Andreas Barckow
Chair, International Accounting Standards Board
Columbus Building
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Canary Wharf
London
E14 4HD

17 January 2025

Dear Mr.Barckow,

Exposure Draft - Equity Method of Accounting – IAS 28 Investment in Associates and Joint Ventures (revised 202x)

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the Exposure Draft - Equity Method of Accounting – IAS 28 Investment in Associates and Joint Ventures (revised 202x) ('the Exposure Draft').

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors, and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society. AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia. AFME is registered on the EU Transparency Register, registration number 65110063986-76.

The appendix to this letter sets out our responses to the questions in the Exposure Draft. We trust that our comments are helpful, and we look forward to engaging further with the IASB on the Exposure Draft.

Yours sincerely,

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APPENDIX

EXPOSURE DRAFT

EQUITY METHOD OF ACCOUNTING – IAS 28 INVESTMENT IN ASSOCIATES AND JOINT VENTURES (REVISED 202X)

Questions for respondents

Proposed amendments to IAS 28

For simplicity, Questions 1–5 are expressed in relation to investments in associates. References to 'investor,' 'associate' and 'significant influence' should be read as also referring to 'joint venturer', 'joint venture' and 'joint control' in relation to investments in joint ventures. For investments in subsidiaries to which the equity method is applied in separate financial statements, see Question 6.

Question 1—Measurement of cost of an associate

(Appendix A and paragraphs 13, 22, 26 and 29 of [draft] IAS 28 (revised 202x))

Paragraph 32 of IAS 28 requires an investor that obtains significant influence to account for the difference between the cost of the investment and the investor's share of the net fair value of the associate's identifiable assets and liabilities either as goodwill (included in the carrying amount of the investment) or as a gain from a bargain purchase (recognised in profit or loss). However, IAS 28 does not include requirements for how an investor measures the cost of the investment on obtaining significant influence—for example:

(a) whether to measure any previously held ownership interest in the associate at fair value; or

(b) whether and if so how to recognise and measure contingent consideration.

The IASB is proposing an investor:

(a) measure the cost of an associate, on obtaining significant influence, at the fair value of the consideration transferred, including the fair value of any previously held interest in the associate.

(b) recognise contingent consideration as part of the consideration transferred and measure it at fair value. Thereafter:

(i) not remeasure contingent consideration classified as an equity instrument; and

(ii) measure other contingent consideration at fair value at each reporting date and recognise changes in fair value in profit or loss.

Paragraphs BC17–BC18 and BC89–BC93 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

We generally support the Board's proposals on measurement of investment in associates and joint ventures.

We note diversity in the normative analysis regarding the inclusion of deferred taxes in the investor's share of the fair value of the associate's or joint venture's identifiable assets and liabilities. Indeed, some member firms support view A (supporting ED's proposal), whereas others support view B, both views deliberated by the IASB in April 2023.

We believe the proposal to include the deferred tax effects into the measurement of the investments in associates and joint ventures may add additional complications in practice when obtaining information from the investees (for example, details about the related tax environment of the investee are not always known) to comply with current requirements of IAS28.32) – an area which historically has been challenging when implementing equity method of accounting in practice. We thus recommend that both approaches be permitted.

Regarding all the ED proposals addressed in Q1, given the complexity of some of transactions affected, we would recommend that changes should apply prospectively.

Question 2—Changes in an investor's ownership interest while retaining significant influence

(Paragraphs 30–34 of [draft] IAS 28 (revised 202x))

IAS 28 does not include requirements on how an investor accounts for changes in its ownership interest in an associate, while retaining significant influence, that arise from:

(a) the purchase of an additional ownership interest in the associate;

(b) the disposal of an ownership interest (partial disposal) in the associate; or

(c) other changes in the investor's ownership interest in the associate.

The IASB is proposing to require that an investor:

(a) at the date of purchasing an additional ownership interest in an associate:

> (i) recognise that additional ownership interest and measure it at the fair value of the consideration transferred;
>
> (ii) include in the carrying amount the investor's additional share of the fair value of the associate's identifiable assets and liabilities; and

(iii) account for any difference between (i) and (ii) either as goodwill included as part of the carrying amount of the investment or as a gain from a bargain purchase in profit or loss.

(b) at the date of disposing of an ownership interest:

> (i) derecognise the disposed portion of its investment in the associate measured as a percentage of the carrying amount of the investment; and
>
> (ii) recognise any difference between the consideration received and the amount of the disposed portion as a gain or loss in profit or loss.

(c) for other changes in its ownership interest in an associate:

> (i) recognise an increase in its ownership interest, as if purchasing an additional ownership interest. In (a)(i), 'the fair value of the consideration transferred' shall be read as 'the investor's share of the change in its associate's net assets arising from the associate's redemption of equity instruments'.
>
> (ii) recognise a decrease in its ownership interest, as if disposing of an ownership interest. In (b)(ii) 'the consideration received' shall be read as 'the investor's share of the change in its associate's net assets arising from the associate's issue of equity instruments'.

Paragraphs BC20–BC44 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? If you disagree, please explain why you disagree and your suggested alternative.

We agree with the objective and extent of these proposals. However, for the acquisition of additional interests while retaining significant influence, the requirement to perform a Purchase Price Allocation (PPA) for each change in ownership is difficult to apply in practice, as investors may not have full access to the necessary financial data to perform a PPA. This requirement is also inconsistent with the fact that investments in associates follow net presentation rather than individual gross presentation of assets and liabilities of the investee. In addition, there is an inconsistency between the cumulative layers approach proposed for the acquisition of additional interests and the approach for the partial disposal, for which associate is viewed and managed as a whole instrument. Therefore, an operational simplification or practical expedient would be welcome.

Question 3—Recognition of the investor's share of losses

(Paragraphs 49–52 of [draft] IAS 28 (revised 202x))

Paragraph 38 of IAS 28 requires that if an investor's share of losses equals or exceeds its interest in the associate, the investor discontinue recognising its share of further losses. However, IAS 28 does not include requirements on whether an investor that has reduced the carrying amount of its investment in an associate to nil:

(a) on purchasing an additional ownership interest, recognises any losses not recognised as a 'catch up' adjustment by deducting those losses from the cost of the additional ownership interest; or

(b) recognises separately its share of each component of the associate's comprehensive income.

The IASB is proposing an investor:

(a) on purchasing an additional ownership interest, not recognise its share of an associate's losses that it has not recognised by reducing the carrying amount of the additional ownership interest.

(b) recognise and present separately its share of the associate's profit or loss and its share of the associate's other comprehensive income.

Paragraphs BC47–BC62 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? If you disagree, please explain why you disagree and your suggested alternative.

We agree with these proposals.

Question 4—Transactions with associates

(Paragraph 53 of [draft] IAS 28 (revised 202x))

Paragraph 28 of IAS 28 requires an investor to recognise gains and losses resulting from transactions between itself and an associate only to the extent of unrelated investors' interests in the associate.* This requirement applies to both 'downstream' transactions (such as a sale or contribution of assets from an investor to an associate) and 'upstream' transactions (such as a sale of assets from an associate to an investor).

If an investor loses control of a subsidiary in a transaction with an associate, the requirement in IAS 28 to recognise only a portion of the gains or losses is inconsistent with the requirement in IFRS 10 to recognise in full the gain or loss on losing control of a subsidiary.

The IASB is proposing to require that an investor recognise in full gains and losses resulting from all 'upstream' and 'downstream' transactions with its associates, including transactions involving the loss of control of a subsidiary.

Paragraphs BC63–BC84 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with this proposal?

If you disagree, please explain why you disagree and your suggested alternative.

*This Invitation to Comment describes the requirement in paragraph 28 of IAS 28 that is currently in effect. The IASB amended that requirement when it issued Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28) in 2014, but the effective date of those amendments has been deferred indefinitely

Whilst we acknowledge the IASB's proposal to address the inconsistency between IFRS 10 and IAS 28 in order to reduce diversity in application, we note that diversity in practice exists amongst our member firms as some recognise the gain or loss in full whilst others do not agree with the proposal to recognise in full the gain or loss on losing control of a subsidiary in a transaction with an associate or joint venture we therefore recommend that the IASB conducts detailed outreach to understand existing practice prior to finalisation of the ED.

Our members have noted two different views which reflect current application of the requirements:

View 1

Proponents of this view note that entities may frequently partially divest of an investment in a subsidiary via transactions with an associate or joint venture. Applying IFRS 10 in such instances would result in recognition of the full gain or loss on such transactions despite a significant portion being unrealised as it relates to the investor's retained interest. The inclusion of the full gain or loss in the statement of profit, at the time of partial divestment, does not faithfully represent the investor's performance (as referred to in the Conceptual

Framework), as a significant portion of that gain or loss only becomes realised when the retained interest is ultimately disposed of to a third party.

As an alternative, we request that the IASB reconsider Alternative 2 (noted in BC67(b)) whereby the investor would recognise only partial gains or losses on transactions involving the loss of control of a subsidiary in a transaction with an associate or joint venture.

View 2

Proponents of this view note that recognition of gains and losses resulting from downstream transactions with its associates in full when there is loss of control of a subsidiary corresponds to the current practice of many preparers. These members note that the arguments included in BC 79-83 are particularly relevant because:

-per IFRS definition, a group is limited to the parent entity and the entities it controls, ie. its subsidiaries.

-IFRS 10 considers the loss of control of a subsidiary as a significant economic event that justifies the derecognition of a subsidiary's assets and liabilities and the measurement of any retained investment at fair value, with recognition of the full gain or loss of control.

This proposal has the merit of simplifying the accounting treatment.

Some members also noted that the IASB should consider extending this approach to all 'upstream' and 'downstream' transactions between an investor and its associates for simplicity reasons on the basis of the arguments included in BC82 and 83.

Question 5—Impairment indicators (decline in fair value)

(Paragraph 57 of [draft] IAS 28 (revised 202x))

Paragraphs 41A–41C of IAS 28 describe various events that indicate the net investment in an associate could be impaired. Paragraph 41C of IAS 28 states that a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is objective evidence of impairment. One of the application questions asked whether an investor should assess a decline in the fair value of an investment by comparing that fair value to the carrying amount of the net investment in the associate at the reporting date or to the cost of the investment on initial recognition.

The IASB is proposing:

(a) to replace 'decline…below cost' of an investment in paragraph 41C of IAS 28 with 'decline…to less than its carrying amount';

(b) to remove 'significant or prolonged' decline in fair value; and

(c) to add requirements to IAS 28 explaining that information about the fair value of the investment might be observed from the price paid to purchase an additional interest in the associate or received to sell part of the interest, or from a quoted market price for the investment.

The IASB is also proposing to reorganise the requirements in IAS 28 relating to impairment to make them easier to apply, and to align their wording with the requirements in IAS 36 Impairment of Assets.

Paragraphs BC94–BC106 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative

We have concerns about the proposed amendments to paragraph 41C included in Q5b) [i.e. to remove 'significant or prolonged' decline in fair value;] and would prefer to keep the current wording as there is well established practice that is well understood by auditors, users and investors.

We believe that the current wording of IAS 28.41C " A <u>significant or prolonged</u> decline in the fair value of an investment in an equity instrument below its cost is also objective evidence of impairment." is useful. Indeed, regarding the case of listed investments, it does not seem relevant to perform an impairment test when there is any one-off decrease in share price representing the investment below its carrying amount. This particular event may not be evidence of an impairment of the investment.

With the IASB's proposal to remove the terms "significant or prolonged," preparers might be required to perform impairment tests very often, that would not lead to the recognition of an *impairment in case the value in use of the investment is higher than its carrying amount. Such systematic impairment test would be costly and burdensome.*

We therefore propose keeping the current wording of IAS 28.41C.

Our members also note that the proposal in Q5a) [i.e. to replace 'decline…below cost' of an investment in paragraph 41C of IAS 28 with 'decline…to less than its carrying amount';] is useful and clarifies existing practice.

Application of the proposed requirements to investments in subsidiaries to which the equity method is applied in separate financial statements

Question 6—Investments in subsidiaries to which the equity method is applied in separate financial statements

Paragraph 10 of IAS 27 permits a parent entity to use the equity method in IAS 28 to account for investments in subsidiaries, joint ventures and associates in separate financial statements.

The IASB is proposing to retain paragraph 10 of IAS 27 unchanged, meaning that the proposals in this Exposure Draft would apply to investments in subsidiaries to which the equity method is applied in the investor's separate financial statements.

Paragraphs BC112–BC127 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with this proposal?

If you disagree, please explain why you disagree and your suggested alternative.

We agree with this proposal and have no specific concerns to note.

Proposed amendments to IFRS 12 and IAS 27—Disclosure requirements

Question 7—Disclosure requirements

(Paragraphs 20(c), 21(d)–21(e) and 23A–23B of IFRS 12 and paragraph 17A of IAS 27)

The IASB is proposing amendments to IFRS 12 in this Exposure Draft. For investments accounted for using the equity method, the IASB is proposing to require an investor or a joint venturer to disclose:

(a) gains or losses from other changes in its ownership interest.

(b) gains or losses resulting from 'downstream' transactions with its associates or joint ventures.

(c) information about contingent consideration arrangements; and

(d) a reconciliation between the opening and closing carrying amount of its investments.

The IASB is also proposing an amendment to IAS 27 to require a parent—if it uses the equity method to account for its investments in subsidiaries in separate financial statements—to disclose the gains or losses resulting from its 'downstream' transactions with its subsidiaries.

Paragraphs BC137–BC171 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

We agree with these proposals. However, we are concerned about the commercial sensitivity of some of the information which investors or joint venturers would be required to disclose. This is particularly the case for contingent consideration arrangements and transactions between associates and joint ventures and its investor. We recommend that the disclosure framework considers the level of aggregation that is required to ensure that commercially sensitive information is not disclosed.

Our members also note that it would be helpful if the IASB considers including a clear definition of 'downstream' transactions. This could be achieved through providing a non-exhaustive list of examples in the application guidance.

Proposed amendments to IFRS 19

Question 8—Disclosure requirements for eligible subsidiaries

(Paragraphs 88(c), 91A and 240A of IFRS 19)

IFRS 19 permits eligible subsidiaries to apply IFRS Accounting Standards with reduced disclosure requirements. It specifies the disclosure requirements an eligible subsidiary applies instead of the disclosure requirements in other IFRS Accounting Standards.

As part of developing proposed amendments to the disclosure requirements in other IFRS Accounting Standards, the IASB regularly considers which of those proposed amendments should be included in IFRS 19, based on the IASB's principles for reducing disclosure requirements for eligible subsidiaries.

The IASB is proposing amendments to IFRS 19 to require an eligible subsidiary:

(a) to disclose information about contingent consideration arrangements; and

(b) to disclose gains or losses resulting from 'downstream' transactions with its associates or joint ventures.

The IASB is also proposing an amendment to IFRS 19 to require a subsidiary that chooses to apply the equity method to account for its investments in subsidiaries in separate financial statements to disclose gains or losses resulting from 'downstream' transactions with those subsidiaries.

Paragraphs BC172–BC177 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative, taking into consideration the principles for reducing disclosure requirements for eligible subsidiaries applying IFRS 19 (see paragraph BC175 of the Basis for Conclusions).

These proposals have limited to no effect on our members so we will not comment further.

Other matters

Question 9—Transition

(Paragraphs C3–C10 of [draft] IAS 28 (revised 202x))

The IASB is proposing to require an entity:

(a) to apply retrospectively the requirement to recognise the full gain or loss on all transactions with associates or joint ventures;

(b) to apply the requirements on contingent consideration by recognising and measuring contingent consideration at fair value at the transition date— generally the beginning of the annual reporting period immediately preceding the date of initial application—and adjusting the carrying amount of its investments in associates or joint ventures accordingly; and

(c) to apply prospectively all the other requirements from the transition date.

The IASB is also proposing relief from restating any additional prior periods presented. Paragraphs BC178–BC216 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals?

If you disagree, please explain why you disagree and your suggested alternative.

While we acknowledge the transition relief proposed by the IASB there are some areas that our members consider require further consideration as follows:

Notwithstanding our comments regarding downstream transactions involving the loss of control of a subsidiary, should the IASB continue with the proposed amendments, we suggest that the IASB provide specific transition relief relating to transactions with associates or joint ventures involving the loss of control of a subsidiary.

Retrospective recognition of the full gain or loss on all transactions with associates or joint ventures would require entities to have recorded the restricted portion of a gain or loss arising from the disposal of a subsidiary to an associate or joint venture. This may not always be the case for the following reasons:

- *Where a subsidiary is sold or contributed in a downstream transaction with an associate or a joint venture, IAS 28.32 requires that upon the acquisition of its interest in the associate or joint venture, the investor recognise the identifiable assets at fair value. However, IAS 28.28 requires an investor to recognise gains and losses resulting from transactions between itself and an associate or joint venture only to the extent of the unrelated investors' interests in the associate or joint venture. The requirements of paragraphs 32 and 28 may be given affect in the accounting records by two different approaches.*
    - *Approach 1: Applying the requirements of IFRS 10 and then eliminating the portion of restricted gains and losses, or*

- *Approach 2: Recognising the investment in the associate or joint venture at the investor's portion of the fair value of new net identifiable assets obtained plus the investor's portion of the book value of the subsidiary sold or contributed.*

  Both approaches have the same mathematical outcome, however Approach 2 does not determine the fair value of the subsidiary disposed of or record the restricted portion of the gain or loss.

- *The gain or loss is not consumed over time but rather becomes realised only upon the ultimate disposal of the associate or joint venture to a third party, or alternatively when the associate or joint venture realises the underlying net assets. A record of the restricted portion of the gain or loss is therefore not necessary to apply the existing requirements in IAS 28 and for this reason entities had no need to keep record of it.*

To the extent that Approach 2 above has been followed by members, retrospective recognition of the previously restricted gain or loss would require the use of hindsight to determine the fair value of the retained interest at the time of the transaction, however we note IAS 8.53 specifically precludes the use of hindsight when applying a new accounting policy to a prior period.

As an alternative, our members note that there are two potential alternatives the IASB may consider as follows: i) allowing grandfathering of investments that have been accounted for according to IAS 28.28 rather than IFRS 10. Such grandfathering would allow relief for preparers who in response to the perceived conflict of IAS 28 and IFRS 10, have elected an accounting policy choice to account for such transactions according to IAS 28.28 rather than IFRS 10 or ii) the prospective application of the requirement to recognise the full gain or loss on all transactions with associates or joint venture

Finally, our members consider that the requirement to recognise and measure the contingent consideration at the fair value at the transition date is burdensome therefore our members note that the IASB should consider this requirement to be applied prospectively.

Question 10—Expected effects of the proposals

Paragraphs BC217–BC229 of the Basis for Conclusions explain the IASB's analysis of the expected effects of implementing its proposals. Do you agree with this analysis? If not, which aspects of the analysis do you disagree with and why?

See details as noted in the responses for the other questions.

Question 11—Other comments

Do you have any comments on the other proposals in this Exposure Draft, including Appendix D to the Exposure Draft or the Illustrative Examples accompanying the Exposure Draft?

Do you have any comments or suggestions on the way the IASB is proposing to re-order the requirements in IAS 28, as set out in [draft] IAS 28 (revised 202x)?

We do not have any other comments.