

{Draft}

~~Comment Letter~~

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Comment Letter

International Accounting Standards Board
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom
{XX20 January 2025}

Dear Mr Barckow,

Re: Exposure Draft Equity Method of Accounting IAS 28 *Investments in Associates and Joint Ventures* (revised 202x)

On behalf of the EFRAG, I am writing to comment on the Exposure Draft Equity Method of Accounting IAS 28 *Investments in Associates and Joint Ventures* (revised 202x), issued by the IASB on 19 September 2024 (the ‘ED’).

This letter is intended to contribute to the IASB’s due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on the endorsement of definitive IFRS Accounting Standards in the European Union and European Economic Area.

EFRAG acknowledges that the primary focus of the ED is not to fundamentally revise the equity method but to address existing application challenges, reduce the existing diversity in practice in the application of IAS 28 requirements, enhance the understandability of these requirements, and increase the comparability of reported information. Overall, from the feedback received so

~~far, stakeholders consider~~EFRAG considers that the ED's proposals are a positive step that will help to ~~reduce existing diversity in practice and~~ meet the ~~other~~ intended objectives. EFRAG recommends the IASB finalise the amendments based on the feedback to the ED as soon as possible. At the same time, based on the feedback received, EFRAG recommends that a fundamental review of the equity method should thereafter be added to the IASB workplan (as the second phase of the project) after finalising the amendments proposed in the ED.

Areas where EFRAG supports the ED's specific proposals: EFRAG supports the following proposals in the ED.

- Measurement of cost of an associate or joint venture: EFRAG generally supports the ED's proposal on the measurement of the cost of associates or joint ventures.
- Transactions of an investor/reporting entity with associates and joint ventures requiring full recognition of related gains or losses: EFRAG considers that the proposal will result in desirable consistency in the application of the equity method for ~~all~~ transactions with associates or joint ventures. It is also a simplified and less costly solution compared to the other alternatives considered by the IASB. However, EFRAG expresses some concerns with the proposals (restructuring opportunities and earnings management) and recommends enhanced disclosures as well as clarification about whether side stream transactions are covered by the proposed amendments.
- Disclosures: While acknowledging that there are concerns with some of the proposed disclosures, EFRAG supports the proposed disclosures taking into account the ED proposals for transactions with associates or joint ventures. We have made suggestions to further enhance the disclosures.
- Impairment indicators: While acknowledging there are mixed views, EFRAG supports the ED's proposals related to indicators of impairment of associates or joint ventures.

EFRAG's specific concerns with the ED's proposals: EFRAG has also highlighted key concerns and made suggestions for the following proposals.

- Measurement of cost of an associate or joint venture: The ED is silent on whether transaction costs are included in the carrying amount of the investment. EFRAG recommends that they be included, and this is in line with the July 2009 IFRIC update. EFRAG recommends clarifying the appropriate accounting treatment for transaction costs, i.e., whether to expense or capitalise these costs and how this can depend on whether the investment relates to either the acquisition of a business or an asset.

- ~~Via a question for constituents, because of mixed views received, EFRAG is also exploring whether there are any issues related to the ED's proposed inclusion of deferred taxes in the carrying amount of the investment.~~
- Acquiring additional ownership interest while retaining significant influence (layered approach): ~~Though~~ EFRAG considers the ED's proposal to treat each additional acquired layer as a separate unit of account as being the only alternative preferable to the fair value remeasurement of the entire investment. ~~However~~, EFRAG questions the need for a full-fledged purchase price allocation of each acquisition and highlights stakeholders' significant concerns about the cost and complexity of aspects of the ~~version of~~ layered approach proposed in the ED. ~~We seek constituents' views on stakeholders' EFRAG recommends further simplification of this proposed alternatives approach. In our response to Question 2, we suggest a modified-PPA approach that the IASB can consider as a starting point.~~
- Other changes in ownership interest while retaining significant influence (e.g. an associate's or joint venture's issuance or redemption of shares): ~~As opposed to treating these EFRAG disagrees with the ED's proposal to treat~~ other changes in ownership arising from non-exchange transactions as deemed purchases or disposals of ownership interest. ~~This is~~ due to the associated cost ~~and~~ complexity, ~~EFRAG recommends of the proposed accounting treatment and lack of economic equivalence between these transactions and acquisitions or disposals of ownership interests that changes in ownership arising from non-exchange transactions (those addressed in the ED, issued hybrid instruments, etc.) be scoped out of the amendments until are based on the exchange of consideration. Thus, we recommend that, unless~~ a holistic, principles-based solution that is not unduly costly can be developed, these changes should be scoped out of the IAS 28 amendments. A transitional scoping out of these other changes in ownership interests may fail to remedy existing diversity in practice but it will certainly not worsen it. Plus, the IASB has in any case considered that existing diversity is acceptable for the other changes in ownership transactions that were not in the scope of the ED.
- Recognition of the investor's share of losses: EFRAG recommends that, in addition to the ED's proposals, the IASB prohibit the recognition of additional goodwill for acquired additional interest when the carrying amount of the investment is reduced to nil. due to investor's share of losses. Moreover, we note several areas where the proposals for the recognition of share of profit or loss and other comprehensive income need further clarification and enhancement.

- Separate financial statements: EFRAG ~~notes there are mixed views on~~ supports the ED's proposed application of a single equity method across IFRS Accounting Standards, ~~with a concern expressed by some stakeholders similar to~~ except for the Alternative View in the ED about the application recognition of the ED's proposals to account for full gains or losses from transactions with subsidiaries ~~in separate financial statements. Via a question to constituents, EFRAG is assessing the pervasiveness of the application of the equity method in separate financial statements and whether there are any concerns related to the ED's proposal within EU jurisdictions.~~ EFRAG also suggests that the IASB clarify whether the ED's proposals for the equity method are applicable when an investment is measured at cost in separate financial statements.
- Transition requirements: EFRAG agrees with the proposed transition requirements except for the proposal to apply retrospectively the requirement to recognise the full gain or loss on all transactions with associates or joint ventures. ~~EFRAG has received mixed views from stakeholders on this proposal. EFRAG asks for clarification on other specific aspects of the proposed transition requirements (investments measured at nil and unrecognised gains or losses) (See response to Question 9).~~

In general, EFRAG notes that the simplification principle is only selectively applied in some of the proposed solutions (e.g. for the full recognition of gains or losses for transactions with associates and joint ventures) and it could ~~be~~ also be applied ~~towardsto~~ other proposals (e.g. the layered approach of accounting for acquired additional ownership interests while retaining significant influence).

EFRAG's detailed comments and responses to the questions in the ED are set out in the Appendix.

If you would like to discuss our comments further, please do not hesitate to contact Aleksandra Sivash, Vincent Papa or me.

Yours sincerely,

Wolf Klinz

EFRAG FRB Chair

Appendix – EFRAG’s responses to the questions raised in the ED

Overall comments on the ED proposals

- 1 EFRAG acknowledges that the primary focus of the ED is to address existing application challenges, reduce existing diversity in practice in the application of IAS 28 requirements, enhance the understandability of these requirements, and increase the comparability of reported information. Overall, the feedback received so far indicates that stakeholders consider the ED’s proposals to be a positive step that will help to ~~reduce existing diversity in practice and~~ meet the ~~other~~ intended objectives.
- 2 EFRAG is cognisant that the ED is not focused on fundamentally revising the equity method or clarifying whether the equity method is either a measurement approach or a one-line consolidation. EFRAG understands that a more fundamental review would likely lengthen the project duration and defer the resolution of current application challenges. We also acknowledge that Table 2 and BC 15 to 16 in the Basis for Conclusions delineate the principles (i.e. principles A to H) underlying the classification, the boundary of the reporting entity, initial recognition, subsequent measurement and derecognition requirements of IAS 28. These principles taken in conjunction with other IFRS Accounting Standards (e.g. IFRS 3) and the Conceptual Framework for Financial Reporting (Conceptual Framework) have informed the proposals in the ED. EFRAG acknowledges that, as evaluated in the 2014 EFRAG Short Discussion Series paper¹ (SDS) and other National Standard Setters² publications, instead of having mutually exclusive underpinnings, depending on the nature of the transaction or event, the equity method can be a hybrid approach encompassing³ the features of both a consolidation approach and measurement method.
- 3 In general, EFRAG observes that some of the proposals are significant amendments that will change current practice. For example, the recognition of full gains or losses for transactions with associates addressed in Question 4, and the application of a single equity

¹ 2014 EFRAG Short Discussion Series – [The Equity Method: A measurement basis or one-line consolidation?](#)

² Korean Accounting Standards Board – [Research Report No 35 The Equity Method](#)

³ The equity method can encompass the features of a consolidation approach (e.g. goodwill recognition occurs on acquisition of ownership interests; bargain purchase gains are recognised in profit and loss; the elimination of the investor’s or joint venturer’s share of profits and losses from upstream and downstream transactions; etc.) as well as have the features of a measurement basis (including the transaction cost in carrying amount, the non-recognition of losses in excess of the carrying value in most circumstances, and not restricting gains or losses on upstream and downstream transactions with investees).

method across the consolidated and separate financial statements addressed in Question 6. There are unaddressed areas (e.g. the treatment of transaction costs) and insufficiently addressed areas (other changes in ownership while retaining significant influence). EFRAG also notes that the simplification principle is only selectively applied in some of the proposed solutions (e.g. for the full recognition of gains or losses for transactions with associates and joint ventures) and it could be also applied for other proposals (e.g. the layered approach of accounting for acquired ownership interests while retaining significant influence) as indicated in our response to Question 2.

4 Finally, EFRAG notes that during the outreach on the ED, notwithstanding the justification mentioned in paragraph 2 above for the exclusion of a fundamental review of equity method from the scope of the ED, in addition to feedback on the specific proposals to address practical challenges, EFRAG has heard a range of views on the usefulness of the equity method relative to other recognition and measurement approaches. Some stakeholders including users have confirmed its usefulness and complementary nature to fair value or cost measurement basis in the accounting for the acquisition of ownership interests in a business. However, many other stakeholders including other users are more sceptical about its usefulness. Furthermore, many respondents to EFRAG's draft comment letter have pointed out that the IASB's definition of the nature and purpose of the equity method could have enhanced the formulation of suitable answers to the practical application challenges. A similar message emerged from a survey by academics from Spanish Universities with responses from 117 diverse professionals (academics, auditors, analysts and preparers). These survey results were presented at the EFRAG Academic Panel.

5 As noted above, EFRAG considers the ED proposals to be a positive step, and we encourage the IASB to finalise the IAS 28 amendments proposed in the ED as soon as possible. Thereafter, after the issuance of the amendments, EFRAG recommends that a fundamental review of the equity method should be added to the IASB work plan as the second phase of the project.

Question 1 – Measurement of cost of an associate or joint venture

Notes to constituents – Summary of proposals in the ED

Measurement of the cost of an associate on obtaining significant influence

~~4 IAS 28 currently require an investor or joint venturer that obtains significant influence in an associate or joint venture to account for the difference between the cost of the investment and its share of the net fair value of the associate's identifiable assets and liabilities as~~

~~goodwill or bargain purchase. However, IAS 28 does not specify how to measure the cost of the investment, resulting in diversity in practice. Therefore, the IASB decided to propose requiring that:~~

- ~~a) the cost of an associate or joint venture, upon obtaining significant influence, be measured at fair value of the consideration transferred, including the fair value of any previously held interest in the associate or joint venture.~~
- ~~b) contingent consideration be recognised as part of the consideration transferred and measured at fair value. After initial recognition:
 - ~~(i) contingent consideration classified as equity should not be measured;~~
 - ~~(ii) other contingent consideration should be measured at fair value at each reporting date, with changes recognised in profit or loss.~~~~

~~5 These amendments aim to ensure consistency with IFRS 3 Business Combinations principles on business combinations. The requirement to measure the cost of an investment at fair value of the consideration transferred, including the fair value of any previously held ownership interest is based on the considerations that:~~

- ~~a) obtaining significant influence changes both the relationship between the investor and the investee, and the accounting method used by the investor;~~
- ~~b) measuring the cost of the investment at fair value would align with measurement at fair value of the underlying assets and liabilities;~~
- ~~c) measuring previously held interest at fair value would not be overly costly for entities because the previously held interest would have been measured at fair value in accordance with IFRS 9 Financial Instruments.~~

~~Contingent considerations:~~

~~6 The IASB proposes that, on obtaining an investment in an associate or joint venture or purchasing an additional interest, the investor or joint venturer should recognise contingent consideration as part of the consideration transferred and measure it at fair value. The IASB further proposes that contingent consideration classified as equity should not be measured after initial recognition, and any settlement of this consideration should be recorded within equity. For contingent consideration classified as a liability, the IASB recommends that it be measured at fair value at each reporting date, with any changes in fair value recognised in profit or loss.~~

~~7—In reaching this decision, the IASB considered that the proposed requirements would be similar to those in IFRS 3 for contingent consideration on the acquisition of a subsidiary. Further, the IASB understands that this approach is already commonly applied in practice when accounting for contingent consideration on the initial recognition of an investment in an associate or the purchase of an additional interest. Therefore, IASB thinks that in most cases, the new requirements are not expected to impose significant additional costs on preparers.~~

~~Recognition of Deferred Taxes~~

~~8—IAS 28 requires an investor or joint venturer to determine its share of the net fair value of the associate's or joint venture's identifiable assets and liabilities, which includes adjustments to the carrying amounts of the assets and liabilities as reported in the associate's financial statements (referred to as 'fair value adjustments'). An application question arises about whether the investor or joint venturer is required to include the deferred tax effects related to those fair value adjustments in the carrying amount of an investment in an associate on initial recognition of the investment. The IASB understands that various approaches are applied in practice. The most common practice is to include those deferred tax effects in the carrying amount of the investment.~~

~~9—The IASB decided to propose requiring an investor or joint venturer to include in the carrying amount of its investment the deferred tax effects related to measuring its share of the associate's identifiable assets and liabilities at fair value both at obtaining significant influence and when purchasing additional ownership interest. In reaching this decision, the IASB considered that the proposed approach would:~~

- ~~a)—be consistent with concepts underlying the procedures used in accounting for the acquisition of a subsidiary as outlined in IFRS 3;~~
- ~~b)—provide faithful representation of the financial effects related to future tax consequences;~~
- ~~c)—provide useful information to users, for example, when the adjustments to the investor's or joint venturer's share of the associate's or joint venture's profit or loss in subsequent reporting periods would include both the reversal of fair value adjustments and the reversal of related deferred tax effects.~~

~~10—The IASB acknowledged that applying the proposed approach would result in some costs and complexity for preparers, but took the view that the benefits to users of the proposed approach would outweigh the costs to preparers.~~

ED Question 1- Measurement of cost of associate or joint venture

Paragraph 32 of IAS 28 requires an investor that obtains significant influence to account for the difference between the cost of the investment and the investor's share of the net fair value of the associate's identifiable assets and liabilities either as goodwill (included in the carrying amount of the investment) or as a gain from a bargain purchase (recognised in profit or loss). However, IAS 28 does not include requirements for how an investor measures the cost of the investment on obtaining significant influence—for example:

- (a) whether to measure any previously held ownership interest in the associate at fair value; or
- (b) whether and if so how to recognise and measure contingent consideration.

The IASB is proposing an investor:

- (a) measure the cost of an associate, on obtaining significant influence, at the fair value of the consideration transferred, including the fair value of any previously held interest in the associate.
- (b) recognise contingent consideration as part of the consideration transferred and measure it at fair value. Thereafter:
 - (i) not remeasure contingent consideration classified as an equity instrument; and
 - (ii) measure other contingent consideration at fair value at each reporting date and recognise changes in fair value in profit or loss.

Paragraphs BC17–BC18 and BC89–BC93 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 1 – Measurement of cost of associate or joint venture

General ~~comment – inconsistency in the comments~~

~~Cost definition – of cost in the ED versus other IFRS Accounting Standards~~

~~116~~ : The definition of cost⁴ in Appendix A of the ED is similar to that under IFRS 3 but it is not exactly the same as the definition of cost⁵ in other IFRS Accounting Standards (IAS 16.6, IAS 38.8 and IAS 40.5). ~~As a cross-cutting concern, some stakeholders~~ Stakeholders have highlighted that the different definitions of cost across ~~some various~~ IFRS Accounting Standards and the absence of its definition in other Standards may lead to confusion on what ought to be included in (a) what is explicitly labelled as the cost amount and (b) measurements deemed to be part of the notion of cost-based measurement, including the equity method (see our response to Question 6 on separate financial statements). In this regard, EFRAG notes that in the feedback⁶ to the Discussion Paper⁷ *Accounting for Variable Consideration – A Purchaser's Perspective* some stakeholders similarly supported a single definition of cost across IFRS Accounting Standards to enable consistent interpretation. However, there was also an argument put forward by other stakeholders against the same definition, i.e. it might not result in the most relevant reported information.

~~127~~ Hence, ~~EFRAG acknowledges there is unlikely to be a definition of cost applicable across IFRS Accounting Standards. and~~ Based on the above, we suggest ~~that~~ that Appendix AA's definition of cost should be enhanced to clarify its interaction with either cost as defined or other notions of cost applied in other IFRS Accounting Standards (see our response to Question 6 on separate financial statements).

8 Acquisition of a business versus an asset: IAS 28 does not distinguish between the acquisition of a business and the acquisition of an asset. However, the appropriate accounting treatment for various application questions (e.g., whether to recognise goodwill on acquisition of ownership interests, how to treat transaction costs, contingent

⁴ Appendix A defines cost of associate or joint venture as 'Fair value of the consideration transferred, including the fair value of any previously held ownership interest (or any investment retained) in the *associate or joint venture*, measured at the date an investor obtains *significant influence* or a *joint venturer* obtains *joint control*.'

⁵ Under IAS 16, IAS 38 and IAS 40, cost is defined as the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction, or, when applicable, the amount attributed to that asset when initially recognised under the specific requirements of other IFRS Accounting Standards, e.g. IFRS 2 *Share-based Payment*.

⁶ EFRAG, April 2024, [Feedback Statement](#), *Accounting for Variable Consideration – A Purchaser Perspective*, Discussion Paper.

⁷ EFRAG, September 2022, [Accounting for Variable Consideration – A Purchaser Perspective, Discussion Paper](#).

consideration transactions) would depend on whether the investment represents either the acquisition of a business or an asset.

9 Moreover, based on stakeholders' feedback, EFRAG is aware that the revision of the definition of a business under IFRS 3 led to more transactions (e.g. exploration or an operating license held through an investee) being classified as asset acquisitions rather than business acquisitions and such transactions are widespread in certain industries. Therefore, EFRAG recommends the IASB should clarify the accounting for recognition and subsequent changes in ownership interests in assets, including ownership interests in non-financial assets, when an investor has a significant influence.

10 Significant influence: Based on the feedback received, EFRAG suggests that the requirements to assess whether an entity has significant influence, as outlined in IAS 28.6 and paragraph 9 of the ED, and is correspondingly within the scope of IAS 28 requirements, should also take into account an investor's restrictions to accessing investee information. Such restrictions could arise due to practical or regulatory barriers (e.g., if the investee is listed, the equal access to information rules for listed companies will prohibit allowing privileged access for some investors). This imposes challenges for reporting entities to apply the ED's proposed requirements (e.g., towards applying the requirements for the acquisition of additional ownership interest mentioned in Question 2).

Specific comments on the ED proposals for measurement of cost of associate or joint venture

Measurement of previously held ownership interest on obtaining significant influence

~~1311~~ EFRAG supports the proposed measurement of the previously held ownership interest at fair value. This proposal is unlikely to be too costly for entities to apply because, before obtaining significant influence, the previously held ownership interest would have already been measured at fair value under IFRS 9 *Financial Instruments*, unless the consideration transferred constitutes mainly non-monetary asset and would inherently contain higher measurement uncertainty.

~~1412~~ That said, EFRAG notes that for a previously held ownership interest in an unquoted company, the fair value measurement would only have taken place at certain points in time (e.g. at a reporting date). Therefore, additional costs to determine the fair value of previously held interest may be incurred at the time that significant influence is obtained. ~~There may also be additional costs in cases where an updated valuation of the previously held ownership interest is necessary after the investor obtains significant influence and there is an embedded significant influence premium.~~ EFRAG assumes that these incremental costs are likely to be insignificant.

~~13~~ Some stakeholders have highlighted to EFRAG the lack of clarity on the accounting for increases in ownership interests in assets rather than businesses and on whether the equity method principles, including the fair value remeasurement of previously held interest on obtaining significant influence, would be applicable. These stakeholders have indicated Further, EFRAG suggests that the IASB should:

- (a) clarify, similarly to the requirement in paragraph 42 of IFRS 3, how to account for the difference, if any, between the fair value of the previously held ownership interest and its previous carrying amount. This clarification could be helpful, as the unit of account used to determine the fair value of any previously (i.e. before obtaining significant influence) held ownership interest can have an impact on the determination of the fair value of this ownership interest (i.e. whether a premium for significant influence should be included in the fair value); and
- (b) specify what is meant by ‘the fair value of any previously held ownership interest’, as the current definition could lead to confusion as to whether it refers to the fair value already recognised by the investor of its previously held ownership interest or it refers to a remeasurement of the investor’s previously held ownership interest when purchasing an additional ownership interest (obtaining significant influence).

~~15~~ ~~that the revision of the definition of a business under IFRS 3 led to more transactions (e.g. exploration or an operating license held through an investee) being classified as asset acquisitions rather than business acquisitions and such transactions are widespread in certain industries. Therefore, EFRAG recommends the IASB clarify or address in a different project the accounting for increases in ownership interests in assets, including ownership interests in non-financial assets.~~

Transaction costs

~~1614~~ The ED is silent on and does not specify how an investor or joint venturer should account for the transaction costs incurred in acquiring ownership interests. Accordingly, it is unclear whether ~~or not~~ the principles of IFRS 3 should be analogised⁸ to determine the appropriate

⁸ In accordance with IFRS 3, the acquisition related costs are not part of the exchange transaction between the acquirer and the acquiree (or its former owners); they are not considered part of the business combination. Therefore, as clarified in the May 2009 IFRIC update: ‘except for certain specific costs, IFRS 3 requires an entity to account for acquisition-related costs as expenses in the periods in which the costs are incurred and the services are received’. However, in accordance with the July 2009 IFRIC update, paragraph 23 of IASB’s agenda paper 13a from

accounting treatment for the transaction costs incurred. ~~In this regard, EFRAG observes that the chosen treatment for transaction costs may depend on whether the equity method is deemed to be akin to a consolidation approach as done under IFRS 3 (and then costs would be expensed as incurred) or to be a measurement method (where costs would be included in the carrying amount). Based on the feedback received so far and consistent with the July 2009 IFRIC update, EFRAG recommends that transaction costs be included in the carrying amount of the investment. We have also posed a question seeking constituents' views on the appropriate treatment for transaction costs. or July 2009 IFRIC update should be applied.~~

15 EFRAG's constituents expressed mixed views indicating the need for clarification otherwise the diversity in practice will persist. The view favouring expensing transaction costs was premised on analogising the IFRS 9 Financial Instruments and IFRS 3 treatment of transaction costs. The view favouring capitalisation of transaction costs was premised on considering the equity method is inherently a cost-based approach adjusted for changes in net assets and such treatment would be consistent with the accounting for other assets accounted at cost, consistency with the 2009 IFRIC agenda decision; and capitalising the transaction costs aligns with the local requirements for certain jurisdictions.

1716 Hence, EFRAG suggests the IASB clarify the appropriate accounting treatment for transaction costs, and in so doing distinguish between the treatment of transaction costs for the acquisition of a business versus the acquisition of an asset. Our response to Question 6 also touches on unaddressed questions related to transaction costs under separate financial statements.

Contingent consideration

18 EFRAG supports the proposed initial and subsequent measurement of contingent consideration at fair value as this is similar to the approach applied under IFRS 3. However, EFRAG notes that the IFRS 3 definition of contingent consideration is applied in the context of obtaining control and IFRS 3 only applies to an acquisition of business ~~whereas IAS 28 does not explicitly distinguish between the acquisition of a business and the acquisition of an asset.~~

October 2023 notes: 'in contrast, the cost of an equity-accounted investment comprises its purchase price and any directly attributable expenditure necessary to obtain it'.

17 . Therefore, to avoid ambiguity and exacerbating the inconsistency in the accounting for variable and contingent consideration as highlighted in the 2022 EFRAG Discussion Paper⁹, EFRAG suggests that the IASB provide additional guidance in IAS 28 defining contingent consideration in the context of an investor/reporting entity obtaining significant influence in either an asset or business.

1918 EFRAG also suggests that the IASB clarify whether a 12-month window to revise contingent consideration, as permitted under IFRS 3, will be allowed in the context of IAS 28.

19 Further, EFRAG suggests that the IASB clarify that [paragraph B55 of IFRS 18 *Presentation and Disclosure in Financial Statements*, which states that remeasurements of the fair value of a liability for contingent consideration in a business combination recognised applying IFRS 3 should be classified in the operating category, is also applicable for the equity method under IAS 28.](#)

Recognition of goodwill and bargain purchase gains

20 Stakeholders have expressed mixed views on the ED proposals for the recognition of goodwill or bargain purchase gains for the equity-method-accounted investments. Several stakeholders support this aspect of the ED proposals, which is consistent with current practice as far as they are aware. At the same time, other stakeholders, including some users, question the relevance of recognising goodwill in the context of equity-accounted investments where only significant influence but no control is obtained. ~~Moreover, as IAS 28 does not differentiate between the acquisition of an asset or a business, stakeholders have questioned the appropriateness of recognition of goodwill or bargain purchase gains for an asset acquisition. These stakeholders argue that goodwill is more meaningful in the context of the consolidation of businesses and where the reporting entity has control over the subsidiary. and/or in case of an asset acquisition.~~

21 Should the ED proposals be retained, EFRAG suggests the amendments include disclosures that help users identify¹⁰ goodwill and bargain purchase gains derived from acquisitions of ownership interests that are accounted for under the equity method.

⁹ [EFRAG's Discussion Paper Accounting for Variable Consideration](#) outlines complexities related to both recognition and measurement of the contingent liability as well as the measurement of the related asset.

¹⁰ Unlike goodwill arising from a business combination, equity-method-derived goodwill is included in the carrying amount of the investment and is not separately presented as an identifiable asset.

- 22 *Offsetting bargain purchase gains against goodwill:* EFRAG notes that the recognition of goodwill and ~~expensing of~~ bargain purchase gains on the acquisition of ownership interests is indicative of the equity method being viewed as akin to a consolidation approach, even though this inference is not explicitly stated in the ED. That said, some stakeholders have expressed concern about inconsistency in the treatment of goodwill that is recognised as an asset versus bargain purchase gains that are ~~accounted for~~recognised in profit or loss. These stakeholders have argued that the economic value of the investment is better reflected if bargain purchase gains are first netted against the previously recognised goodwill. Moreover, some banking sector stakeholders were concerned about the adverse effects of an “overstated goodwill” amount on their prudential regulatory capital ratios. Hence, EFRAG suggests the IASB should reconsider the proposal by giving more weight to the faithful representation of the economics of an investment than to conceptual consistency/alignment with IFRS 3 principles.
- 23 *Faithful representation of bargain purchase gains:* ~~During~~ EFRAG’s ~~outreach,~~ users/constituents have also emphasised the need for checks and transparency on the recognition of bargain purchase gains as such gains may be a reflection of an entity’s structuring activities. Hence, EFRAG suggests that the ED proposals for the recognition of bargain purchase gains have similar safeguards to those included in the related IFRS 3 requirements¹¹. In addition, in our response to Question 7, we recommend disclosures that inform users about bargain purchase gains.

Deferred tax effects

- ~~24~~ ~~EFRAG has gotten mixed views from~~ Despite concerns raised by some stakeholders ~~on~~ relating to the cost and complexity of recognising and tracking the reversal of deferred taxes and/or changes in local tax rates and the investee’s fiscal status, EFRAG supports the ED’s proposed inclusion of deferred tax effects ~~arising from the fair value adjustments of the associate’s identifiable assets and liabilities~~ in the carrying amount of the investment. ~~Some stakeholders support this inclusion, which~~ This proposal is consistent with current practice ~~as far as they are aware. These stakeholders agree~~ and is aligned with the

¹¹ Paragraph 36 of IFRS 3 requires that, ‘before recognising a gain on a bargain purchase, the acquirer shall reassess whether it has correctly identified all of the assets acquired and all of the liabilities assumed and shall recognise any additional assets or liabilities that are identified in that review. The acquirer shall then review the procedures used to measure the amounts ...’.

~~alignment of the inclusion to IFRS 3 principles, where deferred taxes arising from fair value adjustments are included in the purchase price allocation (PPA).~~

~~2524 EFRAG [notes also agrees with the IASB's reasoning](#) that the inclusion of a deferred tax asset or liability in the carrying amount of the investment ~~also~~ allows a faithful representation of the tax effects that could arise after significant influence is obtained. ~~For instance, as illustrated in an IASB staff paper¹², if an associate disposes¹³ an asset after significant influence is obtained, such inclusion will avoid the recognition of the investor's share of the associate's current tax expense/income without the corresponding recognition of the investor's share of the associate's gain/loss on disposal of the asset.~~~~

~~26 However, some stakeholders have raised concerns about including deferred tax effects in the carrying amount of the investment. They question the appropriateness of the chosen unit of account¹⁴ and they point out that the investee's assets and liabilities (upon which the tax base for the investee's deferred tax determination is ascertained) are not part of the reporting boundary of the investor/reporting entity.~~

~~27 Stakeholders have also raised practical challenges, including difficulties in obtaining the necessary information to calculate deferred taxes due to limited data availability from associates and joint ventures in different tax jurisdictions upon initial recognition and~~

¹² https://www.ifrs.org/content/dam/ifrs/meetings/2023/march/iasb/ap13d_initial_recognition_of_an_investment_in_an_associate_deferred_taxes.pdf

¹³ ~~Consider a scenario where the carrying amount of the investor's share of the associate's asset was increased to its fair value on obtaining significant influence and the tax base of the asset remained at cost to the associate. If the associate subsequently disposes of the asset, it will report a gain and tax expense in its profit or loss. In tandem, if the investor did not recognise a deferred tax liability on obtaining significant influence, it will recognise its share of the tax expense without a corresponding gain on the disposal of the asset. Under the ED's proposal, the investor would derecognise the deferred tax liability instead of recognising the associate's tax expense, and there wouldn't be a P&L mismatch.~~

¹⁴ ~~These stakeholders consider the unit of account for an associate to be the investment as a whole (IAS 28.10) and, therefore, that the deferred tax and IAS 12 ought to only apply on acquisition if the tax base and the cost of investment differ (i.e. as defined by paragraph 5 of IAS 12). As per this view, there should not be any deferred tax recognition arising from the purchase price allocation (PPA) allocation on obtaining significant influence. Moreover, it could be argued that unlike assets and liabilities of a subsidiary, which are recognised in an entity's consolidated financial statements, the individual assets and liabilities of an associate are not recognised in the investor's financial statements. Therefore, an entity does not identify temporary differences arising from the fair value adjustments of the associate's assets and liabilities.~~

~~throughout the life of an investment when the deferred taxes are reversed. Other stakeholders have questioned the appropriateness of applying the proposals when the associate or joint venture does not meet the definition of a business.~~

~~28 Due to the mixed views expressed by stakeholders on this matter, via a question to constituents, EFRAG is assessing current practices in the treatment of deferred tax effects.~~

~~EFRAG's questions to constituents – Measurement of cost of an associate or joint venture~~

~~1.1 Should transaction costs incurred during the acquisition of an associate or joint venture be included in the cost of the investment and capitalised, or expensed as incurred? Please provide reasons for your preference and describe any practical implications.~~

~~1.2 As outlined in paragraphs to , some stakeholders are concerned about a) the proposed recognition of goodwill upon obtaining significant influence and for each subsequent layer of ownership interest acquired (addressed in Question 2 of the ED); and b) the ED's proposal to not offset bargain purchase gains with previously recognised goodwill. Do you agree with these concerns? Please explain.~~

~~1.3 As described in paragraphs to , EFRAG has received mixed views on the proposed inclusion of deferred tax effects in the carrying amount of investment. Do you agree or disagree with the proposed inclusion of deferred tax effects in the carrying amount of all equity-method accounted investments? Based on your experience, is the proposed treatment of including deferred tax effects in the carrying amount of the investment common in practice? Please explain.~~

Question 2 – Changes in an investor's ownership interest while retaining significant influence

Notes to constituents – Summary of proposals in the ED

~~29 IAS 28 does not specify how an investor or joint venturer is required to account for the purchase of an additional interest, for the disposal of a portion of its investment or for other changes of its ownership interest in an associate or joint venture while retaining significant influence, leading to diversity in practice.~~

Purchase of an additional ownership interest

~~30 The IASB decided to propose requiring the investor or joint venturer, at the date of purchase:~~

~~a) to recognise that additional ownership interest and measure it at the fair value of the consideration transferred;~~

~~b) to include in the carrying amount of that additional ownership interest the investor's or joint venturer's share of the fair value of the associate's or joint venture's identifiable assets and liabilities; and~~

~~c) to account for any difference between (a) and (b) either as goodwill included as part of the carrying amount of the investment or as a gain from a bargain purchase in profit or loss.~~

~~31 The IASB decided to use an approach that would result in the investor or joint venturer measuring its additional interests in an associate or joint venture after obtaining significant influence as an accumulation of purchases, so the investor or joint venturer would not remeasure the carrying amount of its previously held interest in its associate or joint venture, because:~~

~~a) in this circumstance, the purchase of an additional interest would not change the relationship between an investor and an investee, or the accounting method an investor applies;~~

~~b) the proposed approach is consistent with the requirements in IFRS 11 where a joint operator purchasing an additional interest in a joint operation does not remeasure its previously held interest;~~

~~c) remeasuring the previously held interest when purchasing an additional interest would result in intermittent revaluation of an investment which would not provide useful information to users.~~

~~32 In requiring including in the carrying amount of the additional ownership interest the investor's or joint venturer's share of the fair value of the associate's or joint venture's net assets, the IASB considered that:~~

~~a) measuring the acquiree's identifiable assets and liabilities at fair value provides relevant information;~~

~~b) the proposed approach is consistent with the requirements of IFRS 11 when an entity acquires an interest in a joint operation which is a business (IFRS 11 requires to apply the principles of IFRS 3 that do not conflict with IFRS 11);~~

~~c) any additional goodwill included in the investment would be faithfully represented because it would be measured in the same way as the initial goodwill.~~

~~33 Since the purchase of an additional ownership interest is treated as an accumulation of purchases measured separately and does not result in a remeasurement of previously held~~

~~interest, the IASB decided that it would be appropriate to treat each acquired layer as a separate unit of account and thus do not require an investor or joint venturer's to offset a bargain purchase gain against previously identified goodwill, but to recognise it in profit or loss.~~

Disposal of an ownership interest

~~34—The IASB decided to propose requiring the investor or joint venturer at the date of the disposal:~~

- ~~a) to derecognise the disposed portion of its investment in the associate or joint venture;~~
- ~~b) to measure the disposed portion of its investment as a percentage of the carrying amount of the investment (that percentage is calculated as the disposed ownership interest divided by the total ownership interest); and~~
- ~~c) to recognise any difference between the consideration received and the disposed portion as a gain or loss in profit or loss.~~

~~35—When developing the proposal, the IASB considered whether the derecognition requirements should mirror the principle of accumulation of purchases outlined above. If an investment is considered as comprising multiple components, an investor or joint venturer would need to determine which layers of the investment to derecognise in a partial disposal. Possible approaches considered by the IASB included specific identification method or the use of cost formula, such as FIFO, LIFO or weighted average.~~

~~36—However, the IASB noted that viewing the investment as a single unit of account would be more consistent with the principles underlying IAS 28 and would:~~

- ~~a) provide a more faithful representation of an investment that comprises instruments with the same economic rights, because each instrument is fungible;~~
- ~~b) reflect that an investment in an associate or joint venture is usually managed as a single asset;~~
- ~~c) be more understandable (for example, the measurement of the amount derecognised in a partial disposal would be easier to understand); and~~
- ~~d) be less complex and, therefore, less costly for entities to apply.~~

Other changes in the investor's ownership interest

~~37—The IASB considered the situations in which the associate or joint venture issues or redeems its shares changing the investor's or joint venturer's ownership interest with or without its participation in said issuance or redemption of shares.~~

~~38—The IASB decided to propose requiring an investor or joint venturer that retains significant influence to:~~

- ~~a) recognise an increase in its ownership interest, as if purchasing an additional ownership interest; and~~
- ~~b) recognise a decrease in its ownership interest, as if disposing of an ownership interest.~~

~~39—In reaching this decision, the IASB considered paragraph 1.12 of the Conceptual Framework stating that general purpose financial statements provide information about the effects of transactions and other events that change a reporting entity's economic resources and claims. In IASB's view, changes to an investor's or joint venturer's ownership interest is an event that changes the investor's or joint venturer's economic resources. Further, the proposed approach would be consistent with the definition of the equity method, which states that the investment is adjusted for the post-acquisition change in the investor's or joint venturer's share of the investee's net assets.~~

~~40—The IASB also considered whether to require an investor or joint venturer to present the gain or loss associated with a dilution in profit or loss or in other comprehensive income, noting that in principle all items of income and expense are to be presented in the statement of profit or loss and that the IASB did not identify any reason to require an investor or joint venturer to present the dilution gain or loss in other comprehensive income instead of in profit or loss.~~

~~41—As outlined in paragraphs BC45 and BC46 of the Basis for Conclusions, the IASB decided not to address application questions related to equity-settled share-based payments and share warrants because "in practice, there are many types of transactions in which entities issue potentially dilutive instruments". The IASB considered that developing requirements to address such transactions when applying the equity method would have been time-consuming and would probably delay the project considerably. Therefore, in the IASB's view, the costs of developing requirements to address these transactions when applying the equity method were likely to outweigh the benefits, as such transactions typically do not have a pervasive or significant effect for investors or joint venturers.~~

ED Question 2- Change in ownership

IAS 28 does not include requirements on how an investor accounts for changes in its ownership interest in an associate while retaining significant influence, that arise from:

- (a) the purchase of an additional ownership interest in the associate;
- (b) the disposal of an ownership interest (partial disposal) in the associate; or
- (c) other changes in the investor's ownership interest in the associate.

The IASB is proposing to require that an investor:

- (a) at the date of purchasing an additional ownership interest in an associate:
 - (i) recognise that additional ownership interest and measure it at the fair value of the consideration transferred;
 - (ii) include in the carrying amount the investor's additional share of the fair value of the associate's identifiable assets and liabilities; and
 - (iii) account for any difference between (i) and (ii) either as goodwill included as part of the carrying amount of the investment or as a gain from a bargain purchase in profit or loss.
- (b) at the date of disposing of an ownership interest:
 - (i) derecognise the disposed portion of its investment in the associate measured as a percentage of the carrying amount of the investment; and
 - (ii) recognise any difference between the consideration received and the amount of the disposed portion as a gain or loss in profit or loss.
- (c) for other changes in its ownership interest in an associate:
 - (i) recognise an increase in its ownership interest, as if purchasing an additional ownership interest. In (a)(i), 'the fair value of the consideration transferred' shall be read as 'the investor's share of the change in its associate's net assets arising from the associate's redemption of equity instruments'.
 - (ii) recognise a decrease in its ownership interest, as if disposing of an ownership interest. In (b)(ii) 'the consideration received' shall be read as 'the investor's share of the change in its associate's net assets arising from the associate's issue of equity instruments'.

Paragraphs BC20–BC44 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 2 – Change in ownership

General comments

~~42— Paragraphs BC34 and BC35 of the Basis for Conclusions outline that the IASB considered treating the investment as a single unit of account as this would be more consistent with the principles underlying IAS 28 (summarised in Principles B and E in Table 2 of the Basis for Conclusions). Moreover, it would provide a more faithful representation of the underlying economic substance due to the fungibility of the investment, and it would also be more understandable, and less complex and costly to apply. EFRAG agrees with this reasoning.~~

~~43— However, EFRAG notes that different units of account are used across proposals for the treatment of additional purchases versus disposals of ownership interests while retaining significant influence. EFRAG questions whether this may distort the representation of the economics of the investment.~~

Specific comments on the ED proposals for changes in ownership interest while retaining significant influence

Purchase of additional interest while retaining significant influence

~~44— EFRAG understands acknowledges the reason for conceptual reasoning behind the ED's proposal of treating each additional acquired ownership interest while retaining significant influence as a separate unit of account and to not requiring require the remeasurement of the carrying amount of its previously held interest in an associate or joint venture when purchasing an additional interest while retaining significant influence. ~~As outlined in paragraph BC23 of the Basis for Conclusions, this proposal is conceptually justified and is often applied in practice. Moreover, during EFRAG's discussions with stakeholders when the ED proposals were being developed, both preparers and users disagreed with an alternative approach explored and discarded by the IASB entailing the remeasurement of the carrying amount of previously held interest at fair value when an additional ownership interest is purchased. Stakeholders deemed that such an approach would lead to inconsistent and incomparable reporting (i.e. fair value remeasurement of previously held ownership interests only being done by those entities that acquire additional ownership interests while retaining significant influence) and that this could lead to opportunistic acquisitions and earnings management.~~~~

~~4525 However, EFRAG highlights significant concerns expressed by stakeholders, including preparers, about the ED proposals for the measurement of additional purchased ownership interest. Under the proposed requirements, at acquisition, ; and, for each additional layer is treated as a separate unit of account, and the investor's acquired, the investor or joint~~

~~venturer's additional share of the associate's or joint venture's~~ venturer is required to measure at fair value the investee's identifiable assets and liabilities ~~are measured at their fair value~~ at the acquisition date and perform a purchase price allocation- ~~(PPA performed (this accounting treatment is also)~~ recognising ensuing goodwill or bargain purchase gain (referred to as the layered approach in this comment letter). This proposal would result in significant cost and complexity for preparers. For example, getting access to the investee's internal information (i.e. business plans, cash flow projections, customer relationship data, etc.) and obtaining the fair value of net assets of the associate or joint venture at the date of each acquisition of additional ownership interest while retaining significant influence would be challenging for many investor/reporting entities. Inter alia, preparers would expend considerable efforts performing the purchase price allocation exercise and they would also incur additional audit costs.

26 ~~Moreover, EFRAG notes that~~ Though conceptually consistent with the initial measurement of the investment, most stakeholders have significant concerns about the cost of each additional layer and complexity of ownership interest ~~the layered approach. Specifically, with regards to:~~

(a) difficulties in obtaining all needed information when the investor does not control the investee and /or when the investee is a listed company not being measured at a different underlying fair value of the associate's or joint venture's assets and liabilities, therefore able to provide one investor with more information than any other investor. These difficulties will be not be encountered only at initial recognition, but throughout the life of the investment (tracking of the deferred taxes and their reversal, items in other comprehensive income and their recycling etc.);

~~(c)~~(b) significant complexity in applying the equity method on an ongoing basis. For example, IAS 28 requires that the profit or loss, other comprehensive income and net assets taken into account for the equity method should be determined after adjustments are made for uniform accounting policies (i.e. if there are changes in the fair value of the net assets of the same underlying associate or joint venture being considered for different acquired layers, it may be cumbersome for preparers to ascertain and reflect the necessary adjustments in the mentioned fair value of the net assets of the associate or joint venture). Of note, many including changes in the fair value of the net assets). Many preparers have indicated that such adjustments would need to be considered for each individual layer of ownership interest, and this would

necessitate multiple ledgers to account for the different layers of ownership interest held through a reporting entity's holding period of an investment;

(c) application difficulties as an investor would be required to reset to nil any investee's item of other comprehensive income recognised in its financial statements, when the equity method is applied for the first time, and for any subsequent additional layer. Such periodic resets would create major practical difficulties and impair the investor's capacity to identify and track those items;

(d) complexity to the implementation of the requirements in paragraphs 21(b)(ii) and B12-B13 of IFRS 12 *Disclosure of Interests in Other Entities* to disclose summarised financial information on current and non-current assets and liabilities of joint ventures and associates with related fair value step-ups. Applying the layered approach would result in presenting amounts of assets and liabilities arising from a compilation of several values and result in limited usefulness for users;

~~4627~~ Further to the noted cost and complexity concerns, stakeholders question the overall usefulness of a full-fledged PPA for each additional acquired ownership interest while retaining significant influence. They note that the identified goodwill is part of the carrying amount of the investments and it is not recognised as a separate line item on the face of financial statements, and it is therefore ignored by users. Moreover, as highlighted in our response to Question 1, stakeholders consider conducting a PPA to be inappropriate for the acquisition of an asset.

~~47~~ Based on the ~~above paragraphs~~ cost-benefit and complexity concerns, EFRAG recommends that ~~while retaining the concept of treating each acquisition of ownership interest as a separate unit of account and not remeasuring previously held ownership, the the IASB should further assess the cost-benefit balance of the version of the~~ explores simplifying the proposed layered approach ~~proposed in the ED.~~ In addition, ~~the IASB should explore simplified alternative approaches. For example, some~~ this regard, EFRAG notes that many stakeholders have suggested the following two alternatives:

~~28~~ Alternative 1 (Using ~~expressed support for a modified-PPA approach that we sought feedback on. Under this approach, the~~ PPA-related information that was applied while obtaining significant influence): ~~Under this approach, instead of continually gathering updated~~ is the reference point for the measurement of the additional acquired layers of ownership interest while retaining significant influence. Key features of the modified-PPA model are as follows:

~~(a) Initial PPA information from the associate or joint venture in order to perform a PPA for each acquired layer, the:~~ The fair value of assets and liabilities of the investee (associate or joint venture) that was identified when the investor obtained significant influence can be used ~~as a basis for estimating the revised fair value of the net assets of the investee at the date of acquisition of additional ownership interest~~ for any subsequent acquisitions while retaining significant influence.

~~(b) Subsequent-period adjustments: These initial fair values of assets and liabilities need to be adjusted for depreciation, amortisation, impairment and other changes. For instance, it can be adjusted to reflect the proportion of the additional ownership interest acquired and with~~ by applying a premium or discount ~~applied~~ for changes in the economic prospects of the investee since the investor obtained significant influence.

~~(d)(c)~~ This ~~suggested~~ subsequent-period adjustment of the fair value of the net assets of the investee at the time significant influence was obtained requires judgment and a reasonable estimation basis ~~and may. To alleviate this estimation uncertainty, subsequent-period adjustments can~~ be restricted (for example, with a requirement for updating the PPA after a certain period). ~~This alternative PPA-determination approach will reduce the mentioned cost and burden concerns.~~

~~4829~~ This ~~The suggested modified-PPA~~ approach would ~~also~~ be consistent with the principle of IFRS 10.23 that specifies that the transactions with non-controlling interest (NCI) that do not change the accounting method are to be accounted for as equity transactions (i.e., no PPA occurs for the changes in NCI's ownership interests). Similarly, a parent does not record any additional goodwill to reflect its subsequent purchases of additional shares in a subsidiary if there is no change in control.

~~a) — Alternative 2 — No PPA approach. Under this approach, the fair value of the consideration transferred is assumed to be a proxy for the investor's share of the fair value of the assets and liabilities of the associate or joint venture related to the acquired additional interest. In this case, a PPA (with the accompanying recognition of either goodwill in investee carrying amount or bargain purchase gains in profit or loss) is unnecessary. This is because it is assumed that the investor's share of the fair value of net assets related to the acquired additional ownership interest would be equal to the fair value of the consideration transferred by the investor. Similar to Alternative 1 and the ED's version of the layered approach, under Alternative 2, each acquisition would be a separate unit of account. However, unlike Alternative 1 and~~

~~the ED's version of the layered approach, Alternative 2 would deemphasise the equity method being applied similarly to a consolidation approach.~~

~~49 EFRAG has also included a question to constituents in order to gather views on Alternatives 1 and 2 or any other potential alternatives for the measurement of additional ownership interests acquired while retaining significant influence.~~

30 There are other approaches besides the modified-PPA approach that would also be simpler and less costly than the ED's layered approach. However, these other approaches would conceptually differ and be a fundamental departure from the ED's approach. For instance, this would be the case for the cost-accumulation, non-PPA approach¹⁵ that EFRAG sought feedback on and other¹⁶ approaches that stakeholders highlighted. Feedback received by EFRAG also highlighted a) the challenges in subsequent measurement; and b) the need for a rethink of the ED's proposed initial measurement of cost, if a cost-accumulation approach was the alternative to the ED's layered approach.

31 Overall, based on constituents' feedback, EFRAG recommends that the IASB further explores plausible simplifications to the ED's layered approach and it could consider the modified-PPA approach as a starting point. The other alternatives including the cost-accumulation could be considered were the IASB to undertake a fundamental review of the equity method.

Disposing of an ownership interest while retaining significant influence

5032 EFRAG supports the ED proposal for an entity to measure the disposed portion of its investment as a percentage of the carrying amount of the investment. EFRAG acknowledges that when taking the decision, the IASB viewed the proposed approach for

¹⁵ EFRAG Draft Comment Letter included **Alternative 2** which is a cost-accumulation, non-PPA approach. Under this approach, the fair value of the consideration transferred is assumed to be a proxy for the fair value of each incremental acquisition. This approach is akin the cost accumulation approach with no required PPA. Similar to modified PPA approach and the ED's version of the layered approach, under the cost-accumulation approach, each acquisition would be a separate unit of account. However, unlike modified PPA and the ED's version of the layered approach, Alternative 2 would deemphasise the IAS 28 requirements being applied similarly to IFRS 3 principle.

¹⁶ One constituent suggested that the IASB consider the approach where goodwill is determined as the difference between the consideration transferred and the current book value of the net assets at the time of the additional purchase.

accounting for disposals of ownership interests as more understandable and less complex, and EFRAG agrees with this statement.

33 However, EFRAG notes that different units of account are used across the ED's proposals for the treatment of additional purchases of ownership interests while retaining significant influence versus those for the disposals of ownership interests while retaining significant influence. EFRAG questions whether this may distort the representation of the economics of the investment and lead to structuring opportunities, for example, when the acquisition of ownership interests and their subsequent disposal occur within narrow time windows.

51 Further, stakeholders have provided examples of where a specific identification method would be more appropriate and simpler to apply. For instance, this would be the case if individual entities A, B and C are part of a consolidated group ABC and each of these individual entities obtains a proportion of ownership interest in entity X and, in the ABC consolidated financial statements, investee X is accounted for using the equity method. In case one of the entities disposes of its ownership interest, a specific identification method could more faithfully represent the economic consequences of the disposal and be less complex than the derecognition of a portion of the investments of the other entities within the group.

~~5234~~ A specific identification method may also be appropriate in the following cases: a) Similar considerations may be relevant where ownership interests in the associate or joint venture are related to different classes of ordinary shares; ~~or b) when the acquisition and disposal happen within a short time period.~~ Overall, EFRAG considers there are situations where the specific identification method would better reflect the economics of the disposal.

35 Whereas EFRAG understands and shares the concerns expressed by the stakeholders outlined above asking for allowing or requiring, in certain circumstances, a specific identification method, EFRAG also acknowledges that the specific identification would potentially reduce comparability between entities, create structuring opportunities and it would contradict a consolidation view that assumes the group is a single economic entity.

36 Further, EFRAG suggests the IASB clarify how the share of the net assets disposed of is determined, making paragraph 32(b) of the ED more explicit and providing more guidance in BC35(a) with relation to the equity instruments with different economic rights (i.e. preference shares).

Other changes in ownership interest while retaining significant influence

~~5337~~ EFRAG is aware that ~~some~~many stakeholders are concerned with the ED proposal on other changes in ownership that occur in the absence of an exchange transaction (e.g. an associate's or joint venture's issuance or redemption of its shares). Under the ED proposals, these other changes in ownership are deemed to be equivalent to a) the purchase of additional ownership interests while retaining significant influence (deemed purchases), and b) the disposal of ownership interests while retaining significant influence (deemed disposals). Reasons provided for disagreeing with the ED proposals include:

~~(a) Stakeholders are concerned about applying the ED proposals in the absence of other changes without~~ an exchange transaction ~~between the investor and~~ not economically equivalent to actual acquisitions and ~~the associate or joint venture~~. They consider the ~~changed disposals~~ of ownership interest ~~(via dilution or anti-dilution of the proportion of the investor's holdings) to~~ be a 'mechanical' adjustment that will be costly adjustments.

~~(e)~~(b) requirement to perform a separate PPA for each deemed acquisition is overly burdensome and costly with limited benefits (as outlined in response to acquiring additional ownership interest). This concern is particularly acute for entities whose associates or joint ventures have high volumes of share buybacks for example.

~~54~~ In addition, some stakeholders noted that it was not clear from the ED whether an investor or joint venturer needs to consider only the changes at the level of its direct associate or joint venture or also the changes that its associate or joint venture may have within their group. Similarly, stakeholders questioned if the ED proposals are also to be applied towards other types of events like the issuance of hybrid instruments that may impact the expected dividends but not the investor's ownership interests, including voting rights. Moreover, as noted earlier, applying the version of the layered approach proposed in the ED for acquired additional ownership interests while retaining significant influence is complex, costly and of questionable usefulness. Extending the ED's layered approach to deemed purchases increases the overall complexity and lessens the usefulness of the ED proposals for other changes in ownership.

~~5538~~ EFRAG notes that, as stated in BC 46 in the Basis for Conclusions, due to the associated complexity the IASB did not develop proposals for a change of ownership arising from equity-settled share-based payments and share warrants. Similar reasoning ought to have been applied towards the ED's proposals for deemed purchases and disposals.

~~5639~~ Hence, EFRAG recommends that ~~unless~~ the IASB ~~can~~ develop a simpler and a more balanced approach for layered acquisitions from a cost/benefit perspective along with a holistic principle-based approach that encompasses all non-exchange transactions and events within an investee (associate or joint venture) that result in changes in ownership and/or the investor's claims on the investee's resources. ~~Unless the IASB can do so, then~~ all such transactions and events should be scoped out of the amendments to IAS 28.

~~40~~ #A transitional scoping out of these other changes in ownership interests may fail to remedy existing diversity in practice but it will certainly not worsen it. Plus, the IASB has in any case considered that existing diversity is acceptable for the other changes in ownership transactions that were not in the scope of the ED.

~~41~~ Were the IASB to retain the proposal, based on the feedback received, EFRAG points to the following areas not addressed in the ED where further clarifications would be required:

(a) whether an investor or joint venturer needs to consider only the changes at the level of its direct associate or joint venture or also the changes that its associate or joint venture may have within their group and is meant to capture the broader term of 'economic ownership';

(b) whether and how to apply the ED proposals in situations where an investee's net asset changes as a result of a transaction with non-controlling interests within the investee or share buy-backs (in situations where the investee is a consolidated group by itself);

(c) if the ED proposals are retained, some stakeholders have suggested that the IASB clarify that the requirements of ~~also~~ to be applied towards other types of events like the issuance of hybrid instruments that may impact the expected dividends but not the investor's ownership interests, including voting rights;

(d) the calculation of the investee's net assets. The absence of this may lead to confusion and diversity in practice; and

~~(f)~~(e) with regard to the decrease in relative ownership interest, whether such changes should result in a realisation of any accumulate currency translation adjustment (CTA) and that IFRS 5 ~~Non-Current~~current Assets Held for Sale and Discontinued Operations would not be applicable for deemed disposals. These stakeholders construe that an investor's sale/disposal of its ownership interests would be in the scope of ~~should not~~ apply in such cases, because the application of IFRS 5 ~~but a non-exchange change in ownership interest/ deemed disposal would not.~~ would require an actual sale of interests in the investee.

Question 3 – Recognition of the investor’s share of losses

EFRAG question to constituents – change in ownership while retaining significant influence

2.1. Question 3- Recognition of investor’s share of losses

Paragraph ~~lays out alternatives to~~ 38 of IAS 28 requires that if an investor’s share of losses equals or exceeds its interest in the ED’s proposal ~~associate, the investor discontinues recognising its share of further losses. However, IAS 28 does not include requirements on whether an investor that has reduced the carrying amount of its investment in an associate to nil:~~

(a) on purchasing an additional ownership interest, recognises any losses not recognised as a ‘catch up’ adjustment by deducting those losses from the cost of the additional ownership interest; or

(b) recognises separately its share of each component of the associate’s comprehensive income.

The IASB is proposing an investor:

(a) on purchasing an additional ownership interest, not recognise its share of an associate’s losses that it has not recognised by reducing the carrying amount of the additional ownership interest.

(b) recognise and present separately its share of the associate’s profit or loss and its share of the associate’s other comprehensive income.

Paragraphs BC47–BC62 of the Basis for accounting ~~Conclusions explain the IASB’s rationale for purchases of additional ownership interest. Considering the complexity and cost, do these proposals.~~

Do you agree with the these proposals?

If you disagree, please explain why you disagree and your suggested alternative measurement methods when accounting for purchases of an additional ownership interest while retaining significant influence?–.

Question 3 – Recognition of the investor’s share of losses

Notes to constituents – Summary of proposals in the ED

Losses not recognised and purchase of an additional interest

57—IAS 28 does not specify if an investor or joint venturer that has reduced its investment in an associate or joint venture to nil is required to ‘catch up’ unrecognised losses if it purchases

~~an additional interest in an associate or joint venture. The IASB decided to propose that an investor or joint venturer would not deduct its share of any losses not recognised from the cost of the additional ownership interest. In reaching its decision, the IASB considered that this approach would be consistent with its proposed approach to the purchase of an additional ownership interest measured as an accumulation of purchases, each independent of another. An investor or joint venturer would, therefore, not remeasure the previously held interest in an associate or joint venture when recognising the additional interest. In the IASB's view, requiring an investor or joint venturer to deduct any losses not recognised relating to the previously held interest from the cost of an additional interest would be inconsistent with its proposed approach to the purchase of the additional interest.~~

~~58—Further, in IASB's view, this approach would faithfully represent the purchase of the additional interest, because deducting the investor's or joint venturer's share of losses not recognised from the cost of the additional investment could imply that the investment is impaired. However, the IASB noted that the presence of unrecognised losses does not necessarily mean the investment is impaired. If an impairment exists, an investor or joint venturer would be required to apply the requirements in IAS 28 and IAS 36 Impairment of Assets. Recognition of an impairment loss immediately following the recognition of a purchase of an additional interest in the associate or joint ventures would provide relevant information to users of the investor's or joint venturer's financial statements. That information might include, for example, an explanation of the investor's or joint venturer's rationale for investing additional funds in the associate or joint venture.~~

~~Recognition of each component of comprehensive income~~

~~59—IFRS 18 (and its predecessor, IAS 1 Presentation of Financial Statements) requires an investor or joint venturer to present:~~

- ~~a) its share of the profit or loss from associates or joint ventures accounted for using the equity method in the statement of profit or loss; and~~
- ~~b) its share of other comprehensive income of associates or joint ventures accounted for using the equity method in other comprehensive income.~~

~~60—An associate or joint venture might report a loss in its statement of profit or loss and a loss in its other comprehensive income. If the investor's or joint venturer's share of those losses, in total, exceeds the carrying amount of its investment, an application question arises about the amount of losses it should recognise in profit or loss and in other comprehensive income. Various approaches are applied in practice. For example, an investor or joint venturer might recognise its share of the associate's or joint venture's total losses in profit or loss and other~~

~~comprehensive income proportionately—or it might first recognise the full amount of its share of the associate's or joint venture's loss in profit or loss and then recognise the remaining balance of its share of the associate's or joint venture's total losses in other comprehensive income.~~

~~61—Another application question arises once the investor or joint venturer has reduced the carrying amount of its investment to nil and an associate or joint venture subsequently reports a loss in its statement of profit or loss and income in its other comprehensive income (or vice versa). In this situation, the question arises as to whether the investor or joint venturer should recognise any amounts for its share of the associate's or joint venture's loss (or profit) and other comprehensive income.~~

~~62—The IASB decided to propose requiring an investor or joint venturer to recognise its share of an associate's or joint venture's total comprehensive income (which, therefore, would include a loss reported in an associate's or joint venture's other comprehensive income) until the investor's or joint venturer's investment in the associate or joint venture is reduced to nil.~~

~~63—The IASB also decided to propose requiring the investor or joint venturer to recognise separately its share of the associate's or joint venture's profit or loss and its share of the associate's or joint venture's other comprehensive income. Furthermore:~~

~~a)—if the investor's or joint venturer's share of profit or loss and its share of other comprehensive income are both losses that in aggregate equal or exceed its net investment in the associate or joint venture, an investor or joint venturer would first recognise its share of profit or loss and then its share of other comprehensive income.~~

~~b)—after an investor or joint venturer has reduced its investment to nil, it would continue to recognise separately its share of profit or loss and its share of other comprehensive income. For example, if an investor's share of profit or loss is a loss of CU250 and its share of other comprehensive income is a profit of CU100, the investor would recognise a loss of CU100 in profit or loss and a profit of CU100 in other comprehensive income. The carrying amount of the investor's investment would remain at nil.~~

~~64—The IASB decided not to develop proposed answers for other related application questions, such as the order of recognising profits in profit or loss and in other comprehensive income when an investor or joint venturer resumes recognising its share of the associate's or joint~~

~~venture's profits. Those questions do not commonly arise in practice and, therefore, were not on the list of application questions selected for the project.~~

~~Question 3 – Recognition of investor's share of losses~~

~~Paragraph 38 of IAS 28 requires that if an investor's share of losses equals or exceeds its interest in the associate, the investor discontinues recognising its share of further losses. However, IAS 28 does not include requirements on whether an investor that has reduced the carrying amount of its investment in an associate to nil:~~

~~(a) on purchasing an additional ownership interest, recognises any losses not recognised as a 'catch up' adjustment by deducting those losses from the cost of the additional ownership interest; or~~

~~(b) recognises separately its share of each component of the associate's comprehensive income.~~

~~The IASB is proposing an investor:~~

~~(a) on purchasing an additional ownership interest, not recognise its share of an associate's losses that it has not recognised by reducing the carrying amount of the additional ownership interest.~~

~~(b) recognise and present separately its share of the associate's profit or loss and its share of the associate's other comprehensive income.~~

~~Paragraphs BC47–BC62 of the Basis for Conclusions explain the IASB's rationale for these proposals.~~

~~Do you agree with these proposals?~~

~~If you disagree, please explain why you disagree and your suggested alternative.~~

EFRAG's response to Question 3: Recognition of investor's share of losses

Losses not recognised and purchase of an additional interest

6542 EFRAG acknowledges and does not disagree with the reasons underpinning the ED proposal not to offset losses of previously held ownership interest against the carrying amount of an additional ownership interest acquired (while retaining significant influence). That is, the latter is a separate and different unit of account from the former. Moreover, as noted in paragraph BC 53 of the Basis for Conclusions, the losses of an associate or joint venture are not necessarily an indicator of the impairment of the investment (e.g. it could be a tech

start-up facing early-stage startup losses but albeit having ~~easy~~favourable long-term economic prospects).

~~6643~~ However, in line with our concerns raised in QuestionsQuestion 1 and 2based on most of the feedback received, EFRAG considers that the recognition of additional goodwill in situations where the net assets of an investee are already negative would be inappropriate. Giving primacy toEmphasising the application of a consistentseparate unit of account in this instance even when it may distort the faithful representation of economic reality seems to be unjustified. Moreover, the relevance and faithful representation of reported information should beand lead to structuring opportunities. Furthermore, EFRAG notes that the feedback from users of financial statements indicates they already struggle with interpreting the topmost consideration for reporting requirementseconomic meaning of goodwill recognised under the equity method. This limited usefulness will be exacerbated if goodwill is recognised in circumstances where the carrying amount of the investment is nil. Hence, in addition to the ED proposals, EFRAG recommends that the IASB also prohibit the recognition of additional goodwill when the carrying amount of the investment is nil due to the share of investee's losses.

~~67~~ Moreover, not recognising the investor's share of losses when the carrying amount of the investment is reduced to nil as proposed by the ED is aligned with the view of the equity method as a measurement basis (i.e. the entire investment is viewed as a single unit of account) rather than as a consolidation approach. The emphasis on the acquired ownership interest as a separate unit of account from previously held interest is more aligned with the view of the equity method as a consolidation approach. There is conceptual inconsistency in this regard.

~~6844~~ Finally, ifl the IASB proceeds with the current proposal, EFRAG suggests that the IASB explicitly state that when an entity purchases an additional ownership interest while having unrecognised losses, an entity needs to assess if this additional investment represents an implicit funding of the associate or the joint venture and whether this is indicative that a constructive obligation has been created. If that were to be the case, the unrecognised losses need to be recognised in line with the requirement of paragraph 47 of the ED.

45 Finally, EFRAG asks the IASB to clarify:

(a) whether the original and new interests should be tracked separately, and how they should be accounted for going forward;

(b) how the composition of the associate's carrying amount should be seen in the case net assets are negative. Would the carrying amount of the associate be seen in total as goodwill, or will the goodwill be higher and offset by the negative asset value?

Recognition of each component of comprehensive income

~~6946~~ EFRAG supports the ED proposal that when an investor has reduced the carrying amount of its investment in an associate to nil, the investor shall recognise and present separately its share of the associate's profit or loss and its share of the associate's other comprehensive income. However, based on the feedback received so far, there is a need for further clarification of aspects of this proposal.

~~70~~—Specifically, with respect to paragraph 48 of the ED ~~states: "subsequently, if an investor's or joint venturer's share of an associate's or joint venture's total comprehensive income is a profit¹⁷, the investor or joint venturer shall resume recognising its share of that profit only when that share exceeds its share of losses not recognised."~~ At the same time, paragraph 50 of the ED ~~states: "the investor or joint venturer shall recognise separately its share of the associate's or joint venture's profit or loss and its share of the associate's or joint venture's other comprehensive income"~~. Therefore, stakeholders have called for clarification on IASB should clarify whether the investor's share of unrecognised losses are

47 to be considered-:

- (a) separately for the respective profit or loss and other comprehensive income portions and whether the corresponding resumed recognition of share of profit in total comprehensive income (i.e. in excess of the unrecognised losses) is to then be similarly recognised separately for profit or loss and other comprehensive income; or
- (b) ~~to be considered~~ in their entirety at the level of total comprehensive income without differentiating the amounts respectively arising from profit or loss and other comprehensive income.

~~7148~~ Further, paragraph 52 of the ED ~~states: "an investor or joint venturer that has reduced its net investment to nil shall continue to recognise separately its share of an associate's or~~

¹⁷ "subsequently, if an investor's or joint venturer's share of an associate's or joint venture's total comprehensive income is a profit, the investor or joint venturer shall resume recognising its share of that profit only when that share exceeds its share of losses not recognised." At the same time, paragraph 50 of the ED states: "the investor or joint venturer shall recognise separately its share of the associate's or joint venture's profit or loss and its share of the associate's or joint venture's other comprehensive income."

~~joint venture's profit or loss and its share of an associate's or joint venture's other comprehensive income, retaining a carrying amount in the net investment of nil". It is not clear if this requirement~~ Further, whether paragraph 52 of the ED¹⁸ shall also be applied when an investor or joint venturer has an accumulation of unrecognised losses across the total comprehensive income (i.e. profit or loss amount and other comprehensive amount taken collectively). ~~Stakeholders suggested~~ Based on feedback received, EFRAG suggests that the example included in paragraph 52 be extended to ~~the~~ include situations where ~~an investor's or joint venturer's share of profit or loss is a profit and its share of other comprehensive income is a loss and to clarify how the application of the ED proposals considering the primacy of the statement of profit or loss.:~~

- (a) an investor's or joint venturer's share of profit or loss is a profit and its share of other comprehensive income is a loss;
- (b) the net investment is not reduced to nil;
- (c) the investor's share in total comprehensive income is a loss that exceeds the net investment in the associate; and
- (d) the investor's share in profit or loss is a loss and its share of the other comprehensive income is a profit (or vice versa).

~~7249~~ With regard to other comprehensive income, ~~stakeholders raised concerns that~~ the ED proposal does not address how and whether to allocate an investor's or joint venturer's share of its associate's or joint venture's other comprehensive income through various components of the other comprehensive income.

50 Moreover, EFRAG is unconvinced by the IASB's arguments expressed in paragraph BC62 of the Basis for Conclusions for being silent and not developing answers for the order of recognising profits in profit or loss and in other comprehensive income when an investor or joint venturer resumes recognising its share of the associate's or of the joint venture's profits. ~~The IASB argues~~ (such as what is the order of priority between recyclable and non-recyclable components of other comprehensive income or to allocate on a proportionate basis between all components of other comprehensive income and how the history of prior

¹⁸ "an investor or joint venturer that has reduced its net investment to nil shall continue to recognise separately its share of an associate's or joint venture's profit or loss and its share of an associate's or joint venture's other comprehensive income, retaining a carrying amount in the net investment of nil."

unrecognised losses be considered when determining the accounting for the comprehensive income of the period).

~~7351~~ Notwithstanding, the IASB's argument that ~~thesethe above~~ situations are rare in practice and were not in the application questions, EFRAG considers that the treatment of profit or loss versus OCI is a conceptual question that ought to be addressed ~~by the IASB~~ via reference to the Conceptual Framework principles and it should not be dependent on the pervasiveness of arising situations. In this sense, accounting standard-setting should cater for both losses and gains in the recovery of losses and not only provide asymmetrical answers. In addition, feedback obtained by EFRAG indicates that the matter is considered significant and pervasive by many stakeholders.

Question 4 – Transactions with associates and joint ventures

~~Notes to constituents – Summary of proposals in the ED~~

~~74— The IASB is proposing to change the requirements in IAS 28 and require that an investor or joint venturer recognise in full gains and losses resulting from all transactions with associates or joint ventures. This includes 'upstream' transactions (such as a sale of assets from an associate or joint venture to an investor or joint venturer) and 'downstream' transactions (such as a sale or contribution of assets from an investor or joint venturer to an associate or joint venture) including the sale of a subsidiary to its associate or joint venture resulting in the loss of control of a subsidiary.~~

~~75— Currently, paragraph 28 of IAS 28 requires an investor to recognise gains and losses resulting from transactions with an associate or a joint venture only to the extent of unrelated investors' interests in the associate or joint venture. For example, if an investor owns 25% of an associate and sells an asset to that associate, the investor recognises 75% of the gain at the date of the sale (the third parties share), and the remaining 25% over the asset's life or when the asset is sold to third parties. This requirement in IAS 28 for partial recognition of gains and losses on a sale of a subsidiary to an associate or joint venture is different to the requirement in IFRS 10 to recognise in full the gain or loss on losing control of a subsidiary. IAS 28 does not provide specific guidance on transactions between equity-accounted investees and whether unrealised profit or losses on such transactions should be eliminated.~~

~~76— The proposed amendment addresses the application questions on the accounting for transactions with associates or joint ventures that are listed in Table 1 of paragraph BC13~~

~~of the Basis for Conclusions of the ED. Some of the application questions arose because of the inconsistency with IFRS 10.~~

~~77—The IASB is proposing that an investor or joint venturer disclose the amount of gains or losses from ‘downstream’ transactions (sales from an investor to its associates or joint ventures). See question 7 on disclosure requirements.~~

~~78—As explained in paragraph B67 of the Basis for Conclusions, in reaching its decision on transactions with associates or joint venturers the IASB considered the following alternatives:~~

~~e)—Alternative 1—Apply the approach in IFRS 10 and recognise in full the gains and losses on all transactions with an associate and a joint venturer.~~

~~d)—Alternative 2—Apply the approach in IFRS 10 first, and then an overlay using the approach in current IAS 28 and recognise only partial gains and losses on all transactions with an associate and a joint venture.~~

~~e)—Alternative 3—Apply the approach in current IAS 28 (partial gain or loss) or IFRS 10 (full gain or loss), depending on whether the transaction involved the transfer of an output of the entity’s ordinary activities (i.e. whether this transaction is within the scope of IFRS 15 Revenue from Contracts with Customers or not). This approach would require partial gains or losses on transactions in the scope of IFRS 15 and full gains or losses if outside the scope of IFRS 15.~~

~~f)—Alternative 4—Under this approach the investor would recognise the full gains or losses when a transaction constitutes a business and partial gains or losses when a transaction constitutes an asset.~~

~~79—The IASB noted that unlike a subsidiary, an associate or a joint venture is not part of the group and is not controlled by the parent. A group’s investment in an associate or joint venture is considered more like an asset of the group. It is therefore questionable why IAS 28 restricts gains or losses and requires the elimination of the “unrealised” gain or loss. When an entity sells an item of property, plant and equipment, IAS 16 Property Plant and Equipment requires the entity to recognise the full gain or loss on disposal of the asset. This is in line with Alternative 1. Alternative 2 would continue to require the recognition of partial gains and losses.~~

~~80—The IASB considered that Alternatives 3 and 4 would be complex to apply as they would require judgement to determine which requirements to apply and also raised conceptual questions. For instance, the IASB notes that Alternative 4 could be perceived as inconsistent~~

~~with the IASB's views in developing IFRS 10 that the loss of control of a subsidiary is, from the group's perspective, the loss of control over some of the group's individual assets and liabilities. Therefore, drawing a line for different requirements between the sale of an asset and the sale of a business would be difficult to justify.~~

~~81—After considering user information needs, practical application to preparers and conceptual reasoning as to why it is not conceptually justified why an investor or joint venturer should eliminate its portion of the gain or loss in a transaction with an associate or joint venture (as these investments are not part of the group entity), the IASB considered Alternative 1 as the best alternative.~~

~~Contribution of non-monetary assets in exchange for equity interest~~

~~82—The IASB decided to combine paragraphs 30 and 31 of current IAS 28 into a single paragraph as proposed in paragraph 54 of the ED. The IASB did not change the existing requirements except for the effects of paragraph 53 of the ED on full recognition of gains and losses on “downstream” and “upstream transactions”. Specifically, paragraph 54 of the ED says:~~

- ~~a) —If an investor or joint venturer contributes non-monetary assets to an associate or joint venture in exchange for an equity interest in that associate or joint venture, and that contribution lacks ‘commercial substance’ as described in IAS 16 Property, Plant and Equipment, the investor or joint venturer shall regard the gain or loss on that contribution as unrealised and eliminate it against the carrying amount of the investment.~~
- ~~b) —If, in addition to receiving an equity interest in the associate or joint venture, an investor or joint venturer receives monetary or non-monetary assets, the investor or joint venturer shall recognise in full in profit or loss the portion of the gain or loss on the non-monetary contribution relating to the monetary and non-monetary assets received.~~

Question 4- Transactions with associates and joint ventures

Paragraph 28 of IAS 28 requires an investor to recognise gains and losses resulting from transactions between itself and an associate only to the extent of unrelated investors' interests in the associate. This requirement applies to both 'downstream' transactions (such as a sale or contribution of assets from an investor to an associate) and 'upstream' transactions (such as a sale of assets from an associate to an investor).

If an investor loses control of a subsidiary in a transaction with an associate, the requirement in IAS 28 to recognise only a portion of the gains or losses is inconsistent with the requirement in IFRS 10 to recognise in full the gain or loss on losing control of a subsidiary.

The IASB is proposing to require that an investor recognise in full gains and losses resulting from all 'upstream' and 'downstream' transactions with its associates, including transactions involving the loss of control of a subsidiary.

Paragraphs BC63–BC84 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 4: Transactions with associates and joint ventures

General comments

8352 EFRAG supports the ED's proposal to require that an investor recognises the full gains or losses from its 'upstream' and 'downstream' transactions with its associates and joint ventures. The proposal is a significant change to the existing requirement in IAS 28 to recognise gains or losses to the extent of unrelated investors' interests in the associate (for instance, an investor with a 25% ownership interest recognises 75% of gains or losses) and it eliminates the conflict between IFRS 10 and IAS 28 on the accounting for the sale/contribution of a subsidiary to its associate or joint venture.

8453 The ED's proposal is consistent with the IFRS 10, which requires the full gain or loss to be recognised on the sale or contribution of a subsidiary (loss of control of a subsidiary). Similarly, when an entity sells an item of property, plant or equipment, IAS 16 requires the full gain or loss on disposal of the asset.

8554 ~~Overall, though there are concerns about possible structuring opportunities, especially for joint ventures and downstream transactions that have been raised by stakeholders (as further described in the paragraphs below),~~ Overall, EFRAG considers that the proposal will result in a desirable consistency in the application of the equity method for all transactions with associates or joint ventures. It is also a simplified and less costly solution compared to the other alternatives considered by the IASB that are summarised in paragraph B67 of the ED's Basis for Conclusions. ~~Moreover, as described below and in Question 7, the proposed disclosures for downstream transactions can alleviate concerns about structuring opportunities.~~

55 [However, EFRAG notes that some stakeholders expressed concerns about restructuring opportunities and earnings management particularly for transactions between associates and joint ventures under common control. As discussed in more detail below \(also see our response to Question 7\), EFRAG recommends enhanced disclosures to improve the transparency and information content to users on gains and losses recognised on transactions with equity-accounted investments.](#)

56 [Furthermore, EFRAG notes that the ED does not refer to or discuss side stream transactions and whether they are covered by the scope of the proposals. We understand side stream transactions to be transactions between associates, joint ventures and/or between subsidiaries of a parent entity. EFRAG therefore recommends that the IASB clarify whether side stream transactions are within the scope of the proposal and if so, we recommend that disclosure of any gains or losses arising from such transactions be required. \(See our response to Question 7\).](#)

Specific comments on the ED proposal

Reasons for supporting proposed recognition of full gains or losses

[8657](#) EFRAG notes that an associate or joint venture is not controlled by the parent entity and is therefore not part of the reporting boundary for consolidated financial statements under IFRS 10. EFRAG therefore agrees with the IASB's reasoning set out in paragraphs BC76 – BC80 of the Basis for Conclusions of the ED that elimination of gains or losses on transactions with associates or joint ventures should not be required.

[8758](#) EFRAG also agrees with the arguments in BC75(b) of the Basis for Conclusions that the proposal will reduce costs for preparers as an entity will no longer need to gather the required information to perform the elimination entries and track the unrecognised gains and losses over future periods.

Concerns about full recognition of gains and losses for transactions with joint ventures

[8859](#) Some stakeholders have raised concerns about requiring an entity to recognise the full gain or loss for transactions with a joint venture because such a requirement could potentially allow a joint venturer to manage its earnings and structure transactions that are not arm's length transactions and these include roundtrip transactions. This concern was [also](#) acknowledged by the IASB and explained in paragraph BC111 of the Basis for Conclusions.

[8960](#) As noted in our response to Question 7, EFRAG considers that disclosing the amount of any gains and losses on 'downstream transactions' will be helpful to users of financial statements as it will help users understand the pricing of such transactions and benchmark it against market terms, whether these are undertaken at arm's length and if there are

structuring activities including roundtrip transactions occurring. [In this light, EFRAG recommends that the IASB further examine how to enhance the disclosure requirements for all transactions between a parent and its equity-accounted investees \(including upstream and side stream transactions\) without duplicating any existing related party disclosures under IAS 24 Related Party Disclosures. This would help to provide transparency on the rationale on the rationale and pricing for these types of related party transactions and provide useful information to users.](#)

~~9061~~ [Given](#) ~~Finally, given~~ that this proposal of the ED is a significant amendment that will result in a change in current practice and that it may elevate earnings management concerns, EFRAG notes that some stakeholders have called for stronger articulation of the principles underlying this particular ED proposal and also raised questions about the clarity and robustness of requirements for transactions that lack commercial substance (see paragraphs below), particularly for transactions with subsidiaries which are equity-accounted in the separate financial statements.

Separate financial statements

~~9162~~ As addressed in EFRAG's response to Question 6, some stakeholders have [raised significant](#) concerns with applying the proposals for subsidiaries (controlled by the investor/parent) accounted for under the equity method in the separate financial statements.

Other comments

~~9263~~ *Transactions that lack commercial substance.* Some stakeholders have expressed that there are difficulties in interpreting paragraph 54, which combines paragraphs 30 and 31 of existing IAS 28 into a single paragraph without changing existing requirements. EFRAG understands that paragraph 54 is consistent with the requirements in IAS 16 on exchanges of non-monetary assets and acts as a safeguard for transactions that lack commercial substance, as described in paragraph 25 of IAS 16. If a transaction lacks commercial substance, then no gain or loss is recognised on the transferred non-monetary asset. However, EFRAG notes that the accounting for gains or losses seems to depend on whether the exchange results in the entity receiving an equity interest or receiving monetary or non-monetary assets. For the sake of clarity of the requirements in paragraph 54 of the ED, EFRAG suggests the IASB provide a related illustrative example. EFRAG notes that, given the proposal for full recognition of gains or losses from transactions with investees, the point on commercial substance is of particular [relevance for transactions with subsidiaries](#) that are equity-accounted in the separate financial statements.

Question 5 – Impairment indicators (decline in fair value)

Notes to constituents – Summary of proposals in the ED

~~93—IAS 28 requires an investor or joint venturer to determine whether there is any objective evidence indicating that its net investment in an associate or joint venture might be impaired. If there is indication of impairment, an investor or joint venturer tests its net investment in an associate or joint venture for impairment in accordance with IAS 36. IAS 28 describe various events that are indications of impairment and states that a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is objective evidence of impairment. An application question arises about whether an investor or joint venturer should assess a decline in the fair value of an investment by comparing that fair value to the carrying amount of the net investment in the associate or joint venture at the reporting date or to the cost of the investment on initial recognition. Approaches applied in practice vary, but it is common for entities to compare the fair value of the investment with its carrying amount at the reporting date.~~

Cost or carrying amount

~~94—The IASB decided to propose replacing ‘cost’ in paragraph 41C of IAS 28 with ‘carrying amount’ to require the investor or joint venturer to compare the fair value of the investment to its carrying amount, not its cost on initial recognition, when determining whether a decline in fair value indicates that an investment in an associate or joint venture might be impaired. In the IASB’s view, this approach is aligned with IAS 36. When applying IAS 36, the investor or joint venturer measures the impairment of an investment in an associate or joint venture by comparing the investment’s recoverable amount with its carrying amount, not its original cost.~~

A significant or prolonged decline in fair value

~~95—When deciding to propose replacing ‘cost’ with ‘carrying amount’, the IASB also decided to propose removing ‘significant or prolonged’ to further align the requirements with IAS 36. If an investor or joint venturer recognises an impairment of an investment in an associate or joint venture, it subsequently recognises a reversal of that impairment loss if the impairment no longer exists or decreases. The IASB therefore considered that the rationale for referring to a ‘significant or prolonged’ decline in fair value did not apply in the context of an investment in an associate or joint venture accounted for using the equity method. The IASB also noted that application difficulties had arisen in the past about how entities assessed whether a decline in the fair value of an available-for-sale equity instrument was significant or prolonged.~~

Additional impairment guidance

~~96— The IASB decided to propose adding further guidance on the impairment requirements in IAS 28 to explain that information about the fair value of an investment might be observed from the price paid to purchase an additional ownership interest in an associate or joint venture or the price received to sell an ownership interest. As such, the IASB noted that a bargain purchase gain might be an indication of impairment.~~

Question 5- Impairment indicators (decline in fair value)

Paragraphs 41A–41C of IAS 28 describe various events that indicate the net investment in an associate could be impaired. Paragraph 41C of IAS 28 states that a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is objective evidence of impairment. One of the application questions asked whether an investor should assess a decline in the fair value of an investment by comparing that fair value to the carrying amount of the net investment in the associate at the reporting date or to the cost of the investment on initial recognition.

The IASB is proposing:

- (a) to replace ‘decline...below cost’ of an investment in paragraph 41C of IAS 28 with ‘decline...to less than its carrying amount’;
- (b) to remove ‘significant or prolonged’ decline in fair value; and
- (c) to add requirements to IAS 28 explaining that information about the fair value of the investment might be observed from the price paid to purchase an additional interest in the associate or received to sell part of the interest, or from a quoted market price for the investment.

The IASB is also proposing to reorganise the requirements in IAS 28 relating to impairment to make them easier to apply, and to align their wording with the requirements in IAS 36 Impairment of Assets.

Paragraphs BC94–BC106 of the Basis for Conclusions explain the IASB’s rationale for these proposals. Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG’s response to Question 5: Impairment indicators (decline in fair value)

~~9764~~ *General comment on the unit of account.* The ED specifies that when performing an impairment test an entity is to consider the carrying amount as a whole and any impairment loss recognised is not allocated to any asset, including goodwill, which forms

part of the carrying amount of the net investment. EFRAG notes that the unit of account of impairment (i.e. entire investment) differs from the unit of account applied for the recognition of goodwill (i.e. each purchased layer while retaining significant influence).

~~9865~~ *Specific comment on the ED proposals.* EFRAG supports the ED proposals related to the impairment of investments in associates or joint ventures. Specifically, EFRAG welcomes the IASB's decision to replace 'cost' with 'carrying amount' in paragraph 41C of the current IAS 28 guidance. Further, EFRAG supports specifying that information about the fair value of an investment might be observed from the price paid to purchase additional ownership interest and adding this clarification as part of the objective evidence within the IAS 28 requirements.

~~9966~~ From the feedback received, EFRAG is supportive albeit aware of mixed views amongst stakeholders on the ED proposal to remove the "significant or prolonged" decline in fair value' criterion. Supporters of this proposal note that it would alleviate application difficulties related to the judgemental assessment of this criterion and thus would reduce diversity in practice.

~~10067~~ On the other hand, some stakeholders noted that this criterion has been useful in practice and its removal would increase the frequency of the impairment tests that an investor or joint venturer would undertake and that this will impose an incremental burden on preparers. These stakeholders have also expressed concerns that more frequent impairment testing due to no longer considering whether there is a significant and prolonged decline in fair value might result in more frequent impairment write-downs and their subsequent reversals. They are concerned that such volatility could lessen the predictive value of reported earnings (earnings quality) for users of financial statements. Relatedly, some users have indicated that rather than relying on the signal of the impairment of equity-accounted investments to gauge the prospects of an associate or joint venture, they rely on their own valuation and other sources of the fair value of the associates or joint ventures (e.g. the financial statements of the associates or joint ventures).

~~10168~~ That said, with regard to the above paragraph, EFRAG observes that under the ED proposal, the impairment would only occur if the recoverable amount (i.e. the higher of value in use and fair value) is less than the carrying amount and the impairment testing would only occur as frequently as done for other assets. As for users' relying on other complementary information while assessing the prospects of associates or joint ventures, EFRAG observes that the equity method is currently deemed to be the relevant accounting method for

associates and joint ventures (i.e. where the investor has significant influence), and impairment only helps to ensure the depiction of a relevant and faithfully representative carrying amount of the associate or joint venture. EFRAG notes that users' reliance on other complementary information (i.e. besides the consolidated financial statements information) should not lessen the need to provide relevant and faithfully representative information in the consolidated financial statements.

~~10269~~ In supporting the removal of the "significant or prolonged" decline in fair value' criterion, EFRAG takes into account that it was removed while developing IFRS 9 requirements for the impairment of financial assets and that consistency in the accounting requirements for similar transactions is desirable.

70 Reversal of impairment loss under IAS 28 requirements. Some stakeholders have indicated that there was a lack of clarity on how the requirements for reversing an impairment loss in IAS 36 interact with the requirements in paragraph 58 of the ED (i.e. in situations where an investor recognises an impairment of an associate in one period, and the associate recognises an impairment loss of its assets in a later period, therefore, reducing the carrying amount of the net assets of the associate with no change in the investor's recoverable amount for the investment). The stakeholder suggested that impairment requirements in IAS 28 should include additional provisions allowing for reversal of impairment of the associate in such situations as the carrying amount of the investment would be below its recoverable amount.

~~10371~~ Finally, based on stakeholders' feedback, EFRAG recommends that IAS 28 simply reference IAS 36 requirements as the applicable guidance for the impairment of an associate or joint venture without repeating the IAS 36 impairment indicators in the IAS 28 text.

Question 6 – Investments in subsidiaries to which the equity method is applied in separate financial statements

Notes to constituents – Summary of proposals in the ED

Use of the equity method in separate financial statements

~~104~~ ~~Paragraph 10 of IAS 27 Separate Financial Statements requires an entity that prepares separate financial statements to account for investments in subsidiaries, joint ventures and associates:~~

- ~~a) at cost;~~
- ~~b) In accordance with IFRS 9; or~~
- ~~c) using the equity method as described in IAS 28~~

~~105—The use of the equity method was reintroduced by the IASB in 2014, as a measurement option for investments in subsidiaries, joint ventures and associates in separate financial statements because the law in some jurisdictions requires listed companies to present separate financial statements using the equity method for investments in subsidiaries, joint ventures and associates.~~

~~Retaining the equity method when applying it in the separate financial statements~~

~~106—When developing the proposals in the ED, the IASB decided not to develop a different equity method for use in the separate financial statements. This means that paragraph 10 of IAS 27 will remain unchanged and would apply to investments in subsidiaries to which the equity method is applied in the investor's separate financial statements.~~

~~107—The IASB noted that for separate financial statements, the focus is on the performance of the assets as investments, including investments in subsidiaries. Paragraph BC117 of the Basis for Conclusions explains that paragraph BC7 of the Basis for Conclusions on IAS 27 notes that the IASB drew a distinction between accounting for investments in subsidiaries as equity instruments and accounting for the economic entity that a parent controls. Therefore:~~

- ~~a) —in separate financial statements, an investment in a subsidiary is accounted for as an asset under the parent's control (similar to an investment in an associate or joint venture), using one of the measurement options in IAS 27; whereas~~
- ~~b) —in consolidated financial statements, a subsidiary is accounted for as an entity under the parent's control, so that the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity~~

~~108—Paragraph BC121 of the Basis for Conclusions of the ED explains that feedback from outreach with stakeholders suggests that the use of the equity method to account for investments in subsidiaries in separate financial statements is prevalent in only a few jurisdictions. In other jurisdictions in which separate financial statements are prepared, the cost option in IAS 27 is typically used.~~

~~Differences between the results of the equity method in the consolidated accounts and separate financial statements~~

~~109—Paragraph BC10G of the Basis for Conclusions on IAS 27 notes that there could be situations in which applying the equity method to investments in subsidiaries in separate financial statements would give a different result compared to consolidated financial statements.~~

~~110—As explained in paragraph BC122, the IASB was informed that there is diversity in practice when the equity method is applied to investments in subsidiaries in separate financial statements. For example, when a parent entity applies the equity method to an investment in a subsidiary:~~

- ~~a) —some parent entities aim to align the amounts reported in separate financial statements with those reported in consolidated financial statements, by analogising to IFRS 3 and IFRS 10; whereas~~
- ~~b) —other parent entities do not aim to achieve that alignment.~~

~~111—Hence the IASB notes that the effects, in practice, of applying the IASB’s proposed solutions to the application questions to investments in subsidiaries in separate financial statements will vary depending on a parent entity’s existing accounting policies.~~

~~112—Paragraph BC10G of IAS 27 explains the situations in which applying the equity method in separate financial statements to investments in subsidiaries would give a **different result compared to the consolidated financial statements**. These include:~~

- ~~a) —impairment testing requirements in IAS 28. For an investment in a subsidiary accounted for in separate financial statements using the equity method, goodwill is tested for impairment as a single asset, which is different to what is done in the consolidated financial statements of the entity.~~
- ~~b) —subsidiary that has a net liability position. IAS 28 requires an investor to discontinue recognising its share of further losses when its cumulative share of losses of the investee equals or exceeds its interest in the investee, unless a liability exists whereas there is no such requirement in relation to the consolidated financial statements.~~
- ~~c) —capitalisation of borrowing costs incurred by a parent in relation to the assets of a subsidiary. In some circumstances, it may be appropriate to include all borrowings of the parent and its subsidiaries when computing a weighted average of the borrowing costs. However, this might not be the case in the separate financial statements of the parent if the parent’s investment in the subsidiary is a financial asset, which is not a qualifying asset.~~

~~113—As explained above, there are already differences between consolidated and separate financial statements regarding the equity method. The IASB acknowledged that in some cases, new or increased differences between separate and consolidated financial statements could arise from the ED proposals. For example, applying the proposed~~

~~requirements, the parent would recognise, in full, gains or losses on transactions with subsidiaries in its separate financial statements. However, in its consolidated financial statements, it would eliminate, in full, such gains or losses.~~

~~Aligning the amounts reported in separate financial statements with those reported in consolidated financial statements for subsidiaries~~

~~114—In practice entities that opt to apply the equity method in the separate financial statements for subsidiaries generally want to achieve the same result for net assets and profit or loss attributable to the owners in the entity's separate financial statements as in the consolidated financial statements. This could be because the separate financial statements are used to determine dividend payouts or tax reasons.~~

~~Alternative View of IASB member Mr Tadeu Cendon~~

~~115—As explained in paragraph AV1 of the Basis for Conclusions of the ED, Mr Cendon supports the proposals in the ED including recognition, in full, the gains and losses resulting from all its upstream and downstream transactions with its associates or joint ventures. However, he considers that IAS 27 should have been amended to include an option to apply the equity method of accounting differently when the parent has control of the investee (the investee is a subsidiary) and the entity elects to apply the equity method.~~

~~116—In Mr Cendon's provides the following arguments in support of his alternative view:~~

- ~~a) — associates or joint ventures not part of the reporting entity in consolidated financial statements. However, this characteristic is not present when the investee is a subsidiary. Subsidiaries are part of the reporting entity as the parent controls the individual assets and liabilities of the subsidiary.~~
- ~~b) — The proposed amendments, in practice, assume that the equity method is a measurement basis because they disregard the existence of control and require the same treatment in both consolidated and separate accounts prepared under IFRS. However, he notes that because of the notion of control, a subsidiary is fundamentally different from an associate or joint venture.~~
- ~~c) — IAS 27 does not provide much insight into the purpose of separate financial statements or the principles behind the accounting options for investments in subsidiaries, joint ventures or associates.~~
- ~~d) — The proposed amendment to recognise full gains and losses on transactions on transactions with a subsidiary when applying the equity method in the separate financial statements will result in **an additional difference** to the outcome in the~~

~~consolidated financial statement (such gains and losses are eliminated under IFRS 10). This will pose a concern in jurisdictions where separate financial statements play an important role (for example for taxation and capital maintenance, including paying dividends and assessing insolvency and bankruptcy) and an entity opts to apply the equity method for subsidiaries in its separate financial statements. Such differences between the two sets of accounts could increase the cost of compliance and add complexity for users as they would need to understand why such differences exist.~~

~~117— In conclusion, Mr Cendon believes that, until the IASB addresses the conceptual questions about the nature and purpose of the equity method and the purpose of separate financial statements:~~

- ~~a) — An option should be added to IAS 27 to allow a parent to apply the equity method for investments in subsidiaries consistently with the procedures used when preparing consolidated financial statements.~~
- ~~b) — A parent choosing this option would eliminate gains or losses resulting from upstream and downstream transactions with its subsidiaries and remeasure the previously held interest when it obtains control of an associate or joint venture, or remeasure its retained investment when an entity loses control of a subsidiary and retains an investment in that former subsidiary as an investment in an associate or joint venture.~~

~~118— Paragraphs AV2–AV13 of the Basis for Conclusions of the ED explain Mr Cendon’s alternative view.~~

Question 6 - Separate financial statements

Paragraph 10 of IAS 27 permits a parent entity to use the equity method in IAS 28 to account for investments in subsidiaries, joint ventures and associates in separate financial statements.

The IASB is proposing to retain paragraph 10 of IAS 27 unchanged, meaning that the proposals in this Exposure Draft would apply to investments in subsidiaries to which the equity method is applied in the investor’s separate financial statements.

Paragraphs BC112–BC127 of the Basis for Conclusions explain the IASB’s rationale for this proposal. Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 6 – Separate Financial Statements

General comments

~~72~~ ~~The ED proposes the application of~~ EFRAG supports having a single equity method across consolidated and separate financial statements prepared under IFRS Accounting Standards. ~~EFRAG notes there are mixed stakeholder views on the ED's proposals. Most stakeholders we've heard from so far support the ED proposal as they consider~~ EFRAG considers that introducing two versions of the equity method would introduce unnecessary complexity. ~~At the same time, some stakeholders have reservations with the ED's proposal, and EFRAG also~~

~~119~~ ~~EFRAG acknowledges the Alternative View expressed in the ED (by Mr Cendon),~~

~~120~~ ~~Based on the feedback, on balance, EFRAG cautiously supports the ED's proposal and seeks further feedback from constituents on the pervasiveness of the application of the equity method in the separate financial statements of EU entities, any concerns with the ED proposal, and the suggested possible steps to alleviate these concerns.~~

~~121~~73 ~~EFRAG's initial position of cautious support is based on the understanding~~ that applying the same equity method for subsidiaries, associates or joint ventures in separate financial statements is consistent with the IASB's view that, in separate financial statements, an investment in a subsidiary is accounted for as an asset controlled by the investor (the parent entity) rather than as a business and that the focus is on the performance of the asset. Therefore, regardless of whether an investor has control or significant influence over the investee, the same equity method is used to measure the investments reported in the separate financial statements.

~~122~~74 ~~EFRAG also notes that based on outreach conducted by the IASB (see paragraph BC121 of the Basis for Conclusions of the ED),~~ Consistent with the IASB observation, the use of equity in separate financial statements is prevalent in only a few jurisdictions. ~~Instead, and~~ the cost option under IAS 27 is typically¹⁹ used. ~~However, EFRAG considers that this could~~

¹⁹A study by academics from the University of Zaragoza and University of Autonomia Madrid found that 47% of assessed companies used the equity method in their consolidation financial statements.

In contrast, the EFRAG Secretariat has found indicative (not statistically representative) evidence of a limited use of the equity method to account for subsidiaries in separate financial statements through the review of a selection of financial statements. Due to limited databases, EFRAG Secretariat reviewed the

~~change in the future if local requirements change. (paragraph BC121 of the ED's Basis for Conclusions), feedback received by EFRAG confirmed the limited use of the equity method in the separate financial statements.~~

~~Concerns with the Recognition of full gains or losses for transactions with subsidiaries~~
~~Stakeholders in jurisdictions with limited use are not concerned with the impacts of the ED's proposals~~

~~Alternative View in the ED~~

~~12375~~ EFRAG acknowledges that, as highlighted. In contrast, several stakeholders that operate in Mr Cendon's Alternative View, there could be a question about the conceptual merits of juxtaposing the principles of the equity method applied in the consolidated financial statements to jurisdictions that apply the equity method applied to subsidiaries in separate financial statements have expressed significant concerns with the ED's proposals for recognising full gains or losses for an investor's transactions with subsidiaries in the separate financial statements.

76 These stakeholders consider that subsidiaries are fundamentally different from transactions with associates and that full recognition of gains and losses could potentially lead to transactions that do not reflect the economic substance and create the risk of structuring opportunities and earnings management as there is no conflict of interest between shareholders. Furthermore, although some consider that enhanced disclosure could mitigate these concerns, it has also been noted that additional disclosures will not be sufficient to mitigate the noted risks. EFRAG therefore considers that the proposed disclosures (Question 7) are necessary but not sufficient to allow users to assess the reasonableness and sustainability of these transactions and their pricing for benchmarking against market terms.

~~12477~~ Another concern is the widening of differences²⁰ between consolidated and separate financial statements from the ED proposals due to:

financial statements of a limited judgmental (non-representative) sample of 37 companies across eight countries (Belgium, Denmark, Italy, Netherlands, Norway, Portugal, Spain, Switzerland) and a variety of industries. Only 5 of these companies (13.5%) were clearly identified as applying the equity method in the separate financial statements. 14 (38%) applied the cost method and 18 (48.6%) did not disclose or applied fair value.

²⁰ There are existing differences between consolidated and separate financial statements due to differences in impairment testing, recognition of losses and differing requirements for capitalisation of borrowing costs.

~~{(a)}~~ the required full recognition of gains or losses for transactions with controlled subsidiaries instead of restricting the reporting entity's/investor's share, as required under IFRS 10; and

~~{(a)}~~ applying the layered approach instead of IFRS 3 principles when acquiring additional interest in controlled subsidiaries.

78 ~~That said, even though~~ For the above reasons, EFRAG recommends that transactions with subsidiaries be exempted from the requirement for the recognition of full gains or losses in the separate financial statements.

Project on IAS 27

~~125~~79 EFRAG acknowledges that separate financial statements play an important role when used to declare dividends, tax reasons and/or fulfil commercial law requirements. However, we consider that, ~~if at all,~~ any issues and concerns related to separate financial statements ought to be addressed in a project on IAS 27 rather than under amendments to IAS 28. EFRAG acknowledges and agrees that the uptake of such a project^{21 22} would depend on stakeholder feedback to future IASB agenda consultations.

Recognition of full gains or losses for transactions with subsidiaries

~~126~~ Similar to Mr Cendon's Alternative View referred to in paragraphs 126 and 127 a above, some stakeholders are concerned with applying the ED's proposal for full recognition of gains or losses from transactions with subsidiaries (where the parent has control) in the separate financial statements.

~~127~~ For these stakeholders, concerns about possible earnings management and structuring are elevated when the ED's proposals are applied for transactions with controlled subsidiaries. That said, EFRAG notes that, as addressed in Question 7, the ED requires disclosures that will allow users to assess the reasonableness and sustainability of these transactions and their pricing for benchmarking against market terms.

²¹ The application of the equity method in the separate financial statements was eliminated by the IASB in 2003 and reintroduced in 2014 as it was mandated by some jurisdictions.

²² If a project were undertaken by the IASB, the 2014 EFRAG [Discussion Paper, Separate Financial Statements](#), and the related 2015 EFRAG [Feedback Statement, Responses to the Discussion Paper, Separate Financial Statements](#) would be a useful reference point as they contains some useful related thinking (e.g. outlines the perspectives of users of separate financial statements and has suggestions for narrowing differences between consolidated financial statements).

Transaction costs and cost definition in Appendix A

Transaction costs

~~12880~~ Similar to consolidated financial statements addressed in Question 1, ~~stakeholders have highlighted~~ EFRAG notes that it is unclear how transaction costs are treated in separate financial statements when an entity opts for applying the equity method to account for its subsidiaries. Moreover, EFRAG is concerned that the definition of the cost of an associate or joint venture as defined in Appendix A of the ED could have implications on the accounting for transaction costs relating to subsidiaries that are equity-accounted-for in separate financial statements.

Applicability of the equity method proposals for investments measured at cost in separate financial statements

~~12981~~ Stakeholders have indicated EFRAG notes that it is not clear whether the clarification regarding the definition of the cost of an associate or a joint venture in Appendix A is also applicable to the cost of a subsidiary. Hence, to avoid divergence in practice EFRAG suggests the IASB clarify whether the definition of cost is the same for all types of investments (i.e. associates, joint venturers and subsidiaries) especially given that, as per the ED proposals, the fair value of a contingent consideration is deemed to part of the cost of an investment in an associate or a joint venture. As explained in paragraphs BC91-92, this proposal is consistent with IFRS 3 and consistent with predominant current practice.

~~13082~~ Stakeholders have EFRAG also questioned and are seeking clarification on recommends that the IASB clarifies whether the fair value of contingent consideration is also part of the cost of an investment measured at cost. This clarification is needed because the equity method is also understood as a variant of the notion of cost measurement and thus ~~some stakeholders may expect~~ consistency across different notions of cost ~~could be expected~~.

~~13183~~ Similarly, stakeholders are seeking clarification on whether the equity method proposals for a step acquisition or the loss of control of a subsidiary extend to investments that are measured at cost in the separate financial statements. As explained in paragraph BC132, the absence of a change in the accounting method suggests that the parent should not remeasure the previously held interest or the retained interest. Some stakeholders consider that this argument is valid also when the investment is measured at cost before and after the transaction.

~~13284~~ As per paragraph 128, EFRAG is cognisant that separate financial statement issues may need to be addressed in a future project based on feedback to future IASB agenda consultations. However, at a minimum, based on the expressed stakeholder concerns,

EFRAG suggests and considers this to be a key opportunity for the IASB to clarify the applicability of the ED's equity methods proposals (i.e. in respect of contingent consideration, step acquisitions and loss of control of subsidiaries) towards investments measured at cost in separate financial statements.

Other suggested next steps

~~133 EFRAG seeks constituents' views on whether to recommend that the IASB explore the proposal by Mr Cendon (see paragraph AV13 of the Basis for Conclusions) to add an option to IAS 27 to allow a parent to apply the equity method for investments in subsidiaries consistently with the procedures used when preparing consolidated financial statements. This means that a parent entity choosing this option would:~~

- ~~a) eliminate gains or losses resulting from upstream and downstream transactions with its subsidiaries; and~~
- ~~b) remeasure the previously held interest when it obtains control of an associate or joint venture or remeasure its retained investment when an entity loses control of a subsidiary and retains an investment in that former subsidiary as an investment in an associate or joint venture.~~

~~134 EFRAG is also seeking constituents' views on whether to recommend that the IASB consider requiring an entity that applies the equity method for subsidiaries in its separate financial statements to provide a reconciliation²³ that explains the differences between the amounts in the consolidated financial statements and the separate financial statements. The reconciliation could explain the following:~~

- ~~a) amounts reported in the shareholder's equity in the parent's separate financial statements, with the equity attributable to the owners of the parent in consolidated financial statements; and~~
- ~~b) the carrying amount of its investment in a subsidiary in the parent's separate financial statements, with the net assets of the subsidiary attributable to the parent as in the parent's consolidated financial statements.~~

~~135 The reconciliation could be an aggregate for all subsidiaries or require disaggregated information for each material subsidiary (that is material to the reporting entity). EFRAG understands that gauging the suitability of such a reconciliation will depend on balancing~~

²³The reconciliation would be in the separate financial statements

~~the practicability versus the benefits of transparency on the differences between consolidated and separate financial statements for users of financial statements. Hence, via a question to constituents and outreach, EFRAG is seeking views on this reconciliation.~~

EFRAG questions to constituents – separate financial statements

~~6.1. In your jurisdiction, is the equity method for transactions with subsidiaries applied by companies? If so, is it analogised to IFRS 3 and IFRS 10 requirements (e.g., for transaction costs, and the elimination of gains or losses for transactions with subsidiaries)? Are there significant differences between any of the line items in the separate financial statements versus consolidated financial statements?~~

~~6.2. Do you agree with the suggested clarification of the applicability of the equity method principles towards investments that are measured at cost in separate financial statements?~~

~~6.3 Do you agree with the suggestion for an option to be allowed and a reconciliation required as stated in paragraphs 132 to 134? If not, please explain why.~~

Question 7 – Disclosure requirements

Notes to the constituents – Summary of proposals in the ED

Proposed amendments to IFRS 12

~~136—The IASB is proposing to amend IFRS 12, in relation to:~~

- ~~a) —Changes in an investor’s ownership interest while retaining significant influence.~~
- ~~b) —Transactions with associates;~~
- ~~c) —Contingent consideration; and~~
- ~~d) —Other matters raised by users.~~

Changes in an investor’s ownership interest while retaining significant influence

~~137—The IASB decided not to propose new disclosure requirements for the purchase or the disposal of an ownership interest in an associate or joint venture, while retaining significant influence, to be consistent with existing disclosure requirements in IFRS Accounting Standards applied to investments in associates.~~

~~138—The IASB decided to require investors to disclose gains and losses resulting from changes in ownership interest in profit or loss, as it is not expected to be costly for preparers of financial statements and would provide useful information.~~

Transactions with associates

~~139—The IASB decided to propose requiring an investor to disclose any gains or losses from downstream transactions with its associates. This would help users to assess earning quality. It would also allow users to adjust the recognised gain or loss in their analysis and to assess the reasonableness and sustainability of these transactions and their pricing for benchmarking against market terms.~~

Contingent consideration

~~140—The IASB decided to propose requiring an investor that enters into a contingent consideration arrangement to disclose:~~

~~a) —For the period in which it obtains significant influence over an associate or joint venture or purchases an additional ownership interest:~~

~~(i) —the amount recognised as at the date the entity obtains significant influence or purchases an additional ownership interest.~~

~~(ii) —a description of the arrangement and the basis for determining the amount of the payment.~~

~~(iii) —an estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, the fact, and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the investor would be required to disclose that fact.~~

~~b) —For each subsequent reporting period until the investor collects or settles the contingent consideration or it is cancelled or expires:~~

~~(i) —any changes in the amounts recognised, including any differences arising upon settlement.~~

~~(ii) —any changes in the range of outcomes (undiscounted) and the reasons for those changes.~~

~~(iii) —the valuation techniques and key model inputs used to measure the contingent consideration.~~

Other matters raised by users

~~141—The IASB acknowledged users' request for additional disclosure on interests in other entities. However, it also noted that it would need to assess the costs of implementing the new requirements and the benefits of the additional information. Because the IASB concluded~~

~~that entities can meet the disclosure objective in IFRS 12, it assessed the matter to be of low priority.~~

~~142—The IASB decided to propose:~~

- ~~a) a disclosure objective requiring an investor to disclose information that enables users of its financial statements to evaluate the changes in the carrying amount of investments in associates or joint ventures; and~~
- ~~b) a reconciliation between the opening and closing carrying amount of its investments in associates or joint ventures, to meet the new disclosure objective. In the IASB's view, it would help users distinguish between changes arising from cash transactions and changes arising from non-cash transactions.~~

~~143—The IASB observed that a reconciliation between the opening and closing amount of particular types of assets and liabilities is often required in other IFRS Accounting Standards. The IASB does not expect the proposed requirement to disclose such a reconciliation to be overly costly for preparers.~~

~~Applying the proposed disclosure requirements to investments in joint ventures~~

~~144—The IASB decided to propose the same improved disclosure requirements for investments in joint ventures, as it would be consistent with IFRS 12, which generally requires the same information to be disclosed for the two categories of investments.~~

~~145—The IASB decided not to develop a specific requirement with two separate reconciliations—one for the investor's investments in its associates and another for its investments in joint ventures.~~

~~146—The IASB also considered whether to extend the proposed disclosure requirement relating to downstream transactions to gains or losses from upstream transactions with joint ventures but decided not to do so. It would be costly to apply, and entities sometimes experience difficulties with accessing information about gains or losses recognised by an associate in upstream transactions.~~

~~Proposed amendments to IAS 27 Separate Financial Statements~~

~~147—The IASB decided that its proposed solutions to the application questions in the scope of the project would also apply to a parent that chose to use the equity method to account for its investments in subsidiaries in its separate financial statements.~~

~~148—The IASB decided, with one exception, not to require the same information to be disclosed, for two reasons: the disclosure requirements in IFRS 12 generally do not apply to separate financial statements; and the disclosure requirements in IAS 27 or other IFRS Accounting~~

~~Standards do not require the disclosure of quantitative information in separate financial statements about investments in subsidiaries to which the equity method is applied.~~

~~149 However, the IASB decided to propose requiring a parent that chose to use the equity method to account for investments in subsidiaries in its separate financial statements to disclose gains or losses from downstream transactions with its subsidiaries. The information would help users understand how much of the parent's profit or loss was generated from such transactions.~~

~~150 The IASB decided to not propose similar disclosure requirements for gains or losses recognised by the parent's subsidiaries in upstream transactions.~~

Question 7- Disclosures

The IASB is proposing amendments to IFRS 12 in this Exposure Draft. For investments accounted for using the equity method, the IASB is proposing to require an investor or a joint venturer to disclose:

- (a) gains or losses from other changes in its ownership interest;
- (b) gains or losses resulting from 'downstream' transactions with its associates or joint ventures;
- (c) information about contingent consideration arrangements; and
- (d) a reconciliation between the opening and closing carrying amount of its investments.

The IASB is also proposing an amendment to IAS 27 to require a parent—if it uses the equity method to account for its investments in subsidiaries in separate financial statements—to disclose the gains or losses resulting from its 'downstream' transactions with its subsidiaries.

Paragraphs BC137–BC171 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 7 – Disclosures

~~15185~~ **Reconciliation of open and closing carrying amount:** Based on feedback from users, EFRAG welcomes the proposed requirements and especially the reconciliation between the opening and closing carrying amount of the equity-accounted investments. We recommend a requirement to further disaggregate this information as that would be useful for users' assessment of the prospects of the reporting entity's associates and joint

ventures (dividend distribution and share of net income/losses). To minimise the reporting burden, EFRAG also recommends that a more disaggregated roll forward should only be required for material investments.

~~15286~~ Despite users supporting the reconciliation of opening and closing balances, some preparers have highlighted that such a reconciliation would be costly and complex to prepare while others have observed that many entities already include a reconciliation between the opening and closing carrying amount of their investments, albeit with different level of details.

~~15387~~ *IFRS 12 Disclosures of Interests in Other Entities*: IFRS 12 requires an investor/reporting entity to disclose²⁴ selected financial information for material joint venturers and associates. Relatedly, stakeholders have indicated to EFRAG that it is not clear which adjustments to fair value are to be considered as there could be multiple fair value adjustments if step acquisitions of ownership interests occur while retaining significant influence. It is also not clear how that information is to be reconciled to the carrying amount of the investment. EFRAG therefore suggests that the IASB provide further clarification on these aspects.

~~15488~~ *Disclosures related to bargain purchase gains*: In the response to Question 1, EFRAG noted that users have called for transparency on bargain purchase gains as these may reflect an entity's structuring activities. Hence, though not included in the ED proposals, EFRAG recommends that the IASB include disclosure requirements for bargain purchase gains similar to the related requirements under IFRS 3. Requiring the suggested disclosures would provide transparency on the reasons for the bargain purchase gains, and this would be beneficial for users of financial statements.

~~15589~~ *Disclosures of gains or losses from 'downstream' transactions with associates or joint ventures*: EFRAG acknowledges the reason for this disclosure articulated in paragraph BC 144 of the Basis for Conclusions (i.e. to assess earning quality, allow users to make analytical adjustments of recognised gains or losses, and assess reasonableness and sustainability of these transactions). This proposed disclosure will complement the existing

²⁴ Paragraph B14 of IFRS 12 specifies that the joint venturer's or associate's financial information shall be adjusted to reflect adjustments made by the entity when using the equity method, such as fair value adjustments made at the time of acquisition and adjustments for differences in accounting policies. Paragraph B14 requires also that an entity provide a reconciliation of the summarised financial information presented to the carrying amount of its interest in the joint venture or associate.

IAS 24 *Related Party Transactions* requirements for the disclosure of related party information on transactions with associates or joint ventures.

~~15690~~ However, some stakeholders have raised concerns about the cost and complexity of detailed tracking of transactions with associates and joint ventures. Hence, these stakeholders have called for the IASB to further consider the cost-benefit balance of this disclosure. EFRAG also suggests that the IASB further clarify the level of disaggregation required for this information.

~~15791~~ In addition, some stakeholders have called for the IASB to clarify which gains or losses from transactions with an investee (associate or joint venture) are in the scope of the ED's proposed disclosure requirements. For example, stakeholders noted that it was not clear whether, in the case of an investor/reporting entity having a lease arrangement with its investee, the interest received/receivable from this lease arrangement should be accounted for as a gain. [It is also not clear whether side stream transactions \(transactions between subsidiaries\) are within the scope of this proposal.](#)

~~15892~~ *Disclosure requirements related to other changes*: EFRAG suggests clarifying whether the required disclosure on gains or losses from 'other changes', as stated in paragraph 21(d) of the amended IFRS 12 presented in the ED, refers only to changes that occur when an associate or joint venture redeems or issues equity instruments or if it means any other overall changes. [Furthermore, EFRAG suggests that changes in ownership interest should be disaggregated into those related to acquisitions, disposals and other changes in ownership interest.](#)

Question 8 – Disclosure requirements for eligible subsidiaries

~~Notes to constituents – Summary of proposals in the ED~~

~~159 – The IASB decided to propose amendments to IFRS 19 to require an eligible subsidiary:~~

- ~~a) – To disclose gains or losses resulting from downstream transactions with its associates or joint ventures;~~
- ~~b) – To disclose, in the period in which the entity obtains significant influence or joint control or purchases an additional ownership interest, for contingent consideration arrangements:
 - ~~(i) – The amount recognised at the date it obtains significant influence or joint control, or at the date it purchases that additional ownership interest;~~
 - ~~(ii) – A description of the arrangement; and~~~~

~~(iii) The basis for determining the amount of the payment;~~

~~e) To disclose, for each subsequent reporting period until the entity collects or settles that contingent consideration or it is cancelled or expires:~~

~~(i) Any changes in the recognised amounts, including any differences arising upon settlement; and~~

~~(ii) The valuation techniques and key model inputs used to measure contingent consideration; and~~

~~d) To disclose gains or losses resulting from downstream transactions with its subsidiaries if the entity is a parent that uses the equity method to account for its investments in subsidiaries in its separate financial statements.~~

~~160 Based on the principles that inspired the IASB to develop IFRS 19, in the IASB's view:~~

~~a) The information about contingent consideration would provide users with useful information about cash flows and commitments. Also, the proposed disclosure requirements are consistent with the disclosure requirements in IFRS 19 for contingent consideration in business combinations.~~

~~b) The information about gains or losses from downstream transactions would help users disaggregate those gains or losses from gains or losses from transactions with third parties, and is, therefore, consistent with the disaggregation principle.~~

~~161 The IASB also decided not to propose amendments to IFRS 19 for the other proposed amendments to IFRS 12.~~

Question 8 – Disclosure requirements for eligible subsidiaries

IFRS 19 permits eligible subsidiaries to apply IFRS Accounting Standards with reduced disclosure requirements. It specifies the disclosure requirements an eligible subsidiary applies instead of the disclosure requirements in other IFRS Accounting Standards.

As part of developing proposed amendments to the disclosure requirements in other IFRS Accounting Standards, the IASB regularly considers which of those proposed amendments should be included in IFRS 19, based on the IASB's principles for reducing disclosure requirements for eligible subsidiaries.

The IASB is proposing amendments to IFRS 19 to require an eligible subsidiary:

(a) to disclose information about contingent consideration arrangements; and

(b) to disclose gains or losses resulting from 'downstream' transactions with its associates or joint ventures.

The IASB is also proposing an amendment to IFRS 19 to require a subsidiary that chooses to apply the equity method to account for its investments in subsidiaries in separate financial statements to disclose gains or losses resulting from 'downstream' transactions with those subsidiaries.

Paragraphs BC172–BC177 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative, taking into consideration the principles for reducing disclosure requirements for eligible subsidiaries applying IFRS 19 (see paragraph BC175 of the Basis for Conclusions).

EFRAG's response to Question 8 – Disclosure requirements for eligible subsidiaries

~~16293~~ EFRAG notes that the reconciliation table between the opening and the closing carrying amount of the investments would also be relevant for users of financial statements of subsidiaries without public accountability.

~~16394~~ EFRAG acknowledges that this information is expected to be available at the subsidiary level especially for subsidiaries applying the equity method, thus alleviating the cost of obtaining this information from the parent entity.

~~16495~~ EFRAG has received feedback conveying that contingent consideration can be beneficial for users who rely on subsidiary-level reports for decision-making.

Question 9 – Transition

~~Notes to the constituents – Summary of the proposals in the ED~~

~~165 – The proposed requirements would require some entities to change their accounting policies when using the equity method to account for an investment in an associate or joint venture.~~

~~166 – The ED proposes that, on transition, an investor or joint venturer shall apply the proposed amendments prospectively, except in the following cases:~~

- ~~a) – Gains or losses from transactions with associates or joint ventures (Paragraph C4 of the ED and BC183 of the Basis for Conclusions) – apply retrospectively the requirement to recognise the full gain or loss on all transactions with associates or joint ventures (paragraph 53 of the ED). This means that, at **transition date**, an~~

~~investor shall recognise it shall recognise the previously restricted portion of gains or losses:~~

~~(i) — In the opening balance of retained earnings for transactions that occurred before the transition date; and~~

~~(ii) — In the profit or loss in the comparative period for transactions that occurred in the comparative period.~~

~~b) — Paragraph B99A of IFRS 10 — Paragraph B99A of IFRS 10 has been deleted. Under Paragraph C5 of the ED an investor that applied paragraph B99A of IFRS 10 early shall apply paragraph C4 of the ED to any gain or loss from the remeasurement at fair value of an investment retained in a former subsidiary.~~

~~167 — Contingent consideration (Paragraph C6 of the ED and BC192 of the Basis for Conclusions)~~

~~— An investor shall recognise and measure contingent consideration (for investments or joint venturers purchased before the transition date) as follows: at **fair value at the transition date**. The investor or joint venturer shall classify contingent consideration in accordance with paragraph 26 of the ED and recognise any corresponding adjustment to the carrying amount of its investments in associates or joint ventures at that date. The IASB's reasoning for retrospective application for gains and losses on transactions with equity-accounted investees are explained in paragraphs BC182 — BC186 of the Basis for Conclusions. Essentially, the IASB considers that the information should be available to preparers. For contingent consideration, the IASB argues in paragraphs BC187-BC192 of the Basis for Conclusions that applying the proposals prospectively would result in a lack of comparability.~~

~~168 — The IASB proposes that in relation to transition:~~

~~a) — the date of initial application is the beginning of the annual reporting period in which an investor or joint venturer first applies the proposed requirements; and~~

~~b) — **the transition date is the beginning of the annual period immediately preceding the date of initial application**, except for entities that present more than one period of comparative information.~~

~~169 — In deciding on the transition requirements, the IASB acknowledged that retrospective application would result in the most useful information for users. However, the IASB concluded that for the other proposed amendments the costs to preparers to apply the proposals retrospectively would outweigh the benefits to users.~~

~~The IASB is also proposing relief from restating any additional prior periods presented. As explained in C9 of the ED, the IASB is granting an option not to adjust prior periods if an entity presents more than one period of comparative information.~~

Question 9- Transition

The IASB is proposing to require an entity:

- (a) to apply retrospectively the requirement to recognise the full gain or loss on all transactions with associates or joint ventures;
- (b) to apply the requirements on contingent consideration by recognising and measuring contingent consideration at fair value at the transition date—generally the beginning of the annual reporting period immediately preceding the date of initial application—and adjusting the carrying amount of its investments in associates or joint ventures accordingly; and
- (c) to apply prospectively all the other requirements from the transition date.

The IASB is also proposing relief from restating any additional prior periods presented. Paragraphs BC178–BC216 of the Basis for Conclusions explain the IASB’s rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG’s response to Question 9 - Transition

~~171~~—EFRAG agrees with the proposed transition requirements except for the proposal to apply retrospectively the requirement to recognise the full gain or loss on ~~all~~ transactions with associates or joint ventures. As explained below, EFRAG has received mixed views also seeks clarification from stakeholders the IASB on this proposal as we elaborate below.

~~172~~—BC 183 notes the retrospective application some aspects of the proposed in the ED requires an investor to recognise any remaining portion of the previously restricted gain or loss:

- ~~a)~~—in the opening balance of retained earnings for transactions that occurred before the transition date; and
- ~~b)~~—in profit or loss in the comparative period for transactions that occurred in the comparative period.

~~173~~⁹⁶Further, BC 185 notes that IAS 8 includes requirements to limit retrospective application if it is impracticable for an entity to determine the effects of a change in accounting policy.

~~174~~ ~~Some~~ EFRAG notes that ~~some~~ stakeholders support the proposal as they deem this to be less burdensome than continually monitoring the amortisation or future realisation of the previously unrecognised restricted gains or losses.

~~175~~⁹⁷ However, ~~either~~ ~~the majority of our~~ stakeholders ~~have concerns about~~ ~~did not support the retrospective application for gains and losses on transactions with associates and joint ventures. These stakeholders are concerned that~~ applying ~~this proposal~~ ~~the proposals~~ retrospectively. ~~They are concerned it~~ will result in them not reflecting the gains or losses at the time of realisation in profit or loss (e.g., on the disposal of assets). For example, entities that have a net investment hedge on the associate or joint venture ²⁵ expressed this concern.

98 Based on the concerns noted by our stakeholders, EFRAG ~~tentatively~~ recommends that the IASB ~~consider requiring~~ require prospective application for recognition of gains or losses from transactions with investees that occurred prior to application date. This would mean that previously unrecognised gains or losses from transactions with investees that occurred before the application date should be recognised under the existing IAS 28 requirements (i.e., they would be amortised or realised and reflected in profit or loss over time). In other words, the proposal for full gains or losses would only apply to transactions with investees from the date the proposal becomes applicable. ~~EFRAG seeks constituents' views on its tentative recommendation~~

Application of retrospective application for ~~a prospective approach for gains and losses~~

99 BC 183 notes the retrospective application proposed in the ED requires an investor to recognise any remaining portion of the previously restricted ~~gains~~ gain or ~~losses from~~ loss:

(a) in the opening balance of retained earnings for transactions ~~with investees that~~ occurred before the transition date; and

(b) in profit or loss in the comparative period for transactions that occurred in the comparative period.

100 Further, BC 185 notes that IAS 8 includes requirements to limit retrospective application if it is impracticable for an entity to determine the effects of a change in accounting policy.

²⁵ During EFRAG's outreach, fact patterns were presented highlighting this difficulty. For instance, it was highlighted in cases where an entity applied a net investment hedge for an associate or joint venture located in a foreign jurisdiction.

101 In EFRAG's view, it is not clear whether paragraph C4 is intended to require a full retrospective or whether it's a modified retrospective approach.

~~176~~102 Therefore, should the IASB decide to require retrospective application of unrecognised gains and losses arising from past transactions as stated in paragraph C4 of the ED, EFRAG recommends the IASB clarify how retrospective application is intended to be applied and provide an example to illustrate this requirement.

Clarification point in Appendix C of the ED

~~177~~103 Paragraph C8 of Appendix C of the ED states: 'If an investor or joint venturer applying paragraphs C4–C7 increases the carrying amount of its investment in an associate or joint venture and estimated the recoverable amount of that investment at the transition date, in accordance with IAS 36, the investor or joint venturer shall reduce that carrying amount to that recoverable amount, if applicable. The investor or joint venturer shall recognise any impairment loss in the opening balance of retained earnings at the transition date.'

~~178~~104 EFRAG is uncertain if the intention of paragraph C8 is to require an entity to determine the recoverable amount of its investment in an associate or joint venture when it increases the carrying amount of the investment when applying the transition requirements in C4-C7 or whether it is an option. EFRAG considers that if an entity increases the carrying amount of the investment at the transition date, it should be required to carry out an impairment test at the date of transition. This would avoid an entity having to recognise future impairments that result from past adjustments in profit and loss.

~~EFRAG Question to constituents~~

~~9.1 Do you agree with EFRAG's recommendation for prospective application for restricted (unrecognised) gains or losses from transactions with investees prior to application date?
Please explain~~

~~Question 10—Expected effects (cost benefit balance) of the proposals~~

~~Notes to constituents—Summary of proposals in the ED~~

~~179—The ED proposals would affect entities that:~~

- ~~a) —Are required to apply the equity method under IAS 28 to investments in associates and joint venturers in their consolidated financial statements or in individual financial statements; and~~

- ~~b) Choose to use the equity method for investments in subsidiaries, associates and joint ventures in the separate financial statements as permitted under IAS 27.~~

~~180 The impact of the proposals on affected entities will depend on the level of transactions entities undertake with equity accounted investees and on how different the entity's existing accounting policies are from the proposed requirements for those transactions.~~

~~Expected effects on information reported in the financial statements~~

~~181 Paragraph BC221 provides a table that summarises the IASB's view on the expected effects on information reported in the consolidated financial statements and where applicable in the separate financial statements.~~

~~182 The IASB explains that:~~

- ~~a) The main effects will arise because the proposals in the ED might require an entity to change their accounting policies (for example changes in ownership interest, recognition of losses and transactions with equity accounted investees. The other effect will arise from the additional proposed disclosure requirements.~~
- ~~b) With regards to the proposals on the accounting for deferred taxes and contingent consideration, the IASB notes that, although approaches in practice vary, it is common for entities to apply a similar approach to that required by IFRS 3 for business combinations.~~
- ~~c) Concerning the impairment proposals, the IASB notes that the proposals do not change the way an entity tests equity accounted investees for impairment.~~

~~Expected benefits of the quality of information reported (paragraphs BC222 and BC223 of the Basis for Conclusions)~~

~~183 The IASB explains that:~~

- ~~a) Users will benefit from more comparable information given that the proposals in the ED address aspects of the equity method for which there is currently no guidance or where current guidance is inconsistent with other IFRS Accounting Standards.~~
- ~~b) Users will also benefit from the proposed disclosure requirements which ought to provide a better understanding of transactions with equity accounted investees.~~

~~Expected costs of implementing and applying the proposals (paragraphs BC224—BC229 of the Basis for Conclusions)~~

~~184 The IASB considers that the proposals will reduce costs to preparers, auditors and regulators by providing answers to application questions arising in practice for entities applying the equity method.~~

~~185 The IASB acknowledges that entities will need to change their current accounting policies to apply many of the proposals and will also need to provide additional disclosure. This will attract additional costs to preparers. For example, the IASB notes that the proposal to measure the investor's additional share of the associate's identifiable assets and liabilities at their net fair value, and include the related deferred tax effects, when purchasing an additional interest in an associate, may be more costly than what entities currently do.~~

~~However, the IASB notes that some other proposals (for instance the proposals on full recognition of gains and losses for transactions with associates and joint venturers) will be less costly to apply than the current requirements/ current accounting policies in place (as tracking of the unrealised gain or loss will no longer be required). Investments measured at nil and unrecognised gains and losses~~

105 EFRAG notes that the following aspects of the proposed transition requirements are unclear:

- (a) how the proposed prospective transition requirements in paragraph C3 of the ED would apply to investments measured at nil at the transition date and subsequent periods, for which the investor ceased to recognise losses.
- (b) How unrecognised gains and losses could be accounted for prospectively.

106 Regarding (a) above, EFRAG seeks clarification on how to deal with the following questions related to transition requirements for unrecognised losses:

- (a) Should the amount of unrecognised losses be reset to nil at the transition date?
- (b) Should that amount continue to be monitored under the current accounting policy, which would result in two accounting policies being applied in parallel?
- (c) Should the amount of unrecognised losses be recalculated retrospectively, and if so, how should it be allocated between profit or loss and the recyclable and non-recyclable components of other comprehensive income?

Question 10 – Expected effects (cost-benefit balance) of the proposals

Question 10 – Expected effects of the proposals

Paragraphs BC217-229 of the Basis for Conclusions explain the IASB's analysis of the expected effects of implementing its proposals. Do you agree with this analysis? If not, which aspects of the analysis do you disagree with and why?

If you disagree, please explain why you disagree and your suggested alternative.

EFRAG's response to Question 10 – Expected effects of the proposals:

~~187~~107 As highlighted in our responses to the earlier questions, the feedback from preparers and other stakeholders highlights their concerns about the cost and/or complexity of the ED proposals in respect of:

~~(a)~~(a) acquiring additional ownership interest while retaining significant influence (i.e. layered approach) and the need to conduct a purchase price allocation for each acquisition;

~~(b)~~(b) changes in ownership interests that occur without exchange transactions by the reporting entity (e.g. share buybacks by associates and joint ventures);

~~(c)~~(c) removing the “significant or prolonged” decline in fair value’ criterion increasing the frequency of impairment testing;

~~(d)~~(d) disclosure requirements (e.g., reconciliation of opening and closing carrying amounts of investments); ~~and~~.

~~188~~108 At the same time, EFRAG acknowledges that there is an anticipated benefit of more complete and understandable IAS 28 requirements that will reduce diversity in practice and increase comparability. Users are expected to benefit from such comparability as well as from the increased transparency that will result from the proposed disclosures.

~~189~~ EFRAG will further evaluate the cost-benefit balance based on the constituents’ response to Question 10 of the ED and their feedback during EFRAG’s ongoing outreach.

Question 11 – Other comments

Question 11- Other comments

Do you have any comments on the other proposals in this Exposure Draft, including Appendix D to the Exposure Draft or the Illustrative Examples accompanying the Exposure Draft?

Do you have any comments or suggestions on the way the IASB is proposing to re-order the requirements in IAS 28, as set out in [draft] IAS 28 (revised 202x)?

EFRAG's response to Question 11- Other comments

~~190~~1 EFRAG acknowledges that Table 2 and paragraphs BC 15 to 16 in the Basis for Conclusions delineate the principles (i.e. principles A to H) underlying the classification, boundary of the reporting entity, initial recognition, subsequent measurement and derecognition requirements of IAS 28. EFRAG recommends that these principles be updated to, among other things, include the unit of account applied and presentation as well as any other principle analogised from other IFRS Accounting Standards (IFRS 3, IFRS 10) or derived from

~~the Conceptual Framework. These principles should also be integrated into the description of the revised IAS 28 requirements.~~

~~191 Further, EFRAG notes that the definition of the equity method in Appendix A is more of a description of its mechanics and that the link made to the cost of associate or joint venture within the definition results in a circular statement.~~

~~192 Similarly, the description of the proposed scope of the revised IAS 28 in paragraph 2 of the ED is circular, i.e. if the definitions of associate and joint venture from Appendix A were to be synonymously inserted into Paragraph 2. Hence, EFRAG suggests that the IASB consider rewording paragraph 2 of the ED as follows: 'This Standard shall be applied when an entity is: (a) an investor in an associate; or (b) a joint controlling entity in a joint venture.'~~

~~193109 With regard to interaction/Interaction with other standards, many: Many~~

stakeholders raised concerns in relation to the interaction of current IAS 28 and IFRS 18 *Presentation and Disclosure in Financial Statements* requirements. Specifically, IFRS 18 requires all entities to classify income and expenses from equity-accounted-for investments within the investing category of the statement of profit or loss. However, upon transition entities are allowed to reconsider the possibility provided by IAS 28.18 to measure the investment at fair value through profit or loss under IFRS 9.

~~194110~~ Stakeholders raised concerns that the current provisions of IAS 28.18 are subject to interpretation – for example, the notion of 'similar entities' is not clear and results in diversity in practice. Further, it was noted that the fair value option is provided based on the structure of the parent entity (venture organisation, mutual fund, unit trust, etc.) and not based on the characteristics of the associate entity. As such, the same investment held by a different entity would be accounted for differently.

111 In light of the implementation of IFRS 18, many stakeholders, especially entities in the banking and insurance sectors, raised this issue as a significant matter. Indeed/For instance, for the insurance entities it is a common practice to have equity-accounted-for investments being part of the specific business models, which may include a direct link between investments in the equity-accounted-for associates or joint ventures to insurance liabilities forming part of the underwriting result included within the operating profit. Such contracts are generally accounted for under the variable fee approach (VFA).

112 The same question about the application of IAS 28.18 is raised for other types of contracts, for example, Property and Casualty contracts (P&C), accounted for under the general model or the premium allocation approach (PAA). Whereas there will be a direct link

between the insurance liability and its servicing asset under the VFA model, there will be no direct link for the contracts accounted for under the general model or PAA. However, the investments in associates or joint ventures will still serve the same purpose – i.e., provide income to the insurance entity so that it can service its insurance liabilities.

195113 Similarly, the banking industry has a practice of establishing joint ventures with entities which provide technical support or other shared services for a pool of banks. ~~EFRAG's stakeholders consider that the fair value option should be possible for these situations regardless of the structure of the entity which holds the investment (venture organisation, mutual fund or similar entities) as it would better reflect their operating activity considering IFRS 18 requirements. Because of the current diversity in the interpretation of the requirements of IAS 28.18, it was not always possible for the concerned entities to select the fair value option in order to mitigate the classification mismatch. Consequently, the intended outcome of the IFRS 18 transition requirements of mitigating the classification mismatch may not be met.~~

114 Based on the concerns raised by stakeholders, EFRAG suggests the IASB should either introduce a general option in IAS 28 allowing an entity to account for the associates and joint ventures at FV through PL or to broaden the scope of IAS 28.18 to accommodate all types of investments (VFA and non-VFA contracts for example) which are backing up insurance liabilities.

115 Integrate articulation of concepts: EFRAG acknowledges that Table 2 and paragraphs BC 15 to 16 in the Basis for Conclusions delineate the principles (i.e. principles A to H) underlying the classification, boundary of the reporting entity, initial recognition, subsequent measurement and derecognition requirements of IAS 28. EFRAG recommends that these principles be updated to, among other things, include the unit of account applied and presentation as well as any other principle analogised from other IFRS Accounting Standards (IFRS 3, IFRS 10) or derived from the Conceptual Framework. These principles should also be integrated into the description of the revised IAS 28 requirements.

116 Scope: The description of the proposed scope of the revised IAS 28 in paragraph 2 of the ED is circular, i.e. if the definitions of associate and joint venture from Appendix A were to be synonymously inserted into Paragraph 2. Hence, EFRAG suggests that the IASB consider rewording paragraph 2 of the ED as follows: 'This Standard shall be applied when an entity is: (a) an investor in an associate; or (b) a joint controlling entity in a joint venture.'

117 Further, EFRAG notes that the definition of the equity method in Appendix A is more of a description of its mechanics and that the link made to the cost of associate or joint venture within the definition results in a circular statement.