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ED/2013/10 Equity Method in Separate Financial Statements - Proposed amendments to IAS 27

Grant Thornton International Ltd is pleased to comment on the International Accounting Standards Board's (the Board) *Exposure Draft ED/2013/10 Equity Method in Separate Financial Statements - Proposed amendments to IAS 27* (the ED). We have considered the ED, as well as the accompanying draft Basis for Conclusions.

On balance, we support the inclusion of 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.

Our responses to the questions in the ED's Invitation to Comment are set out in the Appendix.

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If you have any questions on our response, or wish us to amplify our comments, please contact our Global Head of IFRS, Andrew Watchman (andrew.watchman@gti.gt.com or telephone + 44 207 391 9510).

Yours sincerely,

Kenneth C Sharp

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Responses to Invitation to Comment questions

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?

We support the inclusion of 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. Reinstating this option will reduce the burdens on entities in jurisdictions that require the preparation of separate financial statements and the use of the equity method in those statements.

Set against this, there are some concerns with these amendments. Introducing additional accounting policy options to enable consistency with local jurisdictional requirements is not consistent with the concept of a single set of global standards, and may create additional pressures for similar changes in future. The amendments will reduce consistency, lack a clear conceptual basis and raise questions as to the purpose of separate financial statements. Moreover, as noted in the Board's work plan, the equity method is often criticised and will be subject to a research project in due course.

On balance, however, we support the proposals mainly on pragmatic grounds.

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?

We agree with the proposed transition provisions.

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?

We agree that a special relief is not required for first-time adopters.

Question 4 – Consequential amendment to IAS 28 Investments in Associates and Joint Ventures

The IASB proposes to amend paragraph 25 of IAS 28 in order to avoid a conflict with the principles of IFRS 10 Consolidated Financial Statements 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?

We find the proposed amendment, and explanation for it in BC11, unclear.

BC11 suggests that the equity method as described in IAS 28 would lead to a conflict with IFRS 10's principles. We do not think that any conflict arises in the circumstances described because IFRS 10 does not apply to a parent's or investor's separate financial statements. Also, paragraph 25 of IAS 28 refers to proportionate reclassification of gains or losses recognised on OCI whereas BC11 refers to remeasurement of the retained interest.

We suggest that, if a parent entity elects to apply the equity method for investments in subsidiaries (and associates and joint ventures) in its separate financial statements then it should apply the requirements of IAS 28. In the event of a change of status (eg from subsidiary to associate) the guidance in paragraph 24 of IAS 28 should then be applied such that the retained interest would not be remeasured.

We note that IAS 28 refers to associates and joint ventures in several paragraphs. It might be helpful to include a statement (either in IAS 27 or IAS 28) to the effect that, when a parent entity applies the equity method for investments in subsidiaries in its separate financial statements, IAS 28's references to associates and joint ventures should be taken to include subsidiaries.

Question 5 – Other comments

Do you have any other comments on the proposals?

The proposed amendment to paragraph 6 of IAS 27 is potentially confusing in that it seems to provide a definition of 'separate financial statements' that is inconsistent with the definition in paragraph 4.

Also, in the same paragraph, the second reference to 'in addition to' may need to be clarified. If a non-parent investor with significant influence over an associate and/or joint control over a joint venture elects to use the equity method in its separate financial statements then those statements would be identical to the investor's required financial statements apart from any disclosure differences resulting from the scope of IFRS 12 (the disclosures in paragraphs 20 – 23 of IFRS 12 would not apply in the separate financial statements but would apply in the required financial statements).

The proposed amendments to paragraph 12 of IAS 27 address the accounting for a dividend received from an equity-accounted investment in separate financial statements. The requirement to account for a dividend as a reduction in the carrying amount is presumably subject to the restrictions in paragraph 39 of IAS 28 on reducing the carrying amount to less than zero.

We note that paragraph 10 of IAS 27, as proposed, would permit a parent entity to choose different methods for different categories of investment (cost, fair value or equity). For example, an entity could choose the equity method for subsidiaries and cost for associates. This may lead to some uncertainties in how to account for a change of status. For example, if an equity-accounted subsidiary becomes a cost-accounted associate, should 'cost' be interpreted as original cost or the proportionate share of the equity carrying value? We do not suggest developing guidance to address all possible permutations, as this would over-complicate what is intended to be a facilitative amendment. However, the Board should be aware of these complexities in evaluating the pros and cons of moving ahead with the proposal.

BC 10 of the ED mentions one situation in which consolidating a subsidiary would yield a different amount of net assets and profit or loss attributable to the equity holders of the investor compared to use of the equity method. Another important example is an investment in a subsidiary that has net liabilities. The final version of the Basis for Conclusions might usefully refer to this.