ICAEW
REPRESENTATION 49/21

POST-IMPLEMENTATION REVIEW – IFRS 10 CONSOLIDATED FINANCIAL STATEMENTS, IFRS 11 JOINT ARRANGEMENTS, IFRS 12 DISCLOSURE OF INTERESTS IN OTHER ENTITIES

Issued 10 May 2021

ICAEW welcomes the opportunity to comment on the *Request for Information – Post Implementation Review – IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in Other Entities* (the PIR) published by IASB in December 2020, a copy of which is available from this link.

We believe that the publication of IFRS 10, 11 and 12 considerably improved how interests in other entities are accounted for. There are, however, areas where we believe further improvements can be made. These are highlighted in the 'key points' section below and throughout this letter.

This response of 10 May 2021 has been prepared by the ICAEW Financial Reporting Faculty. Recognised internationally as a leading authority on financial reporting, the faculty, through its Financial Reporting Committee, is responsible for formulating ICAEW policy on financial reporting issues and makes submissions to standard setters and other external bodies on behalf of ICAEW. The faculty provides an extensive range of services to its members including providing practical assistance with common financial reporting problems.

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KEY POINTS

PRINCIPLES NOT RULES

1. ICAEW has long supported principles-based standards and therefore welcomed the publication of IFRS 10, 11 and 12 back in May 2011 as we firmly believed that the then new suite of standards was a considerable improvement on the old more rules-based approach to accounting for interests in other entities.
2. The introduction of a single consolidation model that identifies control as the basis of consolidation for all types of entities has resulted in more consistent accounting treatment and eliminated the 'bright line' distinctions that created structuring opportunities under previous guidance. As such, we believe the Board has succeeded in improving the usefulness of consolidated financial statements and reducing divergent practice.
3. Likewise, we believe that the introduction of a principles-based approach applicable to all joint arrangements requiring parties to them to recognise their rights and obligations arising from the arrangement has further enhanced the usefulness of financial statements.
4. However, the number of issues referred to the IFRS Interpretations Committee (hereafter referred to as the Interpretations Committee) in relation to these standards may be indicative that the principles they contain are not sufficiently clear. We suggest that the Board looks closely at these principles and provides greater clarity on how they should be applied in certain circumstances.

POTENTIAL IMPROVEMENTS TO THE STANDARDS

5. There are, however, areas where we believe further improvements can be made. In particular, we have identified:
   - gaps in existing guidance;
   - conflicts between the standards covered by this review and other existing standards;
   - guidance contained in Interpretations Committee agenda decisions that could usefully be incorporated into the standards themselves; and
   - areas where we believe additional disclosures would be helpful.
6. We have also identified a number of areas where there are challenges in implementation, which may give rise to inconsistent application of the standards. In some cases, this could be remedied by a clearer articulation of the principles, application guidance or supporting examples in the standards. In other cases, it may be that application of principles results in entities struggling with difficult and complex judgements. We have highlighted these areas throughout this letter and encourage the Board to consider what action, if any, is necessary to support more consistent application.

IFRS 10 CONSOLIDATED FINANCIAL STATEMENTS

7. IFRS 10 provides principles for assessing whether the reporting entity controls one or more other entities. In many straightforward situations, control is easy to assess. Preparers and auditors do, however, need to apply significant judgement in some instances.
8. While we agree that the use of judgement in determining if an investor controls an investee is necessary and appropriate, there are some parts of the standard that entities are struggling to apply in practice, which may lead to inconsistent conclusions being reached in circumstances where fact patterns are similar. In our experience, entities find the following areas particularly challenging:
   - Determining where control lies when two or more investors have the unilateral ability to direct different relevant activities.

- Determining whether the controlling party can change over time as the product lifecycle progresses.
- Determining whether holding veto rights would give a significant shareholder control if it does not otherwise have contractual or 'de facto' control.
- Determining whether 'de facto' control exists in some circumstances.

9. There are also challenges in applying the definition and typical characteristics of an investment entity in practice. Although practice has now become somewhat settled, the assessment in certain cases remains judgemental and this can lead to inconsistent outcomes.
10. A further issue is the loss of information where an intermediate holding company meets the definition of an investment entity and is therefore measured at fair value with movements through profit or loss, rather than being consolidated. We recommend that the Board looks at this area again and considers if and when consolidation of such intermediate holding companies may be appropriate. Regardless of whether or not fair value measurement of the above types of intermediate holding companies is revisited, we recommend that the Board considers enhancing the disclosures for unconsolidated subsidiaries of investment entities. This could form part of a short-term improvement project.
11. These issues are discussed further in our answers to questions 2-5 below.

IFRS 11 JOINT ARRANGEMENTS

12. IFRS 11 sets out a single model of accounting for interests in joint arrangements, focussing on the rights and obligations of the arrangement rather than its legal form. In our experience, the standard generally works well but entities often need to turn to the various agenda decisions published by the Interpretations Committee to help them apply their judgement. We suggest that the Board looks at ways of incorporating these agenda decisions into principles-based guidance in the standard as part of the current review.
13. Unincorporated collaborative arrangements that do not meet the IFRS 11 definition of a joint arrangement are particularly common in the extractive and life sciences sectors but are also encountered elsewhere. In many cases, these arrangements are not subject to joint control but may operate in a very similar way to joint arrangements. There is currently no specific guidance on how to account for these arrangements and other collaborative arrangements. We suggest the Board considers addressing these arrangements more widely.
14. These issues are discussed further in our answers to questions 6-8 below.

IFRS 12 DISCLOSURE OF INTERESTS IN OTHER ENTITIES

15. IFRS 12 requires disclosure of information to help users to assess the nature and financial effects of an entity's relationship with other entities. We are not aware of any significant problems with the application of this standard in practice.
16. As discussed above, entities will often have to use significant judgement when applying IFRS 10 and IFRS 11. Paragraphs 7-9 of IFRS 12 already require entities to disclose significant judgements and assumptions made in applying these standards. The Board may wish to take the opportunity to re-emphasise the importance of these disclosures and the role they play in enabling users to understand the impact that interests in other entities has on the financial statements.
17. Our thoughts on the standard are discussed further in our answer to question 9 below.

INTERACTION WITH OTHER STANDARDS

18. A key area of concern is the interaction between IFRS 10 and other standards including IFRS 15 *Revenue from Contracts with Customers*, IFRS 16 *Leases,* IAS 28 *Investments in Associates and Joint Ventures* and IAS 32 *Financial Instruments: Presentation*.
19. The Interpretations Committee has looked at a number of these areas in recent years but now may be a good time for the Board to revisit them and provide more comprehensive principles-based guidance.
20. While the Discussion Paper on *Financial Instruments with the Characteristics of Equity* considered the accounting for put options over non-controlling interests and mandatory tender offers, such transactions are very common and there remains widespread diversity in accounting, depending on whether IFRS 10 or IAS 32 is referred to. We would recommend that the interaction of these standards is again considered as a priority issue to tackle, as part of the PIR.
21. Resolution of the issues identified in relation to the conflict between IFRS 10 and IAS 28 which led to the deferral of the 2014 amendments to these standards would also be very welcome.
22. These and other issues are discussed further in our answers to questions 5(a) and 10 below.

ANSWERS TO SPECIFIC QUESTIONS

INFORMATION ABOUT THE RESPONDENT

Question 1 – your background

To understand whether groups of stakeholders share similar views, the Board would like to know:

(a) your principal role in relation to financial reporting. Are you a user or a preparer of financial statements, an auditor, a regulator, a standard-setter or an academic? Do you represent a professional accounting body? If you are a user of financial statements, what kind of user are you, for example, are you a buy-side analyst, sell-side analyst, credit rating analyst, creditor or lender, or asset or portfolio manager?

(b) your principal jurisdiction and industry. For example, if you are a user of financial statements, which regions do you follow or invest in? Please state whether your responses to questions 2–10 are unrelated to your principal jurisdiction or industry.

23. ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of sustainable economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 156,000 chartered accountant members in over 149 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

IFRS 10 CONSOLIDATED FINANCIAL STATEMENTS

Question 2(a) – power over an investee – relevant activities

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?

24. Paragraphs 10-14 and B11-B13 of IFRS 10 provide useful guidance to help an investor identify the relevant activities of an investee. In some instances, however, it can be difficult to identify and assess the investee's relevant activities.

25. This can be particularly challenging when two or more investors have the unilateral ability to direct different relevant activities. In such circumstances, paragraph B13 says that the investor that has the current ability to direct the relevant activities that most significantly affect the returns of the investee has power over the investee. This can be difficult to apply in practice as determining which activities have the most significant effect can be very judgemental. Consequently, differing conclusions over control may be reached by different investors or in circumstances where fact patterns are similar.

26. One example of where it is difficult to determine which of the relevant activities most significantly affects the returns of the investee is where the entity in question develops, produces and sells products as all three activities are not only significant to the success of the entity but also dependent on one another. Each activity could be directed by a different investor. Assuming there is no joint control, each investor would need to assess whether they believe their activity most significantly affects the investee's returns. This is particularly difficult, given the co-dependence.

27. Example 1 of IFRS 10 looks at a situation similar to this (although the activities happen at different times) and sets out some factors to consider in determining which activity most significantly affects the investee's returns. While this is helpful, many preparers nonetheless struggle to make this assessment as a result of the co-dependence noted above.

28. Paragraphs 8 and B80-B85 of IFRS 10 say that an investor should reassess whether it controls an investee if there are changes to one or more of the three elements of control. This raises questions about what the appropriate treatment would be if the relevant activities take place in sequence, for example development followed by production followed by sales. Example 1 of IFRS 10 implies that this determination is made at the outset but paragraph B13 also notes that the investors shall reconsider this assessment if relevant facts or circumstances change. However, some might argue that the controlling party may change over time as the assessment of which activity most significantly affects the investee's returns (and the current ability to direct that activity) may change as the product lifecycle progresses.

Question 2(b) – power over an investee – rights that give an investor power

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?

29. Paragraphs B22-B24 and B26-B33 of IFRS 10 provide useful guidance to enable an investor to determine if rights are substantive or protective.

30. While this is helpful, in practice it can sometimes be difficult to apply this guidance. Significant judgement is often needed to determine whether rights are substantive or protective.

31. One challenging area is around the issue of veto rights, where these are not clearly protective. Paragraph B15 of IFRS 10 mentions a veto over changes to transactions as an example of rights that individually or in combination with other rights can give power. The ability to veto changes to significant transactions is also cited in paragraph B18 (in conjunction with the investor's rights and indicators of power) as a situation that may provide

evidence that the investor's rights (although not contractual) are sufficient to give it power over the investee. There is, however, some uncertainty about how these two paragraphs interact meaning it is unclear whether holding such veto rights alone could give an investor power since veto rights allow the investor to block but not direct the investee to enter into transactions. The Board may want to revisit the clarity of the guidance on veto rights to help its application in practice.

32. Another issue is in what circumstances a significant shareholder that has contractual rights (eg, over the composition of the board) may not have power over the investee if another investor holds veto rights that are more substantive rather than clearly protective. This is an important issue as it is not uncommon for arrangements to give one or more investors veto rights over budgets. In such cases, the practical effect may be that the holders of veto rights will need to agree with those operating decisions embodied in the budget and thus would likely have joint control. However, the assessment of control or joint control may depend on the full facts and circumstances including, inter alia, whether the budget covers the relevant activities that most significantly affect the investee's returns and the consequences of non-approval.

Question 2(c) – power over an investee – control without a majority of the voting rights

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?

33. IFRS 10 makes it clear that an investor can control an investee with less than 50% of voting rights. We agree that control should not be based on quantitative thresholds and that it is possible to have 'de facto' control in a situation where an investor with a minority shareholding has the practical ability to direct the relevant activities unilaterally as the remaining voting rights are widely dispersed and the remaining shareholders are unable to consult or make collective decisions.

34. While the guidance in the standard is helpful, the 'de facto' control concept can be difficult to apply in practice. Significant judgement is often needed, which can lead to differing outcomes for similar fact patterns. Moreover, regulators do sometimes raise concerns about whether or not holdings lower than those seen in the examples in the standard result in 'de facto' control and should be consolidated.

35. It is particularly difficult to determine if any one shareholder (for example with a shareholding of 30%) has 'de facto' control in a situation where there are a small number of shareholders each of whom has a fairly substantial shareholding, with other shareholdings being widely dispersed. Whether the 30% investor has 'de facto' control may be difficult to assess and will be very much dependent on an analysis of past voting patterns, how dispersed other shareholdings are and the significance of this information in predicting future behaviour. The standard only includes one example where a minority voting interest (48%, with other shareholdings very widely dispersed) is considered conclusive evidence of 'de facto' control. However, it appears that 'de facto' control may often be achieved at much lower shareholdings.

36. The assessment of 'de facto' control can be very challenging in situations where there is no historical data on voting patterns or where historical information may not be predictive of the

future or of whether other shareholders will act in concert. A number of different factors may affect future behaviour, including changes in ownership or an increase in voting participation (eg, due to a significant transaction being approved, dissatisfaction with management performance or the recent increased use of virtual meetings with higher but more unpredictable shareholder participation). This raises the question as to what extent changes in expectations about the future, as a result of changes in circumstances that have occurred, should affect current judgements.

37. This judgement may need to be revisited frequently depending on changes in shareholdings and voting patterns. Entities are often unclear on how and when they should monitor these changes and exact determination of when control changes may be difficult to determine in some instances, especially where there is a gradual change in the shareholder base.

38. A further issue is uncertainty about whether a control assessment should be undertaken based on the relative voting strengths and participation of the investor and other shareholders at each general meeting or whether the key to determining 'de facto' control is sustained dominance in the longer term.

39. These issues are particularly relevant in the funds industry and the insurance sector, especially in relation to holdings in open-ended investment companies (OEICs), the level of which can change with third party redemptions and therefore needs to be monitored continually to determine whether de facto control exists or has been lost.

40. We suggest that the Board consider whether further guidance and/or examples – but not rules – could be provided to assist entities in understanding and applying the principles relating to 'de facto' control.

Question 3(a) – the link between power and returns – principals and agents

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?

41. The guidance on agency relationships is particularly relevant in investment management situations, where fund managers charge investors a management fee to make investment decisions and decisions on managing the underlying investments on their behalf.

42. In most cases applying the standard – with the help of the application guidance and examples – is relatively straightforward. However, in some marginal cases where removal rights are not clearly substantive, determining whether the investor has sufficient exposure to variable returns to constitute power requires greater judgement and could lead to inconsistent conclusions and diversity in practice.

43. Specifically, entities can find it difficult to interpret the guidance on the magnitude and variability of returns (as referenced in paragraph B68 of IFRS 10) where there are different investors and different return profiles into the fund, for example, collateralised loan obligation vehicles with waterfall payment structures. Another example relates to the managers of money market funds that invest in low-risk instruments. Particularly given prevailing low to negative interest rates, the scale of their fee can be quite substantial relative to other returns as the net asset value tends to stay relatively constant.

Question 3(b) – the link between power and returns—non-contractual agency relationships

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.

44. It is not uncommon for entities to apply the guidance on 'de facto' agency relationships. When doing so, some entities experience challenges in identifying when other parties are 'de facto' agents given the interaction with the control concept deriving from the rights of the investor.

Question 4(a) – investment entities – criteria for identifying an investment entity

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.

45. There are challenges in applying the definition and typical characteristics of an investment entity in practice. Although practice has now become somewhat settled, the assessment in certain cases remains judgemental and this can lead to inconsistent outcomes. Specifically:

- The application guidance says that the investment entity can participate in providing management services and strategic advice to an investee if these activities are undertaken to maximise the investment return from its investees and do not represent a separate substantial business activity or a separate substantial source of income to the investment entity. It is not clear, however, how much involvement would prevent the investor from meeting the definition of an investment entity. This issue has become particularly relevant as funds increase their investments into the renewable energy sector (see paragraph 46 below).
- The application guidance explains that investment entities should not plan to hold investments indefinitely and that such entities should have an exit strategy documenting how they plan to realise capital appreciation from substantially all their investments. It is, however, unclear how formal this exit strategy needs to be. For example, it is unclear how the exit strategy needs to be documented. We would not favour prescriptive guidance in this area. Instead, we believe that emphasis should be placed on ensuring that IFRSs require adequate disclosures describing an entity's exit strategy.
- We further note that the requirement to have a documented exit strategy for substantially all the investments means that some funds, especially in the real estate sector, fail the definition of an investment entity and may need to consolidate subsidiary investments rather than measure them at fair value (which may be more aligned with their business model).

- The application guidance states that an entity is not an investment entity if it, or another group member, obtains other benefits from the entity's investments that are not available to other unrelated parties to the investee. Questions have arisen as to whether an arm's length loan between an investor (or a member of its group) and investee represents a substantial business activity or is an investment at fair value that would not preclude investment entity classification.

46. An emerging issue where the assessment of the investor's involvement is judgemental relates to investments in the renewable energy sector. Solar farms, wind farms and similar assets may have characteristics of investments but also require proper installation and some management. There are difficulties in applying the guidance in paragraph B85D on investment-related activities (eg, whether there is a separate substantial business activity) to such assets. We suggest that the Board takes a closer look at this area, given it is likely to be of growing significance.

47. Some issues on classification were addressed by the Interpretations Committee in its March 2017 agenda decision. Incorporating this guidance into the standard would be helpful.

Question 4(b) – investment entities – subsidiaries that are investment entities

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?

48. There is a loss of information where an intermediate holding company meets the definition of an investment entity and is therefore measured at fair value with movements through profit or loss, rather than being consolidated.

49. This is particularly the case where the intermediate holding company that is an investment entity holds cash or debt that is used to finance the portfolio of companies beneath it and/or provides investment management services. In such circumstances, information about cash available to meet commitments or liquidity issues in the group may not be transparent to users of the financial statements. In addition, revenue from investment management services will not be shown.

50. In some instances, it may therefore be more appropriate to consolidate intermediate holding companies even where they meet the definition of an investment entity. This may be the case, for example, where the intermediate holding company is just a corporate vehicle for holding other investments. In such instances, measuring the intermediate holding company at fair value is unlikely to provide meaningful information. We therefore encourage the Board to revisit this area and consider if and when consolidation of such intermediate holding companies may be appropriate. In doing so, the Board may wish to consider the approach adopted under UK GAAP, which focuses on the purpose of the parent's investment in the intermediate holding company and only allows fair value measurement if it is held as part of an investment portfolio.

51. Regardless of whether or not fair value measurement of the above types of intermediate holding companies is revisited, we recommend that the Board considers enhancing the disclosures for unconsolidated subsidiaries of investment entities, potentially through investment entity-specific disclosure objectives focusing on liquidity and other risks associated with the corporate structure, together with the associated risk management

policies. These could be supplemented with specific disclosures of the external debt and guarantees (including where in the corporate structure) and significant share-based payment arrangements of these subsidiaries. This could form part of a short-term improvement project.

52. In March 2014, the Interpretations Committee concluded that intermediate holding companies created solely for tax optimisation purposes should be accounted for at fair value because they do not provide investment-related services or activities and therefore do not meet the requirements for consolidation. However, given that these companies have little activity, we believe that accounting for these entities at fair value (rather than consolidating the intermediate holding company and fair valuing its portfolio investments) does not always provide the most relevant information.

53. Where portfolio investments are held by an intermediate holding company, we consider that users may find it helpful if IFRS 13 *Fair Value Measurement* disclosures are given for the underlying portfolio investments held by the intermediate holding company (rather than of the investment in the intermediate holding company carried at fair value). In practice, we observe that narrative reporting in the annual report focuses on fair value performance at a disaggregated level which is not required in the financial statements. Some companies already give more disaggregated disclosure voluntarily.

Question 5(a) – accounting requirements – change in the relationship between an investor and an investee

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.

54. In our experience, there are a number of situations where there is a change in the status of the relationship between an investor and an investee that are not adequately addressed in IFRS standards. Some of these are detailed below.

55. There is a lack of guidance on how to account for a change in ownership where there is no loss of control. In particular, there is some diversity in practice as to how the non-controlling interest is adjusted after the transaction, when measured using the proportionate share of the subsidiary's net assets on initial recognition. For example, there are different approaches seen as to whether goodwill arising on the original acquisition is reallocated between the non-controlling interest and owners of the parent (and whether on a proportionate basis or not) or the non-controlling interest is adjusted only for the change in its share of the subsidiary's net identifiable assets.

56. There is a lack of guidance on how to measure a retained interest in a joint operation after loss of control. This issue was considered by the Interpretations Committee in July 2016, who noted that paragraphs B34-B35 of IFRS 11 specify that an entity recognises gains or losses on the sale or contribution of assets to a joint operation only to the extent of the other parties' interests in the joint operation. However, IFRS 10 specifies that an entity remeasures any retained interest when it loses control of a subsidiary. Therefore, there is

potential for diversity arising from these conflicting requirements as to whether the retained interest is remeasured at fair value or not.

57. There is a similar acknowledged conflict between IFRS 10 and IAS 28 where a subsidiary is sold or contributed to an associate or joint venture as to whether the retained interest should be remeasured at fair value or only a proportionate gain or loss should be recognised. We observe that both treatments are seen in practice, whether the subsidiary is a business or not, because IFRS 10 does not specifically make that distinction. Currently, it appears possible to obtain different accounting answers by structuring a transaction in a different way. For example, a contribution of a subsidiary to a newly incorporated joint venture falls within IAS 28 and IFRS 10, effectively allowing a choice of recognising a full or proportionate gain. However, a sale of a subsidiary to a third party or via dilution, leading to a loss of control, would not be within scope of IAS 28 so a full gain would be required (although the end effect of the transaction is very similar).

58. Another area of difficulty (when not applying the 2014 amendments to IFRS 10 and IAS 28) relates to a transfer of an unincorporated business into an associate or joint venture. As this is not a loss of control of a subsidiary, it falls outside IFRS 10 but could fall in scope of IAS 28's requirements. If IAS 28 is intended to apply to business transfers as well as asset transfers, it follows that only a proportionate gain or loss should be recognised in line with its guidance on 'upstream' and 'downstream' transactions. However, there appears to be some diversity of practice as to whether entities analogise to IFRS 10 or apply IAS 28.

59. Resolution of the issues identified in relation to the conflict between IFRS 10 and IAS 28 which led to the deferral of the 2014 amendments to these standards would, therefore, be welcome. However, the amendments only address a direct sale or contribution of a subsidiary to an associate or joint venture. They still would not address a dilution of ownership of a subsidiary becoming an associate or joint venture, and therefore a full gain would be recognised if paragraph 25 of IFRS 10 was applied, even if the subsidiary was not a business.

60. There is a more general issue here that certain IFRSs do draw a distinction between the accounting for transactions involving businesses and those involving assets. There seems to be a lack of coherence in how this distinction is made across accounting standards. In particular, IFRS 3 draws a distinction between the accounting for a business combination and an asset acquisition. Similarly, the amendment to IFRS 11 on accounting for acquisitions of interests in joint operations requires the principles of business combination accounting to be applied to acquisitions of interests in a joint operation whose activities constitute a business.

61. However, IFRS 10's guidance on loss of control does not distinguish between a subsidiary that is a business or not (although this distinction was made in the 2014 amendments to IFRS 10 and IAS 28, suggesting it may be relevant). Since the underlying concept of consolidated financial statements portrays the group as a single entity, it seems counterintuitive that transactions such as a disposal of an asset (or a business) should be accounted differently if wrapped in a corporate shell. Aspects of this debate have resurfaced in the recent discussions of the interaction of IFRS 10 and IFRS 15, and IFRS 10 and IFRS 16, in relation to certain transactions involving single-asset entities and we would urge the Board to address this issue more holistically (see paragraphs 80-81 below).

62. We, therefore, recommend that the Board look further at this area, with a view to introducing consistency across IFRS standards and reducing structuring opportunities. This issue becomes particularly relevant, given the recent changes to the definition of a business in

IFRS 3 *Business Combinations* which may widen the number of transactions considered as asset acquisitions.

Question 5(b) – accounting requirements – partial acquisition of a subsidiary that does not constitute a business

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?

63. When an investor acquires control of a non-wholly owned subsidiary that does not constitute a business, the investor typically recognises a non-controlling interest for equity not attributable to the parent. However, there is limited guidance on how this non-controlling interest should be measured or on how any pre-existing interest should be measured or remeasured in determining the cost of the transaction to be allocated to the assets and liabilities recognised in accordance with paragraph 2(b) of IFRS 3.

64. There are a number of possible approaches to the initial measurement of non-controlling interest including measuring it at the:

- proportionate share of the fair values of the identifiable net assets recognised;
- fair value of the non-controlling interest (as a whole); and
- proportionate share of the consolidated book values of the net assets, with or without transaction costs.

65. There is also diversity as to how any pre-existing holdings should be measured or remeasured in such circumstances.

66. Further guidance on the above matter would be helpful as such transactions occur fairly frequently already and are likely to be more common given many entities are now applying the ‘concentration test’ introduced by the October 2018 amendment to IFRS 3.

IFRS 11 JOINT ARRANGEMENTS

Question 6 – collaborative arrangements outside the scope of IFRS 11

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?

67. Unincorporated collaborative arrangements that do not meet the IFRS 11 definition of a joint arrangement are particularly common in the extractive and life sciences sectors but are also encountered elsewhere. In many cases these arrangements are not subject to joint control but may operate in a very similar way to joint arrangements.

68. Examples include situations where a majority vote for decisions cannot be made by a single participant (so no control) but can be achieved through different combinations of participants (so that the investors do not have joint control). There is currently no specific guidance on how to account for such arrangements and other collaborative arrangements. Consequently, other relevant IFRSs must be applied (including, for example, determining whether there is a

'customer relationship' under IFRS 15) depending on the nature of the arrangements, which may be complex and some diversity may exist.

69. Paragraph 26 above looks at a scenario where an entity develops, produces and sells products and explains that in such cases it can be difficult to assess where control lies as it is not always clear which activity most significantly affects the returns of the investee. Similar issues can arise when assessing where decision making powers lie in unincorporated collaborative arrangements.

70. We suggest the Board considers addressing unincorporated collaborative arrangements more widely in a project with a view to potential standard setting activities.

Question 7 – classifying joint arrangements

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?

71. In our experience, it is fairly common (particularly in the extractives sector) for parties to joint arrangements to consider 'other facts and circumstances' when determining whether the arrangement should be classified as a joint operation or a joint venture as looking at the legal form and the contractual arrangement does not always give a clear answer.

72. The guidance in paragraphs B29-B32 of IFRS 11 is helpful but is not always sufficient on its own to enable entities to make decisions about the appropriate classification of a joint arrangement. Entities will often turn to the various agenda decisions published by the Interpretations Committee on this matter to help them apply their judgement. While these agenda decisions provide useful insights, it seems incongruous that this helpful guidance does not sit within the standard itself. In addition, agenda decisions by their nature only address the fact patterns submitted. We suggest that the Board looks at ways of incorporating these and other relevant agenda decisions into principles-based guidance in the standard (including its application guidance and examples) as part of the current review.

Question 8 – accounting requirements for joint operations

In your experience:

(a) 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?

(b) 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.

73. In most instances, applying the requirements in IFRS 11 enables a joint operator to report assets, liabilities, revenue and expenses in a relevant and faithful manner. There are, however, some situations where this may not be the case.

74. The accounting treatment is unclear in situations where the joint operator's share of output purchased differs from its share of ownership interest in the joint operation, although the determination of revenue has been clarified in the Interpretations Committee March 2019 agenda decision. The Interpretations Committee looked at this issue in March 2015 and declined to add the item to its agenda, noting that it is important to understand why the share

of the output purchased differs from the ownership interests in the joint operation and that judgement will therefore be needed to determine the appropriate accounting.

75. There are, however, still concerns about the sufficiency of the guidance in IFRS 11 on the accounting by a joint operator in the circumstances described. Now may be a good time for the Board to undertake a broader analysis of the issue.

76. The Interpretations Committee provided additional guidance on certain aspects of joint operation accounting in its March 2019 agenda decision, including addressing transactions where a joint operator has a direct legal liability (eg, the joint operator enters into a lease contract for the purposes of the joint operation as sole signatory). The principles behind this decision, which are of wider application than the fact pattern considered, could also usefully be incorporated within IFRS 11.

IFRS 12 DISCLOSURE OF INTERESTS IN OTHER ENTITIES

Question 9 – disclosure of interests in other entities

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.

77. IFRS 12 requires disclosure of information to help users to assess the nature and financial effects of an entity's relationship with other entities. We have encountered few problems with the application of this standard in practice.

78. As discussed above, entities will often have to use significant judgement when applying IFRS 10 and IFRS 11. Paragraphs 7-9 of IFRS 12 already require entities to disclose significant judgements and assumptions made in applying these standards. The Board may wish to take the opportunity to re-emphasise the importance of these disclosures and the role they play in enabling users to understand the impact that interests in other entities have on the financial statements.

79. As noted in paragraphs 48-53 above, there is a loss of information where an intermediate holding company meets the definition of an investment entity and is therefore measured at fair value with movements through profit or loss, rather than being consolidated. We recommend that the Board considers enhancing the disclosures for unconsolidated subsidiaries of investment entities. This could form part of a short-term improvement project.

OTHER TOPICS

Question 10 – other topics

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.

80. A key area of concern is the interaction between IFRS 10 and other standards including:
    - IFRS 15 Revenue from Contracts with Customers – sale of a single-asset subsidiary containing real estate;
    - IFRS 16 Leases – sale of a subsidiary with leaseback;
    - IAS 28 Investments in Associates and Joint Ventures - loss of control of a subsidiary in a sale or contribution to an associate or joint venture; and
    - IAS 32 *Financial Instruments: Presentation* – put options over non-controlling interests.

81. The Interpretations Committee has looked at a number of these areas in recent years and some of their agenda decisions are relied upon in practice to provide guidance in contentious areas. However, agenda decisions by their nature are limited to the fact pattern considered. Moreover, it is not always apparent that a consistent approach has been taken to examining these interactions. Therefore, there is uncertainty over the wider application of principles beyond the fact patterns considered, leading to continued diversity in practice. Now may be a good time for the Board to revisit a number of these areas.

82. There are several issues relating to rights and obligations over equity interests that take different contractual or legal forms where a lack of guidance has led to diversity in practice:
    - There is a lack of guidance for put and call arrangements around non-controlling interests. There is diversity in practice as to whether or not the non-controlling interests are recognised in cases where such arrangements are in place and whether the remeasurement of the put liability is recognised in profit or loss or equity.
    - Mandatory tender offers are a related area where there is diversity in practice. While facts and circumstances may vary across different regulatory environments, the issues are whether a mandatory tender offer constitutes a contractual obligation to purchase a non-controlling interest requiring liability recognition or, even if there is not a contractual obligation, whether the same accounting would be appropriate.
    - Additional application guidance and further principles about what 'current ownership interest' means and how it is determined would be helpful. In particular, where an instrument has the same dividend and capital appreciation rights but has preferential rights to return of capital, limiting downside risk compared to an ordinary share.
    - It may be appropriate to consider disclosure enhancements to IFRS 12 alongside the accounting in these areas. For example, IFRS 12 has few specific disclosures on the nature of ownership interests that are not ordinary shares, such as put options, call options, preference share interests, or ownership interests classified as a liability.

83. We believe the following additional topics should be addressed as part of this post-implementation review:
    - Transfers of associates or joint arrangements between entities under common control are not in the scope of this review nor the recent Discussion Paper on *Business Combinations Under Common Control.* There is diversity in practice on accounting for such transactions.
    - There is no guidance in current IFRSs on change in status of a joint operation eg, where an entity ceases to be classified as a joint operation and becomes an equity accounted investee under IAS 28 or a financial asset accounted for under IFRS 9.
    - IFRS standards do not address what a joint operation's own financial statements should contain, given the joint operators are accounting for their share of the joint operation's assets and liabilities.