

International Accounting Standards Board
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom

27 May 2021

Dear Mr Hoogervorst,

Re: Post-implementation Review of IFRS 10, IFRS 11 and IFRS12 - Overview of the Reported Issues

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to provide input on the IASB's Request for Information on the Post-implementation Review of IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, and IFRS 12 *Disclosure of Interests in Other Entities* (**the RFI**).

Due process considerations

This paper is a result of EFRAG Secretariat consulting the EFRAG Board, EFRAG TEG and its Working Groups and EFRAG constituents.

EFRAG took part in IASB's preparatory phase and discussed the topics that should be further considered in the IASB's PIR project. That includes meetings with of the EFRAG Board, EFRAG TEG, EFRAG Consultative Forum of Standard Setters (EFRAG CFSS), and EFRAG User Panel (EFRAG UP).

Following the publication of the RFI, EFRAG Secretariat further informed the members of EFRAG Board, EFRAG TEG, and consulted the members of EFRAG User Panel, EFRAG TEG Working Groups, National Standard Setters, and User and Preparer Organisations. Information was further collected through participation in and organisation of dedicated webinars and conferences involving European constituents. Further, a public questionnaire has been used to collect information from constituents. These consultations have provided the information on which aspects of the Consolidation Package still create implementation or application issues, and which areas lack guidance, require implementation details or other standard setting process in regard to existing IFRS Standards.

This paper has been prepared by the EFRAG Secretariat in order to report the issues heard from constituents for consideration by the IASB in the further phases of PIR, and it has been approved by EFRAG TEG.

EFRAG Secretariat notes that this report does not express EFRAG's assessment of the reported issues, nor it reports a position, such as specific requests from EFRAG for action by the IASB. Moreover, this report has not gone through the entire EFRAG's due process and therefore should not be considered as approved by the EFRAG Board.

Methodology used when drafting this response

EFRAG Secretariat notes that the information on prevalence of the issues or their materiality has not been available for many of the reported aspects. In this respect, the report should be considered as a collection of the issues reported to the EFRAG Secretariat either by stakeholders organizations or by single constituents participating to EFRAG's consultation and outreach process in regard to Consolidation Package implementation or application issues.

Nevertheless, in order to enhance this aspect of the report, the EFRAG Secretariat incorporated the information regarding whether the comments were originated by European National Standard Setters, or other Constituents. Furthermore, during the

drafting process, we have also re-consulted our constituents in order to clarify some of the issues, confirm them, and provide additional details or examples.

Structure of the response

In drafting of the response, EFRAG Secretariat followed the structure of the RFI. The cross-cutting issues has been collected under the response to Question 10.

A complete set of issues raised in by EFRAG Constituents is provided in Appendix 1 to this paper. This Appendix also contains classification of the issues whether they contain our constituents' request for further guidance on the topic or a suggestion to the IASB to consider a change in the existing IFSR principles and guidance.

The details of the issues are provided in Appendix 2 to this letter.

If you would like to further discuss the reported issues, please do not hesitate to contact Robert Stojek (robert.stojek@efrag.org), Didier Andries (didier.andries@efrag.org), Sedat Saritas (sedat.saritas@efrag.org), or me.

Yours sincerely,



Chiara Del Prete
EFRAG TEG Chairwoman

Appendix 1: List and Classification of the Issues Reported by Constituents

List of Reported Issues

The following schedule provides a list of all the issues reported by constituents. The relevant issue details, together with examples and suggestions, are provided in the Appendix of this cover letter.

	Description
Q2	Control – power over an investee
2.1	Assessment of relevant activities
2.2	Changes occurring over an investee’s life
2.3	Changes in the relative weight of relevant activities
2.4	Determining the moment when control arises
2.5	Determining which rights are protective
2.6	Identification of control when legal requirements prevent a shareholder from exercising its rights
2.7	Additional illustrative examples how to determine control in specific cases
2.8	Determining control in crisis situations
2.9	Assessing the role of independent directors
2.10	Golden rights/votes
Q3	Control – the link between power and returns
3.1	Lack of definition of returns
3.2	Assessment of power over investee – considering variable returns
3.3	Variability of servicing fees affected by low interest rate environment
3.4	Interaction IFRS 10 and IFRS 15 wrt principals/agent assessment – legal wrapper
3.5	When does de facto control exist?
Q4	Investment entities
4.1	Definition of investment entities needs further fine-tuning
4.2	Request for more information on group financing and leveraging, which is lost in fair valuation
Q5	Accounting requirements – Change in the relationship between an investor and an investee
5.1	Change in ownership interest in an investment vehicle results in not useful information presented under IFRS 10
5.2	Transactions involving a joint operation

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	Description
5.3	Dealing with NCI when acquiring a subsidiary that is no business
Q5/A	Other issues reported by constituents regarding IFRS 10
5/A.1	Integral and non-integral investments
5/A.2	IFRS 10 lacks the overarching principle which would explain the reason for consolidated financial statements
5/A.3	Providing a proof that nobody requested to present consolidated financial statements in a sub-group seems challenging
5/A.4	Add consolidation exception for bail outs
5/A.5	Concept of control in IFRS 10 vs conceptual framework
Q6	Collaborative arrangements outside the scope of IFRS 11
6.1	Requested guidance on accounting and disclosures for collaborative arrangements
Q8	Accounting requirements for joint operations
8.1	Joint operation accounting in separate financial statements
8.2	Arrangements similar to joint operations
8.3	A re-iterated request to reconsider proportional consolidation
8.4	Relation IFRS 11 and IFRS 8
8.5	Other accounting requirements
Q9	Disclosure of Interests in Other Entities
9.1	No information on the NCI effects on the group as a whole
9.2	Information needed on revenues, cash flows, assets, liabilities, and other performance measures split per particular NCI
9.3	Cash flow statements do not present information split between the majority owned and NCI
9.4	Proportionate EBITDA - as a good example of voluntary disclosure to present information on NCI
9.5	Request for disclosures on unconsolidated structured entities
9.6	The factors used and their weight for judgments needed to classify an investment as a subsidiary, associate, or joint venture
9.7	Economic compulsion
9.8	Risks and cash flows at a more granular level
9.9	Disclosure of information when public entities have different end of year dates
9.10	Assessment of power over investee in de-facto control
Q10	Cross-cutting issues

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	Description
10.1	IFRS 5 Discontinued Operations
10.2	IFRS 16 Leases / IFRS 11
10.3	IAS 27 and IAS 28 should be included in the PIR
10.4	IFRS 10 vs IFRS 15 – corporate wrappers
10.5	Assessment of power over investee – Variable returns
10.6	Accounting for NCI resulting from written put options or forward
10.7	Accounting for contingent consideration

Requests for additional/clarifying guidance vs requests to change the requirements

The following table provides an overview of the issues depending on whether they relate to a request for guidance or to a proposed change in principles.

Nr	Request for guidance	Nr	Proposed change in principles
2.1	Assessment of relevant activities		
2.2	Changes occurring over an investee's life		
2.3	Changes in the relative weight of relevant activities		
2.4	Determining the moment when control arises		
2.5	Determining which rights are protective	2.5	Determining which rights are protective
2.6	Identification of control when legal requirements prevent a shareholder from exercising its rights		
2.7	Additional illustrative examples how to determine control in specific cases		
2.8	Determining control in crisis situations		
		2.9	Assessing the role of independent directors
		2.10	Golden rights/votes
		3.1	Lack of definition of returns
3.2	Assessment of power over investee – considering variable returns		
		3.3	Variability of servicing fees affected by low interest rate environment

PIR of IFRS 10, IFRS 11 and IFRS 12 - Overview of Reported Issues

3.4	Interaction IFRS 10 and IFRS 15 wrt principal/agent assessment – legal wrapper		
3.5	When does de facto control exist?		
		4.1	Definition of investment entities needs further fine-tuning
		4.2	Request for more information on group financing and leveraging, which is lost in fair valuation
		5.1	Change in ownership interest in an investment vehicle results in not useful information presented under IFRS 10
		5.2	Transactions involving a joint operation
5.3	Dealing with NCI when acquiring a subsidiary that is no business		
		5/A.1	Integral and non-integral investments
		5/A.2	IFRS 10 lacks the overarching principle which would explain the reason for consolidated financial statements
		5/A.3	Providing a proof that nobody requested to present consolidated financial statements in a sub-group seems challenging
		5/A.4	Add consolidation exception for bail outs
5/A.5	Concept of control in IFRS 10 vs conceptual framework	5/A.5	Concept of control in IFRS 10 vs conceptual framework
6.1	Requested guidance on accounting and disclosures for collaborative arrangements	6.1	Requested guidance on accounting and disclosures for collaborative arrangements
		8.1	Joint operation accounting in separate financial statements
		8.2	Arrangements similar to joint operations
		8.3	A re-iterated request to reconsider proportional consolidation
8.4	Relation IFRS 11 and IFRS 8		
8.5	Other accounting requirements		
		9.1	No information on the NCI effects on the group as a whole
		9.2	Information needed on revenues, cash flows, assets, liabilities, and other performance measures split per particular NCI

PIR of IFRS 10, IFRS 11 and IFRS 12 - Overview of Reported Issues

		9.3	Cash flow statements do not present information split between the majority owned and NCI
		9.4	Proportionate EBITDA - as a good example of voluntary disclosure to present information on NCI
		9.5	Request for disclosures on unconsolidated structured entities
		9.6	The factors used and their weight for judgments needed to classify an investment as a subsidiary, associate, or joint venture
		9.7	Economic compulsion
		9.8	Risks and cash flows at a more granular level
		9.9	Disclosure of information when public entities have different end of year dates
		9.10	Assessment of power over investee in de-facto control
		10.1	IFRS 5 Discontinued Operations
10.2	IFRS 16 Leases / IFRS 11		
		10.3	IAS 27 and IAS 28 should be included in the PIR
10.4	IFRS 10 vs IFRS 15 – corporate wrappers		
10.5	Assessment of power over investee – Variable returns		
10.6	Accounting for NCI resulting from written put options or forward		
10.7	Accounting for contingent consideration		

Appendix 2: Description of the Reported Issues

IFRS 10 Consolidated Financial Statements

Question 2(a) – Control – power over an investee

In your experience:

- (i) to what extent does applying paragraphs 10–14 and B11–B13 of IFRS 10 enable an investor to identify the relevant activities of an investee?
- (ii) are there situations in which identifying the relevant activities of an investee poses a challenge, and how frequently do these situations arise? In these situations, what other factors are relevant to identifying the relevant activities?

Overview

Issue nr.	Description
2.1	Assessment of relevant activities
2.2	Changes occurring over an investee's life
2.3	Changes in the relative weight of relevant activities

Issue 2.1: Assessment of relevant activities

- 1 Several issues, that create application issues, have been identified:
 - (a) Assessment of the ability to direct activities can be difficult when circumstances change, for example:
 - (i) when a company, owned by a major investor, goes public and the major investor keeps a significant part of the investment;
 - (ii) during a step-acquisition where the stake is gradually increased over a period of time (this situation is reported to occur frequently);
 - (iii) when, due to market changes or conditions, the assessment of the most relevant activities changes (and reverts), what could result in the assessment of control changing in line with market changes resulting in series of acquisitions, de-consolidations; and
 - (iv) when, over time, the product lifecycle progresses, what may trigger the changes in assessment of which activities are most relevant.
 - (b) IFRS 10 defines relevant activities as activities that significantly affect the investee's returns. Investors should assess these relevant activities to determine control and this assessment needs to be reconsidered over time if relevant facts or circumstances change. In that context, in case of a group where the ultimate parent designates the Board/Directors, agrees the budget and any investment activities, a practical expedient could be introduced to simplify the process and to reduce unnecessary assessments.
 - (c) From an auditor's perspective, preparers seem to struggle with identifying and deciding on relevant activities, undertaking a process that sometimes is seen as an accounting exercise only. Constituents explain that the main reason for this issue was is that IFRS 10 was developed combining the old IAS 27 *Consolidated and Separate Financial Statements* with SIC 12 *Special Purpose Vehicles* and bringing together accounting for, and consolidating, operating subsidiaries and structured entities. This contributes to the complexity of the standard. A possible solution could be to streamline the

guidance in order to limit the assessment and application cost and to put an emphasis on how the standard should be applied in those two different situations.

- (d) Paragraph B19 of IFRS 10 mentions special relationships. It is not clear what examples the IASB was thinking of when setting this guidance.
 - (e) A National Standard Setter noted it is not clear how to determine the relevant activities when different parties have unilateral ability to direct different activities e.g., one party directs the R&D and another the sales activities and the investee has just moved from the R&D phase into marketing of the product; it is also not clear whether the eventual changes in assessment should result in sequential consolidation / deconsolidation of the investee.
 - (f) A National Standard Setter noted it is not clear whether identifying one most relevant activity is appropriate and whether control can be assumed when only one but most-relevant activity out of 3 or 4 others can be directed.
- 2 Some of the above issues, in our constituents' views, could be solved by providing guidance on how to assess the ranking of activities. For instance, in the following scenarios:
- (a) two or more investors control different relevant activities and each of them would need to assess whether they believe their activity most significantly affects the investee's returns;
 - (b) one dominant investor may decide alone on the relevant activities, but the minority investor has significant veto rights that would prevent the dominant investor from deciding on one of the activities - the question is whether this is enough to deny control.
- 3 Constituents note that the concept of "relevant activities" of an investee is not clear. In their view control has to do with the impact an investor has on the long-term business strategy, the investments made, the governance structure and the short and long-term financial strategy and not so much with an impact on relevant activities.

Issue 2.2: Changes occurring over an investee's life

- 4 Members of EFRAG User Network as well as a National Standard Setter note that the control analysis can be complex in case the identification of the relevant activities or their relative weight change during the investee's life.
- 5 For example, some project entities are organised so that each investor has the ability to direct one of the investee's relevant activities but at a different time. In such cases, identifying the activity that has the greatest influence on the returns can be difficult. Additionally, it is unclear as to whether the re-assessment of the controlling party is required when the project's phase changes. This may affect sectors such as the infrastructure operation sector and the pharmaceutical sector.

Issue 2.3: Changes in the relative weight of relevant activities

- 6 Some constituents note that circumstances in which the relative influence of each relevant activity on the investee's returns changes over time also create complexities. For example, an investee has two investors and operates two businesses that cannot be considered as silos. Each investor has the ability to direct one of the investee's businesses. In the future, one of the businesses is expected to have the most significant impact on the investee's returns. In such example, it may be difficult to know whether:
- (a) the analysis of each business' relative weight in the investee's returns is made using the data prevailing at a given date or is based on a long-term projection of the investee's activities.

- (b) it is possible to identify situations of change in control, without any change in governance or contractual arrangements, i.e., based solely on a change in the relative weight of the businesses.

Question 2(b) Control – power over an investee

In your experience:

- (i) to what extent does applying paragraphs B26–B33 of IFRS 10 enable an investor to determine if rights are protective rights?
- (ii) to what extent does applying paragraphs B22–B24 of IFRS 10 enable an investor to determine if rights (including potential voting rights) are, or have ceased to be, substantive?

Overview

Issue nr.	Description
2.4	Determining the moment when control arises
2.5	Determining which rights are protective
2.6	Identification of control when legal requirements prevent a shareholder from exercising its rights
2.7	Additional illustrative examples how to determine control in specific cases

Issue 2.4: Determining the moment when control arises

- 7 Potential voting rights might give control to the holder, but it is unclear how control should be assessed in a relatively long intermediate period before the rights get activated. For example, when the management of a trust needs to approve the right, there will be some time before the voting rights are active. The question raised regards whether this would prevent control or not?
- 8 IFRS 10 requires investors to consider substantive potential voting rights. One of the criteria for such potential voting rights to be substantial is that they are currently exercisable. However, the guidance of paragraph B24 of IFRS 10 leaves room for interpretation.
- 9 Similarly, it is not clear how to assess control in a continuous process of acquiring voting rights by the investor and when, during that process, the control is actually acquired.

Issue 2.5: Determining when rights are protective

- 10 Problems arise with assessment of whether substantive rights are protective only, for instance for business combinations when there is a long period between signing date and closing the contract. In such a long period the initial assessment of which substantive rights are only protective may change over time but it is considered unclear from which point such a change occurs. Constituents, including a National Standard Setter, note it is hard to assess who has the greatest influence on variability when one does not exercise (i.e., remains passive), and the other does not have enough rights (i.e., has not yet the ability to exercise its power) because the acquisition process is still ongoing, and everything is “in progress” i.e., they are in the middle of acquisition process. Similarly, difficulties arise with creating an overview of the options related to rights.
- 11 Generally, EFRAG constituents note that the assessment of whether substantive rights are protective only requires a lot of judgement. For instance, non-franchisors

apply the guidance in paragraph B29-B33 (particularly, paragraph B33) of IFRS 10 to argue that substantive rights are merely protective. A solution could be to provide additional guidance or rephrasing the scope of the guidance to limit its application to franchisors only.

- 12 Furthermore, there was a request to reinforce the use of thresholds, which is often the practice both in arrangements and in entities' accounting policies related to the assessment of control. For example, in a fact pattern where there is one dominating investor, the agreement may require all the investors to make a joint decision on relevant topics, when an activity exceeds a predefined threshold. Depending on the level of the threshold, the assessment may reveal that it gives protective rights only or, when it is lower, that the arrangement is similar to a joint arrangement.
- 13 Finally, constituents note that the definitions and differentiation of the terms substantive/non substantive rights (pertaining to the ability to exercise a right) and participating/protective rights (pertaining to exercising power as opposed to protecting an existing right) is not clear and suggest the IASB to clarify this.

Issue 2.6: Identification of control when legal requirements prevent a shareholder from exercising its rights

- 14 In some jurisdictions, the local legislation makes an explicit reference to control as defined by local Company Act and/or regulatory requirements and these are not necessarily consistent with IFRS 10. Hence, it becomes difficult to assess who has control as the outcome under IFRS 10 may be in contradiction to the assessment under local legislation. The solution of the potential conflict is particularly difficult when the investor does not have majority of voting rights (e.g., more than 20% but less than 50% of voting rights).
- 15 An example of another type of conflict, also reported by a National Standard Setter, arises for subsidiaries operating in a regulated sector in another country where all individuals appointed to the Board of Directors must be selected from a list of local citizens, approved by the local ministry office or government agency, and the parent may be not represented.

Issue 2.7 Additional illustrative examples how to determine control in specific cases

- 16 Some constituents note that the requirements in IFRS 10 generally provide a sufficient basis to assess whether an investor controls an investee, and more particularly whether the investor's rights are substantive and whether the rights held by other parties are protective. These constituents also note that entities have developed practices and internal application guidance that have been approved by auditors and regulators.
- 17 Nevertheless, these constituents think that some additional examples in the IFRS 10 would be useful, in particular to address the following points:
 - (a) cases of vehicles that are largely 'autopiloted' but for which some decisions remain to be made during the operating phase;
 - (b) cases of potential voting rights with exercise windows, depending on whether the window is open or closed at the reporting date (or open at the reporting date but closed when financial statements are authorised for issue);
 - (c) case of potential voting rights, and impact of changes in the fair value of the underlying share to the assessment of control.

Question 2(c) Control – power over an investee

In your experience:

- (i) to what extent does applying paragraphs B41–B46 of IFRS 10 to situations in which the other shareholdings are widely dispersed enable an investor that does not hold a majority of the voting rights to make an appropriate assessment of whether it has acquired (or lost) the practical ability to direct an investee’s relevant activities?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 2(c)(i) arise?
- (iii) is the cost of obtaining the information required to make the assessment significant?

Overview

Issue nr.	Description
2.8	Determining control in crisis situations
2.9	Assessing the role of independent directors
2.10	Golden rights/votes

- 18 Constituents noted that those situations only occasionally occur in practice. In addition, it was pointed out that obtaining the information required to make an assessment may also be burdensome in the case of a listed investee (e.g., if the applicable national law of the subsidiary does not provide the controlling entity with information rights).
- 19 Another constituent noted that it is difficult to assess how frequently an investor needs to make this assessment and what circumstances should/could trigger the assessment.
- 20 Constituents noted that IFRS 10 paragraph B43-B46 does not provide rebuttable assumptions, expressing the level of certainty of control and does not offer relevant examples on how to assess de factor control situations. The examples 4 and 6 are considered to be too obvious. This leads to a lot of inconsistency and uncertainty in the financial reports.
- 21 Constituents noted that there is uncertainty about whether a control assessment should be undertaken based on the relative voting strengths and participation of the investor and other shareholders at each general meeting or whether the key to determining ‘de facto’ control is sustained dominance in the longer term. This seems to be relevant in the funds industry and the insurance sector, especially in relation to holdings in open-ended investment companies (OEICs), the level of which can change with third party redemptions and therefore needs to be monitored continuously to determine whether control (or de facto control) exists or has been lost.

Issue 2.8: Determining control in crisis situations

- 22 In the situation of breach of covenants, liquidation, administration, or receivership, it is complex to assess who controls when both the investor and the bank hold substantive rights. The issues are similar when one of the investors is a venture capital fund or trust.

Issue 2.9: Assessing the role of independent directors

- 23 Some constituents, including a National Standard Setter, note diversity in practice how the role of independent directors is appreciated in the analysis of control:
- (a) Either independent directors are considered as any other director of the board, considering their voting rights and thus, their ability to outvote the investor. In other words, those constituents make an analysis of different elements to identify whether the main shareholder is able to make decisions on the board independently of the other directors (independent or not).
 - (b) Or independent directors as a ‘management constraint’ that acts as a safeguard, and in the interest, of all investors. Independent directors are appointed for their expertise and to give advice based on their competence. Their role is not to contradict decisions made. In the assessment of control, they are considered as having a protective role which, such as protective rights, does not prevent an investor from having control. Therefore, the majority rules on the board are analysed ignoring the independent directors.
- 24 Given this diversity in practice constituents ask the IASB to consider the role of independent directors in more depth.

Issue 2.10: Golden rights/votes

- 25 Difficulties exist in determining when (de-facto) control is gained or lost. In some jurisdictions, former state- or government-owned entities have a so-called golden right/vote to block certain decisions for example strategic investment decisions. In these circumstances the majority voting rights does not necessarily give control, but other facts and circumstances need to be assessed as well. Since control “on the ground” is often not defined by local law or is not aligned with IFRS definition of control, there might be divergence in practice. It would help if IFRS 10 could clarify whether these golden votes could be considered as protective rights only.
- 26 It was noted that golden rights/votes also occur in family-owned business where the golden vote is held by a senior family member.

Question 3(a) Control – the link between power and returns

In your experience:

- (i) to what extent does applying the factors listed in paragraph B60 of IFRS 10 (and the application guidance in paragraphs B62–B72 of IFRS 10) enable an investor to determine whether a decision maker is a principal or an agent?
- (ii) are there situations in which it is challenging to identify an agency relationship? If yes, please describe the challenges that arise in these situations.
- (iii) how frequently do these situations arise?

Overview

Issue nr.	Description
3.1	Lack of definition of returns
3.2	Assessment of power over investee - considering variable returns
3.3	Variability of servicing fees affected by low interest rate environment
3.4	Interaction IFRS 10 and IFRS 15 wrt principals and agents

Issue 3.1: Lack of definition of returns

- 27 In describing whether an investor is entitled to variable returns from its involvement with the investee it is unclear how reimbursables should be considered.

Issue 3.2: Assessment of power over investee – Considering variable returns

Situation A

- 28 Constituents reported that it is not clear how to assess investors exposure to variability of returns, when the investor's holding in subsidiary is less than 50% - for instance 40% with the rest of the shareholding dispersed - and the subsidiary makes an investment in an investee. It seems that the variability of returns affects the group holding less than the NCI at the group level.

Situation B

- 29 A National Standard Setter noted that regarding agency relationship, when the variability of investee's returns is correlated with the level of compensation for the fund manager, it was not clear whether to assess that variability of the compensation is related to the decision-making power or rather because it is a compensation for the management service.

Issue 3.3: Variability of servicing fees affected by low interest rate environment

- 30 In some cases, the level of interest rate for monetary funds had been extremely low. Even if the fee is kept by the fund manager/bank when assessing the variability to the return the fee would contribute to a large retention of the variability. This leads to a conclusion that the fund would have to be consolidated. The current consolidation approach does not represent the business model of banks in their function of providing management services.
- 31 A National Standard Setter noted that financial institutions developed internal guidelines because:
- (a) line by line consolidation of funds could be burdensome and does not represent in their view their business model, as they render only management services, therefore:
 - (b) a fund is considered by the banks as a single investment of the group, so it does not seem useful to show all the fund's assets separately on the banks' balance sheet.
- 32 Consequently, financial institutions consolidate in one line 100% in assets with NCI being a liability (being puttable instruments).

Issue 3.4: Interaction IFRS 10 and IFRS 15 with regard to principal/agent assessment – legal wrapper

- 33 A National Standard Setter noted that clarification is needed as to whether and to what extent the requirements on principal/agent assessment in IFRS 10 interacts with the requirements on principal/agent assessment in IFRS 15. In particular, it is unclear whether 100% of the revenue can be recognised (based on the requirements on principals and agents in IFRS 15), even if the entity concludes that (according to IFRS 10) it does not control an investee. In Media & Entertainment industry, this is highly relevant for film productions, structured in separate legal vehicles. In the context of a film production, not all contracting parties are usually directly involved in the film production, but the contracting parties are often granted extensive decision-making rights.

Question 3(b) Control – the link between power and returns

In your experience:

- (i) to what extent does applying paragraphs B73–B75 of IFRS 10 enable an investor to assess whether control exists because another party is acting as a de facto agent (i.e., in the absence of a contractual arrangement between the parties)?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 3(b)(i) arise?
- (iii) please describe the situations that give rise to such a need.

Overview

Issue nr.	Description
3.5	When does de facto control exist?

Issue 3.5: When does de facto control exist?

- 34 A National Standard Setter noted that the Standard is not clear on whether, a need to have a positive vote of few shareholders to pass decisions (where these shareholders are passive and always agree), prevents the investor from assessing control or, on the contrary, whether it is possible to have the ability to direct the relevant activities without having obtained the majority of the voting rights actually exercised (while other investors are passive). In this sense, the application examples in IFRS 10 may not be useful or are sometimes contradictory.
- 35 Moreover, it is not clear how to account for cases where acquisitions occur over a few reporting periods and where, after the investment date, it was assessed that de-facto control exists. It is not clear under IFRS 10 guidance what acquisition date should be considered.

Question 4(a) Investment entities

In your experience:

- (i) to what extent does applying the definition (paragraph 27 of IFRS 10) and the description of the typical characteristics of an investment entity (paragraph 28 of IFRS 10) lead to consistent outcomes? If you have found that inconsistent outcomes arise, please describe these outcomes, and explain the situations in which they arise.
- (ii) to what extent does the definition and the description of typical characteristics result in classification outcomes that, in your view, fail to represent the nature of the entity in a relevant or faithful manner? For example, do the definition and the description of typical characteristics include entities in (or exclude entities from) the category of investment entities that in your view should be excluded (or included)? Please provide the reasons for your answer.

Overview

Issue nr.	Description
4.1	Definition of investment entities needs further fine-tuning

Issue 4.1: definition of investment entities needs further fine-tuning

- 36 The definition states that an investment entity obtains funds from one or more investors, but it gives the impression that the investment entity starts as of today. However, it is also possible that a large conglomerate decides to develop investment

entity activities as of today without obtaining any funds yet. These subsidiaries also need to be allowed to be fair valued. Therefore, the definition should be further fine-tuned.

- 37 Similarly, a National Standard Setter noted that it is common for non-investment entities to hold interest in investment entities for instance in the banking, insurance, and private equity sectors. The National Standard Setter noted that retaining the investment entity's accounting would result in a more decision- useful accounting treatment on the parent entity level and regardless of whether or not the parent entity was an investment entity. Retaining the investment entity's accounting provides more decision-useful information on the parent entity's level, because the characteristics of the (controlled) investment remain the same. The National Standard Setter suggested revisiting the previous IASB's decision on the requirements for a non-investment entity parent of an investment entity subsidiary.
- 38 Some investment entities consist of departments providing for example corporate finance advice or fiscal advice. Some users consider that it is necessary to consolidate these departments to the extent possible. It is noted that in practice it might be a difficult exercise to separate the investment entity activities from the non-investment entity activities.
- 39 Moreover, one of the constituents raised an issue that some Real Estate investment funds fail to qualify as investment entities. This is in particular when the investor may be involved in the development and management of property (i.e., business purpose in paragraph B85D of IFRS 10). Similarly, evidencing a potential exit strategy (paragraph B85F of IFRS 10) seems challenging for Real Estate funds. This seemed to the constituent to be inconsistent with other investment funds' accounting approach.
- 40 There was an issue raised that, when the investor provides both equity and debt finance, it is not clear in accordance with paragraphs 28(d) and B85V-B86W of IFRS10, what proportions of debt / equity financing would disqualify the investor from investment entity accounting.

Question 4(b) Investment entities

In your experience:

- (i) are there situations in which requiring an investment entity to measure at fair value its investment in a subsidiary that is an investment entity itself results in a loss of information? If so, please provide details of the useful information that is missing and explain why you think that information is useful.
- (ii) are there criteria, other than those in paragraph 32 of IFRS 10, that may be relevant to the scope of application of the consolidation exception for investment entities?

Overview

Issue nr.	Description
4.2	Request for more information on group financing and leveraging, which is lost in fair valuation

Issue 4.2: Request for more information on group financing and leveraging, which is lost in fair valuation

- 41 Constituents have advised EFRAG that:
- (a) Generally, they agree that fair valuation of the investments provides useful information. However, they also raise issues that some information shortfalls

may occur because of the lack of information regarding the financial liabilities that investment entities leverage within a bigger group to fund investments (i.e., in circumstances where an intermediate subsidiary – that is itself an investment entity – holds investments or incurs financial liabilities that are not presented in the parent consolidated financial statement but instead subsumed in the fair value of the subsidiary). One proposed solution is to require disclosure of the nature, terms, and conditions of such transactions.

- (b) A National Standard Setter noted that in their opinion the fair value measurement provides useful information. However, in their opinion the definition and criteria to identify investment entities still requires judgement and thus leave room for some entities to achieve their preferred outcome (to apply or not apply the exemption).
- (c) A National Standard Setter believes the use of fair value is also a valid solution for the group financial statements of a non-investment entity parent of an investment entity. This is particularly relevant for conglomerates that operate an 'investment activity' as a separate business activity through an investment entity subsidiary (e.g., as an operating segment) and is a common issue in the banking, and private equity sector. In practice, investments held by an investment entity subsidiary are managed internally like investments of an investment entity, both at the parent entity level, and the investment entity subsidiary level. In these cases, the business model of the (non-investment) entity parent does not differ from the business model of an investment entity as regards the investment held by its investment entity subsidiary, as the investments are managed on a fair value basis, by both, the parent entity, and the investment entity subsidiary. However, under IFRS 10, the non-investment entity parent needs to unwind the specialised accounting at the investment entity subsidiary, i.e., for the same investment two different sets of financial statements need to be prepared and maintained at the parent and subsidiary level, resulting in burdensome costs of consolidating the investment that is not consolidated on the investment entity-subsidiary level. Further, this leads to non-investment entity parents increasingly using management performance measures in their capital market communication to present their view on the performance of their 'investment activities', as this view is currently not reflected by group financial statements that are prepared in accordance with IFRS.
- (d) A new disclosure may be considered, focusing on significant classes of investments held by intermediate investment entities.
- (e) In some instances, it may be more appropriate to consolidate intermediate holding companies (holding cash or debt that is used to finance the portfolio of companies beneath it) even where they meet the definition of an investment entity, for example, where the intermediate holding company is just a corporate vehicle for holding other investments. In such instances, measuring the intermediate holding company at fair value is unlikely to provide meaningful information.

Question 5(a) Change in the relationship between an investor and an investee

In your experience:

- (i) how frequently do transactions, events or circumstances arise that:
 - (a) alter the relationship between an investor and an investee (for example, a change from being a parent to being a joint operator); and
 - (b) are not addressed in IFRS Standards?

- (ii) how do entities account for these transactions, events or circumstances that alter the relationship between an investor and an investee?
- (iii) in transactions, events or circumstances that result in a loss of control, does remeasuring the retained interest at fair value provide relevant information? If not, please explain why not, and describe the relevant transactions, events, or circumstances.

Overview

Issue nr.	Description
5.1	Change in ownership interest in an investment vehicle results in not useful information presented under IFRS 10
5.2	Transactions involving a joint operation

- 42 The constituents noted that, in 2015, the IFRS Interpretations Committee has discussed the topics related to accounting for transactions that change investor's interest in a business. It is suggested that the IASB investigate the conceptually appropriate accounting for transactions that alter the relationship between an investor and an investee and are not addressed in IFRS Standards and address these issues by a broader consideration of how to account for transactions involving changes of interests in a business.
- 43 Constituents suggested also reviewing the issue regarding the deferral and realisation of accumulated translation differences when control is lost due to a change in control.

Issue 5.1: Change in ownership interest in an investment vehicle results in not useful information presented under IFRS 10

- 44 A preparer notes that when accounting for an investment vehicle it is important for them to see the investment result of that vehicle reflected in consolidated accounts. Yet, when applying IFRS 10, a dilution of their rights in that investment vehicle are accounted for directly in equity, not in profit or loss. This does not allow them to identify their performance, and, in addition, the amounts recognised in equity cannot be recycled.
- 45 The preparer provided an example of a decrease in group's ownership interest, where an insurer creates an investment fund and funds it with 100CU. The fund in turn invests cash in bonds eligible for FVOCI. The following year, an increase in bonds fair value of 20CU is recognised. Following that, 50% of the shares are sold as redeemable participating shares to the clients of the fund for 60CU. Based on the characteristics of the participating shares, it is assessed that the insurer keeps control over the investment fund. The relevant balances in the statement of financial position would be then as follows:

Year N: Creation by A of a fund F with 100 of cash, invested in bonds eligible to FVOCI	Year N + 1: URG 20	Year N + 2: A sells 50% of F to third parties for 60
B/S: Bonds 100 Dr Group equity: 100 Cr	B/S Bonds 120 Dr Group Equity (excl. OCI) 100 Cr Group OCI: 20 Cr	B/S Bonds 120 Dr Cash 60 Dr Group Equity (excl. OCI) 110 Cr Group OCI 10 Cr Debt (puttable instruments) 60 Cr

- 46 It should be noted that the redeemable participating shares, compared to the original founder shares, have different rights, and therefore do not form the most subordinate class together with the founder shares. Consequently, they cannot be recognised as equity, but rather as liability in both financial statements of the fund and consolidated statements of the insurer.
- 47 Consistent with IFRS 10, the preparer states that a change in ownership interest in a controlled entity does not impact consolidated profit or loss; therefore, the realised gain recognised in profit or loss in the statutory accounts is reclassified in retained earnings. To the extent that the objective of investment in controlled investment funds is to optimise the benefits for customers (such as policyholders of insurance companies, for instance through participation in life or lower level of premium in profit or loss), it is not appropriate to apply the general principle of IFRS 10. Instead, it would be relevant to account for the impacts of changes in ownership interests in profit or loss in order to avoid providing not useful information and to have an adequate reflection of the performance in profit or loss.

Issue 5.2: Transactions involving a joint operation

Situation A: Moving from control to joint control

- 48 Some constituents, including a National Standard Setter, note that it is common that an investor contributes a business to a new entity that will be then jointly controlled. If the newly formed joint arrangement is a joint operation as defined in IFRS 11, there is no requirement in IFRS Standards to account for such a transaction.
- 49 Accordingly, entities' management have used their judgement in developing and applying an accounting policy to account for those transactions. The following accounting policies have been identified:
- (a) some entities apply paragraph B98 of IFRS 10 that requires to (i) derecognise all the subsidiary's assets and liabilities and (ii) remeasure any retained interest at fair value, or
 - (b) some entities derecognise only the portion of the assets and liabilities to which the investor has no longer any right (assets) or for which it has no longer any obligation (liability) according to the joint operation contract.
- 50 Those accounting policies may result in materially different outcomes, notably because of the potential impact of remeasurement. Hence, standard-setting is requested to correct these outcomes.

Situation B: moving control to joint control

- 51 A National Standard Setter notes that annual improvements to IFRSs, cycle 2015-2017, have clarified how an entity accounts for its previously held interest when it obtains control of a business that is a joint operation. In those circumstances, an

entity applies the requirements for a business combination achieved in stages in IFRS 3, including remeasuring its previously held interest in the joint operation at fair value.

- 52 Some constituents question the relevance of such remeasurement in a situation in which the investor has already direct rights on the assets and obligations for the liabilities of the joint operation.

Question 5(b) Partial acquisition of a subsidiary that does not constitute a business

In your experience:

- (i) how do entities account for transactions in which an investor acquires control of a subsidiary that does not constitute a business, as defined in IFRS 3? Does the investor recognise a non-controlling interest for equity not attributable to the parent?
- (ii) how frequently do these transactions occur?

Overview

Issue nr.	Description
5.3	Dealing with NCI when acquiring a subsidiary that is no business

- 53 Constituents, including a National Standard Setter, generally agree that IFRS 3/IFRS 10 (and IAS 28) lack guidance on accounting for acquisition of interest in entities that do not constitute a business, and acquisitions of businesses without a corporate wrapper.
- 54 Moreover, some IFRS Standards clearly draw a distinction between the accounting for transactions involving businesses and those involving assets. However, IFRS 10 guidance on loss of control does not distinguish between a subsidiary that is a business or not.

Issue 5.3 Dealing with NCI when acquiring a subsidiary that is no business

- 55 A National Standard Setter considers that transactions in which an investor acquires control of a subsidiary that does not constitute a business will become more common further to the publication, in 2018, of the amendments to IFRS 3 Definition of a business that have in practice extended the scope of entities that do not constitute a business.
- 56 Such transactions are already widespread in the real estate industry where (i) single asset entities are common and (ii) acquisitions are structured through share deals instead of asset deals.
- 57 The constituent observes that the prevailing accounting policy results in the recognition of non-controlling interests (NCI) when a partial acquisition occurs. The asset is accounted for 100% of its value (or cost grossed-up to 100%) and the corresponding NCI are presented in the investor's equity.
- 58 The constituent notes there is inconsistency between IFRS 10 that requires to recognise NCI relating to the pro rata share of the net assets of the subsidiary, irrespective of whether the subsidiary contains a business, and IFRS 3 that does not mention the accounting for non-controlling interests when describing the accounting for an acquisition of an entity that does not constitute a business.
- 59 Hence, they ask the IASB to provide application guidance to confirm that NCI shall be recognised even if the subsidiary is not a business.

Question 5/A Other issues raised by constituents regarding IFRS 10

Overview

Issue nr.	Description
5A.1	Integral and non-integral investments
5A.2	IFRS 10 lacks the overarching principle which would explain the reason for consolidated financial statements
5A.3	Providing a proof that nobody requested to present consolidated financial statements in a sub-group seems challenging
5A.4	Add consolidation exception for bail outs
5/A.5	Concept of control in IFRS 10 vs conceptual framework

Issue 5A.1: Integral and non-integral investments

60 Constituents had mixed views about bringing this notion into the group accounting and whether it should be applied to subsidiaries i.e., a non-integral subsidiary would not need to be consolidated. EFRAG recalls its view on integral and non-integral investments as listed in its comment letter of 2 November 2020. EFRAG noted that the proposed separation between integral and non-integral investments would involve a lot of judgement and therefore asked the IASB to revisit the concept. In case the IASB is to proceed with the concept, EFRAG proposed to address this through the disclosures.

Issue 5A.2: IFRS 10 lacks the overarching principle which would explain the reason for consolidated financial statements

61 IFRS 10 lacks an overarching principle explaining that consolidated financial statements reflect group economic activities as it were one entity; this would solve some recent controversial issues. A National Standard Setter noted that questions raised in the absence of such a principle are (non-exhaustive list):

- (a) Considering how consolidated financial statements defined in Appendix A to IFRS 10, does it relate to solely to presentation?
- (b) How should internal gains be split between the entity and the NCI part of that entity; or
- (c) How should intra-period changes in NCI parts be dealt with?

Issue 5A.3: Providing proof that nobody requested present consolidated financial statements in a sub-group seems challenging

62 The application of paragraph 4(a) (i) of IFRS 10 is difficult to apply in practice as it is challenging in respect to providing an audit trail. It is difficult to prove “no objection” without requiring shareholders to give a positive response and getting a response from all shareholders is not practical.

Issue 5A.4: Add consolidation exception for bail outs

63 A National Standard Setter suggested to introduce a consolidation exemption for so-called "bail out acquisitions" where a bank, in its role as a lender, obtains control over a non-performing borrower. In such cases, the bank's economic interest in the investment is different from that of a (strategic) investor, so that a consolidation exception should be considered by the IASB.

Issue 5A.5: Concept of control in IFRS 10 vs Conceptual Framework

- 64 Constituents, amongst one National Standard Setter, also noted that application of the control principle in: (i) the conceptual framework which focuses on the assets that satisfy the criteria (e.g., control), (ii) IFRS^o10 which requires control over a subsidiary to recognise its assets, (iii) IFRS 11 which focuses on assets resulting from rights and obligations, and (iv) IFRS 15 according to which revenue is recognised when control over a good or a service is transferred to a customer, may overlap or the full spectrum of forms of control may not be covered.

IFRS 11 Joint Arrangements

Question 6 Collaborative arrangements outside the scope of IFRS 11

In your experience:

- (i) how widespread are collaborative arrangements that do not meet the IFRS 11 definition of 'joint arrangement' because the parties to the arrangement do not have joint control? Please provide a description of the features of these collaborative arrangements, including whether they are structured through a separate legal vehicle.
- (ii) how do entities that apply IFRS Standards account for such collaborative arrangements? Is the accounting a faithful representation of the arrangement and why?

Overview

Issue nr.	Description
6.1	Requested guidance on accounting and disclosures for collaborative arrangements

Issue 6.1: Requested guidance on accounting and disclosures for collaborative arrangements

Case A

- 65 Typical fact patterns include (provided by National Standard Setters):
- (a) A business held in a form of an arrangement that is similar to a joint operation but where the decision making represents a form of majority decision and more than one set of investors may constitute a sufficient majority. Clearly the arrangement would not satisfy the criteria in IFRS 11 and would not be classified as jointly controlled. Nevertheless, many other aspects may be similar to typical joint operation arrangements, such as offtake according to ownership share, cost-based price arrangements and no external financing, i.e., equity only or a combination of equity and shareholder loans. An explicit regulation of such arrangements would be helpful. Such arrangements exist in the oil & gas, power & utilities, pharmaceutical, chemical, and biotech industries. This leads to divergence in practice, for example unincorporated arrangements are often accounted similarly to joint operations by analogy. Incorporated arrangements are accounted for as associates under the equity method or similarly to joint operations based on an interpretation that other agreements may nullify the corporate structure and establishes rights and obligations to the underlying assets and liabilities for the owners.
 - (b) Joint operations (e.g., in oil industry, extractive, life sciences), sometimes, are not performed through a legal vehicle but rather through joint ownership (a co-ownership) in the actual assets of the operation (or, in other words, as unincorporated collaborative arrangement). There are rules of majority (or often supermajority) to decide upon how the field (assets) are actually

developed. Participants in such arrangements use IFRS 11 by analogy, following IAS 8's general guidance for electing an appropriate accounting policy.

- 66 Constituents proposed to define a clear principle on recognising rights and obligations and extend it to similar situations which are not in the scope of IFRS^o11. Additionally, when there is one controlling investor, it is not clear how other investors should account for their rights and obligations in the investment.
- 67 Another constituent suggested that IFRS Standards should require an investor to account for its investment in an investee applying paragraphs 20–22 of IFRS 11 whenever it has rights to the assets and obligations for the liabilities of that investee, irrespective of whether the investee is jointly controlled. In other words, IFRS Standards should primarily reflect the investor's rights and obligations.

Case B

- 68 When an arrangement without a corporate wrapper is outside the scope of IFRS 11, there may be divergence in practice:
- (a) Some consider IFRS 11 and then be redirected to account for specific assets and liabilities with IFRS 11 disclosures;
 - (b) Some account for individual assets and liabilities as there is no other guidance;
 - (c) Some in the extractive industry (oil and gas) consider they acquire a business (even if without a wrapper) rather than just a purchase of assets, and they initially apply IFRS 3 for recognition and then account under IFRS 11;
 - (d) Some are unclear whether acquiring a share of a business without a corporate wrapper but with significant influence should be equity accounted.

Question 7 Classifying joint arrangements

In your experience:

- (i) how frequently does a party to a joint arrangement need to consider other facts and circumstances to determine the classification of the joint arrangement after having considered the legal form and the contractual arrangement?
- (ii) to what extent does applying paragraphs B29–B32 of IFRS 11 enable an investor to determine the classification of a joint arrangement based on 'other facts and circumstances'? Are there other factors that may be relevant to the classification that are not included in paragraphs B29–B32 of IFRS 11?

Overview

- 69 No specific issue regarding the application of the guidance has been reported. However, some EFRAG constituents reported that there was a visible shift into classifying joint arrangements with corporate wrappers as joint ventures i.e., into equity accounting.
- 70 In some jurisdictions, constituents report joint arrangements with corporate wrappers classified as joint operations to be uncommon. In these jurisdictions, only joint arrangements that are intended to deliver the entire production to its venturers could qualify. Following the agenda decision of IFRS Interpretations Committee decision in March 2015, these constituents – including a National Standard Setter - consider the scope of joint arrangement accounting to be too narrow and suggest the IASB to reconsider the classification criteria to broaden the population of such arrangements.
- 71 The requirements for qualifying as a joint operation are extremely onerous. In many countries there are regulatory boundaries, tax boundaries or similar that makes

structuring of joint operations extremely costly, complex, and sometimes even impossible. It would be highly appreciated if this standard could be reconsidered based on a more practical approach.

- 72 One respondent preferred an approach similar to assessing whether a contract is or contains a lease at inception under IFRS 16. Any reassessment should only be performed if the terms and conditions change. Since minor changes in facts and circumstances can lead to different conclusions due to significant judgment involved, the proposed alternative would lead to better and consistent information for users.

Question 8 Accounting requirements for joint operations

In your experience:

- (i) to what extent does applying the requirements in IFRS 11 enable a joint operator to report its assets, liabilities, revenue, and expenses in a relevant and faithful manner?
- (ii) are there situations in which a joint operator cannot so report? If so, please describe these situations and explain why the report fails to constitute a relevant and faithful representation of the joint operator's assets, liabilities, revenue, and expenses.

Overview

Issue nr.	Description
8.1	Joint operation accounting in separate financial statements
8.2	Arrangements similar to joint operations
8.3	A re-iterated request to reconsider proportional consolidation
8.4	Relation IFRS 11 and IFRS 8
8.5	Other accounting requirements

Issue 8.1: Joint operation accounting in separate financial statements

- 73 According to IFRS 11 interests in joint operations are accounted for in the separate financial statements of the joint operator as in its consolidated financial statements. Some consider that joint operations with corporate wrappers should be treated in the same way as investments in subsidiaries and JVs. They are not convinced that the accounting model of IFRS 11 gives useful information to users of the separate financial statements, because the separate financial statements of the joint operator include assets, liabilities, revenues, and expenses of another legal entity. Moreover, they think that the information provided in the separate financial statements would not be useful to users as it will be a duplication of the information already reported in the consolidated financial statements and for them this seems to be inconsistent with BC 10 of IFRS 10. They also believe that the provisions of IFRS 11 are inconsistent with IAS 27. Indeed, the assets of a jointly controlled entity are recognised in the separate financial statements of the joint operator, while the assets of a subsidiaries are recognised as an investment in the separate financial statements of the parent. The outcome seems counter-intuitive, considering that the stronger is the control, the weaker is the representation.
- 74 Consequently, they note that IAS 27 should be amended so that joint operations are recognised as investments in separate financial statements in the same way for example as joint ventures.

Issue 8.2: Arrangements similar to joint operations

- 75 Does the accounting for arrangements that are similar to joint operations but where the decision making in the arrangement represent a form of majority decision where more than one constellation may constitute a majority, i.e., the arrangement is not jointly controlled. Many other aspects may be similar to typical joint operation arrangements, such as offtake according to ownership share, cost-based price arrangements and no external financing, i.e., equity only or a combination of equity and shareholder loans. An explicit regulation of such arrangements would be helpful. Such arrangements exist both in the oil and gas industry and in some other industries.
- 76 The joint operations in the oil industry are not performed in a legal vehicle. It is a joint ownership (co-ownership) into the actual assets of the operation, but for which there nevertheless are rules of majority (or more often supermajority) to decide upon how the field is developed. Participants in such arrangements therefore use IFRS 11 by analogy following IAS 8's general guidance for selecting an appropriate accounting policy.
- 77 In the off-take agreements, that are common in both hydropower, wind farms and oil and gas, the owner only provides cash as necessary for OPEX. If such operations are within a separate legal vehicle, some want to impair the assets in the financial statements of such vehicles, as the assets do not produce enough cash to support their valuation. It is noted that off-take agreements are prevalent in IFRS 11 situations, but for the entity under joint ownership, and it may be more of an issue for IAS 36.

Issue 8.3: A re-iterated request to reconsider proportional consolidation

- 78 Some constituents (one National Standard Setter amongst them) noted that the removal of the option to proportionally consolidate has been one the most important changes introduced by IFRS 11. They consider that the change resulted in loss of relevant information.
- (a) For example, in the automotive industry and in some jurisdictions, the investments can only be handled through joint ventures. Consequently, in their opinion, the elimination of the proportional consolidation resulted in the revenues, investment's assets, and liabilities, not being reported by the investors. These constituents suggest the IASB to seek feedback on the consequences of applying the equity method to all joint ventures.
- (b) Some entities have developed non-GAAP measures that include revenue, expenses, assets, and liabilities from their joint ventures on a proportionate basis. They disclose—or used to disclose—that information either within their segment reporting or outside their financial statements. A National Standard Setter is of the view thinks the persistence of non-GAAP measures to circumvent the effects of an accounting standard indicates that the Standard may not provide useful information.
- (c) Entities account for joint operations in a manner similar to proportionate consolidation. Nonetheless, few joint arrangements are not structured through a separate vehicle in certain jurisdictions. When those arrangements are structured through a separate vehicle, the investor never (or very seldom) has rights to the assets and obligations for the liabilities of the vehicle. No legal form has been identified for the separate vehicle that would give such rights and obligations to the investor. Nor have contractual arrangements been identified that would override the consequences of the vehicle's legal form. Therefore, whenever an investor concludes it has an interest in a joint operation, it does so on the basis of the 'other facts and circumstances' as described in paragraphs B29-B32 of in IFRS 11 - in those circumstances, joint operations are necessarily production entities, the output of which is bought

by the investors under a take or pay contract. Hence, in the National Standard Setters' view, the scope of joint operations is not properly defined to compensate the consequences of proportionate consolidation's removal on the presentation of an entity's financial performance.

- 79 Moreover, the EFRAG Secretariat's desktop research revealed that some companies, in their directors' or management reports, present performance measures or investment ratios based on proportionally consolidated joint arrangements financial information (at the request from investors). These practices seem to be applied in Real Estate (as shopping malls are often packaged as joint ventures so that different companies share the investment risk), and other industries. During an interview, the preparers explained that they follow industry practice which has been established based on investors' demands to present the group's share in joint venture's performance and the liabilities that the group could be held accountable for. Moreover, the preparers explained that loan-to-value ratios are assessed to provide a more reliable picture when the proportionally consolidated financial information of joint ventures is incorporated into the calculation.
- 80 Constituents provided their views that proportional consolidation could:
- (a) better portray the coverage of fixed obligations,
 - (b) reduce the level of forecasting errors for analysts.

Issue 8.4: Interaction of IFRS 11 and IFRS 8

- 81 Members of EFRAG's User network¹ noted that proportional consolidation may be reflected in segment reporting; however, it was noted that IFRS 8 does not require reconciliation of segments and therefore the explanation of inconsistencies is not provided.

Issue 8.5: Other accounting requirements

- 82 Constituents raised their concerns that IFRS 11 is not clear on the following specific accounting aspects of joint operations;
- (a) The right to the outputs differs from the interest held in the separate vehicle.
 - (b) There is a difference between the right to the output and the actual allocation of the output.
 - (c) The right to the output changes throughout the life of joint operation.
- 83 They noted that despite of the IFRS Interpretations Committee agenda decisions, these aspects still seem to be challenging for preparers.

¹ EFRAG User network are the members of the EFRAG User Panel and other constituents that participated to the outreach process from the users category.

IFRS 12 Disclosure of Interests in Other Entities

Question 9 Disclosure of Interests in Other Entities

In your experience:

- (i) to what extent do the IFRS 12 disclosure requirements assist an entity to meet the objective of IFRS 12, especially the new requirements introduced by IFRS 12 (for example the requirements for summarised information for each material joint venture or associate)?
- (ii) do the IFRS 12 disclosure requirements help an entity determine the level of detail necessary to satisfy the objective of IFRS 12 so that useful information is not obscured by either the inclusion of a large amount of detail or the aggregation of items that have different characteristics?
- (iii) what additional information that is not required by IFRS 12, if any, would be useful to meet the objective of IFRS 12? If there is such information, why and how would it be used? Please provide suggestions on how such information could be disclosed.
- (iv) does IFRS 12 require information to be provided that is not useful to meet the objective of IFRS 12? If yes, please specify the information that you consider unnecessary, why it is unnecessary and what requirements in IFRS 12 give rise to the provision of this information.

Overview

Issue nr.	Description
9.1	No information on the NCI effects on the group as a whole
9.2	Information needed on revenues, cash flows, assets, liabilities, and other performance measures split per particular NCI
9.3	Cash flow statements do not present information split between the majority owned and NCI
9.4	Proportionate EBITDA - as a good example of voluntary disclosure to present information on NCI
9.5	Request for disclosures on unconsolidated structured entities
9.6	The factors used and their weight for judgments needed to classify an investment as a subsidiary, associate, or joint venture
9.7	Economic compulsion
9.8	Risks and cash flows at a more granular level
9.9	Disclosure of information when public entities have different end of year dates
9.10	Assessment of power over investee in de-facto control

84 Preparers generally consider the requirements of IFRS 12 as providing useful and sufficient information.

Issue 9.1: No information on the NCI effects on the group as a whole

85 Members of EFRAG's User network noted IFRS 12 only requires information per individual joint arrangements and investors would be interested in receiving

aggregated information on the effect of NCIs on the group as a whole (incorporating the real degree of ownership of the subsidiaries especially on net income and book equity);

- 86 Even where NCI is just a small number, it may hide a massive impact. The book equity might be small, but what is behind (e.g., liabilities) may be material.
- 87 Constituents noted the information with regard to the “group” could be disclosed in one specific place: subsidiaries, associates, joint arrangements, other structured entities.
- 88 Also, changes should be disclosed, especially when interests in subsidiaries are bought or sold without losing control. These transactions, which often have an impact on the financial structure and the cash flows going forward, are important to assess the direction in which the group is evolving.

Issue 9.2: Information needed on revenues, cash flows, assets, liabilities, and other performance measures split per individual NCI

- 89 Members of EFRAG’s User network called for additional information on material NCIs and their proportionate share of profits and cash flows and sought:
- (a) information on the composition of NCIs (such as, to which subsidiaries an NCI relates);
 - (b) information on the proportionate share of operating cash flows associated with material NCIs; and
 - (c) more detailed information on the assets and liabilities held by subsidiaries with material NCIs, as well as associates and joint ventures.
- 90 Users also called for more information on restrictions on paying dividends, dividend traps, the tax consequences of distributions and subordination of debt in subsidiaries.
- 91 Some consider that the problem with full consolidation is that it assumes that all subsidiaries were 100% owned, which does not represent economic reality and investors typically want information that reflects economic reality rather than legal reality. Ideally, profit or loss, balance sheet, and cash flows would be presented based on economic reality, and IFRS 12 should at least disclose the economic reality of revenues (i.e., considering the investor’s share in the investee’s capital.
- 92 In constituents’ view, there are only two-line items in the entire financial statement that provided economic reality, which are net income and book equity. Companies tended to be valued on cash flows rather than book equity, but the cash flows are 100% consolidated, so investors have to decide how much the NCI was worth and there was no reasonable basis in any annual report to reach a fair value for NCI.
- 93 According to the same constituents, when investors value businesses, they value 100% of all the controlled operations, so what is being valued is narrowly defined and represents the enterprise value, which in the market considers the market cap, debt, and pension deficit. The hardest elements to value are deducting the value of the associates and adding the value of non-controlling interests and if the observed enterprise value is higher than the calculated enterprise value the equity should be sold. The data in the financial statement makes it almost impossible to value equities and NCIs in a reliable manner, as there is insufficient data around the balance sheet structure and the P&L structure. It makes a difference depending on the industry, but the guesswork would have to be very material for some businesses, which increased uncertainty when valuing equity.

Issue 9.3: Cash flow statements do not present information split between the majority owned and NCI

- 94 Members of EFRAG's User network noted the cash flow statement was the only area where there was no NCI and, therefore, the cash flow statement could be very misleading if there was no separation between majority owned entities and NCIs. Users are requesting a solution for this [not further specified].

Issue 9.4: Proportionate EBITDA - as a good example of voluntary disclosure to present information on NCI

- 95 Members of EFRAG's User network wanted proportional representation of EBITDA. It was observed that it would solve the problem of the cash flow statement being 100% consolidated.

Issue 9.5: Request for disclosures on unconsolidated structured entities

- 96 Members of EFRAG's User Network noted that entities may experience difficulties:
- (a) applying the definition of structured entities and identifying unconsolidated structured entities; or
 - (b) obtaining timely information needed to provide the disclosure required.
- 97 The resulting outcome being that some users note a lack of information [not further specified] and there is difficulty in determining information that is individually material.

Issue 9.6: The factors used and their weight for judgements needed to classify an investment as a subsidiary, associate, or joint venture

- 98 Members of EFRAG's User Network are not satisfied in practice about the information provided by IFRS 12. Examples:
- (a) an entity that lists its investments in subsidiaries, associates, and joint ventures, but it is unclear what these consist of and no information on the shares held.
 - (b) a disclosure table where transactions with minority shareholders are presented. However, this also means that since other companies are not providing the same table, this information becomes less useful.
 - (c) an entity listed subsidiaries where a stake of 50% is held and which are consolidated while a list with joint ventures also shows a stake of 50%. The entity did not explain their consideration to account for one as a subsidiary and for the other as a joint venture. It was expected that companies will probably argue that the investments are not material and therefore will not impact the decisions of users, but nonetheless it does not meet the objective of IFRS 12.
- 99 Therefore, it was noted that IFRS 12 currently does not allow users to assess the nature of and risks associated with its interests in other entities and the effect of those interests on its financial position, financial performance, and cash flows, as it is not applied properly in practice.
- 100 So, where judgment is required to classify an investment as a subsidiary, associate, or joint venture, it is important to provide information not only about the result of the assessment, but also what factors were considered, and how those factors were weighted in undertaking the assessment.

Issue 9.7: Economic compulsion

- 101 Members of EFRAG User Network noted that control is not binary but rather a spectrum. Especially in Pharma industry assets are often shared in various forms where sometimes the control assessment is easy but often it is not as casting votes

or certain penalties can be applicable. It was added that next to the formal contractual term where senior and junior stakeholders are visible, there is also economic compulsion if for example a junior stakeholder has a put option which might be a strong tool to put pressure on the company when the senior stakeholder has balance sheet issues. Therefore, the prescribed accounting for situations where control is available or not is a simplified approach as the applicable contracts and situation in reality can be much more complex.

102 As a result, users requested more information regarding economic compulsion.

Issue 9.8: risks and cash flows at a more granular level

Situation A

103 Members of EFRAG's User network noted that with the Primary Financial Statement project, the IASB is working on requiring more granular information for users to understand the operations of an entity, their margin structure, cost structure, etcetera. This all works when entities are 100% owned but as soon as it relates to for example joint ventures it will be distorted, and a lot of information gets lost.

104 When one needs to analyse a joint venture, information from different sources is needed for the modelling. For example, the annual report might tell the stake in a joint venture, however if you want to project future developments you may need to go back to the initial press release when the joint venture was formed. Or information on the profitability of a joint venture might be coming from your knowledge of the industry. In addition, information might be presented during a capital market day or Q&A session with analysts where the company representative might explain that the profitability is deviating from the market average due to certain reasons. Obviously, if a company is not followed closely that information will not be captured. Therefore, modelling joint ventures can be very challenging.

105 There was a strong request for more information on risks and cash flows at a more granular level, as that is critical to an investor's analysis.

106 Some users asked for additional disclosures about:

- (a) The split on non-controlling interest by operating segment;
- (b) The amount of cash and cash equivalent held in such subsidiaries: paragraph B13(a) of IFRS 12 requires disclosing the amount of cash and cash equivalent for each joint venture that is significant to the entity but does not require the same for subsidiaries with significant noncontrolling interests. Constituents believe that such information would be useful, because if dividend distribution is the normal way to transfer cash from a group entity to the other, any such distribution will be allocated on a pro rata basis to non-controlling interests. Therefore, part of the cash on the balance sheet is not really available for the group, and that information should be disclosed.

Situation B

107 The issue raised was with disclosing cash and gross debt instead of assets and liabilities figures.

108 Moreover, in disclosures an aggregated figure of all types of investments may be found and it was hard to evaluate individually. Other requests on granularity: what were the entities, what was the strategic aim and how was shareholder value going to be delivered to the owners of the ultimate company that was reporting; this was impossible to assess from the current numbers.

Issue 9.9: Publishing information by investor before investee's publication date.

109 Members of EFRAG's User network noted that IFRS 12 guidance creates issues when an investor is required to disclose the summarised financial information of its JV, that is a public entity, before this JV publishes the official financial statements

itself. Members suggested to consider an exemption relief applicable to such situations that would allow groups not to publish sensitive information.

- 110 Some members proposed an alternative to align financial years of these entities. However, in more complex situations, aligning the financial year of all the investors and the investee, could be not possible.

Issue 9.10: Assessment of power over investee in de-facto control

- 111 Members of EFRAG's User Network noted that in assessing power over an investee, it is very important to understand whether a company has a de-facto veto right to block decisions that can have a potential negative impact on the company or has the power to force decisions. Especially in the pharmaceutical industry, assets are often shared in various forms where sometimes the control assessment is easy but often it is not as casting votes or certain penalties can be applicable. These situations can be very complex, and the guidance provided is over simplified. For investors it is important to understand the management's thinking in more detail to understand why capital is deployed and why in this or that way.
- 112 Similarly, constituents suggested additional clarification that allows investors to explain better the way their group is structured.
- 113 This was also in line with the view that entities often have to use significant judgement when applying IFRS 10 and IFRS 11. Paragraphs 7-9 of IFRS 12 require entities to disclose significant judgements and assumptions made in applying these standards. Constituents suggested re-emphasising the importance of these disclosures and the role they play in enabling users to understand the impact of interests in other entities on the financial statements.

Other topics – Cross-cutting issues

Question 10 Other topics

Are there topics not addressed in this Request for Information, including those arising from the interaction of IFRS 10 and IFRS 11 and other IFRS Standards, that you consider to be relevant to this Post-implementation Review? If so, please explain the topic and why you think it should be addressed in the Post-implementation Review.

Overview

Issue nr.	Description
10.1	IFRS 5 Discontinued Operations
10.2	IFRS 16 Leases / IFRS 11
10.3	IAS 27 and IAS 28 should be included in the PIR
10.4	IFRS 10 vs IFRS 15 – corporate wrappers
10.5	Assessment of power over investee - Variable returns
10.6	Accounting for NCI resulting from written put options or forward
10.7	Accounting for contingent consideration

Issue 10.1: IFRS 5 Discontinued Operations

- 114 Constituents raise an issue that when a previously fully consolidated entity becomes a discontinued operation or an associate, for users it is difficult to assess the group accounts. Moreover, groups are continuously reviewing their structure and

operations and therefore entities/operations are bouncing around the group, disposed, restructured etc.

- 115 One example relates to two companies that performed an asset swap. The operation was classified as a discontinued operation and by the time the asset swap was finalised, there was not much information given to users besides a profit number.
- 116 Another example relates to a company that planned to exit a certain operation, but it became clear that due to the complexity of the transaction the divestment would take years and needed to be done in stages. The discontinued operation however was accounted for as such very shortly as after selling the next tranche the investment became an associate.
- 117 Some analysts restate their models for these accounting movements, and some do not. It is not easy for the investors to figure out what activities are included in which line items when such movements or changes occur.
- 118 Furthermore, despite the general agreement that in case of loss of control, the retained interest is remeasured at fair value and that this is relevant information for users at that particular time, in some cases entities present the capital gain as a recurring profit when this is not the case. Hence, constituents would support recognising this so-called capital gain in other comprehensive income.

Issue 10.2: IFRS 16 Leases / IFRS 11

- 119 Neither IFRS 11 nor IFRS 16 provide specific guidance on accounting for leases in context of joint operations. It may affect presenting information by operators on leased field assets in extractive industries (e.g., oilfields).
- 120 In March 2019, the IFRS IC published an agenda decision addressing the recognition of lease liabilities by a joint operator when the lease relates to a joint operator's interest in a joint operation. Despite of the agenda decision of the IFRS IC, EFRAG constituents, including a National Standard Setter, still raise issues related to applying IFRS 16 *Leases* guidance to joint operations. We heard that:
 - (a) there were issues with IFRS 16 where the lead operator was asked to present the full liability of a lease as if it was for own use;
 - (b) the recent discussion at IFRS IC on IFRS 16 and IFRS 11 only dealt with the liability and not with the asset side of the lease and, therefore, there were issues on the way to portray some activities.

Issue 10.3: IAS 27 and IAS 28 should be included in the PIR

- 121 EFRAG's constituents noted that IAS 27 and IAS 28 should be included in the PIR, because of the close links between the Standards.
- 122 For instance, application of paragraph B98(c) of IFRS 10 to an acquisition of associate following the deconsolidation of subsidiary seems not to be consistent with IAS 28 guidance which require capitalisation of incidental acquisition costs.
- 123 Another example is a sale or contribution of subsidiary (or group of assets) between an investor and its associate or joint venture (IFRS 10 and IAS 28).
- 124 Moreover, one National Standard Setter noted IAS 28 is lacking guidance on the application of the equity method, with regard to:
 - (a) the elimination of intercompany gains and losses,
 - (b) the elimination of intercompany gains and loss, in the event of changes in the relationship between an investor and an investee, and

- (c) the realisation of gains/loss in transactions involving the transfer or contribution of a subsidiary to a joint venture that is accounted for using the equity method (interaction of IFRS 10 and IAS 28).

125 In practice, these application issues can often only be answered using second-level guidance (such as accounting literature), such as through the IASB's project on equity accounting.

Issue 10.4: IFRS 10 vs IFRS 15 – corporate wrappers

126 One National Standard Setter noted that in situations where there is a sale of a single asset entity (i.e., assets in corporate wrappers) – there is insufficient guidance whether to account for sale (revenue) of the asset or rather sale of entity (disposal of a subsidiary).

Issue 10.5: Assessment of power over investee - Variable returns

Situation A

127 The lack of specific guidance on cases when an investor obtains control over an entity based on a business combination that does not provide for any consideration to be paid. In such cases, it is not clear how to exercise the variable return assessment for the investor in such specific cases, and how to apply specific requirements in IFRS 3:

- (a) IFRS 3 paragraph 43.c) and IFRS 3 paragraph B5 – business is combined by contract only, no consideration given;
- (b) IFRS 3 paragraph 44: 100% net assets' fair value is allocated to non-controlling interest – it is not clear whether it provides useful information at group level;
- (c) How to account for goodwill (if any) - full goodwill, proportionate goodwill?

128 Consequently, EFRAG constituents considered that it is unclear whether, in assessment of control and identification of variable returns, the non-controlling interests should be considered as part of the returns. Or should the investor consider the "variable returns that are not directly received from an investee" only? Or both?

Issue 10.6: Accounting for NCI resulting from written put options or forward

Written put options

129 One National Standard Setter noted that generally, there is no consensus whether the groups should account for written options to issues entity's own equity instruments under IFRS 9 *Financial Instruments* or under IFRS 10.

Forwards

130 Accounting for non-controlling interests when forwards exist, shows frequent divergencies in practice, as also noted by a National Standard Setter.

131 In addition, divergent accounting is reported for forward transactions on the acquisition of:

- (a) subsidiaries; and
- (b) associates

132 It was considered that IAS 32 provides guidance to distinguish between equity and liabilities. A National Standard Setter noted IFRS 9, paragraph 2.2(f) excludes any forward contracts between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination (within the scope of IFRS 3) at a future acquisition date (provided that the term of the forward contract does not

exceed a reasonable period of time, which is normally necessary to obtain any required approvals and to complete the transaction). By contrast, forward contracts on associates are not excluded from the scope of IFRS 9 (ref IFRS 9 paragraph BC22.42). These forward contracts on associates are therefore to be measured at fair value (through profit or loss) in accordance with IFRS 9.

- 133 EFRAG secretariat is aware that this issue is within the scope of the FICE project. However, EFRAG secretariat also notes the FICE project does not appear to be addressing this issue.

Issue 10.7: Accounting for contingent consideration

- 134 A National Standard Setter noted it is considered unclear whether a contingent payment is to be considered as a contingent consideration or as a separate transaction (i.e., arrangements for contingent payments to employees or selling shareholders according to IFRS 3 paragraph B55). Similarly, unclarity exists as to the presentation of an arrangement for contingent payments that (in accordance with IFRS 3 paragraph B55) is not a contingent consideration.