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IFRS in Focus

IASB publishes amendments to IFRS 10 and IAS 28 (2011) dealing with the sale or contribution of assets between an investor and its joint venture or associate

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This edition of IFRS in Focus outlines the recent amendments to the accounting under IFRS 10 *Consolidated Financial Statements* and IAS 28(2011) *Investments in Associates and Joint Ventures* for sales or contributions of assets between an investor and its joint venture or associate.

The Bottom Line

- In a transaction involving an associate or a joint venture, the extent of gain or loss recognition depends on whether the assets sold or contributed constitute a business.
- When an entity:
  - sells or contributes assets that constitute a business to a joint venture or associate; or
  - loses control of a subsidiary that contains a business but it retains joint control or significant influence;

  the gain or loss resulting from that transaction is recognised in full.
- Conversely, when an entity:
  - sells or contributes assets that do not constitute a business to a joint venture or associate; or
  - loses control of a subsidiary that does not contain a business but it retains joint control or significant influence in a transaction involving an associate or a joint venture;

  the gain or loss resulting from that transaction is recognised only to the extent of the unrelated investors' interests in the joint venture or associate, i.e. the entity's share of the gain or loss is eliminated.
- The amendments to IFRS 10 and IAS 28(2011) apply prospectively for annual periods beginning on or after 1 January 2016, with earlier application permitted.

Why have these amendments been issued?

The amendments address a conflict between the requirements of IAS 28(2011) and IFRS 10. In accordance with IAS 28(2011), the gain or loss resulting from the sale or contribution of a non-monetary asset to a joint venture or associate in exchange for an equity interest in that joint venture or associate is restricted to the extent of the unrelated investors' interests in the joint venture or associate. In contrast, IFRS 10 requires full profit or loss recognition on the loss of control of a subsidiary including a sale or contribution of the subsidiary to a joint venture or associate.

To address this conflict, the IASB has issued the amendments to IFRS 10 and IAS 28(2011).

What are the changes introduced by the amendments?

The amendments set out that, on a sale or contribution of assets to a joint venture or associate or on a loss of control when joint control or significant influence is retained in a transaction involving an associate or a joint venture, the extent of any gain or loss recognised depends on whether the assets or subsidiary constitute a business, as defined in IFRS 3 *Business Combinations*. When the assets or subsidiary constitute a business, any gain or loss is recognised in full; when the assets or subsidiary do not constitute a business, the entity's share of the gain or loss is eliminated.

Amendment to IFRS 10 *Consolidated Financial Statements*

The amendment to IFRS 10 introduces an exception from the general requirements of full gain or loss recognition on the loss of control over a subsidiary.

The exception applies to the loss of control over a subsidiary that does not contain a business, as defined in IFRS 3, if the loss of control is the result of a transaction involving an associate or a joint venture that is accounted for using the equity method.

The gain or loss resulting from such transactions is recognised in the parent's profit or loss only to the extent of the unrelated investors' interest in the associate or joint venture that was the counterparty of the transaction. The same requirements apply to related amounts previously recognised in other comprehensive income that would be reclassified to profit or loss on loss of control as a result of such transactions.

In addition, if the parent retains an investment in the former subsidiary and the former subsidiary is now an associate or joint venture that is accounted for using the equity method, the gain or loss resulting from the remeasurement at fair value of the investment retained should be recognised in profit or loss only to the extent of the unrelated investors' interest in the new associate or joint venture.

> Observation
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> The requirements to restrict the gain or loss to the unrelated investors' share do not apply to transactions with third parties, even if the parent retains an investment in the former subsidiary that becomes an associate or a joint venture accounted for using the equity method.

The accounting requirements for transactions where the former subsidiary does contain a business remain unchanged, i.e. any gain or loss from a sale or contribution of a subsidiary containing a business is recognised in full.

> Observation
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> Distinguishing between transactions on this basis places additional emphasis on the definition of a business. Therefore, for transactions of the type set out above, entities need to consider carefully whether a subsidiary contains a business in accordance with IFRS 3.

Amendments to IAS 28(2011) *Investments in Associates and Joint Ventures*

The guidance on gains or losses from 'upstream' and 'downstream' transactions and partial elimination of such gains or losses has been amended so that it only relates to transactions involving assets that do not constitute a business, as defined in IFRS 3.

For transactions involving assets that do constitute a business, an entity is now required to recognise any gain or loss in full. This is in line with the amendments to IFRS 10 above.

IAS 28(2011) now also specifies that, when determining whether the assets sold or contributed constitute a business, an entity needs to consider whether the sale or contribution involves multiple transactions that should be accounted for as one transaction.

> Observation
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> The amendment to IAS 28(2011) also applies to 'upstream' transactions. If a joint venture or associate sells assets that meet the definition of a business in IFRS 3 to its investor, and the investor takes control of that business, the gain or loss from that transaction is recognised in full, i.e. the investor's share in the gain or loss is not eliminated. As a consequence of the amendment, the accounting in the investor's financial statements for upstream transactions involving a business is now consistent with the guidance in IFRS 3 on business combinations that result from step acquisitions.

When do the new requirements apply?

The amendments apply prospectively to transactions occurring in annual periods beginning on or after 1 January 2016. Early application is permitted. If an entity applies the amendments earlier, it shall disclose that fact.

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