Emerging Economies Group meeting

Date: October 2023

Project: Equity Method

Topic: Overview of the IASB’s tentative decisions

Contacts: Filippo Poli (fpoli@ifrs.org)
Mostafa Mouit (mmouit@ifrs.org)
Edlyn Chigerwe (edlyn.chigerwe@ifrs.org)

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Purpose of this session

• Provide EEG members with an overview of the IASB’s tentative decisions on the Equity Method project.

• Ask for views on those tentative decisions, including the potential effects (costs and benefits) of those decisions.
Project background and overview
### Application

- **required in consolidated financial statements** for investments in associates and joint ventures
- **permitted in separate financial statements** for investments in subsidiaries, associates and joint ventures

### Equity method of accounting

- **on obtaining significant influence**, recognise any difference between the cost of the investment and the investor’s share of the net fair value of the investee's identifiable assets and liabilities either as goodwill, or as a gain from a bargain purchase
- thereafter, the **investor’s share of the investee’s**:
  - **profit or loss** is recognised in **profit or loss**.
  - **other comprehensive income** is recognised in **other comprehensive income**.
- **distributions** received adjust the carrying amount of the investment.
Overview of the Equity Method project

Objective
Develop answers to application questions about the equity method, as set out in IAS 28 *Investments in Associates and Joint Ventures*, using the principles derived from IAS 28.

Project approach

<table>
<thead>
<tr>
<th>Identify application questions</th>
<th>Identify the principles</th>
<th>Apply the principles to the application questions</th>
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Project update
IASB has made tentative decisions on application questions, and on improvements to disclosure requirements, for:

- **Associates**

Next steps**
Discuss implications of applying tentative decisions, and possible improvements to disclosure requirements, to:

- **Joint ventures**
- **Subsidiaries in separate financial statements**

* For more details about the project, please refer to the project page on the IFRS website, including the summary of the IASB's tentative decisions on application questions.

** At its October 2023 meeting, the IASB will be asked to decide if all the tentative decisions apply to investments (other than those in associate entities) accounted for using the equity method.
Project timeline

- **Project moved from research programme to standard-setting work plan**: April 2023
- **Aim to complete discussions**: November 2023
- **Exposure Draft publication**: September 2024
- **Deadline for comment**: Q1 2025
- **Redeliberations**: 2025

Consultation period
Overview of IASB’s tentative decisions
### Obtaining significant influence

<table>
<thead>
<tr>
<th>Application question</th>
<th>IASB’s tentative decision</th>
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<tr>
<td>An investor, with a previously held interest in an entity, acquires an additional interest and obtains significant influence. Does the initial measurement of the investment include the original purchase cost of the previously held interest or the carrying amount of that interest in accordance with IFRS 9 <em>Financial Instruments</em>?</td>
<td>An investor would measure the cost of an investment, when an investor obtains significant influence, <strong>at the fair value</strong> of the <strong>consideration transferred</strong>, including the <strong>fair value of any previously held interest</strong> in the associate.</td>
</tr>
</tbody>
</table>
Initial recognition of an investment in an associate – deferred taxes

**Application question**

Does an investor account for a deferred tax asset/liability arising from recognising its share of the associate’s net identifiable assets and liabilities at fair value?

**IASB’s tentative decision**

An investor would account for, and include in the carrying amount of its investment in an associate, a deferred tax asset/liability arising from recognising its share of the associate’s net identifiable assets and liabilities at fair value.
## Contingent consideration

<table>
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<tr>
<th>Application question</th>
<th>IASB’s tentative decision</th>
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<tbody>
<tr>
<td>How does an investor, initially and subsequently, recognise and measure contingent consideration on acquisition of an investment in an associate?</td>
<td>On obtaining significant influence in an associate, an investor would recognise contingent consideration as part of the cost of the investment and measure it at fair value. For each subsequent reporting period, an investor would measure it (except contingent consideration classified as equity) at fair value at each reporting date and recognise changes in fair value in profit or loss.</td>
</tr>
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</table>
### Application question

How does an investor apply the equity method when purchasing an additional interest in an associate while retaining significant influence?

### IASB’s tentative decision

An investor would recognise any difference between the cost of the additional interest and its additional share in the net fair value of the associate’s identifiable assets and liabilities either as goodwill or as a gain from a bargain purchase.

The investment is an accumulation of purchases.
Purchase of an additional interest and ‘catch up’ of unrecognised losses

**Application question**

Is an investor that has reduced the carrying amount of its investment to nil required to ‘catch up’ unrecognised losses if it purchases an additional interest in the associate?

**IASB’s tentative decision**

An investor, that has reduced the carrying amount of its investment to nil and has stopped recognising its share of an associate’s losses, would not recognise any unrecognised losses on purchasing an additional interest in the associate.
### Disposal of an interest in an associate

<table>
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<tr>
<th>Application question</th>
<th>IASB’s tentative decision</th>
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</thead>
</table>
| How does an investor apply the equity method when disposing of an interest in an associate while retaining significant influence? | An investor would measure the portion of the investment to be derecognised as a proportion of the carrying amount of the investment at the date of the disposal. 

The investor is measuring a single investment in an associate. |
### Other changes in an investor’s ownership interests

<table>
<thead>
<tr>
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<th>IASB’s tentative decision</th>
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<tbody>
<tr>
<td>Does an investor recognise its share of other changes in an associate’s net assets while retaining significant influence, and if so, how is the change presented?</td>
<td>When an investor's ownership interest increases or decreases, the investor would recognise that change as a purchase of an additional interest or a partial disposal.</td>
</tr>
</tbody>
</table>
Gains and losses from transactions with associates

Application question

How should an investor recognise gains or losses that arise from the sale of a subsidiary to its associate?

IASB’s tentative decision

An investor would recognise the full gain or loss on all transactions with its associate.
Recognition of losses—share of the associate’s profit or loss and other comprehensive income

**Application question**

How does an investor recognise each component of the investee’s comprehensive income:

- in the period when the carrying amount of the investment is reduced to nil?
- after the carrying amount of the investment has been reduced to nil?

**IASB’s tentative decision**

The IASB tentatively decided that:
- if the share of an associate’s comprehensive income is a loss larger than that carrying amount of its investment, an investor would recognise in order its share of profit or loss and its share of OCI;
- after the carrying amount of its investment has been reduced to nil the investor would recognise separately its share of each component of comprehensive income.
### Impairment – assessing if an investment may be impaired

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| Does an investor assess a decline in fair value in relation to the original purchase price or the carrying amount at the reporting date? | • Change the term ‘cost’ to ‘carrying amount’ in paragraph 41C of IAS 28.  
• Add as objective evidence of impairment the purchase price an investor pays for an additional interest in an associate (or the selling price for a partial disposal) that is lower than the carrying amount of the investment in the associate at the date of the purchase or sale of that interest.  
• Remove the term ‘significant or prolonged’ |
IASB tentative decision on improvements to disclosures for associates

<table>
<thead>
<tr>
<th>Description</th>
<th>Details</th>
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<tbody>
<tr>
<td>Gains or losses on other changes in the associate’s net assets</td>
<td>Amount of the gain or loss.</td>
</tr>
<tr>
<td>Gains and losses on transactions with associates</td>
<td>Amount of the gain or loss from downward transactions</td>
</tr>
<tr>
<td>Contingent consideration arrangements</td>
<td>Information on the nature of the arrangement, amounts recognised and changes in those amounts, and range of possible outcomes</td>
</tr>
<tr>
<td>Changes in the carrying amount of investments</td>
<td>Reconciliation of the opening to the closing balance of the carrying amount</td>
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Questions for EEG members

• As noted in slide 5, at its October 2023, the IASB will be asked to consider the implications of its tentative decisions for joint ventures and subsidiaries in separate financial statements accounted for under the equity method.

• Do you consider there are implications from the IASB’s tentative decisions for these investments? Which one and why?

• What do you expect to be the cost and benefits of the IASB’s tentative decisions to be in your jurisdiction?
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