ICAEW representation

ICAEW REP 10/05

PROPOSED AMENDMENTS TO IAS 27 CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS

Memorandum of comment submitted in October 2005 by the Institute of Chartered Accountants in England and Wales, in response to International Accounting Standards Board exposure draft Proposed Amendments to IAS 27 Consolidated and Separate Financial Statements, published on 30 June 2005

Contents **Paragraph**

Chartered Accountants' Hall PO Box 433 Moorgate Place London EC2P 2BJ
Tel 020 7920 8100 **Fax** 020 7920 0547 DX 877 London/City **www.icaew.co.uk**

INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales welcomes the opportunity to comment on the exposure draft *Proposed Amendments to IAS 27 Consolidated and Separate Financial Statements*, published by the International Accounting Standards Board on 30 June 2005.

WHO WE ARE

2. The Institute of Chartered Accountants in England and Wales (the 'Institute') is the largest accountancy body in Europe, with more than 125,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.

3. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry (DTI) through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy.

MAJOR ISSUES

Process

4. We are concerned that the IASB issued an exposure draft proposing to introduce major changes to IFRS GAAP without first issuing a discussion paper. We believe that it is essential to allow time for constituents to consider and debate the fundamental conceptual changes proposed.

Non-controlling interests and changes in ownership interest

5. The Board appears to consider that inclusion of non-controlling interests within equity is an agreed position. However, we note from the version of IAS 27 that was issued following the improvements project (paragraph DO3) that this was, at best, a tentative conclusion which a dissenting Board member noted was predetermining the outcome of the debate supposedly taking place later. We agree with the three Board members' alternative views expressed in paragraphs AV1 - AV3.

6. Consequently, we do not agree with the proposal that changes in a parent's ownership interest in a subsidiary after control is obtained that do not result in a loss of control, should be accounted for as transactions with equity holders in their capacity as equity holders. The most useful information for shareholders in the parent company, to whom the consolidated accounts are primarily addressed, is the performance achieved by the controlling interest. It is therefore appropriate to reflect appropriate adjustments to goodwill, or record gains or losses in the income statement (see paragraph 7 below). We would

agree that additional guidance on the treatment of such transactions would be useful, especially in step acquisitions, since there is divergence in practice.

Question 1

Draft paragraph 30A proposes that changes in the parent's ownership interest in a subsidiary after control is obtained that do not result in a loss of control should be accounted for as transactions with equity holders in their capacity as equity holders. As a result, no gain or loss on such changes would be recognised in profit or loss (see paragraph BC4 of the Basis for Conclusions).

Do you agree? If not, why not and what alternative would you propose?

7. We disagree with the proposed treatment. In principle, we believe that the consolidated financial statements are intended primarily for the shareholders in the parent company. The most relevant information for these shareholders is performance from the perspective of the controlling interest, and so it is appropriate (as set out in the Alternative View) to report gains or losses in the parent's ownership interest in a subsidiary after control is obtained, that do not result in a loss of control, in profit or loss. In the absence of an informed debate about the advantages of the entity model over the parent model, we can see no conceptual basis for moving to a different model.

Question 2

Paragraph 30D proposes that on loss of control of a subsidiary any non-controlling equity investment remaining in the former subsidiary should be remeasured to its fair value in the consolidated financial statements at the date control is lost. Paragraph 30C proposes that the gain or loss on such remeasurement be included in the determination of the gain or loss arising on loss of control (see paragraph BC7 of the Basis for Conclusions).

Do you agree that the remaining non-controlling equity investment should be remeasured to fair value in these circumstances? If not, why not and what alternative would you propose?

Do you agree with the proposal to include any gain or loss resulting from such remeasurement in the calculation of the gain or loss arising on loss of control? If not, why not, and what alternative would you propose?

8. We can accept that the remaining non-controlling equity investment might be remeasured to fair value, although we question whether it is necessary, since the entity has a continuing interest in the remaining stake. In our view, any resulting gain should not be taken to the income statement, since by its nature it is a revaluation gain.

Question 3

As explained in Question 1, the Exposure Draft proposes that changes in a parent's ownership interest in a subsidiary that do not result in a loss of *control should be treated as transactions with equity holders in their capacity as equity holders. Therefore, no gain or loss would be recognised in profit or loss.*

However, a decrease in the parent's ownership interest resulting in the loss of control of a subsidiary would result in any gain or loss being recognised in profit or loss for the period. The Board is aware that differences in accounting that depend on whether a change in control occurs could create opportunities for entities to structure transactions to achieve a particular accounting result.

To reduce this risk, the Exposure Draft proposes that if one or more of the indicators in paragraph 30F are present, it is presumed that two or more disposal transactions or arrangements that result in a loss of control should be accounted for as a single transaction or arrangement. This presumption can be overcome if the entity can demonstrate clearly that such accounting would be inappropriate (see paragraphs BC9-BC13 of the Basis for Conclusions).

Do you agree that it is appropriate to presume that multiple arrangements that result in a loss of control should be accounted for as a single arrangement when the indicators in paragraph 30F are present? Are the proposed factors suitable indicators? If not, what alternative indicators would you propose?

9. We agree that it is appropriate to presume that multiple arrangements that result in a loss of control should be accounted for as a single arrangement when the indicators in paragraph 30F are present. However, we believe that paragraph 30F is too rigid as drafted. In order to minimise the potential for structuring transactions specifically to avoid the listed indicators, it should be redrafted to clarify that the indicators given are merely examples and do not comprise a closed list.

Question 4

Paragraph 35 proposes that losses applicable to the non-controlling interest in a subsidiary should be allocated to the non-controlling interest even if such losses exceed the non-controlling interest in the subsidiary's equity. Non-controlling interests are part of the equity of the group and, therefore, participate proportionally in the risks and rewards of investment in the subsidiary.

Do you agree with the proposed loss allocation? Do you agree that any guarantees or other support arrangements from the controlling and non-controlling interests should be accounted for separately? If not, why not, and what alternative treatment would you propose?

10. We agree that losses applicable to the non-controlling interest should be allocated to that interest, although we do not agree with the basis for it suggested by the IASB: that is, that non-controlling interests are part of the equity of the group. We believe that this should be done in order to indicate

the future allocation of any profits arising in the subsidiary in which the non-controlling interest exists. We agree that guarantees and other support arrangements should be considered separately, and may consequently affect any accumulated loss carried as a non-controlling interest.

Question 5

The transitional provisions in the Exposure Draft propose that all of its requirements should apply retrospectively, except in limited circumstances in which the Board believes that retrospective application is likely to be impracticable.

Do you agree that proposed paragraphs 30A, 30C and 30D should apply on a prospective basis in the cases set out in paragraph 43B? Do you believe that retrospective application is inappropriate for any other proposals addressed by the Exposure Draft? If so, what other proposals do you believe should be applied prospectively and why?

11. We agree that the prospective basis should apply in the cases specified.

DW/31.10.05
desmond.wright@icaew.co.uk