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**Reference: Request for Information: Post-implementation Review of IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities**

The Comitê de Pronunciamentos Contábeis - CPC (Brazilian Accounting Pronouncements Committee)<sup>1</sup> welcomes the opportunity to respond to the Request for Information on the post-implementation review of IFRSs 10, 11 and 12.

We are a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidance for Brazilian companies.

If you have any questions about our comments, please do not hesitate to contact us at [operacoes@cpc.org.br](mailto:operacoes@cpc.org.br).

Yours sincerely,



Rogério Lopes Mota  
Chair of International Affairs  
Comitê de Pronunciamentos Contábeis (CPC)

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<sup>1</sup>The Brazilian Accounting Pronouncements Committee (CPC) is a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidance for Brazilian companies. Our members are nominated by the following entities: ABRASCA (Brazilian Listed Companies Association), APIMEC (National Association of Capital Market Investment Professionals and Analysts), B3 (Brazilian Stock Exchange and Mercantile & Future Exchange), CFC (Federal Accounting Council), FIPECAFI (Financial and Accounting Research Institute Foundation) and IBRACON (Brazilian Institute of Independent Auditors).

Based on the outreach performed to the preparers of financial statements of Brazilian public entities and members of the CPC<sup>2</sup> regarding the questions included in the request for information as well as the views of the members of the CPC we provide below how we understand that IFRS 10, IFRS 11 and IFRS 12 should be clarified to address divergence in practice.

We summarised our comments in subtopics below, consistent with the sequence of information provided by the request for information:

## 1. IFRS 10 Consolidated Financial Statements

### 1.1. Control—Power over an investee (relevant activities)

As outlined by IFRS 10, an investor has power when it has existing rights that give it the current ability to direct the relevant activities. As such, we understand that the identification of the relevant activities as well as the assessment of existing rights are key aspects of an investor's conclusion as it relates to control.

In our view, especially in arrangements where the existence of voting rights may not be viewed as the determining factor to determine control, the identification of the relevant activities and how the decisions about those relevant activities are made (IFRS 10.B10) is key to assess control. In that regard, as it relates to question 2(a):

**Question 2(a):** *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? 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?*

#### **Our response:**

We agree with the preliminary feedback included in the Request for Information that identifying the relevant activities may not be a straightforward exercise and that judgment is applied when the arrangements provide for the direction of different activities by different investors and that those activities sets may be viewed as relevant depending on the nature of the investor's interest in the investee or the timing in which those activities occur.

IFRS 10.13 states that in such situations power over the investee must be viewed on the basis of the correlation between the direction of the activities that most significantly affect the returns of the investee and, in that sense, two application examples are provided in IFRS 10.B13. While the examples provide relevant facts

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<sup>2</sup> Members of the CPC that participate in the outreach include preparers, regulators and academics, including (i) the São Paulo Stock Exchange; (ii) the Federal Accounting Council; (iii) the Brazilian Association of Listed Companies; (iv) the Brazilian Institute of Independent Auditors; (v) the Research Institute of Accounting, Actuarial and Financial Foundation; and (vi) the National Association of Capital Market Investment Professionals and Analysts.

and circumstances to assist the entities in assessing control when there are different activities that may be viewed as relevant at different points in time, in our view additional examples related to this matter should be provided to clarify how to comply with the existing control requirements within IFRS 10. We believe such examples could help to support consistent application.

### *1.2. Control—Power over an investee (rights that convey power)*

Consistent with IFRS 10.B22, in assessing whether it has power, the investor considers only substantive rights, those that provide the holder with the practical ability to exercise that right. While in our view paragraphs B29 through B33 provide an adequate basis to assess rights held by a franchisor under a franchise agreement, we believe that there is a room for improving the definition of protective rights, e.g. it is unclear what fundamental change means as set out in IFRS 10.B26. We noted that term fundamental changes is not included in the definition of protective rights as per Appendix A in IFRS 10.

Moreover, the assessment of changes in certain facts and circumstances which may lead to changes in conclusions regarding control may be clarified by the Board. In that regard, as it relates to question 2(b):

**Question 2(b):** *To what extent does applying paragraphs B26–B33 of IFRS 10 enable an investor to determine if rights are protective rights? 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?*

#### **Our response:**

As discussed on the Basis for Conclusions for IFRS 10, paragraph 124, changes in market conditions by themselves should not be viewed as a definitive factor that would lead to changes in consolidation conclusions. However, while provided as an example in IFRS 10.B23(c) as a factor to be taken into consideration, there may be situations where the assessment of control may be highly subjective, and the assessment of market conditions may be a significant factor in concluding that a potential voting right is substantive (i.e., a currently exercisable option to acquire control of an investee that would be akin to start-up and at that point it's unclear whether the entity would benefit from the exercise given the uncertainties on the synergies) .

As such we understand that expanding the discussion on changes in facts and circumstances over the life of the involvement with the investee and the potential resulting impact of such changes in light of the guidance provided on IFRS 10.B23 would result in better guidance for the entities and would benefit consistency in reporting.

### *1.3. Control—Power over an investee (control without a majority of the voting rights)*

As it relates to whether an investor possess control without having the majority of voting rights, in our view IFRS 10.B38, B41 and B42 provide guidance that is sufficient for the entities to conclude in those situations. However, we refer to our response to question 2(a) as we believe that expanded guidance on relevant activities would also be beneficial in those situations. Furthermore, we also agree with the Board's views as to avoid providing a specified quantitative threshold as part of the guidance around control as we believe that the holistic assessment taking into consideration all facts and circumstances is the proper approach.

As such, we do not have any additional observations that we believe would be necessary to be considered in response to **question 2(c)**.

### *1.4. Control—The link between power and returns*

As previously discussed in our letter, we have performed an outreach to entities in Brazil to request their views on the questions included in the request for information. As it relates to the matters included in **questions 3(a) and 3(b)**, we do not have any specific observations or views that we believe should be taken into consideration as part of the Board's review process.

### *1.5. Investment entities*

As it relates to the existing criteria to determine whether an entity is an investment entity, we take the view that the Board could expand the guidance provided in paragraphs 27 and 28 of IFRS 10 to include additional criteria that we believe conceptually would also be applicable for the proper determination of an investment entity. As such, we provide the following response to question 4(a)

**Question 4(a):** *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.*

**Our response:**

Consistent with feedback we have provided in previous comment letters (including the comments to the ED/2011/4 – Investment Entities), we believe that the criteria should be expanded to include:

(a) entities that have just one investee in their portfolio, since in the Private Equity industry is common to find entities structured exclusively to invest in a specific business (this type of operation is commonly known as “club deals”); and

(b) entities with a single investor unrelated to the fund manager if this entity meets the following characteristics: (i) the fund manager (or its general partner) has a discretionary management mandate and (ii) the entity’s portfolio is not composed by investees related to the single investor or the fund manager.

As it relates to question 4(b):

**Question 4(b):** *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. 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?*

**Our response:**

We agree with the current guidance provided by paragraphs 31 and 33 as in our view, measuring such investment at fair value better serves the needs of the users of the financial statements and better depicts the nature of the future economic benefit embodied in the investments held by the investment entity (the potential for capital appreciation, investment income, or both and not to achieve operational synergies). As such we do not believe that any information that is omitted due to the lack of consolidation would be significant in light of the users of such financial statements.

**1.6. Accounting requirements**

As it relates to transactions, events or circumstances that alter the relationship between an investor and an investee, such as the example provided by the request for information (when a parent loses control of a subsidiary but retains an interest in a joint operation), in our view, measuring the investment retained at fair value is consistent with the view that the new investor–investee relationship differs from the former, as expressed by the Board in the IFRS 10.BCZ182. However, we believe that remeasuring the retained investment when a parent loses control of a subsidiary does not provide useful information because it appears to be counterintuitive to remeasure the retained interest as if it had been sold to third parties and it does not

properly portray the performance of the investor regarding the loss of control transaction.

In addition, we have the following observations:

**Question 5(a):** *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?*

*How do entities account for these transactions, events or circumstances that alter the relationship between an investor and an investee? 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.*

**Our response:**

While we acknowledge that not all transactions, events or circumstances that alter the relationship between an investor and an investee are to be addressed in the standards, in our view there are certain events that may occur more often and additional guidance as to those would be beneficial for the preparers of the financial statements. For example, when there is a decrease in the investor's share in the investee without loss of control, should a proportion of the goodwill recognised be allocated between the controlling shareholders and non-controlling interest, regardless of whether NCI was measured at fair value or based on its proportionate share of net assets?

Also, how would such changes impact the impairment test of goodwill to be carried out annually? We believe that providing further guidance in the standard addressing those situations would be beneficial for the preparers of the financial statements and would reduce diversity in practice.

Based on the outreach performed to the Brazilian entities we did not identify a large volume of instances where the specific matters included on question 5(b) have been noted. As such, we make no comment on those specific matters.

## **2. IFRS 11 Joint Arrangements**

Based on the outreach performed to the Brazilian entities we did not identify a large volume of instances where the specific matters included in **questions 6** and **7** have been noted. As such, we make no comment on those specific matters.

As it relates to question 8:



**Question 8:** *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? 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.*

**Our response:**

In our view, based on discussion with not only preparers and auditors, but also with analysts who make their analysis and recommendations based on information that is disclosed in the financial statements, the proportionate consolidation provides information that is relevant for of the financial statements, especially in certain segments where the use of joint ventures is recurring and is typically integrated in the group policies and operations (i.e. supply chain and other financing and operating policies). Such information is currently viewed by management and analysts as integral to entity's business objectives, being commonly disclosed by the entities that have relevant interests in joint ventures in other documents accompanying the financial statements.

We acknowledge the Board's views as to the conceptual flaws of this method (especially given the contradiction with the definition of assets and liabilities provided by the Conceptual Framework) but we believe that the users of the financial statements would benefit from optional requirements for the joint venturer to provide detailed information in the footnotes on the share of the assets and liabilities that would have otherwise been consolidated (under the proportionate consolidation method) rather than making decisions as to those investments in joint ventures based on the net balance presented in a "single line consolidation". In our view, since this is information that is actually considered by users of the financial statements (or other documents that accompany the financial statements such as management commentary, for example) as discussed above, the disclosure of the information would be consistent with the stated objective of IFRS 12, to require disclosure of information that enables users to, among others, evaluate the nature of, and risks associated with, its interests in other entities, including joint ventures.

While similar requirements are included in IFRS 12.2(b)(ii) and 21(b)(ii) for material joint ventures, in our view, the concept of "material" in this assessment is typically associated with the magnitude of the investment recognised by the entity using the equity method, where the presentation of the net amount in the balance sheet may overshadow the existence of certain significant assets and liabilities that would have otherwise been assessed as material if presented separately. As such, in our view, the disclosure requirements provided by IFRS 12.B12 and B13 would better represent the extent of the entity's interests in the joint ventures and enables users to evaluate the nature and risks associated with the entity's interests in the operations if the presentation is made based on the entity's share

of assets, liabilities and the items presented in the statement of profit or loss (the items referred to in IFRS 12.B12).

### **3. IFRS 12 Disclosure of Interests in Other Entities**

The objective of the standard, as outlined on IFRS 12.1 is to provide a framework for disclosure of information that allows the users of the financial statements evaluate the nature of, and risks associated with, its interest in other entities and the effects of those interests on its financial position, financial performance and cash flows. Also, as provided by in the February 19, 2010 IASB Update, that also includes information that is associated with structured entities that a reporting entity does not control.

While we take the view that the level of information required to be disclosed is sufficient to provide the users with information that is relevant for the decision-making process, we acknowledge that an in-depth research among users of the financial statements (i.e., investors, lenders and others) has not been performed and while the feedback received from accountants and preparers of financial statements may provide a reasonable basis to assess potential changes to the disclosure requirements, as it relates to the items included in **question 9**, in our view any change in the current requirements should be based on actual feedback from a wider range of users of the financial statements to minimize the risk that additional burden on the preparers of the financial statements on obtaining the required information would not be greater than the expected benefits in terms of the qualitative information to be provided to the users of the financial statements for their decision-making process.

### **4. Other topics**

We have no further matters to comment other than the topics included above.