

STAFF PAPER

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Project	Post-implementation Review of IFRS 10 <i>Consolidated Financial Statements</i>, IFRS 11 <i>Joint Arrangements</i> and IFRS 12 <i>Disclosure of Interests in Other Entities</i>		
Paper topic	Academic literature review update		
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Purpose

1. This paper provides an overview of the academic literature relevant to the Post-implementation Review of IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities*.
2. The Board is not asked any questions, the paper is intended for discussion only.

Structure of this paper

3. The paper is structured as follows:
 - (a) background of the literature review (paragraph 4);
 - (b) academic evidence on IFRS 10—assessment of control (paragraph 5);
 - (c) academic evidence on IFRS 11—joint ventures (paragraphs 6–7);
 - (d) academic evidence on IFRS 12—compliance with IFRS 12 disclosure requirements (paragraph 8);
 - (e) next step (paragraph 9); and
 - (f) Appendix—list of academic papers.

Background of the literature review

4. This literature review is based on:
- (a) an updated summary of the academic literature relevant to IFRS 10, IFRS 11 and IFRS 12 conducted in the first phase of the Post-implementation Review (Agenda Paper 7C, April 2020, Board meeting¹); and
 - (b) two additional papers, referenced in a comment letter by an academic respondents who also participated in the academic outreach workshop with the European Accounting Association.

Academic evidence on IFRS 10

5. Evidence relevant to the Post-implementation Review of IFRS 10 is based on four papers. The main findings are:
- (a) applying the concept of control as defined in IFRS 10 resulted in a change to the number of subsidiaries consolidated. Some entities reported an increase in the number of subsidiaries consolidated while others reported a decrease.²
 - (b) entities reported minor changes in assets, liabilities and profit or loss in the year of implementation of IFRS 10 compared to the previous year.³
 - (c) empirical evidence on the effects of applying IFRS 10 on a sample of 500 Australian entities,⁴ found:
 - (i) entities consolidated less subsidiaries. The authors also documented an increase in entities' disposals of subsidiaries.

¹ Agenda Paper 7C in April 2020 meeting can be accessed [here](#).

² Gluzova (2015), Lopes and Lopes (2019) and Vasek and Gluzova (2014).

³ Lopes and Lopes (2019).

⁴ Bedford, Bugeja, and Nelson (2021).

- (ii) entities that consolidated less subsidiaries subsequently reported higher consolidated profits.
- (iii) entities reported fewer subsidiaries where the parent holds less than the majority of voting rights.
- (iv) the implementation of IFRS 10 was associated with:
 - 1. an increase in the value relevance—association with stock prices and returns—of equity for all entities; and
 - 2. a decrease in the value relevance of earnings for entities consolidating less subsidiaries.
- (v) after implementing IFRS 10:
 - 1. entities audited by the Big Four Firms consolidated less subsidiaries than entities audited by other audit firms. Prior to the implementation of IFRS 10, there was no association between the number of subsidiaries and auditor type.⁵
 - 2. entities where the Chief Executive Officer (CEO) has a higher ownership share were more likely to consolidate subsidiaries where the parent holds less than the majority of the voting rights. Prior to the implementation of IFRS 10, these entities were less likely to consolidate non-majority owned subsidiaries.⁶

⁵ The academic literature shows that entities' consolidation decisions are influenced by their monitoring mechanisms, such as external auditors.

⁶ The academic literature shows that consolidation decisions in entities with high CEO ownership are influenced by management incentives to conceal poor performance to uphold market valuations.

Academic evidence on IFRS 11

6. The literature review for IFRS 11 is based on six academic papers. The findings from these papers are:
- (a) eliminating the accounting policy option for proportionate consolidation:
 - (i) was associated with significant changes in entities' total assets, total liabilities and certain financial ratios, such as return on assets, profit margin and financial leverage;⁷
 - (ii) was associated with a decrease in the value relevance of total assets and liabilities for entities that switched from proportionate consolidation to the equity method; the decrease in the value relevance of total assets and liabilities was not accompanied with an increase in the value relevance of disaggregated information on joint ventures provided in the notes to the financial statements.⁸
 - (b) comparing the value relevance of amounts reported by entities exercising the accounting policy option in favour of either proportionate consolidation or the equity method in IAS 31 *Interests in Joint Ventures*, the information reported applying proportionate consolidation was less value relevant than information reported using the equity method.⁹
 - (c) analysts' information environment was not affected by entities exercising the accounting policy option in favour of either proportionate consolidation or the equity method, regardless of whether entities provided information in the notes. The information environment was measured by forecast bias, accuracy and dispersion of earnings forecasts, target prices and stock recommendations.¹⁰
 - (d) based on a sample of 2,059 entities from 26 jurisdictions which reported applying IFRS Standards from 2005 to 2016, overall comparability

⁷ Lopes and Lopes (2019) and Sarquis and Santos (2018).

⁸ Gavana, Gottardo, Moisello (2020). The paper uses a sample of 120 Italian and French listed entities which reported using IFRS Standards in the period 2008–2015.

⁹ So, Wong, Shun, Zhang and Xu (2018).

¹⁰ Inchausti, Sanchez and Fuentes (2017).

decreased after IFRS 11 was implemented.¹¹ The authors, Sarquis et al (2019), measured comparability as the association between accounting amounts (total assets, liabilities, revenues and expenses) and economic outputs (price, return, cash flow). To assess changes in comparability, the authors identified two groups of entities:

- (i) entities that were required to change from proportionate consolidation to the equity method; and
- (ii) entities that used the equity method both before and after the implementation of IFRS 11.

7. Sarquis et al (2020) analysed comparability further within seven clusters of jurisdictions, grouped on the basis of cultural and institutional factors, such as religion, level of economic development, culture, legal and political system. They compared clusters where the proportionate consolidation option was prevalent before the implementation of IFRS 11 to control clusters where the equity method option was prevalent before the implementation of IFRS 11. Overall, comparability decreased and results were mixed at the cluster level. The researchers’ findings are summarised in the following table.

Cluster	Control cluster	Comparability relative to control cluster
cluster one (South Africa and Philippines)	cluster six (Hong Kong)	Increased
cluster two (Belgium, Germany, Spain, France, Italy, and Poland)	cluster three (Australia, Canada, Ireland, New Zealand, UK)	Increased
cluster two (Belgium, Germany, Spain, France, Italy, and Poland)	cluster six (Hong Kong)	Increased
cluster seven (Kuwait, Malaysia, Sri Lanka and Turkey)	cluster three (Australia, Canada, Ireland, New Zealand, UK)	Increased
cluster four (Brazil, Chile and Mexico)	cluster three (Australia, Canada, Ireland, New Zealand, UK)	Decreased
cluster four (Brazil, Chile and Mexico)	cluster six (Hong Kong)	Decreased

¹¹ Sarquis, Santos, Lourenco and Braunbeck (2020).

Cluster	Control cluster	Comparability relative to control cluster
cluster five (Denmark, Finland, Netherlands, Norway and Sweden)	cluster three (Australia, Canada, Ireland, New Zealand, UK)	Decreased
cluster seven (Kuwait, Malaysia, Sri Lanka and Turkey)	cluster six (Hong Kong)	Decreased
cluster one (South Africa and Philippines)	cluster three (Australia, Canada, Ireland, New Zealand, UK)	Inconclusive ¹²
cluster five (Denmark, Finland, Netherlands, Norway and Sweden)	cluster six (Hong Kong)	Inconclusive

Academic evidence on IFRS 12

8. The evidence from academic research related to IFRS 12 is based on two academic papers. The findings from these papers are:
- (a) based on a sample of 23 entities from the Czech Republic that reported in 2014 applying IFRS Standards, the level of compliance with the disclosure requirements in IFRS 12 was relatively low.¹³
 - (b) based on a sample of 1,858 financial statements reported in the period 2013–2016 by 551 entities from 26 jurisdictions that switched from proportionate consolidation to the equity method:¹⁴
 - (i) the mean (median) level of compliance, measured by the ratio of the number of items disclosed to the maximum number of items required to be disclosed by IFRS 12 about

¹² The results were sensitive to the comparability metric used.

¹³ Ašenbrenerová (2016).

¹⁴ Sarquis, Santos, Lourenco and Braunbeck (2021).

the joint venture’s summarised financial information, was 64.6% (100%).¹⁵

- (ii) the level of compliance varied by country—descriptive statistics by country are presented in the following table.¹⁶

Country	Mean compliance (%)	Median compliance (%)
Australia	50.0	40.0
Belgium	69.0	100.0
Brazil	68.1	100.0
Canada	62.7	100.0
Chile	61.5	100.0
Denmark	64.1	100.0
Finland	59.5	100.0
France	50.2	40.0
Germany	68.7	100.0
Hong Kong	82.1	100.0
Ireland	51.4	60.0
Italy	68.0	100.0
Kuwait¹⁷	20.0	0.0
Malaysia	87.7	100.0
Mexico	60.3	80.0
Netherlands	47.6	40.0
New Zealand	88.9	100.0
Norway	73.7	100.0
Philippines	77.9	100.0
Poland	53.2	90.0
South Africa	78.3	100.0
Spain	58.0	100.0
Sri Lanka	74.0	100.0
Sweden	38.8	40.0
Turkey	65.4	100.0
United Kingdom	75.0	100.0

¹⁵ In 970 of 1858 financial statements, entities disclosed all financial information about investments in joint ventures (max disclosure score 100%) and in 464 of 1858 financial statements entities did not disclose any financial information about investments in joint ventures (minimum disclosure score 0%).

¹⁷ The statistics for Kuwait are based on four yearly observations of one entity—a median of 0.0% likely indicates that in three of its four financial statements, the entity did not disclose any financial information about investments in joint ventures.

- (iii) the level of compliance remained relatively constant in the four years after the implementation of IFRS 12.
- (iv) compliance with the disclosure requirements in IFRS 12 was influenced by entity-level characteristics more than country-level characteristics.
- (v) larger entities, entities with a larger ratio of the entity's share of the joint venture's total assets to the entity's total assets and entities that are not cross listed¹⁸ showed higher levels of compliance.
- (vi) entities with lower leverage, lower ownership concentration and more profitable entities showed higher level of compliance.¹⁹
- (vii) entities from common-law countries and from emerging economies showed a higher level of compliance.

Next step

9. The staff will take into consideration these academic literature evidence in recommending the next step of the Post-implementation Review to the Board. Paragraphs 20 and 21 in Agenda Paper 7 of this meeting provide details of the next step.

¹⁸ Entities are listed in more than one stock exchanges.

¹⁹ This finding was based on weak evidence—it did not hold across all test specifications.

Appendix—list of academic papers

1. Ašenbrenerová, Petra (2016), 'Disclosure of joint ventures and associates in financial statements under IFRS', *European Financial and Accounting Journal*, 11 (3), 85–94.
2. Bedford, Anna, Bugeja, Martin, and Nelson, Ma (2021), 'The Impact of IFRS 10 on Consolidated Financial Reporting', *Accounting & Finance, Forthcoming*
3. Gavana, Giovanna, Gottardo, Pietro, and Moisello, Anna Maria (2020), 'Did the switch to IFRS 11 for joint ventures affect the value relevance of corporate consolidated financial statements? Evidence from France and Italy', *Journal of International Accounting, Auditing and Taxation*, 38, 1–15 .
4. Gluzová, Tereza (2015), 'The adoption of IFRS 10 and its impact on the scope of consolidation', *Acta Academica Karviniensia*, 4, 18–27.
5. Inchausti, Begoña Giner, Sanchez, Raul Iñiguez, and Fuentes, Francisco Poveda (2017), 'Does the interaction between the accounting method choice and disclosure affect financial analysts' information environment? The case of joint ventures under IAS 31', *Spanish Journal of Finance & Accounting / Revista Espanola de Financiacion y Contabilidad*, 46 (3), 298–326.
6. Lopes, Ana Isabel and Lopes, Mariana (2019), 'Effects of adopting IFRS 10 and IFRS 11 on consolidated financial statements: An exploratory research', *Meditari Accountancy Research*, 27 (1), 91–124.
7. Sarquis, Raquel Wille and Santos, Ariovaldo dos (2018), 'Impacts of the elimination of the proportionate consolidation on Itaúsa financial statements', *Revista Contabilidade & Finanças*, 29 (77), 213–28.
8. Sarquis, Raquel Wille, Santos, Ariovaldo dos, Lourenco, Isabel and Braunbeck, Guillermo Oscar (2020), 'Elimination of Accounting Choices and the Comparability of Financial Statements: The Adoption of IFRS 11—Joint Arrangements', working paper.
9. Sarquis, Raquel Wille, Santos, Ariovaldo dos, Lourenco, Isabel and Braunbeck, Guillermo Oscar (2021), 'Joint Venture Investments: An Analysis of the Level of Compliance with the Disclosure Requirements of IFRS 12.' *Journal of International Financial Management and Accounting, Forthcoming*.

10. So, Stella, Wong, Kar Shun, Zhang, Feida and Zhang, Xu (2018), 'Value relevance of proportionate consolidation versus the equity method: Evidence from Hong Kong', *China Journal of Accounting Research*, 11 (4), 255–78.
11. Vasek, Libor and Gluzová, Tereza (2014), 'Can a new concept of control under IFRS have an impact on CCCTB', *European Financial and Accounting Journal*, 9 (4), 110–27.