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HKFRS / IFRS UPDATE 2014/15

SALE OR CONTRIBUTION OF ASSETS BETWEEN AN INVESTOR AND ITS ASSOCIATE OR JOINT VENTURE (AMENDMENTS TO HKFRS/IFRS 10 AND HKAS/IAS 28)

Summary

The International Accounting Standards Board (IASB) published *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture* (Amendments to IFRS 10 and IAS 28) on 11 September 2014. On 7 October 2014, the HKICPA issued the equivalent amendments to HKFRSs to maintain the convergence between HKFRS and IFRS.

The amendments clarify the accounting for transactions where a parent loses control of a subsidiary, that does not constitute a business as defined in HKFRS/IFRS 3 *Business Combinations*, by selling all or part of its interest in that subsidiary to an associate or a joint venture that is accounted for using the equity method.

In the case of any retained interest in the former subsidiary, gains and losses from the remeasurement are treated as follows:

- The retained interest is accounted for as an associate or joint venture using the equity method: The parent recognises the gain or loss in profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture. The remainder is eliminated against the carrying amount of the investment in the associate or joint venture.
- The retained interest is accounted for at fair value in accordance with HKFRS/IFRS 9 *Financial Instruments*: The parent recognises the gain or loss in full in profit or loss.

The effective date for the amendments is 1 January 2016. The amendments are applied on a prospective basis. Early application is permitted.

STATUS
Final

EFFECTIVE DATE
1 January 2016

ACCOUNTING IMPACT
Clarification of the treatment of gains and losses on the sale of a subsidiary to an associate or joint venture which did not qualify as a business

Background

The amendment deals with an inconsistency that originated in HKAS/IAS 27 (rev 2008) and HK(SIC)-INT 13, which relates to the accounting for the contribution of a subsidiary to a jointly controlled entity, joint venture or associate that results in the loss of control of the subsidiary.

The following accounting treatments applied:

- HK(SIC)-INT 13

  The amount of the gain or loss recognised resulting from the contribution of a non-monetary asset to a jointly controlled entity in exchange for an equity interest in that jointly controlled entity was restricted to the extent of the interests attributable to the unrelated investors in the jointly controlled entity.

- HKAS/IAS 27 (rev 2008)

  On the date of the loss of control of a subsidiary, any gains or losses were recognised in full in profit or loss.

HKAS/IAS 27 (rev 2008) was replaced by HKFRS/IFRS 10 and HK(SIC)-INT 13 was withdrawn with its requirements being incorporated into HKAS/IAS 28. However, the inconsistency remained within HKFRS/IFRS 10 as its requirements for the loss of control are similar to HKAS/IAS 27 (rev 2008).

The issue was the potential for structuring, as the same transaction might be accounted for differently depending on whether the assets were:

- Transferred in a transaction that is structured as a sale of assets or a sale of the entity that holds the assets; or
- Sold in exchange for cash or an equity interest.

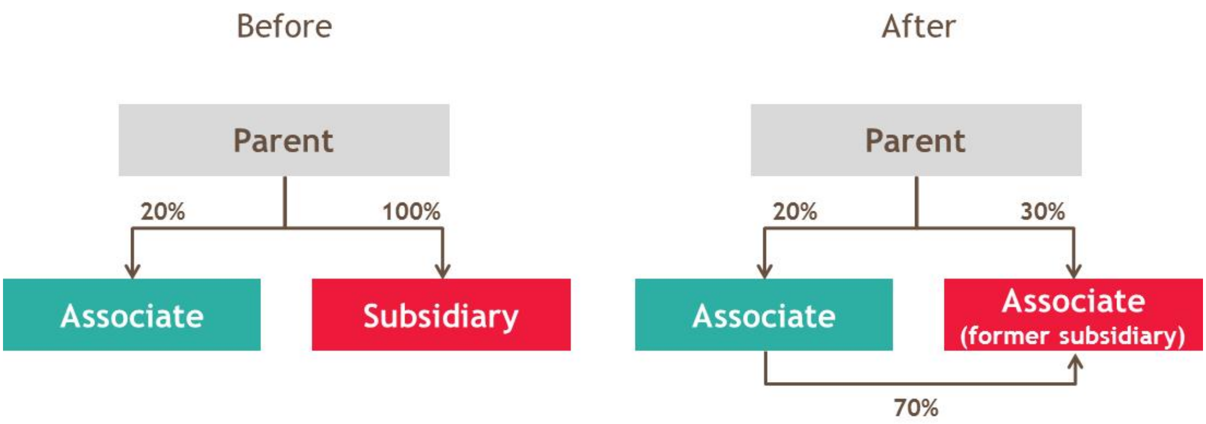
Amendments to HKFRS/IFRS 10 and HKAS/IAS 28

The amendments also clarify the accounting approach to be followed if an entity sells only part of the subsidiary that does not constitute a business, and instead retains an investment in the newly created associate or joint venture that is accounted for using the equity method. In these cases, gains and losses are eliminated against the carrying amount of the investment in the newly created associate or joint venture to the extent that the parent retains an interest in the former subsidiary.

In case the retained interest is accounted for at fair value in accordance with HKFRS/IFRS 9 *Financial Instruments* the parent recognises any gain or loss in full in profit or loss.

This interest will be held both directly in the newly created associate or joint venture, and indirectly via the associate or joint venture to which the interest in the former subsidiary has been sold.

An example of such a restructuring relates to a parent which sells 70% of its share in its subsidiary (that does not constitute a business) to its 20% associate. The parent therefore loses control of the subsidiary which is now accounted for as an associate using the equity method.



Consideration received	CU210
Carrying amount of net assets of the subsidiary	CU100
Fair value of investment retained in former subsidiary	CU90
30% of carrying amount of net assets of the subsidiary	CU30
Gain resulting from remeasurement at fair value	CU60

In the above case, the gain comprises of two components of which part is recognised in profit or loss and part is offset with the carrying amount of the investment retained in the former subsidiary:

1. **Sale of 70% interest**
   Difference between the fair value of the consideration received (CU210) and the carrying amount of the interest sold (70% x CU100) represents the gain from the sale of the 70% interest. The parent recognises in its profit or loss the amounts of the gain attributable to the unrelated investors interests in the existing associate being:
   - 80% x CU140 = CU112 → Recognised in profit or loss
   - 20% x CU140 = CU28 → Eliminated against investment in associate

2. **Gain from remeasurement at fair value of the direct retained investment**
   This amount is the difference between the fair value of the investment retained in the former subsidiary (CU90) and 30% of the carrying amount of the assets of the subsidiary (CU30, being 30% x CU100), which is the gain from the remeasurement of the asset at fair value.
   - CU60 x (70% x 80%) = CU34 → Recognised in profit or loss
   - CU60 x 44% = CU26 → Eliminated against investment in associate.

   The elimination of 44% corresponds to the directly held interest of 30%, and the indirectly held interest of 14% (20% x 70%).

Effective date and transition

The effective date for the amendments is for annual periods beginning on or after 1 January 2016, and it to be applied prospectively.

Early application is permitted. Entities that decide to adopt the requirements early shall disclose that fact.

BDO's support and assistance on HKFRS/IFRS

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