ASAF Meeting AP3A

Preliminary Input to IFRS 10-12 Post-implementation Review

Accounting Standards Board of Japan

December 2019

About this presentation

- **This presentation is based on the presentation that was discussed at the Asian-Oceanian Standard-Setters Group (AOSSG) meeting held in November 2019, reflecting the feedback received at that meeting**

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asian-oceanian standard-setters group

THE ELEVENTH ANNUAL AOSSG MEETING

Joining hands in regional cooperation and the development of IFRS

12-13 November, 2019, India

What is a PIR?

- **According to the Due Process Handbook, the IASB is required to conduct a Post-implementation Review (PIR) of each new Standard**
  - **The PIR is a mandatory step in the due process for new IFRS Standards or major amendments to IFRS Standards**
- **A PIR is structured in two phases:**

Phase 1: **Initial identification and assessment of the matters to be examined, which will be subject to a public consultation in the form of a Request for Information (RFI)**

- **This involves gathering input from the broad network of IFRS-related bodies and interested bodies, including national standard setters**

Phase 2: **The IASB considers the comments that it receives from the RFI**

- **The IASB may or may not make changes to the Standards that is subject to review**

PIR of IFRS 10-12

- The IASB activated the PIR of IFRS 10-12 after its September 2019 Board meeting
- The IFRS Standards within the scope are
  - IFRS 10 Consolidated Financial Statements
  - IFRS 11 Joint Arrangements
  - IFRS 12 Disclosure of Interests in Other Entities
- The IASB staff will seek input on the scope of the PIR at the following consultative group meetings:

Group	Date
Global Preparers Forum (GPF) Capital Markets Advisory Committee (CMAC)	October 2019
IFRS Interpretations Committee (IFRS-IC)	November 2019
Emerging Economies Group (EEG) Accounting Standards Advisory Forum (ASAF)	December 2019

Background and Objective of this Meeting

- The ASBJ, as the Working Group (WG) Leader of the Business Groups and Assets WG of the AOSSG, received a request from IASB staff to gather the views within the AO region regarding the potential issues to be included in the forthcoming RFI
- In preparation for this meeting, we have asked members of the Business Groups and Assets WG to provide us with their preliminary views on the overall assessment of IFRS 10-12
- The objective of this meeting is to discuss whether AOSSG members have any additional issues that should be considered by the IASB to be included in the RFI
- We plan to present the outcome of this meeting at the forthcoming ASAF meeting in December 2019
- This is not your last opportunity to participate in the process – AOSSG members have the opportunity to respond to the RFI once it is issued for public comment by the IASB

IFRS 10 Summary of views

- **Many WG members noted that, overall, IFRS 10 provided useful information to users**
- **However, several WG members asked for clarification of the following concepts:**
  - **"fundamental changes" in the context of protective rights (para. B26) [slide 18]**
  - **"not clear" when the investor has power (para. B46) [slide 20]**
  - **"market conditions" in the context of the investor's assessment of control or its status as principal or agent (para. B85) [slide 14]**
  - **"impracticable" in the context of having the same reporting date (para. B92) [slide 23]**
  - **"significant transactions or events" in the context of making adjustments when the reporting date is different (para. B93) [slide 23]**

IFRS 10 Summary of views (continued)

- Some WG members noted that, while IFRS 10 included explanations and examples, the general principles in making decisions related to the following concepts were not clear:
  - relevant activities [slides 15-16]
  - potential voting rights [slide 21]
- Some WG members were concerned that IFRS 10 was relying on form over substance (the so-called "corporate wrapper" issue) [slide 24]
- Some WG members noted that it was difficult to make the assessment in a timely manner because the factors to consider were out of the control of the entity [slide 21]
  - Therefore, it was difficult to conduct "continuous assessment"
- Some WG members noted that remeasuring the retained interests (and recognising any gains or losses) when control was lost did not provide useful information because, for the retained interests, nothing has changed [slide 26]

IFRS 10

Summary of views (continued)

- **Some WG members noted that IFRS standards did not cover all patterns of changes in interests**

To: / From:		Financial asset	Equity-accounted investee (significant influence/ joint venture)	Joint operations: Joint operator	Joint operations: Party to a joint operation	Control
Financial Asset		IFRS 9	Unclear	Unclear	Unclear	Remeasure
Equity-accounted investee (significant influence/joint venture)		Remeasure	Do not remeasure	Unclear	Unclear	Remeasure
Joint operations	Joint operator	Remeasure	Unclear	Do not remeasure	Unclear	Remeasure
	Party to a joint operation	Remeasure	Unclear	Do not remeasure	Unclear	Remeasure
Control		Remeasure	Remeasure	Unclear	Unclear	Do not remeasure

Source: AP12B for October 2015 IASB meeting, updated by the ASBJ

IFRS 11 Summary of views

- Many WG members noted that, overall, IFRS 11 provided useful information to users
- Several WG members raised issues related to the equity method:
  - in general
    - clarifying the underlying concept (ie one-line consolidation vs. measurement method) [slide 33]
  - in connection with the IASB's Primary Financial Statements project
    - distinguishing between "integral" and "non-integral" equity method investments [slide 34]
- Many of the comments on IFRS 11 were consistent with the comments on IFRS 10

Summary of views

- **Many WG members noted that, overall, IFRS 12 provided useful information to users**
- **However, several WG members noted that it was difficult to determine what information should be provided**
  - **The concept of "material to the reporting entity" was unclear (paras. 12, 21(a), and 21(b)) [slide 39]**
- **Several WG members noted that, for some of the disclosure requirements, the benefits did not justify the costs of providing the information**
  - **Significant judgements and assumptions (paras. 7-9) [slide 38]**
  - **Individually immaterial joint ventures and associates (para. 21(c)) [slide 40]**

Appendix
Details of Views from WG Members

IFRS 10 Overview

Description	Paras.	Slides
Objective	1-3	
Scope	4-4B	
Control	5-18	
Overall	5-9; B2-B8; B73-B85	13-14
Power	10-14; B9-B54	15-21
Returns	15-16; B55-B57	
Link between power and returns	17-18; B58-B72	22
Accounting requirements	19-26	
Overall	19-21; B86-B93	23
Non-controlling interests	22-24; B94-B96	24
Loss of control	25-26; B97-B99A	25-26
Determining whether an entity is an investment entity	27-30; B85A-B85W	
Investment entities: exception to consolidation	31-33; B100-B101	
(Other)		27

IFRS 10

Related parties

When assessing control, an investor shall consider the nature of its relationship with other parties and whether those other parties are acting on the investor's behalf (ie they are 'de facto agents') (para. B73). One example of such other parties that, by the nature of their relationship, might as de facto agents for the investor is the investor's related parties (para. B75(a)).

- **It is unclear whether the related parties referred to in para. B75(a) are those who meet the definition of a "related party" as defined in IAS 24 Related Party Disclosures**

Market conditions

An investor's initial assessment of control or its status as a principal or an agent would not change simply because of a change in market conditions, unless the change in market conditions changes one or more of the three elements of control or changes the overall relationship between a principal and an agent (para. B85).

- **The term "market conditions" is not defined**

IFRS 10

Two or more investors with the current ability to direct

If two or more investors each have existing rights that give them the unilateral ability to direct different relevant activities, the investor that has the current ability to direct the activities that most significantly affect the returns of the investee has power over the investee (para. 13). When two or more investors have the current ability to direct relevant activities and those activities occur at different times, the investors are required to determine which investor is able to direct the activities that most significantly affect those returns consistently with the treatment of concurrent decision making rights (para. B13).

- **The above guidance is insufficient. The IASB should provide more guidance on how to determine the relevant activity that most significantly affects the returns**
- **It is difficult to assess the involvement of investors when the investee operates on "auto-pilot"**

Two or more investors with the current ability to direct (continued)

- **It is difficult to determine who has control or joint control between investors who enter into a cooperation arrangement**
  - **Power can shift from one entity to another based on the changes in the relevant activities**
    - **For example, in the film industry, one investor directs the relevant activities during the production stage and the other directs the relevant activities during the distribution stage, based on their expertise**

IFS 10

Not having the contractual right to appoint key management personnel

In assessing control, the investor considers whether it can, without having the contractual right to do so, appoint or approve the investee's key management personnel who have the ability to direct the relevant activities (para. B18(a)).

- **It is unclear how an investor can appoint or approve the investee's key management personnel without having the contractual right to do so because in this commentator's jurisdiction, the investor usually has the contractual right to do so**

IFRS 10 Protective rights

In evaluating whether rights give an investor power over an investee, the investor is required to assess whether its rights, and rights held by others, are protective rights. Protective rights relate to fundamental changes to the activities of an investee or apply in exceptional circumstances (para. B26).

- **It is unclear what is meant by "fundamental changes"**
- **Some investors have the right to dissolve or liquidate the investee. It is not clear whether such right qualifies as a protective right**

Less than majority of voting rights

An investor can have power even if it holds less than a majority of the voting rights of an investee (para. B38).

- **It is difficult to determine whether the investor has power over an investee when it holds less than a majority of the voting rights**

IFRS 10 Not clear

If it is not clear, having considered the factors listed in paragraph B42(a)-(d) that the investor has power, the investor does not control the investee (para. B46).

- **It is difficult to determine whether it was "not clear" or not**

IFRS 10

Assessing voting rights, including potential voting rights

In assessing whether an investor's voting rights are sufficient to give it power, an investor is required to consider voting patterns at previous shareholders' meetings (para. B42(d)). In addition, an investor is required to consider the potential voting rights held by other parties (para. B47).

- **These assessments require judgement and it is questionable whether entities can arrive at the same conclusion under identical fact patterns**
- **It is difficult to make the assessment in a timely manner because the factors to consider are out of the control of the entity**
  - **It is difficult to conduct "continuous assessment"**
- **The usefulness of the resulting information is questionable when the situation at the time of the assessment is only temporary**
- **Although IFRS 10 includes an explanation and examples of "potential voting rights", the general principles in making decisions related to those potential voting rights are not clear**

IFRS 10 Principal vs. agent

A decision maker is required to consider the overall relationship between itself, the investee being managed and other parties involved with the investee, in determining whether it is an agent, including the decision maker's exposure to variability of returns from other interests that it holds in the investee (paras. B60(d), B71-B72).

- **It is difficult to determine whether the decision maker is a principal or an agent, for general managers in the fund industry**

IFRS 10 Reporting date

The financial statements of the parent and its subsidiaries used in the preparation of consolidated financial statements shall have the same reporting date. When the end of the reporting period of the parent is different from that of a subsidiary, the subsidiary prepares, for consolidation purposes, additional information as of the same date as the financial statements of the parent to enable the parent to consolidate the financial information of the subsidiary, unless it is impracticable to do so (para. B92). If it is impracticable to do so, the parent shall consolidate the financial information of the subsidiary using the most recent financial statements of the subsidiary adjusted for the effects of significant transactions or events that occur between the date of those financial statements and the date of the consolidated financial statements (para. B93).

- It is difficult to determine whether it is "impracticable" or not
  - It is unclear whether the definition of "impracticable" in IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors applies
- It is difficult to determine the scope of "significant transactions or events" and how to account for them

IFRS 10

Changes in proportion held by NCIs

When the proportion of the equity held by non-controlling interests changes, an entity is required to adjust the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary. The entity is required to recognise directly in equity any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received, and attribute it to the owners or the parent (para. B96).

- **This requirement gives rise to the so-called "corporate wrapper" issue, which leads to different outcomes even though the economic substance are the same**
  - **For example, in the case of real estate:**
    - **If an entity securitises real estate through another entity and initially holds 100% of the interest but subsequently sells 10% of the interest in the entity, no gains or losses would be recognised**
    - **If the entity directly sells 10% of the real estate, a gain or loss would be recognised**

Multiple arrangements as a single transaction

One or more of the following indicate that the parent should account for the multiple arrangements as a single transaction:

(a) They are entered into at the same time or in contemplation of each other.

(b) They form a single transaction designed to achieve an overall commercial effect.

(c) The occurrence of one arrangement is dependent on the occurrence of at least one other arrangement.

(d) One arrangement considered on its own is not economically justified, but it is economically justified when considered together with other arrangements. An example is when a disposal of shares is priced below market and is compensated for by subsequent disposal priced above market.

(para. B97)

- It is unclear how to account for multiple arrangements as a single transaction, when some of those multiple arrangements are completed by the end of reporting period but not all

IFRS 10 Loss of control

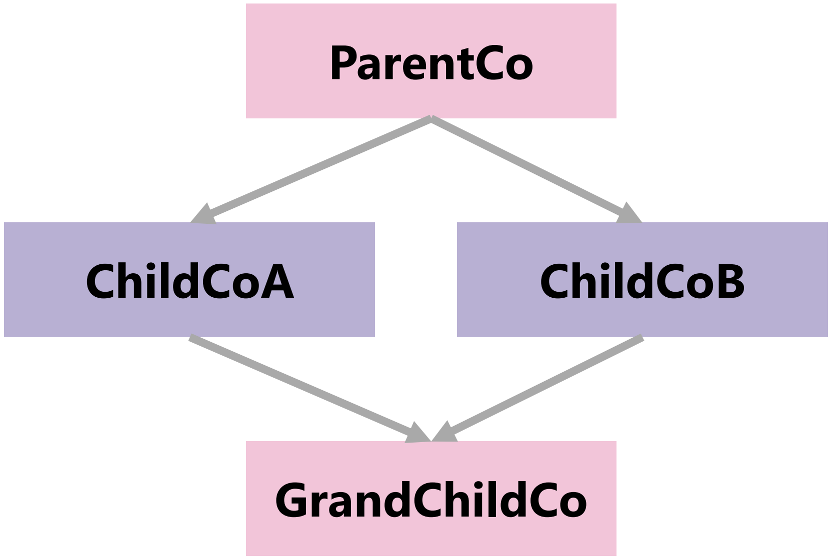
If a parent loses control of a subsidiary, the parent is required to recognise any investment retained in the former subsidiary at its fair value at the date when control is lost (para. B98(b)(iii)). In addition, the parent is required to recognise any resulting difference between the items recognised and derecognised as a gain or loss in profit or loss attributable to the parent (para. B98(d)).

- **Remeasuring the retained interests (and recognising any gains or losses) when control was lost did not provide useful information because, for the retained interests, nothing has changed**
  - **The relevance of the information in terms of profit or loss is questionable since the transactions do not involve actual exchange transactions**
- **While the Annual Improvements to IFRS Standards 2015-2017 Cycle issued in December 2017 addressed some patterns of changes in interests, IFRS standards do not cover all patterns**

IFRS 10

Consolidation by entities under common control

- **When two subsidiaries (ChildCoA and ChildCoB) under the common control of a parent (ParentCo) invest in another entity (GrandChildCo), determining whether ChildCoA or ChildCoB should consolidate GrandChildCo may lead to preparing the consolidated financial statements of ChildCoA and the consolidated financial statements of ChildCoB with limited usefulness, because ParentCo has control over ChildCoA and ChildCoB and can arbitrarily design who should consolidate the entity**



IFRS 11 Overview

Description	Paras.	Slides
Objective	1-2	
Scope	3	29
Joint arrangements	4-19	
Overall	4-6; B2-B4	
Joint control	7-13; B5-B11	30
Types of joint arrangement	14-19; B12-B33	
Financial statements of parties to a joint arrangement	20-25	
Joint operations	20-23; B33A-B37	31-32
Joint ventures	24-25	33-34
Separate financial statements	26-27	
(Other)		35

Scope

IFRS 11 is required to be applied by all entities that are a party to a joint arrangement (para. 3). A joint arrangement is an arrangement of which two or more parties have joint control (para. 4).

- **It is difficult to determine whether certain arrangements are joint arrangements. Examples include the following:**
  - **Joint research and development (R&D) projects**
  - **Joint marketing projects**

IFRS 11

Relevant activities

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control (para. 7).

- **While it is fairly straightforward to determine whether a single entity has control over another entity, it is difficult to determine whether two or more parties have joint control because it is difficult to identify how the parties are involved with the relevant activities**
- **While conceptually all parties to the joint arrangement should reach the same conclusion as to whether joint control exists, that is not guaranteed**
- **Power can shift between entities based on the changes in the relevant activities**

IFRS 11 Joint operations

A joint operator is required to recognise, in relation to its interest in a joint operation:
(a) its assets, including its share of any assets held jointly;
(b) its liabilities, including its share of any liabilities incurred jointly;
(c) its revenue from the sale of its share of the output arising from the joint operation;
(d) its share of the revenue from the sale of output by the joint operation; and
(e) its expenses, including its share of any expenses incurred jointly.
(para. 20).

- **This requirement gives rise to the so-called "corporate wrapper" issue, which leads to different outcomes even though the economic substance are the same:**
  - **If an entity becomes a party to the joint operation with rights to 10% of the assets and liabilities of the joint operation, it would recognise 10% of the assets and liabilities of the joint operation**
  - **If an entity invested 10% in an entity that holds the same assets and liabilities, that investment would be treated as a financial instrument and would be subject to IFRS 9**

Joint operations (continued)

- **There is diversity in practice related to how revenue and costs are recognised by the joint operators**
- **The guidance in IFRS 11 is limited and, therefore, it is unclear as to how to account for:**
  - **assets that are held jointly by the joint operators**
  - **liabilities that are jointly liable by the joint operators**
  - **liabilities that were incurred by one joint operator on behalf of the joint operation**
    - **It is unclear whether to apply IFRS 16 *Leases* in particular as to subleases between the lead operator and the joint operation**

Equity method

A joint venture is required to recognise its interest in a joint venture as an investment and to account for that investment using the equity method in accordance with IAS 28 *Investments in Associates and Joint Ventures* unless the entity is exempted from applying the equity method as specified in that standard (para. 24).

- **Comments on the equity method in general:**
  - **It is difficult to understand the requirements related to the equity method because they are scattered throughout IAS 28, IFRS 3 and IFRS 9**
  - **The IASB needs to clarify the concepts underlying the equity method of accounting**
    - **One-line consolidation vs. measurement method**

IFRS 11

Equity method (continued)

- **Comments on the equity method in connection with the IASB's Primary Financial Statements project:**
  - **The IASB has tentatively decided that income and expense from equity method investments should be classified into those arising from "integral" equity method investments and "non-integral" equity method investments**
    - **It is unclear whether this tentative decision would change the scope of investments that are currently accounted for using the equity method**
    - **It is difficult to envision any equity method investment being "non-integral" to the entity**
  - **For those entities with many equity method investments, the effective tax rate is understated because the income from equity method investments is presented as a post-tax figure before the income tax line**

IFRS 11 Changes in interests

- **IFRS standards do not cover all patterns of changes in interests**
  - **Missing patterns include the following:**
    - **Change from a joint operator to an equity method investment (and the opposite)**
    - **Change from a joint operator to a party to a joint operation**
    - **Changes in interests of a party to a joint operation**

IFRS 12 Overview

Description	Paras.	Slides
Objective	1-4; B2-B6	37
Scope	5-6	
Significant judgements and assumptions	7-9B	38
Interests in subsidiaries	10-19; B10-B11	39
Interests in unconsolidated subsidiaries (investment entities)	19A-19G	
Interests in joint arrangements and associates	20-23; B12-B20	40
Interests in unconsolidated structured entities	24-31; B21-26	41
(Other)		

IFRS 12 Objective

The objective of IFRS 12 is to require an entity to disclose information that enables users of its financial statements to evaluate:

(a) the nature of, and risks associated with, its interests in other entities; and

(b) the effects of those interests on its financial position, financial performance and cash flows.

(para. 1)

If the disclosures required by IFRS 12, together with disclosures required by other IFRSs, do not meet the objective above, an entity is required to disclose whatever additional information that is necessary to meet that objective (para. 3).

- **It is difficult to determine whether an entity meets the objective and, if not, what additional information would be needed to meet the objective**

IFRS 12

Significant judgements and assumptions

An entity shall disclose information about significant judgements and assumptions it has made (and changes to those judgements and assumptions) in determining:

(a) that it has control of another entity, ie an investee as described in paras. 5 and 6 of IFRS 10;

(b) that it has joint control of an arrangement or significant influence over another entity; and

(c) the type of joint arrangement (ie joint operation or joint venture) when the arrangement has been structured through a separate vehicle.

(para. 7)

- **Disclosures provided in accordance with paras. 7-9 have become "boilerplate" disclosures, with little information value**

IFRS 12 “Material to the reporting entity”

An entity is required to disclose information about each of its subsidiaries that have non-controlling interests that is material to the reporting entity (para. 12).
Also, an entity is required to disclose information about each joint arrangement and associate that is material to the reporting entity (para. 21(a)) and information about each joint venture and associate that is material to the reporting entity (para. 21(b)).

- The definition of “material to the reporting entity” is unclear

IFRS 12

Individually immaterial joint ventures and associates

An entity is required to disclose financial information as specified in paragraph B16 about the entity's investments in joint ventures and associates that are not individually material:
(i) in aggregate for all individually immaterial joint ventures and, separately,
(ii) in aggregate for all individually immaterial associates.
(para. 21(c))

- **This requirement incurs costs to the preparers when only limited benefits are provided to users**

IFRS 12 Structured entities

A structured entity is an entity that has been designed so that voting or similar rights are not the dominating factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements (para. B21).

- **This paragraph and the following paragraphs in IFRS 12 are too vague to apply in practice**

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