Staff paper

Agenda reference: 13B

IASB® meeting

Date	**October 2023**
Project	**Equity Method**
Topic	**Towards an Exposure Draft—Implications of applying the IASB's tentative decisions to investments in joint ventures**
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Introduction

1. IAS 28 *Investments in Associates and Joint Ventures* and IFRS 11 *Joint Arrangements* require application of the equity method when an investor has investments in associates and joint ventures.

2. At its July 2023 meeting, the International Accounting Standards Board (IASB) concluded its discussions on application questions in the scope of the Equity Method project for investments in associates.[1] The IASB's approach was to develop answers to the application questions for investments in associates and, later, consider any implications for other investments accounted for applying the equity method.

3. At its September 2023 meeting, the IASB:
   (a) discussed application of the equity method to investments in joint ventures;
   (b) considered the staff's preliminary analysis on whether the rationale for the IASB's tentative decisions for investments in associates can be applied to investments in joint ventures; and
   (c) asked the staff to prepare a paper for decision-making.[2]

[1] Access the summary of the IASB's tentative decisions.
[2] See September 2023 IASB meeting; Agenda Paper 13B.

Purpose of this paper

4. The purpose of this paper is to ask the IASB to:

   (a) consider the staff analysis that includes feedback from Accounting Standards Advisory Forum (ASAF); and

   (b) decide whether its tentative decisions on application questions for investments in associates apply to investments in joint ventures.

Staff recommendation

5. The staff recommend the IASB applies its tentative decisions on application questions for investments in associates to investments in joint ventures.

Structure of this paper

6. The paper is structured as follows:

   (a) approach to the staff's analysis (paragraphs 7–8 of this paper);

   (b) September 2023 IASB discussion (paragraph 9 of this paper);

   (c) feedback from ASAF (paragraph 10 of this paper);

   (d) staff's analysis (paragraphs 11–21 of this paper); and

   (e) question for the IASB.

Approach to the staff's analysis

7. The staff's approach to assessing whether the IASB's tentative decisions on application questions for investments in associates can be applied to investments in joint ventures (see paragraph 2 of this paper) is to consider any possible unintended consequences (including inconsistencies) with the requirements in IAS 28, IFRS 11, IFRS 10 *Consolidated Financial Statements* and the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*).

8. Given the Equity Method project's objective is to develop answers to application questions, the staff have not reconsidered the IASB's decision when developing IFRS 11 to apply the equity method to investments in joint ventures. Instead, the staff have focused on whether the rationale for the IASB's tentative decisions in answering the application questions for investments in associates holds for investments in joint ventures, including whether there are other factors the IASB should consider.

September 2023 IASB discussion

9. Agenda Paper 13B of the September 2023 IASB meeting discussed:

   (a) the rationale of applying the equity method for investments in joint ventures, including why the IASB decided the equity method was appropriate for joint ventures;

   (b) the requirements in IAS 28 for changes in an investor's ownership interest while continuing to apply the equity method, which are relevant to the IASB's tentative decisions; and

   (c) the staff's preliminary analysis on the following two categories of tentative decisions for possible unintended consequences when applied to investments in joint ventures:

      (i) *changes in ownership interest on purchasing an additional interest*—the IASB has tentatively decided that an investor purchasing an additional interest in an investee would recognise any difference between the cost of the additional interest (being the fair value of the consideration transferred) and its additional share in the net fair value of the investee's identifiable assets and liabilities either as goodwill, or as a gain from a bargain purchase. The cost of investment is an accumulation of purchases.

      (ii) *transactions with equity-accounted investments*—the IASB has tentatively decided that an investor would recognise the full gains or losses on all transactions with its investee.

Feedback from ASAF

10. At its meeting in September 2023, ASAF members were asked for their views on Agenda Paper 13B of the September 2023 IASB meeting. Overall, ASAF members agreed with the IASB technical staff analysis that the rationale for the IASB's tentative decisions for investments in associates can be applied to investments in joint ventures.

Staff's analysis

11. In the following sections of this paper, the staff have drawn on the rationale from Agenda Paper 13B of the September 2023 IASB meeting noted in paragraph 9 of this paper.

Rationale for applying the equity method for investments in joint ventures

12. In developing IFRS 11, the IASB decided that investors should recognise their interests in joint ventures using the equity method as applicable in IAS 28. Although the IASB acknowledged that significant influence and joint control are different, the IASB decided that the equity method is the most appropriate method to account for investments in joint ventures because it is a method that accounts for an investor's interest in the net assets of an investee.[3]

13. At the September 2023 IASB meeting, some IASB members were concerned that introducing two versions of equity method would require reconsidering the IASB's decision when developing IFRS 11.

[3] Paragraph BC41 of the Basis for Conclusions on IFRS 11.

Changes in an investor's ownership interest while continuing to apply the equity method

14. Paragraph 24 of IAS 28 states that (*emphasis* added):

> If an investment in an associate becomes an investment in a joint venture or an investment in a joint venture becomes an investment in an associate, the entity *continues* to apply the *equity method* and *does not remeasure* the retained interest.

15. When developing the requirement set out in paragraph 24 of IAS 28, the IASB acknowledged that in the case of losing joint control and obtaining a significant influence, the nature of the investment changes. However, both investments (the joint venture and the associate) continue to be measured using the equity method. The IASB concluded that losing joint control and obtaining significant influence is not an event that warrants remeasurement of the retained interest at fair value, considering there is no change in:

    (a) the group boundaries; or

    (b) the measurement requirements.[4]

16. At the September 2023 IASB meeting, some IASB members said that if a different equity method is introduced for joint ventures, the IASB would also need to reconsider the accounting for when an investment moves from an associate to a joint venture and vice versa, which could introduce complexities; that is, it would require changing the requirements of paragraph 24 of IAS 28.

[4] Paragraph BC30 of the Basis for Conclusions on IAS 28.

IASB's tentative decision on changes in ownership interest on purchasing an additional interest

17. As noted in paragraph 9(c)(i) of this paper, the IASB's tentative decision is that the cost of the investment is an accumulation of purchases. Table 1 of this paper, sets out the staff analysis of whether the IASB's rationale to answer this application question for investments in associates can be applied to investments in joint ventures.[5] In the staff's view, the analysis in Table 1 of this paper demonstrates that the IASB's rationale for the tentative decision set out in paragraph 9(c)(i) of this paper can be applied to investments in joint ventures.

Table 1: IASB rationale for purchasing an additional interest

IASB's rationale for investments in associates	Whether the same applies to investments in joint ventures
Measuring the investor's additional share of the associate's net identifiable assets and liabilities, while retaining significant influence, at fair value provides the most useful information.	The comparable circumstance would be acquiring additional interest while retaining joint control. Therefore, the same rationale applies because the measurement at fair value provides the most useful information.
The IASB tentative decision is consistent with the requirements in paragraphs 21A and B33C of IFRS 11 for the purchase of additional interests in a joint operation, in which the activity of the joint operation constitutes a business, for example: — apply the principles in IFRS 3 *Business Combinations* that do not conflict with the guidance in IFRS 11, including those on measuring identifiable assets/liabilities at fair value. — previously held interests in the joint operation are not remeasured if the joint operator retains joint control.	The same rationale applies; see above. Also, previously held interests in the joint venture would not be remeasured as the joint venturer: — retains joint control, with no change in the measurement requirements; and — does not obtain control, that is, no change to the group's boundaries as defined in IFRS 10. See paragraphs 14–16 of this paper.

[5] See paragraphs 16–32 of AP13A: Purchase of an additional interest in an associate while retaining significant influence for more details.

IASB's tentative decision on transactions with equity-accounted investments

18. As noted in paragraph 9(c)(ii) of this paper, the IASB has tentatively decided that an investor would recognise the full gains or losses on all transactions with its investee. Table 2 of this paper, sets out the staff analysis of whether the IASB's rationale to answer this application question can be applied to investments in joint ventures.[6]

19. In the staff's view, the analysis in Table 2 of this paper demonstrates that the IASB's rationale for the tentative decision set out in paragraph 9(c)(ii) of this paper can be applied to investments in joint ventures.

Table 2 IASB's rationale for transactions with equity-accounted investments

IASB's rationale for investments in associates	Whether the same applies to investments in joint ventures
Recognising the full gains or losses on all transactions between an investor and its associate:[7] — is consistent with the IASB's most recent thinking about the 'loss of control' reasoned in both IFRS 10 and IFRS 15 *Revenue from Contracts with Customers*. — is consistent with the definition of a 'group' and the *Conceptual Framework*, where the associate is not part of the group. — simplifies the effort needed and costs of applying the equity method procedures. — removes the diversity that has emerged in practice, which would enhance comparability and provide useful and consistent information (with less disruption to reported earnings in future periods) to users of financial statements.	The comparable circumstance would be recognising the full gains or losses on all transactions between a joint venturer and its joint venture. Therefore, the same rationale applies; in particular, because the joint venture is also not controlled by the joint venturer.

[6] See paragraphs 20–94 of AP13B: Perceived conflict between IFRS 10 and IAS 28 for more details.

[7] See also paragraphs 35–43 of AP13B: Perceived conflict between IFRS 10 and IAS 28 for further discussion that restricting gains or losses was not about the application of the equity method; instead, it was about the rationale supporting proportionate consolidation, which the IASB removed when developing IFRS 11.

20. As noted in paragraph 25 of Agenda Paper 13B of the September 2023 IASB meeting, some stakeholders cautioned that joint venturers could potentially manage earnings—for example, the joint venturer could sell assets to its joint venture at a profit and, without the requirement to eliminate the joint venturer's share of that profit (paragraph 28 of IAS 28), the profit or loss could be overstated if the transaction is not on market terms. However, as discussed in paragraphs 26–31 of that paper, in the staff's view:

    (a) the IASB should not introduce requirements solely for anti-abuse reasons;

    (b) the IASB's tentative decision to propose that an investor disclose its gains or losses on transactions to its associates is also relevant for transactions between a joint venturer and its joint venture;[8]

    (c) disclosing that gain or loss, as noted in (b), is consistent with the IASB's previous decision that the equity method is the appropriate method to account for investments in joint ventures; and

    (d) because the IASB has concluded that the equity method is appropriate for both investments in joint ventures and associates, any attempt to create two versions of the equity method would introduce unnecessary complexity into IFRS Accounting Standards.

Conclusion

21. Considering the staff's analysis in paragraphs 11–20 of this paper, the staff think that applying the IASB's tentative decisions on application questions for investments in associates to investments in joint ventures would not lead to unintended consequences (including inconsistencies) with the requirements in IAS 28, IFRS 11, IFRS 10 and the *Conceptual Framework*.

[8] See IASB Update September 2023.

Question for the IASB

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1. Does the IASB agree with the staff recommendation in paragraph 5 of this paper to apply its tentative decisions on application questions for investments in associates to investments in joint ventures?