International Financial Reporting Standard

Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

September 2014

BASES FOR CONCLUSIONS – AMENDMENTS

[IFRS 10 and IAS 28]

[Related to AASB 2014-10]

Amendments to the Basis for Conclusions on IFRS 10 *Consolidated Financial Statements*

Paragraphs BC190A–BC190K and their related heading are added. New text is underlined.

Sale or contribution of assets between an investor and its associate or joint venture—amendments to IFRS 10 and IAS 28

BC190A The IFRS Interpretations 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*[2] and IAS 28 (as amended in 2011) apply when a business is contributed to a jointly controlled entity (as defined in IAS 31[3]), a joint venture (as defined in IFRS 11) or an associate, in exchange for an equity interest in that jointly controlled entity, joint venture or associate. The business may be contributed either when the jointly controlled entity, joint venture or associate is established or thereafter.

BC190B The Board noted that this matter is related to the issues arising from the acknowledged inconsistency between the requirements in IAS 27 (as revised in 2008) and SIC-13, when accounting for the contribution of a subsidiary to a jointly controlled entity, joint venture or associate (resulting in the loss of control of the subsidiary). In accordance with SIC-13, the amount of the gain or loss recognised resulting from the contribution of a non-monetary asset to a jointly controlled entity in exchange for an equity interest in that jointly controlled entity is restricted to the extent of the interests attributable to the unrelated investors in the jointly controlled entity. However, IAS 27 (as revised in 2008) requires full profit or loss recognition on the loss of control of a subsidiary.

BC190C This inconsistency between IAS 27 (as revised in 2008) and SIC-13 remained after IFRS 10 replaced IAS 27 (as revised in 2008) and SIC-13 was withdrawn. The requirements in IFRS 10 on the accounting for the loss of control of a subsidiary are similar to the requirements in IAS 27 (as revised in 2008). The requirements in SIC-13 are incorporated into paragraphs 28 and 30 of IAS 28 (as amended in 2011) and apply to the sale or contribution of assets between an investor and its associate or joint venture. Because IAS 27 (as revised in 2008) and SIC-13 have been superseded at the time when the amendments become effective, the Board decided to amend only IFRS 10 and IAS 28 (as amended in 2011).

BC190D In dealing with the conflict between the requirements in IFRS 10 and IAS 28 (as amended in 2011), the Board was concerned that the existing requirements could result in the accounting for a transaction being driven by its form rather

2 SIC-13 has been withdrawn. The requirements in SIC-13 are incorporated into IAS 28 (as amended in 2011).

3 IAS 31 was superseded by IFRS 11 *Joint Arrangements* issued in May 2011.

than by its substance. For example, different accounting might be applied to a transaction involving the same underlying assets depending on whether those assets were:

(a) transferred in a transaction that is structured as a sale of assets or as a sale of the entity that holds the assets; or

(b) sold in exchange for cash or contributed in exchange for an equity interest.

BC190E The Board concluded that:

(a) the accounting for the loss of control of a business, as defined in IFRS 3, should be consistent with the conclusions in IFRS 3; and

(b) a full gain or loss should therefore be recognised on the loss of control of a business, regardless of whether that business is housed in a subsidiary or not.

BC190F Because assets that do not constitute a business were not part of the Business Combinations project, the Board concluded that:

(a) the current requirements in IAS 28 (as amended in 2011) for the partial gain or loss recognition for transactions between an investor and its associate or joint venture should only apply to the gain or loss resulting from the sale or contribution of assets that do not constitute a business; and

(b) IFRS 10 should be amended so that a partial gain or loss is recognised in accounting for the loss of control of a subsidiary that does not constitute a business as a result of a transaction between an investor and its associate or joint venture.

BC190G The Board discussed whether all sales and contributions (including the sale or contribution of assets that do not constitute a business) should be consistent with IFRS 3. Although it considered this alternative to be the most robust from a conceptual point of view, it noted that this would require addressing multiple cross-cutting issues. Because of concerns that the cross-cutting issues could not be addressed on a timely basis, the conclusions described in paragraphs BC190E–BC190F were considered the best way to address this issue.

BC190H The Board decided that both 'upstream' and 'downstream' transactions should be affected by the amendments to IFRS 10 and IAS 28 (as amended in 2011). The Board noted that if assets that constitute a business were sold by an associate or a joint venture to the investor (in an upstream transaction), with the result that the investor takes control of that business, the investor would account for this transaction as a business combination in accordance with IFRS 3.

BC190I In response to concerns expressed by some interested parties, the Board clarified that paragraph B99A of IFRS 10 applies to all transactions between an investor and its associate or joint venture (that is accounted for using the equity method) that result in the loss of control of a subsidiary that does not constitute a business. Consequently, paragraph B99A of IFRS 10 does not apply:

(a) to transactions with third parties, even if the parent retains an investment in the former subsidiary that becomes an associate or a joint venture accounted for using the equity method; or

(b) when the investor elects to measure its investments in associates or joint ventures at fair value in accordance with IFRS 9.

BC190J During the finalisation of the amendments, the Board also clarified that the gain or loss resulting from a transaction within the scope of paragraph B99A of IFRS 10 includes:

(a) the amounts previously recognised in other comprehensive income that would be reclassified to profit or loss in accordance with paragraph B99 of IFRS 10. This is because those amounts are part of the gain or loss recognised on the disposal of the subsidiary.

(b) the part of the gain or loss resulting from the remeasurement of the investment retained in a former subsidiary. The Board noted that if the former subsidiary is now an associate or a joint venture that is accounted for using the equity method, the parent will recognise this part of the gain or loss in its profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture. This is because the Board had previously decided that when a subsidiary is not a business the requirements of IAS 28 for the partial gain or loss recognition should be applied. If the parent retains an investment in the former subsidiary that is now accounted for in accordance with IFRS 9, the part of the gain or loss resulting from the remeasurement at fair value of the investment retained in the former subsidiary is recognised in full in the parent's profit or loss. This is because, in this case, the requirements of IFRS 9, rather than the requirements of IAS 28, apply for the partial gain or loss recognition.

BC190K The Board decided that the amendments to IFRS 10 and IAS 28 (as amended in 2011) should apply prospectively to transactions that occur in annual periods beginning on or after the date that the amendments become effective. The Board observed that the requirements in IAS 27 (as revised in 2008) for the loss of control of a subsidiary were applied prospectively (see paragraph 45(c) of IAS 27 as revised in 2008). The Board also noted that transactions dealing with the loss of control of a subsidiary or a business between an investor and its associate or joint venture are discrete non-recurring transactions. Consequently, the Board concluded that the benefits of comparative information would not exceed the cost of providing it. The Board also decided to allow entities to early apply the amendments to IFRS 10 and IAS 28 (as amended in 2011).

Amendments to the Basis for Conclusions on IAS 28 *Investments in Associates and Joint Ventures*

Paragraphs BC37A–BC37I and their related heading are added. New text is underlined.

Sale or contribution of assets between an investor and its associate or joint venture—amendments to IFRS 10 and IAS 28

BC37A The IFRS Interpretations 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[4] and IAS 28 (as revised in 2011) apply when a business is contributed to a jointly controlled entity (as defined in IAS 31[5]), a joint venture (as defined in IFRS 11) or an associate, in exchange for an equity interest in that jointly controlled entity, joint venture or associate. The business may be contributed either when the jointly controlled entity, joint venture or associate is established or thereafter.

BC37B The Board noted that this matter is related to the issues arising from the acknowledged inconsistency between the requirements in IAS 27 (as revised in 2008) and SIC-13, when accounting for the contribution of a subsidiary to a jointly controlled entity, joint venture or associate (resulting in the loss of control of the subsidiary). In accordance with SIC-13, the amount of the gain or loss recognised resulting from the contribution of a non-monetary asset to a jointly controlled entity in exchange for an equity interest in that jointly controlled entity is restricted to the extent of the interests attributable to the unrelated investors in the jointly controlled entity. However, IAS 27 (as revised in 2008) requires full profit or loss recognition on the loss of control of a subsidiary.

BC37C This inconsistency between IAS 27 (as revised in 2008) and SIC-13 remained after IFRS 10 replaced IAS 27 (as revised in 2008) and SIC-13 was withdrawn. The requirements in IFRS 10 on the accounting for the loss of control of a subsidiary are similar to the requirements in IAS 27 (as revised in 2008). The requirements in SIC-13 are incorporated into paragraphs 28 and 30 of IAS 28 (as amended in 2011) and apply to the sale or contribution of assets between an investor and its associate or joint venture. Because IAS 27 (as revised in 2008) and SIC-13 have been superseded at the time when the amendments become effective, the Board decided to amend only IFRS 10 and IAS 28 (as amended in 2011).

BC37D In dealing with the conflict between the requirements in IFRS 10 and IAS 28 (as amended in 2011), the Board was concerned that the existing requirements could result in the accounting for a transaction being driven by its form rather than by its substance. For example, different accounting might be applied to a transaction involving the same underlying assets depending on whether those assets were:

4 SIC-13 has been withdrawn. The requirements in SIC-13 are incorporated into IAS 28 (as amended in 2011).

5 IAS 31 was superseded by IFRS 11 *Joint Arrangements* issued in May 2011.

(a) transferred in a transaction that is structured as a sale of assets or as a sale of the entity that holds the assets; or

(b) sold in exchange for cash or contributed in exchange for an equity interest.

BC37E The Board concluded that:

(a) the accounting for the loss of control of a business, as defined in IFRS 3, should be consistent with the conclusions in IFRS 3; and

(b) a full gain or loss should therefore be recognised on the loss of control of a business, regardless of whether that business is housed in a subsidiary or not.

BC37F Because assets that do not constitute a business were not part of the Business Combinations project, the Board concluded that:

(a) the current requirements in IAS 28 (as amended in 2011) for the partial gain or loss recognition for transactions between an investor and its associate or joint venture should only apply to the gain or loss resulting from the sale or contribution of assets that do not constitute a business; and

(b) IFRS 10 should be amended so that a partial gain or loss is recognised in accounting for the loss of control of a subsidiary that does not constitute a business as a result of a transaction between an investor and its associate or joint venture.

BC37G The Board discussed whether all sales and contributions (including the sale or contribution of assets that do not constitute a business) should be consistent with IFRS 3. Although it considered this alternative to be the most robust from a conceptual point of view, it noted that this would require addressing multiple cross-cutting issues. Because of concerns that the cross-cutting issues could not be addressed on a timely basis the conclusions described in paragraphs BC37E–BC37F were considered the best way to address this issue.

BC37H The Board decided that both 'upstream' and 'downstream' transactions should be affected by the amendments to IFRS 10 and IAS 28 (as amended in 2011). The Board noted that if assets that constitute a business were sold by an associate or a joint venture to the investor (in an upstream transaction), with the result that the investor takes control of that business, the investor would account for this transaction as a business combination in accordance with IFRS 3.

BC37I The Board decided that the amendments to IFRS 10 and IAS 28 (as amended in 2011) should apply prospectively to transactions that occur in annual periods beginning on or after the date that the amendments become effective. The Board observed that the requirements in IAS 27 (as revised in 2008) for the loss of control of a subsidiary (see paragraph 45(c) of IAS 27 as revised in 2008) were applied prospectively. The Board also noted that transactions dealing with the loss of control of a subsidiary or a business between an investor and its associate or joint venture are discrete non-recurring transactions. Consequently, the Board concluded that the benefits of comparative information would not exceed the cost of providing it. The Board also decided to allow entities to early apply the amendments to IFRS 10 and IAS 28 (as amended in 2011).

Dissenting Opinions

Dissenting Opinions from *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28) as issued in September 2014

DO1 Mr Kabureck, Ms Lloyd and Mr Ochi voted against the publication of *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28). The reasons for their dissents are set out below.

Dissent of Mr Kabureck

DO2 Mr Kabureck dissents from the amendments to IFRS 10 and IAS 28, which require full gain or loss recognition in the accounting for the loss of control when a parent (investor) sells or contributes a business, as defined in IFRS 3 *Business Combinations*, to an investee (ie an associate or a joint venture) that is accounted for using the equity method.

DO3 He agrees that the control of a business can be lost regardless of whether the acquirer is a related or an unrelated party. However, he believes that the accounting for the gain or loss should be different if the sale or contribution is to an investee that is accounted for using the equity method. He observes that the investor's interest in the gain or loss will eventually affect the future investee's profit or loss recognised in the investor's profit or loss.

DO4 His concern can be illustrated by a simple example:

An investor sells a business to a 40 per cent-owned associate accounted for using the equity method. The full gain is CU100.[6] This gain of CU100 is reflected in the associate's financial statements through the higher value of the net assets acquired. Over time, assuming that no goodwill or indefinite lived intangible assets are involved, the associate's future profits or losses will be lower by CU100 as the assets are consumed and, therefore, the investor's share of the associate's profits or losses will be lower by CU40. Consequently, the net gain of the investor over time is CU60, not CU100.

DO5 Accordingly, he believes that a more faithful representation of the transaction would be to recognise an immediate gain of CU60 and a deferred gain of CU40, which would be amortised into income, making it consistent with the consumption of the sold assets in the investee's operations. He believes that it would be inappropriate to immediately recognise the full gain knowing that over time there would be lower profits to the extent of the equity interest in the investee.

DO6 Mr Kabureck observes that his preferred partial gain or loss accounting is consistent with the accounting for the sales of assets that do not constitute a business, as described in paragraphs BC190F of IFRS 10 and BC37F of IAS 28. Whether or not the assets sold or contributed do, or do not, constitute a business, seems to him to provide little rationale for different gain or loss

6 In this document, monetary items are denominated by 'currency units' (CU).

treatment. He further observes that the line between what constitutes a business versus a collection of assets is frequently unclear, often based on judgement and represents an interpretation challenge in practice. He disagrees with introducing another accounting difference that is dependent on the interpretation of the definition of a business.

Dissent of Ms Lloyd and Mr Ochi

DO7 Ms Lloyd and Mr Ochi agree that the sale of assets that constitute a business and the sale of assets that do not constitute a business should be treated differently for the reasons given in paragraphs BC190G of IFRS 10 and BC37G of IAS 28. However, they also believe that the accounting result should not differ depending on whether assets that do not constitute a business are transferred in a transaction that is structured as a sale of assets or as a sale of the entity that holds those assets. Ms Lloyd and Mr Ochi believe that these amendments do not achieve that result.

DO8 The stated objective of these amendments is to address the conflict between the requirements of IFRS 10 and IAS 28. Prior to these amendments, IFRS 10 required full gain or loss recognition on the loss of control of a subsidiary, whereas IAS 28 restricted the gain or loss resulting from the sale or contribution of assets to an associate or a joint venture to the extent of the interests that were attributable to unrelated investors in that associate or joint venture (downstream transactions).

DO9 As a result of these amendments, there will continue to be a full gain or loss recognition on the loss of control of a subsidiary that constitutes a business under IFRS 10, as well as a full gain or loss recognition resulting from the sale or contribution of assets that constitute a business between an investor and its associate or joint venture under IAS 28. The gain or loss recognised on the sale of the business will be the same whether it is structured as a sale of assets that constitute a business or as a sale of the entity that contains a business. As stated above, Ms Lloyd and Mr Ochi agree with this result.

DO10 Even after the amendments, IAS 28 will continue to restrict the gain or loss resulting from the sale or contribution of assets that do not constitute a business to an associate or a joint venture to the extent of the interests that are attributable to unrelated investors in that associate or joint venture. However, as a result of these amendments, under IFRS 10, when an entity sells an interest in a subsidiary that does not contain a business to an associate or a joint venture and as a result loses control of that subsidiary but retains joint control or significant influence over it, the gain or loss recognised is also limited to the unrelated investor’s interests in the associate or joint venture to which the interest in the subsidiary was sold. In addition, the entity will remeasure its retained interest in the former subsidiary to fair value at the date it loses control, even though that retained interest is not in an entity that constitutes a business. Ms Lloyd and Mr Ochi acknowledge that under the amendments, recognition of the gain or loss on remeasurement will be limited to the unrelated investor’s interests in the associate or joint venture to which the interest in the subsidiary was sold. However, because Ms Lloyd and Mr Ochi believe the sale of a subsidiary that does not constitute a business, and the sale of the assets held in that subsidiary, is substantially the same transaction, they do not find any justification for the recognition of any additional gain on the remeasurement of the retained portion.

DO11 Furthermore, Ms Lloyd and Mr Ochi note that if the retained interest in the former subsidiary is an investment accounted for in accordance with IFRS 9 *Financial Instruments* or IAS 39 *Financial Instruments: Recognition and Measurement*, the amount of gain or loss recognised on remeasurement will not be restricted. A full gain or loss will be recognised on remeasurement of the retained interest even though that interest is not in an entity that constitutes a business. As a result of the remeasurement of the retained interest in the former subsidiary, the amount of gain or loss recognised in a transaction involving the same underlying assets will still be different depending on whether those assets are transferred in a transaction that is structured as a sale of assets or as a sale of the entity that holds the assets. Ms Lloyd and Mr Ochi disagree with this result. They believe that the remeasurement of a retained interest in a former subsidiary to fair value when control is lost is a fundamental principle of IFRS 10. They also believe that accounting for equity interests that do not represent control, joint control or significant influence at fair value is a fundamental principle of IFRS 9 and IAS 39. Ms Lloyd and Mr Ochi do not believe that these principles can be reconciled in a limited-scope amendment to the treatment in IAS 28 of downstream transactions that involve the sale of assets that do not constitute a business.

DO12 Consequently, Ms Lloyd and Mr Ochi dissent from these amendments because they do not fully address the concerns of the Board and the IFRS Interpretations Committee as set out in paragraphs BC190D of IFRS 10 and BC37D of IAS 28.