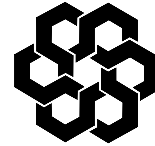

30 Cannon Street, London EC4M 6XH, United Kingdom
Tel: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411
Email: iasb@iasb.org Website: www.iasb.org

International Accounting Standards Board

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.
These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting:	**22 February 2007, London**
Project:	**Business Combinations II**
Subject:	**Transition Provisions for the Business Combinations and Noncontrolling Interest Standards (Agenda Paper 2D)**

PURPOSE OF THE MEETING

1. The purpose of this memo is to ask the Boards to consider the transition provisions for:

    a. The Business Combinations standard (BC standard)

    b. Their separate Noncontrolling Interest standards (NCI standards)

    c. Entities with partially owned subsidiaries on the date they apply the BC standard and the NCI standards.

2. The staff will bring the Boards a paper about effective date near the end of redeliberations.

BACKGROUND—INITIAL DELIBERATION MATERIALS

3. The Boards considered transition at the following Board meetings:

    a. May 28, 2003 FASB Board Meeting

    b. May 2003 IASB Board Meeting.

PROPOSED TRANSITION REQUIREMENTS—BUSINESS COMBINATIONS

General Transition Guidance

4. The business combinations Exposure Draft (BC ED) proposes the following:

   a. *The final BC standard should be applied* ***prospectively*** *to business combinations for which the acquisition date is on or after the date that the standard is applied.* The Boards agreed that the final BC standard should be applied prospectively because it would be impractical to recast previous acquisitions. They also agreed to preclude retrospective application on the basis that it would impair comparability.

   b. *The final BC standard should only be applied at the beginning of an annual period that begins on or after the BC standard is issued and that the BC standard and the NCI standard must be applied at the same time.* The Boards decided to require that the BC standard be applied at the beginning of an annual period because the Boards decided to require that the NCI standard be applied at the beginning of an annual period. The Boards agreed that the BC standard and the NCI standards must be applied at the same time because the NCI standards provide the guidance for subsequent acquisitions or dispositions of noncontrolling interests and for the presentation and disclosure of noncontrolling interests. That guidance would be necessary if an entity does a partial acquisition under the new BC standard.

"Contingent Liabilities" (IASB Only)

5. In the IASB's BC ED, the IASB proposed the following transition guidance for previously recognised contingent liabilities:

> Any contingent liability recognised relating to a business combination for which the acquisition date was before this [draft] IFRS is applied shall be assessed to determine whether it satisfies the definition of a liability (see [draft] IAS 37 (revised 200X)). If not, any recognised amount shall be derecognised with an offsetting adjustment to any goodwill that arose from that business combination. The adjustment to goodwill is limited to the lesser of the carrying amount of goodwill or the amount originally recognised at the acquisition date for the contingent liability. Any remaining recognised amount (that is, any balance in excess of the carrying amount of goodwill that arose in that business combination and any changes in the measurement of the contingent liability after the acquisition date) shall be derecognised as an adjustment to the opening balance of retained earnings.

Other Specific Transition Guidance

6. The BC ED also proposed specific transition guidance for mutual entities and the subsequent recognition of acquired deferred tax benefits related to business combinations completed before the BC standard becomes effective. No comments were received on those transition proposals. The staff is reviewing this guidance and will bring back any issues that come to the staff's attention during that process.

Comment Letter Responses

7. Very few respondents commented on the proposed transition requirements. Those who did stated that they agreed with the proposed business combination transition requirements.

Staff Analysis and Recommendation

8. The staff recommends that the Boards affirm the transition provisions in the BC ED. That is, the staff recommends that the Boards affirm:

    a. The final BC standard should be applied **prospectively** to business combinations whose acquisition date is on or after the date that the standard is applied.

    b. Retrospective application of the BC standard to acquisitions completed before the new BC standard is applied should be precluded.

    c. That the final BC standard should be applied at the same time the final NCI standard is applied

    d. Assuming the Boards affirm that the NCI standards must be applied at the beginning of an annual period, that the BC standard be applied at the beginning of the same annual period.

9. The staff continues to believe that it would be costly and likely impossible for entities to comply with retrospective application of the BC standard to acquisitions completed before the BC standard is issued. After the acquisition date, the assets and liabilities related to a business combination unwind and change. To require a business combination to be recast would be difficult if not impossible. In addition, the staff recommends against allowing retrospective application of the BC standard. If the Boards allowed retrospective application to those combinations that an entity was able recast, an entity might choose to recast only if recasting got

them preferable accounting treatment. Allowing retrospective application also impairs comparability. In addition, users have stated that they prefer a single transition method. Therefore, the staff believes that all business combinations accounted for under predecessor standards should not be changed.

10. Assuming the Boards affirm that the NCI standard must be applied at the beginning of an annual period, the staff believes that the BC standard should also be applied at the beginning of the same annual period. That is because they are complementary standards—it is not practical to apply one without the other since the BC standard provides guidance on acquisitions, including partial acquisitions, and the NCI standards provide guidance on accounting and reporting noncontrolling interests, including changes in those interests, after the acquisition date.

11. The staff questions whether the IASB wants to retain its proposed transition guidance for "contingent liabilities" recognised under IFRS 3, *Business Combinations,* or IAS 22, *Business Combinations*. In January 2007, the IASB affirmed that the BC standard should clarify that only those items that satisfy the definition of an asset or liability should be recognised in a business combination. Therefore, the terms "contingent asset" and "contingent liability" should not be used in the BC standard to make it clear that possible assets and possible liabilities should not be recognised. In many cases, contingent liabilities recognised for previous acquisitions would either satisfy the definition of a liability or would have been derecognised by the time the new BC standard is applied. However, entities may still have some contingent liabilities recognised when the new BC standard is applied. The staff believes that the provisions of the BC standard should be applied to new acquisitions and not those previously accounted for under predecessor standards (IFRS 3 or IAS 22). The Boards have not proposed changing the amounts recognised for other assets or liabilities if those amounts would have been recognised or measured differently under IFRS 3 or IAS 22. For example, the new BC standard does not propose reclassifying from goodwill amounts for reacquired rights that were recognised in goodwill under IFRS 3 or IAS 22. As such, the staff believes the IASB should eliminate this proposed transition provision.

12. ***Do the Boards agree that:***

    a. ***The final BC standard should be applied prospectively to business combinations for which the acquisition date is on or after the date that the standard is applied?***

    b. ***Retrospective application of the BC standard to acquisitions completed before the BC standard is applied should be precluded?***

    c. ***The final BC standard must be applied at the same time the final NCI standard is applied?***

    d. ***Assuming the Boards affirm that the NCI standard must be applied at the beginning of an annual period, that the BC standard be applied at the beginning of the same annual period?***

13. ***Does the IASB wish to affirm or eliminate the transition guidance for previously recognised contingent liabilities?***

PROPOSED TRANSITION REQUIREMENTS—NCI

Should some or all of the provisions of the NCI EDs be retrospectively applied to prior period financial statements?

14. In the NCI EDs, the Boards proposed that an entity apply the presentation and disclosure requirements retrospectively. As such, an entity would recast any prior periods presented in its financial statements as if the NCI presentation and disclosure requirements had been in effect for all periods presented. The objective of recasting prior period financial statements is to improve the comparability of financial information. However, the Boards decided that two of the NCI proposals could not applied retrospectively to transactions that occurred before the provisions of the new NCI standards are applied due to practicability and cost-benefit concerns. Therefore, the Boards decided that those transactions should not be recast.

15. Below is a summary of the transition provisions and the Boards' decisions related to transition.

Recast Prior Period Financial Statements (Retrospective Application)

16. The Boards agreed that the following proposals should be retrospectively applied and that prior period financial statements should be recast to improve comparability and because they met the cost-benefit test (that is, it is not overly costly or difficult to recast these proposals):

a. An entity would reclassify noncontrolling interests to equity from the liability or mezzanine section and present separately from the parent's shareholders' equity (¶33(a) / already required in IAS 27 ((¶33))

b. An entity would recast consolidated net income so that consolidated net income attributable *the noncontrolling interest* was included in the amount reported for consolidated net income (¶33(b) / already required in IAS 1 (¶82))

c. An entity would re-attribute consolidated net income and consolidated other comprehensive income in accordance with the requirements of the NCI standards. (The primary change would be that losses in excess of the NCI balance would be attributed to the NCI rather than attributed to the controlling interest) (¶33(c and d) / ¶35)

d. An entity would disclose the information required by the NCI standard for all periods presented (¶33(f and g) / ¶40)

e. An entity would reclassify any gains or losses that were recognised in income for decreases or dispositions of noncontrolling interests from income (retained earnings) to equity (¶33(e) / ¶30A for decreases or dispositions of NCI)

***Do Not* Recast Prior Period Financial Statements**

17. The Boards agreed that the following proposals should **not** be retrospectively applied and that prior period financial statements should **not** be recast because they did not meet the cost-benefit test (that is, it is costly or difficult to recast these proposals) or because recasting would require the use of hindsight to remeasure previously recognised amounts:

a. An entity would not change the amounts recorded if the entity increased or acquired noncontrolling interests in a subsidiary before the NCI standards are applied (¶34(a)/¶43B (a)) *(Those transactions were accounted for by the partial purchase method under U.S. GAAP and possibly under IFRS, so it would be impracticable to restate those transactions, which is the same reasoning the Boards used to decide that the BC standard should be applied prospectively.)*

b. An entity would not change the amounts recorded in income if control of a subsidiary was lost before the NCI standard is applied. Therefore, the gain or loss recognised in income before the NCI standards are applied would not be recast to remeasure any retained NCI in the former subsidiary to fair value. (That is, in measuring the gain or loss, any retained NCI would be measured at carrying value rather than fair value as proposed in the NCI EDs) (¶34(b) / ¶43B (b)) *(The Boards did not want entities to use hindsight in remeasuring any retained noncontrolling interest to fair value.)*

c. If an entity has a partially owned subsidiary when the NCI standard is applied, the assets and liabilities of the partially owned subsidiary would not

change upon application of the NCI standards. The entity would account for any subsequent acquisitions or dispositions of noncontrolling interests using the guidance in the NCI standards (that is, those transactions would be accounted for as equity transactions) (¶34(a) / ¶43B (a)) *(This is the result of the combination of the prospective business combinations transition proposals and the new guidance for accounting for acquisitions of noncontrolling interests in the NCI standards. The staff addresses this issue in the last section of the memo).*

Comment Letter Responses

18. Because the FASB and IASB issued separate NCI EDs, the staff summarises respondents' comments to the NCI EDs separately. However, some respondents to the NCI EDs raised similar concerns in their comment letters, which are discussed more fully in the Staff Analysis section.

Respondents to the FASB's NCI ED

19. Few respondents to the FASB's NCI ED addressed transition in their comment letters. Those that did generally agreed with the transition proposals. Some respondents disagreed that an entity should recast prior period financial statements for the presentation and disclosure provisions because they believe it would be impracticable or too difficult to do so, particularly for entities with a substantial number of partially owned subsidiaries at the date of transition.

20. As stated above, the NCI EDs preclude retrospective application to prior periods for (a) for acquisitions of noncontrolling interests and (b) accounting and reporting for the loss of control of a subsidiary. With respect to that proposal, Deloitte (CL #7) stated "that retrospective application of paragraphs 34(a) and 34(b) (f. and g. above) of the proposed Statement should be permitted, but only to the extent an entity could apply the provisions to all historical transactions (i.e., an 'all-or-none' retrospective application)."

Respondents to the IASB's NCI ED

21. Most respondents to the IASB's NCI ED agreed with the transition proposals with respect to prior period financial statements. However, several respondents suggested that retrospective application not be required for some or all or some of the proposed amendments to IAS 27. For example, a few respondents stated that the proposed requirements should not be applied to any changes in noncontrolling

ownership interests (increases or decreases) and that any gains and losses should continue to be reported in income rather than be reclassified to equity.

Staff Analysis and Recommendations

Retrospective Application is Impractical or Too Difficult (Proposals a. through d.)

22. Some respondents to both NCI EDs disagreed that an entity should recast prior period financial statements for the presentation and disclosure provisions because they believe it would be impracticable or too difficult to do so, particularly for entities with a substantial number of partially owned subsidiaries at the date of transition.

23. During initial deliberations, the staff and Boards considered the merits of a variety of transition alternatives. As noted in the basis for conclusions in both NCI EDs, the Boards believe that retrospective application is generally preferred to improve the comparability of financial information. The staff continues to believe that recasting prior period financial statements for the presentation and disclosure provisions is not overly burdensome and that the benefits of comparability outweigh the costs. The proposed requirements do not require any new computations or measurements. They simply require reclassification of previously measured amounts within the basic financial statements.

Should Dispositions (Decreases) of Noncontrolling Ownership Interests That Occur Before the NCI Standards Are Applied Be Recast (Proposals e. and f.)

24. A few respondents to the IASB's NCI ED suggested that retrospective application not be required for either decreases or increases in ownership interests. That change would mean that the transition provisions are the same for all changes ownership interests without a loss of control. For example, the German Accounting Standards Committee (IASB CL #19) stated:

> …we wonder why IAS 27.43 B (a) refers only to increases, which implies that a prospective application of the provision is limited to increases, while decreases need to be accounted for retrospectively. GASB recommends clarifying that prospective treatment applies to increases as well as decreases.

25. A decrease in a parent's controlling ownership interest (sale of an equity interest in the subsidiary) would be reported as an equity transaction under the NCI EDs.

Applying that proposal retrospectively to prior periods would require a relatively simple reclassification. Therefore, requiring an entity to recast its financial statements for decreases in a parent's controlling ownership would not be too difficult or costly.

26. The acquisition of a NCI would also be reported as an equity transaction under the proposal. In contrast, FASB Statement No. 141, *Business Combinations*, requires acquisitions of noncontrolling interests to be accounted for using the purchase method, which results in the recognition of an additional purchase layer of net identifiable assets and goodwill each time noncontrolling interests are acquired. IFRS 3 does not provide specific guidance on how to account for acquisitions of additional noncontrolling interests after control is obtained, which has resulted in diversity in practice. (Two accounting firms (Deloitte and KPMG) stated that entities have been applying one of as many as four or five different methods to account acquisitions of additional interests after control is obtained.) Retrospective application of the NCI EDs to those transactions would entail an unwinding of those prior step acquisitions, and the information needed might not be readily available at a reasonable cost. Therefore, the Boards proposed in the NCI EDs not to change the accounting for increases in a parent's controlling ownership interest in a subsidiary recognised in a prior period.

27. The staff believes the Boards have the following alternatives to consider for transition related to increases and decreases in ownership interests:

    a. **Alternative A:** Affirm the proposed transition requirements in the NCI EDs. That is, require that an entity (1) recast prior period financial statements for **decreases** in a parent's controlling interest that do not result in a loss of control that occurred before the new NCI standards are applied and, (2) not recast prior period financial statements for **increases** in a parent's controlling interest that do not result in a loss of control that occurred before the new NCI standards are applied.

    b. **Alternative B:** Preclude an entity from recasting prior period financial statements for both **increases and decreases** in a parent's controlling interest that do not result in a loss of control that occurred before the new NCI standards are applied.

Staff Recommendation

28. The staff is divided on its recommendation. Some staff believe that recasting prior period financial statements when practicable improves the comparability of

financial information. As noted above, recasting for decreases in a parent's controlling interest would require a relatively simple reclassification.

29. Other staff believe that Alternative B might be more logical because increases and decreases would be treated symmetrically. In addition, those staff believe that it would be cleaner to only require recasting for disclosure and presentation and that the recording of previous transactions should not be changed upon transition.

Which alternative do the Boards support?

Issues Related to Subsequent Increases (Acquisitions) of Noncontrolling Interests After the New NCI Standards Are Applied (Proposal h.)

30. Upon adoption of the final NCI standards, the balance of any noncontrolling interest in subsidiaries that were classified as liabilities (or in a mezzanine section) would be reclassified to equity. The reported amount of that noncontrolling interest would not be remeasured. Some respondents expressed concern about that provision in light of the requirement to subsequently account for an acquisition of those interests as equity transactions. They believe that requirement might lead to an artificial reduction in the controlling interest's shareholders' equity (assuming the value of the noncontrolling shares has increased). This concern is magnified for partially owned subsidiaries acquired before the new BC standard is applied because the requirements (such as full goodwill) in the BC ED would be applied on a prospective basis, and thus, would not be required for partial acquisitions that occurred before the adoption of the final Statements. Respondents that expressed this concern are quoted below:

31. PwC (CL #12) stated:

> Subsequent to the effective date of the standards, if the parent entity decides to purchase the non-controlling interest and the non-controlling interest has appreciated over time, the parent entity may record a significant reduction in its equity which would not reflect any underlying economic event.

32. Citibank (CL #14) stated:

> The impact [of the proposed accounting for changes in ownership interest in a subsidiary], when taken in conjunction with the proposed accounting in Business Combinations ED, would have absurd accounting results. Subsequent to recording

> 100% of the goodwill, purchases of additional stakes at prices different from the acquisition of a controlling stake, will reflect incorrect goodwill and carrying value of the subsidiary. Any gain or loss on account of the sale of a noncontrolling stake in a subsidiary would be accounted for as an equity transaction without the recognition of a gain or loss. This will lead to "accounting" gains/losses being different from economic gains/losses. It will also open up this area for potential abuses in timing and structuring of transactions with the objective of managing the recognition of gains or losses.

33. Affiliated Managers Group (CL #38) stated:

> ...[i]f the Proposed Standard is adopted as currently drafted, the transition approach offered will not result in financial statements being presented on a comparable basis for business combinations consummated before the adoption of the Proposed Standard. For companies that acquire controlling interests in businesses, there will be a permanent difference in the method of accounting for acquisitions completed before and after January 1, 2007. This difference will make comparability of financial statements difficult for financial statement users.

34. The staff understands the concerns expressed by respondents. The Boards were aware of this issue and carefully considered alternatives before the BC and NCI EDs were issued. (The Boards considered this issue at the May 28, 2003 Board meeting and the May 2003 IASB Board meeting.) Also, during the FASB's field visits in 2004, Affiliated Managers Group noted this issue. At that time, the FASB staff attempted to develop an alternative that would mitigate the issue, but we were unable to develop a superior alternative.[1]

35. The following table provides the transition alternatives that have previously been considered by the Boards:

[1] Summary of Field Visits Observations Memo dated October 29, 2004.

Transition Alternative	**Description of Alternative**	**Analysis**
Continue to allow the partial purchase method for subsidiaries that are partially owned at the date this standard is applied	For subsidiaries that are partially owned at the date the BC and NCI standards are applied, allow the entity to **account** for additional acquisitions of noncontrolling interests as step acquisitions. Note: The step acquisition method is currently required in Statement 141 and was required under APB 16. However, IFRS 3 requires that an acquiree's identifiable net assets be recognised at their fair values; therefore, this transition issue might occur with respect to goodwill attributable to the noncontrolling interests. In contrast, IAS 22 was similar to Statement 141 and partial acquisitions were accounted for by the partial purchase method. As a result, the guidance that would be provided under this alternative would vary for IFRS users depending on whether the acquisition was accounted for under IFRS 3 or IAS 22.	The Boards did not believe this was a practical transition alternative because it would: • Add complexity to the standard by carrying forward guidance for applying the partial purchase method, which would apply to a small number of entities (that is, the guidance would only apply to entities with partially owned subsidiaries before the application of the standards that subsequently acquire additional noncontrolling interests). • Result in another blended measure for assets and liabilities (that is, part fair value when control is obtained and part fair value when additional noncontrolling interests are acquired). • Result in divergence between the IASB and FASB because the partial purchase method is not required in accordance with IFRS 3.
Apply the requirements of the BC standard retrospectively for subsidiaries that are partially owned when the BC standard is	For subsidiaries that are partially owned at the date the BC and NCI standards are applied, **retrospectively apply** the requirements of the BC standard to the partially owned subsidiaries on the date of application.	The Boards rejected this alternative for the same reason they rejected retrospective application for the final BC standard: • In many circumstances, it might be impossible to retrospectively apply the requirements of the BC standard to combinations completed before the BC

Transition Alternative	Description of Alternative	Analysis
applied		standard is applied. For example, for combinations that occurred many years ago, it would be difficult to determine the values of the acquiree's assets and liabilities. In addition, the information needed to restate prior financial statements might not exist any longer. • Hindsight in measuring fair values would provide an incentive for an entity to restate its financial statements to benefit the entity, which would decrease the quality of financial reporting.
Apply the **measurement** requirements of the final BC standard to the assets and liabilities of partially owned subsidiaries on the date the BC standard is applied	For subsidiaries that are partially owned at the date the BC and NCI standards are applied, **apply the measurement requirements** of the final BC standard to the assets and liabilities of those partially owned subsidiaries. That is, restate the assets and liabilities of the partially owned subsidiaries to fair value as of the date the BC standard is applied.	The Boards rejected this transition alternative because it would be costly to apply and it allows particular entities (those with partially owned subsidiaries) to remeasure particular assets and liabilities (only those of the partially owned subsidiary) when other entities would not be afforded the same option.
Restate any NCI in partially owned subsidiaries to fair value on the date the BC and NCI standards are applied	For subsidiaries that are partially owned at the date the BC and NCI standards are applied, remeasure the NCI to fair value and recognise the adjustment as a gain or loss.	This would be an easier alternative that would reduce the problem without requiring a revaluation of every asset and liability when the new standards are applied. However, this alternative would result in some odd reporting because the entity would not revalue the

Transition Alternative	Description of Alternative	Analysis
		controlling interest's equity, it would not affect the value of the underlying assets and liabilities of the partially owned subsidiary, and in many cases, the entity would need to measure the entire subsidiary to measure the fair value of the NCI, so it seems like the previous alternative (revalue the assets, liabilities and NCI of the partially owned sub upon adoption of the new standards) would be a more faithful representation than this alternative. This alternative might mitigate the problem, but as noted earlier, this issue is not really a transition issue. It will arise any time an entity acquires noncontrolling shares that have appreciated since the acquisition date (although the full goodwill proposal and more fair value measurements will decrease the problem.) This alternative might be a better fix for IFRS because there is still a larger 'gap' caused by the partial purchase method used in U.S. GAAP.

36. The staff notes that the concern expressed by some respondents about artificial reductions in equity when noncontrolling interests are subsequently acquired is not solely a transition issue. The phenomenon occurs because the amount paid to subsequently acquire the NCI is presumably its fair value, yet the carrying value of that acquired NCI is measured using a historical cost accounting model. Thus, the difference between the fair value of the acquired interest and its historical cost carrying amount is accounted for as a charge or credit to equity. The difference between the fair value and carrying amount of acquired NCI might be greater for those partially owned subsidiaries acquired before application of the new BC and NCI standards (in part because the BC standard records NCI at fair value), but the point is that such differences can also exist for NCI's arising after the new BC and NCI standards are applied (because our historical cost accounting model causes the carrying value of the NCI and its fair value to diverge over time).

37. The following factors will mitigate the impact to equity when additional noncontrolling interests are acquired:

    a. Recognising the fair value of assets and liabilities in a partial acquisition (as required by IFRS 3 and as will be required by the new BC standard) and recognising the fair value of the NCI (or the full goodwill method).

    b. More fair value measurements in the partially owned subsidiary's financial statements after the acquisition date. As more assets and liabilities are measured at fair value, the closer the recorded amount for the NCI will move toward fair value. As a result, the difference between the recorded amount for the NCI and the proceeds from an acquisition or disposition of noncontrolling shares will be smaller.

38. Those two things will result in the NCI balance being stated closer to fair value so the impact on equity will not be as great if the acquirer acquired some of the outstanding noncontrolling interests.

39. The staff also notes that the FASB is the process of finalizing Statement 15X, *The Fair Value Option for Financial Assets and Financial Liabilities,* to expand the use of fair value measurements which might reduce the concerns expressed by respondents for those who choose the option. The IASB has already incorporated a fair value option for financial instruments in IAS 39, *Financial Instruments: Recognition and Measurement*.

40. The staff believes that concerns about the "artificial" reduction to equity will be mitigated by recognising the NCI at fair value in a partial acquisition (full goodwill) as illustrated in the following example:

41. [Paragraph omitted from observer note].

42. [Paragraph omitted from observer note].

43. The staff notes that the issue of "artificial" reductions of equity also arises when an entity reacquires some of its own shares through treasury share transactions. That is, when an entity reacquires some of its own shares at a fair value that differs from the historical cost carrying amount, the result is a charge or credit to equity. Some argue that recognising a reduction of equity because the value of the shares is increasing is unreasonable. The staff thinks that the accounting for acquisitions or NCI or treasury stock may not be the problem—the problem is our transaction based accounting model that fails to recognise many changes in assets and liabilities in the absence of transactions. The staff notes that even if the entity accounted for the acquisition of shares as an income statement transaction, it would still result in a reduction of equity. However, that reduction would be recognised in retained earnings rather than additional paid-in capital.

Staff Recommendation

44. The staff continues to support the transition proposal in the NCI EDs that the recognised amounts for the assets and liabilities of partially owned subsidiaries should not be changed upon application of the NCI standards. While the staff understands the concerns about the potential reduction in partially owned subsidiary's equity if the parent acquires some of the outstanding noncontrolling shares in that subsidiary and the value of those shares has increased, the staff cannot find a better transition alternative. Additionally, we believe that the concerns about an "artificial" reduction in equity can be mitigated through disclosure.

45. ***Do the Boards agree that the assets and liabilities of partially owned subsidiaries should not be changed upon application of the NCI standards?***