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**International Accounting Standards Board**

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*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

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| **Board Meeting:** | **Wednesday 20 February 2008, London** |
| **Project:** | **ED Annual improvements process–Comment analysis** |
| **Subject:** | **Q22 and Q25 – Disclosure requirements for investments in associates and jointly controlled entities accounted for in accordance with IAS 39 (Agenda paper 4I)** |

*Issue: Entities that account for investments in associates or jointly controlled entities at fair value, in accordance with IAS 39* Financial Instruments: Recognition and Measurement*, are outside the scope of IAS 28* Investments in Associates *and IAS 31* Interests in Joint Ventures*. However, IAS 32* Financial Instruments*:* Presentation *and its replacement IFRS 7* Financial Instruments: Disclosures *require those entities to comply with the disclosure requirements of IAS 28 / IAS 31 for such investments. The Board has been told that this requirement is not clear because the scope sections of IAS 28 and IAS 31 conflict with the scope sections of IAS 32 and IFRS 7.*

*The proposal in the exposure draft is to clarify that it is necessary to comply with the disclosure requirements in IAS 28 / IAS 31 even if the investment in an associate / jointly controlled entity is accounted for in accordance with IAS 39. However, in reviewing those disclosure requirements the Board* *proposed giving some relief in relation to those investments by limiting the required disclosures to a subset of the IAS 28 / IAS 31 requirements.*

**STAFF RECOMMENDATION**

1. The staff recommends that the Board proceed with the amendments to IAS 28 and IAS 31 as proposed in the ED.

**BACKGROUND**

2. The proposed improvement is in response to an apparent inconsistency in the disclosure requirements for entities that account for investments in associates and jointly controlled entities at fair value in accordance with IAS 39. Investments in associates and jointly controlled entities held by venture capital organisations or mutual funds, unit trusts and similar entities including investment-linked insurance funds may be excluded from the scope of IAS 28 and IAS 31 if they are designated as at fair value though profit or loss or are held for trading in accordance with IAS 39. In such cases, they should, instead, be accounted for in accordance with IAS 39. However, IAS 32 and IFRS 7 both require entities that account for investments in associates and jointly controlled entities in accordance with IAS 39 to give the disclosures required by IAS 28 and IAS 31 in addition to the disclosures required by IAS 32 or IFRS 7.

3. The annual improvements ED proposed removing from IAS 32 and IFRS 7 the general requirements to give the IAS 28/IAS 31 disclosures, and identifying the specific disclosures that should be given. In addition, the ED proposed removing from IAS 32 and IFRS 7 the requirement to give the disclosures in IAS 27 because this duplicated the requirement in IAS 27.

4. Replacing the general disclosure requirement would be references to specific disclosures that an entity holding such investments should give, as follows:

   a. Paragraph 37(f) of IAS 28 for an investment in associates:

      37(f) the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of associates to transfer funds to the investor in the form of cash dividends, or repayment of loans or advances;

b. Paragraphs 55 and 56 of IAS 31 for an investment in joint ventures:

> 55 A venturer shall disclose the aggregate amount of the following commitments in respect of its interests in joint ventures separately from other commitments:
>
> (a) any capital commitments of the venturer in relation to its interests in joint ventures and its share in the capital commitments that have been incurred jointly with other venturers; and
>
> (b) its share of the capital commitments of the joint ventures themselves.
>
> 56 A venturer shall disclose a listing and description of interests in significant joint ventures and the proportion of ownership interest held in jointly controlled entities. A venturer that recognises its interests in jointly controlled entities using the line-by-line reporting format for proportionate consolidation or the equity method shall disclose the aggregate amounts of each of current assets, long-term assets, current liabilities, long-term liabilities, income and expenses related to its interests in joint ventures.

5. Appendix 2 to this paper contains a list of the disclosure requirements in IAS 28 and IAS 31 with the staff assessment of their relevance for an entity holding investments in associates or jointly controlled entities accounted for in accordance with IAS 39.

## COMMENT LETTER ANALYSIS

### An overview

6. From 75 letters received, 35 respondents commented on this issue. The majority of those that commented agreed with the proposal. Those respondents acknowledged that there is a need to eliminate an inconsistency and supported the modified disclosure requirements. Some respondents disagreed because they thought the amendments would be increasing the disclosure requirements, many of which they questioned.

7. Other specific points raised, but not planned for discussion, are summarised in Appendix 1 to this paper.

**Consistent disclosure on financial instruments in IAS 39**

8. The respondents[1] who disagreed with the proposals did so mainly because they considered that the investments in associates and jointly controlled entities that are accounted for at fair value have similar characteristics to financial instruments subject to the requirements of IAS 39. They questioned the rationale for, and usefulness of, the additional information for certain types of the financial instruments.

> ''We do not see the rationale behind requiring entities that applied the fair value option in accordance with IAS 28.1 to provide disclosure in accordance with IAS 28.37(f). The reason for allowing entities to apply the fair value option was that they manage their investments like 'normal' financial instruments. This is the reason why the Board introduced the option for those institutions to fair value all their investments (IAS 28.BC5). We do not believe the nature of those investments is different from that of other financial instruments accounted for under IAS 39 from the perspective of those entities and hence, we believe that there should be no additional disclosure requirements.'' [CL 44]

**Rationale for and extent of the additional disclosures for fair value measurement**

9. Some respondents[2] queried whether the Board's decision on the disclosures in IAS 28 and IAS 31, considered relevant for investments in associates or joint ventures accounted for at fair value, is based on a clear rationale. They requested the inclusion of that rationale in the Basis for Conclusions.

10. One respondent asked that the disclosures relating to contingent liabilities to also be required to be included in the separate financial statements of the investor in an associate and venturer in a jointly controlled entity (CL 21).

11. One respondent also suggested that an entity holding an investment in jointly controlled entities accounted for in accordance with IAS 39 should not be required to disclose its share of capital commitments of the joint ventures themselves as described in paragraph 55(b) of IAS 31 'because such commitments are not part of the venturer's business' (CL 50). That respondent also questioned the need for the disclosures in paragraph 56 of IAS 31 to require a description of investments in the jointly controlled entity accounted for under

[1] Eg CL 19, 24 and 44.
[2] Eg CL 11, 32 and 50.

IAS 39, because it is not required under IAS 27 and IAS 28 for the investments in associates.

> ‘‘We also have concerns with the Board requiring an entity to include the disclosures required by paragraph 56 in IAS 31 for joint ventures held at fair value through profit or loss (FVTPL). Paragraph 56 requires an entity to disclose a listing **and description** of interests in significant joint ventures. We note that a similar requirement is not included in IAS 28, nor has the Board specifically required this disclosure for associates held at FVTPL in the Exposure Draft. However, we also note that IAS 27 requires entities to disclose a list of significant investments in subsidiaries, jointly controlled entities and associates. There is no discussion in the ED as to whether this requirement will apply to both associates and joint ventures held at FVTPL. We recommend that the Board makes all of these disclosure requirements consistent and avoid duplication.’’

***Staff analysis and recommendation***

12. The purpose of the proposed improvement is to clarify that entities with investments in associates and jointly controlled entities must meet the disclosure requirements in IAS 28 and IAS 31 regardless of how they account for these investments. The staff assessment is that this was the original intention when IAS 39 and IFRS 7 were approved. On this basis the disclosure requirements are not new. The staff thinks the concerns raised by respondents about consistency, and the absence of a rationale for requiring these disclosures, are valid. However, these disclosures are already being discussed in the joint arrangements and consolidations projects. The staff thinks any discussions about the more general disclosure requirements should take place in those projects.

13. The fact that the Board is eliminating some disclosure requirements for the affected entities is a practical step to remove some requirements that are inconsistent with the accounting.

**IFRSs that should specify disclosures requirements**

14. Some respondents[3] argued that an entity that accounts for its interests in associates or jointly controlled entities in accordance with IAS 39 is outside the scope of IAS 28/IAS 31, and therefore should not be required to give disclosures in accordance with those standards. Instead, the respondents

[3] Eg CL 23 and 24.

proposed that the disclosure requirements on such an investment should be given in the standards that provide specific guidance on financial instruments.

15. The staff assessment is that it is more practical to specify in IAS 28 and IAS 31 that entities holding such investments are not exempt form making specific disclosures in accordance with those standards. The staff therefore recommends affirming the proposed amendment in the ED.

## RECOMMENDATION AND QUESTION TO THE BOARD

16. The staff recommends that the Board proceed with the amendments to IAS 28 *Investments in Associates* and IAS 31 *Interests in Joint Ventures* as proposed in the ED.

***Does the Board agree?***

## APPENDIX 1: OTHER COMMENTS NOT CONSIDERED IN DETAIL IN THE AGENDA PAPER

17. In addition to the comments discussed in the agenda paper, some respondents raised additional points. The staff does not intend to discuss each of these in detail, but instead has set out below a summary of the points raised with brief staff responses.

### Scope of the annual improvement project

18. A respondent admitted that there is an inconsistency, but expressed concerns about the consequences of the amendment. The change in the disclosure requirements should not be made as part of the annual improvements process.

> ‘‘in the case of adoption of this amendment, disclosures reported by such entities under IAS 28 [IAS 31] may significantly decrease, and this may not be in favor of the users of financial statements. Therefore, the [respondents] believe that this issue probably should be scoped out from annual improvements project and be more comprehensively considered within a specific project.’’ [CL 16]

19. The staff understands that, in practice, many entities with investments in associates or jointly controlled entities scoped out of IAS 28 and IAS 31 do not provide the disclosures required by those standards, in addition to IAS 32 and IFRS 7. Therefore, the staff does not anticipate any loss of information as a result of this amendment.

### Cost—benefit consideration

20. Some respondents[4] agreed that an inconsistency should be eliminated but, because they concluded that the amendments would be requiring new disclosures, a more formal cost and benefit assessment should be undertaken.

21. As noted in paragraph 12, the staff assessment is that the disclosure requirements are not new and therefore do not justify a cost and benefit assessment.

[4] Eg CL 38, 69 and 75.

## Disclosures in IAS 28 and IAS 31

22. One respondent noted that the scope of the disclosures under IAS 28 should be extended:

> ‘‘We consider the usefulness of the disclosure of the principal associates to be just as great where held by a venture capital organisation as in other cases. All the disclosure requirements of IAS 31 should apply to them, including the holdings and identities of associated companies.’’ [CL 53]

23. Other respondents suggested that the consistency between IAS 28 and IAS 31 should be improved:

> ‘‘We would also recommend the Board to consider whether consistent disclosures are required between associates and joint ventures accounted for at fair value through profit or loss.’’ [CL 50]

24. The staff notes that this would require considering the disclosure requirements of IAS 28 and IAS 31 in general. This issue is outside the scope of the annual improvement process. The staff recommends that it be discussed as part of the project on joint arrangements. ED 9 *Joint Arrangements* published in September 2007 addresses the consistency of disclosures required by IAS 28 and IAS 31.

## APPENDIX 2: RELEVANCE OF IAS 28 AND IAS 31 DISCLOSURE REQUIREMENTS TO FAIR VALUE ACCOUNTING

**(excerpt from May 2007 Board paper, updated based on decisions made by the Board at the meeting)**

25. The tables below specifies the disclosure requirements of IAS 28 and IAS 31 and applicability assessment for associates and jointly controlled entities accounted for at fair value.

### IAS 28 Disclosure requirements:

| **Disclosure Requirement** | **Applicability assessment for associates accounted for at fair value** |
|---|---|
| **37** The following disclosures shall be made: | |
| **(a)** the fair value of investments in associates for which there are published price quotations; | **Not applicable.** Investment measured at fair value. Paragraphs 25 – 30 of IFRS 7 require general fair value disclosures. |
| **(b)** summarised financial information of associates, including the aggregated amounts of assets, liabilities, revenues and profit or loss; | **Not relevant.** Fair value considered to be the most appropriate measure for these investments. |
| **(c)** the reasons why the presumption that an investor does not have significant influence is overcome if the investor holds, directly or indirectly through subsidiaries, less than 20 per cent of the voting or potential voting power of the investee but concludes that it has significant influence; | **Not applicable.** Fair value accounting applied on basis of nature of investor. |
| **(d)** the reasons why the presumption that an investor has significant influence is overcome if the investor holds, directly or indirectly through subsidiaries, 20 per cent or more of the voting or potential voting power of the investee but concludes that it does not have significant influence; | **Not applicable.** Fair value accounting applied on basis of nature of investor. |

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| **(e)** the reporting date of the financial statements of an associate, when such financial statements are used in applying the equity method and are as of a reporting date or for a period that is different from that of the investor, and the reason for using a different reporting date or different period; | **Not applicable**.<br>Investment measured at fair value. |
| **(f)** the nature and extent of any significant restrictions (eg resulting from borrowing arrangements or regulatory requirements) on the ability of associates to transfer funds to the investor in the form of cash dividends, or repayment of loans or advances; | **Relevant**.<br>Useful information for users of financial statements, irrespective of how the investment in the associate is measured. |
| **(g)** the unrecognised share of losses of an associate, both for the period and cumulatively, if an investor has discontinued recognition of its share of losses of an associate; | **Not applicable**.<br>Investment measured at fair value. |
| **(h)** the fact that an associate is not accounted for using the equity method in accordance with paragraph 13; and | **Not applicable**.<br>The scope exemption from equity accounting arises from the exemption in paragraph 1 of IAS 28 rather than the exemption in paragraph 13. |
| **(i)** summarised financial information of associates, either individually or in groups, that are not accounted for using the equity method, including the amounts of total assets, total liabilities, revenues and profit or loss. | **Not relevant**.<br>Same disclosures as would be required by paragraph 37(b). |
| **38** Investments in associates accounted for using the equity method shall be classified as non-current assets. The investor's share of the profit or loss of such associates, and the carrying amount of those investments, shall be separately disclosed. The investor's share of any discontinued operations of such associates shall also be separately disclosed. | **Not applicable.**<br>Investment measured at fair value. |
| **39** The investor's share of changes recognised directly in the associate's equity shall be recognised directly in equity by the investor and shall be disclosed in the statement of changes in equity as required by IAS 1 *Presentation of Financial Statements*. | **Not applicable**.<br>Investment measured at fair value. |
| **40** In accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* the investor shall disclose: | |

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|---|---|
| **(a)** its share of the contingent liabilities of an associate incurred jointly with other investors; and | **Relevant, but duplicates** disclosure required in paragraph 86 of IAS 37 (because the investor has a possible obligation). |
| (b) those contingent liabilities that arise because the investor is severally liable for all or part of the liabilities of the associate. | |

**IAS 31 Disclosure requirements:**

| **Disclosure Requirement** | **Applicability assessment for jointly controlled entities accounted for at fair value** |
|---|---|
| **54** A venturer shall disclose the aggregate amount of the following contingent liabilities, unless the probability of loss is remote, separately from the amount of other contingent liabilities: | |
| **(a)** any contingent liabilities that the venturer has incurred in relation to its interests in joint ventures and its share in each of the contingent liabilities that have been incurred jointly with other venturers; | **Relevant, but duplicates** disclosure required in paragraph 86 of IAS 37 (because the investor has a possible obligation). |
| **(b)** its share of the contingent liabilities of the joint ventures themselves for which it is contingently liable; and | |
| **(c)** those contingent liabilities that arise because the venturer is contingently liable for the liabilities of the other venturers of a joint venture. | |
| **55** A venturer shall disclose the aggregate amount of the following commitments in respect of its interests in joint ventures separately from other commitments: | |
| **(a)** any capital commitments of the venturer in relation to its interests in joint ventures and its share in the capital commitments that have been incurred jointly with other venturers; and | **Relevant.** Useful for users, given the capital intensive nature of many joint ventures, and the increased likelihood of an investor committing to provide capital when it has joint control. |
| **(b)** its share of the capital commitments of the joint ventures themselves. | |

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| **56** A venturer shall disclose a listing and description of interests in significant joint ventures and the proportion of ownership interest held in jointly controlled entities. | **Relevant.**<br>Users would find useful a list and description of significant joint ventures, irrespective of how the interest in the joint venture is measured, because of the special relationship between a venturer and joint venture (ie the existence of joint control). |
| A venturer that recognises its interests in jointly controlled entities using the line-by-line reporting format for proportionate consolidation or the equity method shall disclose the aggregate amounts of each of current assets, long-term assets, current liabilities, long-term liabilities, income and expenses related to its interests in joint ventures. | **Not applicable**.<br>Venturer does not apply either proportionate consolidation or equity accounting. |
| **57** A venturer shall disclose the method it uses to recognise its interests in jointly controlled entities. | **Relevant, but duplicates** disclosure in paragraph 108 of IAS 1 (summary of significant accounting policies). |

## APPENDIX 3: PROPOSED AMENDMENTS TO IAS 28 AND IAS 31

26. [Paragraph omitted from the observer note]