IFRS

STAFF PAPER

January 2019

IFRS® Interpretations Committee meeting

Project	**Investment in a subsidiary accounted for at cost: Partial disposal (IAS 27)**		
Paper topic	Agenda decision to finalise		
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Introduction

1. At its September 2018 meeting, the IFRS Interpretations Committee (Committee) discussed how an entity applies the requirements in IAS 27 *Separate Financial Statements* to a fact pattern involving an investment in a subsidiary. In the fact pattern described in the submission, the entity preparing separate financial statements:

   (a) elects to account for its investments in subsidiaries at cost applying paragraph 10 of IAS 27.

   (b) holds an initial investment in a subsidiary (investee). The investment is an investment in an equity instrument as defined in paragraph 11 of IAS 32 *Financial Instruments: Presentation*.

   (c) subsequently disposes of part of its investment and loses control of the investee. After the disposal, the entity has neither joint control of, nor significant influence over, the investee (partial disposal transaction).

2. The submitter asked whether:

   (a) the investment retained (retained interest) is eligible for the presentation election in paragraph 4.1.4 of IFRS 9 *Financial Instruments*. That election permits the holder of particular investments in equity instruments to present subsequent changes in fair value in other comprehensive income (OCI) (Question A).

(b) the entity presents in profit or loss or OCI any difference between the cost of the retained interest and its fair value on the date of losing control of the investee (Question B).

3. The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to account for a partial disposal transaction in its separate financial statements. Consequently, the Committee tentatively decided not to add these matters to its standard-setting agenda and in September 2018 published a tentative agenda decision.

4. The purpose of this paper is to:

(a) analyse the comments on the tentative agenda decision; and

(b) ask the Committee whether it agrees with our recommendation to finalise the agenda decision.

5. This paper has two appendices:

(a) Appendix A—proposed wording of the agenda decision; and

(b) Appendix B—comment letters.

Feedback summary and staff analysis

6. We received six comment letters, reproduced in Appendix B to this paper. All respondents agree with the Committee's conclusions on these matters. Nonetheless, two respondents (KPMG and Deloitte) question the Committee's rationale for its conclusion on Question B. Some respondents also provide feedback on other aspects of the tentative agenda decision. Respondents' comments, together with our analysis, are presented below.

Rationale for conclusion on Question B

Summary of feedback

7. Deloitte and KPMG question the Committee's rationale for its conclusion on Question B. Both respondents suggest replacing the reference to similar and related issues in paragraph 22(b) of IAS 28 *Investment in Associates and Joint Ventures* and paragraph 11B of IAS 27 with a reference to paragraph 88 of IAS 1 *Presentation of Financial Statements*. This is because:

   (a) the reference to similar and related issues is not persuasive (Deloitte); and

   (b) no IFRS Standard permits or requires an entity to present a gain or loss on disposal of an investment outside profit or loss (KPMG).

8. Mazars agrees that paragraph 22(b) of IAS 28 deals with a similar and related issue, but nonetheless suggests adding a reference to paragraph 88 of IAS 1.

Staff analysis and conclusion

9. We agree with these respondents who say that, in effect, any difference between the cost and fair value of the retained interest on the date the entity loses control (a) meets the definitions of income or expenses in the 2018 *Conceptual Framework for Financial Reporting*, and (b) applying paragraph 88 of IAS 1, would be recognised in profit or loss. This is consistent with our analysis in September 2018 (see paragraph 30 of Agenda Paper 6A of the Committee's September 2018 meeting).

10. Accordingly, we recommend that the Committee expand the rationale for its conclusion on Question B by specifying that:

    (a) any difference between the cost of the retained interest and its fair value on the date of losing control of the investee meets the definitions of income or expenses in the *Conceptual Framework for Financial Reporting*; and

    (b) applying paragraph 88 of IAS 1, an entity recognises this difference in profit or loss.

11. We also recommend retaining the references to the requirements in paragraph 22(b) of IAS 28 and paragraph 11B of IAS 27, which deal with similar and related issues.

12. Appendix A to this paper sets out our proposed changes to the tentative agenda decision in this respect.

Other suggestions

Scope of agenda decision

Summary of feedback

13. The Global Financial Reporting Collective suggests widening the application of the Committee's conclusion by replacing the phrase 'cost of the retained interest' with 'carrying amount of the retained interest' in the agenda decision. In that way, the Committee's conclusion would also apply to other situations, such as when an entity accounts for its initial investment using the equity method.

Staff analysis and conclusion

14. We think this suggestion is beyond the scope of the matters raised in the submission and recommend no change to the agenda decision in this respect.

Request for standard-setting

Summary of feedback

15. The MASB agrees with the Committee's conclusions but nonetheless suggests that, for clarity, the Committee consider reporting the matter to the Board to determine whether to amend IAS 27.

Staff analysis and conclusion

16. We continue to agree with the Committee's conclusion that the principles and requirements in IFRS Standards provide an adequate basis for an entity to account for the partial disposal transaction. Accordingly, we see no need to consider amending IAS 27 in this respect. Although we report all matters discussed by the Committee to the Board at a public meeting, we recommend not specifically asking the Board to consider amending IAS 27 in this respect.

Wording and other suggestions

Summary of feedback

17. KPMG and Mazars agree with the Committee's conclusion on Question A—ie the entity can apply the presentation election in paragraph 4.1.4 of IFRS 9 to the retained interest when it begins to apply the requirements in IFRS 9 to that interest. Nonetheless, those respondents suggest replacing the words '…when the entity *first applies* IFRS 9 to the retained interest' with the words '…at *initial recognition* of the retained interest applying IFRS 9'.

18. One respondent (L Dias) comments on the implications of the Committee's analysis on consolidated financial statements—that respondent suggests clarifying that an entity recognises (a) any gain or loss on disposal in profit or loss, and (b) any subsequent changes in the fair value of the retained interest in profit or loss or in OCI (depending on whether it applies the presentation election in paragraph 4.1.4 of IFRS 9).

Staff analysis and conclusion

19. We agree with KPMG's and Mazars' suggestion and think that amending the wording could improve the clarity of the Committee's conclusion. We note that paragraph 4.1.4 of IFRS 9 uses the words 'at initial recognition'. Appendix A to this paper sets out our proposed changes to the wording of the tentative agenda decision in this respect.

20. Regarding the comment from L Dias, we note that the agenda decision already specifies in the context of separate financial statements (a) how an entity accounts for any difference between the cost of the retained interest and its fair value on the date of the partial disposal transaction, and (b) whether the entity can apply the presentation election in paragraph 4.1.4 of IFRS 9 to the retained interest. We think no further clarification is needed in this respect.

Staff recommendation

21. Based on our analysis, we recommend finalising the agenda decision as published in IFRIC® Update in September 2018, subject to the changes noted in paragraphs 10 and

19 of this paper and some editorial changes. Appendix A to this paper sets out the proposed wording of the final agenda decision.

Question for the Committee
Does the Committee agree with the staff recommendation to finalise the agenda decision set out in Appendix A to this paper?

Appendix A—Proposed wording of the agenda decision

A1. We propose the following wording for the final agenda decision (new text is underlined and deleted text is struck through).

Investment in a subsidiary accounted for at cost: Partial disposal (IAS 27 *Separate Financial Statements*)

The Committee received a request about how an entity applies the requirements in IAS 27 to a fact pattern involving an investment in a subsidiary.

In the fact pattern described in the request, the entity preparing separate financial statements:

- elects to account for its investments in subsidiaries at cost applying paragraph 10 of IAS 27.

- holds an initial investment in a subsidiary (investee). The investment is an investment in an equity instrument as defined in paragraph 11 of IAS 32 *Financial Instruments: Presentation*.

- subsequently disposes of part of its investment and loses control of the investee. After the disposal, the entity has neither joint control of, nor significant influence over, the investee.

The request asked whether:

(a) the investment retained (retained interest) is eligible for the presentation election in paragraph 4.1.4 of IFRS 9 *Financial Instruments*. That election permits the holder of particular investments in equity instruments to present subsequent changes in fair value in other comprehensive income (OCI) (Question A).

(b) the entity presents in profit or loss or OCI any difference between the cost of the retained interest and its fair value on the date of losing control of the investee (Question B).

Question A

Paragraph 9 of IAS 27 requires an entity to apply all applicable IFRS Standards in its separate financial statements, except when accounting for investments in subsidiaries, associates and joint ventures. After the partial disposal transaction, the investee is not a subsidiary, associate or joint venture of the entity. Accordingly, the entity applies IFRS 9 for the first time in accounting for its retained interest in the investee. The Committee observed that the presentation election in paragraph 4.1.4 of IFRS 9 applies at initial recognition of an investment in an equity instrument. An investment in an equity instrument within the scope of IFRS 9 is eligible for the election if it is neither held for trading (as defined in Appendix A of IFRS 9) nor contingent consideration recognised by an acquirer in a business combination to which IFRS 3 *Business Combinations* applies.

In the fact pattern described in the request, assuming the retained interest is not held for trading, the Committee concluded that (a) the retained interest is eligible for the presentation election in paragraph 4.1.4 of IFRS 9, and (b) the entity would make this presentation election ~~when it first applies IFRS 9 to~~ at initial recognition of the retained interest applying IFRS 9 (ie at the date of losing control of the investee).

Question B

~~IAS 27 does not explicitly specify how, in its separate financial statements, an entity recognises a~~Any difference between the cost of the retained interest and its fair value on the date the entity loses control of a subsidiary meets the definitions of income or expenses in the *Conceptual Framework for Financial Reporting*. ~~In such circumstances, the entity applies the requirements in paragraphs 10-11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in developing and applying an accounting policy. The entity's management refers to, and considers the applicability of, requirements in other IFRS Standards dealing with similar and related issues.~~ ~~The Committee observed that paragraph 22(b) of IAS 28 *Investments in Associates and Joint Ventures* and paragraph 11B of IAS 27 deal with similar and related issues.~~ ~~Based on its analysis of those requirements,~~ Accordingly, the Committee concluded that, applying paragraph 88 of IAS 1 *Presentation of Financial Statements*, the entity recognises this difference in profit or loss. This is the case regardless of whether the entity presents subsequent changes in ~~the~~ fair value of the retained interest in profit or loss or OCI.

The Committee also noted that its conclusion is consistent with the requirements in paragraph 22(b) of IAS 28 *Investments in Associates and Joint Ventures* and paragraph 11B of IAS 27, which deal with similar and related issues.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to account for a partial disposal transaction in its separate financial statements.

Consequently, the Committee ~~[~~decided~~]~~ not to add this matter to its standard-setting agenda.

Appendix B—Comment letters

Deloitte.

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21 November 2018

Sue Lloyd
Chair
IFRS Interpretations Committee
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Dear Ms Lloyd

Tentative agenda decision – IAS 27 *Separate Financial Statements*: Investment in a subsidiary accounted for at cost – Partial disposal

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the September IFRIC Update of the tentative decision not to take onto the Committee's agenda the request for clarification on the accounting for a loss of control of a subsidiary measured at cost in separate financial statements.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision although we do not find the analogies to IAS 28 *Investments in Associates and Joint Ventures* and to the investment entity requirements of IAS 27 persuasive in terms of the recognition of any difference between cost and fair value when IFRS 9 *Financial Instruments* is first applied. We recommend that this material be replaced in the tentative agenda decision by a simple reference to the requirements of paragraph 88 of IAS 1 *Presentation of Financial Statements* (that an entity shall recognise all items of income and expense in a period in profit or loss unless an IFRS requires or permits otherwise).

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader

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Ms Sue Lloyd
International Accounting Standards Board
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Our ref RD/288

21 November 2018

Dear Ms Lloyd

Tentative agenda decision: Investment in a subsidiary accounted for at cost: Partial disposal (IAS 27 Separate Financial Statements)

We appreciate the opportunity to comment on the IFRS Interpretations Committee's (the Committee) tentative agenda decision *Investment in a subsidiary accounted for at cost: Partial disposal (IAS 27 Separate Financial Statements)* (IFRIC Update September 2018). We have consulted with, and this letter represents the views of, the KPMG network.

Question A

In the second paragraph of Question A, we recommend replacing the sentence '(ii) the entity would make this presentation election when it first applies IFRS 9 to the retained interest' with '(ii) the entity would make this presentation election on the initial recognition of the retained interest under IFRS 9 (ie at the date of losing control of the investee)' to clarify that the election under paragraph 4.1.4 applies only on the initial recognition under IFRS 9. That is the rationale behind the decision, and so it should be cleary stated.

Question B

We note that the Committee's conclusion focused on applying the requirements in paragraphs 10-11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, and subsequently referred to the applicability of IAS 28 *Investments in Associates and Joint Ventures,* in developing an accounting policy to determine how to recognise any difference between the cost of the retained interest and its fair value on the date the entity loses control of a subsidiary.

While we agree with the Committee's conclusion that the difference should be recognised in profit or loss, regardless of whether the entity presents subsequent changes in fair value in profit or loss or other comprehensive income, we believe the rationale given in the tentative agenda decision is not appropriate. While IAS 27 does not specifically address the accounting for the transaction in Question B, we believe that paragraph 88 of IAS 1 *Presentation of Financial Statements* sets out the generic requirements for when income and expenses are recognised in profit or loss. The paragraph sets a general requirement to recognise all income and expense items in profit or loss unless another IFRS states differently. No other IFRS requires or permits a gain or loss on disposal of an investment to be recognised outside of profit or loss and therefore we believe the agenda decision should refer to the requirements of IAS 1.

We would be happy to discuss our comments in more detail.

Please contact Mike Metcalf at +44 (0) 20 7694 8871 if you wish to discuss any of the issues raised.

Yours sincerely

KPMG IFRG Limited

KPMG IFRG Limited

Mrs Sue Lloyd

IFRS Interpretations Committee
Columbus Building,
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United Kingdom

Paris, November 23, 2018

Tentative Agenda Decisions – IFRIC Update September 2018

Dear Sue,

MAZARS is pleased to comment on the various IFRS Interpretations Committee tentative agenda decisions published in the September 2018 IFRIC Update.

We have gathered all our comments as appendices to this letter, which can be read separately and are meant to be self-explanatory.

We note that the Tentative Agenda Decisions are sometimes based on a strict reading of existing IFRSs without considering the relevance of the financial information resulting from the decision. In our opinion, this is especially the case for the step acquisition issue (IAS 27, see Appendix 4) and the cash flow hedge relationship (IFRS 9 and IAS 39, see Appendix 6). We consider it key to question the relevance of the accounting consequences of an Agenda Decision before finalizing it, to avoid some counterintuitive accounting and to enhance at the same time the credibility of the work undertaken by the Interpretations Committee.

Should you have any questions regarding our comments on the various tentative agenda decisions, please do not hesitate to contact Michel Barbet-Massin (+33 1 49 97 62 27) or Edouard Fossat (+33 1 49 97 65 92).

Yours faithfully

Michel Barbet-Massin **Edouard Fossat**

Financial Reporting Advisory

Appendix 3

Investment in a subsidiary accounted for at cost: Partial disposal (IAS 27 Separate Financial Statements) — Agenda Paper 6A

We agree with the conclusions reached by the Committee on the two questions raised in the submission.

Question A: whether the retained interest is eligible for the FVOCI option in IFRS 9

The Committee's conclusion relies on the fact that the first application of IFRS 9 to the retained interest on the date of losing control over the investee corresponds to the initial recognition of an investment in an equity instrument of an investee that is not a subsidiary.

We agree with that conclusion, and believe that this rationale could be made clearer by slightly modifying the agenda decision (deleted text is struck through; new text is underlined and in bold characters):

> *"In the fact pattern described in the request, assuming the retained interest is not held for trading, the Committee concluded that (i) the retained interest is eligible for the presentation election in paragraph 4.1.4 of IFRS 9, and (ii) the entity would make this presentation election when it first applies IFRS 9* ***on initial recognition of*** ~~*to*~~ *the retained interest (ie at the date of losing control of the investee)."*

Question B: whether to present in OCI or P&L any difference between the cost of the retained interest and its fair value on the date of losing control over the investee

We agree with the Committee's conclusion that any difference between the cost of the retained interest and its fair value shall be recognized in profit or loss. We agree with the reference to IAS 28.22(b) that clearly deals with a similar issue. We think that an additional rationale could have been added: the Committee could make reference to IAS 1.88 that requires all items of income and expenses to be recognized in profit or loss unless an IFRS requires or permits otherwise.

MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

21 November 2018

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee (Committee)
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd

Tentative Agenda Decision - Investments in a subsidiary accounted for at cost: Partial disposal (IAS 27 *Separate Financial Statements*)

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the above Tentative Agenda Decision.

We agree with the Committee's conclusion for both Questions A and B. However, for clarity purpose we recommend that the Committee considers reporting the issue to the International Accounting Standards Board to determine whether any amendment should be made to IAS 27.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,

TAN BEE LENG
Executive Director

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Global Financial Reporting Collective
incorporating the Pacioli Initiative

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17 November 2018

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The Global Financial Reporting Collective is pleased to offer its comments on the Tentative Agenda Decision—Investments in a Subsidiary Accounted for at Cost - partial disposal.

We agree with conclusions reached by the Committee.

We suggest that you consider amending the wording to say that any difference between the carrying amount of the retained interest and the initial measurement at fair value be recognised in profit or loss. It seems to us that the same logic should apply whether the parent has been measuring its interests in the separate financial statements at cost or by applying the equity method.

Of course that raises some questions about equity method components that have been recognised in OCI. The accounting set out in IAS 27.11B(b) and IAS 28.22(c) seems appropriate here. When the equity method is no longer being used the OCI components are accounted for as if as if the entity had been disposed of. We also note that paragraph 22 only refers to associates and joint ventures. We think it should probably have been amended to refer to subsidiaries when the IASB amended IAS 27.10 to allow entities to use the equity method in its separate financial statements for subsidiaries, joint ventures and associates.

Thank you for considering our comments.

Global
Financial
Reporting
Collective

Global Financial Reporting Collective

17 November 2018

November 20, 2018

Mr. Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EX 4M 6XH
United Kingdom

Submitted Online

Dear Mr. Hoogervorst,

Re: Tentative Agenda Decision and comment letters – Investments in a Subsidiary Accounted for at Cost: Partial Disposal

I appreciate the opportunity to provide my comments to the IFRS Interpretations Committee on the matter of clarifying the accounting treatment for investment interest retained after partial disposal and loss of control previously held in that investment. My comments are as follows:

General Comments:

I agree with the Committee's decision to address the matter of measuring the cost of investment retained in a subsidiary after partial disposal of its controlling interest resulting in a loss of control. The partial disposal of an investment along with loss of control would require an understanding of multiple accounting standards for its measurement and recognition. Accordingly, this interpretation will provide guidance in navigating through the standards affecting such transactions. This clarification will help in the consistent application of the standard.

Specific Comments:

Question 1
When an entity subsequently disposes of part of its investment, loses control of the investee and has neither joint control of, nor significant influence over, the investee, should the investment retained (retained interest) be eligible for the presentation election in paragraph 4.1.4 of IFRS 9, *Financial Instruments*? This election permits the holder of particular investments in equity instruments to present subsequent changes in fair value in other comprehensive income (OCI).

Response 1) Agree with the conclusion drawn by the Committee. If the retained interest is not held for trading and the presentation election in IFRS 9, paragraph 4.1.4 is made when first applied to the retained interest at the date of losing control of the investee, subsequent changes in the fair value of the retained interest should be presented in other comprehensive income (OCI).

The Committee did not specifically note that the retained interest in the equity investment, would be reflective of the disposal-date fair value of the non-controlling interest held and would approximately equate to its retained interest in the shareholders' equity of its former subsidiary. IAS 27.10 states that when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either: at cost; in accordance with IFRS 9; or using the equity method as described in IAS 28. This retained interest in the investor company preparing separate financial statements which had been recognized at cost under IAS 27.10, prior to the date of disposal and loss of control, would be revalued upon loss of control to reflect its deemed fair value. Accordingly, the increase in the value of the investment over cost on initial recognition of the disposal would be recognized in the statement of Income (loss) or Other Comprehensive Income (loss) depending on the classification prior to disposal, in the consolidated financial statements or in the entity separate financial statements as determined by its status for purposes of financial statement presentation.

Question 2
Should the entity present in profit or loss or OCI any difference between the cost of the retained interest and its fair value on the date of losing control of the investee?

Response 2) Under IFRS 27.10, *Separate financial statements*, the standard states that when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates 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*.

In the fact pattern under consideration, on the date of losing control of the subsidiary, the difference between:

a) the deemed fair value of the disposed investment as represented by a proportion of the shareholders equity in the investee; and
b) the carrying cost of the disposed investment in the parent,

would be recognized as a gain or loss on disposal of investment in the statement of income (loss) in the entity's separate financial statements.

Likewise, the retained portion of investment would be revalued to the deemed fair value of the investment recognizing the gain or loss on the value of retained interest in the statement of income (loss). Subsequent changes should be recognized in the statement of other comprehensive income if the investment is not held for trading and the presentation election under IFRS 9 paragraph 4.1.4 is made.

The retained interest in the investment is measured at fair value, where an acquirer previously prepared consolidated financial statements, as the fair value gain or loss on the total controlling interest held in its former subsidiary would have been included in the consolidated financial position of the consolidated group of entities, prior to disposition. Post disposition, the fair value gain or loss of the retained interest will have to be recognized on the separate financial statements of the entity, previously holding controlling interest, as the investment interest entity will no longer be consolidated under IAS1.51 with the former controlling entity. The value of the retained interest must not be measured by any alternative measurement basis. If the cost basis of measurement is applied and the retained interest is measured at its original consideration paid, the entity would not be recognizing the fair value of the non-controlling interest it currently holds, which is incorrect. The retained investment should be measured consistent with the spirit of the accounting standards if the fair value basis of measurement is applied.

IAS 28.22(b) makes reference to measuring retained interest in the former associate or joint venture at fair value. However prior to disposal and realization of a gain or loss on an investment held, the investment is measured at cost. IFRS 27.10 states that 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 classified for sale or for distribution. IFRS 5.15-15A states that a non-current asset or a disposal group classified as held for sale shall be measured at the lower of carrying amount or fair value less costs to sell. In keeping with these standards, an investment is measured at cost prior to its disposal in the separate financial statements of the controlling entity.

The Committee may consider clarifying that the deemed fair value on the investment disposition would give rise to a gain or loss in the parent and should be recognized in the statement of income (loss), whereas the gain or loss on the deemed fair value of the retained interest would be recognized in the statement of income (loss) or statement of other comprehensive income (loss) if not held for trading and the presentation election is made under IFRS 9.

If you have any questions please do not hesitate to contact me by email at lynessadias@gmail.com.

Yours sincerely,

Lynessa Dias, CPA, CGA, CFA, FRM, CAIA