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

INFORMATION FOR OBSERVERS

Board Meeting: **19 June 2007, London**

Project: **Business Combinations II**

Subject: **NCI Sweep Issues (Agenda Paper 2A)**

PURPOSE OF THIS MEMORANDUM

1. The purpose of this memo is to ask the Boards to reconsider one of the transition requirements of the NCI standard.

Transition for Losses in Excess of the Noncontrolling Interests Equity that Were Attributed to the Parent

2. ARB 51 and IAS 27 currently require that if losses applicable to the minority (noncontrolling) interest exceed the minority interest equity balance, such excess and any further losses applicable to the minority interest are charged against the majority interest since there is no obligation of the minority interest to make good such losses. If future earnings do materialize, the majority interest should be credited to the extent of such losses previously absorbed. The NCI standard will amend ARB 51 and IAS 27 to change that requirement. As such, the parent and noncontrolling interest are attributed their share of the losses even if the noncontrolling interest balance becomes a deficit.

3. The transition section of the Preballot Draft of the NCI standard proposes to require that if the parent controls the subsidiary when the standard is applied, the parent would recast consolidated net income attributable to the parent to deduct any losses that were attributed to the parent because those losses exceeded the noncontrolling interest in the equity capital of the subsidiary. Those losses would be reattributed to the noncontrolling interest. The Boards believed recasting for excess losses would improve comparability. The staff is now concerned that this decision will cause practice issues that will outweigh the benefits of comparability.

4. The staff recommends that the Boards change this decision. We recommend that the Boards only require that consolidated net income be recast to combine the amounts attributable to the parent and noncontrolling interest, but that the amounts attributable to the parent and the noncontrolling interest NOT be changed if the parent was previously attributed excess losses. The staff is concerned that this will lead to practice issues, such as:

    a. The NCI transition decisions were premised on the view that the disclosure provisions should be applied retrospectively for comparability, but that transactions and amount recognized in the financial statements should not be changed. Recasting for excess losses is not just a simple recast. It would require preparers to restate their earnings attributable to the controlling interest and, therefore, will affect EPS in prior periods.

    b. It is much simpler for the preparer not to recast prior earnings. If the Boards do not change this decision, they would need to provide additional guidance about how far back earnings should be recast or else questions will arise.

    c. The Boards would have to provide guidance on how to record that recast in the period of adoption (that is, would it be a charge to beginning retained earnings).

5. The recast is only applied if the subsidiary is still owned by the parent when the parent adopts the NCI standard. If the subsidiary is not owned by the parent when the NCI standard is adopted, then earnings would not be recast because that would change the amount recognized as a gain or loss when the subsidiary was disposed of. Thus, comparability will not be achieved anyway.