ED/2012/3
Equity Method: Share of Other Net Asset Changes (Proposed amendments to IAS 28)

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1. Background of ED/2012/3 (1/4)

- Intention: to specify the application of the equity method, when an investor is accounting for it´s share of the other net asset changes of an associate or joint venture
- Other net asset changes: changes in the net assets of an investee that are not recognised in profit or loss or other comprehensive income (OCI) of the investee, and that are not distributions received
- Examples:
  - Investee issues additional shares to third parties or buys back shares from third parties
  - Equity-settled share-based payments
  - Disposal or acquisition of non-controlling interests in subsidiaries of the investee

1. Background of ED/2012/3 (2/4)

- diversity in practice resulting from consequential amendments made to IAS 28 in 2007
- IFRS IC: started consideration of this issue in March 2011, proposed a narrow-scope amendment with the following principles:
  - Reduction of an investor´s ownership interest: partial disposal recognised in profit or loss
  - Increase in an investor´s ownership interest: incremental purchase recognised at cost
  - Call option transactions not in scope of proposed amendments
- IASB: Rejection of IFRS IC-proposal
  - Call option transactions, in particular share-based payments, not addressed
  - Concerned of additional complexity, since proposed accounting did not provide symmetry between a reduction and an increase
  - Intention: generalised approach that addresses all types of other net asset changes as a short-term solution

1. Background of ED/2012/3 (3/4)

- Consideration of share-based payments (in particular equity settled share-based payments) for employees of an investee

- Investee:

Dr employee expense ↓ Cr equity ↓

- Investor (equity method):

proportion of net profit or loss recognised in P&L (so proportion of share-based payment expense is included)

in question: accounting for the change in equity recognised by the investee

1. Background of ED/2012/3 (4/4)

- Investee:

	Dr employee expense	Cr equity
	↓	↓

- Investor (equity method):

IFRS IC-approach:	proportional in P&L	**proportional in P&L**

  - Consequence: nil-net expense in the vesting period of the share-based plan
  - Dilution loss is only recognised if and when employee´s awards are exercised and ownership interest is reduced (through P&L)

IASB-approach:	proportional in P&L	**proportional in equity**

  - Consequence: Recognition in P&L and in equity during the vesting period
  - If awards are exercised, dilution loss is recognised in equity

2. Content of ED/2012/3 (1/3)

- Amendments published on 22 November 2012
- Comments to be received by 22 March 2013
- IASB´s view: return to the requirements of IAS 28 before the consequential amendments of 2007
- Approach is a short-term solution
- Retrospective application of the proposed requirements
- Effective date will be determined after evaluating the comments received (with earlier application permitted)

2. Content of ED/2012/3 (2/3)

Proposed amendments in detail:

- Clarification for the recognition of the investor´s share of the investee´s OCI
  - IAS 28.10 (b): *The investor's share of the investee's components of other comprehensive income is recognised in the investor's other comprehensive income (see IAS 1 Presentation of Financial Statements). Such changes include those arising from the remeasurements of the net defined benefit liability (asset), from the revaluation of property, plant and equipment and from foreign exchange translation differences.*
- Explanation of possible distributions
  - IAS 28.10 (c): *Such distributions include dividends in cash or other assets and returns of invested capital.*

2. Content of ED/2012/3 (3/3)

- Clarification that the investor´s share of the investee´s other net asset changes is recognised in the investor´s equity
  - IAS 28.10 (d): *The investor's share of the investee's net asset changes, other than profit or loss or other comprehensive income and distributions received, is recognised in the investor's equity. Examples of such changes include those arising from movements in the share capital of the investee (for example, when an investee issues additional shares to third parties or buys back shares from third parties) and movements in other components of the investee's equity (for example, when an investee accounts for an equity-settled share-based payment transaction).*
- Clarification for the discontinuation of the equity method
  - IAS 28.22 (c): *When an investor discontinues the use of the equity method, the investor shall […] (ii) reclassify to profit or loss the cumulative amount of equity that had previously been recognised in accordance with paragraph 10(d).*

3. Alternative view (1/2)

Vote against the ED by one IASB-member due to the following concerns:

- Inconsistency with the concept of IAS 1
  - According to IAS 1, changes in equity arising from transactions with owners have to be seperated from other changes in equity (non-owner changes)
  - IASB-approach would impaire this separation
- Inconsistency with the concept of IFRS 10
  - IFRS 10.25: the gain or loss associated with the loss of control of a subsidiary is recognised through P&L (i.e. share of subsidiary is reduced from 50% to 30% as a consequence of other net asset changes)
  - If transaction was made in two steps, different accounting treatment would be applicable:
    - Gain or loss arising from the loss of control: through P&L
    - Gain or loss arising from the reduction in ownership interest: in equity

3. Alternative view (2/2)

- Change in the nature of equity
  - Concern that equity transactions of an associate´s associate (and of any further remote transactions) would be recognised in the investor´s equity
  - No distinction from the investor´s own equity transactions in the consolidated financial statements
  - Recycling leads to additional complexity and risks confusion about the distinction between OCI and equity
- Equity accounting vs. one-line consolidation
  - Disagreement with the interpretation of the equity method as a one-line consolidation
  - Changes in ownership resulting from other net asset changes are interpreted as indirect disposals or acquisitions

4. EFRAG´s Draft Comment Letter

- No consensus reached, 3 views set out
  - View 1: the investor should recognise directly in equity its ownership interest of the investee´s other net asset changes (approach of the IASB-ED)
    - Main point: other net asset changes do not represent a performance of the investee (no P&L or OCI), therefore recognition in equity
  - View 2: investor should not recognise the investee´s other net asset changes
    - Main point: other net asset changes of the investee result from equity transactions in which the investor did not participate, therefore they should not affect the investor´s accounting
  - View 3: recognition of the investee´s other net asset changes as deemed disposals or acquisitions of the investor (approach of the IFRS IC)
    - Main points: IASB-approach is inconsistent with existing IFRS-principles, does not relate to the documented practice and would not provide timely and useful information about the investor´s performance; economically comparable transactions would be accounted for differently

5. IASB´s Questions (1/3)

Question 1

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

Do you agree? Why or why not?

Tentative view of ASCG´s IFRS-Committee

- Agrees with the proposed amendments
- Rates the amendments as a pragmatic short-term solution
- Appreciates generalised approach that addresses all types of other net asset changes
- Supports recognition in equity, since other net asset changes result from the investee´s equity transactions

5. IASB´s Questions (2/3)

Question 2

The IASB also proposes that an investor shall reclassify to profit or loss the cumulative amount of equity that the investor had previously recognised when the investor discontinues the use of the equity method.

Do you agree? Why or why not?

Tentative view of ASCG´s IFRS-Committee

- Agrees with the proposal

5. IASB´s Questions (3/3)

Question 3

Do you have any other comments on the proposals?

Tentative answer of ASCG´s IFRS-Committee

- Assessment of the amendments as a pragmatic short-term solution
- Comprehensive debate about the conceptual issues related to the equity method is deemed necessary

Thank you!

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