STAFF PAPER

September 2022

IASB® meeting

Project	**Equity Method**
Paper topic	Cover paper

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Introduction

1. The International Accounting Standards Board (IASB) has been discussing, as part of its equity method research project, the application question: *How does an investor apply the equity method when purchasing an additional interest in an associate while retaining significant influence.*

2. The IASB has selected a preferred approach to the application question and has asked the staff to develop further analysis applying its preferred approach. The IASB is also considering the implications for an alternative approach:

Approach	Description
Preferred approach	After obtaining significant influence, an investor measures its additional interests in an associate as an accumulation of purchases. An investor recognises, at the date of purchasing an additional interest, its additional share in the fair value of the associate's net assets and measures that additional interest at the fair value of the consideration transferred.
Alternative approach	After obtaining significant influence, an investor measures its investment in the associate as a single asset. An investor measures its aggregated share of the associate's net assets at fair value and remeasures the cost of the investment at fair value at the date of acquiring an additional interest in an associate while retaining significant influence.

Structure of this paper

3. This paper sets out:

   (a) project background;

   (b) purpose of this meeting;

   (c) next steps;

   (d) Appendix A—principles identified as underlying IAS 28;

   (e) Appendix B—summary of the IASB's tentative decisions, including application questions discussed; and

   (f) Appendix C—application questions within the scope of the project yet to be discussed.

Project background

4. At its October 2020 meeting, the IASB decided on the objective and approach of the Equity Method project and moved the project from the research pipeline to its research programme. The IASB decided that the objective of the Equity Method project is:

   > To assess whether application questions with the equity method, as set out in IAS 28 *Investments in Associates and Joint Ventures*, can be addressed in consolidated and individual financial statements by identifying and explaining principles in IAS 28.[1]

5. The IASB decided that to achieve the objective, it would apply the following approach:

   (a) identify application questions and decide which of these questions to address.

   (b) address the application questions by identifying and explaining the principles in IAS 28. This would allow the IASB to develop new requirements (or application guidance), which will amend the Standard.

6. Some application questions cannot be addressed by the principles identified in IAS 28. The IASB decided it will develop the principles needed to address these

[1] See AP13 of the October 2020 IASB Meeting and the IASB Update October 2020.

application questions by analogising to the principles identified and apply the judgment required when developing an accounting policy applying IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*—that is considering the applicability of the requirements in IFRS Accounting Standards dealing with similar and related issues and the definitions, recognition criteria and measurement concepts in the *Conceptual Framework*.[2]

7. At its October 2021 meeting, the IASB received an update on the application questions within the scope of the project; these application questions are set out in Appendix B and C to this paper.

Purpose of this meeting

8. The purpose of this meeting is to:

   (a) continue discussions from the June 2022 meeting on the disposal of an interest in an associate while retaining significant influence—Agenda Paper 13A explores alternatives for measuring the portion of the carrying amount of an investment in an associate to be derecognised when an investor applies the preferred approach to a partial disposal while retaining significant influence;

   (b) continue discussion on other changes in an associate's net assets—Agenda Paper 13B discusses how an investor could apply the preferred approach to changes in the associate's net assets that change an investor's ownership interest while retaining significant influence; and

   (c) introduce the application question on transactions between an investor and its associate—Agenda Paper 13C discusses how should an investor account for gains and losses that arise from the sale of a subsidiary to its associate, applying the requirements of IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures*.

9. Agenda papers for discussion at this meeting include:

   (a) Agenda Paper 13A *Partial disposals—how to measure the portion to be derecognised*;

[2] See AP13 of the June 2021 IASB Meeting and the IASB Update June 2021.

(b) Agenda Paper 13B *Changes in an associate's net assets that change the investor's ownership interest*; and

(c) Agenda Paper 13C *Transactions between an investor and its associate—an acknowledged inconsistency between the requirements of IFRS 10* Consolidated Financial Statements *and IAS 28* Investments in Associates and Joint Ventures.

Next steps

10. At the October 2022 IASB meeting, the staff plan to ask if the IASB agree to continue with the equity method research project, based on the project's progress to date.

11. If the IASB agree to continue with the equity method research project, the staff plan to:

    (a) continue discussing application question on the inconsistency between the requirements in IFRS 10 and those in IAS 28, and to refine its analysis and develop recommendations for decision-making at a future meeting;

    (b) ask the IASB to decide on the preferred or the alternative approach to applying the equity method for changes in an investor's ownership interest in an associate while retaining significant influence;

    (c) present the staff analysis on other application questions within the scope of the project (see appendix C to this paper); and

    (d) ask the IASB whether to extend the scope of the project to other application questions that the IASB received.

Appendix A—Principles identified as underlying IAS 28

	Principles Identified	Paragraph
Classification		
A	Power to participate is an investor's shared power to affect changes in, and to access net assets.	IAS 28.3 *Definition* IAS 28.5-9 IAS 28.12–14
Boundary of the reporting entity		
B	Application of the equity method includes an investor's share in the associate's or joint venture's net asset changes in an investor's statement of financial position.	IAS 28.3 *Definition* IAS 28.10-11 IAS 28.35
C	An investor's share of an associate's or joint venture's net assets is part of the reporting entity.	IAS 28.28
Measurement on initial recognition		
D	Fair value at the date that significant influence or joint control is obtained provides the most relevant information and faithful representation of an associate's or joint venture's identifiable net assets.	IAS 28.30–31B IAS 28.32 IFRS 3 BC25/198
Subsequent measurement		
E	An investor recognises changes in an associate's or joint venture's net assets. An investor recognises the share of changes in net assets that it can currently access.	IAS 28.3 *Definition* IAS 28.10–13 IAS 28.26 IAS 28.28 IAS 28.30–31B IAS 28.33–36 (includes 35) IAS 28.37
F	An investor's maximum exposure is the gross interest in an associate or joint venture.	IAS 28.14A/29/38–43
G	When an investor has a decrease in its ownership interest in an associate or joint venture and continues to apply the equity method, it reclassifies amounts previously recognised in other comprehensive income.	IAS 28.24–25
Derecognition		
H	An investor: (a) applies IFRS 3 and IFRS 10 if it obtains control of an associate or joint venture; (b) applies IFRS 9 if it no longer has significant influence or joint control but retains an interest in a former associate or joint venture; and (c) recognises a gain or loss and reclassifies amounts recognised in other comprehensive income on the date that significant influence or joint control is lost.	IAS 28.22–23 IFRS 3.41–42

Principles Identified	Paragraph
Unallocated (not being addressed in the project)	
Presentation	IAS 28.15/20–21
Exceptions to the application of the equity method	IAS 28.16–19 IAS 28.27 IAS 28.36A

Appendix B—Summary of the IASB tentative decisions, including application questions discussed

Table B1—Summary of IASB's tentative decision

IASB Meeting	Topic	Staff condensed summary of the IASB's tentative decisions
October 2020	Objective and approach	1. The IASB decided on the objective and approach of the Equity Method project and moved the project from the research pipeline to its research programme.
March 2021	Scope—application questions	2. The IASB discussed the process for selecting application questions to be addressed by the project.
June 2021	Approach—principles underlying IAS 28	3. The IASB discussed: (a) the principles identified as underlying IAS 28; and (b) how to develop additional principles to guide how an entity applies the equity method in situations to which none of these underlying principles apply.
October 2021	Scope—application questions	4. The IASB received an update on application questions within the scope of the project—identified applying the process that the IASB discussed at its March 2021 meeting. 5. The IASB tentatively decided the staff should undertake research before considering the application questions within the scope of the project.
April 2022	Approach—identify principles in IFRS Accounting Standards	6. The IASB reviewed the research findings on changes made to IFRS Accounting Standards arising from the *Conceptual Framework*, Business Combinations and Joint Arrangements projects.

Table B2—Summary of IASB's tentative decisions on application questions

Application question(s)	IASB Meeting	IASB's tentative decisions
Changes in an investor's interest while retaining significant influence		
How does an investor apply the equity method when purchasing an additional interest in an associate while retaining significant influence?	April 2022	1. The IASB tentatively decided to consult with stakeholders on measuring the cost of an investment, when an investor obtains significant influence, as the fair value of the consideration transferred, including the fair value of any previously held interest in the investee. 2. The IASB considered three approaches to applying the equity method when an investor purchases an additional interest in an associate while retaining significant influence. The IASB instructed the staff to continue exploring: (a) a preferred approach whereby an investor, after obtaining significant influence, would measure the investment in the associate as an accumulation of purchases. (b) an alternative approach whereby an investor would measure the investment as a single asset at its fair value at the date of the purchase of an additional interest.
	June 2022	3. The IASB tentatively decided that an investor applying the preferred approach to a bargain purchase of an additional interest, while retaining significant influence, would recognise a bargain purchase gain in profit or loss.
How does an investor apply the equity method when disposing of an interest in an associate while retaining significant influence?	June 2022	4. The IASB tentatively decided that an investor applying the preferred approach to a partial disposal, while retaining significant influence, would measure the portion of the carrying amount of an investment in an associate to be derecognised using:

Application question(s)	IASB Meeting	IASB's tentative decisions
		(a) a specific identification method, if the investor can identify the specific portion of the investment being disposed of and its cost; and (b) the last-in, first-out method, if the specific portion of the investment being disposed of cannot be identified. 5. The IASB decided to explore practical methods of measuring the portion of the carrying amount of an investment in an associate to be derecognised when an investor applies the preferred approach to a partial disposal while retaining significant influence.

Appendix C —Application questions within the scope of the project yet to be discussed

Application question(s)
Changes in an investor's interest while retaining significant influence
Whether an investor recognises its share of other changes in an associate's net assets, and if so, how is the change presented?
Recognition of losses
Whether an investor that has reduced its interest in an investee to nil is required to 'catch up' unrecognised losses if it purchases an additional interest in the investee?
Whether an investor that has reduced its interest in an investee to nil continues eliminating its share of gains arising from a downstream transaction?
Whether an investor that has reduced its interest in an investee to nil recognises each component of comprehensive income separately? For example, in a financial year, an investee recognises a loss in comprehensive income that includes, a profit in its statement of profit and loss, and a loss in its statement of other comprehensive income.
Transactions between investor and associate
Whether to recognise the portion of the investor's share of gain that exceeds the carrying amount of its investment in the investee in a downstream transaction?
Whether the investor's share of gain or loss is eliminated from the carrying amount of the investment in the investee or the acquired asset in an upstream transaction?
Whether the provision of service and transactions that are not transfer of assets are upstream or downstream transaction?

Application question(s)
How should an investor account for gains and losses that arise from the sale of a subsidiary to an investee given the requirements of IFRS 10 and IAS 28? In a transaction where an investor sells a subsidiary to its investee: (a) paragraph 25 of IFRS 10 requires the investor to recognise in full the gain or loss from the sale of a subsidiary, remeasuring any retained interest, if any, at fair value; whereas (b) paragraph 28 of IAS 28 requires an investor to restrict the gain or loss recognised to the extent of the unrelated investors' interests in its associate.
Transactions between two associates
Whether the requirement for adjustment of gains and losses in intra-group transactions between subsidiaries should be applied by analogy to transactions between investees that are accounted for applying the equity method?
Impairment
Whether the decline in fair value is assessed in relation to the original purchase price or the carrying amount at the reporting date?
Initial recognition
Whether the investor recognises deferred tax assets and liabilities on the differences between the fair value and the tax base of its share of the investee's net assets?
Contingent consideration
How to initially and subsequently account for contingent consideration in the acquisition of an investee applying IAS 28?