over the investee. The new requirements involving situations without the majority of voting rights (including de facto, agency/principal relationships) build on the existing control principles and

extend these principles to all investees that an entity controls. Similarly, the development of a uniform control basis (based on control) that applies to structured entities, will enhance comparability of information as entities will conduct the control assessment for all their investees using the same requirements.

52 However, the uniform basis of consolidation will entail a higher degree of judgement and use of assumptions, which might impact comparability and diminish the usefulness of information. In this respect, IFRS 12 requires comprehensive disclosure about the use of judgements and assumptions made by management in reaching consolidation conclusions. This should help users in understanding the consolidation decisions reached by management, particularly in situations involving less than a majority of the voting rights or situations involving complex ownership structures.

53 Furthermore, the disclosures required by IFRS 12 with regard to consolidated and unconsolidated structured entities help users in making a comprehensive analysis of the investor's involvement in such entities and understanding the risks and support obligations associated with those interests. EFRAG believes this will provide significant benefits for users.

Conclusion on benefits for preparers and users

54 Overall, EFRAG's assessment is that preparers and users are likely to benefit from IFRS 10. In particular in areas where current IFRSs was silent or contained limited guidance, the new requirements should enhance consistency of application and increase comparability for users, in a significant way.

Conclusion

55 To summarise, EFRAG reached the following individual conclusions on each of the areas discussed above. The following assessment combines the effects of one-off and ongoing costs to preparers and users with the benefits expected from the new requirements in IFRS 10.

(a) Reading and understanding the new elements – No significant costs or benefits are likely.

(b) Transition requirements – The requirements are likely to result in some increased costs for preparers and users. However, the relief provisions provided will reduce the initial costs for preparers in applying IFRS 10, although for some preparers the costs will remain high.

(c) Ability to direct the investee's relevant activities – The requirements will not necessarily broaden the scope of consolidation for preparers in a significant way and the level of judgement required will not be so significant that it will affect costs in a significant way. Overall, the costs and benefits will probably balance out.

(d) De facto control – The costs will depend on the size and complexity of the investee, and may in individual cases be significant, particularly for those entities that did not previously consolidate de facto controlled investees.

(e) Potential voting rights – No significant costs or benefits are likely.

(f) Agency/principal relationships – For some entities (particularly banks and insurers) the costs are likely to exceed the benefits in the first year of implementation. However, the costs to monitor existing relationships will unlikely to be significant as entities will develop internal guidelines to apply the requirements in a consistent manner.

(g) Structured entities – The benefits derived are likely to exceed the costs.

56 EFRAG's assessment is that de facto control, agency/relationships and structured entities are the main factors listed above which need to be assessed by EFRAG as part of its assessment of IFRS 10. EFRAG believes that the net benefits arising from the application of a uniform consolidation basis for structured entities and having clearer guidance on the accounting for transactions involving less than a majority of the voting rights (de facto control) and agency/principal relationships, exceed the net costs arising from implementing these new requirements for the first time and on an ongoing basis.

57 Therefore, EFRAG's overall assessment is that, on balance, the benefits that are expected to arise from the implementation of IFRS 10 in the EU will exceed the costs expected to be incurred.

APPENDIX 2A – SUMMARY OF IFRS 11

Background

1 Entities will generally enter into a 'joint arrangement' when they decide to share control of one or more economic activities with one or more parties. Such arrangements are common in the oil and gas and construction industries, although they can also be found in other industries.

2 IAS 31 *Interests in Joint Ventures* (IAS 31) defines a joint venture as a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control.

3 Users of financial statements have criticised IAS 31 for permitting a choice of accounting policy for jointly controlled entities (the use of either proportionate consolidation or equity accounting). This was one of the main reasons why the IASB decided to change IAS 31.

4 The IASB also believed that the accounting requirements under IAS 31 depended too much on the form of the arrangement (i.e. the existence of a separate entity) which, combined with the choice of accounting treatment for jointly controlled entities, resulted in some arrangements giving parties similar rights and obligations to be accounted for differently and, conversely, arrangements that give the parties different rights and obligations but are accounted for similarly under existing IFRSs.

5 The IASB therefore decided to amend IAS 31 to address the concerns described above. In particular, IFRS 11 aims to establish a set of principles that determine the accounting for all joint arrangements.

6 The IASB 'Joint ventures' project was initiated as a part of the Memorandum of Understanding between the FASB and the IASB. One of its objectives was to achieve further convergence between IFRS and US GAAP.

What has changed?

7 IFRS 11 replaces the term 'joint venture' in IAS 31 with 'joint arrangement', which is defined as 'an arrangement of which two or more parties have joint control.

8 IFRS 11 introduces the following new elements in accounting for joint arrangements:

(a) Core principal for classification and accounting for interests in joint arrangements;

(b) Parties without joint control having an interest in a joint operation; and

(c) Accounting for interests in joint operations in separate financial statements.

Core principal for classification and accounting for interests in joint arrangements

9 The 'core principle' in IFRS 11 is that the classification and accounting for the interests in joint arrangements is based on the rights and obligations of the parties to a joint arrangement.

Classification: type of joint arrangements

10 IFRS 11 requires that the classification of a joint arrangement be based on whether the parties to the arrangement have 'rights' to assets and 'obligations' for liabilities of the underlying arrangement or, alternatively, only have rights to the net assets of the joint arrangement.

11 Following the 'core principle', IFRS 11 identifies two types of joint arrangements: a joint operation and a joint venture.

(a) In a joint operation, the parties have rights to the assets and obligations for the liabilities of the arrangement. The notion of 'jointly controlled assets' that existed in IAS 31 has been merged into one type of joint arrangement called 'joint operation'.

(b) In contrast, in a joint venture, the parties to the arrangement have rights to the net assets of the arrangement.

12 The term 'jointly controlled entity' is not used in IFRS 11. Under IAS 31 the distinction between 'jointly controlled entities' and all other joint ventures (previously called jointly controlled assets/operations) was based on the existence of a legal entity. This is not the case in IFRS 11, which states that if the legal separation of rights to assets and obligations for liabilities is overcome by the legal form, contractual terms or other facts and circumstances, the arrangement is accounted for in the same way as arrangements in which there is no separate structure at all. Appendix B of IFRS 11 sets out the application requirements and specific tests for each of these. To summarise:

(a) Joint arrangements *not* structured through a separate vehicle: If a joint arrangement is not structured through a separate vehicle, IFRS 11 states that the parties to a joint arrangement have rights and obligations to the assets and liabilities of the arrangement and hence the arrangement must be classified as a joint operation. No further assessment is required.

(b) Joint arrangements structured through a separate vehicle: If a joint arrangement is structured through a separate vehicle this could be either a joint venture or a joint operation. In such a case the parties need to assess whether the legal form of the separate vehicle, the terms of the contractual arrangement and, when relevant, any other facts and circumstances give them: rights to the assets, and obligations for the liabilities (i.e. the arrangement is a joint operation) or rights to the net assets to the arrangement (i.e. the arrangement is a joint venture). In other words, the existence of a separate vehicle is a necessary, but not sufficient, condition for a joint arrangement to be considered a joint venture.

13 In some cases, the parties to a joint arrangement are bound by a framework agreement that sets up the contractual terms for undertaking one or more activities, which might be undertaken through different joint arrangements to deal with specific activities that form part of the agreement. In such cases, the rights and obligations of the parties might differ with regard to the different joint arrangements. In such cases, each joint arrangement set up under the framework agreement should be assessed separately and classified either as a joint operation or a joint venture.

Accounting for joint arrangements

14 The method of accounting will depend on the type of joint arrangement. The focus is no longer on the legal structure of the joint arrangements, but rather on how rights and obligations are shared by the parties to the arrangement. A party to a joint operation recognises – in accordance with all applicable IFRSs – in its financial statements:

(a) its assets, including its share of any assets held jointly;

(b) its liabilities, including its share of any liabilities incurred jointly;

(c) its revenue from the sale of its share of the output of the joint operation;

(d) its share of revenue from the sale of the output by the joint operation; and

(e) its expenses, including its share of any expenses incurred jointly.

15 A joint venturer accounts for its interest in a joint venture using the equity method of accounting under IAS 28 (2011). The existing accounting option to apply proportional consolidation to jointly controlled entities in IAS 31 has been eliminated.

Parties that participate in a joint arrangement but which do not have joint control

16 Under existing IFRSs, a party to a joint venture (under IAS 31 the term 'joint venture' included all types of joint arrangements) that did not have joint control should account for its interest in the joint venture in accordance with IFRS 9 *Financial Instruments* (IFRS 9) or IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39) or under existing IAS 28 (if it had significant influence over the joint venture).

17 Under IFRS 11, parties to *a joint operation* which do not have joint control in the arrangement, are required to measure their interest in the arrangement in the same way as joint operators if they have rights over the assets and obligations for the liabilities of the arrangement (recognition of assets, liabilities, revenue and expenses). Parties to a joint operation that do not have joint control and neither rights to assets nor obligations for the liabilities, account for their interests in the joint operation in accordance with IFRSs applicable to their interests.

18 Under IFRS 11, parties to *a joint venture* that do not have joint control, will continue to account for their investment in accordance with IFRS 9/IAS 39, unless they have significant influence over the joint venture, in which case they shall account for it in accordance with IAS 28 (2011).

Accounting for interests in joint operations in separate financial statements

19 Under existing IAS 27 *Consolidated and Separate Financial Statements* (IAS 27), all interests in jointly controlled entities are accounted for at cost or at fair value in accordance with IFRS 9 or IAS 39.

20 Under IFRS 11, interests in joint operations are accounted for in the separate financial statements in the same manner as they are accounted for in the consolidated financial statements. That is, a joint operator will recognise its assets,

liabilities, revenues and expenses relating to the joint operation. This requirement has been extended to parties to a *joint operation* that do not have joint control, but have rights to the assets and obligations for the liabilities of the arrangement.

21 Joint ventures are accounted for either at cost or fair value in accordance with IFRS 9 or IAS 39 in the separate financial statements of the joint venturers.

Other changes

The scope exception in existing IAS 31

22 The scope exception in existing IAS 31 for venture capital organisations, mutual funds, unit trusts or similar entities, including investment-linked insurance funds, has been removed and characterised as a measurement exception. As a result, entities are required to provide the disclosures in IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12) for all interests in joint ventures, including those that are held by venture capital organisations or similar entities and measured at fair value.

SIC-13 *Jointly Controlled Entities – Non Monetary Contributions by Venturers*

23 The guidance in SIC-13 *Jointly Controlled Entities – Non Monetary Contributions by Venturers* has been incorporated into IAS 28 (2011) *Investments in Associates and Joint Ventures* (IAS 28 (2011)).

Disclosure requirements under IFRS 12 for joint arrangements

24 IFRS 12 requires extensive disclosures about an entity's interests in joint arrangements in response to user needs and as a result of the new accounting model for joint arrangements in IFRS 11.

25 Among others, IFRS 12 requires an entity to disclose the nature of the activities of the joint arrangement and summarised financial information about each joint venture that is material to the entity.

26 In relation to individually immaterial joint ventures, an entity is required to provide *aggregate information* about the carrying amounts of those investments and limited aggregate information about profit and loss and comprehensive income.

27 IFRS 12 requires less information about interests in joint operations than about interests in joint ventures, mainly because IFRS 11 requires a joint operator to account for (and disclose information about) assets and liabilities, income and expenses relating to its interest in a joint operation, in accordance with applicable IFRSs.

When does IFRS 11 become effective?

28 IFRS 11 is effective for annual periods beginning on or after 1 January 2013, with early application permitted provided IFRS 10 *Consolidated Financial Statements* (IFRS 10), IFRS 12, IAS 27 (2011) *Separate Financial Statements (IAS 27 (2011))* and IAS 28 (2011) are adopted at the same time.

APPENDIX 2B – ANALYSIS OF THE COSTS AND BENEFITS OF IFRS 11

EFRAG's initial analysis of the costs and benefits of IFRS 11

1 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IFRS 11, both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – EFRAG's initial assessment was that:

(i) IFRS 11 is likely to result in incremental one-off costs for preparers, which for some preparers could be significant. Preparers that expect to be most affected are (1) those that have interests in joint operations structured through a separate vehicle, which were previously accounted for under the equity method, and (2) those that present only separate financial statements and have interests in joint operations structured through a separate vehicle;

(ii) The incremental ongoing costs will not be significant for most of preparers. However, the ongoing costs could be significant for some preparers; in particular those that have interests in numerous joint operations structured through a separate vehicle and that present only separate financial statements; and

(iii) IFRS 11 is unlikely to result in significant costs for users.

(b) *Benefits* – EFRAG's initial assessment was that IFRS 11 will provide significant benefits for users and some benefits for preparers.

2 EFRAG published its initial assessment and supporting analysis on 9 February 2012. It invited comments on the material by 11 March 2012. In response, EFRAG received 21 comment letters. Nine respondents agreed with EFRAG's assessment of the benefits of implementing IFRS 11 and the associated costs involved for users and preparers. Nine respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing IFRS 11 in the EU, but supported EFRAG's recommendation that IFRS 11 be adopted for use in Europe. Three respondents did not agree with EFRAG's assessment of the benefits of implementing IFRS 11 and/or the associated costs or did not comment on this specific assessment.

EFRAG's final analysis of the costs and benefits of IFRS 11

3 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IFRS 11 is presented below.

Core principle for classification and accounting for interests in joint arrangements

Cost for preparers

4 EFRAG has carried out an assessment of the cost implications for preparers resulting from IFRS 11 in relation to the determining of the type of the joint arrangement and the change in method of accounting.

One-off costs incurred on transition

5 To proceed with the transition from IAS 31 to IFRS 11, it is expected that preparers will need to incur the following types of costs:

(a) reading and understanding of IFRS 11;

(b) analysis of arrangements and data collection; and

(c) systems and processes modifications.

6 These types of costs are discussed in details in the paragraphs that follow. The relief provided by IFRS 11 transitional requirements from retrospective reassessment of the data is also discussed.

Reading and understanding of IFRS 11

7 Preparers will incur one-off costs to get acquainted with the new requirements, understand their impact on the reporting processes and to train their employees accordingly. These costs would need to be incurred by all entities that are a party to a joint arrangement, regardless of whether they currently use the proportionate consolidation or equity method. EFRAG foresees some effort to read and understand the new requirements, with no significant costs for preparers.

8 In addition, preparers may need to incur some costs of communicating and explaining the changes in their financial statements to users. In EFRAG's view, this cost will not be significant.

Analysis of arrangements and data collection

9 EFRAG notes that one of the most significant costs preparers will incur relates to the need to analyse and classify the joint arrangements as either a joint operation or a joint venture.

10 When a joint arrangement is structured through a separate vehicle, preparers will need to consider the legal form, contractual agreements and other facts and circumstances in order to classify the joint arrangement as a joint venture or joint operation. For some entities this assessment will be straightforward and the cost of assessment will be insignificant. However, for other preparers classification of their joint arrangements will require more effort and lead to higher costs. In some cases, it might not be clear whether the legal form of the joint arrangement or the contractual agreement confer separation between the vehicle and the parties to the arrangement. In these cases, preparers may need to seek legal advice and engage external advisors or consultants, which would lead to entities incurring additional costs.

11 In EFRAG's view preparers that currently use proportionate consolidation may have access to all the data necessary to make the transition either to the equity accounting for their interests in joint ventures or to recognise assets, liabilities, revenue and expenses of their joint operations. However, in some cases entities may need to collect additional information about individual assets, liabilities, revenue and expenses of the joint operation to be able to recognise the appropriate share (percentage of assets, liabilities, revenue and expenses) in the financial statements.

12 Entities that currently use the equity method and that will classify some of their interests in joint arrangements structured through separate vehicle as joint operations might need to get access to additional information to recognise their share of assets, liabilities, revenue and expenses of a joint operation. Where the contractual arrangements currently do not foresee the provision of such detailed information, entities may need to agree with other joint operators on a way to obtain the required data.

Systems and processes modifications

13 Preparers are likely to incur costs to adapt and in some cases modify their financial systems and internal processes in order to make the transition either from proportionate consolidation to the equity method or from the equity method to accounting for assets, liabilities, revenue and expenses. That will depend on the classification of their interests in joint arrangements under IFRS 11 and the method of accounting currently used.

14 Some preparers which currently use equity method, will classify their interests in IAS 31 jointly controlled entities as joint ventures. In this case, they will continue using equity method.

15 Other preparers which currently use equity method, will classify some of their interests in IAS 31 jointly controlled entities as joint operations, in which case they might need to change existing systems and processes.

16 Some preparers which currently use proportionate consolidation, will classify their interests in IAS 31 jointly controlled entities as joint ventures and they will need to change from proportionate consolidation to the equity method. If these companies continue to use proportionate consolidation in their management reporting, it is possible that they will need to enhance their systems.

17 Other preparers which currently use proportionate consolidation, will classify their interests in IAS 31 jointly controlled entities to joint operations and will not need to modify their systems significantly. However, in cases when – according to the arrangement – a different percentage of individual assets, liabilities, revenue and expenses will need to be recognised (e.g. because their share of output taken differs from their legal ownership share in the vehicle), enhancement of the financial system might be needed.

18 EFRAG's assessment is that the one-off costs to modify and change systems and processes will be significant for some preparers, in particular those which currently use the equity method and will classify some IAS 31 jointly controlled entities as joint operations.

Transition requirements

19 Preparers would need to incur one-off costs of restating retrospectively joint arrangements (from proportionate consolidation to the equity method or from the equity method to accounting for assets and liabilities) for comparative periods.

20 EFRAG notes that the transitional provisions in IFRS 11 bring some relief in the following situations:

(a) In case of transition from proportionate consolidation to equity method entities will need to recognise their investments in joint ventures at the beginning of

the earliest period presented as an aggregate of the *existing* carrying amounts of assets and liabilities that the entity previously proportionally consolidated. No remeasurement or restatement of the previous accounting is required.

(b) In case of transition from equity method to recognition of assets and liabilities entities will need to derecognise their existing investment and recognise their share of assets and liabilities in a joint operation at the beginning of the earliest period presented. Entities do not need to remeasure the recognised assets and liabilities at the date of transition.

21 Overall, in EFRAG's opinion the reliefs mentioned above will reduce the initial costs for preparers of applying IFRS 11.

Impact on the cost of capital for joint arrangements classified as joint ventures

22 The change in the accounting method from proportionate consolidation to the equity method will result in different information being reported in financial statements. For example, total assets and total revenue reported by entities will decrease on the face of financial statements. If analysis were not to modify their approach, that change would have impact on certain key financial ratios, which may then affect the cost of capital for those entities.

23 However, users will be provided with summarised financial information about each joint venture that is material to the entity and for all immaterial joint ventures in aggregate, as required by IFRS 12. This should enable users to conduct their analysis in a way they believe is most relevant and appropriate. Moreover, having financial data about all joint arrangements in the notes being disaggregated from assets, liabilities and revenue and expenses of joint venturers, is likely to be useful for users.

Ongoing costs

24 Preparers are expected to incur the following incremental recurring costs to implement IFRS 11:

(a) data collection; and

(b) analysis of arrangements.

25 These costs are discussed in the paragraphs that follow.

Data collection

26 In some cases, IFRS 11 will lead to costs savings in terms of data collection and processing, in particular when the entity will change from the proportionate consolidation to the equity method.

27 However, some preparers may decide to continue to use proportionate consolidation for their management reporting under IFRS 8. For those entities implementation of equity method will not bring savings.

28 EFRAG notes that under IFRS 12, entities will need to collect data to present summarised financial information on joint ventures that are considered material to the entity. As a result, the overall costs savings in changing from proportionate consolidation to the equity method are not expected to be significant.

29 For the entities that currently use the equity method and will classify some or all their interests in jointly controlled entities as joint operations, IFRS 11 may lead to an increase in ongoing costs of data collecting and processing. For some entities this cost will be insignificant, however for others it could be more significant, and will depend on the number of joint operations, characteristics of the joint arrangement and accessibility of the financial data.

30 For some entities that currently use proportionate consolidation, the reclassification of some of their interests to joint operations could lead to some increase in the costs of collecting and processing data, in order to be able to capture the additional information on a transaction level.

<u>Analysis of arrangements</u>

31 Entities will need to monitor the changes in key clauses of their contractual arrangements, in order to verify the correct classification of their joint arrangements on an ongoing basis. However, the changes to contracts or shareholders agreements that would trigger reclassification are not expected to occur frequently.

Conclusion on costs for preparers

32 Overall, EFRAG's assessment is that IFRS 11 is likely to result in incremental one-off costs for preparers, which for some preparers could be significant. Preparers which expect to be most impacted are those that have interests in joint operations structured through separate vehicle, which were previously accounted for under the equity method.

33 Overall, EFRAG's assessment is that the ongoing costs will not be significant for most preparers.

Costs for users

34 EFRAG has carried out an assessment of the cost implications for users resulting from IFRS 11.

35 Users will need to understand the new requirements and analyse why the numbers in the financial statements are different in order to amend their models and compare year-to-year figures. However, this cost is expected to be reduced by the fact that on transition preparers are required to provide the comparative data for all periods presented in their financial statements. Moreover, entities are required to provide reconciliation between the interests in joint arrangements accounted under IAS 31 as equity investment or proportionate consolidation and the interest in joint arrangements accounted for using different method under IFRS 11. This should make the transition more understandable for users.

36 Users will lose some information reported on the face of the financial statements in relation to jointly controlled entities that are currently proportionally consolidated. However, the summarised financial information for each material interest in joint venture, and in aggregate for all immaterial joint ventures, will be provided in the notes to the financial statements. The expanded disclosures are expected to compensate partially for the loss of information on the face of the primary financial statements.

Conclusion on costs for users

37 Overall, EFRAG's assessment is that the IFRS 11 is unlikely to result in significant costs for users.

Benefits for preparers and users

38 EFRAG has carried out an assessment of the benefits for users and preparers resulting from IFRS 11.

39 IFRS 11 eliminates the existing accounting option for jointly controlled entities, and provides guidance on the classification of joint arrangements created through a separate vehicle. As a result, it is expected that users and preparers will benefit from the increased comparability of the financial statements under IFRS 11.

40 Moreover, the principle in IFRS 11 is based on recognising rights to assets and obligations for liabilities that arise from parties' involvement in a joint arrangement, and not on the legal form of the arrangement. IFRS 12 requires more comprehensive disclosure about key financial data and risks and debt obligations associated with joint ventures. Having a consistent principle, with comprehensive disclosure is likely to increase usefulness of information to users.

Conclusion on benefits for preparers and users

41 For the reasons explained above, EFRAG assessment is that preparers are likely to benefit from IFRS 11. Moreover, EFRAG's assessment is that IFRS 11 will provide significant benefits for users.

Overall assessment about the costs and benefits of implementing the IFRS 11 core principle for classification and accounting

42 EFRAG's assessment is that the overall benefits resulting from IFRS 11 are likely to outweigh costs associated with implementation of new requirements.

Parties without joint control having interests in joint operation

Cost for preparers

43 EFRAG has carried out an assessment of the cost implications for preparers resulting from the guidance in IFRS 11 on accounting by parties without joint control having interests in joint operation.

44 The parties to the joint operations that do not have joint control but have rights to assets and obligations for liabilities of the joint operations, will need to change their accounting from applying IFRS 9/IAS 39 (or IAS 28 in case of significant influence) to recognising assets and liabilities based on the contractual rights they have under the joint arrangement.

45 EFRAG acknowledges that those entities will need to incur some additional costs of reviewing the contracts and collecting the necessary data to change the current accounting practice. In EFRAG's view, the costs involved are unlikely to be significant.

46 In EFRAG's view, the ongoing costs involved are unlikely to be significant.

Costs for users

47 EFRAG has carried out an assessment of the cost implications for users resulting from the IFRS 11 guidance on accounting in the financial statements of parties without joint control having interests in joint operation.

48 EFRAG acknowledges that users will need to make some effort to understand the changes – in the financial statements of the parties that do not have joint control but only rights to the assets and obligations for the liabilities of the joint operation – and to update their analyses. However, as the scope of this change is limited, in EFRAG believes that the cost for users will not be significant.

Benefits for preparers and users

49 EFRAG has carried out an assessment of the benefits for users and preparers resulting from the IFRS 11 guidance on accounting in the financial statements of parties without joint control having interests in joint operation.

50 In EFRAG's view, preparers without joint control that have rights to the assets and obligations for the liabilities of a joint operation will benefit from the new accounting guidance in IFRS 11 as they will be able to reflect better the activities conducted in cooperation with the joint arrangement.

51 In EFRAG's view, users are expected to benefit from the IFRS 11 guidance on parties without joint control having interests in joint arrangement, because they will be provided with useful and relevant information about the rights to the assets and obligations for the liabilities which the parties without joint control have in relation to their interest in joint arrangements.

Overall assessment about the costs and benefits of implementing the IFRS 11 guidance on parties without joint control having interests in joint operation

52 EFRAG's assessment is that the overall benefits from the IFRS 11 guidance, on parties without control that have an interest in a joint operation, are likely to outweigh costs associated with implementation of the new requirements.

Accounting for interests in joint operations in separate financial statements

Cost for preparers

53 EFRAG has carried out an assessment of the cost implications for preparers resulting from IFRS 11 in relation to accounting in the separate financial statements.

54 IFRS 11 requires the same accounting for the interests in joint operations, which is the recognition of assets and liabilities, revenue and expenses in separate and consolidated financial statements of the joint operator. Some of the joint arrangements structured through a separate vehicle will be classified as joint operations under IFRS 11. Under IAS 31 they may have been classified as jointly controlled entities and accounted for at cost or at fair value according to existing IAS 27.

One-off costs

55 In EFRAG's view, entities that prepare consolidated financial statements will not incur additional significant costs to apply the requirements in the separate financial statements.

56 However, EFRAG acknowledges that entities which prepare only separate financial statements may need to incur additional costs. As explained above in 'consolidated financial statements', costs will be incurred to determine classification of the joint arrangement, collecting of additional data (about the underlying assets and liabilities), and modification of systems and processes.

57 Those preparers may also need to incur additional costs to explain and communicate this change in their separate financial statements to users.

58 In addition, preparers for which the separate financial statements are the basis for the tax declarations may need to incur costs that result from the underlying tax implications.

59 One-off costs will also (similar to those discussed above) be incurred by parties to a joint operation that do not have joint control but have rights to assets and liabilities for obligations relating to the arrangement.

60 EFRAG's assessment is that one-off costs of implementing IFRS 11 might be significant for some entities that prepare only separate financial statements and have interests in joint operations structured through separate vehicle. In addition, the eventual tax implications that result from assessing tax obligations based on different numbers will also result in some preparers incurring additional costs (it should be noted that there is an equal and opposite benefit to the tax authorities).

Ongoing costs

61 Similar to one-off costs, preparers that currently account for their interests in joint operations structured through separate vehicle at cost or at fair value in their separate financial statements will incur some additional ongoing costs of providing the information about their rights to the assets and obligations for the liabilities of the joint operations.

62 The additional ongoing costs may include costs of data collection and processing, additional reconciliations with tax declarations and higher audit fees.

63 EFRAG's assessment is that the ongoing costs could be significant for some of the entities (that prepare only separate financial statements), in particular having interests in numerous joint operations structures through separate vehicle.

Conclusion on costs for preparers

64 Overall, EFRAG's assessment is that the guidance in IFRS 11 on accounting for the interests in joint arrangements in the separate financial statements is likely to result in incremental one-off and ongoing costs for preparers, which prepare separate financial statements.

65 These costs could be significant for preparers that present only separate financial statements and have interests in a number of joint operations structured through separate vehicle. For other preparers the costs are expected to be insignificant.

Costs for users

66 EFRAG has carried out an assessment of the cost implications for users resulting from the IFRS 11 guidance on accounting in separate financial statements.

67 Users will need to incur some costs of understanding the changes arising from IFRS 11 on the separate financial statements of joint operators and other parties to the joint operations that have rights to the assets and obligations for the liabilities relating to the joint operation. However, similarly to the consolidated financial statements, this cost will be mitigated by the fact that that the entities are required to provide reconciliation between the investment derecognised (at cost or at fair value) and the assets and liabilities recognised.

Conclusion on costs for users

68 Overall, EFRAG's assessment is that the guidance in IFRS 11 on accounting in separate financial statements is unlikely to result in significant costs for users.

Benefits for preparers and users

69 EFRAG has carried out an assessment of the benefits for users and preparers resulting from IFRS 11 in respect to separate financial statements.

70 Users will have access to the information about a joint operator's assets, liabilities, revenue and expenses relating to its interests in a joint operation, directly from the separate financial statements. This level of detail is unlikely to be readily available in the consolidated accounts, given that they have different focus and require less disclosure of information for each individual joint operation. In EFRAG's view it will allow users to better understand the rights and obligations of the joint operators that arise from the interests in joint operation. This would be important in particular for the financial statements of the entities which do not prepare consolidated financial statements.

71 Furthermore, the information about the joint operations would be the same in the separate and consolidated financial statements, which would enhance comparability.

Conclusion on benefits for preparers and users

72 EFRAG assessment is that users are likely to benefit from the requirements in IFRS 11 in respect to separate financial statements.

Overall assessment about the costs and benefits of IFRS 11 guidance on accounting in the separate financial statements

73 EFRAG's assessment is that the overall benefits resulting from IFRS 11 guidance on accounting in separate financial statements are likely to outweigh costs associated with implementation of the new requirements.

Overall assessment about the costs and benefits of implementing IFRS 11 in the EU

74 To summarise, EFRAG reached the following individual conclusions on each of the areas discussed above. The following assessment combines the effects of one-off

and ongoing costs to preparers and users with the benefits expected from the new requirements in IFRS 11:

(a) *Core principle for classification and accounting for interests in joint arrangements* – The requirements are likely to result in increased costs for preparers and for some preparers the one-off costs could be significant. However, the benefits for users of the increased comparability and relevance of financial reporting are expected to outweigh the costs of implementation.

(b) *Parties without joint control having interests in joint operations* – The requirement is unlikely to result in significant costs for preparers and users, and therefore the benefits of a more faithful representation of rights and obligations of parties to a joint operation that do not have joint control, are likely to outweigh the costs of implementation.

(c) *Accounting for interests in joint operation in separate financial statements* – The requirement is likely to result in increased costs for preparers. These costs could be significant for those preparers that have interest in numerous joint operations structured through separate vehicle and which prepare only separate financial statements. However, the benefits for users of a more faithful representation of rights and obligations of joint operators in their separate financial statements are likely to outweigh the costs.

75 On balance, EFRAG's assessment is that the overall benefits resulting from IFRS 11 are likely to outweigh costs associated with implementation of new requirements.

APPENDIX 3A – SUMMARY OF IFRS 12

Background

1 Users of financial statements have consistently requested improvements to the disclosure of information provided by an entity (the investor) in relation to its interests in other entities (investees). The global financial crisis has highlighted a lack of transparency about the risks to which an entity is exposed to from its involvement with structured entities (special purpose entities) and the need for better information about an entity's interests in structured entities, including those that are not consolidated.

2 In addition, users have requested further information about non-controlling interests (NCI) in consolidated entities to help them understand the profit or loss and cash flows attributable to the shareholders of the parent entity and those attributable to the NCI.

3 The development of IFRS 10 *Consolidated Financial Statements* (IFRS 10) and IFRS 11 *Joint Arrangements* (IFRS 11) has shifted the focus to a more principles-based control model and replaced the choice of accounting policy in existing IAS 31 *Interests in Joint Venturers* (IAS 31) with a principle that focuses on the rights and obligations of the parties to a joint arrangement, rather than on its legal form. The new requirements require management to make certain assumptions and to exercise judgement in the assessments made and conclusions reached, which creates a need for additional disclosure to support users' analysis.

4 Users have also indicated that the information provided in the notes is sometimes fragmented and not easy to find, which makes the information less understandable and less comparable between entities.

Objective of IFRS 12

5 IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12) was developed to address the concerns of users about the information on interests in other entities. The standard focuses only on information provided in the consolidated financial statements.

6 The objective of IFRS 12 is to set out a single source of guidance for all disclosure requirements for an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities.

7 The standard establishes principles-based disclosure objectives and specifies the minimum information an entity must provide to meet those objectives. IFRS 12 emphasises that information should not be obscured by excessive detail and should be presented in a structured and understandable way.

8 IFRS 12 requires an entity to disclose information that helps users of financial information understand and evaluate:

(a) the nature of, and risks associated with, its interests in other entities; and

(b) the effects of those interests on its financial position, financial performance and cash flows.

What has changed?

9 Set out below is a description of the new elements and additional disclosure requirements introduced by IFRS 12:

(a) Unconsolidated structured entities;

(b) Significant judgements and assumptions;

(c) Interests in subsidiaries with material non-controlling interests;

(d) Consolidated structured entities;

(e) Interests in joint arrangements and associates; and

(f) Venture capital organisations, mutual funds or unit trusts and similar entities including investment-linked insurance funds that have an interest in a joint venture or associate.

10 Although the standard requires more granular information in some areas (with a focus on materiality), it does permit information with similar characteristics to be aggregated. The primary objective of IFRS 12 is to provide information to users in a structured and meaningful way.

Unconsolidated structured entities

11 IFRS 12 introduces disclosures about unconsolidated structured entities that were not required previously under IAS 27 *Consolidated and Separate Financial Statements* (IAS 27). The objective is to increase transparency about investees that are not consolidated.

12 IFRS 12 defines a structured entity as ‘an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity’.

13 IFRS 12 requires an entity to disclose qualitative and quantitative (summarised information) about the nature of its interest in unconsolidated structured entities and the risks to which an entity is exposed from that interest, including:

(a) nature, purpose, size and activities of the structured entity;

(b) how the structured entity is financed;

(c) the carrying amounts of the assets and liabilities relating to its interests in unconsolidated structured entity and how they compare to the maximum exposure to loss from that interest;

(d) the type and amount of the support provided to the structured entity without a contractual obligation to do so, and reasons for that; and

(e) current intention to provide support to the structured entity.

14 When an entity has no contractual involvement with the structured entity at the end of the reporting period but was a sponsor of that structured entity, it must disclose

income received from the structured entity during the reporting period and all assets transferred to structured entities during the reporting period.

Significant judgments and assumptions

15 The introduction of a uniform consolidation model in IFRS 10 and the classification of a joint arrangement in IFRS 11 have resulted in the need for further disclosures to enable users to understand the significant judgements and assumptions made by management when deciding how an entity should account for its involvement with another entity.

16 The disclosures in IFRS 12 are intended to supplement the general disclosure requirements in IAS 1 *Presentation of Financial Statements* with more specific requirements relating to an entity's decision about whether it controls, jointly controls or exercises significance influence over another entity.

17 An entity must disclose qualitative information about significant judgements and assumptions it has made in determining the nature of the relationship with the other entity (whether it has control, joint control or significant influence) and the type of joint arrangement it is involved with (joint operation or joint venture).

Interests in subsidiaries with material non-controlling interests

18 Some of the disclosures in existing IAS 27 have been carried forward to IFRS 12 without significant changes.

19 However, IFRS 12 requires (1) new disclosures in relation to subsidiaries with non-controlling interests (NCI) that are material to the entity and (2) extends the disclosure requirements about significant restrictions (on the parent's ability to access or use the assets and settle the liabilities of its subsidiaries).

Interests in subsidiaries with non-controlling interests

20 IFRS 12 requires an entity to disclose – for each non-controlling interest that is material to the entity – the following information:

(a) the name of the subsidiary and its place of business;

(b) the proportion of ownership interests held by NCI and the proportion of voting rights (if different);

(c) the profit or loss allocated to NCI;

(d) accumulated NCI at the end of the reporting period;

(e) dividends paid to NCI; and

(f) summarised financial information about the subsidiary.

21 Some information about NCI is already required under IAS 1, such as total NCI within equity, profit and loss including total comprehensive income for the period attributable to NCI and a reconciliation between the opening and closing balance for NCI for the period. In response to user needs, IFRS 12 expands the disclosure requirements in relation to NCI.

22 The standard requires disclosures of summarised financial information to be presented for each subsidiary with material NCI, such as current assets, non-current assets, current liabilities, non-current liabilities, revenue, profit or loss, and total comprehensive income. This information is based on the amounts before consolidation eliminations.

Significant restrictions on an entity's ability to access or use assets, and settle liabilities

23 Existing IAS 27 already requires disclosures about the nature and extent of any significant restrictions on an entity's ability to transfer funds to its parent.

24 IFRS 12 expands the existing requirements about a parent's ability to access or use the assets and settle the liabilities of its subsidiaries (including statutory, contractual and regulatory restrictions and the nature of protective rights of NCI on the entities ability to access or use assets and settle liabilities of the group).

25 The standard also requires disclosure of the carrying amounts in the consolidated financial statements of the assets and liabilities to which these restrictions apply.

Consolidated structured entities

26 Involvement in structured entities can expose an entity to risks that are different to those that typically arise from investing in other subsidiaries, due to factors such as the restricted activities of the structured entity, insufficient equity to fund losses or its design and intended purpose.

27 IFRS 12 requires disclosures about the risks associated with an entity's involvement with consolidated structured entities when it could be required to provide financial support to them. To summarise, an entity must disclose:

(a) any contractual arrangements to provide support to consolidated structured entities, including the circumstances that could expose the reporting entity to loss;

(b) the type, amount and the reasons of any support provided to the consolidated structured entity during the reporting period without obligation to do so;

(c) the situation when provision of support to the previously unconsolidated structured entity resulted in obtaining control over that entity; and

(d) any current intention to provide support to a consolidated structured entity.

Interests in joint arrangements and associates

28 IFRS 12 extends the disclosure requirements in relation to an entity's interests in joint arrangements and associates in response to user needs, and as a result of the new classification and accounting requirements for joint arrangements in IFRS 11.

29 For each joint venture and associate that is material to the reporting entity, an entity must disclose the following qualitative and quantitative information:

(a) name, place of business, nature of activities, and proportion of ownership;

(b) measurement method (equity method or fair value);

(c) summarised financial information; and

(d) fair value of an investment accounted for using equity method, if there is a quoted market price for the investment.

30 The required summarised financial information in (c) above, consists of different items included in the statement of financial position and the statement of comprehensive income of the individual joint venture and associate, and some additional information for joint ventures that are material to the reporting entity.

31 In relation to individually immaterial joint ventures and associates, an entity is required to provide *aggregate information* about the carrying amounts of those investments and limited aggregate information about profit and loss and comprehensive income.

32 IFRS 12 also aligns most of the disclosures for joint ventures and associates.

33 IFRS 12 requires less information about interests in joint operations than about interests in joint ventures, mainly because IFRS 11 requires a joint operator to account for assets and liabilities, income and expenses relating to its interest in a joint operation, in accordance with applicable IFRSs.

Venture capital organisations, mutual funds, unit trusts and similar entities including investment-linked insurance funds that have an interest in a joint venture or associate

34 IFRS 12 requires the same disclosures to be provided in respect to all associates and joint ventures, including those held by the venture capital organisations, mutual funds, unit trusts and similar entities including investment-linked insurance funds and measured at fair value. This is a change from existing IAS 28 *Investments in Associates* (IAS 28) and IAS 31, which require only specific limited disclosures when an entity is a venture capital organisation or a similar entity.

35 This requirement is consistent with the IASB's decision to remove the scope exclusion in the amended IAS 28 *Investments in Associates and Joint Ventures* (IAS 28 (2011)) and IAS 31 when it was replaced by IFRS 11.

When does IFRS 12 become effective?

36 IFRS 12 becomes effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. An entity is encouraged to provide information required by IFRS 12 early, without being compelled to comply with all the requirements of IFRS 12 or to apply IFRS 10, IFRS 11, IAS 27 *Separate Financial Statements* (IAS 27 (2011)) and IAS 28 (2011) at the same time.

37 There are no specific transitional requirements. Therefore, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, retrospective application is required.

APPENDIX 3B – ANALYSIS OF THE COSTS AND BENEFITS OF IFRS 12

EFRAG's initial analysis of the costs and benefits of IFRS 12

1 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IFRS 12, both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – To summarise, EFRAG's assessment was that:

(i) some preparers are likely to incur significant one-off costs from implementing IFRS 12, in particular when they have numerous interests in other entities and when getting access to data is difficult;

(ii) the ongoing costs of providing the disclosures are likely to be insignificant in most cases, once preparers are acquainted with the new requirements and have adapted their systems and processes to meet the requirements and collected data for the first time; and

(iii) IFRS 12 is likely to result in significant one-off costs for users (particularly in those cases where detailed changes to their models are needed) and in cost savings on an ongoing basis.

(b) *Benefits* – To summarise, EFRAG's initial assessment was that preparers were likely to benefit from IFRS 12 as the new disclosures are expected to improve the communication with users. Furthermore, EFRAG's initial assessment was that IFRS 12 will bring significant long-term benefits to users.

2 EFRAG published its initial assessment and supporting analysis on 9 February 2012. It invited comments on the material by 11 March 2012. In response, EFRAG received 23 comment letters. Eight respondents agreed with EFRAG's assessment of the benefits of implementing IFRS 12 and the associated costs involved for users and preparers. Eleven respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing IFRS 12 in the EU, but supported EFRAG's recommendation that IFRS 12 be adopted for use in Europe. Three respondents did not agree with EFRAG's initial assessment of the costs and benefits of implementing IFRS 12. One respondent did not comment on this specific assessment.

EFRAG's final analysis of the costs and benefits of IFRS 12

3 Based on its analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IFRS 12 is presented below.

Cost for preparers

4 The significance of the costs to preparers of implementing IFRS 12 will depend largely on the volume of investees including joint ventures and associates and whether they are considered to be structured entities (special purpose entities) and involve complex ownership structures and contractual terms.

One-off costs

Reading and understanding IFRS 12

5 Preparers will incur one-off costs to read and understand the new requirements and to train their employees accordingly.

6 EFRAG notes that although IFRS 12 already includes a number of definitions of the terms used in the standard, some terms have not been defined (for example, a 'sponsorship', and 'size' of a structured entity). EFRAG believes that the lack of guidance on some undefined terms may cause some preparers to incur additional one-off costs.

Aggregation of data

7 IFRS 12 emphasises that information should not be obscured by excessive detail and should be presented in a structured and understandable way. The objective is to provide information to users in a meaningful way, in which items with similar characteristics are aggregated and vice versa.

8 EFRAG acknowledges that aggregating data in a meaningful and understandable way will not always be an easy task and it will require time and effort to aggregate the information. The overall difficultly will depend on the number of investees under consideration, the complexity of the structures and arrangements that an entity is involved with, and whether they have similar characteristics. The effort could be significant when applying IFRS 12 for the first time.

9 EFRAG observes that IFRS 12 provides guidance on how an entity should aggregate the data and clarifies that materiality is a key point of focus. The focus on 'materiality' is expected to bring relief to preparers in respect of developing a consistent and understandable pattern of aggregation policies for items that have similar characteristics. Materiality will also play an important role for preparers in determining which disclosures need to be aggregated and presented in the financial statements. The relief provided through aggregation should reduce the burden of providing the required disclosures.

10 Overall, EFRAG's assessment is that the costs of developing aggregation policies that are relevant to their business model and consistent with the standard's objectives should not be significant.

Collecting of information, systems and processes modifications

11 The new and more comprehensive disclosure requirements in IFRS 12 may require preparers to adjust or change current systems and reporting processes, to obtain the respective information. The related costs are discussed below.

Unconsolidated structured entities

12 EFRAG understands that one of the main costs of implementing IFRS 12 relates to the requirements about unconsolidated structured entities. These are new requirements that will result in initial costs of adjusting and changing financial systems and existing processes to produce the information the first time. For example, preparers may need to modify their systems in order to be able to track its transactions with structured entities. Furthermore, entities will incur analysis costs to review their interests in other entities, and conclude on whether they satisfy the

definition of a 'structured entity' under IFRS 12. For some preparers these costs will be significant.

13 However, EFRAG notes that some of the required information is likely to be already collected for purposes other than the financial statements (for example, risk management purposes, regulatory requirements and investors' relations). In some cases, the information might need to be converged with IFRS, which will result in costs for preparers. In other cases, a preparer may have limited access to the information, in particular when the structured entity is managed by other parties.

14 EFRAG's assessment is that one-off costs of modifying systems and processes to collect and process the required information about unconsolidated structured entities are expected to be significant for some entities. Preparers in the insurance and banking industry having numerous interests in structured entities are likely to be affected most.

Subsidiaries with material non-controlling interests

15 In EFRAG's view, the information necessary to meet the disclosure requirements about interests in subsidiaries with material NCI, which are currently consolidated, should be mostly available and it is unlikely to result in significant year-one costs for preparers.

16 However, in respect to the structured entities which will be consolidated for the first time under IFRS 10, collecting of information for the disclosure purposes might require more effort and result in additional costs. This is expected to be the case for some companies with interests in funds that were not consolidated under current standards, but that will be consolidated under IFRS 10 as a result of the new requirements on de-facto control and agent-principal relationships.

Interests in joint arrangements and associates

17 Some preparers may need to establish new processes and enhance their systems to be able to collect and process the summarised financial information required for interests in joint ventures and associates considered to be material to the reporting entity. EFRAG's assessment is that these costs are not expected to be significant for most preparers, because in number of cases this data is already collected either to apply the equity method or proportionate consolidation under existing IFRSs, or for management reporting purposes (or both).

18 However, those costs may be significant for some venture capital and similar organisations, as the disclosure requirements are new and the respective data might have been collected before. For preparers that use the equity method to account for jointly controlled entities (IFRS 11 joint ventures) and for associates, the required IFRS data may not be readily available and they will incur some initial costs to implement this requirement.

Disclosure about significant judgements and assumptions

19 The introduction of a uniform principles-based consolidation model in IFRS 10 and the classification of joint arrangements in IFRS 11 have resulted in an increase in the level of judgement and assumptions applied when determining control, joint control and classification of a joint arrangement. For most preparers, this cost is likely to be insignificant. However, for preparers involved in more complex

relationships with investees the requirement may entail some significant costs to set up reporting systems to produce the required information.

Transition requirements

20 IFRS 12 shall be applied for annual periods beginning on or after 1 January 2013, with earlier application being permitted. As there are no specific transition requirements set out in IFRS 12, IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors applies and retrospective application is required.

21 EFRAG's assessment is that in relation to the disclosure requirements about interests in consolidated subsidiaries, and interests in joint ventures and associates, the transition itself will not result in significant incremental costs to preparers. However, some preparers may find it challenging to apply some of the disclosure requirements retrospectively, in particular:

(a) The disclosures for unconsolidated structured entities will require an entity to identify whether, before applying IFRS 12, it had (has) interests in entities that meet the definition of structured entities.

(b) The disclosures for interest in subsidiaries' with material non-controlling interests that are currently not consolidated (for example investment funds).

(c) The disclosures required by venture capital organisations, mutual funds, unit trusts and similar entities that have interests in a joint ventures or associates measured at fair value are mainly new requirements as these entities provide only limited disclosures under existing IAS 28 and IAS 31.

Ongoing costs

22 Similar to EFRAG's assessment on one-off costs of implementing IFRS 12, the significance of ongoing costs will depend on the volume of investees, and the nature and complexity of an investee. EFRAG notes that due to the new and expanded disclosure requirements entities will incur additional recurring costs to collect and process the data.

23 EFRAG's assessment of ongoing costs is discussed below.

Unconsolidated structured entities

24 EFRAG notes that some information required by IFRS 12 is already being collected for risk management purposes and compliance with regulatory requirements. However, EFRAG acknowledges that the data gathered for other purposes might not be in the format needed to satisfy IFRS 12 disclosure requirements, and result in ongoing costs to preparing at each reporting period.

25 However, the main difficulty in providing the disclosures on unconsolidated structured entities is the scope of the requirements and the potential difficulty in obtaining some of the information. Moreover, for all new transactions preparers will need to perform the assessment on whether they represent an interest in a structured entity.

26 EFRAG observes that the disclosures about interests in unconsolidated structured entities are quite extensive, and preparers might be required to invest time and effort to aggregate the data in a meaningful way.

27 The requirement to provide disclosures about unconsolidated structured entities is expected to affect mostly large financial institutions, particularly banks and insurance companies. In EFRAG's view, the ongoing costs are likely to be higher for these preparers. Overall, EFRAG believes that over time, ongoing costs will decrease as preparers conform and automate their reporting systems to more easily produce the required information.

Significant judgements and assumptions

28 As explained above in 'one-off' costs, compiling disclosures about the significant judgement and assumptions is largely a one-off exercise. However, EFRAG acknowledges that the preparers will need to update the disclosure when the facts and circumstances change and for new investments.

29 EFRAG's assessment is that ongoing costs of updating the disclosure about significant judgements and assumptions will not be significant.

Subsidiaries with material non-controlling interests (NCI)

30 EFRAG thinks that the information required by IFRS 12 about subsidiaries with material NCI is already collected for consolidation purposes, and can be easily reproduced from the available financial data. EFRAG notes that preparers having interests in numerous subsidiaries with material NCI – that were previously not consolidated – will need to make some additional effort to aggregate the information. Overall, EFRAG's assessment is that the ongoing costs of aggregating the data and providing this disclosure are not expected to be significant for most preparers.

Consolidated structured entities

31 Preparers with interests in consolidated structured entities would need to review their contracts with structured investees to establish whether they have contractual arrangements that would require them to provide financial support to those entities. Some preparers may find this requirement challenging particularly if they have interests in numerous consolidated structured entities which they need to 'maintain', and also if they regularly invest in such structures.

32 EFRAG notes that some of the information is already collected for risk management purposes, regulatory requirements and communication with investors and does not expect the cost to gather and process the data on an ongoing basis to be significant.

Interests in joint arrangements and associates

33 EFRAG notes that in some cases the requirement to disclose summarised financial information for every material joint venture and associate will to need to be collected solely for the purpose of providing the disclosure under IFRS 12. In EFRAG's view, while some companies already collect all (most) of this information (and their cost to report it would be low), other companies will incur additional ongoing costs of gathering and processing the information.

34 EFRAG understands that an operational difficulty, and an increase in costs, might arise when:

(a) The information available is not based on IFRS.

(b) Information will need to be audited (when previously it was not because it was not required for the IFRS consolidated accounts).

(c) In some jurisdictions, it may be difficult to access the information, because under local legislation, investors may not be allowed to disclose data about the investees that is not yet published.

(d) The requirement to provide a reconciliation of the data in the summarised financial information (of the joint venture or associate) to the carrying amount of the investment.

Venture capital organisations, mutual funds, unit trusts and similar entities that have an interest in a joint venture or associate

35 In EFRAG's view, the ongoing costs to collect and process the data to implement the disclosure requirements are likely to be higher for venture capital organisations or similar entities that have material interests in numerous joint ventures and associates. However, in EFRAG's view the number of preparers affected will be relatively limited.

Costs for users

36 EFRAG has carried out an assessment of the cost implications for users resulting from implementing IFRS 12.

37 Users will need to understand why the numbers in the financial statements are different and what this means when performing their analysis. Considering the significance of the change and the increase in the information provided in the notes, in some cases detailed changes to the models will be needed, and therefore the one-off costs are expected to be significant for users.

38 However, users are expected to benefit from the significant ongoing cost savings, because they will not need to undertake alternative procedures to collect relevant information that was previously not made available in the financial statements.

39 The ongoing costs of analysing the additional disclosure are not expected to be significant for users, as the entities are required to aggregate the data and provide it in the meaningful way. However, if entities do not aggregate the data in a meaningful way, users may need to spend more time and effort to search for relevant information and this will lead to higher ongoing costs for them. In such cases, the ongoing costs will be higher for entities that have interests in many unconsolidated structured entities.

Benefits for preparers and users

40 EFRAG has carried out an assessment of the benefits for users and preparers resulting from implementing IFRS 12.

Preparers

41 EFRAG notes that the new disclosures about an entity's involvement with unconsolidated structured entities and the expanded disclosure about the nature and extent of risks associated with an entity's interests in other entities, will improve financial reporting. Hence, it will enhance communication and user confidence which is likely to lead to a decrease in the cost of capital.

Users

42 IFRS 12 has been developed primarily to address concerns expressed by users who have indicated their dissatisfaction with the lack of information for unconsolidated structured entities, fragmented information and lack of transparency about NCI (how cash flows will be distributed to the shareholders of parent and which part is attributable to non-controlling interests) and requested additional information about interests in associates and jointly controlled entities.

43 In EFRAG's view, the more comprehensive disclosures will help users to understand the nature and extent of risks associated with an entity's interests in other entities. Furthermore, EFRAG notes that the information should be easier to find as it will be presented in the notes to the financial statements, even if some of the information is already presented outside the financial statements on a voluntary basis. This will enhance relevance and understandability of information. Comparability will also be enhanced by harmonising the way information is presented. Under IFRS 12 all entities will be required to provide the same disclosures for the same types of investees they are involved with.

44 To summarise:

(a) Disclosure of an entity's interests in unconsolidated structured entities will allow users to assess and understand the nature and extent of risks to which an entity is exposed and the extent to which its financial and investment activities are dependent on the transactions with the structured entities.

(b) Disclosure of significant judgements and assumptions will enable users to understand significant judgements and assumptions made by an entity when deciding how to recognise and account for its involvement with another entity.

(c) Disclosure of an entity's interests in subsidiaries with material NCI will provide users with information about a group's composition and will enable them to assess the impact of NCI on the group (for example restrictions on transfer of assets and funds and minority protection rights) and cash flow distributions to the ultimate shareholders.

(d) Disclosure of an entity's interests in consolidated structured entities provides users with information about how the entity makes use of the resources and whether some of resources are allocated to provide financial support to consolidated structured entities.

(e) Disclosure of an entity's interests in joint arrangements and associates will provide users with an understanding of the relationship an investor has with joint arrangements and associates and the extent of the activity carried out through joint arrangements. The expanded disclosure will inform users about the investee's debt position, profitability for each material joint venture and associate. The same information will be disclosed for all material joint ventures and associates, which is likely to improve comparability and consistency in the financial reporting and therefore facilitate user analysis.

Overall conclusion

45 EFRAG's assessment is that IFRS 12 is likely to result in one-off and ongoing costs for preparers. The one-off costs are likely to be significant for some preparers, mainly those with interests in numerous structured entities, joint ventures and

associates, and particularly when getting access to the required information is difficult.

46 The ongoing costs of providing the disclosures are unlikely to be significant in most cases, once preparers are acquainted with the new requirements and have adopted their systems and processes to implement the requirements.

47 EFRAG's assessment is that the IFRS 12 is likely to result in significant one-off costs for users (particularly in those cases where detailed changes to their models are needed) and in cost savings on an ongoing basis.

48 EFRAG's assessment is that preparers are likely to benefit from implementing IFRS 12, as the standard requires the provision of more robust disclosures about nature and extent of risks an entity is exposed to, and as such, improve financial reporting and communication with users.

49 EFRAG's assessment is that IFRS 12 will bring significant long term benefits to users.

50 Taken together, EFRAG's assessment is that the overall benefits of enhanced financial information resulting from IFRS 12 are likely to outweigh the costs involved.

APPENDIX 4A – SUMMARY OF IAS 27 (2011)

Background

1 Some of the changes in IAS 27 (2011) result from the development of IFRS 10 Consolidated Financial Statements (IFRS 10) and, as a consequence, the guidance on consolidation has been moved from the existing IAS 27 Consolidated and Separate Financial Statements (IAS 27) to IFRS 10.

2 Other amendments result from the development of IFRS 11 *Joint Arrangements* (IFRS 11)*,* which addresses the accounting for joint arrangements:

(a) Joint ventures that are to be accounted for under the equity method; and

(b) Joint operations for which an entity recognises the assets, liabilities, revenue and expenses relating to its interest in a joint operation in accordance with applicable IFRSs.

3 Currently, entities that prepare separate financial statements under IFRSs, account for investments in jointly controlled entities (which could be classified under IFRS 11 as joint ventures or as joint operations) either at cost or in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* (i.e. the reference to IFRS 9 *Financial Instruments* should be read as a reference to IAS 39).

What has changed?

4 Most of the existing requirements to account for investments in subsidiaries, joint ventures (as defined in existing IAS 31 *Interests in Joint Ventures* (IAS 31)) and associates in the separate financial statements prepared under IFRSs have been carried forward to IAS 27 (2011). Only a limited number of minor clarifications have been added which are described below:

(a) Terms and definitions: The definitions and terms used in IAS 27 (2011) have been made consistent with the terminology used in IFRS 10, IFRS 11, IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12) and IAS 28 (2011) *Investments in Associates and Joint Ventures* (IAS 28 (2011)).

(b) Relocation of requirements: Except for (c) below, the requirements applicable to separate financial statements have been moved from existing IAS 28 *Investments in Associates* and IAS 31 to IAS 27 (2011).

(c) Accounting for joint operations: The accounting requirements in the separate financial statements (of the joint operators and of the parties without joint control) relating to interests in joint operations structured through a separate vehicle have been moved to IFRS 11. This means that interests in joint operations will be accounted for in the separate financial statements in the same way as in the consolidated financial statements. EFRAG's initial assessments of IFRS 11, including this amendment, are discussed in a separate document.

(d) IFRSs applicable for separate financial statements: The standard clarifies that an entity that prepares separate financial statements under IFRSs, must apply *all* relevant IFRSs.

(e) Disclosure: To achieve consistency with the requirements in IFRS 12, an entity is required to disclose the principal place of business of the entity (and country of incorporation if different) of a parent and of all significant investments in subsidiaries, joint ventures and associates.

When does IAS 27 (2011) become effective?

5 IAS 27 (2011) becomes effective for the annual periods beginning on or after 1 January 2013. Earlier application is permitted, but only if an entity applies IAS 27 (2011) together with IFRS 10, IFRS 11, IFRS 12 and IAS 28 (2011).

APPENDIX 4B – ANALYSIS OF THE COSTS AND BENEFITS OF IAS 27 (2011)

EFRAG's initial analysis of the costs and benefits of IAS 27 (2011)

1 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IAS 27 (2011), both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – EFRAG's initial assessment was that IAS 27 (2011) will not result in any significant costs for users and preparers.

(b) *Benefits* – EFRAG's initial assessment was that IAS 27 (2011) will not result in any significant benefits for prepares and users.

2 EFRAG published its initial assessment and supporting analysis on 9 February 2012. It invited comments on the material by 11 March 2012. In response, EFRAG received 21 comment letters. Nine respondents agreed with EFRAG's assessment of the benefits of implementing IAS 27 (2011) and the associated costs involved for users and preparers. Eleven respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing IAS 27 (2011) in the EU, but supported EFRAG's recommendation that IAS 27 (2011) be adopted for use in Europe. One respondent did not comment on this specific assessment.

EFRAG's final analysis of the costs and benefits of IAS 27 (2011)

3 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IAS 27 (2011) is presented below.

Approach adopted for EFRAG's cost and benefit assessments of IAS 27 (2011)

4 The approach adopted to conduct EFRAG's assessments on the costs and benefits of IAS 27 (2011) is similar to the approach EFRAG undertook in its technical assessments of IAS 27 (2011). EFRAG focused on the changes ('amendments') to existing IAS 27 that are likely to result in additional costs and additional benefits to preparers and users.

5 EFRAG notes that the following amendments to existing IAS 27 are mainly minor consequential amendments or clarifications of existing IFRSs:

(a) Terms and definitions: The definition and terms used have been made consistent with the terminology used in IFRS 10, IFRS 11, IFRS 12 and IAS 28(2011).

(b) Relocation of requirements: Except for the accounting for joint arrangements classified as joint operations under IFRS 11, the requirements applicable to separate financial statements have been moved from existing IFRSs to IAS 27 (2011).

(c) IFRSs applicable for separate financial statements: The standard clarifies that an entity that prepares separate financial statements under IFRSs, must apply *all* relevant IFRSs.

(d) Disclosure: To achieve consistency with the requirements in IFRS 12, an entity is required to disclose the principal place of business of the entity (and country of incorporation if different) of a parent and of all significant investments in subsidiaries, joint ventures and associates.

6 In EFRAG's view, these four amendments to IAS 27 are straightforward – they clarify or correct existing IFRS in minor ways – and do not raise significant concerns about costs and benefits to preparers and users. For this reason, they are not discussed specifically in this Appendix.

7 In EFRAG's view, the only significant amendment to existing IAS 27, relates to the accounting for joint arrangements classified as joint operations under IFRS 11. EFRAG initial assessments on IFRS 11, including this amendment, are discussed in a separate document.

Conclusion

8 EFRAG's overall assessment is that IAS 27 (2011) will not involve any significant change in costs or benefits for preparers or users (excluding the amendment relating to the accounting for joint operations in the separate financial statements of a joint operator, which is assessed as part of EFRAG's assessment overall assessment on IFRS 11).

APPENDIX 5A– SUMMARY OF IAS 28 (2011)

Background

1 Existing IAS 28 *Investments in Associates* (IAS 28) provides guidance on the accounting for associates and the application of the equity method.

2 The changes to existing IAS 28 result from the IASB's project on IFRS 11 *Joint Arrangements* (IFRS 11), which replaces the existing IAS 31 *Interests in Joint Ventures* (IAS 31).

3 Under IFRS 11, joint arrangements are classified either as joint operations or joint ventures and joint ventures are required to be accounted for using the equity method. The IASB decided to incorporate the accounting for joint ventures in IAS 28 (2011) given that the equity method is required for both investments in associates and joint ventures.

The issue

4 The *majority* of changes to IAS 28 result from the incorporation of the accounting for joint arrangements classified as "joint ventures" under IFRS 11, into IAS 28 (2011).

5 It was not the IASB's intention to reconsider the fundamental approach to the equity method established by IAS 28 and related Interpretations. Therefore, the assessment of significant influence and the approach underlying the equity method of accounting have been carried forward from existing IAS 28.

What has changed?

6 The title of IAS 28 has been changed to reflect that it addresses the application of the equity method with regard to associates and joint ventures.

7 IAS 28 (2011) introduces a number of small amendments to the existing IAS 28, which are summarised below:

(a) Potential voting rights: The additional guidance on potential voting rights when assessing significant influence or joint control has been moved from *Guidance on implementing IAS 27 Consolidated and Separate Financial Statements, IAS 28 and IAS 31* to IAS 28 (2011). The guidance requires an entity to take into account the effect of potential voting rights that currently give the entity access to the returns associated with an ownership interests. The guidance has *not* been amended to reflect the new guidance on potential voting rights in IFRS 10 *Consolidated Financial Statements* (IFRS 10), because the IASB did not reconsider the definition of significant influence when it amended IAS 28 and concluded that it would not be appropriate to change one element of significant influence in isolation.

(b) Classification as held for sale: IAS 28 (2011) clarifies that an entity must apply the requirements in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* to a portion of an investment in an associate or a joint venture that meets the criteria to be classified as held for sale.

(c) Partial use of fair value option extended to a portion of an associate: The use of the fair value measurement option in existing IAS 28 is extended to a portion of an investment in an associate if that portion is held indirectly through a venture capital organisation or a similar entity. Existing IAS 28 is silent in this respect and different accounting practices have emerged. The guidance on partial use of fair value option does not apply to interests in joint ventures, because the IASB thought that such events would be unlikely in practice.

(d) Incorporation of SIC-13 *Jointly Controlled Entities–Non-Monetary Contributions by Venturers*: SIC-13 provides guidance on non-monetary contributions to a jointly controlled entity being made in exchange for an equity interest in the jointly controlled entity, and limits a venturer to recognise in profit or loss only the portion of the gain or loss attributable to the equity interests of the other venturers. The guidance in SIC-13 has been substantially carried forward to IAS 28 (2011) and applies also to interests in associates.

8 IAS 28 (2011) also introduces the following two more significant amendments to accounting and disclosure requirements:

(a) Changes in interests held when an associate becomes a joint venture or vice versa:

A change was introduced in the accounting with respect to scenarios where an investment in an associate becomes an investment in a joint venture, or vice versa. Currently such changes trigger a remeasurement. IAS 28 (2011) eliminates the requirement to remeasure the retained interest, because the IASB noted that the composition of the group is unaffected, when an interest in a joint venture becomes an associate or vice versa. In such cases, both investments (i.e. the joint venture and the associate) continue to be measured using the equity method. Considering that there is neither a change in the group boundaries nor a change in the measurement requirements, the IASB concluded that losing joint control and retaining significant influence is not an event that triggers remeasurement.

(b) Disclosures in IFRS 12 *Disclosure of Interests in Other Entities* (IFRS 12) – apply to all interests within the scope of IAS 28:

The scope exception in existing IAS 28 for investments held in venture capital organisations and similar entities has been removed and characterised as a measurement exception. As a result, entities are required to provide the disclosures in IFRS 12 for all interests in joint ventures and associates, including those that are held by venture capital organisations or similar entities and measured at fair value.

When does IAS 28 (2011) become effective?

9 IAS 28 (2011) becomes effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. Early adopters would need to disclose that fact and apply IFRS 10, IFRS 11, IFRS 12 and IAS 27 (2011) *Separate Financial Statements* at the same time.

APPENDIX 5B – ANALYSIS OF THE COSTS AND BENEFITS OF IAS 28 (2011)

EFRAG's initial analysis of the costs and benefits of IAS 28 (2011)

1 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users from implementing IAS 28 (2011), both in year one and in subsequent years. The results of EFRAG's initial assessment can be summarised as follows:

(a) *Costs* – EFRAG's initial assessment was that, for preparers, IAS 28 (2011) would involve a decrease in costs. For users, costs are unlikely to be significantly affected by IAS 28 (2011).

(b) *Benefits* – EFRAG's initial assessment was that IAS 28 (2011) does not affect benefits for preparers in any significant way, and the users are likely to benefit from IAS 28 (2011), as the information resulting from them will assist users in their analysis.

2 EFRAG published its initial assessment and supporting analysis on 9 February 2012. It invited comments on the material by 11 March 2012. In response, EFRAG received 21 comment letters. Eight respondents agreed with EFRAG's assessment of the benefits of implementing IAS 28 (2011) and the associated costs involved for users and preparers. Eleven respondents did not comment specifically on EFRAG's initial assessment of the costs and benefits of implementing the IAS 28 (2011) in the EU, but supported EFRAG's recommendation that IAS 28 (2011) be adopted for use in Europe. Two respondents did not agree with EFRAG's assessment of the benefits of implementing IFRS 11 and/or the associated costs or did not comment on this specific assessment.

EFRAG's final analysis of the costs and benefits of IAS 28 (2011)

3 Based on its initial analysis and stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of IAS 28 (2011) is presented below.

Approach adopted for EFRAG's cost and benefit assessments of IAS 28 (2011)

4 The approach adopted to conduct EFRAG's assessments on the costs and benefits of IAS 28 (2011) is similar to the approach EFRAG undertook in its technical assessments of IAS 28 (2011). Essentially, EFRAG focused on the changes that are likely to result in additional costs and additional benefits to preparers and users.

5 EFRAG notes that the following small changes resulting from IAS 28 (2011) are primarily clarifications of existing IFRSs or confirm existing practices in the absence of specific guidance in IFRSs:

(a) Potential voting rights;

(b) Classification as held for sale;

(c) Partial use of fair value option extended to a portion of an associate;

(d) Application of IFRS 5; and

(e) Incorporation of SIC-13 into IAS 28.

6 In EFRAG's view, the first four amendments to IAS 28 are straightforward – they clarify or correct existing IFRS in minor ways – and do not raise any significant new concerns about costs and benefits. For this reason, they are not discussed specifically in this Appendix.

7 The amendment regarding the incorporation of SIC-13 *Jointly Controlled Entities – Non-Monetary Contributions by Venturers* into IAS 28, it was not the IASB's intention to reconsider the fundamental approach to the equity method established by IAS 28 and related Interpretations. Therefore, the assessment of significant influence and the approach underlying the equity method of accounting have been carried forward from existing IAS 28. As a consequence, the amendment is not discussed specifically in this Appendix.

8 The amendment relating to disclosure is assessed as part of EFRAG's assessments on IFRS 12.

9 IAS 28 (2011) introduces a change in accounting with respect to scenarios where an investment in an associate becomes an investment in a joint venture, or vice versa, and eliminates the requirement to remeasure the retained interest. This amendment is discussed in the paragraphs below.

Cost for preparers and users

10 EFRAG has carried out an assessment of the cost implications for preparers and users resulting from IAS 28 (2011).

11 EFRAG's overall assessment is that IAS 28 (2011) will result in a decrease in costs to preparers, primarily because an entity does not have to remeasure an investment at fair value, when it changes its interest in the investment from a joint venture to an associate and vice versa. Costs to users are unlikely to be significantly affected by IAS 28 (2011).

Benefits for preparers and users

12 EFRAG has carried out an assessment of the benefits for preparers and users resulting from IAS 28 (2011).

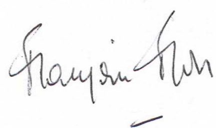
13 EFRAG's assessment is that benefits for preparers are unlikely to be significantly affected by IAS 28 (2011).

14 Overall, EFRAG's assessment is that users are likely to benefit from IAS 28 (2011) as the information resulting from it will generally remove inconsistencies in accounting and therefore increase comparability between entities and will enhance their analysis.

Conclusion

15 EFRAG's overall assessment is that overall the benefits to be derived from IAS 28 (2011) (excluding the amendment relating to disclosure, which is assessed as part of EFRAG's initial assessments on IFRS 12) are likely to outweigh any incremental costs associated with them.

30 March 2012



Françoise Flores
EFRAG Chairman