

10 May 2021

Mr. Hans Hoogervorst  
Chair  
International Accounting Standards Board  
7 Westferry Circus  
Canary Wharf  
London, E14 4HD  
United Kingdom

Dear Mr. Hoogervorst,

The Asian-Oceanian Standard-Setters Group (AOSSG) is pleased to provide comments on the International Accounting Standards Board's ('the IASB's') Request for Information (RFI) *Post-implementation Review of IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities*. In formulating these comments, the views of the constituents within each jurisdiction were sought and considered.

The AOSSG currently has 27 member standard-setters from the Asian-Oceanian region: Australia, Bangladesh, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan and Vietnam. To the extent feasible, this submission to the IASB reflects in broad terms the collective views of AOSSG members. The intention of the AOSSG is to enhance the input to the IASB from the Asia-Oceania region and not to prevent the IASB from receiving the variety of views that individual member standard-setters may hold. This submission has been circulated to all AOSSG members for their comment. In responding to the RFI, AOSSG members have provided their responses to the questions in the RFI as described in Appendix of this submission.

### **IFRS 10 - Assessment of control**

While some AOSSG members observed that IFRS 10 generally works well, most AOSSG members were informed that further guidance and/or illustrative examples were needed on certain areas of IFRS 10. AOSSG members observed the following areas in which further guidance and/or illustrative examples were warranted:

### Identification of relevant activities

AOSSG members observed challenges in identifying relevant activities in the following situations:

- an investee has multiple phases during its life and different investors have decision-making rights in different phases
- two or more investors have the unilateral ability to direct different activities of the investee at the same time
- implicit rights are considered arising from other than a formal contract for structured entities
- an arrangement is considered to have no relevant activities (index-linked funds and auto pilot SPEs)
- the activities that affect only limited returns relative to the overall returns are identified

### Determination of protective rights

AOSSG members observed that it was challenging to determine whether rights were protective rights in the following situations:

- when an SPE is involved and a veto right is held by a lender (usually a financial institution) over the investment decisions of the borrower (an SPE)
- an investor has a veto right over the profit distribution plan of the investee
- franchisors direct franchisees' activities
- when a bank lends money to a customer to finance a venture, the bank is a shareholder in the venture, and is entitled to a share in its profits or loss (and hence is exposed to variable returns) and has various rights in the contract (for example, rights to be consulted on certain actions)

### Determination of whether a decision maker is a principal or an agent

AOSSG members noted challenges in determining whether a decision maker was a principal or an agent particularly in the fund and asset management industry, for example, in considering the roles of the general partner, limited partner (i.e. investors) and asset manager. In addition, AOSSG members noted the following situations in which the determination of a principal or an agent was challenging:

- seed money is invested by an asset manager into a fund and that investment is ejected over time
- a fund manager's exposure to variability of returns from its interest is low

## **IFRS 10 - Accounting requirements**

### Accounting for an investee which does not constitute a business

Some AOSSG members observed that transactions occur in which an investor acquired control or lost control over an investee which did not constitute a business. Furthermore, some AOSSG members were informed that some of the stakeholders desired the clarification of the accounting for an investee which did not constitute a business.

### Usefulness of the information from the remeasuring retained interests on the loss of control

Some AOSSG members observed that there were mixed views among the stakeholders. Some stakeholders commented that remeasurement did not provide relevant information because the retained interests were not actually sold at the time of the loss of control. On the other hand, other stakeholders commented that remeasurement provided relevant information because the remeasurement reflected the value of the retained interests at the time of the loss of control.

## **IFRS 11**

Most AOSSG members did not identify major difficulties regarding implementation of IFRS 11, while some AOSSG members received feedback that clarification was needed in certain areas. Specific areas varied by jurisdiction.

## **IFRS 12**

Most AOSSG members found that the disclosure requirements in IFRS 12 were adequate, while some AOSSG members were informed that the following additional disclosures would be helpful:

- detailed cash flow information for subsidiaries with material non-controlling interests
- the potential dilution of ownership interests due to outstanding shares
- the amount of interest-bearing borrowings within paragraphs B13(b)-(c) of IFRS 12 to assist users in determining the entity's gearing level
- the cash contribution from all equity method investments
- the criteria for determining materiality in disclosure of interests in other entities

On the other hand, some AOSSG members were informed that some stakeholders questioned the usefulness of the following information required by IFRS 12:

- the aggregate carrying amount of interests in associates and joint ventures that are individually immaterial
- disclosures of interests in unconsolidated structured entities when there is some overlap with the disclosure requirements in other IFRS Standards
- the disclosure of sponsorship in interests in unconsolidated structured entities

### Other topics - Equity method

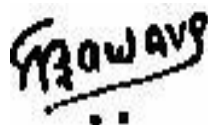
As to the issues regarding the equity method of accounting which is applied when an investee is classified as a joint venture in accordance with IFRS 11, some AOSSG members were informed of the following issues:

- guidance is needed on the accounting for an additional stake in a joint venture without a change in joint control
- benefits and disadvantages should be considered of proportionate consolidation and equity method, while acknowledging that the IASB considered the withdrawal of proportionate consolidation at length

Furthermore, one AOSSG member suggested that the IASB undertook a project to develop principles that would clarify when to focus on the one-line consolidation aspect and when to focus on the measurement basis aspect.

If you have any questions regarding this submission, please contact either one of us.

Yours sincerely



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Chair, AOSSG



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## Appendix – Comments from AOSSG members

Comments from some jurisdictions in this paper are based on staff's view. Therefore, these comments may not necessarily reflect the views of the official entity in each jurisdiction.

### IASB RFI Post-implementation Review

#### Questions for respondents

##### Question 2(a)

In your experience:

- (i) to what extent does applying paragraphs 10–14 and B11–B13 of IFRS 10 enable an investor to identify the relevant activities of an investee?
- (ii) are there situations in which identifying the relevant activities of an investee poses a challenge, and how frequently do these situations arise? In these situations, what other factors are relevant to identifying the relevant activities?

#### AOSSG members' comments on Question 2(a) (including general comments on IFRS 10)

##### [Australia]

Consistent with the feedback noted in the RFI, Australian stakeholders also consider identifying the relevant activities of an investee to, at times, be challenging and very judgmental.

Australian stakeholders noted that determining which activities are most relevant to the control assessment can be complex in situations where an investee has multiple stages during its life and various investors have decision-making rights in different stages. For example, stakeholders suggested that the requirements of IFRS 10 are not clear whether control is assessed by considering the relevant activities over the entire life of the entity even though the entity has multiple stages, and therefore which party has decision-making abilities over the 'most relevant' activities. Alternatively, whether should control be assessed by considering each stage of life separately, noting that only certain decisions are relevant at some stages, the control may be transitory.

Australia is aware of a view that control can change from one investor to another over time following the reassessment of an entity's relevant activities (e.g., if one investor has decision-making rights over research and development, including regulatory approval and another has decision-making rights over manufacture and sale, once regulatory approval is obtained,

research and development can no longer be a relevant activity. The relevant activity now relates to manufacture and sale). It was noted that IFRS 10 Application Example 1 states that investors need to consider the activities that **most** significantly affect the investee's returns (emphasis added). This appears to imply that these are meant to be the overall returns over the whole life of the investee. The ambiguity might arise from the use of 'current' in paragraph 13 and whether that implies that an investor would disregard the fact that they only have decision-making rights in the next stage of the project's life. However, the application example doesn't appear to support an assessment per stage of the entity's life.

Australia understands there is often extensive debate due to the judgement required to determine which activities are the most significant.

Despite the principles of IFRS 10 and the application guidance and examples, feedback received from stakeholders suggests that the IASB's intention is not clear in relation to assessing the relevant activities in phases or for the totality of the investee's life. Therefore, Australia recommends that the IASB consider including additional illustrative examples and detailed educational guidance to clarify how to identify an investee's relevant activities where the entity has multiple stages during its life and different investors have decision-making rights in different phases.

#### [China]

**Identifying the relevant activities of an investee:** when two or more investors have the unilateral ability to direct different relevant activities of the investee at the same time, or when two or more investors have the unilateral ability to direct relevant activities of the investee at different stages, how to use qualitative factors and quantitative thresholds to determine the activities that most significantly affect the returns of the investee.

#### [Korea]

Many respondents said that issues relating to assessing the power of the structured entities frequently occur in Korea. However, they say that there are relatively few examples of structured entities in IFRS 10 despite the importance of the matter.

- In Korea, the number of structured entities is increasing as companies use it as a method of financing. Given this, judgment on whether to consolidate structured entities may have significant impacts on the financial position of the reporting entity.
- Unlike other companies, there is a complexity of considering the implicit rights arising from other than a formal contract for structured companies, as there is the involvement and decisions made at the investee's inception as part of its design (B51~B52). However, there is a lack of example that demonstrates how to incorporate paragraph B51~B52 to structured entities control judgment.

Many respondents suggest providing a specific example on control assessment of ‘structured entities’ as there seems to be a high tendency for companies to use ‘structured entities’ in recent years.

### **[Hong Kong]**

Hong Kong observed that the identification of relevant activities is not a significant issue for preparers and auditors after understanding the commercial rationale and business model of the investee. The related requirements and application guidance in IFRS 10 are sufficient and working as intended.

Respondents considered that identification of relevant activities involves significant judgement in complex situations; examples include:

- whether price setting is a relevant activity if it is regulated by a government who is also a shareholder;
- two or more investors direct different relevant activities at different times;
- multiple parties have different responsibilities, which is common when state-owned enterprises are involved; and
- cases involving of special purpose entities (SPE).

### **[Japan]**

#### **(Identification of the relevant activities)**

- Preparers commented that identifying the relevant activities in determining the scope of the consolidation has not been an issue or that such situations were rare.
- One preparer and auditors commented that difficulties in identifying the relevant activities may arise in the following cases, but the difficulties are not significant enough to warrant amendments to the standard:
  - (1) There is more than one relevant activity.
  - (2) A special-purpose entity (SPE) holds only bonds held to maturity.
  - (3) In assessing whether an arrangement is a joint arrangement and who control the entity, two parties to an arrangement identify different activities as the relevant activities.
- On the other hand, other preparers suggested adding new examples and improving existing examples:
  - (1) Identifying the relevant activities (a) when an arrangement is considered to have no relevant activities (index-linked funds and auto pilot SPEs) and (b) when the activities that affect only limited returns relative to the overall returns are identified as the

relevant activities may be challenging and thus new examples should be added.

- (2) When there is more than one activity (the approval of the business plan, the approval of dividend payment, or the approval of the investment or loan), determining which activities most significantly affect the investee's returns may be challenging and thus new examples should be added to illustrate how to make that determination. In addition, existing examples should be improved to illustrate how the determination was made.

### **[Malaysia]**

Respondents were generally of the view that applying paragraphs 10-14 and B11-B13 of IFRS 10 would, in most circumstances, enable an investor to identify the relevant activities of an investee.

Some respondents noted challenges in situations where two or more investors each have existing rights that give them the unilateral ability to direct different relevant activities. In such situations, paragraph 13 of IFRS 10 states that the investor that has the current ability to direct the activities that most significantly affect the returns of the investee has power over the investee.

Respondents provided the following examples where different judgements may be reached about which activities most significantly affect the returns of the investee, thereby resulting in lack of comparability between entities:

- (a) In some situations, both investors conclude that the relevant activities they direct are significant, currently and/or in future periods, and it can be difficult to determine what weightings to give the different activities in assessing which most significantly affect the investee's returns. For example, at a point in time, a particular activity might be more pertinent than all of the other activities, and different judgements could be reached on whether the investor directing those activities has power over the investee even when the other investor directs all other significant activities.

In addition, the most significant activities can vary over time depending on the stage of the investment. To result in more consistent application of judgement, some stakeholders think it would be helpful to have a clear principle on how to rank the different activities of the investee when applying paragraph 13 of IFRS 10, rather than just providing examples of activities that, depending on the circumstances, can be relevant activities (as in paragraph B11 of IFRS 10).

These stakeholders noted that it would be more useful for the IASB to explain or illustrate the thought process of applying the principle rather than providing additional examples for specific fact patterns.



- (b) Some respondents noted that there are different interpretations in practice of ‘investee’s returns’ used in the definition of relevant activities. For example, it is unclear if this refers to the investee’s current profits, expected profits, returns to stakeholders, or some other measure of performance.

Some respondents suggested IFRS 10 should define ‘investee’s returns’ to ensure a more consistent application of the notion of relevant activities and also help entities to rank the different activities as highlighted in (a).

- (c) One stakeholder provided a specific example where challenges exist both in prioritising the relevant activities at different stages of an investee’s operating cycle, and also determining whether rights of a minority interest are protective rights. This example is included in Question 2(b) below.

One stakeholder noted that while the principles in paragraphs 10–14 of IFRS 10 are clear and relevant for determining whether an ‘investor’ or ‘sponsor’ controls an investee operating on ‘auto-pilot’, those principles have not been described in a way that is readily recognisable by the industry players involved in this type of structures. It was observed that certain industry players held a different view although the others and the auditors are mostly clear on the applicability of IFRS 10. This stakeholder observed that articulation similar to that previously used in SIC 12 *Consolidation—Special Purpose Entities* would be helpful to demonstrate the consistent application of the IFRS 10 principles including to an ‘auto-pilot’ structure established by the investor who is considered the ‘sponsor’. This may involve using or adding the relevant key words in describing how the principles should be applied or to add ‘auto-pilot’ into the application guidance.

#### **[Pakistan]**

##### **IFRS 10 Consolidated Financial Statements**

Overall, Pakistan notes that the implementation of IFRS 10 has had a positive effect on financial reporting as it introduced one single control model for all entities. This has improved the application and comparability of financial information across a range of entities.

Pakistan recognises that IFRS 10 is a principle-based Standard, however, further guidance and Illustrative Examples would help in common understanding and consistent application of the Standard. For example, the definition of investment entities requires a high degree of judgement. Similarly, the determination of protective versus substantive rights also involve judgment. Another area of the Standard that requires consideration of various factors, accordingly involves judgment is agent/principal assessment.

Pakistan suggests that IASB provide further guidance and Illustrative Examples with regards to the determination of investment entities, assessment of protective versus substantive rights and the agent/principal assessment.

### Question 2(b)

In your experience:

- (i) to what extent does applying paragraphs B26–B33 of IFRS 10 enable an investor to determine if rights are protective rights?
- (ii) to what extent does applying paragraphs B22–B24 of IFRS 10 enable an investor to determine if rights (including potential voting rights) are, or have ceased to be, substantive?

### AOSSG members' comments on Question 2(b)

#### [Australia]

##### *General feedback*

Stakeholder feedback identified that assessing whether rights are protective or substantive is an area of significant debate, and many entities have difficulty applying the IFRS 10 guidance.

In general, stakeholders suggested that making the assessment is difficult because there are no bright lines. It was noted that while the guidance in IFRS 10 is supplemented by application examples that are intended to help investors determine whether or not they control an investee, they are not sufficient as they tend only to have one variable and show only one aspect of the decision-making assessment. Further, stakeholders noted that it is not always clear how the IFRS 10 principles have been applied when developing the guidance and illustrative examples. There are overarching principles in the Standard and guidance that draw certain conclusions for certain isolated fact patterns, but the connection between the two is not always evident. Accordingly, if it is not clear how the principles are applied, it is more difficult to combine different scenarios and apply the guidance.

As in practice, there can be many factors to consider when determining whether rights are protective or substantive, Australia recommends that the IASB consider providing detailed educational guidance with a similar level of detail to an IFRS Interpretations Committee (IFRS IC) Tentative Agenda Decision. That is, examples that illustrate complex fact patterns and provide a step-by-step analysis of how the IASB intended the principles in IFRS 10 to be applied.

Australia prefers principles-based standard-setting but acknowledge that, in practice, additional guidance is sometimes necessary to assist in decision making.

#### *Franchise arrangements*

In relation to franchise arrangements, consistent with the feedback in the RFI, Australian stakeholders confirmed that assessing whether rights are substantive or protective in franchise arrangements is challenging. In particular, the Standard suggests that franchisor rights are generally protective. However, stakeholders questioned whether this is true in practice and aligns with the principles of IFRS 10.

For example, in the stakeholders' experience, the franchisor typically sets the price, the operating hours and mandates the suppliers. Franchisors may also provide financing and can assist with recruitment too. As these activities are examples of activities that typically significantly affect franchisee's returns, if some of these activities are directed by the franchisor and others by the franchisee, it is necessary to determine which of the activities most significantly affect the franchisee's returns. Australia understands that in practice, it is not uncommon for franchisors to direct most of the activities noted above and if the decision-making rights are considered substantive, this would be contrary to the conclusions drawn in the guidance. However, while a franchisor may appear to control a franchisee, stakeholders suggested it is either uncommon for franchisees to be consolidated or at best there are inconsistencies in this regard. This is because the guidance in IFRS 10 is not clear as it states that franchisor rights are normally protective.

Therefore, if the IASB intended that franchisees may need to be consolidated under certain circumstances, Australia recommends it needs to be made clearer that this could occur, as the concept is not clearly understood. Australia also recommends the IASB revisit the guidance on franchises and consider removing statements that imply that franchisor rights are normally protective in nature.

#### **[China]**

**The distinction between substantive rights and protective rights:** if the investor has vote veto over the profit distribution plan of the investee, whether the right is a protective right or not.

#### **[Hong Kong]**

Hong Kong observed that determination of whether rights are substantive or protective is challenging. Challenges are often seen in the real estate industry, asset management industry and when SPE are involved. For example, diversity in practice is noted in determining whether a veto right held by a lender (usually a financial institution) over the investment decisions of the borrower (a SPE) is substantive or protective. IFRS 10.B28(a) states that a

lender right which restricts the borrower from undertaking activities that could significantly change the credit risk of the borrower is an example of protective right. However, as the investment decisions are significant to the returns of the SPE, such a right could also be viewed as substantive. Further clarification of the definition of protective rights and additional guidance on how to assess whether such a veto right is substantive or protective would be useful.

## **[Japan]**

### **(Determining whether an investor's rights are protective and substantive)**

- Regarding the determination of whether an investor's rights are protective and substantive, preparers noted the following:
  - (1) Whether the rights are protective is not questioned in most cases because protective rights arise only in limited circumstances. The requirements in IFRS 10 provide guidance for assessing whether a right is substantive.
  - (2) The meaning of 'fundamental changes to the activities of an investee' in the assessment of protective rights in paragraph B26 of IFRS 10 is unclear, which may lead to diversity in judgment among the investors. Protective rights are viewed as those that contribute to protecting the interests of the investors.

## **[Malaysia]**

Respondents were generally of the view that the principles of and the requirements for protective rights and substantive rights are clear.

However, they observed that as there is limited guidance on how to apply those principles, different parties can make different judgements when applying the principles resulting in different outcomes. Nevertheless, some respondents observed that, as long as the key assumptions and the analysis are sufficiently disclosed, in most cases the outcome is considered reasonable as a result of applying the principle-based standards.

On the other hand, some stakeholders observed that the assessment of whether rights are protective can be challenging in some situation. Such challenges can often arise in Malaysia in an Islamic banking arrangement under Musharaka financing. When a bank lends money to a customer to finance a venture, the bank is a shareholder in the venture and is entitled to a share in its profits or loss (and hence is exposed to variable returns). The bank also includes various rights in the contract, for example, rights to be consulted on certain actions and the right to block any actions by the customer with respect to the venture that it does not consider to be favourable. The bank's intent for including these rights in the contract is to manage credit or recoverability risk of the financing provided. However, respondents observed that

different judgements could be made as to whether the bank's contractual rights are merely protective or whether they prevent the customer from exercising power over the venture. Nevertheless, it was noted that there is currently no noted diversity in practice and banks are not consolidating such investees.

One respondent observed that the assessment of whether rights are protective can be challenging for certain reserved Matters in shareholders' agreement (matters that require the consent of all of the shareholders or directors of the entity before being approved and implemented). Although decision-making rights about reserved matters are usually clearly protective rights, this is not always the case and different parties can reach different conclusions on whether they are merely protective rights applying the requirements in IFRS 10. For example, occasionally it can be challenging to assess whether the following matters constitute only protective rights:

- Decisions on major capital expenditure
- Decisions on approval or variation of annual budgets
- Decisions on approval or variation of business plan/ change of business model
- Decisions to divest material assets
- Decisions on significant changes to projects
- Decisions on appointment of key management personnel

For example:

- the assessment of whether decision making rights over the approval and variation of annual budgets are considered to be protective rights may depend on the level of detail within the annual budget that is subject to such approval.
- if the decision-making rights are only regarding approval of the appointment of a candidate as key management personnel, they are likely to be protective rights. However, if the rights include decisions on sourcing, selection, evaluation and nomination of candidates as well they might be considered more than merely protective.

There can also challenges in assessing whether the following rights are protective in some situations:

- investor has the right to appoint different members of the investee's key management personnel;
- rights under a franchise agreement that substantially restrict the ability of other parties to direct relevant activities; and
- deadlock clauses that affect the nature of the rights held by the entity or other parties

Protective rights are defined by IFRS 10 as rights designed to protect the ‘interest’ of the party holding those rights without giving that party power over the entity to which those rights relate. To result in more consistent application of judgement, some respondents suggested it would be helpful to extend the definition of protective rights by including a clear explanation of what protective rights are designed to protect, for example how to identify what is the ‘interest’ of the party that the rights aim to protect.

One stakeholder provided the following specific example where challenges exist both in prioritising the relevant activities at different stages of an investee’s operating cycle, and also determining whether rights of a minority interest are protective rights or result in joint control:

Investor A owns 60% of the shares in a company and can appoint a majority of the Board of Directors and Investor B (a private equity fund with access to capital) owns the remaining 40% of the shares. The company constructs an asset, e.g., a power plant, and upon completion operates that asset, e.g., supplies electricity to a customer for the life of the power plant. In the shareholder agreement between the two investors, appointment of contractors / suppliers and capital expenditures/funding exceeding \$X million are reserved matters requiring the shareholders' joint approval. Therefore, during the construction phase (which includes the raising of funds, capital expenditure on the plant and selecting contractors), Investor B’s rights are more than merely protective and different judgements may be reached on whether Investor A has power over the relevant activities during this phase or whether the two investors have joint control. However, after the construction phase, Investor A clearly has power over the relevant activities.

### Question 2(c)

In your experience:

- (i) to what extent does applying paragraphs B41–B46 of IFRS 10 to situations in which the other shareholdings are widely dispersed enable an investor that does not hold a majority of the voting rights to make an appropriate assessment of whether it has acquired (or lost) the practical ability to direct an investee’s relevant activities?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 2(c)(i) arise?
- (iii) is the cost of obtaining the information required to make the assessment significant?

### AOSSG members’ comments on Question 2(c)

#### [Australia]

Australia does not have comments in response to this question.

### [China]

**The assessment of de facto control without holding a majority of voting rights:** First, when voting rights were widely dispersed, significant judgment involves in the assessment on whether other investors may jointly exercise their voting rights to exceed the voting rights of the investor, which leads into diversity in practice. Second, investors without holding a majority of voting rights may sign a consensus agreement with other parties to increase the concentration of their voting rights so as to ensure the control status. However, there are diverse views in practice on whether the duration of the consensus agreement needs to be considered or not.

### [Hong Kong]

Hong Kong noted that challenges in assessing de facto control arise regularly in Hong Kong and China, and complexity increases when state-owned enterprises are involved. Application of the requirements and guidance in IFRS 10 is highly judgemental and questions may arise as to whether that judgement is appropriate. More comprehensive examples to illustrate factors for consideration in a holistic assessment would be helpful.

### [Japan]

- Preparers commented on the assessment of control when the entity does not hold a majority of the voting rights as follows:
  - (1) In situations where the other shareholdings are widely dispersed, the ratio of voting rights at shareholders' meetings is used to determine whether the entity has effective control. However, this has not been in an issue when assessing the power over the investee.
  - (2) The factors set out in paragraphs B42(a) to (c) of IFRS 10 and the examples alone may lead to inconsistent judgments because the specific assessment guidelines are unclear. For example, it is unclear how widely the other holders of voting rights need to be dispersed to be sufficient to determine that the entity has power, and it is unclear at what point in time or for what period the entity should refer to the historical voting patterns.
  - (3) Monitoring for the reassessment is quite costly as it requires the assessment of the relative size of the holding for each investment.

### [Malaysia]

Respondents were generally of the view that applying paragraphs B41-B46 of IFRS 10 to situations in which the other shareholdings are widely dispersed would, in most circumstances, enable an investor that does not hold a majority of the voting rights to make



an appropriate assessment of whether it has acquired (or lost) the practical ability to direct an investee's relevant activities.

Respondents generally observed that the situation described in 2(c)(i) can arise occasionally for publicly listed investees, and in practice it is usually clear whether the investor has control. Therefore, the cost of obtaining the information required to make the assessment is not significant.

However, Malaysia observed that it could be difficult to assess whether an investor has the current ability to direct the relevant activities of a publicly listed investee because many shareholders do not join routine meetings. For example, during previous years, approximately 30% of other shareholders may have attended routine meetings. In this case it may be difficult to determine whether an investor holding 40% has control, because 60% of shareholders could potentially show up if the meeting included a major decision related to the investee.

### Question 3(a)

In your experience:

- (i) to what extent does applying the factors listed in paragraph B60 of IFRS 10 (and the application guidance in paragraphs B62–B72 of IFRS 10) enable an investor to determine whether a decision maker is a principal or an agent?
- (ii) are there situations in which it is challenging to identify an agency relationship? If yes, please describe the challenges that arise in these situations.
- (iii) how frequently do these situations arise?

### AOSSG members' comments on Question 3(a)

#### [Australia]

Consistent with the feedback in the RFI, stakeholders also confirmed that determining whether an agency relationship exists can be challenging as the assessment can require a significant amount of judgement, particularly in the funds management industry where there are often complex remuneration arrangements in place. This leads to diversity in outcomes for similar arrangements and structures.

When assessing whether a decision-maker is acting as an agent or a principal, stakeholders suggested that generally, it is the rights held by third parties to remove the decision-maker and the exposure to variable returns through other interests that often require the most consideration.



For example, stakeholders were unsure how the requirements correlate in a situation where an investor can remove the fund manager without cause (an indication that the fund manager acts as an agent), but remuneration is not market-related (an indication that the fund manager acts as a principal). A further example is a fund manager that only holds a small investment and is being remunerated at market rates (an indication that the fund manager acts as an agent) but can't be removed without cause (an indication that the fund manager acts as a principal). In this case, there is only minimal variability of returns, however, it was unclear whether there is still a link between power and returns.

Australia acknowledges that in most asset management scenarios involving retail investors, management will necessarily conclude that the remuneration is commensurate with the service provided and based on market terms. This is because retail investors would invest elsewhere if this were not the case. However, Australia notes that IFRS 10.B68 suggests that "the greater the magnitude of, and variability associated with, the decision maker's remuneration relative to the returns expected from the activities of the investee, the more likely the decision-maker is a principal" and therefore judgement is required.

#### *IFRS 10 Application Examples*

IFRS 10 Application Examples 13-15 set out three common remuneration structures. Whilst these examples are useful in illustrating how to apply the principles and guidance in IFRS 10, stakeholders regard the scenarios as too simplistic. The simplistic nature of the examples is particularly evident in that they do not consider scenarios where there are different and less straightforward remuneration arrangements. For this reason, Australia suggests it would be helpful for the IASB to expand on the discussion included in the application examples to explain why/how on balance, a specific conclusion was reached by referring back to the general principles of control in IFRS 10 paragraph 7 and the supporting application guidance.

For example, in Application Example 13, there is the variability of returns and no substantive removal rights (indicating a principal relationship). However, the overall conclusion is that the fund manager is an agent because of restricted parameters governing the assets the fund manager can invest in and only limited exposure to variability of returns. The example does not explain why the fact that the manager was involved in the establishment – and therefore presumably – the design of the investee (paragraph B63) does not appear to be relevant in this context and why the other interests held (i.e., the 10% investment) do not result in sufficient exposure to variability of returns from other interests when considered together with the remuneration received (paragraphs B71 and B72).

Further, application examples 14A to 14C all use the same basic fact pattern but then vary one or two factors, being the ownership interest and the removal rights. The examples conclude that with a 2% investment but no substantive removal rights, the fund manager

would be an agent, but that a 20% investment could be sufficient to conclude that there is control. Example 14B further states that control may also arise at different levels of the investment if the fact pattern is different. In example 14C, the other investors have substantive removal rights, and therefore the fund manager concludes that they do not control the fund even though they have a 20% investment.

While these examples do illustrate some common scenarios, in practice, it is often not as clear whether rights held by other parties are substantive or protective and fund managers may also have exposure to variable returns through other mechanisms (e.g., a requirement to fund losses or entitlement to residual returns of the investee). While paragraph B72 says that it will be necessary to consider the magnitude of, and variability associated with, the economic interest and whether this is different to other investors, this obviously involves a significant amount of judgement. Further, there may be situations with contradictory indicators, such as when the fund manager can be removed without the cause, but the remuneration is not market-related (or vice versa).

In summary, while additional interpretive guidance may be helpful to assist with applying the principles, this could undermine the principle-based nature of IFRS 10. For this reason, instead of adding more application examples or guidance paragraphs to the Standard, Australia recommends the IASB consider providing detailed educational guidance with a similar level of detail to an IFRS Interpretations Committee (IFRS IC) Tentative Agenda Decision. That is examples that illustrate complex fact patterns and provide a step-by-step analysis of how the IASB intended the principles in IFRS 10 to be applied.

#### [China]

**The determination of whether a decision-maker is acting as a principal or an agent:** in terms of how to consider the quantitative criteria for the magnitude and the variability of variable returns, especially in special circumstances such as whether to control structured entities, there are many difficulties and disputes.

#### [Korea]

Many respondents said that ‘principal vs agent’ frequently occurs in Korea. However, they say that there is a lack of guidance on it.

- ‘Principal vs agent’ decision would have a significant impact on the financial institutions that hold investments in a myriad of funds.
- For instance, if a decision maker (General Partner) is determined to be an agent, it is challenging to identify the principal among multiple investors (Limited Partners) since guidance in IFRS 10 is focused on identifying only whether the decision maker acts as an agent.

- In example 14A, the fund manager is determined as an agent as its exposure to variability of returns from its interest is low (2%). In example 14B, with all other things being equal, the fund manager is determined as a principal as its exposure to variability of returns from its interest is high (20%). Many respondents requested examples where the fund manager's interest is between 2% and 20%.

They suggest providing more guidance or examples on the 'principal vs agent' decision.

### **[Hong Kong]**

Hong Kong noticed that it is challenging and highly judgemental to assess whether the decision maker is a principal or an agent, particularly in the fund and asset management industries. This can arise when assessing certain fund structures and considering the role of the general partner, limited partner (i.e. investors) and asset manager. It also arises in cases where seed money is invested by an asset manager into a fund and that investment is ejected over time. Questions arise as to whether the asset manager is a principal or an agent based on minimal equity interests but a potentially significant variability in returns (i.e. magnitude versus variability of returns). Hong Kong considers non-industry specific illustrative examples may be helpful.

### **[Japan]**

- Preparers commented that whether an investor is a principal or an agent has not been an issue or that such situations were rare. On the other hand, one preparer noted the following:
  - (1) When the asset manager and the investors in the fund belong to the same entity and, based on the size of the return, the decision-maker would be determined to be the principal but other parties have the right to remove the asset manager in proportion to their interests, paragraph B65 of IFRS 10 alone is not clear to determine whether the size of the return or the removal rights should be given priority.
  - (2) Fixed and performance-based remuneration as an asset manager is difficult to consider in determining whether a party is a principal or an agent because the fund manager's proportion of economic involvement would vary.

### **[Malaysia]**

Respondents were generally of the view that the factors listed in paragraph B60 of IFRS 10 (and the application guidance in paragraphs B62–B72 of IFRS 10) are clear.

However, some respondents observed that different parties make different judgements when applying the principles to fund managers of unit trust funds resulting in different outcomes. In particular, given a specific scenario, there will be different views on at what threshold the percentage of a fund manager's investment in a fund under its control and management

creates exposure to variability of returns that is of such significance that the fund manager is considered a principal, rather than an agent (for example 5%,10% etc). Nevertheless, some respondents observed that, with sufficient disclosure of the key assumptions and basis applied, in most cases the outcome is considered a reasonable application of principle-based standards.

One respondent also noted that it can be challenging to identify whether an agency relationship exists when the decision maker is a director or a related party of the investor. However, such situations are not encountered frequently.

### Question 3(b)

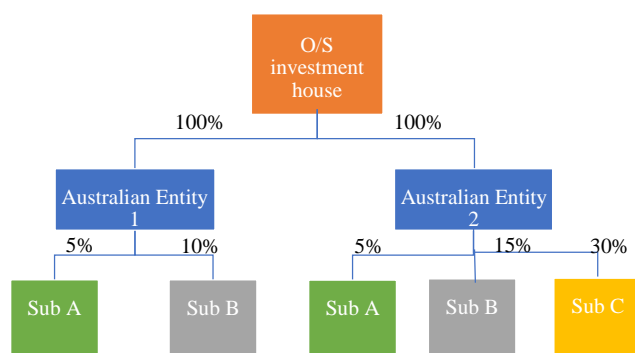
In your experience:

- (i) to what extent does applying paragraphs B73–B75 of IFRS 10 enable an investor to assess whether control exists because another party is acting as a de facto agent (ie in the absence of a contractual arrangement between the parties)?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 3(b)(i) arise?
- (iii) please describe the situations that give rise to such a need.

### AOSSG members' comments on Question 3(b)

#### [Australia]

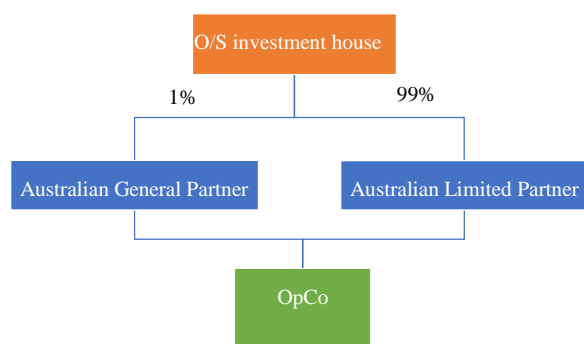
The feedback received from stakeholders highlighted that the question of de facto agency relationships is common in Australia, particularly in connection with cross-border ownership considerations. A common example for an Australian entity is where an overseas investment house invests in multiple entities in Australia and those Australian subsidiaries also have multiple investments, often in common investees (see example below).



As Australian Entity 1 and Australian Entity 2 are often required by local legislation to prepare financial statements, it will be necessary to determine how Australian Entity 1 and 2 should treat their investments in Sub A and Sub B. For example, if the remaining

shareholdings in Sub A and Sub B are dispersed, could the ultimate control by I/S investment house provide Australian Entities 1 and 2 with significant influence or should the investment be accounted for at fair value through the profit and loss. Alternatively, suppose the shareholdings in Sub A and Sub B are larger. In that case, it will be necessary to consider whether Australian Entity 1 is a de facto agent of Australian Entity 2 or vice versa such that either Australian Entity 1 or 2 may need to consolidate Sub A and Sub B. This will be difficult in particular, where there are no contractual arrangements in place.

Australia also understands that these arrangements can be structured using a limited partnership arrangement (see example below). In this simplified example, presume General Partner has all of the decision-making rights and Limited Partner has no decision-making ability).



The guidance in paragraph B74 indicates that in this situation, Australian Limited Partner may be required to consolidate OpCo, notwithstanding that they do not have any decision-making rights. This is because Australian Limited Partner has the most significant exposure to returns.

Australia acknowledges that the issue of whether any of the Australian entities would need to consolidate the subsidiaries/OpCo may not be an issue in other jurisdictions if the local intermediate investors are either not required to prepare and lodge financial statements, or could apply the consolidated exemption in paragraph 4 of IFRS 10. However, if this is a concern in other jurisdictions, Australia recommends that additional guidance may be warranted to make the requirements clearer.

**[Hong Kong]**

Hong Kong considers that the de facto agency guidance is well-meant, but it is hard to operationalise and it can be challenging to prove or disprove the existence of de facto agency relationships. This is particularly the case where there is a lack of contractual agreement. This issue is commonly seen among group companies and in the fund industry, and when SPE are involved. For example, power and returns may be split between different parties in closely

held funds or private equity structures for regulatory or tax planning purposes, in which case it is difficult to carry out the de facto agency assessment.

Hong Kong also considers that non-contractual agency relationships are difficult and controversial to assess. However, it is unavoidable as it does exist in practice. Hong Kong suggests the IASB consider whether it would be appropriate to set a rebuttable presumption or principle for assessing whether a de facto agency relationship exists in certain situation to minimise structuring opportunities.

#### [Japan]

- Preparers did not express any specific comments on the assessment of control based on the determination of the de facto agent.
- Auditors stated that paragraph B75 of IFRS 10 provides examples of parties that might act as de facto agents, but paragraphs B73 and B74 of IFRS 10 do not provide principles for determining when a party is considered to be a de facto agent, and the guidance is insufficient compared to other issues. Adding principles and specific guidance may reduce diversity in practice.

#### [Malaysia]

The respondents have not encountered issues on this area.

#### Question 4(a)

In your experience:

- (i) to what extent does applying the definition (paragraph 27 of IFRS 10) and the description of the typical characteristics of an investment entity (paragraph 28 of IFRS 10) lead to consistent outcomes? If you have found that inconsistent outcomes arise, please describe these outcomes and explain the situations in which they arise.
- (ii) to what extent does the definition and the description of typical characteristics result in classification outcomes that, in your view, fail to represent the nature of the entity in a relevant or faithful manner? For example, do the definition and the description of typical characteristics include entities in (or exclude entities from) the category of investment entities that in your view should be excluded (or included)? Please provide the reasons for your answer.

## **AOSSG members' comments on Question 4(a)**

### **[Australia]**

Feedback from Australian stakeholders confirmed that determining whether an entity is an investment entity by its nature is unnecessarily complex and that the requirements are difficult to apply in practice.

Stakeholders also raised the issue of potential inconsistencies within the Standard. For example, IFRS 10.27 contains mandatory elements when assessing whether or not an entity is an investment entity and IFRS 10.28 includes typical characteristics to consider. However, Appendix B notes that the typical characteristics need not be present. Stakeholders suggested that it is not clear how the mandatory elements interact with the typical characteristics, if the typical characteristics are not necessarily required to be present. For example, IFRS10.B85N indicates that the absence of one of the typical characteristics does not disqualify an entity from being classified as an investment entity. However, it does indicate that additional judgment is required.

If other stakeholders raise this matter, Australia recommends the IASB consider whether additional guidance is needed to clarify the interaction between the mandatory elements and the typical characteristics.

Australia further notes that the fair value appears to be inconsistent with accounting principles in other Standards. For example, the IASB decided that proportionate consolidation was not appropriate for joint ventures as the joint venture partner has rights to the net assets, and that proportionate consolidation is only appropriate where the investor has rights to the assets and liabilities of the investee. In contrast, in an investment entity scenario the investor has rights to, and controls, the assets and liabilities. However, fair value accounting was considered more appropriate than consolidation.

### *Disclosures*

Feedback from stakeholders expressed concern that fair value accounting does not provide users with the information they need. For example, two entities may appear to have consistent fair values, however, without information about the underlying net assets of the entities, the fair value may be misleading as one entity may be in the early stages of its life and may have good prospects. In contrast, the other entity may be in the declining phase of its life with decreasing market share and significant debt levels.

This lack of information is particularly concerning for listed investment entities, which Australia understands often have complex group structures involving multiple layers and overseas subsidiaries. Consider the following simplified example:



IE1 holds a 100% investment in SubParent1, which holds an investment in SubParent2, who holds an investment in SubParent3 who holds the underlying debt and equity investments. SubParents1-3 are often located in overseas jurisdictions and may not prepare IFRS-compliant financial statements.

IE1 is listed and is required to lodge financial statements with the securities regulator. IE1's financial statements show a single line item (its investment in SubParent 1 at fair value), which effectively represents its investment in SubParents 1, 2 and 3 as well as the investments held by SubParent3.

However, there is no detailed information about the nature of SubParent3's investments in IE1's financial statements and instead, users need to refer to the accompanying financial statements of SubParent3 to understand the risks that IE1 is exposed to through SubParent3's investments.

The Australian securities regulator, the Australian Securities Exchange (ASX) requires listed investment entities to provide the ASX with the financial statements of the investees and must also make those available to their shareholders on request.<sup>1</sup> Australia suggests the requirement to lodge accompanying financial statements supports concerns that investment entity accounting does not provide sufficient information to users.

While Australia notes that the IASB considered feedback about a potential loss in information when the proposals were developed, Australia suggests there may be merit in reconsidering the exception or even whether disclosures about the underlying net assets may be warranted. This is because users remain concerned about the lack of information provided by fair value accounting.

#### *Exit strategy*

Consistent with the feedback in the RFI, Australia received feedback from stakeholders suggesting that the requirements of the Standard are unclear in relation to a documented exit strategy. Australia understands that the lack of guidance is a concern in practice and Australia understands it is a common issue as it may give rise to structuring opportunities. For example, it is not clear whether there is an implied exit strategy where an entity has a limited life and must be wound up at the end of it. It is Australia's understanding that this is often accepted as meeting the requirements in IFRS 10. Similarly, is there an implied exit strategy where an investment must be redeemed after a certain period of time, which can be a

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<sup>1</sup> Listing Rules 4.8 and 4.8.1 require that if a listed entity's main asset are securities in an unlisted entity, the listed entity is required to give the ASX the latest accounts of the unlisted entity, together with any auditor's report or statement, when it gives the ASX its annual report. Australia understands that this information can be provided in local GAAP of the investee. The listed entity must also provide these financial statements to its security holders on request.



long time in the future? Australia understands this is also often accepted. However, would the conclusion change if the investment entity was able to make further investments after redemption of the original investment?

Feedback from stakeholders suggested that private entities may prefer fair value accounting and may therefore structure their operations to meet the investment entity requirements to avoid consolidation accounting and showing the values of the underlying net assets. For example, in this context, would an exit strategy that is to occur in 99 years be sufficient to conclude that the entity does not plan to hold the investment indefinitely? That is, is it a genuine plan for an exit and is there substance to that plan?

Australia notes that IFRS 10 allows for different exit strategies for different types of investments and provides some examples (e.g., IPO, private placement, trade sale, distribution of ownership interests in investees and sales of assets followed by a liquidation).

Australia also notes there is no guidance in IFRS 10 regarding assessing an exit strategy for substance or the level of documentation that is required to meet the requirements.

Further, Australia understands that the lack of clarity around what constitutes an acceptable exit strategy has led to diversity in practice.

Therefore, Australia recommends that if the investment entity exception is retained, the IASB clarifies the requirements for an exit strategy, including providing guidance about assessing whether a strategy is genuine.

#### **[Hong Kong]**

Hong Kong does not find the application of the investment entities consolidation exception to be common among Hong Kong entities. Having said that, some practice firms in Hong Kong audit investment entities that are incorporated overseas, and in general, they do not find significant issues with the criteria for identifying investment entities.

#### **[Japan]**

- No specific comments were received on the criteria for identifying an investment entity.

#### **[Malaysia]**

Respondents generally observed that they have not encountered issues with investment entities. Some noted that entities in Malaysia that provide investors with investment management services generally consolidated their investments, and they do not generally measure and evaluate the performance of the investments on a fair value basis.

**Question 4(b)**

In your experience:

- (i) are there situations in which requiring an investment entity to measure at fair value its investment in a subsidiary that is an investment entity itself results in a loss of information? If so, please provide details of the useful information that is missing and explain why you think that information is useful.
- (ii) are there criteria, other than those in paragraph 32 of IFRS 10, that may be relevant to the scope of application of the consolidation exception for investment entities?

**AOSSG members' comments on Question 4(b)****[Australia]**

See response to Question 4(a).

**[Hong Kong]**

Some respondents raised the concern about the loss of information about intermediate subsidiaries applying the investment entities consolidation exception. Some respondents suggested that the IASB reconsider the accounting for intermediate subsidiaries, particularly for those that are set up solely for tax purposes while others suggested that instead of changing the existing measurement approach, the IASB should consider requiring entities to provide additional disclosures about the intermediate subsidiaries to meet users' information needs.

Hong Kong noted difficulties in identifying a conceptual basis or a practical way to distinguish different types of subsidiaries that are investment entities. In this regard, Hong Kong considers that additional disclosure requirements would be helpful in solving the issues about the loss of information on intermediate subsidiaries and that the IASB could further explore on what information would be useful to users.

**[Japan]**

- No specific comments were received on the usefulness of the information on requiring an investment entity to measure its investments in a subsidiary at fair value. However, a user and a preparer requested the following amendments to IFRS 10 when a parent entity that is not an investment entity has a subsidiary that is an investment entity.
  - (1) When a non-investment entity parent holds an investment entity subsidiary who also has subsidiaries (sub-subsidiaries), and if the investment in the sub-subsidiary is held for trading, fair value measurement of the sub-subsidiary, rather than consolidation, reflects economic substance.

- (2) When an investment entity subsidiary invests in a manufacturing entity to earn capital gains and the investee is determined to be a subsidiary (sub-subsidiary), the consolidated financial statements of the non-investment entity parent may be misleading because they would be presented as if the parent company operated a manufacturing business. Therefore, the requirement not to retain fair value measurement of an investment entity subsidiary impairs the usefulness of information. The optional application of IFRS 9 *Financial Instruments* should be considered as in the exemption from the application of the equity method to an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities (including investment-linked insurance funds) in IAS 28 *Investments in Associates and Joint Ventures*.

**[Malaysia]**

See response to Question 4(a).

**Question 5(a)**

In your experience:

- (i) how frequently do transactions, events or circumstances arise that:
  - (a) alter the relationship between an investor and an investee (for example, a change from being a parent to being a joint operator); and
  - (b) are not addressed in IFRS Standards?
- (ii) how do entities account for these transactions, events or circumstances that alter the relationship between an investor and an investee?
- (iii) in transactions, events or circumstances that result in a loss of control, does remeasuring the retained interest at fair value provide relevant information? If not, please explain why not, and describe the relevant transactions, events or circumstances.

**AOSSG members' comments on Question 5(a)**

**[Australia]**

Stakeholders provided feedback that they frequently see transactions in which ownership interests change and they noted the following:

- There is a lack of guidance holistically across all types of transactions, and in particular where the transaction is not a business combination (because there is no business involved). For example, an equity accounted investment becoming a controlled investment, however as the investment does not represent a business there is no clear guidance on the accounting treatment.

Stakeholders noted that accounting for acquisitions that are not businesses is becoming more common as the revised definition of a business has resulted in more transactions being outside the scope of IFRS 3 *Business Combinations*. Additionally, the indefinite deferral of amendments made to IFRS 10 and IAS 28 *Investments in Associates and Joint Ventures* in 2014 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* has retained diversity in practice.

- Another example of challenging transactions are those in which two investors are contributing into a joint arrangement and one investor contributes a business but the other investor contributes assets that do not constitute a business.

Australia acknowledges that the IASB has previously considered accounting for changes in ownership interests, including the introduction of requirements to address accounting for a situation in which a parent loses control of a subsidiary and retains an interest in an associate (refer IFRS 10.25). The IFRS Interpretations Committee was also asked to consider whether previously held interests in the assets and liabilities of a joint operation should be remeasured in certain transactions that do not meet the definition of a business.

However, feedback from stakeholders suggests that gaps remain in the principles that make accounting for such transactions challenging, which may also lead to diversity in accounting outcomes. For this reason, Australia recommends the IASB consider expanding the principles in IFRS Standards to address accounting for changes in ownership interests more holistically which would increase consistency. Australia also thinks it would be useful for these principles to include accounting for transactions that do not constitute a business as transactions as these types of transactions are becoming more common for the reasons outlined above.

### **[Hong Kong]**

Hong Kong recommends that the IASB clarify the accounting for loss of control over single-asset entities, specifically how the guidance in IFRS 10.25(b) interacts with the recognition of gains/loss in other standards, in particular whether the requirement is applicable to disposals of a subsidiary when the subsidiary does not constitute a business.

There is diversity in practice in accounting for a partial disposal of a subsidiary that results in a loss of control where the subsidiary does not constitute a business. Some entities remeasure the retained interest (being an associate or a joint venture) at fair value applying IFRS 10.25(b), while others adopt a cost-based approach (i.e. no remeasurement).

Companies applying a cost-based approach generally believe that there should be symmetry between how an acquirer and a seller account for such a transaction – either as a

purchase/sale of shares or a purchase/sale of assets, with the assessment of whether the subsidiary constitutes a business driving that decision.

Even though the guidance in IFRS 10.25(b) and B98(b)(iii) does not distinguish between subsidiaries that are businesses from those that are not, practice has emerged to take this factor into account in part due to the introduction of the ‘business or non-business’ concept, from a *seller’s* perspective, in the *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28).

Transactions involving single-asset entities/corporate wrappers (i.e. a company that is set up solely to hold an asset) are common in the real estate industry in Hong Kong and China. Some stakeholders considered that applying IFRS 10.25(b) in such cases to recognise a net gain/loss instead of applying IFRS 15 to recognise gross revenue and the related costs of sale may not always reflect the substance of the transaction or provide useful information to users.

Many respondents questioned the technical analyses and the apparent lack of consistency between the IFRS Interpretations Committee’s conclusions on submissions about the sale of a subsidiary to a customer<sup>2</sup>, and sale and leaseback of an asset in a single-asset entity<sup>3</sup>. Accordingly, Hong Kong recommends that the IASB consider the accounting for transactions involving single-asset entities more holistically in this project.

Additionally, for an asset deal, questions often arise as to whether an entity remeasures the previously held equity interest in the acquiree or applies a cost-based approach (i.e. no remeasurement of previously held equity interest). Hong Kong suggests that the IASB provide more guidance on this area.

## [Japan]

### **(Transactions that change the relationship between an investor and an investee that are not addressed in IFRS Standards)**

- Preparers noted the following:
  - (1) There have been no transactions that change the relationship between an investor and an investee that are not addressed in IFRS Standards.
  - (2) Accounting for a change from a parent company to a joint operator is not addressed in IFRS Standards, but in this case, the retained interest is considered to be remeasured at fair value.
  - (3) Although they have not occurred frequently, transactions that are not addressed in

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<sup>2</sup><https://cdn.ifrs.org/-/media/feature/meetings/2020/june/iasb/ap12a-maintenance-and-consistent-application.pdf>

<sup>3</sup><https://cdn.ifrs.org/-/media/feature/meetings/2021/february/ifric/ap02-sale-and-leaseback-of-an-asset-in-a-single-asset-entity.pdf>

IFRS Standards have occurred, such as changes between a parent company and a joint operator and between a joint operator and a party to a joint operation.

- (4) The retained interest would be remeasured when the change was between a parent company and a joint operator if it constituted a business and the retained interest would not be remeasured if it did not constitute a business. A change between a joint operator and a party to a joint operation would not be remeasured. It would be desirable to develop accounting requirements in IFRS Standards systematically, including the clarification of whether remeasurement would depend on whether the investee constitutes a business.
- Auditors commented that there is no fixed effective date for the amendment to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28), which sets out the accounting for the loss of control over a subsidiary that does not contain a business as a result of a transaction with an entity accounted for using the equity method of accounting. Auditors suggested that the status of these amendments be re-examined.

**(Usefulness of the information on gains or losses arising from interests retained on the loss of control and arising from previously held interests on step acquisitions)**

- One user noted that the user was comfortable with fair value measurement because the acquisition of control changes the degree of management involvement, but the information would not be useful unless the assumptions used to determine fair value were disclosed.
- Other users commented that remeasurement at fair value would not provide relevant information:
  - (1) The construct of the transaction, treating it as if all interests were sold at fair value and reacquired departs from the actual economic activity. The construct of the transaction, which is inconsistent with the views of the investors, reduces the usefulness of the profit or loss information.
  - (2) Investors consider that the amount of investment required to acquire control through a step acquisition would be the cumulative amount of expenditure. The existing accounting requirement is to remeasure the existing interests when control is obtained. When a gain is recognised from remeasurement and goodwill is recognised, the amount of investment required to acquire control would include amounts that were not actually invested. Accordingly, such information would not contribute to forecasting future performance and is not useful for analysis.
  - (3) When an entity elects, at the time of loss of control, to present subsequent changes in fair value in other comprehensive income under IFRS 9 for the retained interest, the

gain or loss arising from the remeasurement of that interest to fair value at the time of the loss of control would be recognised in profit or loss rather than in other comprehensive income.

- On the other hand, preparers held diverse views on the usefulness of the information in remeasuring the retained interest at fair value at the time of loss of control, mainly due to the different perspectives on their involvement with their subsidiaries and associates. Similarly, although it is not the subject of this RFI, preparer held diverse views step acquisitions under IFRS 3.
- The views of preparers who commented that remeasurement at fair value does not provide relevant information were as follows:
  - (1) An investment held through the exercise of significant influence over an associate and an investment held through control of a subsidiary do not differ in the nature of an investment in that the investor holds these interests for the purposes of conducting business activities through the involvement in the investees and to achieve results from such involvement. The nature of the investment does not change when control is lost and a subsidiary becomes an associate and, therefore, measuring the retained interests at fair value as if the nature of the investment had changed, does not provide relevant information.
  - (2) When an entity continues to retain significant influence as an equity method associate after the loss of control, and there is no intention to sell the entity, it would be difficult to say that the remeasurement gain represents the company's performance, and it would also prevent presenting the inherent performance of the entity. For the same reason, remeasurement at fair value of the previously held equity interests in a step acquisition when the associate becomes a subsidiary would not provide the relevant information.
  - (3) As a result of recognising remeasurement gains, the carrying amount of the equity method investment would be increased. That unintentionally exposes the entity to impairment risk after the loss of control, and the profit or loss on equity method investments would not represent the economic substance.
  - (4) It is difficult to appropriately assess the fair value of the retained interests.
- The views of preparers who commented that remeasurement at fair value provides relevant information were as follows:
  - (1) Involvement in subsidiaries and involvement in associates are different. There is a difference between managing the subsidiary as a controlling shareholder in an integrated manner and managing an associate in such a way that an associate



contributes to the group's business by exercising significant influence.

- (2) Therefore, when an involvement in an associate changes to an involvement in a subsidiary, quantitatively confirming the investment outcome resulting from the previous involvement by remeasuring at fair value makes certain sense.
  - (3) Also, the concept of treating the previously held interest as sold and re-acquired at fair value is not uncomfortable.
  - (4) If the previously held interest is not remeasured in a step acquisition, the information would be misleading for the users because the accounting outcome for a one-step acquisition and a multi-step acquisition would be different even though the economic effect of the acquisition (that is, the entity obtaining control) is the same.
- Regardless of the views taken above, preparers stated that the gain or loss resulting from the remeasurement is treated separately from profit and loss from ordinary activities as a one-off gain or loss.

#### [Malaysia]

The respondents have not encountered issues on this area in relation to IFRS 10 and 11.

However, some respondent noted that IAS 27 is silent on accounting for step acquisitions and measurement of a retained interest in an investee on loss of control when applying the cost model in the separate financial statements. In the absence of specific requirements in IAS 27, diversity can arise in practice resulting in a lack of comparability. In its January 2019 Agenda Decision Investment in a subsidiary accounted for at cost: Step acquisition (IAS 27 *Separate Financial Statements*) the IFRS Interpretations Committee observed that IAS 27 does not define 'cost', nor does it specify how an entity determines the cost of an investment acquired in stages. Based on its analysis, the Committee concluded that a reasonable reading of the requirements in IFRS Standards could result in the application of either a fair value as deemed cost approach or accumulated cost approach.

One stakeholder stated its view that remeasuring the retained interest at fair value does not provide relevant information because that part of the interest is not sold or otherwise realised. However, another stakeholder commented that remeasuring the retained interest at fair value provides relevant information because it reflects the current valuation of the investment, which is consistent with the requirements in IFRS 3 *Business Combinations*.



**Question 5(b)**

In your experience:

- (i) how do entities account for transactions in which an investor acquires control of a subsidiary that does not constitute a business, as defined in IFRS 3? Does the investor recognise a non-controlling interest for equity not attributable to the parent?
- (ii) how frequently do these transactions occur?

**AOSSG members' comments on Question 5(b)**

**[Australia]**

See response to Question 5(a).

**[Hong Kong]**

Hong Kong does not find this accounting issue to be persuasive in Hong Kong.

**[Japan]**

**(Partial acquisition of a subsidiary that does not constitute a business)**

- One preparer stated that transactions to acquire control of a subsidiary that does not constitute a business occur only rarely, but when they do, non-controlling interests are recognised.
- Another preparer stated that although non-controlling interests are recognised in transactions that acquire control of a subsidiary that does not constitute a business, reconsideration may be needed as to whether it is relevant to require the same accounting treatment for a subsidiary that constitutes a business and a subsidiary that does not constitute a business.

**(Accounting for a single asset entity)**

- One preparer commented on the accounting treatment of a single asset entity as follows:
  - (1) Although such transactions have not been frequent, when a real estate is held through a trust to which IFRS 10 is applied, and a portion of the entity is sold to a third party and control is maintained, any difference between the consideration and the carrying amount would be recognised in equity rather than in profit or loss. This accounting does not represent the economic substance of the transaction, which is a partial sale of the real estate. This implies that the scope of IFRS 10 may be too biased towards the form of the transaction.
- Auditors commented as follows:

- (1) Whether assets held by a subsidiary should be accounted for as assets held directly by the parent or as an entity that is a subsidiary under IFRS 10 is not systematically addressed in IFRS Standards. Therefore, there are practical issues in many contexts (for example, the measurement of variable consideration and partial sale of an interest without loss of control). It is necessary to provide guidance in IFRS Standards rather than providing guidance in the form of agenda decisions, which do not constitute IFRS Standards.

**[Malaysia]**

While respondents noted such transactions are rare, the following observation and view were shared.

Two respondents noted that if an entity acquires control of a subsidiary that does not constitute as business as defined in IFRS 3, the entity accounts for transaction as an asset acquisition in accordance with paragraph 2 of IFRS 3. The consideration paid is allocated to the identifiable asset and liabilities acquired on the relative fair value basis. If the acquired subsidiary is not wholly-owned (whether it is a business or not a business), any non-controlling interest is recognised separately.

One respondent noted that such transactions can occasionally arise when the acquiree is a start-up company that does not yet meet the definition of a business, or is a shell-company that only holds assets and does not have substantive activities.

**Question 6**

In your experience:

- (a) how widespread are collaborative arrangements that do not meet the IFRS 11 definition of 'joint arrangement' because the parties to the arrangement do not have joint control? Please provide a description of the features of these collaborative arrangements, including whether they are structured through a separate legal vehicle
- (b) how do entities that apply IFRS Standards account for such collaborative arrangements? Is the accounting a faithful representation of the arrangement and why?

**AOSSG members' comments on Question 6 (including general comments on IFRS 11)**

**[Australia]**

Australia received feedback that collaborative arrangements are common in Australia. For example, there are many instances where there are multiple investors and the agreement does not state which investors must agree and therefore which investors control the arrangement as decisions are made based on majority votes. In these situations, as the agreement does not

require unanimous consent or gives one investor the ability to direct the decision-making (i.e., control) many collaborative arrangements are outside of the scope of IFRS 11.

Australia understands that in most cases, despite the lack of joint control, the investors have the same underlying rights to the assets and liabilities as they would if unanimous consent was required, so often the accounting treatment is analogised to the accounting for joint operations in IFRS 11. Australia understands that this treatment is very common in Australia, particularly in the extractives industry, as this approach reflects the substance of the arrangement (e.g., to recognise the investor's share of the assets and liabilities as that is what the investor has rights to). This treatment is also consistent with the accounting by an investor who participates in a joint arrangement but does not have joint control per IFRS 11.23.

### [China]

**Collaborative arrangements that do not meet the definition of “joint arrangement”:** collaborative arrangements are common in practice due to lack of joint control and thus do not qualify as joint arrangement as defined in IFRS 11, especially in film and media industry, research and development in pharmaceutical and biotechnical industry and real estate development industry. For example, when two parties conduct a business together, one party is responsible for and directs some of the related activities, and the other party is responsible for and directs other part of the related activities. Both parties share the return of the business. Although contractually this arrangement may not meet the definition of joint control, it has a lot in common with the joint arrangement described in IFRS 11. Further guidance is needed for this kind of arrangement.

### [Hong Kong]

Hong Kong observed that collaborative arrangements that are outside the scope of IFRS 11 are common in the pharmaceutical industry and entertainment industry in Hong Kong. It is often very difficult to characterise the arrangements appropriately, i.e. is it a joint arrangement, an associate, an equity investment under IFRS 9 *Financial Instruments*, a debt-type loan, a supplier-customer relationship, a prepayment for future expenditure, etc?

In some cases, these collaborative arrangements are not joint arrangements as defined because there is more than one combination in which the required level of votes can be achieved, for example, when regulation requires votes to be cast by independent directors or employees who are not shareholders of the arrangement. These arrangements are often project-based and may not necessarily be structured through a separate legal entity, and they are often accounted for as an associate or as a financial asset under IFRS 9 depending on

facts and circumstances. Respondents, however, considered that such an outcome does not provide useful information.

As most respondents considered that to account for such a collaborative arrangement similar to a joint operation would more faithfully represent the substance of the arrangement, Hong Kong recommends that the IASB develop clear principles for collaborative arrangements to better reflect the substance of the arrangement.

#### **[Japan]**

- Preparers noted the following related to collaborative arrangements outside the scope of IFRS 11:
  - (1) There are arrangements with third parties, such as general business partnerships, which are entered into for the purposes of exchanging information, the engaging in commercial activities and pursuing synergies. However, these arrangements are not subject to special accounting treatments.
  - (2) When the entity is considered to have joint rights to the assets and joint obligations for the liabilities through a vehicle that is not a legal entity, the assets and liabilities are recognised in proportion to the interests, by analogy to the accounting requirements for joint operations in IFRS 11.
- On the other hand, some preparers commented on the scope of joint operations as follows:
  - (1) There are concerns about the scope of joint operations – the determination can be different depending on whether the investment is made directly or through an entity.
  - (2) There are concerns about the scope of joint operations – the determination is too dependent on the legal form of the investment and the existence of explicit contractual arrangements.

#### **[Malaysia]**

Respondents have not encountered such situations that are not covered under IFRS 11 or IAS 28.

#### **[Pakistan]**

##### ***IFRS 11 Joint Arrangements***

In Pakistan, Pakistan does not face any major difficulties for the application of IFRS 11. The existing guidance in IFRS 11 is sufficient to determine joint operations and joint ventures, however, Pakistan would welcome further illustrative examples on areas of Standard that involve significant judgments.

### Question 7

In your experience:

- (a) how frequently does a party to a joint arrangement need to consider other facts and circumstances to determine the classification of the joint arrangement after having considered the legal form and the contractual arrangement?
- (b) to what extent does applying paragraphs B29–B32 of IFRS 11 enable an investor to determine the classification of a joint arrangement based on ‘other facts and circumstances’? Are there other factors that may be relevant to the classification that are not included in paragraphs B29–B32 of IFRS 11?

### AOSSG members’ comments on Question 7

#### [Australia]

Feedback from Australian stakeholders suggested that there may not be sufficient guidance on what constitutes a separate vehicle. For example, in practice, feedback suggested that a significant amount of time is spent assessing whether partnerships and unincorporated joint venture arrangements are considered separate legal vehicles.

While determining whether a partnership is a separate vehicle is beyond the remit of Standard-Setters and may vary by jurisdiction, Australia understands that the guidance to determine what constitutes a separate vehicle is insufficient in practice. For example, if an unincorporated joint venture keeps its own books and records, would it be considered a separate vehicle.

Australia acknowledges that divergence exists in accounting for such arrangements as each arrangement is assessed based on its own individual facts and circumstances. However, because determining whether a separate legal vehicle exists can be complex, Australia recommends that the IASB considers providing principles regarding what factors should be considered. This may reduce diversity in practice and therefore, there may be a practical benefit in the IASB considering this.

#### [Hong Kong]

Respondents shared that it is common that one has to consider ‘other facts and circumstances’ to determine the classification of joint arrangements in the oil and gas industry, real estate industry and telecommunications industry.

Respondents generally find the consideration of ‘other facts and circumstances’ difficult to apply in practice as it is subjective and allows for structuring. It allows management to override the contractual provisions by asserting through facts and circumstances that the parties to the arrangement have or do not have rights to the net assets, hence changing the

joint venture/ joint operation classification to achieve a desired outcome, e.g. when a joint operation makes losses they could argue there has been a change in facts and circumstances to reclassify the arrangement to a joint venture to stop recognising further losses under the equity accounting method, and vice versa.

On the other hand, it is often difficult for auditors to use ‘other facts and circumstances’ to challenge management’s classification based on the legal form and contractual terms of the arrangement.

In light of the above, Hong Kong recommends that the IASB provide more detailed guidance that can be objectively applied in this regard.

#### **[Japan]**

- One preparer commented that the guidance on 'other facts and circumstances' in IFRS 11 is helpful, for the classification of joint arrangements, but only to a limited extent, because it is intended to cover specific cases. None of the preparers Japan interviewed, including this preparer, identified issues that warrant amendments to IFRS Standards.

#### **[Malaysia]**

One respondent had encountered situations requiring consideration of other facts and circumstances to determine the classification of the joint arrangement. This respondent observed that there were no challenges in applying the requirements. Other respondents have not encountered such situations.

Respondents did not identify other factors that may be relevant to the classification that are not included in paragraphs B29–B32 of IFRS 11.

#### **Question 8**

In your experience:

- to what extent does applying the requirements in IFRS 11 enable a joint operator to report its assets, liabilities, revenue and expenses in a relevant and faithful manner?
- are there situations in which a joint operator cannot so report? If so, please describe these situations and explain why the report fails to constitute a relevant and faithful representation of the joint operator’s assets, liabilities, revenue and expenses.

#### **AOSSG members’ comments on Question 8**

#### **[Australia]**

Many users suggested that in their view, proportionate consolidation provides more useful information at the statement of financial position, cash flow and income statement levels than

the equity-accounting approach. This is the case, even if the proportionately consolidated information is aggregated. In their view, the presentation of information in a single line as is required for the equity method of accounting is a concern because it does not provide a complete picture of the investee.

Australia understands that some of these concerns arise from applying the equity method of accounting, for example, that losses are not always recognised even when it is likely that an investor may be required to fund these losses at least in part. However, Australia recognises that addressing concerns about the equity method of accounting is beyond the scope of this project and may be better considered as part of the IASB's research project on the equity method of accounting.

Australia also acknowledges the IASB's comprehensive deliberations on the issue of proportionate consolidates versus the equity method of accounting, including the IASB's previous view that eliminating proportionate consolidation would not cause a loss of information for financial statement users. This was because the IASB expected the disclosures required by IFRS 12 when compared with what was required by IAS 31 *Interests In Joint Ventures* would improve the quality of the information provided to users relating to an entity's interest in joint ventures.

However, while paragraphs B12 and B13 of IFRS 12 require the disclosure of summarised financial information for each joint venture and associate that is material to the reporting entity, feedback from users indicated that they need more detailed information about the underlying assets and liabilities of the investee to allow them to estimate their market value. Specifically, users indicated that they would like to see more granular information about the performance, cash flows and debt position of significant equity-accounted investments. Australia notes that this was previously raised by respondents to ED 9 *Joint Arrangements* and dismissed by the IASB at the time.

Therefore, Australia suggests that if similar feedback about the proportionate consolidation method is received from other jurisdictions, the IASB may wish to consider a research project on the benefits and disadvantages of the equity method versus the proportionate consolidation method as it may provide useful insights as to whether the IASB's previous decisions may need to be ultimately revisited.

Australia also recommends that if the IASB decides not to revisit allowing the proportionate consolidation method, the IASB revisit the disclosures under IFRS 12 to consider whether users should be provided with more detailed information about an entity's interests in equity-accounted investments.

### [Hong Kong]

Hong Kong noted from the respondents that joint operations are common only in specific industries and therefore application issues of accounting for joint operations are not pervasive in Hong Kong.

Be that as it may, Hong Kong has noted that there may be certain cases where accounting requirements for joint operations may be insufficient and lacking in guidance on how to determine the joint operator's share of assets, liabilities, revenue and expenses. This is particularly the case when the joint operator's share of output purchased differs from its share of ownership interest in a joint operation (the IFRIC March 2015 Agenda Decision only highlighted the importance of understanding the difference between the two without providing further guidance), which may lead to diversity in practice.

### [Japan]

- Preparers commented that they had not identified any issues with the accounting requirements for joint operations.
- Auditors stated that agenda decisions provide guidance on a number of practical issues, but the guidance should be included in IFRS Standards, not in agenda decisions.

### [Malaysia]

One stakeholder submitted a comment letter expressing concerns about the IFRS Interpretations Committee conclusions in the March 2019 Agenda Decision, Liabilities in relation to a Joint Operator's Interest in a Joint Operation (IFRS 11 *Joint Arrangements*) comments and the interaction of IFRS 11 and IFRS 16 for joint operations.<sup>4</sup> In particular, this stakeholder explained its view that the lead operator should only recognise its share of the liability, rather than 100% of the liability, to reflect the economic substance and contractual obligations of the arrangement. This stakeholder has resubmitted its comments for consideration as part of this Post-Implementation Review.

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[http://eifrs.ifrs.org/eifrs/comment\\_letters//508/508\\_25032\\_FirdausTarmiziPETRONAS\\_0\\_PETRONASLettertoIASB.pdf](http://eifrs.ifrs.org/eifrs/comment_letters//508/508_25032_FirdausTarmiziPETRONAS_0_PETRONASLettertoIASB.pdf)



### Question 9

In your experience:

- (a) to what extent do the IFRS 12 disclosure requirements assist an entity to meet the objective of IFRS 12, especially the new requirements introduced by IFRS 12 (for example the requirements for summarised information for each material joint venture or associate)?
- (b) do the IFRS 12 disclosure requirements help an entity determine the level of detail necessary to satisfy the objective of IFRS 12 so that useful information is not obscured by either the inclusion of a large amount of detail or the aggregation of items that have different characteristics?
- (c) what additional information that is not required by IFRS 12, if any, would be useful to meet the objective of IFRS 12? If there is such information, why and how would it be used? Please provide suggestions on how such information could be disclosed.
- (d) does IFRS 12 require information to be provided that is not useful to meet the objective of IFRS 12? If yes, please specify the information that you consider unnecessary, why it is unnecessary and what requirements in IFRS 12 give rise to the provision of this information.

### AOSSG members' comments on Question 9

#### [Australia]

Stakeholder feedback, predominantly from the user community, suggested that additional disclosures are required in certain areas (see below). Australia does, however, recommend that the IASB fully test any proposed increases in disclosures to ensure that they are useful to a significant number of users and are not the request of a very small number of constituents.

#### **Subsidiaries and non-controlling interests**

Feedback from users suggested that there is often not enough information about subsidiaries with non-controlling interests (NCI) and whether there are any significant restrictions. For example, suppose a significant portion of a company's value is tied up in its controlling stake in an overseas company. In that case, it is often unclear how much of the subsidiary's cash could actually be distributed to the parent. While Australia acknowledges that IFRS 12 does require disclosures about significant restrictions, this disclosure relates only to statutory, contractual and regulatory restrictions. Users indicated they would also like to see information about other forms of restrictions that could prevent accessing the subsidiary's assets. For this reason, Australia recommends the IASB consider broadening the scope of the disclosures required by paragraph 13 of IFRS 12 regarding the nature and extent of significant restrictions to include other forms of restrictions such as economic restrictions.

Users also highlighted that disclosures of ownership interests and the profit contribution of subsidiaries in paragraph 12 of IFRS 12 without information on cashflows, can be of limited value. This is because profit information alone doesn't always give a complete picture of the subsidiary's operations. For this reason, subject to other jurisdictions providing consistent feedback, Australia recommends the IASB consider requiring disclosure of a subsidiary's cash flows contribution in addition to the subsidiary's profit contribution.

### **Dilution of ownership interests due to outstanding shares**

Users expressed concerns that they are not getting sufficient information about the possible dilution of an entity's ownership interest due to outstanding shares. That is, users wanted disclosures to help them understand whether an NCI or another investor could exercise outstanding options that would reduce the entity's ownership interest in a subsidiary, associate or joint venture. For example, where the financial statements disclose a 25% ownership interest in an investee, however there may be significant rights over shares outstanding that, if exercised, can materially change (dilute) the investor's ownership interest in the investee.

Australia notes that paragraph 79 of IAS 1 *Presentation of Financial Statements* requires the disclosure of shares reserved for issue under options and contracts. However, this disclosure only applies to shares of the entity preparing the financial report, not to shares of its investees. As there are no requirements in IFRS 12 to provide similar information in relation to subsidiaries, associates and joint ventures, Australia recommends the IASB consider whether this disclosure should be required to provide users with the information they require.

### **Individually immaterial equity accounted investments**

Feedback from users indicated that they do not always receive sufficient information about individually immaterial equity-accounted investments. They suggested it could be helpful to disclose:

- aggregated information about the financial performance and financial position of individually immaterial equity-accounted investments;
- the number of immaterial equity-accounted investments included in the aggregated disclosure; and
- the names of any individually immaterial equity-accounted investments that represent more than 10% of the aggregate of the individually immaterial total (e.g., if the revenue or total assets of any of the individually immaterial equity-accounted investments represents more than 10% of the aggregated total of all individually immaterial equity-accounted investments the name of the investee should be disclosed)

Australia recommends the IASB consider aligning the disclosure of individually immaterial equity-accounted investments (in aggregate) with those required for individually material

equity-accounted investments. Users suggested that requiring disclosures about individually immaterial equity-accounted investments representing more than 10% of the aggregate of the individually immaterial total may be helpful. Australia notes that disclosure of this is consistent with the quantitative threshold used in paragraph 34 of IFRS 8 *Operating Segments* regarding reliance on major customers, however the cost versus benefit of this disclosure should be considered.

Australia acknowledges the importance of balancing the user need for information with disclosure overload, especially as these investments are judged to be individually immaterial by the entity. However, Australia suggests there may be situations where quantitatively investments may be individually immaterial, however, they may be material by nature. For example, a newly acquired investment in a previously unestablished jurisdiction could signal a change in an entity's future strategic direction. An interest in a long-term contract that is in the early stages may also be immaterial, however, it may provide meaningful information as it highlights a future capital commitment. In each of these examples, an investment in the early stages is likely to be quantitatively immaterial. However, the substance and the potential future commitment and cash flows may be quite material by nature to an investor's understanding of the arrangement. Australia understands that often the disclosures required by paragraph B16 of IFRS 12 focus on quantitatively individually immaterial investments. However, Australia suggests it is important to clarify how an assessment of material by nature corresponds with this assessment.

#### [China]

**Disclosure of interest in other entities:** how to determine “material” associates or joint ventures when disclosing the related information in accordance with IFRS 12.

#### [Korea]

Many respondents said that many companies fail to faithfully apply the requirements in IFRS 12 in practice.

- Control assessment usually involves highly subjective judgment. Therefore, companies need to disclose information used in making their judgment for users to understand their rationale, and to this effect, IFRS 12 already requires such information.
- However, Korea has noted that many companies fail to faithfully apply the requirements in IFRS 12 in practice. For example, many companies tend to simply disclose their judgment itself, saying that they do not control another entity even though they hold more than half of the voting rights, without mentioning any concrete reason behind the judgment made.

Some respondents recommend setting out illustrative examples in IFRS 12 to encourage faithful disclosure. They believe that illustrative examples will help improve the disclosing practice.

### **[Hong Kong]**

Hong Kong considers that the disclosure requirements in IFRS 12 are adequate.

### **[Japan]**

#### **(Disclosures of subsidiaries with material non-controlling interests)**

- Users commented on the disclosures of subsidiaries with material non-controlling interests as follows:
  - (1) The current disclosures for subsidiaries with material non-controlling interests are useful in that they provide the information about the dividends flowing outside the group. However, detailed cash flow information is needed to analyse cash flows excluding the cash flow attributable to non-controlling interests.
  - (2) Disclosures are provided only when the preparer considers the non-controlling interests to be material. Requiring disclosure of the criteria for determining materiality would be useful.
- Preparers commented on the disclosures relating to subsidiaries with material non-controlling interests as follows:
  - (1) Japan does not understand how the information is used by users and the usefulness of the information is questionable.

#### **(Disclosures of associates and joint ventures)**

- One user commented on the disclosures of associates and joint ventures as follows:
  - (1) The disclosure of the total amount of dividends received from equity method investments is needed to analyse the cash contribution from all equity method investments, not only from joint ventures or associates that are material to the entity (paragraph B12(a) of IFRS 12).
- Preparers made the following comments on the disclosures of joint ventures and associates that is material:
  - (1) There have been no discussions with users, including investors, related to the disclosure of material associates and joint ventures. However, there is a cost for determining the materiality threshold, and the usefulness of the information compared to such costs is questionable.

- (2) The information to be disclosed and the usefulness of the information is limited when there are regulatory restrictions on disclosures of a listed company (as discussed in the agenda decision in January 2015 of the IFRS Interpretations Committee), or when the consent of the other partners to the disclosures cannot be obtained.
- Preparers also made the following comment on the disclosures of immaterial associates and joint ventures:
    - (1) There is no material information value in disclosing the aggregate carrying amount of interests in associates and joint ventures, and disclosing separately the aggregate amount of interests in associates and joint ventures that are individually immaterial.

**(Disclosures of interests in unconsolidated structured entities)**

- Some preparers made the following comments on the disclosures of interests in unconsolidated structured entities:
  - (1) The definitions of ‘structured entity’, ‘maximum exposure’ (paragraph 29 of IFRS 12) and ‘sponsor’ (paragraph 27 of IFRS 12) in the IFRS Standards are not clear.
  - (2) It is practically impossible to identify all unconsolidated structured entities.
  - (3) Relating to the disclosures of interests in unconsolidated structured entities (paragraphs 24 to 31 of IFRS 12), it would be useful to provide information only for those depending on the level of involvement and the materiality of the risk, rather than for all interests in unconsolidated structured entities.
  - (4) The interests in unconsolidated structured entities may be recognised in the consolidated balance sheet in accordance with other IFRS Standards. In addition, there is some overlap with the disclosure requirements for contingent liabilities and for the risks arising from the financial instruments under IFRS 7 *Financial Instruments: Disclosures*, which increases costs.
  - (5) The disclosure of sponsorship in interests in unconsolidated structured entities (paragraph 27 of IFRS 12) needs to be revised. It is questionable that the objective of this disclosure, which is to provide a sense of the extent of the entity’s reliance on unconsolidated structured entities (paragraph BC90 of IFRS 12), is achieved by disclosing information about income from structured entities and assets transferred to structured entities.

**(Other disclosures)**

- One user commented that the scope of consolidation involves significant judgement and, therefore, the materiality thresholds for consolidation should be disclosed when there are subsidiaries that are not consolidated.

- Auditors noted that the extent of the disclosure is determined based on the disclosure objective of IFRS 12, but the disclosure objective is not sufficiently clear to encourage proactive disclosures. Improvement is needed in light of the disclosure projects currently undertaken by the IASB.

### [Malaysia]

Respondents were generally of the view that the IFRS 12 disclosure requirements are sufficient to satisfy the objective of IFRS 12. However, one stakeholder felt that the disclosures are onerous.

Two respondents questioned whether the requirement in paragraph B16 of IFRS 12 to disclose aggregate information about individually immaterial joint ventures or associates provides useful information for users. One noted in particular that the nature of the investments' businesses could be different.

Paragraphs B13(b)-(c) of IFRS 12 require that for each material joint venture the reporting entity discloses the amount of current and non-current financial liabilities (excluding trade and other payables and provisions). One respondent suggested that the entity should also be required to identify the amount of interest-bearing borrowings within paragraphs B13(b)-(c) to assist users in determining the entity's gearing level.

Another respondent also queried the rationale for requiring the summarised financial information required by paragraph B10(b) of IFRS 12 to be the amounts before inter-company eliminations (paragraph B11 of IFRS 12).

### [Pakistan]

#### ***IFRS 12 Disclosure of Interests in Other Entities***

Pakistan notes that the existing disclosure requirements of IFRS 12 regarding subsidiaries, joint arrangements and associates are adequate and useful.

<b>Question 10</b>
Are there topics not addressed in this Request for Information, including those arising from the interaction of IFRS 10 and IFRS 11 and other IFRS Standards, that you consider to be relevant to this Post-implementation Review? If so, please explain the topic and why you think it should be addressed in the Post-implementation Review.

#### **AOSSG members' comments on Question 10**

### [Australia]

Australia does not have any further comments.

**[China]**

**Other topics:** with regard to the scope, there were cross-cutting concerns about IFRS 10, IFRS 15 and IFRS 16, which standard to apply and whether applying this standard can reflect the economic substance. For example, an entity disposes assets that held under a corporate wrapper in the form of disposal equity held in the corporate wrapper, and this transaction occurs in the course of the entity's ordinary business. For the transaction, should the entity recognize the disposal gain as investment income in accordance with IFRS 10 or recognize the disposal proceeds as revenue in accordance with IFRS 15? There is another example. An entity disposes a subsidiary but leases back the office buildings or properties from the disposed subsidiary, should the entity recognize full disposal gain in accordance with IFRS 10 or recognize the disposal gain only limited to the proportion of the total gain that relates to the rights transferred to the buyer-lessor in accordance with IFRS 16 at the same time?

**[Hong Kong]**

Hong Kong does not have further comments.

**[Japan]**

**(Equity method of accounting)**

- The equity method of accounting is not included in the scope of the RFI. However, when an investee is classified as a joint venture in accordance with IFRS 11, the equity method of accounting is applied and, therefore, in Japan's outreach Japan obtained views on the equity method of accounting.

Issues in equity method of accounting — impairment

- Most preparers commented on the issue of impairment accounting for equity method investments:
  - (1) As is the case with the investments in the consolidated subsidiaries, goodwill recognised in an equity method investment may involve the expectation of the synergies with the investee's business. However, accounting for impairment of the equity method investments differs from that for goodwill where control is held because the nature of the equity method of accounting is not determined by one-line consolidation. As a result, there are practical issues about the recognition of impairment losses.
  - (2) Regarding the recognition of impairment losses on investments in associates and joint ventures, IAS 28 only requires that such investments shall be tested for impairment as a single asset. The steps for impairment testing of the identifiable assets and goodwill which comprise the investment are not clear.



- (3) The lack of clarity in existing accounting standards on the nature of the equity method of accounting has led to fundamental problems about the impairment of equity method investments. Impairment may be double counted when the investor recognises the impairment on the carrying amount of the entire equity method investment followed by the impairment on individual assets or groups of assets in the investee's financial statements.
- (4) Based on paragraph 14A of IAS 28, the losses from the expected credit loss model under IFRS 9 and the losses from the equity method under IAS 28 could be double counted, which is problematic. Re-consideration including a fundamental review of the equity method of accounting is needed
- (5) When there is a minority discount in investing in a joint venture or an associate, a conflict may arise between the measurement of the 'inside' assets (including intangible assets recognised on acquisition of the investment) of the equity method investee as one-line consolidation, which does not take into account the minority discount, and the measurement of the equity method investment as a whole (the 'outside') which takes into account the minority discount.

#### Issues in equity method of accounting — other issues

- One preparer commented that, when the transaction price of an investment accounted for using the equity method is determined at its present value based on a budget to lose cash initial years but generate cash in future years, and the investee recognises losses as initially planned, it would be counterintuitive to recognise losses if the nature of the equity method of accounting is considered to be a measurement basis.

#### Comments on the equity method of accounting

- Regarding the current equity method of accounting, users and some preparers raised concerns about the scope of the equity method of accounting. Furthermore, some users and preparers noted that dividend income information supplements the assessment of the investments in addition to the information provided by the equity method of accounting. Moreover, one preparer noted that the application of the equity method accounting to investments held for the purposes of expecting increases in value of such investments (financial investments) does not provide useful information.
- However, most preparers stated that the equity method of accounting provides useful information for investments that are more in the nature of an investment as an extension of consolidation and reflect the performance of the investee, because they consider that these investments are held for the purposes of conducting business activities through the involvement in the investees and to achieve results from such involvement.

- Most of those Japan reached out to did not ask for significant changes from the existing guidance, but highlighted the practical issues that cannot be resolved under existing guidance because such guidance did not provide a conceptual basis regarding the nature of the equity method of accounting, that is, whether it is a one-line consolidation or a measurement basis. This is consistent with the comments Japan has received from preparers on impairment accounting for equity method investments and other issues. In addition, other preparers held the view that clarifying that the equity method of accounting is either a one-line consolidation or a measurement basis would not solve all of the issues that exist today.
- Constituents in Japan are concerned with the IASB addressing individual issues without having conceptual discussions. One example would be the IASB's proposal in the Exposure Draft *General Presentation and Disclosures* to present the profit or loss from “integral associates and joint ventures” and from “non-integral associates and joint ventures” separately.
- Based on the above, Japan suggests that the IASB maintain the major requirements related to the equity method of accounting. At the same time, Japan suggests that the IASB undertake a project to develop principles that would clarify when to focus on the one-line consolidation aspect and when to focus on the measurement basis aspect, in order to resolve the practical issues that were identified by constituents in Japan, such as the accounting for impairment. In addition, Japan thinks that addressing individual issues separately would not only be inefficient but could also lead to unintended consequences.

## [Malaysia]

### Accounting for an additional stake in a joint venture without a change in joint control

In November 2020, the staff of Malaysia presented a paper to the IASB<sup>5</sup> to ask for guidance on the appropriate accounting treatment for the acquisition of an additional stake in a joint venture that does not result in a change in joint control. Malaysia recommends that this issue is considered as part of this post-implementation review or, failing this, as part of the IAS 28 equity method research project.

### Interaction with IAS 27 and IAS 28

Some respondents expressed concerns about the IASB’s decision to exclude IAS 27 *Separate Financial Statements* and 28 *Investments in Associates and Joint Ventures* from this post-implementation review. They noted that these Standards are highly interrelated with IFRS 10, 11 and 12 and would need to be considered in order to fully assess application of the

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<sup>5</sup> [09a-eeg-pir-ifs11-change-in-jce-stake-masb-nov-2020.pdf](#)

requirements for group accounting. For example, see Malaysia's response to question 5(a) above.