

STAFF PAPER

May 2012

IASB Meeting

Project	IAS 27 Consolidated and Separate Financial Statements IAS 28 Investments in Associates and Joint Ventures		
Paper topic	Definition of the term 'non-monetary asset' in SIC-13 and IAS 28 (revised in 2011)		
CONTACT(S)	Patrick Le Flao	pleflao@ifrs.org	+44 (0)20 7246 6935

This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

Preliminary comment: this paper was originally posted for the April Board meeting but was deferred until May.

Introduction

1. The Committee received a request to clarify whether a business meets the definition of a 'non-monetary asset'. The question was asked within the context of identifying whether the requirements of SIC-13 *Jointly Controlled Entities Non-Monetary Contributions by Venturers* and IAS 28 *Investments in Associates and Joint Ventures* (revised in 2011) apply where a business is contributed to:
 - (a) a jointly controlled entity (JCE) as defined in IAS 31 *Interests in Joint Ventures*; or to:
 - (b) a joint venture (JV) as defined in IFRS 11 *Joint Arrangements*; or to:
 - (c) an associatein exchange for an equity interest in that JCE/JV or associate.
2. At the January 2012 meeting, the Committee noted that the submission is related to the issues arising from the acknowledged inconsistency between the requirements in IAS 27 *Consolidated and Separate Financial Statements* and SIC-13, in dealing with the loss of control of a subsidiary that is contributed to a JCE/JV or an

associate. The Committee acknowledged that this new submission proposes an alternative way of considering the matter but it continues to think that the best course of action would be to consider the matter as part of a broader Board project.

3. The Committee also acknowledged, however, that the potential timing for the broader project is uncertain and so decided to ask the Board whether it wants the Committee to consider further how to resolve the inconsistency between the requirements in IAS 27 and those in SIC-13. The Committee directed the staff to perform a preliminary analysis of what might be the alternatives by which the Board could address this matter. The Committee discussed these alternatives at the March 2012 meeting. The objective of this paper is to present:
 - (a) the alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011); and
 - (b) the Committee's recommendations on that issue.

Structure of the paper

4. This agenda paper includes:
 - (a) The Committee's discussions at the January 2012 meeting (see introduction above);
 - (b) Background information on the issue;
 - (c) Scope of the transactions analysed in this paper;
 - (d) General considerations regarding the accounting for contributions and sales with regards to structuring opportunities;
 - (e) A summary of the alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011) and the Committee's recommendations;
 - (f) A discussion on whether contributions made to a joint operation as defined in IFRS 11 should also be considered;
 - (g) Appendix A: tables showing the outcome of the alternatives presented in the paper;

- (h) Appendix B: detailed analysis of the alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011); and
- (i) Appendix C: submission.

Background information

5. There is a conflict between IAS 27 and SIC-13 in dealing with the loss of control of a subsidiary that is contributed to a JCE/JV or an associate in exchange for an equity interest in that JCE/JV or associate. Paragraph 5 of SIC-13 restricts gains and losses arising from contributions of non-monetary assets to a JCE to the extent of the interest attributable to the other equity holders in the JCE. Paragraph 34 of IAS 27 requires full profit or loss recognition on the loss of control of the subsidiary. The consequence is that a larger gain or loss (if any) would be accounted for under IAS 27 in comparison to the gain/loss that would be accounted for under SIC-13 at the contribution date.
6. As a result, diversity in practice has emerged on the accounting for a loss of control of a subsidiary when it is contributed to a JCE. Entities, in effect, have an accounting policy choice of applying either IAS 27 or SIC-13.
7. The submitter also notes that the incorporation of SIC-13 into paragraph 30 of IAS 28 (2011) may introduce further diversity of practice in the future when IAS 28 (2011) will become mandatory. Indeed, paragraph 30 of IAS 28 (2011) applies to the contribution of a non-monetary asset to a JV or an associate in exchange for an equity interest in the JV or associate. Some consider that under the current requirements, SIC-13 should only be applied to contributions to a JCE and not to contributions to an associate. However, it should be noted that many also apply SIC-13 by analogy to contributions to an associate (on the basis that paragraph 22 of IAS 28 includes requirements regarding the elimination of profits and losses resulting from upstream and downstream transactions similar to the requirements in IAS 31).
8. The submitter thinks that this diversity in practice could be reduced if there were to be a clarification as to whether a business (as defined in IFRS 3

Business Combinations) qualifies as a non-monetary asset under SIC-13 (and under IAS 28 revised in 2011). The submission is shown in Appendix C.

9. It should be noted that the inconsistency between IAS 27 and SIC-13/IAS 28 (revised in 2011) will remain when IFRS 10 *Consolidated Financial Statements* will replace IAS 27. In fact, the requirements in IFRS 10 (paragraphs 25 and B98) on the accounting for the loss of control of a subsidiary are similar to the requirements in IAS 27 (paragraph 34).

Scope of the transactions analysed in this paper

10. This paper specifically addresses the accounting for the following transactions:
 - (a) Contributions of an interest in a subsidiary to a JCE/JV or associate in exchange for an equity interest in the JCE/JV or associate;
 - (b) Sales of an interest in a subsidiary by a joint-venturer to a JCE/JV or by an investor to an associate in exchange for cash.

This paper also addresses the accounting for contributions/sales of assets not housed in a subsidiary.

11. It should be noted that:
 - (a) In this paper, the contribution of an interest in a subsidiary is referred to as an 'indirect contribution' and the contribution of assets not housed in a subsidiary is referred to as a 'direct contribution'.
 - (b) A subsidiary is defined as in IAS 27 (paragraph 4), ie it is an entity (including an unincorporated entity such as a partnership) that is controlled by another entity.
 - (c) All the contributions/sales considered in this paper result in a loss of control of the subsidiary or assets contributed/sold.
 - (c) The subsidiary or the assets contributed/sold may constitute a business or not.
 - (d) The entity that makes the contribution/sale and the entity that receives the subsidiary or the assets contributed/sold may be under common control (as

defined in IFRS 3). These transactions are not excluded from the scope of IAS 27, IAS 28 or IAS 31/SIC-13.

- (e) The entity that makes the contribution/sale retains joint control on, or significant influence over, the interest in the subsidiary or the assets contributed/sold.
- (f) Contributions/sales may be made by the entity either simultaneously upon establishing the JCE/JV or associate or subsequently.
- (g) In addition to the equity interest in the JCE/JV or associate received in exchange for the contribution, the entity that contributes the subsidiary or the assets may also receive an additional consideration in cash.

12. Contributions made to a Joint Operation (JO) as defined in IFRS 11 are discussed in the last section of this Agenda Paper.

General considerations regarding the accounting for contributions and sales with regards to structuring opportunities

13. We think that the same accounting principles should be applied whether the contribution is a direct or an indirect contribution. In other words, we do not think that the accounting should be driven by whether an entity exists or not. It should rather be driven by the substance of the transaction. If the principles were different for direct and indirect contribution, this would create structuring opportunities. For example, the accounting should be similar in the two following situations:

- (a) Entity A directly contributes a group of assets that constitute a business to Entity B in exchange for an interest in B so that B becomes a JV; or
- (b) Entity A creates a wholly owned Subsidiary S, contributes the assets that constitute a business to S and then contributes S to Entity B in exchange for an interest in B so that B becomes a JV.

14. We also think that the same accounting principles should be applied whether the interest in a subsidiary or the assets are contributed in exchange for an equity interest or are sold in exchange for cash. If they were not accounted for similarly,

this would create structuring opportunities. For example, the accounting should be similar in the two following situations:

- (a) Entity A contributes Subsidiary S to Entity C in exchange for an interest in C so that C becomes a JV;
- (b) Entity A contributes cash to Entity C in exchange for an interest in C so that Entity C becomes a JV and A simultaneously sells Subsidiary S to Entity C in exchange for the cash contributed.

Summary of the alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011) and Committee's recommendations

15. At the March 2012 meeting, the Committee discussed various alternatives in order to resolve the inconsistency noted:

- (a) Alternative 1: account for all contributions similarly in accordance with the rationale developed in IAS 27;
- (b) Alternative 2: account for all contributions of businesses (whether housed in a subsidiary or not) under IAS 27 and account for all other contributions under SIC-13;
- (c) Alternative 3: account for all contributions to JCE/JV or associate under SIC-13;
- (d) Alternative 4: account for all direct contributions (whether they constitute a business or not) to JCE/JV or associate under SIC-13 and account for all indirect contributions under IAS 27; or
- (e) Alternative 5: account for direct contributions of assets that do not constitute a business to JCE/JV or associate under SIC-13 and account for all other contributions under IAS 27.

16. The Committee expressed support for Alternative 1 or Alternative 2. Both alternatives lead to the same outcome for a business that is contributed to a JCE/JV or associate. As a result, with regard to a business that is contributed to a JCE/JV or associate, the Committee expressed support for a full gain recognition on the

loss of control of the business (whether the business is housed in a legal entity or not).

17. A majority of Committee members considered that Alternative 1 is the most robust alternative but requires addressing various cross-cutting issues. The Committee noted that Alternative 2 can be more easily implemented but puts more focus on the definition of a business. Indeed, in Alternative 2, the accounting for contributions of businesses is different from the accounting for contributions of assets that do not constitute a business.
18. The Committee also noted that:
 - (a) Alternative 3 is not consistent with the latest thinking of the Board developed in the Business Combination project;
 - (b) Alternatives 4 and 5 create structuring opportunities. However, structuring opportunities in Alternative 5 are limited to contributions of assets that do not constitute a business. Alternative 5 would still resolve the main issue, which is the accounting for contribution of businesses.
19. Tables showing the current practice and the outcome of the different alternatives described above are provided in Appendix A. A detailed analysis of each alternative is provided in Appendix B.

Question for the Board

Does the Board want the Committee to consider further how to resolve the inconsistency between the requirements in IAS 27 and those in SIC-13/IAS 28 (2011)? If so, does the Board want to express support for one of the alternatives described in this paper?

Contributions to a joint operation in the scope of IFRS 11

20. In this paper, we do not discuss the contributions made to a joint operation as defined in IFRS 11. This question was not raised in the submission. The Committee decided to inform the Board that the Committee had not considered the contributions to joint operations as defined in IFRS 11 and the Committee was therefore not making any recommendations on that issue. We think that the scope of the project should be limited to contributions to a JCE/JV or associate.

Question for the Board

Does the Board agree not to address in this project the accounting for contributions made to joint operations?

Appendix A: tables showing the outcome of the different alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011)

- A1. We provide below tables showing the current practice and the outcome of the different alternatives described in this paper. Each table distinguishes between:
- a. direct contribution of assets that constitute a business;
 - b. direct contribution of assets that do not constitute a business;
 - c. contribution of a subsidiary that constitutes a business;
 - d. contribution of a subsidiary that does not constitute a business;
 - e. the level of interest retained: the interest retained may be an associate within the scope of IAS 28 or a JCE/JV within the scope of IAS 31/IFRS 11.
- A2. For the sake of clarity, the tables also show the treatment applicable when an investment within the scope of IAS 39/IFRS 9 is retained. However, it should be noted that the paper focuses on the accounting for contributions to a JCE/JV or associate, ie contributions for which there is currently diversity in practice.

Current practice: account for contributions either under IAS 27 or under SIC-13

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Full gain or partial gain (1) (2)	Full gain or partial gain (1)	Partial gain (3)	Full gain or partial gain (1)
Retained interest = JCE/JV	Full gain or partial gain (1) (2)	Full gain or partial gain (1)	Partial gain (3)	Full gain or partial gain (1)

- (1) Because of the conflicting guidance in the IFRS literature, the entity has in practice an accounting policy choice of applying consistently either IAS 27 or SIC-13 to all the contribution (although IFRSs do not present it as an accounting policy choice).
- (2) Because IAS 27 defines a subsidiary as an entity (including an unincorporated entity) that is controlled, some consider that a business meets the definition of an entity in IAS 27, and as a result, there is also an accounting policy choice for direct contributions of assets that constitute a business.
- (3) IAS 27 does not apply to direct contributions of assets that do not constitute a business. As a result, SIC-13 applies in that case and there is no accounting policy choice.

Alternative 1: account for all contributions similarly in accordance with the rationale developed in IAS 27

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Full gain	Full gain	Full gain	Full gain
Retained interest =JCE/JV	Full gain	Full gain	Full gain	Full gain

Alternative 2: account for all contributions of businesses under IAS 27 and account for all other contributions under SIC-13

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Full gain	Full gain	Partial gain	Partial gain
Retained interest = JCE/JV	Full gain	Full gain	Partial gain	Partial gain

Alternative 3: account for all contributions to JCE/JV or associate under SIC 13

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Partial gain	Partial gain	Partial gain	Partial gain
Retained interest = JCE/JV	Partial gain	Partial gain	Partial gain	Partial gain

Alternative 4: account for all direct contributions to JCE/JV or associate under SIC 13 and account for all indirect contributions under IAS 27

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Partial gain	Full gain	Partial gain	Full gain
Retained interest = JCE/JV	Partial gain	Full gain	Partial gain	Full gain

Alternative 5: account for direct contributions of assets that do not constitute a business to JCE/JV or associate under SIC 13 and account for all other contributions under IAS 27

All the contributions result in a loss of control	Direct contribution of assets that constitute a business	Contribution of a subsidiary that constitutes a business	Direct contribution of assets that do not constitute a business	Contribution of a subsidiary that does not constitute a business
Retained interest = Investment (IAS 39)	Full gain	Full gain	Full gain	Full gain
Retained interest = Associate	Full gain	Full gain	Partial gain	Full gain
Retained interest = JCE/JV	Full gain	Full gain	Partial gain	Full gain

Appendix B: detailed analysis of the alternatives by which the Board could resolve the inconsistency between IAS 27 and SIC-13/IAS 28 (2011)Alternative 1: account for all contributions similarly in accordance with the rationale developed in IAS 27

- A3. During its discussions on the business combination project that led to the publication of IAS 27 (revised in 2008), the Board decided that the loss of control of a subsidiary is such a significant economic event that it should trigger re-evaluation of the retained interest in the subsidiary at fair value through profit or loss. This logic in IAS 27 also applies if the parent of the subsidiary retains joint control or significant influence over the retained interest.
- A4. The consequence in IAS 27 is that the partial disposal of an interest in a subsidiary resulting in a loss of control is accounted for as a full disposal followed by a reacquisition of the retained interest. This is because the investment retained is substantially different from the initial investment. As a result, any investment retained in the former subsidiary is recognised at its fair value at the date when control is lost.
- A5. Paragraph 37 of IAS 27 states that the fair value of the retained interest in the former subsidiary is the fair value on initial recognition of a financial asset in accordance with IAS 39/IFRS 9 or, when appropriate, the cost on initial recognition of an investment in an associate or JCE/JV. In other words, IAS 27 states that a full gain should be recognised on the loss of control of a subsidiary, even if the investor retains an interest.

34 If a parent loses control of a subsidiary, it:

...

(d) recognises any investment retained in the former subsidiary at its fair value at the date when control is lost;

...

37 The fair value of any investment retained in the former subsidiary at the date when control is lost shall be regarded as the fair value on initial recognition of a financial asset in accordance with IFRS 9 Financial

Instruments or, when appropriate, the cost on initial recognition of an investment in an associate or jointly controlled entity.

- A6. We note that the rationale that underlies SIC-13 is different. SIC-13 is an interpretation that follows the rationale of IAS 28 (paragraph 30 in the revised version and paragraph 22 in the previous version) and IAS 31 (paragraph 48) with regard to the elimination of gains to the extent of the portion of the interest retained in transactions such as contributions or sales of assets between an investor and an associate or between a joint venturer and a JCE/JV). Thus, the rationale in SIC-13 is based on requirements that deal with the application of proportionate consolidation and the equity method.
- A7. We also note that IAS 28 (paragraph 10) states that under the equity method, the investment in an associate or a joint venture is recognised at cost on initial recognition, but this standard does not provide guidance on how to measure the cost of a retained interest in a former subsidiary. Instead IAS 27 (paragraph 37) specifies how to initially recognise and measure the cost of a retained interest in an associate or a joint venture.
- A8. Lastly, we note that according to IAS 27, a group is a parent and all its subsidiaries, ie entities that are controlled. A group does not ‘consolidate’ JCE/JV or associates. Rather, they are considered to be some type of investments accounted for in a particular manner. In that case, some could argue that it does not make sense to partially eliminate gains or losses (if any) in transactions such as contributions or sales of assets between a joint venturer and the JCE/JV or between an investor and an associate because this elimination is a consolidation procedure.
- A9. As a result, we think that the Board could require that all contributions (as described in the section *Scope* above) should be accounted for similarly in accordance with the rationale developed in IAS 27, ie that a full gain should be recognised when the subsidiary or the assets are contributed. The basis for this alternative is that:

- a. the loss of control should be considered a significant event that triggers the reevaluation at fair value of the retained interest in the JCE/JV or associate in all cases; and
 - b. the treatment in IAS 27 represents the latest thinking of the Board.
- A10. If Alternative 1 is applied, we think that the same rationale should be applied to sales (as described in the section *Scope* above). In other words, the loss of control of any asset as a result of a sale would trigger the recognition of a full gain and the recognition of any asset retained at fair value:
- a. whether the assets constitute a business or not;
 - b. whether the assets are housed in a subsidiary or not.
- A11. Alternative 1 would require amending:
- a. paragraph 30 of IAS 28 (2011). This paragraph corresponds to the requirements in SIC-13 incorporated in IAS 28 (2011).
 - b. paragraph 28 of IAS 28 (2011) on the accounting for sales between a joint venturer and a JCE/JV or between an investor and an associate. A full gain would be recognised on these sales (as opposed to a partial gain currently).
- A12. Because IAS 28 (2011) is effective for annual periods beginning on or after 1 January 2013 and because SIC-13 is superseded by IAS 28 (2011), we do not think that there is a need to amend SIC-13 or IAS 28 (old version).

Other considerations with regard to Alternative 1

- A13. We consider that this alternative is a broad project that would require a review of the current literature (as opposed to Alternative 2 or Alternative 3 described below that, in our view, can be more easily implemented). We think that if the Board decides to pursue Alternative 1, the following cross-cutting issues should also be considered:
- a. the definition of a ‘group’ in IAS 27 and its implications on the measurement requirements of investments outside the group boundaries (such as joint arrangements and associates) and the

accounting for 'upstream' and 'downstream' transactions with entities outside the group boundaries (such as joint arrangements and associates);

- b. the procedures to carry out when implementing the 'equity method'.

A14. We also think that it would be preferable if the Board could clarify whether IAS 27/IFRS 10 applies to the loss of control of a subsidiary that does not constitute a business. For example, it is not clear whether the sale of a subsidiary that contains only financial assets (such as loans) should be accounted for under the derecognition requirements of IAS 39/IFRS 9 (or under the requirements of IAS 27/SIC-12).

A15. It should be noted that for direct contributions of assets, the full gain would be accounted for at the date when the assets are derecognised in accordance with the relevant IFRSs. Indeed, at the date of derecognition of the assets, the control of the assets is transferred:

- a. Tangible/intangible assets and inventories are derecognised (and a full gain or loss is accounted for simultaneously) when the criteria listed in IAS 18 paragraph 14 are met (IAS 16 and IAS 38 refer back to IAS 18 for determining the date of disposal of a tangible/intangible asset). Those criteria include the loss of control and the transfer of risks and rewards. In the exposure draft *Revenue from Contracts with Customers*, tangible/intangible assets and inventories would be derecognised when the control of the assets is lost (the transfer of risks and rewards being an indicator of the transfer of control).
- b. Financial assets are derecognised (and a full gain or loss is accounted for simultaneously) when the conditions in IAS 39 (paragraphs 17-20) are met. These conditions include the loss of control and the transfer of risks and rewards. It should be noted that a partial gain or loss is recognised when the entity has a continuing involvement in the financial assets.

Alternative 2: account for all contributions of businesses under IAS 27 and account for all other contributions under SIC-13

- A16. Another proposal could be to limit SIC-13 to contributions of assets that do not constitute a business. In other words, IAS 27 would apply to the loss of control of businesses (whether the business is a subsidiary or not), including cases where the investor has retained joint control or significant influence over the investee.
- A17. The basis of this alternative is that the requirements in IAS 27 on the loss of control of a subsidiary are closely linked to the Business Combinations project, and should therefore apply to all businesses (whether housed in a subsidiary or not). Because groups of assets that do not constitute a business were not part of that project, there is no reason to change the accounting for these contributions.
- A18. However, we think that the conflict between IAS 27 and SIC-13 would be resolved only if it were also made clear that the same accounting should be applied whether the contribution is a direct or an indirect contribution. As a result, clarifying SIC-13 and the definition of a non-monetary asset would not be sufficient to solve the issue in full. In our view, if Alternative 2 is applied, it should be made clear that IAS 27 does not apply to contributions of subsidiaries that do not constitute a business. In that case, contributions of subsidiaries that do not constitute a business to a JCE/JV or an associate would be accounted for under the requirements of SIC-13 and IAS 28 (revised in 2011). If the clarification in IAS 27 were not made, the accounting might be driven by whether an entity exists or not (and not by whether or not a business is present).
- A19. We note that the FASB chose this alternative and amended SFAS 160 *Noncontrolling Interests in Consolidated Financial Statements* such that it applies to the loss of control of a business that is transferred to an equity method investee or joint venture, regardless of its form, ie whether or not the business is housed in a subsidiary (EITF 08-10).
- A20. If alternative 2 is applied, we think that the same logic should be applied for sales by a joint venturer to a JCE/JV or by an investor to an associate. As a result, the requirements in SIC-13 and IAS 28 (revised in 2011) would apply to sales of assets that do not constitute a business. The requirements in IAS 27 would apply to sales of assets that constitute a business. IAS 27 is closely linked

to the Business Combination project and it would make sense, in our view, to apply the guidance in IAS 27 to direct contributions of businesses.

A21. Alternative 2 would require:

- a. amending the definition of non-monetary assets in IAS 28 (2011) so that it excludes businesses (as defined in IFRS 3) and it includes subsidiaries that do not constitute a business;
- b. amending IAS 27 to clarify that it applies to the loss of control of a business not housed in a subsidiary and that it does not apply to the loss of control of a subsidiary that does not constitute a business;
- c. clarifying that paragraph 28 of IAS 28 (2011) on the accounting for sales between a joint venturer and a JCE/JV or between an investor and an associate only applies to sales of assets that do not constitute a business.

Alternative 3: account for all contributions to JCE/JV or associate under SIC 13

A22. The guidance in SIC-13 would apply to all direct and indirect contributions to a JCE/JV or associate:

- a. whether the assets constitute a business or not; and
- b. whether this is a direct contribution of a group of assets or a contribution of an interest in a subsidiary.

A23. This would require specifying that non-monetary assets as defined in SIC-13 and IAS 28 (revised in 2011) include businesses and assets that do not constitute a business.

A24. The guidance in IAS 27 would only apply to contributions of businesses in which the entity that contributes the assets loses control and does not retain joint control or significant influence (ie the entity accounts for a financial asset under IAS 39/IFRS 9 if there is a retained interest). This would require an amendment to IAS 27.

- A25. Sales of assets between a joint venturer and a JCE/JV or between an investor and an associate would remain accounted for under the current requirements of IAS 28, IAS 31 and IAS 28 (revised in 2011).
- A26. We note that this alternative is not consistent with the latest thinking of the Board in the Business Combination project and the rationale developed in IAS 27 that a loss of control of a subsidiary is a significant event (see section on Alternative 1 above). As a result, we do not think that this alternative should be applied. However, we also note that a post-implementation review will be performed on IFRS 3/IAS 27 in 2012/2013 and that this issue will be considered in the post-implementation review.

Alternative 4: account for all direct contributions to JCE/JV or associate under SIC-13 and account for all indirect contributions under IAS 27

- A27. We do not think that this alternative should be applied, as it allows structuring opportunities. Indeed, the accounting would be driven by whether a subsidiary exists or not (and not by the substance of the transaction). Moreover, in our view, this alternative is not consistent with the fact that the guidance in IAS 27 was developed as part of the Business Combination project and should consequently address direct contributions of businesses.

Alternative 5: account for direct contributions of assets that do not constitute a business to JCE/JV or associate under SIC-13 and account for all other contributions under IAS 27

- A28. We do not think that this alternative should be applied, because it allows structuring opportunities for contributions of assets that do not constitute a business. Indeed, in that case, the accounting would be driven by whether a subsidiary exists or not (and not by the substance of the transaction). However, we think that it would still resolve the main issue, which is the accounting for the contribution of businesses.
- A29. If this alternative is applied, the requirements in IAS 27 would apply to all indirect contributions (whether the subsidiary constitutes a business or not) and to direct contributions of businesses. The basis for this treatment is that IAS 27

already applies to all indirect contributions. Combined with the fact that the guidance in IAS 27 was developed as part of the Business Combination project, there would be no reason not to apply the same rationale to direct contributions of businesses. Because direct contributions of assets that do not constitute a business are not within the scope of IAS 27 and were not discussed as part of the Business Combination project, the accounting for such transactions would be left to SIC-13. This alternative would not require amending IAS 27 but would require modifying IAS 28 (2011).

Appendix C: submission

Issue:

In its May 2011 meeting the Interpretations Committee discussed the accounting for a loss of control over a subsidiary through a contribution of the subsidiary to a jointly controlled entity (JCE) or an associate. One of the issues in the agenda request was whether it makes a difference if the subsidiary is a business (as defined in IFRS 3), or is a single-asset entity. The Committee concluded that the issues would be best resolved by the Board as part of a broader project on equity accounting. We believe the Committee could eliminate some diversity in practice before any broader project if the Committee were to provide clarification on the definition of the term 'non-monetary asset' used in SIC-13 and IAS 28 (2011)'.

SIC-13 and IAS 28.30 (2011) require that gains and losses resulting from a contribution of a non-monetary asset to an associate or a joint venture in exchange for equity interest in an associate or a joint venture only be recognised to the extent of unrelated investors' interests in the associate or joint venture. IAS 28.22 requires that profits and losses resulting from sales of assets between an investor and an associate are recognised in the investor's financial statements only to the extent of unrelated investors' interests in the associate.

IAS 27.34 is clear that if a parent loses control of a subsidiary, the parent recognises any investment retained in the former subsidiary at its fair value through profit and loss. Diversity in practice has emerged on the accounting for a loss of control over a business when that business is contributed to a JCE or an associate in exchange for an equity interest in that JCE or associate. The consequence is that some companies would recognise a higher gain/loss and investment in JCE or associate at the contribution date (see Appendix C for example). This diversity in practice could be reduced if there was a clarification as to whether a business qualifies as a non-monetary asset under SIC-13 and IAS 28 (2011).

Current practice:

There are two views currently as to whether a business meets the definition of a non-monetary asset and therefore an entity can apply SIC-13 or IAS 28.30 (2011) for a contribution of a business to a JCE or associate.

View 1: SIC-13 concepts should not be applied to contributions of a 'business', as defined in IFRS 3 (2008), to associates or joint ventures. References to non-monetary assets in IFRS refer to items such as land, intangibles, plant and machinery. IFRS 3.38 differentiates nonmonetary assets from a business (Refer to Appendix A). US GAAP defines non-monetary assets and liabilities as assets and liabilities other than monetary ones and provides examples such as inventories; investments in common stocks; property, plant, and equipment; and liabilities for rent collected in advance. [APB 29, paragraph 3].

A subsidiary is defined in IAS 27.4 as an entity, including an unincorporated entity such as a partnership that is controlled by another entity (known as the parent). In its July meeting the IFRS IC discussed that an acquirer in a reverse acquisition does not need to

be a 'legal entity' because the notion of an 'entity' in IFRS 3 refers to the concept of the 'reporting entity' as defined in the exposure draft Conceptual Framework for Financial Reporting. Therefore, it seems to follow that IAS 27.34 requires a parent to recognise any investment retained in the former 'reporting entity' at its fair value through profit and loss if a parent loses control of a 'reporting entity'.

The guidance in SIC-13 and IAS 28.30 (2011) should be used for non-monetary assets. The guidance in IAS 28.22 should be used for sales of assets between an investor and an associate. The guidance in IAS 27 should be used for loss of control of a subsidiary and gains/losses recognised on the loss of control are not restricted to the amount attributable to the other investors' interests in the JCE or associate.

View 2: Non-monetary asset is defined in IAS 21.16 and may include the concept of a business. Under IAS 21.16, a non-monetary asset is an asset that does not carry the right to receive a fixed or determinable number of units of currency. Non-monetary asset includes PPE, prepaid for goods/services, intangible assets and inventories.

IAS 39 indicates that equity instruments that are held as available for sale financial assets are non-monetary assets (IAS 39.AG83). This suggests that equity investments in subsidiaries, associates or JCEs are non-monetary items. In addition, non-monetary items are defined as opposed to monetary items. Thus, a business could meet the definition of a non-monetary asset. Therefore, it should be possible to apply SIC-13 and IAS 28.30 (2011) to contribution of a business to a JCE.

Reasons for the IFRS IC / IASB to address the issue:

The issue occurs frequently and we believe it is resulting in divergent treatment in practice. At least one large accounting firm has published guidance that there is a policy choice on the accounting for a loss of control over a business when that business is contributed to an associate in exchange for an equity interest in that associate. View 1 is followed under US GAAP based on the amendments to Subtopic 810-10 issued in January 2010 (see Appendix A).

The incorporation of SIC-13 into IAS 28 (2011) may introduce further diversity of practice as currently all but one large accounting firm considers that a policy choice applies to contributions to a JCE but not an associate. Therefore the proposed amendment could avoid further divergence in the accounting for contribution(s) to associate(s). We believe that a minor clarification on the definition of non-monetary assets through an improvement of IAS 28 (2011) could assist entities in making consistent judgements about the accounting for gains and losses resulting from a contribution of a business to an associate or a joint venture in exchange for an equity interest in an associate or a joint venture. See Appendix B for suggested improvements to IAS 28.30 (2011).