

10 May 2021

Hans Hoogervorst
Chair
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London
United Kingdom

Dear Mr Hoogervorst

Post-implementation Review IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities*

Deloitte Touche Tohmatsu Limited is pleased to respond to the International Accounting Standards Board's Post-implementation Review IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities* ("the PIR").

Overall, we believe that these standards provide sound principles and relevant guidance supporting the judgements required to represent faithfully an entity's interests in subsidiaries and joint arrangements. Except for the issues noted below, we believe that no significant changes are required to the relevant standards. We have indicated in our responses to the various questions in the PIR areas that may benefit from clarifications and/or additional illustrative examples.

We believe that key issues that may require the Board's attention relate to

- The loss of information that results from the requirement that an investment entity should measure at fair value all subsidiaries that are themselves investment entities, including those that provide investment-related services or activities. Users of the financial statements seek transparency in respect of operating costs and leverage of an investment entity. Because of the requirement to measure at fair value subsidiaries that are themselves investment entities, entities may be obliged to resort to alternative performance measures to provide a full picture of operating costs and financing, including the amounts that are recorded in subsidiaries that are investment entities. We acknowledge that it may not be possible to redefine the scope of subsidiaries that qualify for consolidation without causing significant disruption to the current model. As an alternative, the Board may consider whether IFRS 12 should be amended to address additional information that should, or may, be presented with respect of costs and leverage of certain investment-entity subsidiaries. This would help limit the proliferation of alternative performance measures. See our response to Question 4(b) for further details.

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- Whether the fact that a transfer of assets that is effected through a corporate structure, rather than directly, should affect the accounting for the transaction. We note that two issues related to this matter were submitted to the IFRS Interpretations Committee recently. If the Board believes that its agenda cannot accommodate such a significant project, we suggest that it may want to consider whether some of these issues (in particular the issue related to the sale of a single asset entity containing real estate) can be addressed as part of a more limited scope project, for example as an amendment to the scope of IFRS 10. See our response to Question 5(a) for further details.
- The accounting for forward purchase contracts and put options written over non-controlling interests, which continues to be a significant source of diversity in practice. If this issue is not addressed as part of the Board's Financial Instruments with Characteristics of Equity project, we believe that it should be addressed as part of a separate project. See our response to Question 10 for further details.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely



Veronica Poole
Global IFRS Leader

Appendix

INFORMATION ABOUT THE RESPONDENT

Question 1 Background

To understand whether groups of stakeholders share similar views, the Board would like to know:

(a) your principal role in relation to financial reporting. Are you a user or a preparer of financial statements, an auditor, a regulator, a standard-setter or an academic? Do you represent a professional accounting body? If you are a user of financial statements, what kind of user are you, for example, are you a buy-side analyst, sell-side analyst, credit rating analyst, creditor or lender, or asset or portfolio manager?

(b) your principal jurisdiction and industry. For example, if you are a user of financial statements, which regions do you follow or invest in? Please state whether your responses to questions 2–10 are unrelated to your principal jurisdiction or industry.

This response is submitted on behalf of member firms of the Deloitte Touche Tohmatsu network. This network includes member firms operating in more than 150 countries and territories and across a wide variety of industries.

For the purposes of responding to the post-implementation review questions, we are commenting in our capacity as auditors of financial statements. In this capacity, we have been involved in the application of IFRS 10, 11 and 12 across many industries and jurisdictions.

CONTROL – POWER OVER AN INVESTEE

Question 2(a) Relevant activities

In your experience:

(i) to what extent does applying paragraphs 10–14 and B11–B13 of IFRS 10 enable an investor to identify the relevant activities of an investee?

(ii) are there situations in which identifying the relevant activities of an investee poses a challenge, and how frequently do these situations arise? In these situations, what other factors are relevant to identifying the relevant activities?

In general, the requirements in IFRS 10: 10-14 and B11-13 are well understood and enable an investor to appropriately identify the relevant activities of its investees. In most situations, this is a straight-forward exercise, and the key relevant activities identified are those that relate to the approval of the budget and strategic plans and hiring/remuneration/termination of key management personnel.

However, some situations require a greater application of judgements and we suggest that the Board may wish to consider whether it could develop additional examples to illustrate the application of the principles in IFRS 10: 10-14 and B11-13. These include

- Situations where relevant activities are not performed concurrently, such that there may be a shift in power over time. These situations are quite common in certain industries, in particular in the mining and pharmaceutical industries. In the mining industry, for example, as the operations of the entity evolve from the development phase to the exploitation phase and finally to the reclamation phase, relevant activities may change with a different investor having power over the relevant activities in the different phases. The Board may consider providing additional examples to illustrate whether control is assessed separately in each phase of the operations of the entity or through a more holistic assessment covering the life of the entity.

- Situations where relevant activities are determined through contractual arrangements, for example when there are operating agreements granting rights and responsibilities to a specific party. These are encountered most frequently in the mining, construction, power and utilities and real estate industries, where one of the shareholders may be granted additional decision-making rights through an operating agreement. In these cases, it is important to consider factors similar to those considered in assessing whether a party with decision-making rights is acting as an agent (e.g. scope of the decision-making authority and removal rights). Currently, the effect of delegated power on the assessment of control is mainly illustrated through examples pertaining to the investment fund industry. The Board may consider providing additional examples illustrating the effect of delegated power in other industries (see also our response to Question 3a).

Finally, there continue to be some misconceptions on the concept of “auto pilot”, in particular in the renewal energy industry. This is another example of the practical difficulties in identifying relevant activities when the operations of an investee evolve over time. The Board may consider providing additional examples illustrating that true auto pilot entities are extremely rare and the factors that may be considered to identify potentially relevant activities when the investee is set up to construct and operate a wind or solar farm, for example assessing whether routine activities such as maintenance may constitute relevant activities in certain situations or whether the right to decide to temporarily shut down production in unexpected situations (e.g. excess supply or extreme weather conditions) should be viewed as a substantive or protective right.

Question 2(b) Protective vs substantive rights

In your experience:

- (i) to what extent does applying paragraphs B26–B33 of IFRS 10 enable an investor to determine if rights are protective rights?
- (ii) to what extent does applying paragraphs B22–B24 of IFRS 10 enable an investor to determine if rights (including potential voting rights) are, or have ceased to be, substantive?

In general, we find that IFRS 10:B26-B33 provide appropriate guidance to determine whether rights are protective.

However, the guidance on franchises in IFRS 10:B29-B33 appear unduly biased towards considering that the rights of franchisors are protective rights. In developing these paragraphs, the Board may have had in mind a specific franchise model in which the rights of the franchisor are indeed specifically designed to protect its brand. However, in practice, franchises operate under various models. In some of these, the franchisor is extensively involved in the operations of the franchises with the franchisee having limited decision-making rights. For example, some franchise arrangements set out when the franchise must operate, what supplies to purchase and from whom, what products to make and sell. Further, in addition to providing financing, the franchisor may also be acting as lessor. An appropriate assessment of whether the rights of the franchisor are protective or substantive requires a more holistic assessment of the arrangement than what may be understood from the guidance in IFRS 10:B29-B33. The Board should consider how to best convey this message.

Question 2(c) Control without majority of voting rights

In your experience:

- (i) to what extent does applying paragraphs B41–B46 of IFRS 10 to situations in which the other shareholdings are widely dispersed enable an investor that does not hold a majority of the voting rights to make an appropriate assessment of whether it has acquired (or lost) the practical ability to direct an investee’s relevant activities?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 2(c)(i) arise?
- (iii) is the cost of obtaining the information required to make the assessment significant?

Even though significant judgement is required, we believe that the guidance in B41–B46 of IFRS 10 provides an appropriate basis to assess whether an investor that does not hold a majority of the voting rights has the practical ability to direct an investee’s relevant activities, which is a common situation.

The key difficulty in practice is that, over time, the power of an investor over an investee may change because of factors that are not solely within the investor’s control, such as a progressive change in the shareholding of other investors. Significant judgement may be involved to determine the date when the investor obtains or loses control in such situations. It would be useful for IFRS 10 to acknowledge this fact and to note that the investor accounts for the acquisition or loss of control prospectively from that date.

Also, arrangements that contemplate a sharing of control between two or more parties generally include dispute resolution mechanisms. In particular, the arrangement may grant one party the right to buy-out the other party. The Board may wish to consider whether guidance could be provided to illustrate the effect, if any, of such clauses to the assessment of control and joint control, at inception of the arrangement and whether reassessment is required at later dates.

CONTROL – LINK BETWEEN POWER AND RETURNS

Question 3(a) Agent vs Principal

In your experience:

- (i) to what extent does applying the factors listed in paragraph B60 of IFRS 10 (and the application guidance in paragraphs B62–B72 of IFRS 10) enable an investor to determine whether a decision maker is a principal or an agent?
- (ii) are there situations in which it is challenging to identify an agency relationship? If yes, please describe the challenges that arise in these situations.
- (iii) how frequently do these situations arise?

We believe that the factors listed in IFRS 10:B60 along with the related application guidance enable an investor to determine whether a decision maker is a principal or an agent.

However, we note the guidance may be overlooked in certain industries despite being relevant. This is because the illustrative examples provided in IFRS 10 relate solely to the investment fund industry. In practice, we have found that the assessment of agent vs principal is also relevant in the extractive, power and utilities, construction and real estate industries. In these industries, it is frequent for the shareholders to designate an “operator” that may have significant decision-making rights. We found that the factors listed in IFRS 10:B60 may be relevant in these circumstances, in particular when the scope of the decision-making rights held by one party does not appear aligned with that party’s exposure to variable returns. We suggest that the Board may wish to consider developing additional examples illustrating the

application of these factors in industries other than the investment fund industry.

Question 3(b) De facto agent

In your experience:

- (i) to what extent does applying paragraphs B73–B75 of IFRS 10 enable an investor to assess whether control exists because another party is acting as a de facto agent (i.e. in the absence of a contractual arrangement between the parties)?
- (ii) how frequently does the situation in which an investor needs to make the assessment described in question 3(b)(i) arise?
- (iii) please describe the situations that give rise to such a need.

We believe that the guidance in IFRS 10:B73-B75 is sufficient to enable an investor to assess whether control exists because another party is acting as a de facto agent. We do not have any additional comments in that respect.

INVESTMENT ENTITIES

Question 4(a) Typical characteristics of an investment entity

In your experience:

- (i) to what extent does applying the definition (paragraph 27 of IFRS 10) and the description of the typical characteristics of an investment entity (paragraph 28 of IFRS 10) lead to consistent outcomes? If you have found that inconsistent outcomes arise, please describe these outcomes and explain the situations in which they arise.
- (ii) to what extent does the definition and the description of typical characteristics result in classification outcomes that, in your view, fail to represent the nature of the entity in a relevant or faithful manner? For example, do the definition and the description of typical characteristics include entities in (or exclude entities from) the category of investment entities that in your view should be excluded (or included)? Please provide the reasons for your answer.

In general, the definition of what constitute an investment entity along with the typical characteristics permit an appropriate identification of such entities.

The aspect of the definition that could benefit from additional guidance is the need for a documented exit strategy as noted in IFRS 10:B85F. We agree that the existence of a documented exit strategy is an important element demonstrating the business purpose of an investment entity. We note that in practice some believe that having set up a limited life entity is sufficient to demonstrate the existence of a documented exit strategy. We do not believe that this is the case. We suggest that it may be useful for the Board to provide illustrative example of what an exit strategy is, i.e. a governance strategy addressing exit plans rather than an ultimate disposal date.

Question 4(b) Loss of information, scope of consolidation exception

In your experience:

- (i) are there situations in which requiring an investment entity to measure at fair value its investment in a subsidiary that is an investment entity itself results in a loss of information? If so, please provide details of the useful information that is missing and explain why you think that information is useful.
- (ii) are there criteria, other than those in paragraph 32 of IFRS 10, that may be relevant to the scope of application of the consolidation exception for investment entities?

We believe that the loss of information that results from the requirement to measure at fair value (rather than consolidate) certain subsidiaries that are themselves investment entities is a key shortcoming of the requirements on investment entities.

Subsidiaries of investment entities may incur operating costs or assume obligations that contribute to the operations of the investment entity group. Users of the financial statements, in particular analysts, seek transparency in that respect. Because of the requirement in IFRS 10:B85E to measure at fair value subsidiaries that are themselves investment entities, fund managers who want to respond to the information needs of users of the financial statements may be obliged to provide the relevant information through alternative performance measures.

We acknowledge that it may not be possible to redefine the scope of subsidiaries that qualify for consolidation in IFRS 10:B85E without causing significant disruption to the current model. As an alternative, the Board may consider whether additional information should, or may, be presented with respect of costs and leverage of investment-entity subsidiaries that provide investment-related services or activities. This would help investment entities to provide relevant information, compliant with IFRS Standards, without having to resort to alternative performance measures.

ACCOUNTING REQUIREMENTS – CHANGE IN RELATIONSHIP

Question 5(a)

In your experience:

- (i) how frequently do transactions, events or circumstances arise that:
 - (a) alter the relationship between an investor and an investee (for example, a change from being a parent to being a joint operator); and
 - (b) are not addressed in IFRS Standards?
- (ii) how do entities account for these transactions, events or circumstances that alter the relationship between an investor and an investee?
- (iii) in transactions, events or circumstances that result in a loss of control, does remeasuring the retained interest at fair value provide relevant information? If not, please explain why not, and describe the relevant transactions, events or circumstances.

Overall, the model on changes in relationship in IFRS 10 appears to provide relevant information.

However, we believe that some of the principles that determine whether a change in ownership results in remeasurement of the interest retained need to be clarified. In particular,

- changes in relationship involving a group of assets that are not held within a corporate structure; and
- contribution of a subsidiary to an existing associate or joint venture.

The difficulties in applying the existing requirements to these transactions seem to relate to a broader “corporate structure/business” issue that include

- Whether the fact that a transfer of assets is effected through the transfer of a corporate structure rather than directly should affect the accounting for the transaction?
- Whether a transaction involving a group of assets should be accounted for differently depending on whether the group of assets constitutes a business?

We note that recently the IFRS Interpretations Committee considered the following issues that are also related to the “corporate structure/business” issue.

- Sale of a single asset entity containing real estate (discussed at the June 2019 meeting of the IFRS Interpretations Committee)
- Sale and leaseback in a corporate wrapper (addressed in the September 2020 IFRIC Update). We note that while the IFRS Interpretations Committee addressed the very specific fact pattern presented in the submission, responses to the tentative agenda decision indicated that more fundamental questions needed to be addressed.

We strongly encourage the Board to consider whether it can address the fundamental questions that form part of the “corporate structure/business” issue. If it believes that its agenda cannot accommodate such a significant project, we suggest that the Board may want to consider whether some of these issues (in particular the issue related to the sale of a single asset entity containing real estate) can be addressed as part of a more limited scope project, for example as an amendment to the scope of IFRS 10.

Question 5(b)

In your experience:

- (i) how do entities account for transactions in which an investor acquires control of a subsidiary that does not constitute a business, as defined in IFRS 3? Does the investor recognise a non-controlling interest for equity not attributable to the parent?
- (ii) how frequently do these transactions occur?

The definition of non-controlling interest (NCI) in IFRS 10 does not depend on whether a subsidiary is a business or not, and therefore we believe that many investors that acquire a subsidiary that is not a business would recognise an NCI. However, we note that the measurement of assets and liabilities acquired in a transaction that is not a business combination based on their relative fair value, as required by IFRS 3:2(b), appears incompatible with the recognition of NCI. As such we expect that diversity in practice exists both in terms of recognition and measurement of the NCI. This issue is not infrequent.

The recent amendments to IFRS 3 on definition of a business and the introduction of the optional concentration test are likely to increase the prevalence of transactions that are accounted for as the acquisition of a group of assets (and not as a business combination).

This is one of the issues that should be considered as part of the overall “corporate structure/business” issue described in our response to Question 5(a).

COLLABORATIVE ARRANGEMENTS

Question 6

In your experience:

(a) how widespread are collaborative arrangements that do not meet the IFRS 11 definition of 'joint arrangement' because the parties to the arrangement do not have joint control? Please provide a description of the features of these collaborative arrangements, including whether they are structured through a separate legal vehicle.

(b) how do entities that apply IFRS Standards account for such collaborative arrangements? Is the accounting a faithful representation of the arrangement and why?

We note that the term "collaborative arrangements" is not defined in IFRS Standards and therefore it is difficult to answer this question. However, we note that arrangements in which two or more parties collaborate on a project without sharing joint control are frequent in the extractive industry. Generally these arrangements are not structured through a separate legal vehicle. Instead, the assets and liabilities required to the conduct of the project are owned as tenants in common. In such situations, typically an analogy is made to the requirements of IFRS 11.

CLASSIFYING JOINT ARRANGEMENTS

Question 7

In your experience:

(a) how frequently does a party to a joint arrangement need to consider other facts and circumstances to determine the classification of the joint arrangement after having considered the legal form and the contractual arrangement?

(b) to what extent does applying paragraphs B29–B32 of IFRS 11 enable an investor to determine the classification of a joint arrangement based on 'other facts and circumstances'? Are there other factors that may be relevant to the classification that are not included in paragraphs B29–B32 of IFRS 11?

The frequency of the reliance on "other facts and circumstances" to classify joint arrangements is greatly dependent on jurisdictions. Anecdotally, these appear more frequently reported in Australia and in Canada which may reflect that joint arrangements are common in the extractive industry.

We acknowledge that the assessment requires significant judgement, but do not believe that any significant changes are required to the Standard to assist in the application of the requirements.

However, we note that the IFRS Interpretations Committee issued several agenda decisions on the application of IFRS 11 in relation to matters considered in Questions 7 and 8. The Board may wish to consider whether the issues addressed in these agenda decisions could be incorporated in IFRS 11 to provide greater visibility to this useful source of guidance.

ACCOUNTING REQUIREMENTS FOR JOINT OPERATIONS

Question 8

In your experience:

(a) to what extent does applying the requirements in IFRS 11 enable a joint operator to report its assets, liabilities, revenue and expenses in a relevant and faithful manner?

(b) are there situations in which a joint operator cannot so report? If so, please describe these situations and explain why the report fails to constitute a relevant and faithful representation of the joint operator's assets, liabilities, revenue and expenses.

In general, we believe that IFRS 11 permits joint operators to provide relevant and faithful representation of their operations and we are not aware of situations where this has not been possible.

We acknowledge that considerable efforts may be required to understand and appropriately capture the legal and economic reality of joint arrangements and there remains some misconceptions on how the requirements of IFRS 11 differ from proportionate consolidation. We also note that the introduction of IFRS 16 raised difficulties in application, for example identifying who is the lessee in the lease contract, whether a sublease (or an in-substance sublease) is in place between the lessee and the joint arrangement. Further, when joint operators (other than the lessee) are required to contribute to the joint operation through cash calls to cover the costs of the lease, a mismatch may arise between the cash call amount and the accounting expense recognised in the statement of profit or loss (as depreciation and interest expense). Significant disclosures may be required to explain this mismatch. The Board may wish to consider whether further clarity could be provided through an illustrative example on how a joint operation accounts for lease contracts.

DISCLOSURE OF INTERESTS IN OTHER ENTITIES

Question 9

In your experience:

- (a) to what extent do the IFRS 12 disclosure requirements assist an entity to meet the objective of IFRS 12, especially the new requirements introduced by IFRS 12 (for example the requirements for summarised information for each material joint venture or associate)?
- (b) do the IFRS 12 disclosure requirements help an entity determine the level of detail necessary to satisfy the objective of IFRS 12 so that useful information is not obscured by either the inclusion of a large amount of detail or the aggregation of items that have different characteristics?
- (c) what additional information that is not required by IFRS 12, if any, would be useful to meet the objective of IFRS 12? If there is such information, why and how would it be used? Please provide suggestions on how such information could be disclosed.
- (d) does IFRS 12 require information to be provided that is not useful to meet the objective of IFRS 12? If yes, please specify the information that you consider unnecessary, why it is unnecessary and what requirements in IFRS 12 give rise to the provision of this information.

We have no specific comments to raise in respect of the requirements in IFRS 12, except as noted in our response to Question 4(b). We suggest that the Board may wish to wait for the outcome of its Disclosure Initiative project to re-evaluate the requirements of IFRS 12.

Question 10

Are there topics not addressed in this Request for Information, including those arising from the interaction of IFRS 10 and IFRS 11 and other IFRS Standards, that you consider to be relevant to this Post-implementation Review? If so, please explain the topic and why you think it should be addressed in the Post-implementation Review

We believe that the most pressing issue that the Board should consider is the “corporate structure/business” issue described in our response to Question 5(a).

We also believe that the Board should address the accounting for forward purchase contracts and put options written over non-controlling interests, which continues to be a significant source of diversity in practice. It may be preferable to address the treatment of such instruments holistically, considering more

broadly all forward purchase contracts and put options to purchase an entity's own equity instruments as part of the Board's project on Financial Instruments with Characteristics of Equity (the FICE project). However, if the scope of the FICE project does not encompass such instruments, we believe that the Board should consider the most effective way to address the diversity in practice arising from the potentially conflicting accounting requirements in IFRS 10 and IAS 32.

We note that the Board is currently considering issues related to the application of the equity method in IAS 28. We suggest that as part of this project on the equity method it may wish to consider whether the definition of significant influence should be amended to reflect the changes made to the definition of control in IFRS 10. For example, aligning how the existence of potential voting rights affect significant influence or addressing whether a party that is determined to be an agent applying the guidance in IFRS 10:B62-B72 can have significant influence.

Paragraph 3.12 of the Conceptual Framework acknowledges the concept of combined financial statements but does not discuss when or how such financial statements can be presented as general-purpose financial statements. The Board may wish to consider whether to undertake a project to provide guidance on the topic, including the practical difficulties that arise when preparing combined financial statements.