7 February 2014

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans

AOSSG comments on IASB Exposure Draft ED/2013/10
Equity Method in Separate Financial Statements

The Asian-Oceanian Standard-Setters Group (AOSSG) is pleased to provide comments on the IASB ED/2013/10 *Equity Method in Separate Financial Statements* (ED). In formulating its views, the AOSSG sought the views of its constituents within each jurisdiction.

The AOSSG currently has 26 member standard-setters from the Asian-Oceania region: Australia, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan, and Vietnam.

To the extent feasible, this submission to the IASB reflects in broad terms the collective views of AOSSG members. Each member standard-setter may also choose to make a separate submission that is consistent or otherwise with aspects of this submission. The intention of the AOSSG is to enhance the input to the IASB from the Asian-Oceania region and not to prevent the IASB from receiving the variety of views that individual member standard-setters may hold. This submission has been circulated to all AOSSG members for their feedback after having initially been developed through the AOSSG Acquisitions and Reporting Entity issues Working Group.

Although some AOSSG members have expressed support for the proposal, many AOSSG members question if the proposed amendments are necessary or appropriate at this point of time, given that the IASB plans to undertake a research project on the equity method of accounting. If the IASB were to proceed with these proposals, these members consider that the IASB should at least provide sufficient rationale in the Basis for Conclusions as to how the proposed changes would improve the quality of financial information. Otherwise, the proposal could be viewed as the IASB inappropriately setting a precedent of amending IFRSs to address specific local legislative requirements rather than arriving at a conclusion in light of conceptual merit.

In addition, many AOSSG members find that the proposed amendment to paragraph 25 of IAS 28 *Investments in Associates and Joint Ventures* and the explanation stated in the Basis for Conclusions in the ED is inconsistent. These AOSSG members recommend that the IASB consider whether such a change is necessary.

Considering the divergent views expressed on the equity method of accounting, AOSSG members believe that it would be more appropriate if the IASB were to undertake a research project first to develop conceptual conclusions as to whether, and if so, what changes are necessary to IAS 27 *Separate Financial Statements*.

The views of the AOSSG in relation to the specific questions in the ED are explained in more detail in the Appendix.

If you have any questions regarding any matters in this submission, please contact either one of us.

Yours sincerely,

Clement Chan
AOSSG Chair

Ikuo Nishikawa
AOSSG Acquisitions and Reporting Entity Issues Working Group Leader

APPENDIX – Detailed comments on ED/2013/10

Question 1 - Use of the equity method

The IASB proposes to permit the equity method as one of the options to account for an entity's investments in subsidiaries, joint ventures and associates in the entity's separate financial statements.

Do you agree with the inclusion of the equity method as one of the options? If not, why?

Comments on Question 1

1. Some AOSSG members strongly support the proposal. These members believe that the amendment will offer relief to many entities as they prepare separate financial statements for regulatory reasons only. Regulatory provisions and tax laws of certain jurisdictions require the use of equity method when financial statements are presented to authorities, where an additional set of financial statements may need to be prepared in order to comply with IFRSs, because IAS 27 does not allow the equity method in separate financial statements. Considering the incremental cost and burden, the proposal would be a welcome change to these jurisdictions.

2. However, many AOSSG members question if the proposed amendments are necessary or appropriate at this point in time, given that the IASB plans to undertake a research project on the equity method of accounting. These AOSSG members think that such activities will involve a fundamental assessment of the equity method in terms of its conceptual ground as well as its usefulness to investors and challenges for preparers.

3. If the IASB were to proceed with these proposals, these members are of the view that it is necessary for the IASB to at least provide sufficient rationale in the Basis for Conclusions as to how the proposed changes would improve the quality of financial information. Otherwise, many AOSSG members are afraid that the proposal could be viewed as the IASB inappropriately setting a precedent of amending IFRS to address specific local legislative requirements rather than arriving at a conclusion in light of conceptual merit.

4. These members believe that, before finalising the proposals, the IASB should deliberate a fundamental question as to whether the equity method of accounting is 'part of measurement' or 'proxy for the consolidation process' (also known as, 'one-line consolidation'). If the IASB were to conclude that the latter view is appropriate, it would be illogical to permit the equity method of accounting in separate financial statements. Accordingly, these AOSSG members recommend that the IASB undertakes the research project before it considers any amendments to IFRS in relation to the application of the equity method.

5. In addition, some AOSSG members believe that the IASB should consider another fundamental question concurrently, if the IASB were to amend paragraph 10 of IAS 27. These members are of the view that the accounting choice permitted under IAS 27 (that is, the choice of cost-based measurement or fair-value measurement in accordance with IFRS 9 *Financial Instruments*) is arbitrary, because it effectively permits the free choice of these fundamentally different measurement bases. These members recommend that the accounting choice based on IFRS 9 be eliminated, considering the nature of investments that are the subjects of the standard (those are, investments in subsidiaries, joint ventures and associate.) In their views, the fair-value measurement would not be considered to be a relevant

measurement basis for such investments, drawing from the IASB's preliminary view regarding how relevant measurement basis for assets can be determined as explained in its Discussion Paper *A Review of the Conceptual Framework for Financial Reporting*.

Question 2 - Transition provisions

The IASB proposes that an entity electing to change to the equity method would be required to apply that change retrospectively, and therefore would be required to apply IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Do you agree with the proposed transition provisions? If not, why and what alternative do you propose?

<u>Comments on Question 2</u>

6. Some AOSSG members believe that the prospective application should be permitted for investments in subsidiaries, considering the operational complexities that might arise from retrospective application. However, many AOSSG members generally support the proposal, because the proposed requirement would not be applied in many circumstances, and the incremental cost resulted from the operational complexity would be reasonably limited.

7. In addition, some AOSSG members also consider that the retrospective application would provide useful comparative information to users, and concurs with the rationale in paragraph BC12 of the ED that entities should be able to comply with this requirement using the information available in preparing consolidated financial statements or financial statements of investor in an associate or joint venture.

Question 3 - First-time adopters

The IASB does not propose to provide any special relief for first-time adopters. A first-time adopter electing to use the equity method would be required to apply the method from the date of transition to IFRSs in accordance with the general requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards*.

Do you agree that a special relief is not required for a first-time adopter? If not, why and what alternative do you propose?

<u>Comments on Question 3</u>

8. Consistent with many AOSSG members' views to Question 2, many AOSSG members support the proposal not to provide any special relief for first-time adopters.

Question 4 - Consequential amendment to IAS 28

The IASB proposes to amend paragraph 25 of IAS 28 in order to avoid a conflict with the principles of IFRS 10 *p* in situations in which an entity loses control of a subsidiary but retains an ownership interest in the former subsidiary that gives the entity significant influence or joint control, and the entity elects to use the equity method to account for the investments in its separate financial statements.

Do you agree with the proposed consequential amendment? If not, why?

APPENDIX – Detailed comments on ED/2013/10

Comments on Question 4

9. Many AOSSG members find it difficult to understand the rationale for the amendment to paragraph 25 of IAS 28. Paragraph BC10 of the ED explains that the existing accounting requirements of paragraph 25 of IAS 28 would be inconsistent with the principles of IFRS 10 *Consolidated Financial Statements*, unless changes are made to the requirement. Some AOSSG members strongly believe that the information presented in an entity's separate financial statements should be identical to those in its consolidated financial statements, if it applies the equity method to investments in its subsidiaries[1]. However, these AOSSG members are not convinced why such a conflict would arise by permitting the equity method of accounting to separate financial statements as proposed by the ED. These members believe that, unless there is sufficient ground to do otherwise, accounting requirements for separate financial statements should not be carried forward to the requirements for consolidated financial statements at least so far as consolidation process is concerned.

10. This is because, in consolidated financial statements, the loss of control of a subsidiary is a significant economic event where the parent subsidiary relationship ceases to exist and an investor-investee relationship begins that differs significantly from the former parent-subsidiary relationship (refer to paragraph BCZ182 of IFRS 10). On the other hand, the nature of an investment in a subsidiary, an associate or a joint venture (that is, an investor-investee relationship) does not change in separate financial statements, as a result of the loss of control of a subsidiary (refer to paragraph BC10 of IAS 27).

11. Notwithstanding the above, if the IASB were to proceed with the proposals, many AOSSG members consider that the proposed amendment to paragraph 25 of IAS 28 does not reflect the intention of the IASB as expressed in paragraph BC11 of the ED and would need to be redrafted. These AOSSG members consider that the proposed amendment to IAS 28 does not require an entity that applies the equity method in separate financial statements to remeasure any retained investment to fair value if an investor loses control over a subsidiary (as explained in paragraph BC11 of the ED). Moreover, these AOSSG members consider that, if the IASB were to proceed with the proposed amendments to IAS 28, there are many other situations that the IASB should consider. These considerations include, for example:

    (1) If Company A reduces its interest in Company B from 60% to 20% (Company A loses control of Company B but still has significant influence over Company B), and Company A accounts for its subsidiaries and associates using the cost method and the equity method respectively, how should Company A recognise the gain or loss on the partial disposal? How should Company A account for the accumulated amounts in other comprehensive income? Should the retained interest be re-measured to fair value at the disposal date and should the difference (if any) be recognised in profit or loss?

    (2) IFRS 3 *Business Combinations* and IFRS 10 currently provide guidance on the accounting in the consolidated financial statements for business combination achieved in stages, acquisition of non-controlling interests, loss of control over subsidiaries, and changes in interest in subsidiaries while maintaining control. Considering the nature of these transactions are similar to those envisaged in the proposed amendments in the ED,

1 For example, the Korean accounting standards provides guidance to ensure the consistency.

the accounting requirements of these transactions in separate financial statements should also be reconsidered.

Question 5 - Other comments

Do you have other comments?

Comments on Question 5

12. As stated in our comments on Question 1, AOSSG members encourage the IASB to undertake its research project on the equity method of accounting before any amendments in IFRS in relation to the equity method. A number of AOSSG members have expressed interest in providing input to the project, once the IASB initiates its planned work. AOSSG members also believe that, based on the outcome of the research project, the IASB will be able to draw conceptual conclusion as to whether, and if so, what changes are necessary to IAS 27.