Project	**Annual Improvement**
Topic	**Information on EITF 08-10 and FASB Proposal on Scope of SFAS 160**

Introduction

1. In November 2008 the FASB's Emerging Issues Task Force discussed implementation issues relating to SFAS 160 *Noncontrolling Interests in Consolidated Financial Statements*. The EITF referred some of the issues to the FASB which on 29 April 2009 discussed amending the scope of the guidance in SFAS 160 on transactions with non-controlling interests that do not result in the loss of control and the loss of control of an entity.

2. The objective of this paper is to inform the Board about the FASB deliberations and to ask the Board whether it wishes to deliberate similar amendments to IAS 27 *Consolidated and Separate Financial Statements*.

   Issue: Should the Board propose amending the scope of the requirements in IAS 27 that deal (a) with transactions with non-controlling interest that do not result in the loss of control and (b) the loss of control of an entity?

Staff recommendation

3. The staff recommends that the Board do not add this issue to the annual improvements project.

Background

4. SFAS 160 (as issued in 2008) has amended the accounting according to US GAAP for transactions that result in a change in the parent's ownership interest in a subsidiary and/or the loss of control. SFAS 160 requires an entity to account for changes in an ownership interest that do not result in the loss of control of the subsidiary as equity transactions. In contrast, an entity deconsolidates a subsidiary when it ceases to control that subsidiary. Upon deconsolidation, the entity recognises a gain or loss in profit or loss attributable to the parent and measures any retained interest in the subsidiary at fair value.

5. Before the publication of SFAS 160, an entity would have applied the recognition criteria in other authoritative literature before deconsolidating a subsidiary and recognising a gain or loss on the transaction. Those criteria include an assessment of whether:

   (a) the seller has a continuing involvement in the business;

   (b) the buyer has a significant financial investment in the business;

   (c) the repayment of debt that constitutes the principal consideration in the transaction is dependent on future successful operations;

   (d) the business continues to depend on debt or contract performance guarantees by the seller.

6. Some US constituents have raised concerns that those criteria might be inconsistent with the requirements in SFAS 160. The problem arises because, in contrast to some of the recognition guidance, SFAS 160 requires an entity to deconsolidate a subsidiary when it loses control without any further evaluation of a continuing involvement in the former subsidiary or the probability that a potential gain from deconsolidation can be realised.

7. US constituents are concerned that SFAS 160 provides structuring opportunities to circumvent the recognition criteria in other standards. For example, an entity might use SFAS 160 to circumvent the criteria in SFAS 66 *Accounting for Sales of Real Estate* to account for transfer of an in-substance real estate or SFAS 140 *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities* to account for the transfer of financial instruments.

EITF Issue 08-10

8. In response to constituents' concerns, the EITF has discussed the following three issues relating to the accounting for:

   (a) sales of interests in a subsidiary that are in-substance real estate;

   (b) a transfer of an interest in a subsidiary to an equity method investee that results in deconsolidation of the subsidiary; and

   (c) the deconsolidation of a subsidiary upon the transfer of an interest in the subsidiary in exchange for a joint venture interest.

9. The EITF has deferred finalising those issues because the FASB has subsequently added a project to its agenda regarding the scope of SFAS 160 which would affect the consensuses-for-exposure reached on the issues in EITF 08-10.

Proposed change to the scope of SFAS 160 by FASB

10. In its 29 April meeting the FASB decided to limit the scope of the guidance in SFAS 160 on (a) transactions with non-controlling interests that do not result in the loss of control and (b) the loss of control to subsidiaries that are businesses or non-profit activities.

11. The FASB also decided to address the matters raised in EITF 08-10 as follows:

    (a) To modify EITF 01-2 *"Interpretations of APB Opinion No. 29"* to clarify that the exchange of a group of assets that constitutes a business in return for an equity interest should be accounted for in accordance with the deconsolidation provisions of SFAS 160.

    (b) The partial sale and deconsolidation provisions of SFAS 160 should not apply to in-substance real estate transactions.

    (c) SFAS 160 will apply when a subsidiary is transferred to an equity method investee or joint venture.

12. The FASB has asked its staff to obtain additional feedback from financial statement users on these issues before exposing the scope modifications to the public.

13. The requirements for transactions with non-controlling interests that do not result in the loss of control and the loss of control in SFAS 160 are aligned with those in IAS 27. Therefore, some IFRS constituents have asked the Board to clarify the scope of the requirements in IAS 27.

Staff Analysis

14. The staff has addressed the issue in paragraph 12 (c) in agenda paper 4A and Item 4 in Appendix B of agenda paper 13K. The issues in paragraphs 12 (a) and (b) are further analysed below:

15. We recommend that the Board does not amend the scope of IAS 27, but reviews as part of its post-implementation review of the business combinations project whether there are practice issues that suggest that the scope of the requirements for (a) transactions with non-controlling interest that do not result in the loss of control and (b) the loss of control in IAS 27 need to be amended.

16. We note that the proposed amendments to SFAS 160 do not affect the accounting requirements but rather, they affect the scope of the standard. However, the scope of those standards is currently not aligned as both refer to different definitions of control. Because of those different definitions, some transactions that satisfy the consolidation criteria according to US GAAP might still have to be consolidated under IFRS and vice versa. Therefore, the proposed amendments to SFAS 160 do not affect the level of alignment between SFAS 160 and IAS 27 that was achieved in phase II of the business combinations project.

17. We believe that the proposed amendments will have two major implications for US GAAP:

    (a) SFAS 160 will apply to the disposal of a business regardless of its form, i.e. whether or not the business is in a subsidiary. This would align the scope of SFAS 160 with that of SFAS 141(R).

    (b) A potential conflict between SFAS 160 and other accounting literature, such as the guidance on real estate transactions in SFAS 66 is resolved.

18. We note that although IFRS 3 and IAS 27 were both revised in phase II of business combination project, their scopes are different. The Board has never publicly deliberated any intention to align the scope of IAS 27 with that of IFRS 3, or to apply some of the requirements in IAS 27 only to subsidiaries that constitute a business. We believe that such a change to the scope of IAS 27 would be a major change to the standard and to practice and would therefore be outside the scope of the annual improvements project.

19. We believe also that there is no significant conflict between IAS 27 and the recognition criteria in other standards because of the lack of the detailed requirements in other standards that exist in US GAAP.

20. We note that an issue arises in US GAAP because it has particular recognition requirements for different transactions, especially for those relating to gain or revenue recognition. For example SFAS 66 contains specific recognition criteria for the sale of real estate and SOP xx for software revenue recognition. Those requirements are potentially inconsistent with the guidance in SFAS 160. This conflict is the main reason for the proposed change.

21. In contrast, there are less specific recognition requirements in IFRSs and those requirements, for example in IAS 18 *Revenue*, tend to be less detailed than the US guidance. We understand that constituents believe that they usually get a reasonable conclusion from applying the principles in IAS 18 and the requirements in IAS 27. For example, in practice the criteria in IAS 18.14 to assess whether revenue on the sale of goods should be recognised are used in conjunction with the control principle in IAS 27 to determine the substance of the transaction. We are not aware of significant practice issues that have evolved under IFRSs with respect to the interaction of IAS 27 and the recognition criteria in other standards.

22. Finally, we note that the Board is currently considering the notion of control in the consolidation project. Any change to the current standard will likely have to be reconsidered in that project.

23. For those reasons the staff recommends that the Board does not add this issue to the annual improvements project.

Question to the Board
Does the Board agree with the staff recommendation not to amend the scope of IAS 27?

Appendix A

A1. Agenda paper of FASB meeting on 29 April 2009 (starting from the next page)