EFRAG

European Financial Reporting Advisory Group

ED/2012/7 *Acquisition of an Interest in a Joint Operation* (Proposed amendment to IFRS 11)

Feedback to Constituents – EFRAG Final Comment Letter

June 2013

Objective of this feedback statement

EFRAG published its final comment letter on the ED/2012/7 *Acquisition of an Interest in a Joint Operation* (Proposed amendments to IFRS 11 *Joint Arrangements*) ('the ED') on 17 April 2013.

This feedback statement summarises the main comments received by EFRAG on its draft comment letter and explains how those comments were considered by EFRAG Technical Expert Group (EFRAG TEG) during its technical discussions when reaching a final position on the ED.

Background to the Exposure Draft

On 13 December 2012, the IASB published the ED with a request for comments by 23 April 2013.

The ED proposed to introduce guidance in IFRS 11 on how a joint operator should account for the acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3 *Business Combinations*.

Neither IFRS 11 nor IAS 31 *Interests in Joint Ventures* (which was superseded by IFRS 11) explicitly address this type of transaction.

The ED proposes to amend IFRS 11 so that a joint operator should apply the relevant principles for business combinations accounting in IFRS 3 and other relevant IFRSs when accounting for the acquisitions referred to above. These principles include:

- Measuring identifiable assets and liabilities at fair value with the exceptions given in IFRS 3 and other IFRSs;
- Recognising acquisition-related costs as expenses when incurred and the services are received, with the exception that the costs to issue debt or equity securities are recognised in accordance with IAS 32 *Financial Instruments: Presentation* and IFRS 9 *Financial Instruments*;
- Recognising deferred tax assets and liabilities arising from the initial recognition of assets or liabilities, except for deferred tax liabilities arising from the initial recognition of goodwill; and
- Recognising the excess of the considered transferred over the net identifiable assets acquired and the liabilities assumed, if any, as goodwill.

EFRAG´s draft comment letter

EFRAG published its draft comment letter on the ED in January 2013. EFRAG generally supported the application of the principles in IFRS 3 *Business Combinations* to account for the acquisition of an interest in a joint operation, when its activity constitutes a business. However, EFRAG raised a number of concerns with the proposed amendments.

Further information is available on the project page on the EFRAG website.

EFRAG's final comment letter

In its final comment letter, EFRAG did not support the proposed amendments. In EFRAG's view, a number of concerns were expressed with regard to the application of the principles in IFRS 3 to acquisitions of interests in joint operations, which, if left unresolved, could result in additional diversity in practice.

Comments received from constituents

EFRAG's tentative position

In its draft comment letter, EFRAG expressed a number of concerns that stemmed from the narrow focus of the ED, and the fact that IFRS 11 was a recent standard.

- The level of judgment required to distinguish a joint operation from a joint venture would place considerable stress on how the definition of a 'joint operation' and a 'business' were understood in practice.
- There were different ways in which an entity can acquire an interest in a joint operation that are not specifically addressed in the ED, and therefore leaves room for new uncertainty and diversity in practice.
- One of the basic principles in IFRS 3 was that the standard applies on the date on which the acquirer obtains control of one or more businesses. The IASB should therefore clarify what the accounting should be in relation to the acquisition of additional interest in a joint operation, where joint control is maintained.
- The ED left open a number of cross-cutting issues that interact with other ongoing IASB projects.

Constituents' comments

Like EFRAG, most respondents expressed a number of concerns that would need to be addressed should the IASB decide to finalise the proposed amendments, and raised new concerns.

One respondent questioned whether an interest in a joint operation can meet the definition of a business. In their view, if what is acquired is property classified as a 'joint operation', the entity has concluded that it does not constitute a business; otherwise it would be classified as a 'joint venture'. Furthermore, they noted that, in their view, the amount that the acquirer is prepared to pay for the assets represents the value of those assets to the acquirer. Accordingly, this amount should be treated as the costs of those assets (as with any other fixed asset). Alternatively, part of the amount may be treated as a separate intangible

EFRAG's response to respondents' comments

In its final comment letter, EFRAG did not support the proposed amendments. As noted in its draft comment letter, a number of concerns were expressed with regard to the application of the principles in IFRS 3 to acquisitions of interests in joint operations, which, if left unresolved, could result in additional diversity in practice. These concerns were confirmed by EFRAG's constituents.

EFRAG considered the additional concerns mentioned and requests for clarification on the application of acquisition accounting in IFRS 3 to an acquisition of an interest in a joint operation. This further highlighted the need for further work on the proposed amendments.

EFRAG agreed that the essence of IFRS 11 is to reflect the rights and obligations that a joint operator has in a joint arrangement that is classified as a joint operation. It was therefore less obvious why a joint operator would apply the principles in IFRS 3 to an acquisition of an interest in a joint operation, regardless of whether the activity of the joint operation would, in itself constitute a business. EFRAG thought that this uncertainty again demonstrated a need for further analysis by the IASB.

In the light of the comments received, EFRAG concluded that it did not believe that resolving divergence in practice by moving to another source of diversity was an appropriate solution to resolving the issue the ED addresses. In EFRAG's view, to achieve consistent accounting for acquisitions of joint operations and related transactions, a more comprehensive analysis of accounting for acquisitions of an interest in a joint operation is required.

Comments received from constituents

asset where this is justified by the circumstances.' This respondent did not support the proposed amendments. Further questions were raised by another respondent about what constitutes 'acquisition of an interest' as this term is neither defined in the ED nor in IFRS 11.

Another respondent emphasised that an interest in a joint operation can also be acquired without the transfer of equity interests. For example, an 'acquirer' can obtain joint control of an entity that was previously accounted for as an associate, due to changes in the contractual agreements with the (formerly) controlling entity. In such a case, no 'equity interests' are transferred. The ED did not address this situation.

Some respondents questioned how the notion of the 'entity perspective', embedded in IFRS 3 and IFRS 10, would affect the 'additional' interest in a joint operation, while maintaining joint control. For example, if non-controlling interests did not exist in a joint operation, it was not clear how an entity should account for 'additional' interest in a joint operation given that IFRS 3 prohibits the recognition of additional goodwill once control is obtained. The IASB should explain this.

EFRAG's response to respondents' comments

List of respondents to EFRAG's draft comment letter

CL01 Accounting Standards Committee Germany

CL02 Financial Reporting Council

CL03 FSR – danske revisorer

CL04 Comissão de Normalização Contabilística

CL05 Dutch Accounting Standards Board

CL06 Instituto de Contabilitad y Auditoria de Cuentas

CL07 Organismo Italiano di Contabilità

CL08 European Securities and Markets Authority

CL09 Autorité des Normes Comptables