AASB Exposure Draft **ED 246**

December 2013

Equity Method in Separate Financial Statements

(proposed amendments to AASB 127)

Comments to the AASB by 24 January 2014

Australian Government

Australian Accounting Standards Board

Commenting on this AASB Exposure Draft

Constituents are strongly encouraged to respond to the AASB and the IASB. The AASB is seeking comment by 24 January 2014. This will enable AASB members to consider Australian constituents' comments in the process of formulating AASB comments to the IASB, which are due by 3 February 2014. Comments should be addressed to:

The Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West Victoria 8007
AUSTRALIA
E-mail: standard@aasb.gov.au

Respondents to the IASB are asked to send their comments electronically to the IFRS Foundation website (www.ifrs.org), using the 'Comment on a proposal' page.

All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chairman of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

Obtaining a Copy of this AASB Exposure Draft

This AASB Exposure Draft is available on the AASB website: www.aasb.gov.au. Alternatively, printed copies of this AASB Exposure Draft are available by contacting:

The Customer Service Officer
Australian Accounting Standards Board
Level 7
600 Bourke Street
Melbourne Victoria
AUSTRALIA

Phone: (03) 9617 7637
Fax: (03) 9617 7608
E-mail: publications@aasb.gov.au
Postal address:
PO Box 204
Collins Street West Victoria 8007

Other Enquiries

Phone: (03) 9617 7600
Fax: (03) 9617 7608
E-mail: standard@aasb.gov.au

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AASB REQUEST FOR COMMENTS

IAS 27 *Separate Financial Statements* (which is incorporated into AASB 127 *Separate Financial Statements*) allows an entity to account for investments in subsidiaries, joint ventures and associates either at cost or in accordance with IFRS 9 *Financial Instruments* (which is incorporated into AASB 9 *Financial Instruments*) in the entity's separate financial statements. The main proposal in this Exposure Draft is to reintroduce an option to use the equity method to account for such investments in an entity's separate financial statements. This option was previously permitted under International Financial Reporting Standards (IFRSs) in respect of investments in subsidiaries and associates, but was removed from IFRSs before Australia adopted IFRSs.

In light of the Australian Accounting Standards Board's (AASB's) policy of incorporating IFRSs into Australian Accounting Standards, the AASB is inviting comments on:

(a) any of the proposals in the attached International Accounting Standards Board (IASB) Exposure Draft, including the specific questions on the proposals as listed in the Invitation to Comment section of the attached IASB Exposure Draft; and

(b) the 'AASB Specific Matters for Comment' listed below.

Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents supplement their opinions with detailed comments, whether supportive or critical, on the major issues. The AASB regards both critical and supportive comments as essential to a balanced review and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

Due Date for Comments to the AASB

Comments should be submitted to the AASB by 24 January 2014. This will enable AASB members to consider those comments in the process of formulating AASB comments to the IASB. Constituents are also strongly encouraged to send their response to the IASB.

Reduced Disclosure Requirements

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 2 comprises the recognition, measurement and presentation requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.

The proposals in this Exposure Draft would not make amendments to any disclosure requirements. Accordingly, this Exposure Draft does not give rise to any particular implications for Tier 2 disclosures.

AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

   (a) not-for-profit entities; and

   (b) public sector entities, including GAAP/GFS implications;

2. whether, overall, the proposals would result in financial statements that would be useful to users;

3. whether the proposals are in the best interests of the Australian economy; and

4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

December 2013

Exposure Draft ED/2013/10

Equity Method in Separate Financial Statements

Proposed amendments to IAS 27

Comments to be received by 3 February 2014

IASB®

IFRS®

Equity Method in Separate Financial Statements

(Proposed amendments to IAS 27)

Comments to be received by 3 February 2014

Exposure Draft ED/2013/10 *Equity Method in Separate Financial Statements* (Proposed amendments to IAS 27) is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received before being issued in final form. Comments need to be received by **3 February 2014** and should be submitted in writing to the address below or electronically via our website www.ifrs.org using the 'Comment on a proposal' page.

All responses will be put on the public record and posted on our website unless the respondent requests confidentiality. Requests for confidentiality will not normally be granted unless supported by good reason, such as commercial confidence.

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IFRS Foundation Publications Department
30 Cannon Street, London EC4M 6XH, United Kingdom
Tel: +44 (0)20 7332 2730 Fax: +44 (0)20 7332 2749
Email: publications@ifrs.org Web: www.ifrs.org

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Introduction

Prior to the revision in 2003 of IAS 27 *Consolidated and Separate Financial Statements* and IAS 28 *Investments in Associates*, the equity method was one of the options available to an entity to account for investments in subsidiaries and associates in the entity's separate financial statements. In 2003, the equity method was removed from the options.

IAS 27 *Separate Financial Statements* allows an entity to account for investments in subsidiaries, joint ventures and associates either at cost or in accordance with IFRS 9 *Financial Instruments* in the entity's separate financial statements.

The International Accounting Standards Board (IASB) has published this Exposure Draft of proposed amendments to IAS 27 to restore the option to use the equity method to account for investments in subsidiaries, joint ventures and associates in the entity's separate financial statements.

Invitation to comment

The IASB invites comments on the proposals in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

(a) comment on the questions as stated;

(b) indicate the specific paragraph(s) to which they relate;

(c) contain a clear rationale; and

(d) describe any alternative that the IASB should consider, if applicable.

Questions for respondents

Question 1—Use of the equity method

The IASB proposes to permit the equity method as one of the options to account for an entity's investments in subsidiaries, joint ventures and associates in the entity's separate financial statements.

Do you agree with the inclusion of the equity method as one of the options? If not, why?

Question 2—Transition provisions

The IASB proposes that an entity electing to change to the equity method would be required to apply that change retrospectively, and therefore would be required to apply IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Do you agree with the proposed transition provisions? If not, why and what alternative do you propose?

Question 3—First-time adopters

The IASB does not propose to provide any special relief for first-time adopters. A first-time adopter electing to use the equity method would be required to apply the method from the date of transition to IFRSs in accordance with the general requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards*.

Do you agree that a special relief is not required for a first-time adopter? If not, why and what alternative do you propose?

Question 4—Consequential amendment to IAS 28 *Investments in Associates and Joint Ventures*

The IASB proposes to amend paragraph 25 of IAS 28 in order to avoid a conflict with the principles of IFRS 10 *Consolidated Financial Statements* in situations in which an entity loses control of a subsidiary but retains an ownership interest in the former subsidiary that gives the entity significant influence or joint control, and the entity elects to use the equity method to account for the investments in its separate financial statements.

Do you agree with the proposed consequential amendment? If not, why?

Question 5—Other comments
Do you have any other comments on the proposals?

[Draft] Amendments to IAS 27 *Separate Financial Statements*

In the Introduction, paragraph IN1 is amended. New text is underlined and deleted text is struck through.

Introduction

IN1 IAS 27 *Separate Financial Statements* contains accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements. The Standard requires an entity preparing separate financial statements to account for those investments either at cost, ~~or~~ in accordance with IFRS 9 *Financial Instruments*, or using the equity method.

Paragraphs 4–7, 10 and 12 are amended and paragraph 18J is added. New text is underlined and deleted text is struck through.

Definitions

4 The following terms are used in this Standard with the meanings specified:

...

Separate financial statements are those presented by a parent (ie an investor with control of a subsidiary) or an investor with joint control of, or significant influence over, an investee, in which the investments are accounted for either at cost, ~~or~~ in accordance with IFRS 9 *Financial Instruments*, or using the equity method as described in IAS 28 *Investments in Associates and Joint Ventures*.

5 The following terms are defined in Appendix A of IFRS 10 *Consolidated Financial Statements*, Appendix A of IFRS 11 *Joint Arrangements* and paragraph 3 of IAS 28 ~~*Investments in Associates and Joint Ventures*~~:

- associate
- equity method
- ...

6 Separate financial statements are those presented in addition to consolidated financial statements or in addition to the financial statements of an entity that does not have investments in subsidiaries, ie investor in an associate or joint venture ~~in which investments in associates or joint ventures are accounted for using the equity method~~, other than in the circumstances set out in paragraphs 8–8A. Separate financial statements need not be appended to, or accompany, those statements.

7 ~~Financial statements in which the equity method is applied are not separate financial statements. Similarly, the~~ The financial statements of an entity that

does not have a subsidiary, associate or joint venturer's interest in a joint venture are not separate financial statements.

...

Preparation of separate financial statements

...

10 When an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either:

(a) at cost;~~, or~~

(b) in accordance with IFRS 9~~.~~; or

(c) using the equity method as described in IAS 28.

The entity shall apply the same accounting for each category of investments. Investments accounted for at cost or using the equity method shall be accounted for in accordance with IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* when they are classified as held for sale or for distribution (or included in a disposal group that is classified as held for sale or for distribution). The measurement of investments accounted for in accordance with IFRS 9 is not changed in such circumstances.

...

12 ~~An entity shall recognise a dividend~~ Dividend from a subsidiary, a joint venture or an associate is recognised ~~in profit or loss~~ in ~~its~~ the separate financial statements of an entity when ~~it's~~ the entity's right to receive the dividend is established. The dividend is recognised:

(a) in profit or loss if the entity elects to measure the investment at cost or in accordance with IFRS 9; or

(b) as a reduction from the carrying amount of the investment if the entity elects to use the equity method.

...

Effective date and transition

...

18J *Equity Method in Separate Financial Statements* (Amendments to IAS 27), issued in [date], amended paragraphs 4–7, 10 and 12. An entity shall apply those paragraphs for annual periods beginning on or after [date] retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Earlier application is permitted.

[Draft] Consequential amendments to other IFRSs

IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Paragraph 39W is added.

Effective date

...

39W *Equity Method in Separate Financial Statements* (Amendments to IAS 27), issued in [date], amended paragraph D14. An entity shall apply that amendment for annual periods beginning on or after [date] retrospectively in accordance with IAS 8. Earlier application is permitted.

In Appendix D, paragraph D14 is amended. New text is underlined and deleted text is struck through.

Investments in subsidiaries, joint ventures and associates

D14 When an entity prepares separate financial statements, IAS 27 requires it to account for its investments in subsidiaries, joint ventures and associates either:

(a) at cost; ~~or~~

(b) in accordance with IFRS 9~~.~~; or

(c) using the equity method as described in IAS 28.

IAS 28 *Investments in Associates and Joint Ventures*

Paragraph 25 is amended. New text is underlined and deleted text is struck through.

Changes in ownership interest

25 If an entity's ownership interest in an associate or a joint venture is reduced, but the investment continues to be classified either as an associate or a joint venture ~~entity continues to apply the equity method~~, the entity shall reclassify to profit or loss the proportion of the gain or loss that had previously been recognised in other comprehensive income relating to that reduction in ownership interest if that gain or loss would be required to be reclassified to profit or loss on the disposal of the related assets or liabilities.

Approval by the Board of *Equity Method in Separate Financial Statements* (Proposed amendments to IAS 27) published in December 2013

The Exposure Draft *Equity Method in Separate Financial Statements* was approved for publication by the sixteen members of the International Accounting Standards Board.

Hans Hoogervorst	Chairman
Ian Mackintosh	Vice-Chairman
Stephen Cooper	
Philippe Danjou	
Martin Edelmann	
Jan Engström	
Patrick Finnegan	
Amaro Luiz de Oliveira Gomes	
Gary Kabureck	
Prabhakar Kalavacherla	
Patricia McConnell	
Takatsugu Ochi	
Darrel Scott	
Chungwoo Suh	
Mary Tokar	
Wei-Guo Zhang	

Basis for Conclusions on the Exposure Draft *Equity Method in Separate Financial Statements* (Proposed amendments to IAS 27)

This Basis for Conclusions accompanies, but is not part of, the proposed amendments.

Introduction

BC1 This Basis for Conclusions summarises the considerations of the IASB when developing the amendments proposed in the Exposure Draft *Equity Method in Separate Financial Statements* (Proposed amendments to IAS 27).

Background

BC2 Prior to the revision in 2003 of IAS 27 *Consolidated and Separate Financial Statements* and IAS 28 *Investments in Associates*, the equity method was one of the options available to an entity for measuring investments in subsidiaries and associates in the entity's separate financial statements. IAS 31 *Interests in Joint Ventures*, however, was silent on the methods to account for interests in jointly controlled entities in the venturer's separate financial statements.

BC3 In 2003, the equity method was removed from the options and the IASB decided to require the use of cost or IAS 39 *Financial Instruments: Recognition and Measurement* for all investments in subsidiaries, jointly controlled entities and associates included in the separate financial statements. The IASB noted that the information provided by the equity method is reflected in the investor's economic entity financial statements and that there was no need to provide the same information in the separate financial statements.

BC4 In their responses to the IASB's 2011 Agenda Consultation, some respondents said that:

(a) the laws of some countries require listed companies to present separate financial statements prepared in accordance with local regulations;

(b) those local regulations require the use of the equity method to account for investments in subsidiaries, joint ventures and associates; and

(c) in most cases, the use of the equity method would be the only difference between the separate financial statements prepared in accordance with IFRSs and those prepared in accordance with local regulations.

BC5 Those respondents strongly supported the inclusion of the equity method as one of the options for measuring investments in subsidiaries, joint ventures and associates in the separate financial statements of an entity.

BC6 In May 2012, the IASB decided to consider restoring the option to use the equity method of accounting in separate financial statements. The IASB decided that this work could proceed without a Discussion Paper and other optional due process steps, such as establishing a consultative group, holding public hearings and undertaking field work, as this is a narrow-scope project to restore an option and the feedback from constituents on the IASB's 2011 Agenda Consultation was sufficient.

Preparation of separate financial statements

BC7 IAS 27 does not mandate which entities produce separate financial statements. Entities may either elect or be required by local regulation to present separate financial statements that comply with IFRSs.

Equity method

BC8 Application of the equity method provides informative reporting of the investor's net assets and profit or loss. According to paragraph QC6 of the *Conceptual Framework for Financial Reporting* information may be relevant even if some users are already aware of it from other sources. Consequently, the fact that the equity method provides information that is already reflected in consolidated financial statements does not mean that it would not provide relevant information.

Application of the equity method

BC9 IAS 28 *Investments in Associates and Joint Ventures* contains guidance on the application of the equity method. Many of the procedures that are appropriate for the application of the equity method are similar to the consolidation procedures described in IFRS 10 *Consolidated Financial Statements* (see paragraph 26 of IAS 28).

BC10 Generally, the investor's net assets and profit or loss attributable to the equity holders of the investor would be the same in its consolidated financial statements and its separate financial statements wherein all investments in subsidiaries, joint ventures and associates are accounted for using the equity method as described in IAS 28. However, there could be situations in which applying the equity method to investments in subsidiaries in separate financial statements would give a different result compared to the consolidated financial statements. One such situation is the recognition of impairment losses on an investment in a subsidiary accounted for using the equity method in separate financial statements in which goodwill that forms part of the carrying amount of the investment in the subsidiary is not tested for impairment separately. Instead, the entire carrying amount of the investment in the subsidiary is tested for impairment in accordance with IAS 36 *Impairment of Assets* as a single asset. However, in the consolidated financial statements of the entity, since goodwill is recognised separately, it is tested for impairment by applying the requirements in IAS 36 for testing goodwill for impairment. The IASB concluded that creating any additional guidance within IAS 28 to eliminate such differences would not be appropriate.

Consequential amendment to IAS 28

BC11 An entity may lose control of a subsidiary but retain an ownership interest that gives the entity significant influence or joint control. In a situation in which the entity elects, under the proposals in this Exposure Draft, to use the equity method to account for the investments in its separate financial statements, by applying paragraph 25 of IAS 28 the entity would reclassify to profit or loss, when required, the proportion relating to that reduction in ownership interest of the gain or loss that had previously been recognised in other comprehensive income, and continue to account for the retained investment using the existing carrying value. This is not in accordance with the principles of IFRS 10 that require an entity to recognise any investment retained in a former subsidiary at its fair value when control is lost. Consequently, the IASB has proposed an amendment to paragraph 25 of IAS 28 to avoid any conflicting accounting in such situations.

Transition requirements

For entities already applying IFRSs

BC12 The IASB noted that an entity should be able to use the information that is used for consolidation of the subsidiary in its consolidated financial statements for applying the equity method to the investment in the subsidiary in its separate financial statements. Investments in associates and joint ventures (after applying the transition provisions of IFRS 11 when needed) are accounted for using the equity method in the consolidated financial statements, which means that an entity need not perform any additional procedures and can use the same information in its separate financial statements.

BC13 Hence, the IASB decided that an entity that elects to use the equity method should be required to apply the proposed amendment to IAS 27 retrospectively in accordance with IAS 8.

For first-time adopters of IFRSs

BC14 The IASB thinks that the same considerations that had been discussed for initial application for entities already applying IFRSs also apply to first-time adopters. Consequently, the IASB decided that a first-time adopter that elects to use the equity method should apply the proposed amendment to IAS 27 from the date of transition to IFRSs in accordance with IFRS 1.

