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International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Comments on the Exposure Draft *Equity Method: Share of Other Net Asset Changes (Proposed amendments to IAS 28)*

To the Board Members:

The Japanese Institute of Certified Public Accountants ("we" and "our") appreciates the continued efforts of the International Accounting Standards Board (IASB) on this project, and welcomes the opportunity to comment on the exposure draft (ED), *Equity Method: Share of Other Net Asset Changes (Proposed amendments to IAS 28.)*

In view of the fact that there are a number of companies in Japan that have a large number of investments in associates and joint ventures, we believe that the proposed amendments would have a certain impact on practice. And therefore, we understand the importance of the IASB's attempt to clarify a method of investors' accounting for share of changes in the investee's equity that do not arise from profit or loss or other comprehensive income, or distributions received ('other net asset changes').

However, we are concerned that the proposed amendments, with IASB's intention to bring a short-term solution, may instead cause conceptual confusion, as well as confusion in practice, related to equity and the equity method. Therefore, we hope that the requirements stated in the proposed amendments would be revised by taking into account, and to be consistent with, the results of the future discussion in IASB's project on the Conceptual Framework.

The following comments are our responses to the questions raised in the ‘Invitation to comment.’

Question 1

The IASB proposes to amend IAS 28 so that an investor should recognise in the investor’s equity its share of the changes in the net assets of the investee that are not recognised in profit or loss or OCI of the investee, and that are not distributions received. Do you agree? Why or why not?

Comment:

1. **Recognizing an equity method investee’s other net asset changes in an investor’s equity**

   We do not agree with the proposal.

   As stated in BC8 of the ED, investee’s other net asset changes are not included in “transactions with owners in their capacity as owners” that would need to be presented in equity as required in IAS 1 *Presentation of Financial Statements*. If the transactions that do not come under the transactions with owners are classified as equity transactions, to merely address diversity in practice and bring about a short-time solution, we are concerned that conceptual issues related to equity (including comprehensive income) may arise, and may cause confusion in practice. As a consequence, as stated in AV1 of the ED, instead of properly addressing diversity in practice, the proposed amendments may be detrimental to the basic concept of consolidated financial statements.

   In addition, although the equity method of accounting has widely been understood to be one type of consolidated accounting as “one-line consolidation,” there is a method that requires using the equity method as a valuation method for investments. We believe that the existence of these two divergent views has also been a cause of the current diversity in practice.

   Therefore, rather than proceeding with the proposed amendments, we believe that it is important for the Board to firstly consider the concept of equity and the application of the equity method in the current project on the Conceptual Framework, and deliver solutions that would be consistent with the outcomes from the Conceptual Framework project.

With that being said, for those transactions stated in the ED, we believe that either (ⅰ) in BC2, or statements as referred to in AV2 should be permitted to minimize the risks of causing conceptual issues and confusion in practice.

We believe that the option in (ⅰ) is reasonable, as changes in the investor's share over the investee, when it is not a business combination, will be accounted for in the same way as the acquisitions or disposals of the shares.

For example, when an investor acquires shares of the investee from third parties, or when the investee buys back its shares from third parties, while there are differences in the type of transactions with payments made either directly or indirectly, the investor's share of the investee net asset would increase. A similar reasoning applies in a decrease in the investor's share of the investee, when the investor sells its shares of the investee to third parties, or when the investee allocates new shares to third-party shareholders. From a group perspective, using of the same accounting treatment for those transactions that would bring about economically equivalent outcomes would be reasonable.

With regard to statements as referred to in AV2 , it is the method of reflecting an increase or decrease in value of the investment in the investor's profit or loss, and avoids asymmetric accounting outcomes for either increase or decrease of the investor's share of investee's net asset. Until the Board establishes the conceptual definitions of the equity and the application of the equity method, we believe that using of it should not also be denied as well. Alternatively, by requiring an entity to disclose its accounting policies as to which of the two methods are continuously employed, we believe that the comparability of financial information would not be seriously affected between entities that apply different methods.

2. A call option written over an equity method investee's own shares (including share-based payments)

By following the definition of the equity method in IAS 28 (2011), it would be appropriate that an investor would not account for the 'credit' side of the call option transactions entered into by an equity method investee over its own equity (including share-based payments).

Paragraph 10 (d) of the ED suggests that the investor should recognize in its equity, "[T]he investor's share of the investee's net asset changes, other than profit or loss or other comprehensive income and distributions received." However, the equity

method is defined in paragraph 3 of IAS 28 as:
"[T]he equity method is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net asset. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income."

Call options over own equity entered into by an equity method investee, which maybe an associate or a joint venture of an investor, would increase the investee's own equity, but the investor's share over the investee would not increase as they are not considered to be the present shares of the investor. Also, it would not be regarded as changes in the investee's net profit or loss, or other comprehensive income. If we follow the current definition of the equity method in paragraph 3 of IAS 28, an equity increase from a call option entered into by an investee would not be accounted for as an increase in equity by an investor, and we have no reason to oppose this accounting treatment.

With respect to this, the cost incurred from share-based payment transactions would be recognized in profit or loss of an investee, and within the definition of the equity method in IAS 28, an investor would also recognize those changes in its profit or loss, and decrease the carrying amount of such investment. This accounting treatment would be consistent with the view that the cost incurred from associate's transactions should be recognized in profit or loss of the investor as stated in BC5 of the ED.

On the other hand, depending on how the equity method would be defined conceptually, we note that this accounting treatment above may not be acceptable, as it is different from the changes in an investor's share over an investee's that should be reflected in the equity method under the view of one-line consolidation. Therefore, in order to avoid confusion, we believe that the Board should clarify the conceptual framework for the equity method.

Question 2

The IASB also proposes that an investor shall reclassify to profit or loss the cumulative amount of equity that the investor had previously recognised when the investor discontinues the use of the equity method. Do you agree? Why or why not?

Comments:

We do not agree with the proposal.

We do not believe that the reclassification to profit or loss of the cumulative amount of equity that had previously been recognized, has not been anticipated either in the current Conceptual Framework project or IAS 1. Furthermore, IASB has not clarified the conceptual basis for the reclassification to profit or loss of other comprehensive income (so called "recycling") in IFRS.

Therefore, we recommend for the Board to consider the proposed requirements again in future, after its project to clarify the conceptual definitions of equity and the equity method is completed.

Question 3

Do you have any other comments on the proposals?

Comments:

Retrospective application

We believe that it would be difficult, in practice, to apply the proposed amendments retrospectively without any transitional provisions, and therefore, the Board should allow entities to apply these prospectively for annual periods beginning on or after the date that the proposed amendments would become effective. The prospective application should be permitted to be consistent with similar consultative documents recently published by the Board, such as ED/2012/6 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Proposed amendments to IFRS 10 and IAS28)* and ED/2012/7 A*cquisition of an Interest in Joint Operation (Proposed amendments to IFRS 11)*, which allow prospective application of the proposed amendments.

Yours faithfully,

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Executive Board Member－Accounting Practice (IFRS)
The Japanese Institute of Certified Public Accountants