Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

DRSC

DRSC e. V. • Joachimsthaler Str. 34 • 10719 Berlin

Jean-Paul Gauzès
EFRAG Board President
35 Square de Meeûs
B-1000 Brussels

IFRS Technical Committee
Phone: +49 (0)30 206412-12
E-Mail: info@drsc.de

Berlin, 10 May 2021

Dear Jean-Paul,

IASB 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*

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to contribute to EFRAG's response 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* (herein referred to as the 'RfI') by providing in advance our feedback vis-à-vis the IASB.

Please find attached our comment letter to the IASB, containing our detailed comments on the questions raised in the RfI.

If you would like to discuss our comments further, please do not hesitate to contact Ilka Canitz (canitz@drsc.de) or me.

Yours sincerely,

Sven Morich

Vice President

DRSC e. V. • Joachimsthaler Str. 34 • D-10719 Berlin

IFRS Technical Committee
Phone: +49 (0)30 206412-12
E-Mail: info@drsc.de

Mr Hans Hoogervorst
Chairman of the
International Accounting Standards Board
Columbus Building
7 Westferry Circus / Canary Wharf
London E14 4HD

Berlin, 10 May 2021

Dear Hans,

IASB 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*

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to provide our views regarding the IASB 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* (herein referred to as the 'RfI'). We appreciate the opportunity to comment on the RfI.

Overall, and consistent with the feedback we have received from our constituency, we believe that IFRS 10 provides a robust set of principles and requirements that enable an investor to determine whether it controls an investee. We acknowledge that in some situations, assessing whether an investor controls an investee can be challenging in practice and requires significant judgement. However, we believe that most of the application issues encountered in practice are due to the complexity of contractual arrangements and are not caused by any fundamental deficiencies in the principles and requirements of IFRS 10. Therefore, we do not believe that comprehensive amendments to IFRS 10 regarding the definition of control are necessary.

Further, although the initial application of IFRS 11 proved challenging in practice (e.g., regarding the classification of joint arrangements), we observe that solutions have been developed for these issues within our jurisdiction.

Notwithstanding our general statement that we believe that IFRS 10 and IFRS 11 are working effectively in general, we observe that in practice some application issues persist for which – although these issues have been discussed intensively by the IASB – IFRS Standards still lack guidance. These issues primarily relate to how the scopes of IFRS 10 and IFRS 11 interact with other IFRS Standards, such as:

- accounting for put/call options on non-controlling interests (IFRS 10, IAS 32, and IFRS 9),
- the sale or contribution of a subsidiary (or a group of assets) between an investor and its associate or joint venture (IFRS 10 and IAS 28),
- whether the legal form of a transaction (e.g., the sale of an equity interest in a single-asset entity rather than a direct sale of the asset within that entity) should result in any difference in accounting for the transaction, and
- the accounting from the perspective of an agent (IFRS 10 and IAS 28), i.e., how do the requirements on '*principals and agents*' in IFRS 10 interact with IAS 28.

As explained in more detail below, we believe that these cross-cutting issues should be addressed by the IASB through standard setting. Please refer to our answers to question 3(a), 5(b) and 10 below.

Further, we recommend the IASB develop (principle-based) guidance on the accounting for (all possible) transactions that alter the relationship between an investor and an investee (as addressed by the IASB in question 5(a) of the RfI); regardless of whether (or not) these transactions occur frequently. We note that IFRS Standards still lack guidance for a number of transactions, as evidenced by several IFRS IC submissions, and many of these transactions involve changes in interests in joint operations.

Regarding the current disclosure requirements according to IFRS 12 (as well as the request expressed by some stakeholders for additional disclosures), we have received feedback from preparers from our constituency that current disclosure requirements are already very extensive and that there is no evidence from capital market communications with investors that '*too little*' information is disclosed on interests in other entities. We, therefore, recommend that the IASB further investigate the cost-benefit profile of its requirements to disclose information on interests in other entities.

Our responses to the complete set of questions raised in the invitation to comment are laid out in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Ilka Canitz (canitz@drsc.de) or me.

Yours sincerely,

Sven Morich

Vice President

Appendix – Answers to the questions in the RfI

Question 1 – Your background
To understand whether groups of stakeholders share similar views, the Board would like to know: (a) your principal role in relation to financial reporting. Are you a user or a preparer of financial statements, an auditor, a regulator, a standard-setter or an academic? Do you represent a professional accounting body? If you are a user of financial statements, what kind of user are you, for example, are you a buy-side analyst, sell-side analyst, credit rating analyst, creditor or lender, or asset or portfolio manager? (b) your principal jurisdiction and industry. For example, if you are a user of financial statements, which regions do you follow or invest in? Please state whether your responses to questions 2–10 are unrelated to your principal jurisdiction or industry

The Accounting Standards Committee of Germany (ASCG) is the national standard setter in the area of group financial reporting in Germany.

The views expressed in this comment letter are based on our experience with the application of IFRS 10, IFRS 11 and IFRS 12 in Germany and also reflect our consultation of German constituents on the IASB's RfI.

Question 2(a) – Power over an investee – Relevant activities
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?

As already explained in our cover letter, we believe that IFRS 10 provides a robust set of principles and requirements that enable an entity to determine whether it controls an investee. Therefore, we do not believe that comprehensive amendments to IFRS 10 regarding the definition of control are necessary.

Regarding the assessment whether an investor is able to direct the activities that most significantly affect the investee's returns, it was brought to our attention that changes in the relevant activities are pre-determined in some collaboration agreements, i.e., when different relevant activities take place at different times or stages during a collaboration arrangement, and the parties to that agreement have different decision-making rights depending on the stage of the collaboration. As a result, a pre-determined change in the relevant activities can also alter the nature of an investor-investee-relationship to a joint arrangement (and vice versa). This applies, for example, to situations in the energy sector, when two or more investors form an investee to (jointly) construct and operate, for example, a wind farm, and:

- during the construction phase, both investors jointly control the investee, e.g., as decision-making rights require the unanimous consent of both investors, and
- after commissioning, during the operational phase, one investor has rights that give him the unilateral ability to direct the relevant activities.

However, the requirements on the (continuous) assessment of the relevant activities appear to focus on an event that changes an investor's rights to direct the relevant activities. Therefore, when reviewing the requirements, the IASB might also want to consider (pre-determined) changes in the relevant activities of an investee, especially in the case of different relevant activities taking place at different times or stages during a collaboration arrangement.

Question 2(b) – Power over an investee – Rights that give an investor power
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?

As already explained in our cover letter, we believe that IFRS 10 provides a robust set of principles and requirements that enable an entity to determine whether it controls an investee. Therefore, we do not believe that comprehensive amendments to IFRS 10 regarding the definition of control are necessary. Instead, we believe that the IASB should address issues related to how the scope of IFRS 10 interacts with other IFRS Standards ('*cross-cutting issues*').

Question 2(c) – Power over an investee – Control without a majority of the voting rights

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?

In our opinion and according to the feedback we have received from our constituency, situations occasionally arise in practice in which an investor with less than a majority of the voting rights controls an investee, as it has the practical ability to direct the investee's relevant activities because of the size of the investor's voting rights relative to the size and dispersion of other shareholdings. In the event that an entity needs to assess whether it controls an investee without a majority of the voting rights, the assessment often requires significant judgement and is subject to discussions.

As regards to the cost of obtaining the information required to make the assessment on a continuous basis, it should be noted that:

- in the case of a listed investee, the information (e.g., attendance at the annual general meeting and voting behaviour) can usually be obtained easily; however, in some cases this may be more complex (e.g., if the applicable national law of the subsidiary does not provide the controlling entity with information rights),
- in the case of an unlisted investee, obtaining the information necessary for the assessment and continuous monitoring is more complex but manageable.

Therefore, we believe that the costs of obtaining the information required to make the assessment are not significant compared to other costs of preparing IFRS financial statements.

Given that costs of obtaining the information required to make the assessment are not significant, we believe that the existing requirements of IFRS 10 on control without a majority of voting rights do not need to be revised (and, in particular, they do not need to be simplified by introducing a minimum level of voting rights needed for control, as some stakeholders have requested).

Instead, we agree with the IASB's statement that requirements based on quantitative thresholds should be avoided (ref. paragraph 19 in the RfI). Quantitative thresholds would, in our opinion, lead to an increase in entities' leeway regarding the assessment of control and, thus, could permit structuring opportunities. Instead, IFRS 10 should continue to provide principle-based requirements. As the IASB explains, the main objective in developing IFRS 10 was to develop a single basis for consolidation that requires a holistic and qualitative assessment of all legal, contractual and other facts and circumstances. Therefore, we disagree with the request expressed by some stakeholders that quantitative thresholds (or a minimum level of voting rights needed for control) should be introduced.

Question 3(a) – The link between power and returns – Principals and agents
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?

Guidance on 'Principals and Agents' (paragraphs B60, B62-B72 of IFRS 10)

We agree with the view expressed by some stakeholders that determining whether a decision-maker is a principal, or an agent can be challenging in practice and requires judgement.

On the one hand, this is often due to the complexity of the contractual arrangements in the relevant circumstances. On the other hand, we observe that specific issues can, in practice, often only be answered using non-authoritative '*second level guidance*' (such as accounting literature). In this respect, we suggest the IASB develop more application guidelines regarding the requirements for determining whether a decision-maker is a principal or an agent. This relates, for example, to the assessment of control over an investment funds, which is actively managed by an asset manager, as well as film productions that are structured in a separate legal vehicle.

However, as already explained in our answer to question 2(c), we do not agree with the request expressed by some stakeholders that quantitative thresholds (or a particular level of returns that would result in the determination of an agency relationship) should be defined. Instead, we agree with the IASB's statement that requirements based on quantitative thresholds should be avoided (ref. paragraph 19 in the RfI).

Accounting for an investment held by an agent

Another issue that we would like to bring to the IASB's attention concerns the accounting for an investment held by an agent. IFRS 10 and IAS 28 are silent on the accounting from the perspective of an agent, as to whether and under which circumstances:

- an investment held by an agent should be accounted for as a financial asset in accordance with IFRS 9, or
- though not controlling the investee (as the decision-maker is acting as an agent), the agent might have significant influence over the investee and, thus, the investment should be accounted for using the equity method in accordance with IAS 28.

In our experience, this is a common issue for asset managers. However, it is not addressed by IFRS 10 nor by IAS 28. This issue was discussed by the IFRS Interpretations Committee (ref. *Fund manager's assessment of significant influence*, IFRIC Update March 2017). However, the IFRS Interpretations Committee concluded that requirements relating to decision-making authority held in the capacity of an agent could not be developed separately from a comprehensive review of the definition of significant influence in IAS 28, and therefore decided not to add this matter to its standard-setting agenda. Therefore, we recommend the IASB consider the accounting for an investment held by an agent as part of the Post-implementation Review of IFRS 10.

Question 3(b) – The link between power and returns – Non-contractual agency relationships
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 (ie 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.

As already explained in our cover letter, we believe that IFRS 10 provides a robust set of principles and requirements that enable an entity to determine whether it controls an investee. Therefore, we do not believe that comprehensive amendments to IFRS 10 regarding the definition of control are necessary. Rather, we believe that the IASB should address issues related to how the scope of IFRS 10 interacts with other IFRS Standards ('*cross-cutting issues*').

Question 4(a) – Investment entities – Criteria for identifying an investment entity

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.

In our experience, and according to the feedback we have received from our constituents, applying the requirements on the definition and the description of the typical characteristics of an investment entity does not cause significant application issues in practice. By contrast, questions on how the requirements on the consolidation exception interact with multi-level group structures are highly relevant in practice. Please refer to our answer to questions 4(b) below.

Question 4(b) – Investment entities – Subsidiaries that are 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?

Investment entity parent of an investment entity subsidiary

In our experience, and according to the feedback we have received from our constituents, group structures in which an investment entity parent holds an interest in a subsidiary that is an investment entity itself are not common in our jurisdiction.

By contrast, group structures in which a non-investment entity parent holds an interest in a subsidiary that is an investment entity are common in the banking, insurance, and private equity sector. However, the exception to consolidation available to an investment entity does not apply to its non-investment entity parent (ref. paragraph 33 of IFRS 10). As explained in more detail below, we, therefore, recommend the IASB revisit its previous decision on the requirements for a non-investment entity parent of an investment entity subsidiary as part of the Post-implementation Review of IFRS 10.

Non-investment entity parent of an investment entity subsidiary (paragraph 33 of IFRS 10)

As previously noted in our comment letters on the IASB´s Exposure Draft ED/2011/4 *Investment Entities* and ED/2014/2 *Investment Entities: Applying the Consolidation Exception,* we reiterate our belief 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.

As noted by the IASB in paragraph BC249 of IFRS 10, the fair value measurement applied by an investment entity to its interests in subsidiaries provides the most relevant information to users of the financial statements, as this appropriately depicts the investment purpose and the performance of the investment. We believe the IASB's reasoning to be equally valid 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 current 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.

We understand from paragraph BC280 of IFRS 10, that the IASB decided to require all non-investment entity parents to consolidate all of their subsidiaries, as it was concerned that a non-investment entity parent could achieve different accounting outcomes by holding subsidiaries directly or indirectly through an investment entity subsidiary. However, we do not agree with the IASB on these structuring concerns, as:

- A potential abuse (if at all) is more likely to be triggered by (lower) cost of preparation rather than by any accounting leeway.
- The advantages of measuring an investment at fair value through profit or loss (i.e., the realisation of fair value gains) are realised over the lifetime of a subsidiary and are not

foreseeable at the acquisition date, so that any intentional structuring at the acquisition date does not appear realistic to us.

- Measuring an investment at fair value through profit or loss results in earnings volatility in the statement of profit or loss, which would have to be explained in capital market communication. Therefore, it is not apparent to us why an entity should expose itself to fair value measurement if it has no 'exit strategy' for an investment. This means, we believe that requiring an entity to measure an investment at fair value through profit or loss is itself an anti-abuse mechanism.
- Furthermore, we believe it would be unlikely that a portfolio manager, who is incentivised through variable remuneration components based on the performance of the managed portfolio, would allow a loss-making operating subsidiary to be held in the portfolio for which he is responsible to achieve a desired accounting outcome at the parent entity level.

Therefore, we recommend the IASB revisit as part of the Post-implementation Review its previous decision requiring a parent of an investment entity to consolidate all entities that it controls, including those controlled through an investment entity subsidiary, unless the parent itself is an investment entity.

Question 5(a) – Accounting requirements – 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.

As explained in more detail below, we suggest 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.

At its July 2015 meeting, the IFRS Interpretations Committee analysed the following matrix of transactions involving changes of interest in a business to identify where there is a lack of guidance and/or diversity of views on whether a previously held (or a retained) interest should be remeasured (ref. IFRS Interpretations Committee, July 2015 Meeting, Agenda Paper 6, p. 14):

To: *From:*		**Financial asset**	**Equity-accounted investee (significant influence/joint venture)**	**Joint operations**		**Control**
				Joint control—joint operation	**Party to a joint operation***	
Financial asset		Follow guidance in IFRS 9 (note 1)	Guidance not clear (TR#1)	Guidance not clear (TR#4)***	Guidance not clear (TR#8)***	Remeasure – IFRS 3.42**
Equity-accounted investee (significant influence/joint venture)		Remeasure – IAS 28.22 (b) and IFRS 9.5.1.1**	Do not remeasure - IAS 28.24**	Guidance not clear (TR#5)***	Guidance not clear (TR#9)***	Remeasure – IFRS 3.42**
Joint Operations	**Joint control—joint operation**	Remeasure – IFRS 9.5.1.1**	Guidance not clear (TR #2)***	Do not remeasure – IFRS 11.B33C	Guidance not clear (TR#10)***	Guidance not clear (TR#13)***
	Party to a joint operation*	Remeasure – IFRS 9.5.1.1**	Guidance not clear (TR#3)***	Guidance not clear – original submission (TR#6)	Guidance not clear (TR#11)***	Guidance not clear (TR#14)***
Control		Remeasure – IFRS 10.25(b) and IFRS 9.5.1.1 **	Remeasure – IFRS 10.25(b)	Guidance not clear (TR#7)***	Guidance not clear (TR#12)***	Do not remeasure – IFRS 10.23**

We note that – although some of these transactions were addressed by the *Annual Improvements to IFRS Standards 2015-2017 Cycle* – there are still a number of transactions for which IFRS Standards lack guidance. Further, we note that many of these transactions involve changes in interests in joint operations.

We, therefore, recommend the IASB develop guidance on the accounting for all these transactions, as the IASB – as the standard setter – should provide a comprehensive approach that covers the accounting for all possible transactions that involve changes in interests in other entities, regardless of whether (or not) these transactions occur frequently in practice. However, at the same time, we believe that transactions involving changes of interests in joint operations infrequently occur in practice, as entities intentionally enter into (and continue) joint operations. Nevertheless, we suggest the IASB investigate the conceptually appropriate accounting for these transactions. If, in the course of its deliberations, a principle is identified on the basis of which all transactions identified by the IFRS Interpretations Committee in its July 2015 meeting can be assessed consistently, the IASB should reflect this accordingly in the relevant IFRS Standards.

We observe that under current IFRS, the IASB conceptually focuses on whether (or not) a change in ownership interest is a '*significant economic event*' and, based on that assessment, requires an entity to remeasure a previously held (or retained) interest at fair value (ref. paragraphs BCZ173 and BCZ182 of IFRS 10, and BC384 and BC389B of IFRS 3). Therefore, as a starting point, we propose that the IASB investigate whether this principle can also be applied to transactions for which IFRS Standards lack guidance.

Further, we believe that the question as to whether remeasuring a retained interest at fair value provides relevant information – as raised by the IASB in question 5(a)(iii) – cannot be answered in isolation. Instead, we believe that this should also be considered in the context of the overarching question of the underlying principle for the accounting of a transaction that involves a change in an entity's ownership interest. We, therefore, propose that the IASB should address these issues by a broader consideration of how to account for transactions involving changes of interests in a business.

We note that there are differing views in practice on whether remeasuring a previously held (or retained) interest at its fair value provides relevant information. On the one hand, we understand and agree with the IASB's reasoning that a change of control is a significant change in the nature of and economic circumstances surrounding an investor-investee relationship which warrants a change in the classification and measurement of that investment (ref. paragraph BC394 of IFRS 3). Therefore, it is conceptually convincing to us that a loss of control is assumed to be a disposal of a subsidiary (i.e., its assets and liabilities), and, at the same time, an acquisition of an investment accounted for using the equity method.

On the other hand, we have received feedback from some preparers from our constituency who are criticising the current requirement to remeasure a previously held (or retained) interest at its fair value, as:

- Recognizing a gain or a loss on a change of control is not always intuitive (e.g., in the event of a business combination achieved in stages) and, thus, difficult to explain in capital market communication. This particularly applies to situations where the ownership interest in an entity has not changed and a change of control occurs due to changes in other facts and circumstances (e.g., a substantive purchase option expires, a change in the relevant activities of the investee occurs (ref. our answer to question 2(a)), or a change in any other contractual relationships between the parties occurs (e.g., a change in customer-supplier-relationships, or leases).
- When a parent loses control but retains an investment that is accounted for using the equity method, remeasuring the retained interest at its fair value may result in an (internally generated) goodwill included in the carrying amount of the investment. Further, these stakeholders criticise the recognition of a gain or a loss to the extent that results from that remeasurement (i.e., the step-up to the fair value on the previously held (or retained) interest). Therefore, these stakeholders question whether measuring a retained interest at the investor's share of the (pre-disposal) carrying amount of the investee's net assets is more appropriate in these circumstances, as no significant changes have occurred to the retained interest.
- Determining the fair value of the previously held (or retained) interest involves significant judgement. As a starting point, the fair value of the previously held (or retained) interest is derived from the consideration transferred for the controlling stake. However, the consideration transferred often is then corrected by a '*control premium*' implicitly paid or other adjustments (e.g., to reflect that there is no active market for the shares acquired).

Overall, having reviewed and considered the differing views expressed, and the reasoning presented, we are on balance in favour of retaining the requirement to remeasure a retained interest at fair value (as required by paragraph B98 of IFRS 10). This applies in particular to transactions involving a transfer of ownership interests between unrelated third parties, i.e., a market transaction in which the buyer and seller each have a different economic interest in the ownership interests sold. Consequently, we also support retaining the overarching principle on whether (or not) a change in ownership interest is a '*significant economic event*' and suggest the IASB investigate whether this principle can also be applied to transactions for which IFRS Standards are still lacking guidance.

Question 5(b) – Accounting requirements – 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?

Partial acquisition of a subsidiary that does not constitute a business

In our experience, and according to the feedback that we have received from our constituency, transactions and the issue described in question 5(b) are common in some industries in our jurisdiction, but not in others. In the pharmaceutical/biotech industry, for example, a partial acquisition of a subsidiary that does not constitute a business occasionally occurs in practice. Such a legal structuring of an acquisition via a separate legal vehicle is preferred (due to tax reasons) to a direct in-licensing of intellectual property. By contrast, the transactions addressed in question 5(b) are common in the real estate sector in our jurisdiction, as a sale of real estate is usually structured as a share deal, with a non-controlling interest (for tax reasons) being retained by the seller.

Further, we believe, that (partial) acquisitions of subsidiaries and the issue described in question 5(b) will become more prevalent given the recent change to the definition of a business in IFRS 3 and the likelihood of an increase in asset acquisitions (that were previously accounted for as businesses). Therefore, we believe that accounting for a partial acquisition of a subsidiary that does not constitute a business (as defined by IFRS 3) should be addressed by the IASB. In our opinion, in the fact pattern described by the IASB in question 5(b), the existence of a legal vehicle should not affect the accounting for the transaction.

In this context, it should be noted that not only the question arises as to whether the acquirer should (or should not) recognise a non-controlling interest for the equity not attributable to the parent. Moreover, similar questions also arise with regard to the accounting for:

- the initial measurement of the assets acquired (and liabilities assumed) through the acquisition of an empty shell,
- variable or contingent considerations, contingent upon future events, and
- call options or forwards contracts on the shares of a (single asset) entity.

Depending on whether the acquisition method according to IFRS 3 is applied, a different presentation of the transaction in the financial statements is achieved.

For example, if an acquirer applies IFRS 3 to a partial acquisition of a subsidiary that does not constitute a business, the consideration transferred includes any contingent consideration arrangements, and is recognised as a liability and measured at fair value at the acquisition date (IFRS 3.37). By contrast, it is common industry practise not to recognise contingent consideration in an asset acquisition before the consideration is due, since the consideration is contingent upon future events that are beyond an entity's control. For example, in the pharmaceutical industry, it is not common to recognise a contingent consideration for potential future milestone or royalty payments at the effective date of an in-licensing transaction, as these contingent payments are often agreed at an early stage of a drug development and payments are not due until a much later date (e.g., upon drug approval).

Another issue that needs to be considered in connection with the partial acquisition of a subsidiary that does not constitute a business, concerns the accounting for call options or forward contracts on the shares of a '*single-asset entity*'. In practice, in the pharmaceutical industry, entities occasionally enter into a forward purchase contract (or buy a call option) on the shares of a single-asset entity containing only one (or few) intangible asset(s). Such call options are occasionally agreed, for example, in an early development phase of a drug and can be exercised if the drug successfully enters Phase III. In practice, different accounting approaches are observed in this case: Under the first approach, the purchase option is accounted for as a purchase of the underlying intangible asset, based on the economic substance of the agreement. Under this approach, the call option has the economic substance of a contract to purchase an intangible asset (i.e., the intellectual property) rather than to purchase shares. Thus, the contract is outside the scope of IFRS 9, as paragraph 9 of IAS 32 excludes options to buy a non-financial asset that are entered into for the purposes of a receipt of that non-financial asset. Therefore, the option premium paid is capitalised as part of the purchase price for the underlying intangible asset(s). Under a second approach, the option to buy shares are potential voting rights (as described by IFRS 10). Therefore, if the investor concludes that the call option provides control over the investee, the investor will consolidate the legal entity, i.e., the investor would apply IFRS 3, and recognise the intangible assets acquired at their acquisition-date fair value. Lastly, under a third approach, if the investor concludes that the call option is considered as an option to buy shares; the call option is a financial instrument within the scope of IAS 32/IFRS 9, and thus accounted for as a derivative if the investor concludes that the call option does not provide control over the investee.

In the real estate industry, transactions involving a partial acquisition of a subsidiary that does not constitute a business occur frequently in practice, as it is more tax beneficial in our jurisdiction to sell the corporate wrapper, with a non-controlling interest being retained, rather than the underlying property itself. These corporate wrappers usually do not constitute a business as defined by IFRS 3, as these entities only contain the property to be disposed of. In practice, these entities are consolidated by the acquirer (i.e., the property acquired, and any liabilities assumed are recognised in the consolidated financial statements of the acquirer and a non-controlling interest (or, in case of a puttable instrument: a financial liability) is recognised for the equity not attributable to the parent). Further, some of these real estate transactions involve variable, or additional payments contingent on future events (e.g., as an incentive for the seller to enter into favourable lease contracts after the transfer of the property to the acquirer). In practice, this variable (or contingent) consideration is usually not taken into account on initial recognition of the property but is added to the cost of the asset initially recorded, when incurred. Furthermore, call options on shares outstanding are also observed in the real estate sector in our jurisdiction; however, the exercise price of these options usually equals the fair value of the retained interest, effecting that usually no derivative is to be recognised. Lastly, questions arise on whether to recognise a deferred tax liability on initial recognition of the transaction, when acquiring a single-asset entity that is not a business, given the initial recognition exception (ref. paragraph 15(b) of IAS 12). This issue was addressed by an agenda decision *Recognition of deferred taxes when acquiring a single-asset entity that is not a business* taken by the IFRS Interpretations Committee in March 2017.

For further details on the overarching issue, whether the existence of a legal vehicle should affect the accounting for a transaction, please refer to our comments below.

A broader consideration is needed within the Post-implementation Review regarding of whether (or not) the existence of a legal vehicle should affect the accounting for a transaction

We agree with the IASB that the issue described in question 5(b) can be linked to a more general discussion on whether the existence of a legal vehicle (‘*corporate wrapper*’) should affect the accounting for a transaction (ref. IASB Meeting April 2020, Agenda ref 7A, paragraphs 69-70). Therefore, we believe that the IASB should address the broader matter of whether the legal form of a transaction (e.g., the sale of an equity interest in a single-asset entity rather than a direct sale of the asset within that entity) should result in any difference in accounting for the transaction.

As explained in our comment letter to the IFRS Interpretations Committee’s tentative agenda decision in its September 2020 meeting, we believe that a transaction that could have been facilitated standalone or through an empty shell should lead to the same accounting, as its economic substance does not differ. In the course of these broader considerations, we also propose the IASB revisit the issues discussed by the IFRS Interpretations Committee:

- ‘*Sale and Leaseback of an Asset in a Single Asset Entity*‘, tentative agenda decision taken by the IFRS Interpretations Committee published in the September 2020 IFRIC Update, and
- ‘*Sale of a subsidiary to a customer*’, or formerly ‘*Sale of a single asset entity containing real estate*’, discussed by the IFRS Interpretations Committee in its June 2019 meeting.

Question 6 – Collaborative arrangements outside the scope of IFRS 11
In your experience: (a) 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. (b) how do entities that apply IFRS Standards account for such collaborative arrangements? Is the accounting a faithful representation of the arrangement and why?

In our experience, collaborative arrangements outside the scope of IFRS 11 as addressed by the IASB in question 5(b), frequently encounter in practice (e.g., in the pharmaceutical, chemical and biotech industry). Accounting issues that arise in this context relate in particular to revenue recognition according to IFRS 15 *Revenue Recognition*. However, typically, one of the parties that participates in a collaborative arrangement acts as a principal (as described by IFRS 15). Therefore, in our view, applying the requirements on ‘*principal versus agent considerations*’ (in paragraphs B34-B38 of IFRS 15) provide sufficient guidance for the accounting issues relevant in the context of such collaborative arrangements.

Overall, we observe that, in practice, solutions have been developed for accounting issues that arise as regards of collaborative arrangements outside the scope of IFRS 11. Therefore, we believe that no significant application issues persist that would need to be addressed by the IASB through standard setting.

Question 7 – Classifying joint arrangements
In your experience: (a) 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? (b) 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?

In our opinion, classifying joint arrangements can be challenging in practice and is subject to significant judgement. This observation is also supported by the number of requests submitted to the IFRS Interpretations Committee about the classification of joint arrangements.

Regarding the classification of joint arrangements within our jurisdiction, we observe that classifying some legal forms (specific to German company law) proved challenging when classifying joint arrangements upon initial application of IFRS 11. However, in practice, solutions have been developed for these issues within our jurisdiction. Therefore, we believe that no significant application issues persist that would need to be addressed by the IASB through standard setting.

However, we agree with the IASB's observation that, in practice, entities often need to consider '*other facts and circumstances'* (applying paragraphs B29-B32 of IFRS 11) to assess whether a joint arrangement is a joint operation or a joint venture after having considered the legal form and the contractual arrangement. Furthermore, the effects of a different classification are significant due to the differences in the accounting presentation depending on the classification made. Therefore, we understand the request by some stakeholders that the requirements in IFRS 11 regarding the classification of joint arrangements should be simpler to apply.

In light of this call for simplifying the requirements in IFRS 11, we have discussed one possible approach that we suggest the IASB to consider. One possible approach to simplify the assessment of whether a joint arrangement is a joint operation, or a joint venture may consist in:

1. classifying joint arrangements that are structured through a separate vehicle (whose legal form causes the separate vehicle to be considered in its own right) as joint ventures by default; and
2. defining (specific) exceptions to this default classification (for example, for those joint arrangements that are primarily designed for the exclusive provision of output to the parties with the effect that the liabilities incurred by the arrangement are, in substance,

settled by the cash flows received from the parties though their purchases of the output (as stipulated by paragraphs B31 and B32 of IFRS 11)).

Such an approach may simplify the assessment of whether a joint arrangement is a joint operation, or a joint venture, because it is not necessary to consider all of the (three) steps in paragraph B15 of IFRS 11 in each case.

Question 8 – Accounting requirements for joint operations
In your experience: (a) 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? (b) 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.

We note that the issues addressed by the IASB in question 8 were subject to several agenda decisions published by the IFRS Interpretations Committee, for example:

- Accounting by the joint operator: the accounting treatment when the joint operator's share of output purchased differs from its share of ownership interest in the joint operation (March 2015),
- Accounting by the joint operator: recognition of revenue by a joint operator (March 2015),
- Sale of Output by a Joint Operator (March 2019), and
- Liabilities in relation to a Joint Operator's Interest in a Joint Operation (March 2019).

Given that the role and the status of agenda decisions published by the Interpretations Committee have recently been clarified by the Amendments to the *Due Process Handbook* (as published in August 2020), we recommend the IASB revisit the agenda decisions published by the IFRS Interpretations Committee regarding IFRS 10, IFRS 11 and IFRS 12 and consider whether they contain additional application guidance that should be included into the IFRS Standards on consolidation. This would also be in line with the previous practice of the IASB to incorporate the agenda decisions of the Interpretations Committee into IFRS Standards at the next occasion through standard setting.

Further, we note that the above-mentioned agenda decisions published by the Interpretations Committee predominantly deal with questions of the interaction of the scope of IFRS 11 with other IFRS Standards (namely IFRS 15 *Revenue Recognition* and IFRS 16 *Leases*). Therefore, we question whether the issues raised in question 8 should be addressed by a more general discussion regarding the interaction of IFRS 11 with other IFRS Standards, i.e., whether (or not) the accounting requirements for joint operations in IFRS 11 take precedence over the accounting requirements in other IFRS Standards (e.g., IFRS 15 and IFRS 16). As also explained in our answer to question 5(b) above, we, therefore, recommend the IASB undertake a broader consideration of how IFRS 10 and IFRS 11 interact with the scope of other IFRS Standards.

As regards to the accounting requirements for joint ventures, we have received feedback from our constituency that the equity method of accounting according to IAS 28 poses some practical challenges and application issues to entities. For further details, please refer to our answer to question 10 below.

Question 9 – Disclosure of interests in other entities

In your experience:

(a) 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)?

(b) 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?

(c) 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.

(d) 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.

Regarding the current disclosure requirements according to IFRS 12 (as well as the request expressed by some stakeholders for additional disclosures), we have received feedback from preparers from our constituency that:

- current disclosure requirements according to IFRS 12 are already very extensive,
- there is no evidence from capital market communications with investors that '*too little*' information is disclosed on interests in other entities,
- in practice, the assessment of whether information on interests in other entities is material for users of financial statements is challenging, possibly contributing to the disclosure problem (as described by the IASB in its former Discussion Paper *Disclosure Initiative – Principles of Disclosures*), and
- it is questionable whether the information required to be disclosed in accordance with IFRS 12 provides users of financial statements with relevant information they need to forecast an entity's future cash flows.

We, therefore, recommend that the IASB further investigate the cost-benefit profile of its requirements to disclose information on interests in other entities. In particular, it should be taken into account that information to be disclosed does come at a cost for investors, as costs for the preparation of financial statements are implicit to be borne by investors. This means that when developing new disclosure requirements, the IASB should not weigh the demand expressed by investors for additional disclosures with the costs incurred by preparers; rather, investors themselves should be forced to weigh their information needs from the perspective of bearing the costs of preparing the disclosures. Since the amount of information to be disclosed in the notes to the financial statements is limited, investors would thus also have to decide which information should not be disclosed (anymore) in return for a new disclosure requirement. We believe that such an approach will help the IASB in assessing which information entities should be required to disclose, as it balances the information needs of users and the costs for preparing the information. Furthermore, this is also supported by findings from academic research.

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.

Cross-cutting issues

We believe that the following application issues which are related to the question of how the scope of IFRS 10 interacts with other IFRS Standards (‘*cross-cutting issues*’) should be addressed by the IASB:

- accounting for put/call options on non-controlling interests (IFRS 10, IAS 32, and IFRS 9), and
- sale or contribution of a subsidiary (or a group of assets) between an investor and its associate or joint venture (IFRS 10 and IAS 28).

As regards to the accounting for put/call options on non-controlling interests, there is a lack of explicit guidance in IFRS Standards and potential contradictions between the requirements of IFRS 10 and IAS 32, resulting in diversity in practice. Accounting issues that arise in this context are:

- whether or not a non-controlling interest should be recognised (including the question whether IAS 32 takes precedence over IFRS 10), and
- whether or not a financial liability for a put option written on non-controlling interest should be recognised and how that financial liability should be measured subsequently.

As put/call options are common in practice, we believe that these issues should be addressed by the IASB either as part of the Post-implementation Review of IFRS 10, or in its *Financial Instruments with Characteristics of Equity* project, which recently has been moved from the research program to the standard-setting program.

Furthermore, we recommend the IASB resume work on its former project ‘*Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*’. In September 2014, the IASB issued narrow-scope amendments to IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures* (2011) to remove an inconsistency between the requirements in IFRS 10 and those in IAS 28 (2011) that relate to the sale or contribution of assets between an investor and its associate or joint venture. In December 2015, the

IASB postponed the effective date of these amendments indefinitely, pending the completion of its research project on the equity method of accounting. Consequently, and, since these amendments were not endorsed by the European Union, entities within the European Union, in practice, need to adopt their own accounting policy choice resulting in diversity in practice. As transactions, including the contribution of assets to an associate or a joint venture, are common in practice, we recommend the IASB resuming work on this project as part of the Post-implementation Review of IFRS 10.

In addition – as already explained in more detail in our answer to question 5(b) – we believe that a broader consideration is needed within the Post-implementation Review regarding whether the existence of a legal vehicle should affect the accounting for a transaction. These issues also are related to the question of how the scopes of IFRS 10 and IFRS 11 interact with the scope of other IFRS Standards (for instance IFRS 15 and IFRS 16).

Bail-out acquisition of a non-performing borrower

As another topic, we suggest the IASB consider so-called '*bail-out acquisitions of non-performing borrowers'* as part of the Post-implementation Review of IFRS 10. This topic refers to situations in which a bank – in its capacity as a lender – obtains control over a borrower because the borrower has become non-performing, and, as a consequence, the bank must consolidate the borrower in its consolidated financial statements in accordance with IFRS 10.

However, consolidation of non-performing borrowers leads to confusion in capital market communication, as it needs to be explained that the provision for credit losses is not only included in the line item '*loss allowances*' in the statement of profit or loss, but in the case of bail-out acquisitions is also reflected in '*other operating income and expenses*' (e.g., impairment expenses on assets acquired in the course of bail-out acquisitions). As a result, ratios calculated on the basis of IFRS figures reflect only an incomplete picture of loss allowances and non-performing loans. By contrast, bail-out acquisitions of non-performing borrowers are not consolidated in the calculation of ratios to be calculated for regulatory purposes (i.e., these acquisitions continue to be treated as what they actually are: impaired non-performing loans). Therefore, we suggest the IASB consider whether a different accounting treatment for bail-out acquisitions would lead to a more appropriate presentation. In particular, we suggest the IASB consider introducing a consolidation exemption for bail-out acquisitions of non-performing borrowers for similar reasons as introduced by the exception to consolidation for investment entities.

One of the main reasons for introducing the consolidation exception for investment entities was that the business model of an investment entity that holds investments for the sole purpose of capital appreciation, investment income, or both, differs significantly when compared to investments in operating subsidiaries and users' information needs are better met by information other than consolidating these investments (i.e., information about the fair value of the investments; ref. paragraph BC217 of IFRS 10). With respect to bail-out acquisitions of non-performing borrowers it could be argued that an entity's activities and business purpose also differ significantly when compared to its investment in operating subsidiaries. The activity and business purpose of an entity in relation to non-performing borrowers primarily involve the liquidation of the acquired assets that were previously pledged as securities.

Forward transactions on the acquisition of subsidiaries vs. associates

As another issue that should be considered as part of the Post-implementation Review relates to the accounting for forward transactions on the acquisition of:

- subsidiaries, and
- associates.

IFRS 9.2.2(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. paragraph BCZ2.42 of IFRS 9). These forward contracts on associates are therefore to be measured at fair value (through profit or loss) in accordance with IFRS 9. We have received feedback from our constituents claiming that this difference in accounting is perceived as inconsistent. Further, it is unclear whether (and under which circumstances) a '*synthetic'* forward contract (i.e., a combination of a written put and a purchased call option that is substantially identical to a forward contract) is excluded from the scope of IFRS 9. Therefore, we suggest the IASB consider forward transactions on the acquisition of subsidiaries (and associates respectively) as part of the Post-implementation Review.

The notion of 'control' across IFRS Standards

We note that IFRS 10 introduced a '*concept of control*' which differs in meaning from other concepts of control, such as, for example, introduced in paragraph 31 of IFRS 15, according to which revenue is recognised when control over a good or a service is transferred to the customer.

Although we are aware of that the concept of control – as used in IFRS 10 and IFRS 11 – cannot be applied to other IFRS Standards (e.g., IFRS 15), we suggest the IASB clarify that the notion of control – as defined by paragraphs 5-18 of IFRS 10 – shall only be applied to matters of assessing whether an investor controls an investee (or whether two or more investors jointly control an investee). However, in the long run, the IASB might want to consider aligning the notion(s) of 'control' across IFRS Standards.

Application issues regarding the equity method of accounting

We have received feedback from our constituency that application issues arise in practice on the equity method of accounting as IAS 28 is lacking guidance, for example, on:

- the elimination profits or losses resulting from intragroup transactions, in particular in the event of a transaction that alters the relationship between an investor and the investment accounted for using the equity method, and
- 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), as already mentioned above.

We note that the IASB has tentatively decided not to consider any conceptual and application issues related to the equity method (according to IAS 28) within the Post-implementation Review, as these issues are considered as part of its separate research project on the equity method. However, in practice, these application issues can often only be answered using second-level guidance (such as accounting literature). Therefore, we recommend the IASB consider these practical application issues as part of the Post-implementation Review.