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Staff paper

Agenda reference: 3

Global Preparers Forum

Date	**10 November 2023**
Project	**Equity Method**
Topic	**Overview of the IASB's tentative decisions**
Contacts	**Filippo Poli** (fpoli@ifrs.org) **Mostafa Mouit** (mmouit@ifrs.org) **Edlyn Chigerwe** (edlynchigerwe@ifrs.org)

Purpose of this session

- Provide GPF members with an overview of the IASB's tentative decisions on the Equity Method project.

- Ask for views on those tentative decisions, including the potential effects (costs and benefits) of those decisions *.

Information for participants

- Slides 4–6 provide background and overview of the Equity method project
- Slides 8–18 provide an overview of the IASB's tentative decisions
- Questions for GPF members are set out on slide 19

Project background and overview

Background — the equity method of accounting

Application	• required in consolidated financial statements for investments in associates and joint ventures • permitted in separate financial statements for investments in subsidiaries, associates and joint ventures
Equity method of accounting	• on obtaining significant influence, recognise any difference between the cost of the investment and the investor's share of the net fair value of the investee's identifiable assets and liabilities either as goodwill, or as a gain from a bargain purchase • thereafter, the investor's share of the investee's: — profit or loss is recognised in profit or loss. — other comprehensive income is recognised in other comprehensive income. • distributions received adjust the carrying amount of the investment.

Overview of the Equity Method project*

Objective

Develop answers to application questions about the equity method, as set out in IAS 28 *Investments in Associates and Joint Ventures*, using the principles derived from IAS 28.

Project update

IASB has made tentative decisions on application questions, and on improvements to disclosure requirements, for:

- Associates ✓

Next steps**

Discuss implications of applying tentative decisions, and possible improvements to disclosure requirements, to:

- Joint ventures
- Subsidiaries in separate financial statements

Project approach

Identify application questions ✓ → Identify the principles ✓ → Apply the principles to the application questions ✓

* For more details about the project, please refer to the [project page](#) on the IFRS website, including the [summary of the IASB's tentative decisions on application questions](#).

** At its October 2023 meeting, the IASB was asked to decide if all the tentative decisions apply to investments (other than those in associate entities) accounted for using the equity method..

Project timeline

April 2023	*Project moved from research programme to standard-setting work plan*
November 2023	*Aim to complete discussions*
September 2024	*Exposure Draft publication*
Q1 2025	*Deadline for comment*
2025	*Redeliberations*

Consultation period

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Overview of IASB's tentative decisions

Obtaining significant influence

Application question

An investor, with a previously held interest in an entity, acquires an additional interest and obtains significant influence.

Does the initial measurement of the investment include the original purchase cost of the previously held interest or the carrying amount of that interest in accordance with IFRS 9 *Financial Instruments*?

IASB's tentative decision

An investor would measure the cost of an investment, when an investor obtains significant influence, at the fair value of the consideration transferred, including the fair value of any previously held interest in the associate.

Initial recognition of an investment in an associate – deferred taxes

Application question	IASB's tentative decision
Does an investor account for a deferred tax asset/liability arising from recognising its share of the associate's net identifiable assets and liabilities at fair value?	An investor would account for, and include in the carrying amount of its investment in an associate, a deferred tax asset/liability arising from recognising its share of the associate's net identifiable assets and liabilities at fair value.

Contingent consideration

Application question

How does an investor, initially and subsequently, recognise and measure contingent consideration on acquisition of an investment in an associate?

IASB's tentative decision

On obtaining significant influence in an associate, an investor would recognise contingent consideration as part of the cost of the investment and measure it at fair value.

For each subsequent reporting period, an investor would measure it (except contingent consideration classified as equity) at fair value at each reporting date and recognise changes in fair value in profit or loss.

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Purchase of an additional interest in an associate

Application question	IASB's tentative decision
How does an investor apply the equity method when purchasing an additional interest in an associate while retaining significant influence?	An investor would recognise any **difference** between the **cost of the additional interest** and **its additional share** in the **net fair value** of the associate's identifiable assets and liabilities either as **goodwill** or as a **gain from a bargain purchase.** The investment is an **accumulation** of **purchases**.

Purchase of an additional interest and ‘catch up’ of unrecognised losses

Application question

Is an investor that has reduced the carrying amount of its investment to nil required to ‘catch up’ unrecognised losses if it purchases an additional interest in the associate?

IASB’s tentative decision

An investor, that has **reduced** the carrying amount of its investment to **nil** and has **stopped recognising** its **share** of an associate’s **losses**, **would not recognise** any **unrecognised losses** on **purchasing an additional interest** in the associate.

Disposal of an interest in an associate

Application question	IASB's tentative decision
How does an investor apply the equity method when disposing of an interest in an associate while retaining significant influence?	An investor would measure the portion of the investment to be derecognised as a proportion of the carrying amount of the investment at the date of the disposal. The investor is measuring a single investment in an associate.

Other changes in an investor’s ownership interests

Application question

Does an investor recognise its share of other changes in an associate’s net assets while retaining significant influence, and if so, how is the change presented?

IASB’s tentative decision

When an investor’s ownership interest increases or decreases, the investor would recognise that change as a purchase of an additional interest or a partial disposal.

Gains and losses from transactions with associates

Application question	IASB's tentative decision
How should an investor recognise gains or losses that arise from the sale of a subsidiary to its associate?	An investor would recognise the full gain or loss on all transactions with its associate.

Recognition of losses–share of the associate's profit or loss and other comprehensive income

Application question

How does an investor recognise each component of the investee's comprehensive income:

- in the period when the carrying amount of the investment is reduced to nil?
- after the carrying amount of the investment has been reduced to nil?

IASB's tentative decision

The IASB tentatively decided that:

- if the share of an associate's comprehensive income is a loss larger than that carrying amount of its investment, an investor would recognise in order its share of profit or loss and its share of OCI;
- after the carrying amount of its investment has been reduced to nil the investor would recognise separately its share of each component of comprehensive income.

Impairment – assessing if an investment may be impaired

Application question

Does an investor assess a decline in fair value in relation to the original purchase price or the carrying amount at the reporting date?

IASB's tentative decision

- Change the term 'cost' to 'carrying amount' in paragraph 41C of IAS 28.
- Add as objective evidence of impairment the purchase price an investor pays for an additional interest in an associate (or the selling price for a partial disposal) that is lower than the carrying amount of the investment in the associate at the date of the purchase or sale of that interest.
- Remove the term 'significant or prolonged'.

IASB tentative decision on improvements to disclosures for associates

Gains or losses on other changes in the associate’s net assets	Amount of the gain or loss.
Gains and losses on transactions with associates	Amount of the gain or loss from downward transactions
Contingent consideration arrangements	Information on the nature of the arrangement, amounts recognised and changes in those amounts, and range of possible outcomes
Changes in the carrying amount of investments	Reconciliation of the opening to the closing balance of the carrying amount

Questions for GPF members

- As noted in slide 5, at its October 2023 meeting, the IASB was asked to consider the implications of its tentative decisions for joint ventures and subsidiaries in separate financial statements accounted for under the equity method.
- Do you consider there are implications from the IASB's tentative decisions for these investments? What implications and why?
- What do you expect the cost and benefits of the IASB's tentative decisions to be in your jurisdiction?

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