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n°54

Paris, the 8th April 2013

Monsieur Hans HOOGERVORST
Chairman
IASB

30 Cannon Street
LONDON EC4M 6XH
UNITED KINGDOM

RE:
-ED/2012/3 Equity method Share of other net asset changes
-ED/2012/6 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture
-ED/ 2012/7 Acquisition of an interest in a joint operation

Dear Mr Hoogervorst,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the three above-mentioned exposure drafts. These views result from the ANC's due process, involving all interested stakeholders. More precisely, the due process includes fundamental work by a diversified experts working group, a full fledge discussion of its assessment by a complete Commission competent for all International standards and then a global and strategic discussion in the Collège (Board) before this letter was signed.

The ANC welcomes the efforts made by the IASB and the IFRS Interpretations Committee to address the issues arising from the application of IAS 28 and IFRS 11.

The ANC underlines that IFRS 11 has made these issues even more important to the extent that this new standard has broadened the scope of the equity method for joint ventures, which in our jurisdiction were mostly accounted for according to the proportionate consolidation method under IAS 31.

The ANC notes that those three proposed amendments, based on the work conducted by the IFRS Interpretations Committee, might be supplemented by other amendments not yet apprehended by the IASB. Indeed, the application of the equity method raises numerous unaddressed issues, some of which are closely related to the proposed amendments (as are those mentioned in our detailed comments).

In order to address all these issues in a consistent way, the ANC considers it necessary to launch a global debate on the meaning and objective of the equity method, with a comprehensive discussion about the conceptual issues underlying this method within the financial statements of the reporting entity.

Instead of performing this comprehensive debate, the Board proposes several narrow scope amendments on limited and specific issues.

The ANC underlines that the proposed limited amendments touch upon a number of fundamental concepts underlying the accounting for investments in associates, joint ventures and joint operations. Without a clear definition of the conceptual basis for equity accounting, the ANC is of the view that it is difficult to assess the consistency of these amendments between them and with other existing IFRS and it is difficult to identify a guideline that would solve all the other cross-cutting issues not addressed at this stage.

Therefore, we deem it necessary to establish an inventory of all the difficulties in applying IFRS 11 and IAS 28, including changes on interest in an associate, joint venture or joint operation, in order to identify all matters not covered by the existing IFRS and in order to develop a consistent set of principles in their entirety.

In the research setting such principles, the IASB should consider the following issues:

- Should the equity method be considered as a one-line consolidation or as a valuation method of the investment?
- What are the objectives of the equity method within the reporting entity?
- What is the relevant measure of the performance of the investee accounted for using the equity method in the consolidated financial statements?

At last, as explained in our comment letter relating to ED 2012/2 : Annual improvements, the ANC considers that the IASB should address any issue related to IFRS 3, within the planned post-implementation review of the standard rather than within a series of separate standard-setting initiatives (in particular : proposed amendments to IFRS 11 *Acquisition of an interest in a joint operation*, and proposed amendments to IFRS 10 and IAS 28 *Sales or contributions of assets between an investor and its associate/joint venture*), which does not enable a global vision of the issues at stake.

Our detailed comments on the three above-mentioned exposure drafts are set out in the Appendix I to this letter. However, we would like to draw your attention to the following concerns:

ED 2012-3:

The ANC considers that the IASB should not deal with this issue as a matter of emergency to the extent that:

- the proposed amendment results in developing a unique solution for all types of other net assets changes that are in substance different;the discussions held in the course of our due process highlight that views diverge on how best to reflect the substance of each transaction within the financial statements of the investor;
- the objective pursued by the IASB was to resolve diversity in practice and we do not observe such divergence of practice in France;
- the systematic solution proposed by the IASB may only be temporary given the inconsistencies raised by this solution and the need for a thorough debate about the conceptual issues relating to the equity method;

- in a large number of cases, the solution proposed by the IASB would require companies to change their method of accounting for dilutions; we question the relevance of such change in so far as this temporary solution might be challenged when the ongoing discussions on performance and reflections which seem necessary on the equity method are finalised.

For all these reasons, the ANC is not in favour of the proposed amendment as currently drafted by the IASB.

ED 2012-6 and ED 2012-7:
The proposed amendments introduce another boundary depending on whether the transactions involve assets constituting a business or not. The definition of a business is not always straightforward to apply as evidenced by the ongoing work of the IFRS IC on this issue. The ANC is concerned that resolving divergence of practice by moving to another source of diversity in practice is not a suitable approach.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely,

Jérôme HAAS

Appendix I.1 - ED/2012/3 Equity method Share of other net asset changes

Question 1
The IASB proposes to amend IAS 28 so that an investor should recognise in the investor's equity its share of the changes in the assets of the investee that are not recognised in profit or loss or OCI of the investee, and that are not distributions received. Do you agree? Why or Why not?

1. The ANC appreciates the efforts made by the IASB and the IFRS IC to address the lack of clarity provided by IAS 28 which does not specify how an investor should account for its share of other net asset changes of its investee that are neither profit or loss, nor other comprehensive income of the investee or distributions received, to the extent that § 10 of IAS 28 is silent on the treatment to be made in such cases.

2. However, the ANC disagrees with the observation made by the IASB in § BC8 of the ED which states that the proposed solution leads to return to the previous requirement of IAS 28 pre 2007:

- The ANC is of the view that the IASB has not demonstrated that the previous wording of IAS 28 implied to account all the other changes of net assets of the investee in the investor's equity. The ANC underlines that all of the examples of "*changes in the investors's proportionate interest in the investee arising from changes in the investee's that have not been recognised in the investee's profit or loss*", provided in § 11 of IAS 28 pre-2007 only reflected changes in the investee's other comprehensive income.

- The ANC points out that in July 2009, the IFRIC noted that there was no specific guidance on the recognition of a gain or loss resulting from a reduction in the investor's ownership interest following the issue of shares by the associate. Therefore, when the IFRIC considered the question in 2009, it has neither considered that such a transaction should be recognised in the investor's equity, nor brought out that the 2009 Wording for rejection was challenging previous practices.

3. The ANC stresses that "other changes in net assets" of the investee that might occur in practice may result from different situations:

– First category: changes in the share capital of the investee (investee's capital increase not subscribed by the investor, acquisition of treasury shares by the investee from third parties or sale of treasury shares to third parties): in such cases the dilutive or anti-dilutive impacts in terms of ownership are immediate and definitive;

– Second category: changes in other components of the investee's equity (share-based payment transactions, transaction involving call options over the own shares of the investee): in such cases the potential dilutive impact of the transaction in terms of ownership is deferred until such instruments are exercised;

– Third category: other transactions of the investee with parties other than the investor, for example when the investee enters into transactions with its own non-controlling interests. These transactions would never lead to change in ownership interest of the investor.

Regarding the first category, in France, we do not observe divergence of practices. When an investor's ownership interest in the associate is reduced, the dilutive impact of the change is recognised as deemed disposal in profit and loss of the investor. This practice is in line with the practices documented in the IFRS manuals published by various audit firms.
Nevertheless, the ANC recognises that for certain situations within the second and third category different accounting practices might have been developed, creating diversity in practice.

The ANC is not convinced that all of these situations must be accounted for in the same way in the financial statements of the investor. The discussions held in the course of our due process highlight that views diverge on how best to reflect the substance of each transaction in all three categories implying other net asset changes.

4. Besides, the ANC is concerned that the proposed amendment will generate other inconsistencies within the provisions of IAS 28:

- IAS 28 § 25 indicates that: "*If an entity's ownership interest in an associate or a joint venture is reduced, but the 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.*"

- the ANC wonders about the relevance of recycling proportional impacts of the transaction from other comprehensive income to profit and loss when such a transaction has to be overall recognised as an equity transaction.
  (Please refer to issues developed for question 2 in § 7)

5. In addition, the ANC considers that the proposed amendment will generate other inconsistencies with others IFRSs. In particular, the ANC stresses that the proposed accounting is to recognise in equity the impact of transactions between the investee (associate or joint venture) and third parties whereas:

- IAS 1.106 (d) indicates that changes in equity only include changes resulting from profit or loss, other comprehensive income and transaction with owners in their capacity as owners, and

- transactions with associates or joint ventures are not considered as transactions with owners (as IFRS 10 appendix A considers that associates and joint ventures are excluded from the group which is defined as a parent and its subsidiaries).

6. Therefore the ANC considers that the IASB should not deal with this issue as a matter of emergency to the extent that:

- the systematic solution proposed by the IASB may only be temporary given the inconsistencies raised by this solution and the need for a thorough debate about the conceptual issues relating to the equity method;

- in a large number of cases, the solution proposed by the IASB would require companies to change their method of accounting for dilutions; we question the relevance of such a change in so far as this temporary solution might be challenged when the ongoing discussions on performance and reflections which seem necessary on the equity method are finalised.

Question 2

The IASB also proposes that an investor shall reclassify to profit or loss the cumulative amount of equity that the investor had previously recognised when the investor discontinues the use of the equity method. Do you agree? Why or why not?

7. As mentioned in our response to question 1, the ANC considers that there is no urgency to adopt this short term temporary solution that may be challenged later and the ANC does not support the ED on recognising all other net asset changes in equity. If the Board retains its plan to recognise other net asset changes in the investor's equity, the ANC would not support the recycling from equity to profit and loss.

8. The Board does not provide any conceptual basis for creating a new category of equity that would be recycled to profit and loss.

- In BC 10 the Board explains that "*The IASB thinks that the cumulative amount of equity that the investor had previously recognised should move to retained earnings if the investor loses significant influence over the investee and discontinues the use of the equity method*." But BC 10 does not explain why the IASB thinks that.
- The ANC underlines that this type of recycling from equity to profit and loss has not been introduced before in any IFRS since so far only items of other comprehensive income have been recycled to profit or loss.
- The ANC is concerned that the proposal will introduce a new category of equity without any preliminary conceptual bases.
- The approach proposed by the IASB would present certain transactions between an investee and third parties as if they were transactions with the investor's owners; such transactions would be accounted for in the same way as transactions with owners of a subsidiary. The ANC underlines that no recycling is required in respect of similar transactions with non controlling interest when a parent loses control of a subsidiary. Therefore, the ANC considers that the recycling proposal is inconsistent with the approach which considers that other net asset changes of the investee should be accounted for in the investor's equity.
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(Please refer to issues developed in § 4 and 5)

9. When thinking of the diverse situations creating other net asset changes of the investee, the ANC wonders about the relevance of recycling in a systematic way, amounts previously recognised in equity.

- Assume that the investee is a holding company that owns several subsidiaries. When the investee sells to non-controlling shareholders an interest in a subsidiary without losing control over this subsidiary, the investee has to account for an "other net asset change" being the difference between the price paid by the new shareholders and the book value of the net assets transferred to non-controlling interests. In that case the other net asset change accounted for by the investee could be considered as being part of the performance of the investee (as a holding company), and the ANC considers that recycling is relevant, even though we could question whether this P&L impact should not be recorded at transaction date rather than at the date when the investor discontinues the use of the equity method.

- On the contrary, when the investee buys non-controlling interests from non-controlling shareholders, the “other net asset change” that has to be accounted for by the investee is not part of its performance, but represents the effect of an additional investment in the subsidiary. In that case the ANC questions the relevance of any P&L impact when the investor discontinues the use of the equity method.
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Question 3
Do you have any other comments on the proposals?

9. The ANC disagrees with the transition proposals and considers that such amendment should be applied prospectively.

10. The ANC notes that the IFRS IC tentatively decided in March 2012 that “*where an investor’s percentage of ownership interest in the investee increases, the impact of the change should be accounted for as an incremental purchase*”. Even if this tentative decision has not been followed by the IASB, the ANC underlines that IAS 28 is silent on the accounting for any subsequent increase in ownership interest in the same associate or joint venture while maintaining significant influence or joint control. Thus this issue should also be addressed by the IASB.

11. The ANC encourages the IASB to relaunch the debate of the equity method of accounting with a more comprehensive discussion about the conceptual issues related to the equity method:

- What is the relevant performance of investee accounted for using the equity method in the consolidated financial statements?

- Should the equity method be considered as one-line consolidation or a basis of measurement?

Appendix I-2- ED/20912/6 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

Question 1: proposed amendment to IFRS10
The IASB proposes to amend IFRS 10 so that the gain or loss resulting from the sale or contribution of subsidiary that does not constitute a business, as defines in IFRS3, between an investor and its associate or joint venture is recognised only to the extent of the unrelated investor's interests in the associate or joint venture. The consequence is that a full gain or loss is recognised on the loss of control of a subsidiary that constitutes a business, as defines in IFRS3, including cases in which the investor retains joint control of, or significant influence over the investee. Do you agree with the amendment proposed? Why or why not? If not what alternative do you propose?
Question 2: proposed amendment to IAS 28 (2011)
The IASB proposes to amend IAS 28 (2011) so that:
a) The current requirement for the partial gain or loss recognition for transactions between an investor and its associate or joint venture only apply to the gain or loss resulting from the sale or contribution of assets that do not constitute a business, as defines in IFRS3 ; and
b) The gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS3, between an investor and its associate or joint venture is recognised in full.
Do you agree with amendment proposed? Why or why not? If not, what alternative do you propose?

1. The ANC concurs with the objective of the IASB to address the inconsistency between IFRS 10 and IAS 28 which conflict on whether a sale or contribution of assets between an investor and its associate or joint venture should be accounted for as a partial or full gain or loss in the financial statements of the investor.

2. The ANC is of the view that the proposed amendment has the merit to resolve divergence of practice in a pragmatic solution.

3. However, the ANC is concerned that moving to a distinction where the accounting rules will depend on whether the assets being sold or contributed to the investee constitute a business or not will trigger further other difficult issues as the definition of a business is not always straightforward to apply. The ANC is concerned that the outcome of the post-implementation review of IFRS 3 might identify issues that could call into question the proposal of the amendment.

4. Besides, the ANC wonders about the relevance of applying the elimination procedures required by § 28 of IAS 28 only to the extent that the assets being sold or contributed do not constitute a business. The ANC is of the view that this issue should be addressed with a more comprehensive discussion about the conceptual issues related to the equity method as already mentioned in our response to the ED 2012/3 (Please refer to issues developed in question 3 of the ED 2012/3 - § 6).

5. Moreover, the ANC notes that B34 of IFRS 11 indicates that: "*When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a sale or contribution of assets, it is conducting the transaction with the other parties to the joint operation and, as such, the joint operator shall recognise gains and losses resulting from such a transaction only to the extent of the other parties' interests in the joint operation.*" As a result, the inconsistency that the board is dealing with in ED 2012/6 between IAS 28 and IFRS 10 also exists between IFRS 11 and IFRS10 and remains unaddressed. The ANC considers that the IASB should also explore this issue.

Question 3: transition requirements

The IASB proposes to apply the proposed amendments to IFRS10 and IAS 28 (2011) prospectively to sales or contribution occurring in annual periods beginning on or after the date that the proposed amendments would become effective.

Do you agree with the proposed transition requirements? Why or why not? If not, what alternative do you propose?

The ANC considers that such amendment should be applied prospectively.

Appendix I-3- ED/ 2012/7 Acquisition of an interest in a joint operation

Question 1: relevant principles *The IASB proposes to amend IFRS 11 and IFRS 1 so that a joint operator accounting for the acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business applies the relevant principles on business combinations accounting in IFRS3 and other Standards, and disclose the relevant information required by those Standards, and discloses the relevant information required by those Standards for business combinations.* *Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?*

1. The ANC supports the objective of the IASB to address the diversity of practices that might arise as neither IFRS 11, nor IAS 31 which IFRS 11 replaced provide guidance on the accounting by a joint operator for the acquisition of an interest in a joint operation.

2. The ANC is of the view that applying principles which have been developed in IFRS 3 to the initial recognition of assets and liabilities of a joint operation which activity constitutes a business is not meaningless. In particular, the ANC is of the view that the recognition of goodwill is relevant in such a case.

3. However, at this stage, the ANC has not been able to perform a comprehensive analysis of all the potential consequences of the proposed amendment for acquisition of an interest in a joint operation.
Indeed, the proposed amendment would imply different accounting treatments for the acquisition of an interest depending on whether the joint arrangement has been considered as a joint venture or a joint operation.
Making the assessment about whether a joint arrangement is a joint operation or a joint venture implies a high degree of judgment. The ANC understands that the IASB is aware of this difficulty as educational material to assist those making the judgements required is in the process of being developed.

4. Moreover, the ANC stresses that the ED only addresses one side of the transaction and that it appears necessary to deal with the other side:

- Formation of a joint operation often involves joint operators contributing their own business to the joint operation;
- No guidance is provided within IFRSs for the loss of control over a business that is contributed to a joint operation in exchange for an interest in that joint operation. As already mentioned in our response to ED/2012/6 the ANC notes that B34 of IFRS 11 indicates that : "*When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a sale or contribution of assets, it is conducting the transaction with the other parties to the joint operation and, as such, the joint operator shall recognise gains and losses resulting from such a transaction only to the extent of the other parties' interests in the joint operation.*" As a result, the inconsistency that the board is dealing with in ED 2012/6 between IAS 28 and IFRS 10 also exists between IFRS 11 and IFRS 10 and is not addressed.
- The ANC considers that it is difficult to apprehend the accounting for acquisition of an interest in a joint operation to the extent that no guidance is provided for the sales or contribution of assets to the joint operation made in exchange.

5. Besides, the ANC considers that the proposed amendment reintroduces other issues which require more thorough analysis:

- Which are the relevant principles of IFRS 3 to be applied?
- What is the relevance of accounting for acquisition costs as expenses for the acquisition of interest in a joint operation whereas similar acquisition costs have to be included in the cost of the investment for joint ventures accounted for using the equity method?

6. As a conclusion, the ANC believes that amendments to IFRS 11 should be determined in a more global analysis in order to identify all matters not covered by the IFRSs and in order to develop a consistent set of principles in their entirety.

Question 2: scope
The IASB intends to apply the proposed amendment to IFRS11 and the proposed consequential amendments to IFRS11 to that acquisition of an interest in a joint operation on its formation. However it should not apply if no existing business is contributed to the joint operation on its formation.
Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

7. The ANC is concerned that the IASB has not addressed the situation where the acquisition of an interest in a joint operation coincides with the creation of the business which might be the case if the business is created due to the contributions of each party in the joint arrangement. The ANC considers that the IASB should also address this issue.

8. Moreover, the ANC would like to understand what the intention of the IASB is when parties involved in a joint operation on its formation have joint control due to the arrangement between the parties whereas each party keeps its owns assets and liabilities.

- § BC 10 of the ED implies that relevant principles of IFRS 3 should also be applied for the acquisition of an interest in a joint operation on its formation,The “acquisition of an interest” is neither defined in the ED nor in IFRS 11,The definition of “interest” in IFRS 12 is very broad as for the purpose of IFRS 12 an interest in another entity *“refers to contractual and non-contractual involvement that exposes an entity to variability of returns from the performance of the other entity. An interest in another entity can be evidenced by, but is not limited to, the holding of equity or debt instruments as well as other forms of involvement such as the provision of funding, liquidity support, credit enhancement and guarantees. It includes the means by which an entity has control or joint control of, or significant influence over, another entity. An entity does not necessarily have an interest in another entity solely because of a typical customer supplier relationship.”*
- Do we have to consider in such cases that each party acquires an interest in the joint operation on its formation?
- What are the relevant principles of IFRS 3 to be applied? Should the assets previously held be re-measured at fair values?

Question 3: transition requirement
The IASB intends to apply the proposed amendment to IFRS 11 and the proposed consequential amendment to IFRS 1 prospectively to acquisitions of interest in joint operations in which the activity of the joint operation constitutes a business on or after the effective date.
Do you agree with the proposed transition requirement? Why or why not? If not, what alternative do you propose?

9. The ANC considers that such amendment should be applied prospectively.